

**Matter of Johnson v Summit Equities, Inc.**

2007 NY Slip Op 33727(U)

November 15, 2007

Supreme Court, New York County

Docket Number: 0104034/2007

Judge: Marcy L. Kahn

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SUPREME COURT OF THE STATE OF NEW YORK - NEW YORK COUNTY

PRESENT: Hon. Marcy L. Kahn PART 50K  
*Justice*

In the Matter of the Arbitration Between  
ELIZABETH JOHNSON, individually and as  
Trustee for the Casaburi Family Trust and  
and as POA for Betty Casaburi,

Respondent,

-and-

Summit Equities, INC. and  
PETER O' NEILL,

Petitioners;

NASD, INC. and Relief Defendant.

INDEX NO. 104034/07

MOTION DATE \_\_\_\_\_

MOTION SEQ. NO. 3

MOTION CAL. NO. \_\_\_\_\_

**FILED**  
NOV 19 2007  
COUNTY CLERK'S OFFICE  
NEW YORK

The following papers, numbered 1 to \_\_\_\_\_ were read on this motion to/for \_\_\_\_\_

	<u>Papers Numbered</u>
Notice of Motion/ <del>Order to Show Cause</del> - Affidavits - Exhibits _____	<u>1, 2</u>
Answering Affidavits - Exhibits _____	<u>3</u>
Replying Affidavits <u>and memoranda of law</u> _____	<u>4, 5, 6</u>

Cross-Motion:  Yes  No

Upon the foregoing papers, it is ordered that this motion is

**MOTION IS DECIDED IN ACCORDANCE  
WITH ACCOMPANYING MEMORANDUM  
DECISION (WRITTEN) EXPLAINING COURT'S  
AUGUST 21, 2007 ORAL RULING.**

Dated: NOV 15 2007

ENTER: *[Signature]*

**HON. MARCY KAHN** J.S.C.

Check One:  FINAL DISPOSITION  NON-FINAL DISPOSITION

SUPREME COURT OF THE STATE OF NEW YORK  
NEW YORK COUNTY: CIVIL TERM: IAS PART 50K

-----x  
 In the Matter of the Arbitration Between :  
 ELIZABETH JOHNSON, individually and as :  
 Trustee for the Casaburi Family Trust : DECISION AND ORDER  
 and as POA for Betty Casaburi, : PURSUANT TO  
 : CPLR §§ 1012, 1013  
 Respondent, :  
 -and- : Motion Seq. No. 3  
 SUMMIT EQUITIES, INC. and : Index No.  
 PETER O'NEILL, : 104034/07  
 Petitioners;

**FILED**  
 NOV 19 2007

NASD, INC. as Relief Defendant

COUNTY CLERK'S OFFICE  
 NEW YORK

MARCY L. KAHN, J.:

By notice of petition and petition dated March 21, 2007, Petitioners/Defendants Summit Equities, Inc. ("Summit") and Peter O'Neill ("O'Neill") (collectively, "petitioners") commenced this proceeding pursuant to section 7510 of the Civil Practice Law and Rules ("CPLR") and Rule 2130 ("Rule 2130") of the National Association of Securities Dealers, Inc. ("NASD")<sup>1</sup> to confirm an arbitration award in NASD Dispute Resolution Case Number 04-04272 ("the arbitration") rendered pursuant to a stipulation of settlement between respondent Elizabeth Johnson ("respondent") and the petitioners on May 22, 2006 by a panel of arbitrators appointed by the NASD. The award, inter alia,

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<sup>1</sup> On July 30, 2007, while this motion was pending, the NASD was merged with the member regulation, enforcement and arbitration operations of the New York Stock Exchange to become the Financial Industry Regulatory Authority ("FINRA"). For purposes of consistence and clarity, in this opinion the court will continue to reference the organization as "NASD."

recommended that all reference to the subject matter of the arbitration be expunged from the records on petitioner O'Neill maintained by the NASD in its Central Registration Depository ("CRD").

By notice of motion and affirmation filed March 26, 2007, the Attorney General of the State of New York (the "Attorney General") seeks leave of court to intervene in this proceeding as an intervenor-respondent for the purpose of opposing confirmation of so much of the arbitration award as recommends expungement of records from the CRD. Petitioners have opposed the Attorney General's motion, arguing that there are no grounds either for its intervention or for vacatur of the award. The Attorney General contends that his office has an interest in the CRD records, that the arbitrators exceeded their authority in granting expungement relief and that the arbitration process and findings were insufficient to support the expungement recommendation. Respondent Johnson has not appeared in this proceeding, and the NASD has not opposed the Attorney General's intervention application.<sup>2</sup>

This court heard oral argument on the intervention issue and on the motion to confirm in this case and another case

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<sup>2</sup> The court has permitted the the North American Securities Administrators Association, Inc. ("NASAA") to appear in the confirmation proceeding as amicus curiae. NASAA has not taken any position on the Attorney General's motion seeking intervention.

[\*4]

raising the same issue on August 21, 2007.<sup>3</sup> At that time, this court granted the motion to intervene in each case in an oral ruling, but reserved decision on the motions to confirm. This written decision further explains the court's oral ruling granting intervention in this case.

I. BACKGROUND

The CRD system is an electronic database used by NASD, the Securities and Exchange Commission ("SEC"), state securities regulators and others which contains information relating to registration and licensing decisions made by those bodies. (NASD Notice to Members 99-54 [July 1999], attached as Exh. F to the Affirm. of James J. Park, Esq., sworn May 2, 2007 ["Park Affirm."]). The information contained in the system includes criminal histories, disciplinary information, customer complaints, certain arbitration awards, and other information which is submitted by registered broker/dealers and regulatory authorities, and is accessible both to regulators for their official use and to the investing public. (Id.). The effectiveness of the centralized national CRD system depends on its containing complete and accurate information. State regulators such as the Attorney General rely on the CRD in lieu of maintaining their own separate licensing and regulatory

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<sup>3</sup> The matter was joined for argument on the same issues in UBS Financial Services, Inc. and Karen A. Kurrasch v. Michael D. Gibson and NASD Dispute Resolution, Index No. 103188/07 (NY Co.).

record systems.<sup>4</sup>

Effective in 2004, the SEC approved amendments to NASD Rule 2130, which provides for the expungement from the CRD of certain customer dispute information. Since that time, expungement is limited to cases in which NASD arbitrators make an affirmative finding that certain specified circumstances exist (NASD Rule 2130[b][1]), where they recommend expungement in their arbitral award, and where a court of competent jurisdiction confirms the award. (NASD Rule 2130[a]).

In this case, on June 3, 2004, respondent Johnson filed a statement of claim against petitioners Summit and O'Neill alleging claims of negligence, recklessness, deceptive practice and breach of the duties of good faith and supervision under state law. In October 2005, the petitioners and respondent Johnson agreed to a stipulated award in lieu of a hearing, which was approved by the members of the panel in May 2006. The award provided for the payment of an unspecified, confidential sum and for the withdrawal of all claims against the petitioners, and contained a recommendation that all reference to this matter be expunged from the petitioners' records in the CRD. (Stipulated Award, NASD Dispute Resolution Arbitration No. 04-04272 [the "award"], attached as Exh. 1 to the Verified Petition of Summit and O'Neill ["petition"]).<sup>5</sup> The stipulated award provided:

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<sup>4</sup> The records are maintained exclusively by electronic means.

<sup>5</sup> The award contained the "understanding that pursuant to NASD Notices to Members 04-16," respondents had to "obtain con-

The arbitration panel has made the following affirmative findings of fact:

The registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation, or conversion of funds.

(Award, §§ 3 & 4).

On May 6, 2006, a telephonic hearing was held in which the counsel for respondent, counsel for petitioners and panel members participated. (Supplemental Affirmation of William A. Despo, Esq., sworn August 21, 2007, ["Despo Suppl. Affirm."], Exh. A, Telephonic Expungement Hearing for the Case of Elizabeth Johnson, et al. v. Summit Equities). Following this hearing, the panel noted that O'Neill's affidavit contained all available evidence and that counsel for Elizabeth Johnson did not oppose the expungement request. The panel revised the portion of the stipulated award granting expungement by basing it "solely upon 2130(b)(1)B" and quoting the relevant language in that subsection verbatim.<sup>6</sup>

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firmation from a court of competent jurisdiction before the CRD will execute the expungement directive." (Award, §§ 3 & 4).

<sup>6</sup> That portion of Rule 2130 states in relevant part:

- (b) Members or associated persons . . . seeking judicial confirmation of an arbitration award containing expungement relief must name NASD as an additional party . . . unless this requirement is waived . . .
- (1) Upon request, NASD may waive the obligation to name NASD as a party if NASD determines that the expungement relief is based on affirmative judicial or arbitral findings that:
  - (A) the claim, the allegation or information is factually impossible or clearly erroneous;
  - (B) the registered person was not involved in the alleged investment-related sales practice violation, forgery,

[\* 7]

On March 26, 2007, petitioners commenced the instant proceeding seeking confirmation of the award by this court. Respondent Johnson has not appeared. The Attorney General's motion to intervene followed on May 2, 2007, and was deemed fully submitted for purposes of the instant motion upon oral argument on August 21, 2007.

## II. PARTIES' CONTENTIONS

The Attorney General argues that leave to intervene as of right pursuant to CPLR §1012 should be granted because the data in the records of the CRD belong jointly to the applicant, NASD and state securities regulators, and because these records are necessary to performance of his statutory duties as New York State's regulator of securities brokers, dealers and their salespersons. He maintains that these duties would be compromised if information concerning registered brokers and dealers were expunged from the depository. He avers that NASD contemplates the intervention of state regulators in judicial confirmation proceedings when a registrant seeks a court order confirming an expungement award.

Petitioners respond that the Attorney General has presented no grounds for vacating the award that fall within the scope of CPLR Article 75, that the SEC has rejected the assertion that the records of the CRD are owned by the State of New York, and that the Attorney General has no right to intervene, since the

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theft, misappropriation, or conversion of funds; or  
(C) the claim, allegation, or information is false.

parties to the proceeding, including NASD, have determined that expungement is appropriate.

The Attorney General replies that its interests are real, are recognized by NASD, and would be compromised if information in the CRD pertaining to dealers licensed in New York were expunged improperly. He maintains that his interest in preserving an accurate and reliable database for his regulatory and licensure purposes, and the investing public's right to complete and accurate information about brokers they may wish to engage, have not been adequately represented in these proceedings.

With respect to the argument for permissive intervention under CPLR §1013, the Attorney General states that his claim raises common issues of law and fact with those that the court will be deciding in the underlying proceeding. Petitioners counter that the State's claim and the relief sought in this confirmation proceeding lack the commonality required for the granting of intervention under CPLR §1013. They also argue that the court should deny discretionary intervention because the Attorney General cannot prevail on the merits, as Rule 2130 preempts any contrary state regulation, where, as here, the arbitrator makes an affirmative finding as provided by Rule 2130 and the NASD determines that expungement is appropriate.

### III. DISCUSSION

#### A. Intervention as of Right

Section 1012 of the CPLR provides in pertinent part:

Intervention as of right. Upon timely motion,

any person shall be permitted to intervene in any action:

. . . .

2. When the representation of the person's interest by the parties is or may be inadequate and the person is or may be bound by the judgment . . . .

(CPLR § 1012[a]).<sup>7</sup>

The CRD was established, and its records are maintained, for the benefit of all securities regulators, which include the NASD, a nationwide self-regulatory organization; the federal government, acting through the SEC; and the regulatory agencies of each individual state. (See § 3.10(a) of the CRD Agreement between the NASD and NASAA dated January 6 and 8, 1993, as amended November 18, 1997, attached as Exhibit G to the Park Affirm., at ¶44). State regulators rely on the data in the CRD to present a complete and accurate record of each broker/dealer firm which can be used in conjunction with, inter alia, license renewals or revocations, requests for public inspection and to ascertain the existence of patterns of misconduct warranting regulatory intercession. If information regarding complaints against registered brokers and dealers is expunged from this depository and no longer available to the New York Attorney General, the ability of that office to perform its licensing and regulatory duties and to keep the public informed may be compromised.

Notwithstanding the vigorous protestations to the contrary

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<sup>7</sup> Leave of court is required prior to intervention in any special proceeding. (CPLR §401).

by petitioners, the agreement establishing the CRD demonstrates that the NASD recognizes that a participating CRD State has a joint property interest in the information contained in the CRD.

The CRD agreement between NASD and NASAA provides as follows:

The data on the CRD Uniform Forms filed with the CRD shall be deemed to have been filed with each CRD State in which the applicant seeks to be licensed and with the NASD and shall be the joint property of NASD and these CRD States (and, in the case of Forms BD and BDW, the SEC). The compilation constituting the CRD database as a whole shall be the property of the NASD.

(CRD Agreement, § 3.10[a]). The information in the CRD, therefore, is joint property of the State of New York and the NASD, while the CRD database itself remains the exclusive property of the NASD.

Contrary to petitioners' contention on this motion, the interest of the state regulators in the CRD data maintained by the NASD is not diminished by a comment in the SEC's statement approving Rule 2130. (SEC Order Granting Approval of Proposed Rule Change, Dec. 16, 2003, 68 Fed.Reg. 74667, 74672 [Dec. 24, 2003] ["SEC approval statement"]). In this comment, the SEC rejected the notion that because the CRD system contains data having public record status, its records comprise a privileged class of public record documents necessarily exempt from expungement. While the SEC allowed for expungement of data under certain circumstances, it still acknowledged the "state 'public record' status" of this data. (*Id.*). In other words, while the disposition of documents and data in the CRD is not

exclusively determined by the needs of state regulatory authorities such as the Attorney General's Investor Protector Division, and expungement may occur without the consent of state regulators, both NASD and the SEC expressly recognize that such agencies have a legitimate interest in the CRD data and in its disposition. This is the dispositive issue for the instant motion, not whether the Attorney General has an exclusive ownership interest in the data, or whether he will necessarily prevail on the question of confirmation. The Attorney General clearly has an interest which may be affected by the court's judgment, and which not been adequately represented by any other party, since respondent Elizabeth Johnson agreed to accept expungement in the parties' stipulation of settlement, has not appeared in this confirmation proceeding, and has not opposed expungement in this case. Moreover, granting or disallowing intervention causes no prejudice to respondent Johnson.

The remaining party, the NASD, which has a dual role as a regulator and as an association constituted of the dealers whom it regulates, has not opposed expungement in this case. In fact, it is in just this situation, where NASD declines to oppose expungement, that the SEC and NASD contemplated intervention by state regulators in court confirmation proceedings. In supporting adoption of the amendments now constituting NASD Rule 2130, the NASD noted that:

states will be able to intervene if they have concerns regarding whether investor protection or regulatory issues have been fairly considered by the NASD.

(SEC approval statement, 68 Fed.Reg. at 74671 [footnote omitted]). The NASD explains that state participation in the court confirmation proceeding:

is an additional safeguard to ensure that courts are aware of the standards of Rule 2130 and relevant regulatory and investor protection interests. . . . The Rule gives NASD and the States the opportunity to participate . . . and make courts fully aware of . . . concerns relating to inappropriate expungements.

(Park Affirm., Exh. L, #9, NASD 2130 Frequently Asked Questions, Question #9 [http://www.nasd.org/RegulatorySystems/CRD/FilingGuidance/NASDW\\_005224](http://www.nasd.org/RegulatorySystems/CRD/FilingGuidance/NASDW_005224), now found at <http://www.finra.org/RegulatorySystems/CRD/FilingGuidance/p005224> [last accessed Nov. 1, 2007]). Thus, the drafters of Rule 2130 expressly acknowledged that states have a legitimate interest and should be allowed to intervene in cases of this kind to protect that interest.

Accordingly, since the New York Attorney General has an interest in this proceeding which may not be adequately be represented by the existing parties, the criteria for intervention under CPLR § 1012(a) are met in this case.

B. Intervention by Permission

Section 1013 of the CPLR provides:

[A]ny person may be permitted to intervene in any action . . . when the person's claim or defense and the main action have a common question of law or fact.

The decision to permit intervention under this section rests in the court's sound exercise of discretion, and turns on

whether the proceeding and the intervenor's claims have issues in common. Intervention should be liberally allowed, in order to give the intervening party an opportunity to protect its interest. (Matter of Teleprompter Manhattan CATV Corp. v. State Bd. of Equalization & Assessment, 34 AD2d 1033 [3<sup>rd</sup> Dept. 1970]). Where a prospective intervenor has a real or substantial interest in the outcome of the case, it is an abuse of discretion to deny intervention. (Plantech Housing, Inc. v. Conlan, 74 AD2d 920, 921 [2<sup>nd</sup> Dept. 1980]).

If the threshold requirement of a common question of law or fact is met, the court may then exercise its discretion in deciding whether to permit intervention.

(Alexander, Practice Commentaries, McKinney's Cons. Laws of NY, Book 7B [1997], CPLR C1013, at 183).

In Teichman v. Community Hospital of Western Suffolk, 87 NY2d 514 (1996), the Court of Appeals stated that in exercising their discretion under this section, trial courts should consider whether the intervenor's claim would be adversely affected without intervention, whether there are common issues of law and fact, and the extent of prejudice to the existing parties if intervention is allowed.

Here, the Attorney General's claim would be adversely affected without intervention, as the data upon which his office relies would be eliminated from the national database used by his office to perform its official regulatory and licensing duties. Further, the Attorney General's claim has in common many questions of law in fact with the confirmation relief

sought in this proceeding, such as whether the petitioners are entitled to expungement, the scope of this court's authority to review the arbitral recommendation of expungement, the standard to be employed in such review, and the propriety of expungement of data owned jointly by NASD and the CRD states.

Finally, involvement of the Attorney General in this proceeding will not unduly prejudice the parties. This is not a case where the presence of the intervenor will complicate a lengthy discovery or trial process, as neither discovery nor trial is contemplated in this special proceeding. No substantial rights of any party will be prejudiced: petitioners' award remains in place, and their position will be fully considered on the issue of confirmation, vacation or modification of that award. In sum, the presence of the Attorney General will simply insure that both sides of these novel and complex legal issues are presented in this proceeding. Therefore, the Attorney General should be allowed to intervene on the basis of permissive intervention, as well.

Accordingly, upon the Notice of Petition and Petition of Petitioners Summit and O'Neill filed on March 26, 2007; the Notice of Motion and Affirmation of James J. Park, Esq., filed May 2, 2007, the Memorandum of Law in Support of the Attorney General's Motion to Intervene, filed May 2, 2007; the Affirmation of William A. Despo, Esq. in Opposition, dated June 14, 2007; Petitioners' Memorandum in Opposition, dated June 14, 2007; the Reply Affirmation of R. Verle Johnson, Esq. in

Support, dated July 12, 2007; the Reply Memorandum of Law in Support, dated July 12, 2007; the Supplemental Affirmation of William A. Despo, Esq., sworn August 21, 2007, and the oral argument heard on August 21, 2007; it is hereby

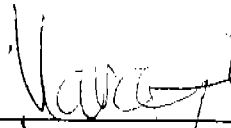
ORDERED, that the motion to intervene is granted and that the Attorney General of the State of New York be permitted to intervene in the above-entitled proceeding as an intervenor-respondent; and it is further

ORDERED, that the notice of petition and petition in the above-entitled proceeding be amended by adding the Attorney General of the State of New York as an intervenor-respondent; and it is further

ORDERED, that the attorney for the intervenor shall serve a copy of this order with notice of entry upon the Clerk of the Court and upon the Clerk of the Trial Support Office (Room 158), who are directed to amend their records to reflect such change in the caption herein.

The foregoing constitutes the decision and order of this court.

ENTER:

  
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Marcy L. Kahn, J.S.  
**FILED**  
NOV 19 2007  
COUNTY CLERK'S OFFICE  
NEW YORK

Dated: New York, New York  
November 15, 2007