

SECURITIES AND EXCHANGE COMMISSION  
Release No. 34-56540; File No. SR-NASD-2006-109

September 26, 2007

Self-Regulatory Organizations; National Association of Securities Dealers, Inc. (n/k/a Financial Industry Regulatory Authority, Inc.); Order Approving Proposed Rule Change as modified by Amendment Nos. 1 and 2 Thereto Relating to Representation of Parties in Arbitration and Mediation

I. Introduction

On September 14, 2006, the National Association of Securities Dealers, Inc. (“NASD”) (n/k/a Financial Industry Regulatory Authority, Inc. (“FINRA”)), through its wholly owned subsidiary, NASD Dispute Resolution, Inc. (“NASD Dispute Resolution”) (n/k/a, FINRA Dispute Resolution, Inc.), filed with the Securities and Exchange Commission (“SEC” or “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change relating to representation of parties in arbitration and mediation.<sup>3</sup> On November 9, 2006 and February 23, 2007, NASD Dispute Resolution submitted Amendment Nos. 1 and 2, respectively, to the proposed rule change. The proposed rule change, as amended, was published for comment in the Federal Register on April 13, 2007.<sup>4</sup> The Commission

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD’s Certificate of Incorporation to reflect its name change to Financial Industry Regulatory Authority Inc., or FINRA, in connection with the consolidation of the member firm regulatory functions of NASD and NYSE Regulation, Inc. See Exchange Act Release No. 56146 (July 26, 2007); 72 FR 42190 (Aug. 1, 2007).

<sup>4</sup> See Securities Exchange Act Release No. 55604 (April 9, 2007), 72 FR 18703 (April 13, 2007).

received five comments on the proposal.<sup>5</sup> For the reasons discussed below, the Commission is approving the proposed rule change, as amended.

## II. Description of the Proposal

The changes to NASD's Code of Arbitration Procedure for Customer Disputes, Code of Arbitration Procedure for Industry Disputes, and Code of Mediation Procedure provide that in both arbitration and mediation: (1) parties may represent themselves; (2) parties may be represented by an attorney, provided certain criteria are met; (3) parties may be represented by a person who is not an attorney, unless state law prohibits such representation or the person is currently suspended or barred from the securities industry in any capacity or is currently suspended from the practice of law or disbarred; and (4) issues regarding qualifications of a representative are governed by applicable law.

First, the proposed rule change codifies current practice by explicitly stating that parties may represent themselves in arbitration.

Second, the proposed rule change codifies current practice permitting the multi-jurisdictional practice of law by attorneys in the NASD Dispute Resolution forum to the extent permitted by state law. In addition, the proposed rule change states that if a party chooses to be represented by an attorney, the attorney must be licensed to practice in a

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<sup>5</sup> See letters to Nancy Morris, Secretary, Commission, from Timothy Canning, Law Offices of Timothy A. Canning, dated May 4, 2007 ("Canning"); Vincent DiCarlo, Law Offices of Vincent DiCarlo, dated May 4, 2007 ("DiCarlo"); Jill I. Gross, Director of Advocacy, Pace Investor Rights Project, dated May 4, 2007 ("Pace"); Richard L. Sacks, dated May 3, 2007 ("Sacks"); and Irwin G. Stein, dated May 4, 2007 ("Stein").

U.S. jurisdiction and be in good standing in that jurisdiction.<sup>6</sup> NASD stated that requiring an attorney to be licensed and in good standing in a U.S. jurisdiction will protect investors by prohibiting individuals who have been suspended from the practice of law or disbarred from representing parties in the NASD forum. Further, NASD stated that the requirement for an attorney to be licensed to practice in a U.S. jurisdiction sets a standard of practice for its forum that is consistent with the other rules and proceedings of NASD.

Third, the proposed rule change addresses the representation of parties by non-attorneys in the NASD forum. Under the proposed rule change, parties may be represented in an arbitration or mediation by a person who is not an attorney, unless applicable law prohibits such representation or the person is currently suspended or barred from the securities industry in any capacity or is currently suspended from the practice of law or disbarred.

While this provision would be applicable to all arbitration claims, it may be particularly beneficial for certain investors that may have difficulty retaining an attorney on a contingency-fee basis. For example, investors with small claims may be unable to retain an attorney because the attorney may believe that the attorney's share of any award would be too small to justify the effort. In these circumstances, investors may benefit from being able to seek other assistance to resolve their arbitration or mediation claims

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<sup>6</sup> The requirement to be licensed to practice in a U.S. jurisdiction and be in good standing in that jurisdiction is in addition to and not in lieu of the requirement that an attorney must comply with applicable laws of the relevant jurisdiction. While the multi-jurisdictional practice of law may be permitted in many jurisdictions, it may constitute a violation of certain states' unauthorized practice of law provisions.

for a more affordable fee.<sup>7</sup> At the same time, NASD stated that such non-attorney representatives should not be persons who have been found by a regulatory body in essence to be unfit to represent clients or to conduct securities business with the public. Thus, to protect investors, the rule would prohibit non-attorney representatives who are currently suspended or barred from the securities industry, or are currently suspended from the practice of law or disbarred, from representing parties in the NASD Dispute Resolution forum.

Last, the proposed rule change would allow an attorney to represent a client in an NASD arbitration or mediation held in any U.S. hearing location, regardless of the jurisdiction in which the attorney is licensed. An attorney's ability to represent clients in a jurisdiction in which he or she is not licensed, however, would be subject to the applicable law of that jurisdiction. The proposed rule change is not intended to preempt state law; it is intended to reflect current practice in the forum which, based on experience, indicates that the outcome of a dispute resolution proceeding depends more on the level of knowledge, training and skill of the attorneys, rather than the jurisdiction from which the attorneys received their license to practice.

### III. Comment Summary and Response to Comments

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<sup>7</sup> Consistent with current practice, the proposed rule would allow a relative, friend or associate to represent or assist a person (e.g., an elderly or disabled person) with his or her arbitration or mediation. In addition, law school securities arbitration clinics can provide investors with affordable legal representation. A securities arbitration clinic also can help an investor who has a smaller claim but is unable to hire an attorney, provided the investor qualifies for assistance. See How to Find an Attorney (for more information on clinic locations and eligibility requirements), available at: <http://www.finra.org/ArbitrationMediation/StartanArbitrationorMediation/HowtoFindanAttorney/index.htm> >.

The Commission received five comments<sup>8</sup> on the proposal and a response to comments.<sup>9</sup> One commenter generally expressed support for the proposed rule change.<sup>10</sup> The remaining four commenters opposed the proposed rule change and the NASD Response addressed these comments.<sup>11</sup>

Three commenters expressed the view that there should be a uniform national rule governing who can represent a party in a NASD forum, rather than permitting the incorporation of state rules that may vary from jurisdiction to jurisdiction.<sup>12</sup> These commenters suggested that NASD should adopt a uniform rule that would preempt contrary state laws.<sup>13</sup> NASD indicated that it had determined that “there is no overriding need for a uniform rule in this area, and that the continued compliance with state rules is in the best interests of all participants in its arbitration forum.”<sup>14</sup> NASD also noted that this position is consistent with its previous position with respect to arbitrator disclosure, distinguishing attorney qualification rules and rules regulating arbitration procedure.<sup>15</sup>

Four commenters stated that the proposed rule change would penalize retroactively those persons who are currently suspended or barred from the securities

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<sup>8</sup> Canning, DiCarlo, Pace, Sacks, and Stein.

<sup>9</sup> See letter to Nancy Morris, Secretary, Commission, from Mignon McLemore, Assistant Chief Counsel, FINRA Dispute Resolution, dated September 17, 2007 (“NASD Response”). While FINRA had been formed at the time of the submission of the NASD Response, for ease of reference the term NASD is used throughout.

<sup>10</sup> Pace.

<sup>11</sup> Canning, DiCarlo, Sacks, and Stein. See also NASD Response.

<sup>12</sup> Canning, DiCarlo, and Stein.

<sup>13</sup> Id.

<sup>14</sup> NASD Response.

<sup>15</sup> Id.

industry by prohibiting them from representing a party in an arbitration or mediation proceeding.<sup>16</sup> In their view, it would impose a new penalty on those who have had their misconduct adjudicated and sanctions imposed.<sup>17</sup> NASD indicated that the rule is “designed to protect investors” and that at a minimum a non-attorney representative should not be “a person whom a regulatory body has suspended or barred from representing clients or conducting securities business with the public.”<sup>18</sup>

In addition, in response to comments that the proposed rule may unduly limit investor choices,<sup>19</sup> NASD stated that it believes that the limitations on the choice of representation under the proposed rule are appropriate and would protect investors.<sup>20</sup>

#### IV. Discussion and Findings

The Commission believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>21</sup> which requires, among other things, that NASD’s rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The Commission believes that the proposed rule change meets this standard by balancing the needs of investors to have access to representation,

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<sup>16</sup> Canning, DiCarlo, Sacks, and Stein.

<sup>17</sup> Id.

<sup>18</sup> NASD Response. NASD noted that “[t]he proposal will apply prospectively as to representation on or after the effective date. If a barred or suspended individual is representing a party in a case pending on the effective date of the rule, he or she may continue to serve on that case, but may not serve on new ones.”

<sup>19</sup> Canning, DiCarlo, Sacks, and Stein.

<sup>20</sup> Id.

<sup>21</sup> 15 U.S.C. 78o-3(b)(6).

particularly in small cases, with NASD's responsibility to protect investors, the integrity of its forum, and the public interest.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>22</sup> that the proposed rule change (SR-NASD-2006-109), as amended, be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>23</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>22</sup> 15 U.S.C. 78s(b)(2).

<sup>23</sup> 17 CFR 200.30-3(a)(12).