Harbor Consultants, Ltd. v Keilly
2006 NY Slip Op 30780(U)
March 8, 2006
Supreme Court, New York County
Docket Number: 110153/05
Judge: Marilyn Shafer

[* 1]

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 36

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HARBOR CONSULTANTS, LTD. f/k/a
SANDS BROTHERS & CO. LTD.,

Petitioner,

-against-

Index No.: 110153/05

RONALD J. KEILLY as administrator of the
ESTATE of RONALD J. KEILLY,

Respondent.

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SHAFER, J.:

By notice of petition and petition, sworn to July 19, 2005, petitioner Harbor Consultants, Ltd. f/k/a Sands Brothers & Co., Ltd seeks an order, pursuant to CPLR 7511, vacating an arbitration award (the Award) of $380,000, dated April 28, 2005, in favor of Ronald J. Keilly (Keilly), on the grounds that the Award was in manifest disregard of the law and irrational, because the claim was time-barred, and because of "public policy considerations" (Petition, ¶ 2). The Award was rendered by a panel of arbitrators (the Arbitration Panel or Arbitrators) of the National Association of Securities Dealers Dispute Resolution (NASD-DR) in the matter entitled *Keilly v Sands Brothers & Co., Ltd* (NASD-DR No.: 03-03553 [the Arbitration]). Respondent cross-moves to confirm the Award.

Petitioner is a Delaware corporation, with its principal place of business in New York, and a member organization of the National Association of Securities Dealers (NASD).

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Respondent is the estate of petitioner's former brokerage client, Keilly.[1] Petitioner states that it was required to arbitrate disputes pursuant to an account opening agreement (the Agreement).

According to petitioner, Keilly filed a claim against it and its two chairmen, Steven Brett Sands and Martin Scott Sands (collectively, Sands), with NASD-DR, on or about May 13, 2003. Keilly's allegations concerned Sands' handling of his financial investments. The Arbitration Panel held hearings, over the course of eight months, commencing August 19, 2004, after which it rendered the $380,000 award in compensatory damages to Keilly, and dismissed the claims against Steven Brett Sands and Martin Scott Sands. The $380,000 award to Keilly is the only part of the Award at issue here. The Arbitrators essentially provided little in terms of written reasoning for the Award. Relevant here, the Award states:

> "After considering the pleadings, and the testimony and evidence presented at the hearing, the Panel has decided in full and final resolution of the issues submitted for determination as follows:
>
> 1. Respondent Sands Brothers is liable for and shall pay to Claimant compensatory damages in the amount of $380,000.00. . ."

(Petition, Exh. C, at 2).

The parties do not dispute that Keilly's claim with NASD-DR was filed and served in May 2003. In his statement of claim, Keilly alleged that he was an inexperienced investor who placed $500,000 that he received as a result of his retirement as an engineer with "Pfizer" into an account with Sands Brothers & Co, Ltd. (Sands Brothers). Keilly further alleged that, in March 1998, his account had a net value of $421,247, while by the end of 1998, the balance was $76,580.00. According to the statement of claim, the account turnover ratio for 1998 was

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[1]During the course of this proceeding, Ronald J. Keilly died and his estate was substituted as respondent.

approximately 22 times average net equity, and while the account's net worth in July 1998 was $417,313, the purchases for that month were $2,490,287. Keilly stated that in "the industry," any trading of six times net equity or more is prima facie evidence of excessive trading or churning. Keilly claimed that the excessive trading continued during 1999 and 2000, and that by the end of 1999 "his net worth was down to $68,261.00" (Petition, Exh. A, ¶ 2). At the closing of the account, in 2001, Keilly alleged that, as a result of Sands Brothers' excessive trading and unsuitable investment, his out-of-pocket loss was $375,318, and that a well-managed account with suitable investments would have yielded at least an additional $200,000 gain above that loss. Keilly also claimed that Steven and Martin Sands were liable for his injury, as controlling persons, for failure to effectively supervise his account.

Sands denied Keilly's allegations. In their statement of answer (Petition, Exh. B, [the NASD-DR Answer]), Sands responded that the reduction in the value of Keilly's account was due to sharp market declines and that Sands Brothers' "financial advisors recommended stocks, in accordance with [Keilly's] financial objectives, that actually enabled him to avoid even greater losses than those suffered by most other market investors eager to achieve speculative growth in their portfolios" (Petition, Exh. B, at 2). Among the affirmative defenses in the NASD-DR Answer, Sands asserted that Keilly's claims were "barred by the applicable statute of limitations and by the doctrines of equitable estoppel, laches and unclean hands" (*id.* at 4).

Petitioner moves to vacate the Award on the ground that the Arbitration Panel's determination is in manifest disregard of the law and irrational. Petitioner contends that the testimony of Keilly and his expert, and the claim itself, demonstrate that Keilly's claims were time-barred, as Keilly incurred the investment loses by October 1998, over 4½ years before the

claim was filed.

Although neither party has submitted the Agreement, they both appear to agree that the arbitration is governed by the Federal Arbitration Act (the FAA). The FAA "embodies a strong 'liberal policy favoring arbitration agreements,' and provides for extremely limited judicial review of an arbitration award" (*Matter of Uram v Garfinkel*, 16 AD3d 347, 348 [1st Dept] *lv denied* 5 NY3d 717 [2005], quoting *Moses H. Cone Mem. Hosp. v Mercury Constr. Corp.*, 460 US 1, 24 [1983]).

In *Wien & Malkin LLP v Helmsley-Spear, Inc.* (2006 WL 396107), the Court of Appeals states that use of the manifest disregard doctrine is limited to those exceedingly rare instances where some "egregious impropriety" on the part of the arbitrators is apparent, but where none of the provisions of the FAA apply (*id.*; *Duferco Intl. Steel Trading v T. Klaveness Shipping A/S*, 333 F3d 383, 389 [2d Cir 2003]). In order to vacate an award for manifest disregard of the law, a reviewing court must find "both that (1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether and (2) the law ignored by the arbitrators was well defined, explicit and clearly applicable to the case" (*Wien & Malkin LLP*, 2006 WL 396107, quoting *Wallace v Buttar*, 378 F3d 182, 189-190 [2d Cir 2004]). "The showing required to avoid summary confirmation of an arbitration award is high . . . and a party moving to vacate the award has the burden of proof" (*Willemijn Houdstermaatschappij, BV v Standard Microsystems Corp.*, 103 F3d 9, 12 [2d Cir 1997] [citation omitted]; *Matter of Roffler v Spear, Leeds & Kellogg*, 13 AD3d 308, 309 [1st Dept 2004]; *Westerbeke Corp. v Daihatsu Motor Co., Ltd.*, 304 F3d 200 [2d Cir 2002]).

Vacatur for manifest disregard of the law requires proof that the arbitrators were fully

aware of the existence of a clearly defined governing legal principle, but refused to apply it, in effect, ignoring it (*Duferco Intl. Steel Trading*, 333 F3d at 389). Thus, the doctrine "'gives extreme deference to arbitrators'"(*Wien & Malkin LLP*, 2006 WL 396107, quoting *DiRussa v Dean Witter Reynolds, Inc.*, 121 F3d 818, 821 [2d Cir 1997], *cert denied* 522 US 1049, *reh denied* 522 US 1154 [1998]) and requires "more than a simple error in law or a failure by the arbitrators to understand or apply it; and, it is more than an erroneous interpretation of the law" (*id.*, quoting *Duferco Intl. Steel Trading, A/S*, 333 F3d at 389). In fact, a court "cannot vacate an arbitral award merely because it is convinced that the arbitration panel made the wrong call on the law" (*Wallace*, 378 F3d at 190).

Where arbitrators decline to provide an explanation or the reasoning for their determination, the court, nevertheless, must confirm the award "if a ground for the arbitrators' decision can be inferred from the facts of the case[,] . . . even if the ground for their decision is based on an error of fact or an error of law" (*Willemijn Houdstermaatschappij, BV*, 103 F3d at 13; *Roffler*, 13 AD3d at 310). In reviewing an arbitration award, a court "cannot presume that the arbitrator is capable of understanding and applying legal principles with the sophistication of a highly skilled attorney" (*Wallace*, 378 F3d at 190).

Petitioner argues that Keilly did not assert a federal securities law claim, use the word "fraud" within his claim or plead fraud with the heightened pleading particularity required by state and federal law. Petitioner also argues that the Arbitration Panel manifestly disregarded the law by not applying the limitations period of section 10 of the Securities Exchange Act of 1934, which had run, to Keilly's claims.

Petitioner further argues that New York Law governs the arbitration,[2] that there are no New York cases which recognize Keilly's claims, and no basis in New York law for the relief requested by Keilly, because his claims were barred by federal securities statutes. Petitioner asserts that the Arbitration Panel "manifestly disregarded the fundamental legal principal [*sic*] that in order to issue an award to a party, the party must have a viable and justiciable claim that is not barred by the statute of limitations" (Petitioner's Memo. of Law, at 4).

In support of its position, petitioner submits copies of the statement of claim, the NASD-DR Answer, and the Award. To support the proposition that NASD-DR arbitrators must abide by applicable statute of limitations, in its memorandum of law, petitioner provides the text of what it states is NASD Code, Rule 10304, from an unspecified time period, and an excerpt from the "August 2004 Arbitrators Manual."

Respondent has submitted the affidavit of Leslie Trager, respondent's attorney in this action, and counsel for Keilly at the Arbitration. Trager swears that at the Arbitration, Keilly pointed out that he brought his claim under state law for breach of contract and fraud, which have six-year statutes of limitations, and cited cases holding that the statute of limitations was

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[2]Claims arising from securities transactions on national exchanges have been viewed as involving interstate commerce (*Smith Barney, Harris Upham & Co., Inc. v Luckie*, 85 NY2d 193 (1995), *rearg denied* 85 NY2d 1033, *cert denied sub nom. Manhard v Merril Lynch, Pierce, Fenner & Smith, Inc.*, 5165 US 811 [1995], and thus subject to the FAA. Moreover, here, both parties argue under the FAA. At one point in its brief, however, petitioner cites to *SCM Corp. v Fisher Park Lane Co.*, 40 NY2d 788 [1976], in which the Court of Appeals affirmed an order staying arbitration where the statute of limitations had run. In the event that a choice of law clause in the Agreement provides that New York law governs enforcement of the Agreement (*see generally 212 Investment Corp. v Kaplan*, NYLJ, Feb. 22, 2005, at 17, col 1, Cahn, J.), the result here would be the same because the scope of judicial review of the Arbitration Panel's determination of the statute of limitations issue in such an instance, where petitioner did not move for a stay of the proceeding, is "virtually nonexistent" (Alexander, Practice Commentaries, McKinney's Cons Law of NY, Book 7B, CPLR C7502:5).

inapplicable to NASD-DR proceedings. Trager swears that Keilly argued that the courts have upheld unsuitability and churning claims under breach of contract and other theories. Respondent has submitted portions of the brief Keilly submitted to the Panel, in which Keilly made numerous arguments to support his position that his claim was not time-barred.[3]

Petitioner has not met its burden to prove manifest disregard because it simply has not provided evidence that the Arbitrators knew of a well-defined, explicit legal principle clearly applicable to the case, yet refused to apply it or ignored it altogether. It appears that petitioner argues that the Arbitration Panel could not have determined that Keilly's allegations constituted a claim to which a six-year statute of limitations applied. "An Arbitrator 'under the test of manifest disregard [, however,] is ordinarily assumed to be a blank slate unless educated in the law by the parties'" (*Wallace*, 378 F3d at 190, quoting *Goldman v Architectural Iron Co.*, 306 F3d 1214, 1216 [2d Cir 2002]). Other than the copy of its NASD-DR Answer, in which it baldly states a "statute of limitations" defense, petitioner has provided no evidence of what it submitted to the Arbitration Panel to demonstrate to it that Keilly's claim was untimely. The record is devoid of the brief petitioner submitted to the Arbitrators, although apparently one was

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[3]Keilly argued that: (1) claims for unsuitability and churning have been recognized in the courts under common-law theories; (2) he brought no federal claim and thus the federal statute of limitations was not applicable; (3) Sands failed to demonstrate an applicable statute of limitations; (4) the Second Circuit has recognized that in arbitration it is the contract which governs when a case may be brought because statutes of limitations apply only to civil actions, not arbitrations, and NASD rules provide for a six-year statute of limitations period; (5) that the applicable New York statute of limitations for fraud and contract are six years and that, in a court, a plaintiff would allege that NASD suitability rules were part of the contract between the parties and that Sands Brothers breached the contract by making unsuitable recommendations; and (6) that the Martin Act was not applicable to Keilly's claims. The court expresses no opinion as to the merit of these arguments, but provides them to illustrate what was presented to the Arbitrators by Keilly.

submitted, a transcript of the proceeding, or any other evidence demonstrating that petitioner "educated" the Arbitration Panel about the applicable statute of limitations.[4] Petitioner has thus provided no record from which this court can determine that petitioner "brought to the arbitrator's attention in a way that assure[d] that the [Arbitrators] knew its controlling nature" an applicable statute of limitations, or arguments and case law demonstrating that Keilly's claims were time-barred (*Goldman v Architectural Iron Co.*, 306 F3d at 1216 ["Manifest disregard can be established only where . . . the arbitrator ignored (a governing legal principle) after it was brought to the arbitrator's attention in a way that assures that the arbitrator knew its controlling nature" *ibid.* (internal quotation marks omitted)]).

In addition, a court "may look upon the evidentiary record of an arbitration only for the purpose of discerning whether a colorable basis exists for the panel's award" (*Wallace*, 378 F3d at 193). Although petitioner argues that the testimony of Keilly and his expert, and the claim itself, demonstrate that Keilly's claims were barred by the statute of limitations, and the Award states that the decision was rendered "[a]fter considering the pleadings, and the testimony and evidence presented at the hearing" (Petition, Exh. C, at 2), petitioner has not submitted a record of this testimony and/or evidence for review here.

Furthermore, it is also not apparent that any error on the part of the Arbitrators was "obvious and capable of being readily and instantly perceived by the average person qualified to serve as an arbitrator" (*Roffler*, 13 AD3d at 313; *see Elite Inc. v Texaco Panama Inc.*, 777 F Supp 289 [SD NY 1991]). At most, the limited record provided by respondent reveals that the

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[4]Although petitioner represented it would provide a copy of the transcript (Petition, ¶ 20), it has not done so.

parties disputed whether the case was time-barred, and that Keilly argued that, for various reasons, his claims were not. Instead of providing the record of what it argued to the Arbitration Panel, petitioner seeks to re-argue the merits of its defense here. That a court may not have decided the legal issues the same way, however, is clearly not the standard for review under the manifest disregard doctrine.[5]

Further, the excerpt from the NASD Code and the August 2004 Arbitrators Manual that petitioner submits here demonstrate no more than that NASD strives to make arbitrators aware that a case may be time-barred by an applicable statute of limitations. Petitioner does not demonstrate that it brought either the Code provision or the manual excerpt to the Arbitration Panel's attention.

Petitioner also argues that the Award is irrational. "[U]nless there is no proof whatsoever to justify the award so as to render it entirely irrational . . . the arbitrator's finding is not subject to judicial oversight" (*Matter of Peckerman v D & D Assoc.*, 165 AD2d 289, 296 [1st Dept 1991]). Petitioner has not demonstrated that there was no proof whatsoever to justify the Award.

On another note, petitioner argues that the Arbitration Panel failed to demonstrate fundamental fairness, and thus violated petitioner's right to due process under the United States Constitution, because it did not provide the reasoning underlying its determination of the award. Petitioner argues that this absence of written reasoning "makes a mockery of the concept of judicial review" (Petition, ¶ 3). Petitioner augments this argument in its memorandum of law,

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[5]The court also notes that case law to support certain common-law fraud and other common-law causes of action in a securities case may be found (*see generally Nanopierce Tech. Inc. v Southridge Capital Mgt, LLC*, 2003 WL 22052894 [SDNY 2003] [reviewing cases which have permitted the assertion of common law claims in securities cases]).

contending that the Award is violative of strong public policy requiring that it have "a basis."

New York law allows vacatur on public policy grounds only when public policy "prohibit(s), in an absolute sense, particular matters being decided or certain relief being granted by an arbitrator" (*Matter of Sprinzen* [*Nomberg*], 46 NY2d 623, 631 [1979]). Unless the public policy violation is clear on the face of the award, without the need for fact finding and legal analysis, an award will not be vacated on public policy grounds (*id.*). Petitioner has not pointed out a matter that the Panel was prohibited from deciding, or relief it was prohibited from giving, on public policy grounds.

Furthermore, it has long been established that arbitrators are not required to discuss how they reach their decision (*see United Steelworkers of Am. v Enterprise Wheel & Car Corp.*, 363 US 593 [1960]; *Wallace*, 378 F3d at 184). Petitioner agreed to submit to the arbitral process, and will not now be heard to argue that the process to which it agreed was a denial of due process.

Finally, without supporting documentation, petitioner argues that respondent has already, and improperly, moved to confirm the Award in a separate action. Indeed, in *Keilly v Sands Brothers & Co. Ltd*, (Sup Ct, NY County, August 30, 2005, Index No. 106562), Justice Cahn dismissed, for improper service, Keilly's petition to confirm. The dismissal was without prejudice to re-file within 20 days of service of notice of entry. Petitioner, however, has not demonstrated that notice of entry was served. Moreover, "upon the denial of a motion to vacate or modify [an arbitration award, the court] shall confirm the award" (CPLR 7511 [e]).[6]

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[6]Similarly, under Section 9 of the FAA, district courts must confirm an arbitration award unless a statutory basis for modification or vacatur exists (*see Ottley v Schwartzberg*, 819 F2d 373, 375 [2d Cir 1987]).

Accordingly, it is

ORDERED that the petition to vacate the damages portion of the Award rendered in favor of Ronald J. Keilly is denied; and it is further

ORDERED that the cross motion of respondent to confirm the award rendered in favor of Ronald J. Keilly is granted and the Award is confirmed; and it is further

ORDERED AND ADJUDGED that respondent Ronald J. Keilly, as administrator of the Estate of Ronald J. Keilly, having an address at 345 Centre Street, Nutley, ~~here~~ NJ. 07110, have judgment and recover against petitioner Harbor Consultants, Ltd. f/k/a Sands Brothers & Co. Ltd. 90 Park Ave, New York, N.Y. 10016 in the amount of $380,000, plus interest at the rate of 9% per annum from the date of May 29, 2005, as computed by the Clerk in the amount of $27,922.19, together with costs and disbursements in the amount of $245.00, as taxed by the Clerk, for the total amount of $408,167.19, and that respondent have execution therefor.

Dated: 3/8/06

FILED
MAR 23 2006
COUNTY CLERK'S OFFICE
NEW YORK

Enter:

J.S.C.

HON. MARILYN SHAFER, JSC

Norman Goodman
CLERK