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By David Bario

Did Goldman Make Bad Gamble With Arbitration Award?

Arbitration / Commercial

Judge Rakoff Confirms \$20.6 Million Arbitration Award Against Goldman Sachs
Goldman Sachs isn't known for tactical blunders. Did the banking giant miscalculate by challenging a \$20.6 million arbitration award?

That's the question we were left pondering after Manhattan federal district court judge Jed Rakoff confirmed the award, which had been issued by a Financial Industry Regulatory Authority panel in June. (Judge Rakoff's one-page order is [here](#); the judge will issue a more detailed opinion later.) The award was won by the creditors' committee of the Bayou Group, which collapsed in 2005 under the cloud of a \$400 million Ponzi scheme orchestrated by its former CEO, Samuel Israel III. In their arbitration claim, Bayou's creditors argued that Goldman, which cleared trades for Bayou, failed to investigate these trades after it learned of potential fraud. Goldman responded that it had no obligation as a prime or clearing broker to detect or report fraud.

The FINRA panel's decision in June got lots of folks on Wall Street gnashing their teeth. The clearing business moves a lot of money and generates plenty of profits for firms like Goldman, and brokers worried that the Bayou award could force them into a policing role and compel them to raise due diligence standards.

Goldman and its lawyers at Shulte, Roth & Zabel filed a lawsuit to vacate the FINRA award in July, arguing that the FINRA panel exceeded its powers "in manifest disregard of the law." The bank got amicus support from the Securities Industry and Financial Markets Association, which asserted that requiring clearing firms to monitor every trade for potential fraud would cripple securities markets. Sidley Austin's Henry Minerop, who authored SIFMA's brief, declined to comment pending an elaborated opinion from Judge Rakoff.

The Bayou creditors' committee, represented by Rich & Intelisano, argued at a September hearing before Judge Rakoff that the FINRA decision was limited to cases in which clearing firms had been notified of a Ponzi-style fraud.

Goldman will hardly miss \$20 million. The problem is that while the FINRA decision may have rankled clearing firms, it was not precedential. Depending on the reasoning in Judge Rakoff's

more detailed ruling, other clearing firms may wish that Goldman had chosen to write the Bayou creditors a \$20.6 million check.

"We've been fighting for a long period of time, and we look forward to the investors getting some of their money back," Ross Intelisano told us. Goldman's lead lawyer, Shulte Roth's Howard Schiffman, referred us to his client, which declined to comment.

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