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New York
Stock Exchange, Inc.

August 14, 1987

The Honorable Edward J. Markey
U. S. House of Representatives
Committee on Energy and Commerce
Subcommittee of Telecommunications and Finance
House Office Building
Washington, DC 20515

Dear Congressman Markey:

In your letter of July 29, 1987 you request information about arbitrations conducted under the auspices of the New York Stock Exchange. Nine specific categories were mentioned in your letter and we shall respond as closely as possible to your categories.

(1) BACKGROUND:

Arbitration is a non-judicial means of resolving disputes and it has a long tradition at the New York Stock Exchange. As early as 1817 the Exchange had an informal method of resolving trading controversies between its members and in 1872 public customers were allowed to use the service. Subsequent changes permitted hearings in major cities other than New York and the use of public arbitrators. Currently, the Exchange staff travels to approximately 33 cities to conduct arbitration hearings.

The Exchange has no rule which requires customers to arbitrate. Customers are always free to arbitrate at the Exchange if they so choose. Some customers, however, are compelled to arbitrate at the Exchange by courts or statutory procedures pursuant to signed agreements between themselves and their brokers. The Exchange does not enforce such agreements nor require customers to sign such agreements.

In 1977 the Exchange became a founding member of the Securities Industry Conference on Arbitration (SICA), which drafted the Uniform Arbitration Code presently in use by all securities industry self regulatory organizations. SICA continues to monitor the arbitration process for the securities industry. The Securities Industry Conference on Arbitration consists of representatives of ten self-regulatory organizations, four public representatives and a representative of the Securities Industry Association. A copy of the fifth and latest report of the conference is enclosed for your information. (Enclosure A)

This report contains the Uniform Arbitration Code (NYSE Rules 600-630), the text of both the small claims and standard procedural pamphlets which explain the process to prospective claimants, and statistical information concerning arbitration at the Exchange and the other self regulatory organizations. A separate schedule contains the statistical information for 1986. (Enclosure B)

(2) CHANGES BEING CONSIDERED

At the present time, rules are being considered to improve discovery, to increase public participation in the arbitration process, to clarify the distinction between public and industry arbitrators, to develop explanatory materials for arbitrators and to ensure that arbitrators are aware of their ability to award punitive damages and attorney's fees. The proposed changes to the discovery provisions of the uniform code will be considered in September. More public participation in the arbitration process and the creation of an arbitration advisory committee at each SRO is to be presented at the September meeting of SICA.

(3) EXISTING SUPERVISORY AND OVERSIGHT PROCEDURES

Rule changes developed by SICA are reviewed and adopted as rules by the Boards of the Exchange and the other SRO's and then submitted to the Securities and Exchange Commission for approval, pursuant to SEC Rule 19(b) (4). Prior to approval the SEC publishes them in the Federal Register and encourages public comment. Only after this comment period are the rules approved and put into effect. In addition to this oversight of the rules, the Securities and Exchange Commission periodically conducts inspections of the arbitration process and makes comments and suggestions to the Exchange. The Exchange has been very responsive to these comments and suggestions.

(4) ARBITRATOR SELECTION

You have asked for information on the arbitration selection criteria at the Exchange. All Exchange arbitrators qualify as neutral arbitrators as defined by statute and the courts. The Exchange further classifies these neutral arbitrators as either public or industry arbitrators. Most cases are heard by three arbitrators, two public and one industry. All arbitrators are

screened before appointment to a particular case to ensure they have no real or apparent conflict of interest. Industry arbitrators are persons employed by or retired from securities industry organizations. Public arbitrators, under current guidelines, must have no securities industry affiliation and may not have had any such affiliation in the past three years. Recently, commentators have suggested that the three year period be extended, and that persons who have spent a substantial portion of their careers in the industry should not be classified as public arbitrators regardless of how many years they are out of the industry. Commentators have also stated that arbitrators with professional ties to the securities industry, such as attorneys and CPA's who regularly represent brokerage houses, should not be classified as public arbitrators. The Exchange has responded administratively to these commentators by reclassifying some arbitrators who fit these categories. The Exchange has always disclosed the current business affiliation of arbitrators and is now also disclosing any past industry affiliation or business connection of other arbitrators. As mentioned previously the Securities Industry Conference on Arbitration is also studying the question of arbitrator classification.

It should be noted, however, that the present procedures do have many safeguards to ensure the impartiality and neutrality of arbitrators. As noted arbitrators are screened for conflicts before appointment to a case. Parties are notified of the names and business affiliations of the arbitrators and are permitted to request additional information on any arbitrator. They are also permitted one peremptory challenge and unlimited challenges for cause. New procedures are being implemented that will provide the parties with more detailed biographical information on each arbitrator. All arbitrators take an oath that they will render a fair and just decision and that they have no direct or indirect interest in the matter. The Exchange realizes that the most important aspect of our arbitration program is the integrity and impartiality of our arbitrators. We are taking every step we can to ensure that we are fair and impartial.

(5) NUMERICAL SUMMARY

Attached are our annual arbitration reports for 1982-1986. (Enclosure C) The only information we have readily available by allegation concerns churning and suitability cases decided in

1985 and 1986. A schedule of those cases showing the number of those claims, the prevailing party and the dollar amount awarded versus the amount claimed is also attached. (Enclosure D) During the past five years customers have received awards in 799 out of 1606 cases decided by arbitrators. Approximately 800 additional cases involving customers were settled prior to arbitrators making a decision. The overall statistical information is contained in Enclosures A and B.

(6) RULES OF PROCEDURES

As noted, the Exchange uses the uniform arbitration code as developed by SICA and approved by the Securities and Exchange Commission. A copy of the Exchange's Rules is enclosed. (Enclosure E)

(7) DISCOVERY

In the area of discovery, our rules require the exchange of documents 10 days prior to the hearing. In addition, SICA is considering a more detailed discovery rule at its September meeting.

Prior to these provisions, discovery was voluntary and in accordance with state law. In addition, documents and witnesses can be subpoenaed, but in most states, subpoenas are returnable only at the time of the hearing. One provision unique to arbitration under the Uniform Arbitration Code is the authority of the arbitrator to direct the appearance of individuals employed in the industry or the production of records under the control of a firm without the necessity of a subpoena.

(8) CLASS ACTIONS

The only experience the Exchange has had with class actions concerned a case which was originally brought in Federal Court. An attempt was made to certify it as a class action. In referring the case to arbitration, the judge said he would retain jurisdiction and decide what to do about the class action request after the arbitrator decided the matter. The case was settled by the parties prior to the arbitrator making a decision.

(9) AVERAGE TIME

In 1985 the average case took 8.5 months from time of filing until resolution. In 1986 the average was 9.1 months. The Exchange now offers first hearings in about 4 months after the case is filed. This time is longer in distant cities. The Exchange now has 733 cases pending and last year concluded 1,004 cases. At this rate on average, the Exchange could close every case pending at this date in 1987 in 8.7 months.

In conclusion the Exchange feels its arbitration program is a service to both the public customer and the Exchange community. We have a substantial commitment to arbitration, and stand ready to continue that. We are always ready to make changes to make that service more responsive to the needs of investors. If you require any additional information regarding arbitration at the Exchange, or have any suggestions for us, please call me.

Very truly yours,