SANCTIONS BY ARBITRATORS

Surveying Readiness, Flexibility, and Measured Responses

By Samantha B. Rabin*

INTRODUCTION

Sanctions imposed by arbitrators serve as a tool to ensure compliance with Panel orders, arbitration rules, and accepted standards of decorum during the proceedings in securities arbitration. Arbitrators have, in recent years, demonstrated a readiness, as seen in the Awards we reviewed for this article, to sanction parties for their inappropriate behavior (or that of their counsel). They have also shown a considerable degree of flexibility in fashioning such sanctions, suggesting that Panels are imposing creative "punishments," more suitable to the perceived "crime."

Whether or not those sanctions were deserved is a judgment this survey of Awards is neither designed, nor able, to address. Explanations in the Awards of the circumstances surrounding a sanction are often cryptic, if there at all. The Awards do reflect the terms of the sanction and, usually, the general reasons why the Panel acted. There is no question that, through both rule changes and training, securities arbitrators have been encouraged to exercise greater control in the arbitration proceedings. Many believe that Panels have, for too long, "spared the crop."

Anecdotally, we have certainly noticed, in our preparation of SAC's *Award Reporter* for publication each month an increasing number of Awards where sanctions were assessed. There have been so many, in fact, that, in selecting Awards to highlight each month on the *Reporter's* cover sheet, we have had to limit the number of sanction-related Awards, in order to allow space for coverage of other types of significant Awards as well. To attempt to put a finer point on this perceived trend, we reviewed NASD and NYSE Awards rendered during the last several years — 1996 through the present. Within this period, we found 246 Awards in which sanctions were seriously considered by the Arbitrators. We also found that some form of sanction was actually imposed in two-thirds of those instances.

PANEL RESPONSES TO PARTY FAILURES & BAD CONDUCT

In the Charts below, our findings are grouped into categories. Within each category are subsections that track the various phases of the arbitration process in a loose chronological fashion. I use the term "loose," because there is overlap among the phases in the conduct that produced the sanction. The Charts do not reflect all of the "sanctions" Awards reviewed. For ease of presentation, we limited those cited in number and forum, endeavoring to focus on a sample which illustrates the diverse range of sanctions employed by the arbitrators.

Do not underestimate our securities arbitrators. If nothing else, when you have finished reading this section, it will be clear to you that arbitrators, although patient and generally measured in their responses, will rein in disruptive and abusive behavior, and will use the ultimate sanction of dismissal or preclusion.

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Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citations	SRO Rule
Failure to Timely File Answer/USA	Defenses Stricken Attorney Fee Sanctions	95-01575; 96-02877; 97-03299; 97-05779*	10314N 10321N

* **EXAMPLE (NASD ID #97-05779):** *Billinger v. Crown Finl.* -- The Panel granted Claimant's motion to exclude and bar Respondents from presenting any matter, argument or defense. Three of the Respondents had made a motion to have the answer of a Respondent, who timely filed, deemed their Answer, but that motion was denied.

Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citations	SRO Rule
Failure to Produce Ordered Docs.	MTD Granted (Cs) Forum Fees Assessed Aggregated Money Sanctions Attorney Fee Sanctions Sanction Part of Lump Sum Adverse Inference Dismissal W/O Prejudice Dismissal W/ Prejudice Pay Fine to NASDR Forum Defenses Stricken	1996-005563; 1997-006866; 94-03852; 95-03759*; 96-00704; 96-00933; 96-02581; 96-05310; 97-01177; 97-04049; 97-04293; 97-04990; 98-01087	619Y 621Y 10305N 10332N

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* **EXAMPLE (NASD ID #95-03759):** *Christman v. Oppenheimer & Co.* -- Claimant refused to produce tax returns and brokerage account statements and, after defying an order of the Panel, his Statement of Claim was dismissed with prejudice.

Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citations	SRO Rule
Failure to Exchange Document & Witness Lists (20-day exchange)	Witnesses Excluded Documents Excluded Damage Calculation Excluded Expert Witness Excluded Disciplinary Referral	95-04949; 95-06003; 97-00705; 97-04719*	10321N 10322N

* **EXAMPLE (NASD ID #97-04719):** *Abbak v. Brooklyn Capital* -- Respondents' motion to preclude two "surprise" witnesses proffered by Claimants who were not reasonably expected to testify was granted.

Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citation	SRO Rule
Last-Minute Postponements	Attorney Fee Sanctions Related Costs & Expenses Dismissal W/ Prejudice	95-01751; 96-05516; 97-01042*	10319N

* **EXAMPLE (NASD ID #97-01042):** *Serio v. International Assets Advisory Corp.* -- Statement of claim dismissed after Claimants failed to pay Respondents' attorney fees of $3,400 as ordered by Panel as condition of prior continuance.

Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citations	SRO Rule
Overreaching and Inaccurate Claims	Attorney Fee Sanctions "Bully Pulpit" -- Censure Aggregated Money Sanction	1996-005734; 92-00768; 94-04296; 96-01761; 96-04440; 97-00108*; 97-01238; 97-03423; 97-04656;	621Y 10324N

* **EXAMPLE (NASD ID #97-00108):** *Olde Discount v. Dimercurio* -- Panel orders sanction of $3,500 in attorney fees paid to Respondents for Olde's pursuit of damages from a buy-in of securities that were caused by Claimant's delay in taking action on the customers' report of the error.

Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citations	SRO Rule
Breach of Arbitration Agreement	Attorney Fee Sanctions Punitive Damages	94-02597*; 95-04364; 95-05798; 97-04056	10101N 10106N

* **EXAMPLE (NASD ID #94-02597):** *Wejman v. Smith Barney Shearson* -- Panel dismisses all claims, some on six-year eligibility grounds, but charges Respondents $12,800 for having caused unnecessary legal expense by seeking injunctive relief in the courts on eligibility grounds.

Nature of Offense	Types of Arbitral Responses	NASD NYSE Award Citations	SRO Rule
Dilatory Tactics & Abusive Behavior	Forum Fee Assessments "Bully Pulpit" -- Censure Aggregated Money Sanctions Dismissal W/ Prejudice Disciplinary Referral Attorney Fee Sanctions	93-00297; 94-04299; 95-04273; 95-05555; ; 96-04716*; 96-04875; 96-02867; 97-05422; 97-05853	10332N

* **EXAMPLE (NASD ID #96-04716):** *Patel v. CS First Boston* -- Dismissal with prejudice awarded CSFB, due to Claimant's failure to pay a money sanction, his repeated failure to comply with prior Panel orders, and failure to prosecute the case. Award confirmation covered in 10 SAC 11&12(19).

JUDICIAL RESPONSES TO ARBITRATOR-IMPOSED SANCTIONS

How have the Courts dealt with sanctions awarded in arbitrations? Although the thrust of this presentation is an analysis of awards where sanctions have been imposed, it is important that arbitrators, if they are to exercise the sanction authority with confidence, have the backing of the courts. A brief look at court decisions dealing with the issue is, therefore, pertinent. With few decisions in this area, I will include decisions that deal with arbitration outside of securities arbitration as well as within.

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•Lawrence M. David v. R. Patrick Abergel, 43 Cal. Rptr. 2d 443 (Cal. App. 2Dist 1996).

A dispute between two doctors resulted in an arbitration award that included an award of $75,000 to respondent under Code of Civil Procedure Section 128.5 in attorney fees for David's (Claimant in arbitration) frivolous action. The arbitrator wrote a 22-page decision. Among other things, the arbitrator found that David and his witnesses took so many "inconsistent positions" in discovery and at trial, that it appeared they all suffered from "chronological dyslexia."

Two issues were before the appellate court. Both were resolved in defendant/appellant's favor.

1. The sanction award against a doctor for bringing frivolous action was within the scope of the arbitrator's authority where the parties confer on arbitrators the power to grant any remedy or relief to which a party is entitled under state law. Where a state statute permits sanction awards by trial courts and in judicial arbitrations, sanctions awards in nonjudicial arbitrations are not precluded.

2. Arbitrator's sanction award was not untimely under the terms of arbitration agreement requiring the award to be made within 30 days after submission of the matter, when award on the merits was timely made and the arbitrator expressly reserved jurisdiction to decide issues regarding costs and fees.

•Luster v. Collins, 19 Cal. Rptr 2d 215 (1993).

Here, the parties agreed to binding arbitration as authorized by the Code of Civil Procedure. They did not include language conferring specific authority on the arbitrator vis-a-vis the remedies he might fashion. In Luster, the arbitrator imposed a monetary penalty designed to accrue on a daily basis until one of the parties complied with the arbitrator's instructions in the Award. The court did not consider this a sanction qua sanction (which it presumably would have permitted), but an economic measure being used to enforce an award. Under California's statutory scheme, according to Luster, there is nothing which authorizes an arbitrator to include economic sanctions as part of the award.

Despite its ruling in this matter, the Court hastens to add: "Our review of the statutory framework reveals the legislature was keenly aware the arbitrator should have sufficient power to deal with problems pertaining to discovery. Section 1283.05, subdivision (b), expressly provides that the arbitrator can enforce discovery orders 'by the imposition of the same terms, conditions, consequences, liabilities, sanctions, and penalties as can be or may be imposed in like circumstances in a civil action by a superior court.'"

•First Preservation Capital, Inc. v. Smith Barney Harris Upham & Co., Inc., 939 F. Supp. 1559 (S.D. Fla. 1996).

Reviewing a decision by the arbitrators in a member-to-member raiding dispute to dismiss the case with prejudice, mid-hearing, for discovery violations, the Court delivers a scathing rebuke to the violator and supports the ultimate sanction of dismissal as within the arbitrators' powers and appropriate under the circumstances.

The dismissal was percipitated by a letter sent by Claimant's principal to former clients of Respondents, with a demand for affidavits. However, those demands took place after discovery had ended and the hearing had commenced. More importantly, the demand letter "contained erroneous statements of law that were interpreted to mean that the processes of the court may be used against [the recipients] for [their] failure to perform a voluntary act, specifically [their] failure to make an affidavit which was enclosed with and referenced in the letter."

Upon hearing of the letter, Smith Barney obtained an injunction against Claimants' principal, and moved for the ultimate sanction—dismissal of the matter "in its entirety." The decision offers much in guidance concerning arbitral sanction powers. The core of the Court's decision lies in this paragraph: "[T]he great discretion arbitrators have over the proceedings must include the ability to halt proceedings such as this one where plaintiff's abhorrent behavior was so clearly disruptive to the proceedings. If arbitrators are not permitted to impose the ultimate sanction of dismissal on plaintiffs who flagrantly disregard rules and procedures put in place to control discovery, arbitrators will not be able to assert the power necessary to properly adjudicate claims.... Parties in arbitration must understand that willful violations of the discovery process can have severe consequences. They must also be aware that arbitrators have the power to enforce their directives."

At the time of this decision, procedures covering this point were not plentiful in the NASD Code. Section 16 of the Code provided for dismissals without prejudice, but the Court declined to infer that this prohibits Panels from issuing dismissals with prejudice. Since then, the NASD Code has been revised and amended. Section 10305(b) specifically empowers arbitrators to dismiss with prejudice claims, defenses or proceedings.

• Goldman Sachs & Co. v. Patel; Credit Suisse First Boston Corp. v. Patel, Index Nos. 121261/98 & 120490/98 (N.Y. Sup. Ct. NY Cty, 1999).

Of more recent vintage, these two cases, consolidated for purposes of disposition only, related to the same underlying NASD arbitration Award. In that proceeding, the Arbitrators determined to dismiss Goldman Sachs on motion and, later, dismissed CSFB with prejudice as a sanction against Respondent Patel for not complying with prior Panel orders, for failing to pay a sanction of $2,000, and for not prosecuting his case. After a full discussion of the events that led to these determinations and consideration of Mr. Patel's challenges to the award, the Court rejects claims that the Panel members exceeded their powers, engaged in misconduct, or were biased.

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Citing Rules 10305 and 10324, as the Panel did in the Award, the Court rules that "[t]hese provisions give the arbitrators express authority to control the proceeding before them and to issue a dismissal for failure to comply with their orders." Opining further, the court states that counsel's actions "warranted the monetary sanction imposed on Respondent, who is responsible for the actions of his counsel" and the additional acts of non-compliance with the order to pay and others "provided a basis for dismissal..."

CONCLUSION

Arbitrators, when asked, will assess sanctions. The examples provided are but a sampling of the many circumstances in which arbitrators will wield their wide array of weapons to maintain fairness, decorum and order through the arbitration process.

The SROs have incorporated into their respective rules provisions that empower arbitrators to do what is necessary to run their cases efficiently and effectively. Further, the courts have thrown their hats into the ring, showing their willingness to back arbitrators in their effort to conduct fair, balanced, and smoothly-run proceedings.

The courts have displayed a keen understanding of the necessity for Panels to have the authority to govern the parties that appear before them and enforce their arbitral orders. Even when that authority includes imposing the ultimate sanction—dismissing a case with prejudice because the behavior of counsel is simply intolerable—the courts have backed up the arbitrators.

When counsel for either side faces an opponent who is rude, loud, and discourteous to the participants during the hearing, or so arrogant and flippant as to appear to believe that the rules do not apply to him/her; or who plays only by the rules of stonewalling, obstructing discovery and take-no-prisoners combativeness – Remember, the arbitrators are probably just as frustrated and sick of the shenanigans as you are. So don't be shy. Ask, when it is warranted and, odds are, you shall receive.

Postnote: For additional court decisions and Awards regarding sanctions, as well as cases dealing with discovery and evidentiary rulings, see SAC's Sanctions, Discovery & Evidentiary Award Package (see coupon on p. 13).