

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-52705; File No. SR-NASD-2004-013)

October 31, 2005

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Granting Approval to Proposed Rule Change and Amendments Nos. 1 and 2 Thereto, and Notice of Filing and Order Granting Accelerated Approval to Amendment No. 3, to Amend NASD Rules for Mediation Proceedings

I. INTRODUCTION

On January 23, 2004, the National Association of Securities Dealers, Inc. (“NASD”), through its wholly-owned subsidiary, NASD Dispute Resolution, Inc., filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to simplify the language of the mediation portion of the NASD Code of Arbitration Procedure (“Code”) and to reorganize those provisions into a separate code for mediations (“Mediation Code”).³ Amendments Nos. 1 and 2 were filed on January 3, 2005 and April 8, 2005, respectively.⁴

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ As explained in more detail below, the proposed Mediation Code is one of three NASD rule proposals that, taken together, would simplify the language of and reorganize the Code. See also Securities Exchange Act Rel. No. 51856 (June 15, 2005); 70 FR 36442 (June 23, 2005) (proposing to revise and create a separate code for NASD arbitration rules pertaining to customer disputes (“Customer Code”)); Securities Exchange Act Rel. No. 51857 (June 15, 2005); 70 FR 36430 (June 23, 2005) (proposing to revise and create a separate code for NASD arbitration rules pertaining to industry disputes (“Industry Code”)).

⁴ Amendment No. 1 deleted a provision that was inadvertently included in the initial rule filing. This provision pertained to a mediator’s disqualification as an expert in any pending or future proceeding related to the subject matter of the mediation, and the unavailability of the mediator’s documents in such a proceeding. Amendment No. 2 made certain conforming changes also proposed in the other rule filings relating to the revision and reorganization of the Code. Specifically, it added references in the definitions rule to NASD’s By-laws and clarified

Notice of filing of the proposed rule change and Amendments Nos. 1 and 2 were published for comment on June 23, 2005.⁵ The Commission received one comment letter on the proposal.⁶ NASD has filed Amendment No. 3 to change the numbering of the proposed Mediation Code and to make other non-substantive revisions, in order to facilitate approval of the proposed rule change⁷ prior to the approval of the two other rule filings relating to the revision and reorganization of the Code. This order approves the proposed rule change and Amendments Nos. 1 and 2 thereto, and issues notice of and grants accelerated approval to Amendment No. 3.

II. DESCRIPTION OF THE PROPOSED RULE CHANGE

A. Description of the Proposed Rule Change

This rule filing is part of a comprehensive plan to simplify and reorganize NASD's dispute resolution rules. NASD has proposed to rewrite the Code using plain English, in accordance with the Commission's plain English guidelines. In addition, it has proposed to reorganize the Code in a more logical, user-friendly way by, among other things, creating two separate codes for customer and industry arbitrations, and one for mediations. Once approved, the three new codes will replace the current NASD Code in its entirety.

the definition of "quorum" for purposes of meetings of the National Arbitration and Mediation Committee, consistent with the Plan of Allocation and Delegation of Functions by NASD to Subsidiaries.

⁵ See Securities Exchange Act Rel. No. 51855 (June 15, 2005); 70 FR 36440 (June 23, 2005).

⁶ See letter to Jonathan G. Katz, Secretary, Commission, from Pace Investor Rights Project, by Jill I. Gross and Barbara Black, dated July 14, 2005 ("Pace Letter").

⁷ NASD has requested accelerated approval for Amendment No. 3. Telephone Conversation with Mignon McLemore, Assistant Chief Counsel, NASD Dispute Resolution, Inc. (Oct. 19, 2005).

Although NASD is proposing to implement several substantive rule changes to its arbitration rules, as described in the Customer Code and Industry Code rule filings,⁸ NASD believes it has not proposed any substantive changes to the current rules governing mediations, apart from adding a definitions rule. The text of the proposed Mediation Code, including the technical changes proposed in Amendment No. 3, is available on the NASD Web site at http://www.nasd.com/web/idcplg?IdcService=SS_GET_PAGE&ssDocName=NASDW_009003&ssSourceNodeId=801.

1. Reorganization

NASD believes that maintaining three separate codes will make it easier for parties to find the rules that apply to their disputes. NASD will maintain electronic versions of each code on its Web site, www.nasd.com, and will make paper copies available upon request.

In keeping with the current NASD rule numbering system, each of the three codes will be numbered in the thousands, and major sections will be numbered in the hundreds. Individual rules within those sections will be numbered in the tens (or ones, if necessary). The current method for numbering and lettering paragraphs within individual rules will remain unchanged. The Customer Code will use the Rule 12000 series, the Industry Code will use the Rule 13000 series, and the Mediation Code ultimately will use the Rule 14000 series, all of which are currently unused. NASD intends to reserve the Rule 10000 series, which is currently used for NASD's dispute resolution rules, for future use.

2. Proposed Definitions Rule

The Mediation Code will include a comprehensive definitions rule that will define terms used throughout the Mediation Code. NASD believes that this rule will provide useful

⁸ See supra note 3.

clarification for parties and mediators.

3. No Substantive Changes

NASD believes that, with the exception of adding a definitions rule, the Mediation Code will not include any substantive changes to NASD's current rules governing mediations.

B. Amendment No. 3

Originally, NASD anticipated that the proposed Mediation Code would be approved at the same time as the Customer Code and Industry Code. Therefore, NASD proposed numbering the Mediation Code using the 14000 series. However, in order to facilitate approving the proposed Mediation Code before the Customer Code and Industry Code, NASD proposes in Amendment No. 3 to change its numbering and to make other non-substantive changes, such that it is consistent with the current Code. NASD intends to propose to renumber the approved Mediation Code as the 14000 series when the Customer Code and Industry Code are approved and become effective.

Specifically, the changes proposed in Amendment No. 3 are as follows:

- The current NASD mediation rules, current Rules 10401 – 10407 of the Code, would be deleted in their entirety. They would be replaced by Rules 14100 – 14109 of the proposed Mediation Code, which would be renumbered as Rules 10401–10410, to remain consistent with the numbering in the current Code. NASD intends to propose to renumber the Mediation Code in the NASD Manual as the 14000 Series when the Customer Code and Industry Code are approved by the Commission.⁹

⁹ The Commission notes that approval of the proposed Mediation Code does not predispose the Commission to approving the proposed rule changes relating to the Customer Code or Industry Code.

- Proposed Rule 10401(g) of the Mediation Code defines “NASD Customer Code.” This paragraph would be reserved until the Customer Code is approved. NASD intends to propose to reinsert the definition into the Mediation Code at that time.
- Proposed Rule 10401(h) of the Mediation Code defines “NASD Industry Code.” This paragraph would be reserved until the Industry Code is approved. NASD intends to propose to reinsert the definition into the Mediation Code at that time.
- In proposed Rule 10405(b), the phrase “NASD Code of Arbitration Procedure” would replace “NASD Customer Code” or “NASD Industry Code.” NASD intends to propose to reinsert those terms when the Customer Code and Industry Code are approved.
- In proposed Rule 10406(b), the term “adjournment” would replace the term “postponement,” consistent with the current Code. NASD intends to propose to change the term back to “postponement” when the Customer Code and Industry Code are approved.
- In proposed Rule 10407(c), references to “Rule 10312(a), (b), and (c) of the NASD Code of Arbitration Procedure” would replace references to “NASD Customer Code Rule 12408” or “NASD Industry Code Rule 13408.” NASD intends to propose to change the reference back to “NASD Customer Code Rule 12408” or “NASD Industry Code Rule 13408,” as appropriate, when the Customer and Industry Codes are approved. These cross references pertain to disclosures mediators are required to make in connection with interests, relationships, or circumstances which might influence their objectivity and impartiality.

C. Comment Summary

The Commission received one comment letter on the proposed Mediation Code, in which the Pace Investor Rights Project endorsed the proposed rule change because it preserves the existing NASD mediation system, while allowing individual investors to better understand the mediation rules through plain English.¹⁰ Pace generally supports the mediation of securities disputes and cites Professor Jill Gross for her conclusion in a forthcoming article that mediation is fair to the individual investor because it maximizes party control over the process and offers procedural justice at relatively low cost, among other things.¹¹

III. DISCUSSION AND FINDINGS

After careful consideration, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association¹² and, in particular, the requirements of Section 15A of the Act¹³ and the rules and regulations thereunder. The Commission finds that the proposed rule change, as amended, is consistent with Section 15A(b)(6) of the Act,¹⁴ which requires, among other things, that the rules of an association 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.¹⁵ The Commission believes that proposed rule change, as amended, accomplishes these goals by improving the readability,

¹⁰ Pace Letter.

¹¹ Id.

¹² In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

¹³ 15 U.S.C. 78o-3.

¹⁴ 15 U.S.C. 78o-3(b)(6).

¹⁵ Id.

accessibility, and therefore usability of procedures that establish an alternative, voluntary, and potentially low-cost forum for dispute resolution in the securities industry.

The Commission believes that there is good cause for approving Amendment No. 3 prior to the 30th day after publication in the Federal Register. The proposed rule change and Amendments Nos. 1 and 2 thereto previously have been published for comment and have been available on NASD's Web site since their filing with the Commission. Amendment No. 3 proposes non-substantive, technical changes to the proposed rule change, consistent with the current Code, in order to facilitate approval of the proposed Mediation Code. Accelerated approval of Amendment No. 3 will allow parties to more quickly utilize the reorganized and revised Mediation Code. Based on the above, the Commission finds good cause, consistent with Section 15A(b)(6) and Section 19(b)(2) of the Act, for approving Amendment No. 3 prior to the 30th day after the date of publication of notice of filing thereof in the Federal Register.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning Amendment No. 3, including whether it is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-NASD-2004-013 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-NASD-2004-013. The file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Section, 100 F Street, NE, Washington, DC 20549. Copies of such filing will also be available for inspection and copying at the principal office of NASD. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer

to SR-2004-013 and should be submitted on or before [insert date 21 days from the date of publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Jonathan G. Katz
Secretary