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Goldman Battles Bayou Decision

By [LIZ MOYER](#)

NEW YORK—[Goldman Sachs Group](#) Inc. is continuing to fight a \$20.5 million arbitration award that, while relatively small from the big bank's perspective, has broader implications for Wall Street.

The award stems from Goldman's role as a clearing broker for a failed hedge fund. Goldman filed an appeal Thursday in the U.S. Court of Appeals in the Second Circuit, arguing as it did last fall in district court that the Financial Industry Regulatory Authority arbitration panel that awarded the sum ignored the law.

On the opposite side are the creditors of Bayou Group LLC, which accused Goldman Sachs Execution & Clearing LP of ignoring signs of fraud at the hedge fund run by Samuel Israel III before it imploded in 2005.

A Finra panel awarded the Bayou creditors \$20.5 million in June 2010. Goldman sued to vacate the arbitration award in July 2010, but Federal Judge [Jed Rakoff](#) confirmed the award in November.

Ross Intelisano, a lawyer for the Bayou creditors at Rich, Intelisano & Katz, said investors are "frustrated" by the delay in receiving their money. "We're looking forward to the Second Circuit reconfirming the arbitration award," he said.

The disputed case comes as regulators are eager to lay blame after the financial crisis exposed rampant cases of Ponzi schemes and other frauds. The \$20.5 million award, if it is upheld, could raise the standards of care required by banks that clear trades for hedge funds, lawyers said.

The Securities Industry and Financial Markets Association, an industry group representing Wall Street sided with Goldman in district court last year and plans to file a brief in support of Goldman in the appeal, a spokesman said.

In May, Goldman said the Commodity Futures Trading Commission had "orally advised" it that it faced civil fraud charges over its role clearing trades for an unnamed client. Goldman said it was cooperating.

In that probe, the potential charges concern whether Goldman knew or should have known the client was using customer accounts in transactions with Goldman rather than the client's own accounts.

In the Bayou case, the creditors argued that the hedge fund's depositing of money into its account at Goldman, and then its shuffling around of that money among accounts, constituted transfers to Goldman that could be recovered by investors.

The creditors also accused Goldman of ignoring several warning signs, including suspicious money transfers. About \$13.9 million of the award concerns money Bayou moved among its accounts.

Bayou was founded in 1996 and exposed as a \$400 million fraud in 2005. Goldman was a prime broker and clearing firm for Bayou from 1999 to 2005. Mr. Israel, who went on the lam briefly, is currently serving a 22-year prison sentence.



New York City's securities industry could lose nearly 10,000 jobs by the end of 2012, New York state's comptroller predicted, a painful blow to the area's economy and government budgets, Aaron Lucchetti reports on Markets Hub. Banks in the New York area are also poised to shed jobs. Photo: AP.



Mary O'Grady and Mary Kissel on how New York's economy and budget depend on Wall Street.

Dan Carlson, a San Diego lawyer who represents investors in Finra arbitrations, said the financial crisis has "opened eyes that clearing firms and brokerages need to be doing more due diligence."

Wall Street firms have argued that extra due diligence will slow down business and increase costs. "In imposing liability on Goldman, the arbitrators disregarded the long-recognized principle that a clearing firm cannot be liable for merely processing transactions received from an authorized source," Sifma wrote in its friend of the court brief siding with Goldman in district court last fall.

"If clearing firms were required to analyze trading in introduced accounts," Sifma added, "the speed and efficiency demanded in the contemporary securities markets would not be possible."

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