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INTERNATIONAL INVESTORS' RIGHTS AND REMEDIES IN THE ADJUDICATION OF DISPUTES WITH U.S. SECURITIES AND COMMODITIES FIRMS IN THE CONTEXT OF U.S. ARBITRAL FORUM SELECTION[†]

Madelaine Eppenstein^{*}

I. INTRODUCTION

The globalization of markets, the internationalization, merger and consolidation of major investment firms, the joiner of commercial and investment banking and the interest of international public investors in utilizing the services of reputable, brand-name brokers, has contributed to a concomitant increase in customer claims filed in arbitration by both domestic and international investors.¹ Yet, in practice, very few defrauded international investors who do business with United

[†] Copyright © 2002 Madelaine Eppenstein, New York, N.Y. Portions of this Article in substantially modified form were originally published by the author in *International Investors' Rights and Remedies in Regard to Fraudulent Investment Activities by U.S. Securities and Commodities Firms*, [Jan.-Dec.] 5 World Sec. L. Rep. (BNA), at 39 (May 1999).

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1. See discussion *infra* note 18. Some of the increase in volume of case filings in 2001 was attributable to the bear market tech stock crash that began in the spring of 2000. See Richard Karp, *Disputed Calls: A Year After Nasdaq's Peak, Arbitration Claims Against Brokers Soar*, BARRON'S, May 21, 2001, at 21.

States securities and commodity futures firms through branch offices based both outside of and within the U.S., appear to be aware of their rights and remedies. Those who are savvy enough to discern that their boilerplate customer agreement with a securities broker-dealer or a commodities futures commission merchant ("FCM") usually requires adjudication of all claims in a U.S. based arbitral institution or reparations tribunal do not always, in the first instance, seek the advice of experienced U.S. counsel. Typically they will contact a member of this specialized bar in the U.S. only after first consulting their local counsel. Unless previously initiated to this area of practice, foreign counsel may advise their clients of potential claims in their own locality, but may be unaware of the investor's ability, if not the clear mandate under the broker's account-opening documentation, to obtain recovery through arbitration in the U.S.² Though international claimants may not

2. Under the Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, "[t]he validity and enforceability of [alternative dispute resolution] clauses may be controversial, particularly if they contradict principles of consumer protection established by the Brussels Convention. Contract terms that deprive a consumer of the right to initiate legal proceedings in the Contract States where the consumer is domiciled are not likely to be enforced." Karol K. Deniston, *Do Pre-Dispute Arbitration Agreements Violate Core Principles?*, Paper Presented at the American Bar Association Section of Dispute Resolution Annual Conference (Apr. 27, 2001) (on file with Journal). *See also* Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, arts. 2, 5, & 17, 1968 O.J. (C 27) 1, 4, 5, 8-9.

Another wrinkle suggested by Deniston may be presented by Article 7 of the Hague Conference on Private International Law, which currently provides that consumers can sue and be sued in the country where they are domiciled and can agree to the venue where a dispute will be adjudicated, but only if "such agreement is entered into after the dispute has arisen." Hague Conference on Private International Law, Preliminary Draft Convention on Jurisdiction and Foreign Judgments in Civil and Commercial Matters, at <http://www.hcch.net/e/workprog/jdgm.html> (Oct. 30, 1999); *see also* Deniston, *supra* note 2. Thus, as a general matter, typical U.S. broker-dealer *pre-dispute* arbitration agreements, which prospectively waive access to the courts, may not be binding against the investor in the European Union. However, they are enforceable against the broker-dealer at the discretion of the international securities or commodity futures customer under applicable rules of U.S. self-regulatory organizations, based on the contract or the membership of the brokerage firm at the organization. *See discussion infra* note 12. Therefore, the practical applicability of these international norms in the

be fully cognizant of the available legal rights and remedies, many intuitively recognize that, as the financial center of the U.S. and a global center for finance, as well as the site of the New York Stock Exchange, Inc. ("NYSE"), and the Nasdaq Stock Market, Inc. ("Nasdaq"), New York is the logical starting point to obtain legal advice.³

International customers who bring their claims under the auspices of the major self-regulatory organizations ("SROs") that run arbitration programs, such as the NYSE and the National Association of Securities Dealers Dispute Resolution, Inc. ("NASD-DR"), usually elect to have their disputes adjudicated in the U.S.⁴ New York City continues to be a magnet for

context of regulated industries, such as the securities industry, may be a moot point.

3. See Carole Silver, *Globalization and the U.S. Market in Legal Services—Shifting Identities*, 31 LAW & POL'Y INT'L BUS. 1093, 1135-36 (2000). The Nasdaq Stock Market, Inc., is currently an affiliate of the National Association of Securities Dealers, Inc., but is in the "process of becoming independent from the [National Association of Securities Dealers]" as part of a restructuring of the two companies, which will result in Nasdaq becoming an independent national securities exchange. *Nasdaq Separates Further From NASD by Completing Share Repurchase*, 34 Sec. Reg. & L. Rep. (BNA) No. 11, at 426 (Mar. 18, 2002).

4. In only limited circumstances in a few locales will the SROs provide overseas venues. See, e.g., Memorandum No. 98-42 from the New York Stock Exchange, to Members and Member Organizations (Dec. 15, 1998), at <http://www.nyse.com/regulation/regulation.html>. The memo states:

In recognition that our members and member organizations are expanding their businesses outside of the United States and increasingly offering their services to public non-institutional customers overseas, the Exchange will, where warranted by due process and fairness considerations, convene arbitration panels in London and Tokyo. Decisions on venue overseas will be made using the same criteria used domestically. Establishing these new hearing locations will accommodate non-U.S. customers of members or member organizations in Europe and Asia who wish to avail themselves of the Exchange's arbitration facilities. In further recognition of this global expansion, members and member organizations doing business with public non-institutional customers outside of the United States, particularly in non-English speaking countries, must insure that the disclosures required by Rule 636 are communicated in a language in which the customer is fluent. Members and member organizations with public non-institutional customers outside the United States, particularly those doing business in non-English speaking countries, must conduct their own internal review of their accounts to insure

arbitration cases in general, as reflected in filing percentages.⁵ International investors who avail themselves of the advantages of U.S. based venue and counsel come from widely diverse economic backgrounds and geographic locations. In the author's practice, some of those who have successfully adjudicated disputes, through arbitration and mediation at the NYSE and NASD-DR, have included: a distant relation of a European royal family; an industrialist from Germany who was a majority shareholder in a company that conducted billions of dollars of global business a year; an international distributor of candy and confections from France; a dentist from Italy; representatives of a large Indonesian textile company; an investment company in Cyprus; a private investor from the Middle East; and a retired furniture manufacturer from Belgium. A common thread was that all of the investors brought claims of alleged wrongdoing in the business conduct of the overseas branch offices of large U.S. firms.⁶

that their Customer Account Agreements are in compliance with the required disclosure of the Arbitration Rules.

Id.

5. See discussion *infra* note 18. However, a breakdown of filings by domestic versus international claimants was not available from sources at the NYSE and NASD-DR. Generally, New York City venued cases account for 30-40% of the NYSE caseload. E-mail from Robert S. Clemente, Director of Arbitration, New York Stock Exchange, to Madelaine Eppenstein (Mar. 18, 2002) (on file with Journal). At NASD-DR, Northeast Region (comprised of offices across the Northeastern and Mid-Atlantic states, New York, Boston, Philadelphia, Pittsburgh, Albany, Buffalo, Baltimore, Norfolk and Richmond, as well as Washington, D.C.) venued cases were approximately 35% of their caseload, with cases centered in New York City comprising 18.3% of the entire region's caseload. Telephone Interview with Elizabeth R. Clancy, Associate Vice President and Regional Director Northeast Region, National Association of Security Dealers Dispute Resolution (Mar. 19, 2002).

6. Each of these cases was settled during arbitration hearings or in mediation prior to the rendering of an arbitral award, with only one exception, a case that was on trial at the time this Article was written. As a result, the filings of these cases at an arbitral institution is not reflected in the database of the SROs awards. For a primary database online, NASD-DR works in conjunction with a service operated jointly by the Commerce Clearing House, Inc., securities and commodities law publisher, in partnership with the Securities Arbitration Commentator, Inc., a publication and database service based in Maplewood, New Jersey, as a way of providing a comprehensive, current, and publicly available database of annotated awards issued by a number of active forums such as NASD-DR, the NYSE, and the independent American Arbitration Association. See NASD Dispute Resolution, *at*

In each case, the international customer, and in almost all cases their local counsel, were unaware or unsure whether improper or fraudulent activity had caused the investment loss. Unfortunately, this phenomenon is widespread. It is also experienced by domestic public investors and has been reported often in U.S. court cases involving misrepresentation and concealed fraud.⁷ In the prosecution of the public customer cases mentioned above, it was only through diligent investigation and discovery, using procedural techniques developed through litigation in U.S. courts and at the SROs, that the nature of the wrongful conduct became apparent.⁸ Each of these international claimants recovered sizable amounts running into millions of dollars on average, sometimes well in excess of their out of pocket losses, through settlements achieved during or after the arbitration hearings (and before award), or in mediation.

While mediation may not have been widely employed in Europe until the end of the last century, except perhaps in the United Kingdom and Germany, “[a]rbitration has long been an accepted and even preferred method for solving international disputes.”⁹ In practice, therefore, the potential claimant from

<http://www.nasdaq.com> (last visited Mar. 6, 2002); Securities Arbitration Commentator, at <http://www.sacarb.com> (last visited Mar. 6, 2002).

7. See, e.g., *Fujisawa Pharm. Co. v. Kapoor*, 115 F.3d 1332, 1335 (7th Cir. 1997); *Law v. Medco Research, Inc.*, 113 F.3d 781, 786 (7th Cir. 1997); *Marks v. CDW Computer Ctr., Inc.*, 122 F.3d 363, 367-69 (7th Cir. 1997); *Nat. Rural Elec. Coop. Assoc. v. Breen Capital Serv. Corp.*, No. 00-722, 2001 WL 294086 (D.N.J. Mar. 28, 2001); *Rotter v. Leahy*, 93 F. Supp. 2d 487, 500-01 (S.D.N.Y. 2000); *Dietrich v. Bauer*, 76 F. Supp. 2d 312, 345 (S.D.N.Y. 1999); *Morin v. Trupin*, 809 F. Supp. 1081, 1097 (S.D.N.Y. 1993); *Patsos v. First Albany Corp.*, 741 N.E.2d 841 (Mass. 2001). Frequently in such cases, the courts have held that the concealed fraud and misrepresentation effectively prevented the plaintiff from being put on inquiry notice of the wrongdoing, which sometimes operates to toll the applicable statutes of limitations.

8. These procedural techniques include, but are not limited to: (1) sophisticated, database driven investigation of the rogue broker and the firm; (2) tracking down prior cases brought against the broker and the firm; (3) aggressively pursuing pre-hearing information and discovery requests and in-person pre-hearing conferences; and (4) early retention and involvement of the claimant's expert witness in initial client interviews and in rigorous analysis of account opening documents, the trading history and available records.

9. Center for Public Resources, *Online Seminar, European ADR 2000: European ADR Practice, Issues and Trends* (Jan. 10-16, 2000), available at

overseas may readily appreciate that arbitration of securities and commodities¹⁰ disputes is a viable, highly appropriate forum for the resolution of their claims.

This Article will focus on the practical considerations of potential claims and remedies available to the international customer in disputes arising against overseas offices of major U.S. broker-dealers and FCMs. Part II will provide the historical context in which the United States Supreme Court has mandated that claims arising under the U.S. securities laws are almost always subject to compulsory arbitration at the various arbitral self-regulatory organizations, where record filings by customers occurred in 2001.¹¹ As demonstrated in Part III, under the commodities laws, however, there may be additional options, including court litigation and reparations. In either case, the international investor may seek the protection of both statutory and common law remedies in the U.S. to gain redress for fraudulent activity. Part IV addresses some recurrent scenarios that have given rise to various theories of liability for fraudulent conduct by a broker, and briefly touches on some common procedural considerations that may differ from sys-

WL 18 ALTHCL 43. Arbitration as a method of resolving disputes that arise in international trade has a long history, and is conducted primarily in the context of model laws enacted over the years to establish uniform standards for the settlement of international commercial disputes. *See generally* Vivienne M. Ashman, *UNCITRAL Initiatives to Further Harmonize and Modernize Arbitration Laws, Rules and Practices*, in *INTERNATIONAL BUSINESS LITIGATION & ARBITRATION 2000*, at 635 (PLI Litig. & Admin. Practice Course, Handbook Series No. 624, 2000) (citing Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 21 U.S.T. 2518, 330 U.N.T.S. 38).

10. The commodity regulations require that public customers be given several options for filing claims, either in court, arbitration or before a reparations tribunal administered by the regulatory body that oversees the commodities markets, the Commodity Futures Trading Commission. *See* Commodity Exchange Act, 7 U.S.C. §§ 1-27 (2000) [hereinafter CEA]. *See generally* discussion *infra* Part III; PHILIP MCBRIDE JOHNSON & THOMAS LEE HAZEN, *COMMODITIES REGULATION* (2d ed. 1989); PHILIP MCBRIDE JOHNSON & THOMAS LEE HAZEN, *COMMODITIES REGULATION* (3d ed. 1998); PHILIP MCBRIDE JOHNSON & THOMAS LEE HAZEN, *SPECIAL SUPPLEMENT: OVERVIEW OF THE COMMODITY FUTURES MODERNIZATION ACT OF 2000* (3d ed. 2002).

11. *See* note 18 *infra*. For a general review of a wide range of topics covering the field of securities disputes, see Constantine N. Katsoris, *The Resolution of Securities Disputes*, 6 *FORDHAM J. CORP. & FIN. L.* 307 (2001) [hereinafter *The Resolution of Securities Disputes*].

tems of justice abroad. Concerns that are often expressed by the international investor when seeking to pursue claims in the U.S. are addressed in Part V. But while these investors will likely face a number of fairly typical procedural and tactical issues, such as defenses based on statutes of limitations and so-called eligibility or timeliness rules at the SROs, along with preemptive, affirmative defenses and counterclaims asserted by the broker, the international investor ultimately has the opportunity to obtain a highly favorable recovery in an American court, arbitration or reparations proceeding.

II. CLAIMS FOR SECURITIES FRAUD AND RELATED CAUSES OF ACTION ARE CUSTOMARILY SUBJECT TO COMPULSORY ARBITRATION UNDER U.S. LAW

Until 1987, defrauded investors could choose to go to court and have a judge and jury decide their federal statutory claims under the U.S. securities laws. In the likely event that the defendant broker-dealer was a member of an SRO, such as the NYSE or the National Association of Securities Dealers, Inc., ("NASD"), claims in arbitration could be asserted upon the demand of the public customer, and access to the arbitral forum could be based on the membership provisions of those organizations even in the absence of an arbitration agreement.¹² Over-

12. Access to SRO arbitration based on membership of the respondent is still the rule. See N.Y. STOCK EXCH., art. XI, 2 N.Y. Stock Exch. Guide (CCH) ¶ 1501; N.Y. STOCK EXCH. R. 600(a), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2600. Arbitration Rule 600(a) states:

Any dispute, claim or controversy between a customer or non-member and a member, allied member, member organization and/or associated person arising in connection with the business of such member, allied member, member organization and/or associated person in connection with his activities as an associated person shall be arbitrated under the Constitution and Rules of the New York Stock Exchange, Inc. as provided by any duly executed and enforceable written agreement or upon the demand of the customer or non-member.

Id. at R. 600(a). The NASD-DR provides similarly as follows:

Any dispute, claim, or controversy eligible for submission under the Rule 10100 Series between a customer and a member and/or associated person arising in connection with the business of such

whelmingly though, the choice for public customers was to go to court. But choice of forum was abrogated in 1987 by the Supreme Court in the seminal case of *Shearson/American Express, Inc. v. McMahon*.¹³ In that case, in which the author's firm represented the investors, the Supreme Court, by a close 5-4 vote, enforced the arbitration clause in a customer agree-

member or in connection with the activities of such associated persons shall be arbitrated under this Code, as provided by any duly executed and enforceable written agreement or upon the demand of the customer.

NAT'L ASS'N OF SEC. DEALERS DISPUTE RESOLUTION, CODE OF ARBITRATION PROCEDURE R. 10301(a) (2001) [hereinafter NASD-DR ARBITRATION CODE].

13. 482 U.S. 220 (1987). *McMahon* was a dispute arising under the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78mm (2000) [hereinafter 1934 Act]. Two years after deciding *McMahon*, in *Rodriguez De Quijas et al. v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), the Court also relegated to arbitration claims arising under the Securities Act of 1933, 15 U.S.C. §§ 77a-77bbb (2000) [hereinafter 1933 Act]. It is thus ironic that, in an area of virtually mandatory arbitration:

Securities disputes also generate a far higher proportion of judicial proceedings relating to arbitrability and interlocutory appeals than construction or other common types of arbitration . . . Securities cases tend to dominate the case law of arbitration. . . . [T]he law of arbitration is being formed in the crucible of disputes between securities brokers and their customers.

Stephen K. Huber & E. Wendy Trachte-Huber, *Top Ten Developments in Arbitration in the 1990s*, 55 DISP. RESOL. J. 24, 34 (2001).

This phenomenon is not entirely inconsistent with the prediction, made by the late Justice Harry A. Blackmun, in his dissent in *McMahon*, that investors would be inclined to bring complaints in court regarding the results of mandatory arbitration. 482 U.S. at 267-68 ("[I]nvestors will be inclined, more than ever, to bring complaints to federal courts that arbitrators were partial or acted in 'manifest disregard' of the securities laws.") (citation omitted). If anything, for a time during the decade following *McMahon*, it was the industry that took the lead in resorting to the courts in an attempt to get judges, and not arbitrators, to micro-manage the arbitration process. See, e.g., Peter Blackman, *No Clear Winner Yet: Brokerage Firms Seek to Derail Arbitration Effort*, N.Y. L.J., Mar. 3, 1994, at 5. But see *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Driessens*, N.Y. L.J., Oct. 24, 1996, at 27 (N.Y. Sup. Ct. Oct. 23, 1996). For a critical overview of the fallout in the arbitration process and the courts following the *McMahon* decision, see Constantine N. Katsoris, *The Betrayal of McMahon*, 24 FORDHAM INT'L L.J. 221 (1997); Constantine N. Katsoris, *Riding the Trojan Horse Back to Wilko?*, 10 SEC. ARB. COMMENTATOR 1 (1999).

ment pursuant to the Federal Arbitration Act ("FAA"),¹⁴ despite historical aversion by both the courts¹⁵ and the Securities and Exchange Commission ("SEC") to the arbitration of securities fraud disputes.¹⁶ Since then, the caseload in arbitration has steadily increased.¹⁷ In 2000, for example, there were approxi-

14. Federal Arbitration Act, 9 U.S.C. §§ 1-307 (2000).

15. Prior to *McMahon*, every circuit court but two had adhered to a long-settled rule that pre-dispute arbitration agreements were unenforceable with respect to claims asserted under the 1934 Act. See, e.g., *Jacobson v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 797 F.2d 1197 (3d Cir. 1986); *Mayaja, Inc. v. Bodkin*, 803 F.2d 157 (5th Cir. 1986); *Conover v. Dean Witter Reynolds, Inc.*, 794 F.2d 520 (9th Cir. 1986); *Wolfe v. E.F. Hutton & Co.*, 800 F.2d 1032 (11th Cir. 1986); *Mansbach v. Prescott, Ball & Turben*, 598 F.2d 1017 (6th Cir. 1979); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Moore*, 590 F.2d 823 (10th Cir. 1978); *Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 558 F.2d 831 (7th Cir. 1977).

The Court of Appeals for the Fourth and District of Columbia Circuits had not appeared to have ruled *per se* on the question prior to *McMahon*. See *King v. Drexel Burnham Lambert, Inc.*, 796 F.2d 59 (5th Cir. 1986); *Miller v. Drexel Burnham Lambert, Inc.*, 791 F.2d 850 (11th Cir. 1986); *Tashea v. Bache, Halsey, Stuart, Shields, Inc.*, 802 F.2d 1337 (11th Cir. 1986); *DeLancie v. Birr, Wilson & Co.*, 648 F.2d 1255 (9th Cir. 1981); *Ayres v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 538 F.2d 532 (3d Cir. 1976); *Sibley v. Tandy Corp.*, 543 F.2d 540 (5th Cir. 1976). Included in this list is the decision of the Court of Appeals for the Second Circuit in favor of the investors below in *McMahon*, styled *McMahon v. Shearson/American Express, Inc.*, 788 F.2d 94 (2d Cir. 1986). The two exceptions were in the Court of Appeals for the First and Eighth Circuits. See, e.g., *Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc.*, 806 F.2d 291 (1st Cir. 1986); *Phillips v. Merrill Lynch, Pierce, Fenner & Smith*, 795 F.2d 1393 (8th Cir. 1986).

16. The stinging dissent of Justice Blackmun observed the contradiction in the SEC's support of the industry as an amicus in *McMahon*:

[U]ntil it filed an amicus brief in this case, the Commission consistently took the position that [section] 10(b) claims, like those under [section] 12(2), should not be sent to arbitration, that predispute arbitration agreements, where the investor was not advised of his right to a judicial forum, were misleading, and that the very regulatory oversight upon which the Commission now relies could not alone make securities industry arbitration adequate.

482 U.S. at 262. See also Exchange Act Release No. 19,813, [1982-1983 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,356, at 85,967 n.6 (May 26, 1983); Exchange Act Release No. 15,984, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 82,122, at 81,977-78 (July 2, 1979).

17. The steady rise in filings in customer arbitrations has historically been punctuated by peaks and valleys as a result of market driven or other forces, for example, the increase in filings following *McMahon*, which swept

mately 5,725 cases filed at the NASD, with a record 7,088 new claims filed in 2001.¹⁸ The NYSE, which historically has maintained a smaller caseload, had 780 filings in 2001.¹⁹

Arbitration generally at the NYSE and the NASD improved significantly after 1987 for the public customer, becoming more user-friendly. The Securities Industry Conference on Arbitration ("SICA"), "formed in 1977 to develop uniform rules governing the arbitration of disputes between broker-dealers and customers at [SROs]," and now comprised of three members of the public, representatives of seven SROs (including the NYSE and NASD-DR), and one voting representative of the Securities Industry Association ("SIA"), was responsible for preparing and adopting a Uniform Code of Arbitration ("Uniform Code") and making recommendations to improve the arbitration system at the SROs in a continuing process of review and evaluation of the operation of the Uniform Code and SRO arbitration.²⁰ The

securities fraud cases under section 10b-5 of the 1934 Act into arbitration, the surge following the precipitous market break commonly known as "Black Monday" (Oct. 19, 1987), and the fall off in filings after the "crash" cases were resolved. See SEC. INDUS. CONFERENCE ON ARBITRATION, ELEVENTH REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION 106-26 (2001), available at http://www.nasdaq.com/pdf-text/sica_report.pdf (last visited Mar. 6, 2002) [hereinafter ELEVENTH REPORT].

18. Press Release, National Association of Securities Dealers Dispute Resolution, NASD Dispute Resolution Has Record Year (Jan. 22, 2002), available at http://www.nasdaq.com/news/pr2002/dr_release_02_001.html [hereinafter Press Release]. NASD-DR reported a 24% increase in filings in 2001 over the previous year's numbers, representing a record 2,137 claims filed in only the first four months of 2001, validating the notion that the tech stock decline in 2000 motivated the subsequent surge in customer complaints. Robust filings in the fourth quarter of 2001 did not appear to be affected by the tragic attacks on the World Trade Center in the heart of the financial center of New York on September 11, 2001. For updated filings and other statistics, see NASD Dispute Resolution, *Dispute Resolution Statistics*, at <http://www.nasdaq.com/statistics.asp#grapha> (last visited Mar. 5, 2002). NASD-DR recorded 20% more cases submitted to arbitration in the first two months of 2002 than the same period in 2001. Telephone Interview with Richard P. Ryder, Editor in Chief, Securities Arbitration Commentator (Mar. 22, 2002).

19. Statistics available from the Director of Arbitration at the NYSE. These claims include customer versus broker-dealer, broker-dealer versus customer and broker-dealer/employee cases.

20. SEC. INDUS. CONFERENCE ON ARBITRATION, TENTH REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION 1 (1998). See also Constantine N. Katsoris, *SICA: The First Twenty Years*, 23 FORDHAM URB. L.J.

advent of enhanced arbitrator selection methods, which provide the parties with greater control of the process, clarification of procedures (generally for the appointment of arbitrators), initiation of continuing arbitrator training programs,²¹ expanded discovery options and the translation of the Uniform Code into plain English,²² provide the parties with a greater understanding and command of the process, providing them with greater input in choosing the arbitrators who will hear and determine their cases.²³ Liberalized rules facilitating the capture of information and document discovery well before the hearings on the merits are conducted improve the fairness of the process.²⁴ This is especially important in the case of the international public customer, who usually does not possess documentary

483, 535-38 (1996). See generally Thomas J. Stipanowich, *Contract and Conflict Management*, 2001 WIS. L. REV. 831, 900 n.403 (2001).

21. Arbitrators are now required to undergo hours of training before they can sit on an arbitration panel, and must attend refresher training sessions to keep abreast of forum requirements and changes. See NAT'L ASS'N OF SEC. DEALERS DISPUTE RESOLUTION, ARBITRATOR RECRUITMENT BROCHURE (2000), available at http://www.nasdaq.com/arb_brochure_htm.asp (last visited Mar. 5, 2002).

22. See ELEVENTH REPORT, *supra* note 17, at 5. The preface to *The Arbitrator's Manual*, compiled by SICA as a guide for arbitrators "designed to supplement and explain the [Uniform Code]," notes that "[s]ignificant differences between the Uniform Code and the procedures of the SROs," require arbitrators to "always consult the rules of the arbitration forum in which they are serving." SEC. INDUS. CONFERENCE ON ARBITRATION, THE ARBITRATOR'S MANUAL, pmbl. (2001), available at http://www.nasdaq.com/sica_manual.asp (last visited Mar. 6, 2002) [hereinafter ARBITRATOR'S MANUAL].

23. In cases where the damages alleged are over \$50,000, NASD-DR Rule 10308(b)(1)(B) provides for three arbitrators to sit on a case. See NASD-DR ARBITRATION CODE, R. 10308(b)(1)(B). NYSE Rule 607(a)(1) provides for a panel of three arbitrators where the matter in controversy exceeds \$10,000. N.Y. STOCK EXCH. R. 607(a)(1), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2607. The method for selection of arbitrators is materially different at these two major SRO arbitral institutions, can be a complicated process and is a subject beyond the scope of this Article. See Theodore G. Eppenstein & Madelaine Eppenstein, Y2K Arbitrator Investigation and Selection, Paper Presented to the Public Investors Arbitration Bar Association Eighth Annual Conference (Oct. 20-22, 1999) (on file with Journal); Theodore G. Eppenstein & Madelaine Eppenstein, *How to Select Arbitrators in Securities Arbitration*, in SEC. ARB. 1996, at 585 (PLI Corp. L. & Practice Course, Handbook Series No. B4-7147, 1996).

24. See NASD-DR ARBITRATION CODE, R. 10321; N.Y. STOCK EXCH. R. 619, 2 N.Y. Stock Exch. Guide (CCH) ¶ 2619.

proof or information concerning witnesses to fraudulent transactions and other wrongdoing, particularly when the latter turn out to be internal employees of the broker-dealer or FCM and their overseas affiliated companies.

III. CLAIMANTS HAVE A RANGE OF OPTIONS WHEN PURSUING COMMODITY FUTURES CLAIMS

In the commodity futures area, investors typically use the services of introducing brokers ("IBs") who often act as investment advisors and utilize the services of FCMs in order to place orders in the commodity futures markets. The IBs are sometimes "guaranteed" by the FCMs pursuant to agreements entered into between the two. Investments can also be placed through associated persons of the FCM itself.²⁵ Fraud claims against commodity futures personnel may be brought against the FCM, the IB, their respective employees and Associate members. The claims can be based on theories of primary liability or aiding and abetting liability, as well as theories of agency and respondeat superior.²⁶

The IBs and FCMs also utilize customer agreements which are unlike those used by their securities industry counterparts. Pursuant to former Commodity Futures Trading Commission ("CFTC") Regulation section 180.3,²⁷ and the parallel amended section under the Commodity Futures Modernization Act of 2000 ("CFMA"),²⁸ when an IB or FCM wishes to place a pre-dispute arbitration clause in its agreement with its public customer, in addition to the use of mandatory language, the customer is given more choices by statute than are available under the securities laws and regulations. To begin with, the pre-

25. See NAT'L FUTURES ASS'N, NATIONAL FUTURES ASSOCIATION MANUAL ¶¶ 5011, 8101 (2001), available at <http://www.nfa.futures.org/compliance/manual/index.html> (last visited Feb. 23, 2002).

26. CEA, 7 U.S.C. § 25 (2000) (affording a private right of action for violations of the CEA); 7 U.S.C. § 6b (prohibiting fraud, false reporting or deception); 7 U.S.C. § 13(c) (providing a private right of action for aiding and abetting liability); 7 U.S.C. § 2(a)(1)(A) (imposing agency/respondeat superior liability).

27. 17 C.F.R. § 180.3 (2001).

28. A New Regulatory Framework for Trading Facilities, Intermediaries, and Clearing Organizations, 66 Fed. Reg. 14262 (proposed Mar. 9, 2001) (to be codified at 17 C.F.R. pt. 166).

dispute arbitration agreement must be accompanied by a separate arbitration clause and signature line. If the customer refuses to sign the separate arbitration clause, then the IB or FCM must still honor the customer's wish to engage the IB or FCM, who cannot turn down a customer for failure to execute the pre-dispute arbitration clause.²⁹ Compare this with the typical securities industry account opening agreement involving credit with its customers, where, although pre-dispute language has become virtually universal and recited in bold print since *McMahon*, the broker-dealer can still insist that the investor sign the pre-dispute agreement as a pre-condition to doing business with the firm: the securities broker-dealer may refuse to accept the customer unless the customer agrees to the entire agreement.³⁰

There are as many as three fora to resolve commodity futures disputes: court, arbitration or reparations proceedings. The

29. 17 C.F.R. §180.3.

30. The SEC determined in 1988, following a study by a Commission staff of sixty-five broker-dealer firms that accounted for approximately 90% of all customer trading accounts in the U.S., that 96% of the margin accounts, 95% of the options accounts and 39% of the cash accounts at those firms at the time of the study were subject to pre-dispute arbitration clauses. SEC Self-Regulatory Organizations; Order Approving Proposed Rule Changes by the New York Stock Exchange, Inc., National Association of Securities Dealers, Inc., and the American Stock Exchange, Inc., Relating to the Arbitration Process and the Use of Predispute Arbitration Clauses, Exchange Act Release No. 26805, [1989 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,414, at 80,111-3 (May 10, 1989). However, despite the adhesive nature of the customer agreement, the SEC and the securities industry's primary SROs mandated in 1989 that the securities industry could no longer prevent public customers from asserting claims by contractually precluding punitive damages, shortening statutes of limitation, or otherwise cutting off statutorily mandated rights, as they had done previously. *Id.* The release further states:

This provision makes clear that the use of arbitration for the resolution of investor/broker-dealer disputes represents solely a choice of arbitration as a means of dispute resolution. Agreements cannot be used to curtail any rights that a party may otherwise have had in a judicial forum. If punitive damages or attorneys fees would be available under applicable law, then the agreement cannot limit parties' rights to request them, nor arbitrators' rights to award them. The agreements may not be used to shorten applicable statutes of limitation, restrict the situs of an arbitration hearing contrary to SRO rules, nor to limit SRO forums otherwise available to parties.

Id. at 80,113

dispute resolution procedures offered under the Commodity Exchange Act ("CEA") are meant to be voluntary.³¹ They give the customer the right to forego arbitration and to file a claim in reparations, which is an administrative hearing before a U.S. administrative law judge.³² There is no jury trial in this proceeding. The customer can file a claim in reparations directly, but is also given forty-five days in order to choose reparations after demand by the IB or FCM to arbitrate under a pre-dispute agreement, since the right to adjudication in reparations cannot be waived.³³ A potentially significant drawback for the international public customer, however, is that under 17 C.F.R. § 12.13(b)(4)(A) of the rules governing reparations, a nonresident of the U.S. must post a bond for double the amount of the claim.

This does not mean that customers cannot arbitrate at the National Futures Association ("NFA") against a member firm where there is no pre-dispute agreement. Claims have been prosecuted in arbitration at the NFA without a pre-dispute clause based solely upon the membership of the IB and FCM at the NFA.³⁴ The NFA has its own arbitration rules,³⁵ and is a registered futures association with oversight by the CFTC.³⁶ Commodity futures disputes can also be heard in arbitration at other alternative dispute resolution institutions, as a matter of contract law, if the organization is listed as an alternative forum in the pre-dispute arbitration agreement (or, as occurs only occasionally, the parties agree to arbitrate in a post-dispute agreement), and under the proposed CFMA rules. The NYSE can also be a potential forum for commodities disputes when the respondent is a member of that exchange. However, although the NYSE's arbitration facility has been used success-

31. 17 C.F.R. § 180.3(a).

32. § 180.3(b)(3) ("The agreement may not require the customer to waive the right to seek reparations under section 14 of the [CEA, 7 U.S.C. § 18] . . ."). See also 17 C.F.R. § 12 (for the rules relating to reparations); *McGough v. Bradford*, 2000 CFTC Lexis 225 (C.F.T.C. Sept. 28, 2000).

33. § 180.3(b)(3).

34. NAT'L FUTURES ASS'N, CODE OF ARBITRATION ¶ 6017.1(a)(1)(i) (2001), available at <http://www.nfa.futures.org> (last visited Mar. 6, 2002) [hereinafter NFA CODE OF ARBITRATION]. This is similar to the rules in effect at the other SROs. See also *supra* note 12.

35. NFA CODE OF ARBITRATION, ¶ 6011.

36. CEA, 7 U.S.C. § 21 (2000).

fully for major futures cases, according to the Director of Arbitration, relatively few of these have been filed at the NYSE.³⁷ Under similar circumstances involving membership, the NASD-DR may also be an appropriate forum.³⁸

Some FCMs, by design, omit the pre-dispute arbitration clause in their contracts. In fact, one major firm utilizes a clause which attempts to require customers, regardless of their domicile, to litigate all claims in the unlikely venue of a court sitting in Chicago. But NFA arbitral jurisdiction can be invoked by filing customer claims against members, despite such onerous clauses requiring court litigation in a distant or otherwise highly inconvenient venue. Where the customer is adequately represented it is possible to negotiate alternatives in such instances, and, for example, to obtain the mutual agreement of the parties to arbitrate the dispute under the auspices of an established futures arbitral institution such as the NFA.³⁹

37. Telephone Interview with Robert S. Clemente, Director of Arbitration, New York Stock Exchange (Mar. 7, 2002).

38. Under the proposed customer protection rules of the CFMA, claimants who choose to file claims in arbitration must be provided with a list of forum choices such as the contract market relating to the transactions at issue, a registered futures association, such as the NFA and at least one other "qualified" arbitral organization. A New Regulatory Framework for Trading Facilities, Intermediaries, and Clearing Organizations, 66 Fed. Reg. 14262 (proposed Mar. 9, 2001) (to be codified at 17 C.F.R. pt. 166). The NYSE and NASD-DR admittedly do not track the number of commodity futures cases which may have been filed there. See *supra* note 18; N.Y. STOCK EXCH. R.R. 600(c), 635, 2 N.Y. Stock Exch. Guide (CCH) ¶¶ 2600, 2635. Such statistics were not available from the Directors of Arbitration. For court decisions and rulings of the CFTC, see, e.g., Comm. Fut. L. Rep. (CCH).

39. Section 180.3 of the C.F.R. provides that:

No futures commission merchant . . . shall enter into any agreement or understanding with a customer in which the customer agrees, prior to the time the claim or grievance arises, to submit such claim or grievance to any settlement procedure except as follows: . . . (3) *The agreement may not require the customer to waive the right to seek reparations* under section 14 of the [CEA] and part 12 of these regulations.

17 C.F.R. § 180.3 (2000) (emphasis added). See also § 180.3-6 (mandated disclosures of non-waiveability of the right to bring a reparation case). The CFMA retains these protections under Section 2(a)(i) of the NFA CODE OF ARBITRATION, in which a customer has the *absolute* right to demand arbitration of a dispute with a member of the NFA. NFA CODE OF ARBITRATION, ¶ 6017.1. In one instance, a consolidation of separate cases on behalf of thirteen

IV. INTERNATIONAL INVESTORS ARE PROTECTED FROM AND MAY SEEK REDRESS FOR FRAUDULENT ACTIVITY

For the most part, the purchase and sale of securities are governed and regulated by the SEC⁴⁰ pursuant to the Securities Act of 1933 ("1933 Act")⁴¹ and the Securities Exchange Act of 1934 ("1934 Act").⁴² Both statutes have anti-fraud provisions, primarily under section 12(2) of the 1933 Act,⁴³ and under Rule 10b-5 of the 1934 Act, section 10(b).⁴⁴ Investors in the commodity futures markets can also seek redress for damages as the result of fraudulent activity under section 4(b) of the CEA.⁴⁵ Except in rare instances, however, individual investors cannot

claimants, the parties entered into a stipulation that abrogated pre-dispute agreements to litigate in court in favor of the post-dispute stipulation to arbitrate under the auspices of the NFA. See National Futures Association, *Background Affiliation Status Information Center*, at <http://www.nfa.futures.org/bsic/details.asp?nfaid=001975&name=REFCO+LLC> (last visited Mar. 5, 2002) (for arbitral awards).

The arbitration was also illustrative of the potential for complexity in resolving such cases: hearings on the merits commenced in fall 1998 and the case concluded with closing arguments in spring 2001; it involved the testimony of fifty-nine witnesses during 104 days of hearings, comprising over 24,000 pages of transcripts, in which over 400 exhibits were entered into evidence. *Id.* The arbitrators issued awards aggregating in total approximately \$43 million in damages. *Id.* See also Peter A. McKay & Ruth Simon, *Group of Investors Gets Award of \$43 Million*, WALL ST. J., July 27, 2001, at C1.

40. The caveat to this general rule is that, while the SEC technically may have oversight authority over the arbitration process and rule changes thereof at the industry SROs pursuant to section 19 of the 1934 Act, as a practical matter, neither the SEC in the securities arena nor the CFTC in the futures industry has the ability to recover the claims of most public investors. 1934 Act § 19, 15 U.S.C. § 78s (2000). The attenuated exception is for commodities investor appeals from decisions in reparations proceedings against FCMs and other commodity professionals registered with the CFTC, which are adjudicated by administrative law judges or a CFTC hearing officer. A form of oversight may arise only because this process is administered by the CFTC, and subject to CFTC and U.S. federal court appellate review. See CEA, 7 U.S.C. § 18 (2000). See generally 13A JERRY W. MARKHAM, *COMMODITIES REGULATION: FRAUD, MANIPULATION & OTHER CLAIMS* § 20.01 (2000).

41. 1933 Act, 15 U.S.C. §§ 77a-77mm (2000).

42. 15 U.S.C. §§ 78a-78bbbb.

43. 15 U.S.C. § 77l(2).

44. 15 U.S.C. § 78j(b).

45. 7 U.S.C. § 6b.

rely on the SEC, the CFTC or the SROs to prosecute their claims of fraud. Only through private civil court actions, arbitration, or reparations proceedings can both international and domestic customers seek compensation.

A. *Theories of Liability*

Claims against U.S. broker-dealers and FCMs, as well as their agents and employees, can be asserted under various theories of liability arising under statutory schemes and the common law. These include: (1) illegal trading where profitable trades and trades generating losses are shifted in and out of accounts of unsuspecting investors; (2) brokers who do not have written power of attorney engaging in unauthorized trading; (3) misrepresentations and omissions of material facts made by brokers in their recommendation of a purchase or sale; (4) brokers who fail to disclose the risks involved in a purchase or sale being recommended to the customer; and (5) market manipulation, to name a few.⁴⁶ Depending upon the facts, other claims that may be asserted are: (1) claims of churning or excessive trading, which may include excessively high turnover in the account and trading effectively controlled by the broker for the purpose of generating commissions which are not in the customer's best interest, among other indicia; (2) unsuitable investments, which include investments recommended by a broker which are not in accordance with the customer's stated investment objectives or not in accordance with the customer's financial condition or tolerance for risk; (3) breach of fiduciary duty; (4) breach of contract; (5) negligence; (6) gross negligence; (7) misrepresentation; and (8) in certain limited instances, violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"),⁴⁷ among others.⁴⁸ Ancillary claims in support of primary fraud causes of action may be asserted in some cases:

46. See generally MARKHAM, *supra* note 40, §§ 14-26; 3 ALLAN R. BROMBERG & LEWIS D. LOWENFELS, BROMBERG AND LOWENFELS ON SECURITIES FRAUD & COMMODITIES FRAUD § 8 (2d ed. 2001) [hereinafter 3 BROMBERG AND LOWENFELS].

47. Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (2000) [hereinafter RICO]. See generally JED S. RAKOFF, RICO: CIVIL AND CRIMINAL LAW AND STRATEGY § 7.04[2] (2000).

48. See generally MARKHAM, *supra* note 40, §§ 14-26; 3 BROMBERG & LOWENFELS, *supra* note 46.

(1) for a firm's failure to properly supervise its salespersons; (2) violation of industry rules and regulations; (3) technical record keeping violations which may enable fraudulent activity; (4) violation of the firm's own policies, rules and regulations; and (5) failure to execute orders in a timely manner.⁴⁹

B. Procedural Considerations

As has been discussed previously, SRO arbitral institutions, such as exist at the NYSE, the NASD-DR and the NFA, administer their own rules of procedure and have great latitude in running arbitration hearings. For example, arbitrators are not technically required to follow the formal rules of evidence.⁵⁰ Thus, more testimony and documentary proof may be accepted into the record than in formal court proceedings. While the court system in the U.S. at both the state and federal level allows for appellate review, there are only limited grounds promulgated under the FAA, such as corruption by the arbitrators, and a limited, judicially created basis ("manifest disregard of the law") by which an arbitration award can be vacated or modified in a court proceeding.⁵¹

49. See, e.g., *In re GNP Commodities, Inc.*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,360, at 39,214 (C.F.T.C. 1992), *aff'd*, *Monieson v. Commodity Futures Trading Comm'n*, 996 F.2d 852 (7th Cir. 1993) ("[F]ailing to place account numbers on order tickets does provide an opportunity to direct profitable fills to favored accounts, and [anti-fraud] section 4b of the CEA prohibits this type of allocation of winning and losing trades."). Under the securities laws and case law, there is virtually no private right of action for violation of stock exchange or other industry rules. However, these allegations are in practice almost always linked to viable primary claims such as statutory fraud violations, breach of fiduciary duty, breach of contract and negligence. See, e.g., 4 ALLAN R. BROMBERG & LEWIS D. LOWENFELS, BROMBERG AND LOWENFELS ON SECURITIES FRAUD & COMMODITIES FRAUD § 15.06 (2d ed. 2001) [hereinafter 4 BROMBERG & LOWENFELS].

50. See, e.g., ARBITRATOR'S MANUAL, *supra* note 22, at 29.

51. The FAA provides that an award may be vacated:

(1) where the award was procured by corruption, fraud or undue means.

(2) where there was evident partiality or corruption in the arbitrators. . . .

(3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any

V. PROCEDURAL AND TACTICAL ISSUES FOR INTERNATIONAL CLAIMANTS

Some of the idiosyncrasies of the rules of practice in the U.S. may be unfamiliar to international claimants. Yet, invariably, and almost intuitively, these clients nevertheless raise questions about defenses they may be subject to, such as statutes of limitations, the potential duty to mitigate and the always popular defense based on the concept of "inquiry notice."

A. *Statutes of Limitations and Eligibility Rules*

Although both the CEA and the securities laws provide for private rights of action for claims of fraud,⁵² there are material differences in the statutes of limitations: two years from discovery of the fraud under the CEA⁵³ and one year from the discovery of the fraud, but no more than three from the accrual of the claim, under section 12(2) of the 1933 Act and section 10b of the 1934 Act.⁵⁴ There is generally an outside limit on the

other misbehavior by which the rights of any party have been prejudiced.

(4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

Federal Arbitration Act, 9 U.S.C. § 10(a)(1)-(4) (2000). For the tension arising in the judicial interpretation of the "manifest disregard" non-statutory ground for setting aside awards, see, e.g., *George Watts & Son, Inc. v. Tiffany & Co.*, 248 F.3d 577, 581 (7th Cir. 2001) ("[T]he 'manifest disregard' principle is limited to two possibilities; an arbitral order requiring the parties to violate the law . . . and an arbitral order that does not adhere to the legal principles specified by contract, and hence unenforceable under [section] (10)(a)(4).") (citing *Eastern Associated Coal Corp. v. United Mine Workers of America*, 531 U.S. 57, 62 (2000)). Cf. *Halligan v. Piper Jaffrey, Inc.*, 148 F.3d 197, 204 (2d Cir. 1998) ("[W]here a reviewing court is inclined to find that arbitrators manifestly disregarded the law or the evidence and that an explanation, if given, would have strained credulity, the absence of explanation may reinforce the reviewing court's confidence that the arbitrators engaged in manifest disregard."). As discussed previously, following reparations proceedings in commodity cases, appeals are taken to a panel of CFTC commissioners and then to a federal circuit court of appeals.

52. See *supra* notes 43-45.

53. CEA, 7 U.S.C. § 25(c) (2000).

54. The affirmative defense of the statute of limitations, governed by a number of sections in the securities laws, including section 13 of the 1933 Act and sections 9(e), 19(c) and 29(b) of the 1934 Act, is too broad a topic for dis-

ability to bring claims in SRO arbitration under the six year "eligibility" rule at the NYSE and the NASD, which, under the Uniform Code, "does not extend applicable statutes of limitation."⁵⁵ The NFA has a meager two year timeliness rule, which tracks the two year statute of limitations under the CEA.⁵⁶ The shorter two year NFA rule has the potential to create a serious conflict when state or federal statutory and common law claims of fraud, breach of fiduciary duty, breach of contract and others have longer statutes of limitations.⁵⁷

discussion here. It is important to note, however, that in 1991, the Supreme Court eliminated some of the complexity by holding that state borrowing provisions, which vary widely across the fifty plus U.S. jurisdictions, would no longer provide the basis for calculating statutes of limitations under the 1934 Act. See *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350 (1991). See generally *ESTATE OF LOUIS LOSS & JOEL SELIGMAN, FUNDAMENTALS OF SECURITIES REGULATION 1261-74* (4th ed. 2001).

55. *The Resolution of Securities Disputes*, *supra* note 11, at 324. NYSE Rule 603 also states:

No dispute, claim or controversy shall be eligible for submission to arbitration under this Code where six (6) years shall have elapsed from the occurrence or event giving rise to the act or the dispute, claim or controversy. This section shall not extend applicable statutes of limitations, nor shall it apply to any case which is directed to arbitration by a court of competent jurisdiction.

N.Y. STOCK EXCH. R. 603, 2 N.Y. Stock Exch. Guide (CCH) ¶ 2603. The NASD-DR rule states essentially the same thing. NASD-DR ARBITRATION CODE, § 10304.

56. NFA CODE OF ARBITRATION, ¶ 6035, §5 & ¶ 6041, § 6(c). Section 5 states:

No Demand for Arbitration may be arbitrated under this Code unless a Demand or notice of intent to arbitrate . . . is received by NFA within two years from the date when the party filing the Demand for Arbitration knew or should have known of the act or transaction that is the subject of the controversy If, in the course of any arbitration, the Panel determines that the requirements of this section have not been met as to a particular claim, the Panel shall thereupon terminate the arbitration of the claim without decision or award.

Id. ¶ 6035, § 5. Section 6(c) provides: "NFA shall reject any claim that is not timely filed, or for which the appropriate fee has not been paid." *Id.* ¶ 6041, § 6(c). The CEA provides: "Any such action shall be brought not later than two years after the date the cause of action arises." 7 U.S.C. § 25(c).

57. If a claim which may have already been accepted for adjudication by the NFA is found in the course of an arbitration to be ineligible ab initio un-

*B. The Adversarial Nature of the Arbitration Procedure:
Affirmative Defenses and Counterclaims*

Not unlike litigation in general, arbitration claimants in securities and commodities disputes frequently grapple with novel issues and aggressive defense tactics. This is particularly evident in the securities context, in which an adverse award with written findings must be reported and usually ends up disclosed in the individual securities broker's Form U-4 or U-5⁵⁸ and Central Registration Depository ("CRD") reports.⁵⁹

der the NFA two-year rule, the panel of arbitrators has the authority to terminate that claim "without decision or award." NFA CODE OF ARBITRATION, ¶ 6035, § 5. Hypothetically, a claimant at the NFA can thus be placed in the untenable position (and the expense) of prosecuting a claim that was initially accepted for adjudication by the forum, which may later be determined to be ineligible under the short two-year rule. Thus, diligence in timely filing claims is absolutely necessary. Some courts have determined that eligibility rules, as opposed to timeliness considerations, are not statutes of limitations, and issues arising under these time bars are matters for the courts, not the arbitrators, to decide. *See, e.g., Edward D. Jones & Co. v. Sorrells*, 957 F.2d 509, 512-13 (7th Cir. 1992).

"A contrary line of authority leaves it to the arbitrators to deal with the six-year limitation period" generally regarding the limitation as procedural and a matter to be decided by the arbitrators. 4 BROMBERG & LOWENFELS, *supra* note 49, § 16.01(800). In New York, issues of timeliness, whether viewed as an eligibility rule or as a procedural statute of limitations, are in the province of the arbitrators and not the courts. *See Smith Barney Shearson Inc. v. Sacharow*, 689 N.E.2d 884, (N.Y. 1997); *PaineWebber, Inc. v. Bybyk*, 81 F.3d 1193, 1199 (2d Cir. 1996). As a result of an apparent conflict in the decisional law among the U.S. federal circuit courts concerning the complex issue of whether arbitrability matters are best decided by the courts or the arbitrators, the Supreme Court recently agreed to resolve the issue. *See Dean Witter Reynolds, Inc. v. Howsam*, 261 F.3d 956 (10th Cir. 2001), *cert. granted*, 70 U.S.L.W. 3385, 3530, 3533 (U.S. Feb. 25, 2002) (No. 01-800).

58. The U-4 is the form used for the required NASD registration of individuals associated with a brokerage firm, which itself must register with the NASD using registration Form BD. These forms also serve as the application for registration with the SEC. Exchange Act Release No. 31,660, [1992-1993 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 85,101 (Dec. 29, 1992). The Form U-5 is filed upon termination of registration. *See NAT'L ASS'N SEC. DEALERS, NASD MANUAL & NOTICE TO MEMBERS* §§ 3070-80 (2001), *available at* <http://www.nasdr.com> (last visited Mar. 6, 2002) [hereinafter *NASD MANUAL AND NOTICE*].

59. The CRD report is a publicly available filing maintained by the NASD which, among other things, lists a history of prior customer complaints against individual account executive registrants and broker-dealers. It is a highly useful tool for the investigation of the broker who is the subject of a

Arbitration of these customer disputes, especially in large and complex cases, more nearly resembles court litigation than the simplified procedure that proponents of compulsory arbitration envisioned in the pre-*McMahon* era—a trend that is mirrored in international commercial arbitration.⁶⁰ In securities and commodity futures arbitrations, a claimant is likely to encounter the gamut of both affirmative defenses and preemptively asserted or baseless counterclaims, which often attempt to portray the investor as the culprit instead of as the victim. Such tactics, if played out in a U.S. court, might be subject to statutory sanctions. Examples include the assertion of groundless racketeering counterclaims,⁶¹ a commonly asserted defense that tax motivated trading caused the customer's losses, and even the dubious defense of a major FCM alleging that a European customer, with no prior investment experience, somehow

customer claim. NASD Regulation, Inc., in its *BROKER/DEALER FIRM USER'S MANUAL*, defines the CRD report system as:

[D]eveloped jointly by the [NASD] and the North American Securities Administrators Association . . . CRD was first launched in 1981 to centralize the registration process for the securities industry. . . . CRD made it possible to complete and send one application for an individual to be registered in all jurisdictions. . . . Over the past two (2) decades, the system has been expanded and modified extensively to meet the evolving needs of the NASD's constituencies. CRD currently maintains this information for more than half a million registered securities employees of member firms.

NASD REGULATION, *BROKER/DEALER FIRM USER'S MANUAL 2* (2002), available at http://www.nasdr.com/webcrd_manual.asp (last visited Mar. 5, 2002). For publicly available information about NASD member firms and their associated persons, see NASD Regulation, *NASD Regulation Public Disclosure Program*, at <http://www.nasdr.com/2001.asp> (last visited Mar. 5, 2002).

60. See generally Christopher R. Drahozal, *Commercial Norms, Commercial Codes, and International Commercial Arbitration*, 33 *VAND. J. TRANSNAT'L L.* 79, 96 (2000) ("Procedurally, international commercial arbitration is becoming more and more like public court litigation, particularly public court litigation as practiced in the United States.").

61. Note that securities fraud allegations based on predicate acts of mail and wire fraud under 18 U.S.C. §§ 1341, 1343, respectively, may no longer form the basis for a RICO claim or counterclaim, pursuant to the 1995 amendment to the RICO statute. RICO, 18 U.S.C. § 1964(c) (2000). See also Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, sec. 107, § 1964(c), 109 Stat. 737, 758 ("[N]o person may rely upon any conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of [RICO] section 1962.").

"knew" of the risks because she was warned by the account executive when opening the account that customers who manage their own funds only have about a 10% success rate in the financial futures marketplace.⁶² It is often the case that the foreign investor, mystified by, and with many questions concerning such tactics, should be introduced to the intricacies and challenges involved in winning a case of financial fraud. The following are just some of the more common defenses.

1. Defense of Contributory Negligence

The defense of contributory negligence is frequently asserted despite the fact that, under common law, contributory or comparative negligence are not defenses to intentional torts such as fraud.⁶³ Nor may contributory or comparative negligence arguments form a valid basis for a defense to fraud by the party who committed the fraud in cases alleging RICO violations.⁶⁴ In *Teamsters Local 282 Pension Trust Fund v. Angelos*, a securities case, the Court of Appeals for the Seventh Circuit emphasized that it would defeat the liquidity and efficiency of the markets to require a potential victim to take elaborate precautions against fraud, stating:

An ordinary investor is under no duty to investigate, though, and many people invest large sums in reliance on representations made to them or on the accuracy of the market price of the investment. The self-interest of those who seek to maintain reputations for honest dealing, and the legal rules against fraud, are the primary guarantors of the accuracy of representations in securities transactions. Investors are entitled to rely on these incentives to speak the truth and to recover damages from those who breach their duty to speak truthfully.⁶⁵

62. If accurate, such a warning would have dissuaded any sane person from opening the account in the first place.

63. See *Greycas, Inc. v. Proud*, 826 F.2d 1560, 1562 (7th Cir. 1987); *City of New York v. Corwen*, 565 N.Y.S.2d 457, 460 (N.Y. App. Div. 1990).

64. *Blue Cross and Blue Shield of New Jersey v. Phillip Morris, Inc.*, 36 F. Supp. 2d 560, 575-76 (E.D.N.Y. 1999); RESTATEMENT (SECOND) OF TORTS, § 545A (1977) ("One who justifiably relies upon a fraudulent misrepresentation is not barred from recovery by his contributory negligence in doing so.").

65. *Teamsters Local 282 Pension Trust Fund v. Angelos*, 762 F.2d 522, 526 (7th Cir. 1985).

The same duty of care extends to commodity claimants. Under the CEA, courts have routinely held that a "customer does not have a duty to investigate the truth of the statements made to him, but may ordinarily rely on the honesty of his account representative's representations."⁶⁶ As case law illustrates, the assertion of this defense is far from a guarantee that the respondent will prevail. Under New York law, and in most other jurisdictions in the U.S., the basic elements necessary to sustain a claim of fraud and misrepresentation sufficient to vitiate a respondent's risk disclosures are: (1) misrepresentation of a material fact; (2) the falsity of that misrepresentation; (3) scienter, or intent to defraud; (4) reasonable reliance on the misrepresentation; and (5) damage caused by such reliance.⁶⁷

In *Indosuez Carr Futures, Inc. v. Commodity Futures Trading Commission*, an account executive was less than candid in telling the customer that account statements should be disregarded because, even though they were inaccurate, that did not matter since the customer's non-discretionary account was hedged.⁶⁸ The Court of Appeals for the Seventh Circuit found that the customer's reliance was justifiable, since the "misrepresentations extended to the validity of the documents themselves."⁶⁹ In *Commodity Futures Trading Commission v. Rosenberg*, a broker's misrepresentations in reporting erroneous account balances and unlawful, unauthorized trading activity, for which the FCM was held vicariously liable, were deemed to "constitute information that a reasonable investor would consider important in trading commodity futures and options on futures," and were held to be in violation of the

66. *Jakobsen v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,812, at 31,393 (C.F.T.C. 1985). See also *In re GNP Commodities, Inc.*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,360 (C.F.T.C. 1992); *Astor Chauffeured Limousine Co. v. Runnfeldt Inv. Corp.*, 910 F.2d 1540, 1550 (7th Cir. 1990) ("[A] liar may not lull the victim into a false sense of security and then say that the reliance was not justifiable.").

67. See *Granite Partners, L.P. v. Bear, Stearns & Co., Inc.*, 58 F. Supp. 2d 228, 257 (S.D.N.Y. 1999).

68. *Indosuez Carr Futures, Inc. v. Commodity Futures Trading Comm'n*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,125, at 41,718 (7th Cir. 1994).

69. *Id.* at 41,723.

CEA.⁷⁰ The CFTC has opined that “[j]ustifiable reliance is not a theory of contributory negligence, but rather is concerned with the causal connection between the misrepresentation and complainant’s loss.”⁷¹ Thus, a finding of non-reliance by a customer would necessarily imply that the customer “would have acted no differently had he known the truth.”⁷²

2. Defense of Duty to Mitigate

The CFTC has held that “the duty to mitigate does not even arise in the context of fraudulent inducement” where there is no awareness by the customer of the material facts, and the broker has concealed his fraud.⁷³ This recognizes the fact that such customers are susceptible to being deceived by the false information: “Indeed, [the customer] was the victim of a fallacy that frequently affects the reasoning of investors—he allowed the accidental or random success of [the broker’s] initial trading to confirm the false information conveyed to him concerning the ability of [the broker’s] program to produce profit while controlling risk.”⁷⁴ In this case, though the investor was the one who was duped by false representations, the CFTC deemed the FCM liable for its IB’s duplicitous activity.⁷⁵

3. Defense of Ratification

Respondents may also allege that a claimant’s actions are barred by the doctrine of ratification, and may also assert the related doctrines of waiver and estoppel, under the theory that the claims should fail as a matter of law because the claimant knowingly and voluntarily assented to them after they occurred. This defense is similar to that used by the defendant in *Karlen v. Ray E. Friedman & Co. Commodities*, in which

70. *Commodity Futures Trading Comm’n v. Rosenberg*, 85 F. Supp. 2d 424, 447-48 (D.N.J. 2000) (citing *Commodity Futures Trading Comm’n v. Skorupskas*, 605 F. Supp. 923, 932-33 (E.D. Mich. 1985)) (finding issuance of false monthly statements constituted fraud in violation of the CEA).

71. *Jakobsen*, [1984-1986 Transfer Binder] *Comm. Fut. L. Rep.* (CCH) at 31,392.

72. *Id.*

73. *Levine v. Refco, Inc.*, [1987-1990 Transfer Binder] *Comm. Fut. L. Rep.* (CCH) ¶ 24,488, at 36,116 (C.F.T.C. 1989).

74. *Id.*

75. *Id.*

the owners of a South Dakota cattle ranch sued their Chicago broker for unauthorized trading and churning.⁷⁶ The FCM based its defense on: (1) the plaintiffs' testimony that the broker plausibly convinced the customer, who called to object to unauthorized trades, that everything was in order; (2) the admission that the plaintiffs received confirmation slips for all trades and monthly activity statements; and (3) the fact that the plaintiffs "continued to invest substantial funds into their accounts even though [the broker] allegedly was disobeying their directions, and they were suffering significant losses."⁷⁷ In *Karlen*, despite the alleged complacency of the plaintiffs, who were lulled by their broker into inaction, the Court of Appeals for the Eighth Circuit refused to accept the defense of ratification on the basis of the defendant's deception.⁷⁸ In affirming the plaintiffs' verdict below, the court squarely addressed the issue of ratification: "The question is not simply whether Karlen assented to the trades; rather it is whether his apparent assent was given voluntarily and intelligently with full knowledge of the facts."⁷⁹ The court emphasized the complexity of the commodities markets and the confusing character of the materials provided by the broker, in which the statements sent to the plaintiffs did not include all trades and used confusing, technical language.⁸⁰

Courts have thus declined to find ratification where an agent has acted fraudulently or in a manner designed to prevent customers from obtaining full knowledge of the trading activity. In another example, *Drexel Burnham Lambert Inc. v. Commodity Futures Trading Commission*, investors sued a wayward commodities broker for unauthorized trades.⁸¹ In affirming the CFTC decision against the broker, the Court of Appeals for the District of Columbia was steadfast in its support of the unwitting customers:

76. *Karlen v. Ray E. Friedman & Co. Commodities*, 688 F.2d 1193 (8th Cir. 1982).

77. *Id.* at 1197-98.

78. *Id.* at 1198.

79. *Id.*

80. *Id.* at 1198-1200.

81. *Drexel Burnham Lambert Inc. v. Commodity Futures Trading Comm'n*, 850 F.2d 742 (D.C. Cir. 1988).

Circuit courts . . . have also deemed knowledge of the relevant facts and an intent to approve the unauthorized action after its occurrence to be preconditions to ratification.

. . . There is no evidence that [the customers were] aware that the checks they signed were to fund [the broker's] trading losses rather than the Treasury bill arbitrage program they were pursuing.⁸²

The confirmation reports and monthly statements which brokers usually rely upon to establish that somehow a claimant was able to determine the status of his accounts cannot be used for that purpose either, where a fraud has been committed against the investor. The *Karlen* court is again instructive:

Karlen's inability to determine the current status of the accounts from the documents sent by Friedman is understandable. [The broker] executed a large number of trades in a short period of time, and Karlen had little experience in commodities to assist him in understanding the transactions. . . . Moreover, the plaintiffs were inundated with a large volume of documents of various types that had differing purposes which Friedman did not describe. Indeed, the documents used technical terms that did not plainly or precisely explain to an inexperienced or unsophisticated trader the information that they were providing. In fact, because the year-end and monthly activity statements sent by Friedman reported only closed transactions, they could convey seriously inaccurate impressions concerning the status of the accounts. For example, as the defendant concedes, the year-end statement for 1974 actually showed a \$1,000 profit, even though Karlen lost thousands of dollars that year when all outstanding contracts were finally closed.⁸³

The law is also clear that "[w]hen a customer lacks the skill or experience to interpret confirmation slips, monthly statements or other such documents" the broker is liable.⁸⁴ As rec-

82. *Id.* at 750. See also *Lazzaro v. Manber*, 701 F. Supp. 353, 363 (E.D.N.Y. 1988) (deeming defendants' claim of ratification insufficient to dismiss a 10b-5 securities fraud action where investors claimed they lacked full knowledge and were unaware of risks due to manipulations and misrepresentations).

83. *Karlen*, 688 F.2d at 1200.

84. *Id.*

ognized by the Court of Appeals for the Eighth Circuit in *Karlen*, as well as by other courts, the duty lies with the broker:

[C]onfirmation slips and monthly statements do not enable a customer to determine his or her overall position or the total amount of real profit or loss occurring, unless the customer is sufficiently skilled to elaborate upon them to make that determination. . . . courts have generally refused to find that they relieve a broker of liability for its misconduct.⁸⁵

4. The "Boilerplate" on the Back of a Broker's Statements, in Confirmations, and in Customer Agreements, Do Not Give Rise to a Valid Ratification Defense

In *Karlen*, the circuit court rejected a typical ratification defense, based on its lengthy examination of the confirmations and monthly statements, including the pro forma legend on the back of the broker's documents:

Friedman confirmed each trade by mailing the plaintiffs, on the morning after the trade, a written confirmation slip describing the type, price and quantity of the commodity traded. In addition, each month Friedman mailed to the plaintiffs an activity statement which reported trades executed during the preceding month, the net profit or loss on transactions that were closed that month, and an account balance reflecting the closed transactions. Each monthly activity statement was accompanied by a document entitled "Statement of Account-Open Trades." These documents reported under the column title "open trade equity," the profit or loss that would have been recognized on all open contracts if they had been closed on the final day included in the monthly statements. The phrase "open trade equity" was not defined or explained in the "Statement of Account-Open Trades" document. Finally, Friedman, from time to time, mailed documents entitled "Statement of Account-Purchase and Sale." Although the purpose of these forms was not described in the record, they were apparently sent when the plaintiffs either deposited funds or closed out their position in any futures contract. All of the documents mailed by the defendant included the name, address and telephone number of Friedman, and contained

85. *Id.* (citations omitted).

the legend: "NOTE: PLEASE REPORT ANY DIFFERENCES IMMEDIATELY."⁸⁶

Numerous other cases have also held that the exculpatory effect of a pro forma risk disclosure statement will be vitiated where the risks of trading are undisclosed or misrepresented.⁸⁷ In *Reed v. Sage Group, Inc.*, the CFTC held that standard risk disclosures are a mere formality, and that boilerplate risk disclosure cannot cure false information and misrepresentations.⁸⁸ Depending on the relationship between the customer and broker, such as cases in which accounts are discretionary, fiduciary obligations may be viewed as more expansive, obligating the broker to disclose *more* than what appears in the standard risk disclosure statement. In *Hannay v. First Commodity Corp.*, the CFTC held that risk disclosures are not dispositive and do not vitiate misrepresentations: "We repeatedly have held that conduct can vitiate the effect of the risk disclosure statement mandated by our rules."⁸⁹

5. Additional Considerations Regarding the Arbitration Process

There are a few other important issues that should be of interest to the international claimant. Securities and commodity futures cases often arise from dealing with SRO member firms that have overseas offices, where international customers may be more conversant than U.S. citizens with financial futures, different currencies and exchange rates. Consistent with the case law cited previously, this does not permit the inference

86. *Id.* at n.7.

87. *See, e.g.,* *Oram v. Nat'l Monetary Fund*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,670 (C.F.T.C. 1987) (risk disclosure not dispositive of reliance where misrepresentations were claimed); *Hannay v. First Commodity Corp.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,936 (C.F.T.C. 1987) (claims of profitability vitiate effect of risk disclosure statement); *Miller v. First Commodity Corp.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,215, at 32,586 (C.F.T.C. 1986) (Exaggerated predictions of "virtually unattainable rate of return" are not negated by risk disclosure statement.).

88. *Reed v. Sage Group, Inc.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,943, at 34,304 (C.F.T.C. 1987).

89. *Hannay*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) at 34,282.

that non-U.S. citizens are sophisticated investors solely on the basis of their familiarity with currency exchange or their conduct of transnational business. Indeed, broker conduct at international branch offices of U.S. broker-dealers can suffer from poor supervision and, as a consequence, brokers at these branches may be more inclined to dispense with following the firm's policies, rules and regulations, even though they are still subject to U.S. law and exchange rules and regulations.

Claimant's counsel usually require expert assistance to understand the intricacies of the markets and how particular products work, and to assist in prosecuting cases either in arbitration, reparations proceedings or in court. More than one expert may be necessary to testify for the claimant in the larger damage case in which, aside from requiring expert testimony on damage theories and calculations, there are back office and supervisory issues, and specific defenses that call for the experience and knowledge of qualified experts who have practiced in the field.

In the event that claimant's counsel deems it necessary to pursue the testimony of former employees of the brokerage firm, there may be some obstacles to obtaining the presence of witnesses domiciled outside the venue of the arbitration forum or outside the U.S.⁹⁰ However, as current account executives and supervisors of foreign branch offices are presumptively registered individuals at the NYSE, NASD, or both, they are required by the forum to appear as a consequence of their registration status.⁹¹ If such individuals are sued personally, jurisdiction usually attaches even though they may have left the industry for several years. The same rule applies with respect to CFTC and NFA registrants.⁹² Similarly, if witnesses are still employed by the firm being sued, even if the witnesses are not registered, they will have to abide by a request from the arbitration panel to appear and testify. Resort should be made to the rules of the forum in which the case is pending and the ap-

90. See generally FED. R. CIV. P. 45; 28 U.S.C. § 1783 (2000) (covering service of subpoenas directed to a witness present in the U.S. or in a foreign country, who is a national or resident of the U.S., respectively).

91. See sources and text cited *supra* note 12.

92. See NFA CODE OF ARBITRATION ¶ 6017.1(a)(1)(i). On retention of jurisdiction, see, e.g., NASD MANUAL AND NOTICE, *supra* note 58, art. III, § 6, art. IV, § 4 & art. V, § 4.

propriate jurisdiction from which subpoenas can be issued in order to have the ability to call all the important witnesses to testify.⁹³

Arbitration is a private matter. As opposed to court proceedings, arbitration cases are held behind closed doors and are not open to the public. Because of the private nature of the process, confidentiality agreements are commonplace with respect to information and documents exchanged by the parties and exhibits entered into evidence at the hearings. When cases are settled prior to an award being rendered by the arbitration panel, the settlements usually contain confidentiality provisions. Arbitration awards, however, are made publicly available by the NASD-DR, NYSE and NFA.⁹⁴

Smaller cases can usually be arbitrated in several days, but the large and complex cases take many days, if not months, to hear. It is not unusual for cases of this genre to stretch out for a period of two to three years, in part because arbitrators have other pursuits, but, unlike judges, they do not sit on a case from day to day until concluded, and may only set aside two or three days a month to conduct hearings. Likewise, the attorneys for the parties may have other trial commitments that make adjournments and delays inevitable.

In almost all cases, preliminary hearings, also known as "initial pre-hearing conferences," are advisable so that the arbitrators can resolve discovery disputes between the parties and other pre-trial matters.⁹⁵ But, discovery in arbitration is relatively limited compared with discovery obtainable in a court proceeding, especially when arbitrators are inclined to interpret requests narrowly; however, counsel usually can prevail by drafting comprehensive demands and requesting rulings

93. See FED. R. CIV. P. 45; 28 U.S.C. § 1783.

94. NASD-DR awards are available online on its website, <http://www.nasdadr.com>, and are required to be made publicly available. See NASD-DR ARBITRATION CODE, R. 10330(f). NYSE awards are accessible online at <http://www.nyse.com/arbitration/decisions>. The NFA provides summary awards online at <http://www.nfa.futures.org/basic> (access requires knowledge of the name of the broker or case identification number). Most are available through Securities Arbitration Commentator, Inc., at <http://www.sacarbitration.com>.

95. See NASD-DR ARBITRATION CODE, R. 10321(d)(1); N.Y. STOCK EXCH. R. 619(d)(1), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2619.

when those demands are unfulfilled. In court, each party can take pre-trial depositions, proceedings in which statements from witnesses and parties are taken under oath and documents are produced. Non-party witnesses are also subject to depositions. Deposition discovery not only lengthens the time period of court litigation but also adds to the cost of the proceedings. These are two fundamental reasons why, except under extraordinary circumstances, depositions are usually not permitted in arbitration.

The arbitrators at the SROs, by regulation, must render an award within thirty days of the close of the proceedings and record, unless otherwise provided.⁹⁶ An additional advantage of SRO arbitration is that members must pay arbitration awards promptly or be subject to regulatory sanction and possible suspension of their licenses to operate.⁹⁷

VI. CONCLUSION

Many international investors have an opportunity to obtain damage awards in the U.S. either through cases brought in

96. See NASD-DR ARBITRATION CODE, R. 10330(h); NASD MANUAL & NOTICE, *supra* note 58, art. VII, § 3; N.Y. STOCK EXCH. R. 627(d), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2627; NFA CODE OF ARBITRATION, ¶ 6059.7(g), § 10.

97. See NASD-DR ARBITRATION CODE, R. 10330(h); NASD MANUAL & NOTICE, *supra* note 58, art. VI, § 3; N.Y. STOCK EXCH. R. 627(g), 2 N.Y. Stock Exch. Guide (CCH) ¶ 2627; NFA CODE OF ARBITRATION, ¶ 6059.7(g), § 10. While motions (or petitions) to vacate arbitration awards are rarely granted, the NASD-DR has promulgated regulations governing the requirement that awards be paid to the customer within thirty days following the granting of a motion (or petition) to affirm the award in court. The relevant section providing for sanctions for noncompliance states:

The NASD after 15 days notice in writing, may suspend or cancel the membership of any member or the registration of any person in arrears in the payment of any fees, dues, assessments, or other charges or for failure to furnish any information or reports requested pursuant to Section 2, or for failure to comply with an award of arbitrators properly rendered pursuant to the Rules of the Association, where a timely motion to vacate or modify such award has not been made pursuant to applicable law or where such a motion has been denied, or for failure to comply with a written and executed settlement agreement obtained in connection with an arbitration or mediation submitted for disposition pursuant to the Rules of the Association.

NASD MANUAL AND NOTICE, *supra* note 58, art. VI, § 3. See also sources and text cited *supra* note 51.

arbitration, court or reparations proceedings. For any aggrieved investor, it is advisable to investigate claims thoroughly prior to initiating proceedings, since a great deal of time and expense can be expended before and at the hearings, and it is essential to explore whether one has a solid case before such a commitment is made. Although the rights and remedies of investors are primarily governed by statute and within the customer agreement, the foreign branch offices of U.S. broker-dealers and FCMs are subject to arbitration procedures based upon the membership of those firms at SROs, such as the NYSE, NASD-DR and the NFA. In all cases, individuals and companies who have been unfairly treated should consult professionals who are knowledgeable in this area for a review of their rights and remedies.

