

INFORMATIONAL

Employment Arbitration Rules

SEC Approves New Arbitration Disclosure Rule And Procedures For Employment Arbitration; Effective Date: January 18, 2000

SUGGESTED ROUTING

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- Legal & Compliance
- Registered Representatives

KEY TOPICS

- Arbitration
- Discrimination
- Employment

Executive Summary

On October 27, 1999, the Securities and Exchange Commission (SEC) approved amendments to National Association of Securities Dealers, Inc. (NASD[®]) rules that create a new Rule 10210 Series, containing special rules applicable to the arbitration of employment discrimination claims; add a new Rule 3080, which contains a model disclosure statement to be given to persons who are signing the Form U-4 to apply for registration; and make conforming changes to Rules 10201 and 10202.¹ These rule changes, which will become effective on January 18, 2000, will enhance the dispute resolution process for the handling of employment discrimination claims and expand disclosure to employees concerning the arbitration of disputes.

Included with this *Notice* is Attachment A, the text of the amendments that will become effective on January 18, 2000.

Questions/Further Information

Questions regarding this *Notice* may be directed to Linda D. Fienberg, Executive Vice President, Office of Dispute Resolution, NASD Regulation, Inc. (NASD RegulationSM), at (202) 728-8407; George H. Friedman, Senior Vice President and Director, Office of Dispute Resolution, NASD Regulation, at (212) 858-4488; or Jean I. Feeney, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-6959.

Background

Effective on January 1, 1999, the NASD removed from the Code of Arbitration Procedure (Code) the requirement for registered persons to arbitrate claims of statutory

employment discrimination.² In approving that change to Rule 10201, the NASD Board of Governors and the NASD Regulation Board of Directors (the Boards) recommended certain enhancements to the arbitration process for discrimination claims. With the assistance of a working group that included attorneys representing employees, member firm general counsels, and arbitrators with expertise in employment matters to advise on issues relating to the arbitration of employment discrimination claims, NASD Regulation developed a series of rules applicable to the arbitration of statutory employment discrimination claims, and related changes to other NASD rules. These rules, as adopted by the Boards and approved by the SEC, deal with the qualifications of arbitrators hearing claims of employment discrimination; the number of arbitrators to hear such claims; special rules for discovery, awards, and attorneys' fees; coordination of claims filed in court and arbitration; and disclosure to associated persons of the effects of the arbitration clause found in the Form U-4. The new rules are described in detail below.

Description Of Amendments**Disclosure Statement**

NASD Regulation has adopted a model disclosure statement to be given to persons who are signing the Form U-4 to apply for registration. This disclosure statement explains the nature and effect of the arbitration clause contained in the Form U-4. It does not address any private arbitration agreement that the applicant might enter into with the member firm. Rather, the member is responsible for either making proper disclosure to its employees about its private arbitration agreement, or risking an adverse decision in later litigation concerning any inadequacy in the disclosure.

New Rule 3080, entitled "Disclosure to Associated Persons When Signing a Form U-4," is modeled on the disclosure given to customers when signing predispute arbitration agreements with member firms, as contained in current Rule 3110(f) and proposed amendments thereto that are awaiting SEC approval.³ Because the rule relates to associated persons, it has been located with other conduct rules that deal with the responsibilities of members relating to associated persons, employees, and other employees. The introductory language of the rule requires members to provide each associated person, whenever the associated person is asked to sign a new or amended Form U-4, with certain specified disclosure language. This means that the disclosure may be given by the same member to the same associated person on more than one occasion during that person's employment, if the associated person has reason to re-sign the Form U-4. The specified disclosure language explains that the Form U-4 contains a predispute arbitration clause, and indicates in which item of the Form U-4 the clause is located.⁴ The disclosure language then advises the associated person to read the predispute arbitration clause.

Subparagraph (1) of new Rule 3080 paraphrases the arbitration clause in the Form U-4 and then provides disclosure that the associated person is giving up the right to sue in court except as provided by the rules of the arbitration forum in which a claim may be filed. Subparagraph (2) incorporates the language of Rule 10201 regarding an exception to the arbitration requirement for claims of statutory employment discrimination. Subparagraph (2) also indicates that the rules of other arbitration forums may be different. Subparagraphs (3) through (7) track the language of proposed

amendments to Rule 3110(f)(1), which sets forth similar disclosures to customers. Those subparagraphs inform the associated person that arbitration awards are generally final and binding, that discovery is generally more limited in arbitration than in court, that arbitrators do not have to explain the reasons for their awards, that the panel of arbitrators may include either public or industry (non-public) arbitrators, and that the rules of some arbitration forums may impose time limits for bringing a claim in arbitration.

New Rule 10210 Series

The new Rule 10210 Series contains special rules applicable to statutory employment discrimination claims. These rules supplement and, in some instances, supersede the provisions of the Code that currently apply to the arbitration of employment disputes. The special rules do not attempt to set forth all procedures applicable to the arbitration of statutory employment discrimination claims, but only those procedures that relate specifically to such claims and may be different from procedures that apply to other intra-industry claims.

Qualifications For Neutrals Who Hear Employment Discrimination Cases

NASD Regulation has on its arbitration roster many arbitrators who have indicated that they have experience or training in employment law, and NASD Regulation currently offers arbitrators training in employment law that is conducted by attorneys experienced in the field of employment law. In addition, NASD Regulation has been preparing a more specialized roster of available arbitrators for intra-industry cases in which statutory discrimination is alleged. As of November 1999, over 200 arbitrators have

been placed on this specialized roster.

New Rule 10211(a) provides that only arbitrators classified as public (non-industry) arbitrators will be selected to consider disputes involving a claim of employment discrimination, including a sexual harassment claim, in violation of a statute. New Rule 10211(a) incorporates by reference the definition of "public arbitrator" in the list selection rule, Rule 10308, which applies both to customer disputes and to intra-industry disputes except where superseded by more specific industry arbitration rules. The definition of "public arbitrator" in Rule 10308 excludes not only securities industry employees and their immediate family members, but also attorneys, accountants, and other professionals who have devoted 20 percent or more of their professional work in the last two years to clients who are engaged in the securities business (as described in Rule 10308). Use of the same definition of public arbitrators throughout the Code provides for more efficient administration of the list selection system.

For chairpersons and single arbitrators, there are additional qualifications in new Rule 10211(b). These qualifications include:

- a law degree;
- membership in the Bar of any jurisdiction;
- substantial familiarity with employment law; and
- ten or more years of legal experience that include at least five years of one of the following:
 - law practice;
 - law school teaching;

- government enforcement of equal employment opportunity (EEO) statutes;
- experience as a judge, arbitrator, or mediator; or
- experience as an EEO officer or in-house counsel of a corporation.

In addition, the chair or single arbitrator may not have represented primarily the views of employees or employers within the past five years. For this purpose, "primarily" is defined to mean 50 percent or more of the arbitrator's business or professional activities within the last five years.

Rule 10211(c) provides that parties may agree, after a dispute arises, to waive any of the special qualifications contained in either paragraph (a) or paragraph (b). Such a waiver is not valid if it is contained in a predispute arbitration agreement.

Composition Of Panels

Until the present rule change, the current arbitration panel composition for statutory discrimination claims and certain other employment claims has been identical to the panel used for customer disputes and consists of either one public (non-industry) arbitrator for single arbitrator cases, or two public arbitrators and one non-public (industry) arbitrator for three arbitrator cases. An all-industry panel is used solely for employment disputes that relate exclusively to claims involving employment contracts, promissory notes, or receipt of commissions.

Under new Rule 10212(a), for cases involving claims of employment discrimination (whether or not other issues are also involved), all arbitrators must be classified as

public. Rule 10212 provides, however, that parties may agree to a different panel composition in a particular case.

New Rule 10212(b) provides a higher maximum dollar limit for single arbitrator cases than is found elsewhere in the Code: a single arbitrator will hear claims of \$100,000 or less. This higher amount reduces the hearing costs for the parties and results in more efficient allocation of qualified employment arbitrators. New Rule 10212(c) provides that claims for more than \$100,000 will be assigned to a three-person panel unless the parties agree to have their case determined by a single arbitrator. A conforming amendment is being made to Rule 10202, the general intra-industry panel composition rule, to include a reference to the above special panel composition rule.

Discovery

New Rule 10213 provides that, in considering the need for depositions, arbitrators should consider the relevancy of the information sought from the persons to be deposed and the issues of time and expense. Existing Rule 10321, which deals with pre-hearing proceedings, is cross-referenced in new Rule 10213(b) to make clear that its provisions also apply to employment discrimination disputes. Paragraphs (d) and (e) of Rule 10321 set forth procedures for deciding unresolved issues either at the pre-hearing conference or by appointment of a selected arbitrator.

Attorneys' Fees

Although the Code is silent with respect to attorneys' fees, such fees may be awarded under current practice.⁵ Normally, parties will brief the arbitrators on applicable law providing for the award of attorneys'

fees in their cases. In view of provisions in the federal civil rights laws that specifically provide for the award of attorneys' fees, NASD Regulation has adopted Rule 10215, which provides that the arbitrator has authority to provide for reasonable attorneys' fee reimbursement, in whole or in part, as part of the remedy in accordance with applicable law. This accords with Title VII of the Civil Rights Act of 1964, which authorizes a court, in its discretion, to allow the prevailing party "a reasonable attorney's fee" as part of the costs.⁶ The intent of new Rule 10215 is to allow the award of attorneys' fees if applicable law permits such an award.

Awards

Rule 10330(e) presently requires certain information to be contained in an award. Under current NASD Regulation practice, parties also may request the arbitrators to provide reasons for their decision, and the arbitrators have discretion to grant or deny the request.⁷ New Rule 10214 has been added to supplement Rule 10330(e) for claims of employment discrimination. Rule 10214 provides that arbitrators will be empowered to award any relief that would be available in court under the law, and sets forth the information that must be contained in the arbitrator's award. Such information includes a summary of the issues, including the types of disputes, the damages or other relief requested and awarded, a statement of any other issues resolved, and a statement regarding the disposition of any statutory claims.

Bifurcation

NASD Regulation has added Rule 10216 to address concerns over the possible splitting or "bifurcation" of employment cases, in which the discrimination claims would proceed in court, while other employment claims that are subject to

mandatory arbitration would proceed in arbitration. Such bifurcation of statutory and common law claims could result in the separation of claims that are often joined together and based on the same alleged facts, which would create a financial burden on employees and members, delay the resolution of claims, and cause scheduling and discovery disputes.

Therefore, NASD Regulation has adopted a new rule on coordination of claims that may be filed in court and those that are normally required to be arbitrated under NASD rules. Currently, if the parties agree to resolve all related claims in court, then the matter need not be submitted to arbitration. New Rule 10216 includes a pre-filing procedure in which the claimant may certify to the Director of Arbitration that he or she communicated with the potential respondent about the possibility of filing all claims in court initially, in order to save the expense of arbitration fees and attorney fees to draft arbitration claim papers. If the potential respondent does not agree to consolidate all claims in court, and an arbitration claim is then filed, Rule 10216 provides several methods for coordinating claims filed in court and in arbitration. Similarly, if a discrimination claim is filed in court and related claims subject to mandatory arbitration are filed in arbitration, a respondent in the arbitration proceeding

has the option to move to combine all claims in court. The rule provides several other opportunities for a party to move to compel that a claim be consolidated with other claims in court. Any claims not accepted by the court under any of these methods, however, would continue to be arbitrable.

In conjunction with the new bifurcation rule, a change has been made to Rule 10201 to add a reference to Rule 10216. This exception is necessary because, under Rule 10216, some claims that might otherwise be required to be arbitrated may be brought in court, at the respondent's option.

Endnotes

¹Exchange Act Rel. No. 42061 (Oct. 27, 1999) (File No. SR-NASD-99-08), 64 Fed. Reg. 59815 (Nov. 3, 1999).

²That rule change did not affect private arbitration agreements that might exist between employees and member firms.

³File No. SR-NASD-98-74.

⁴The member will be responsible for updating this item number on new disclosure statements if it changes in later versions of the Form U-4.

⁵A guide for arbitrators drafted by the Securities Industry Conference on Arbitration (SICA) provides as follows: "Generally, par-

ties to an arbitration are responsible for their personal costs associated with bringing or defending an arbitration action. Exceptions to the rule do exist. Parties should be prepared to argue the statutory or contractual basis that permits an award of attorneys' fees. The arbitrators should consider referring to the authority relied upon if attorneys' fees are awarded." *The Arbitrator's Manual* (October 1996). SICA is a group composed of representatives of the self-regulatory organizations (SROs) that provide arbitration forums; public investors; and the securities industry.

⁶42 U.S.C. Section 2000e-5(k) (1998).

⁷A booklet prepared by SICA and provided to all claimants explains this industry-wide practice as follows: "Arbitrators are not required to write opinions or provide reasons for the award. A party, however, may request an opinion. This request should be made no later than the hearing date." *Arbitration Procedures* (October 1996) (also available via the Internet under the title, *Arbitration Procedures for Investors*, on the NASD Regulation Arbitration/Mediation page at www.nasdr.com). In a 1989 Order approving arbitration rule changes by several SROs, the SEC decided not to require written opinions in awards but expressed the view that arbitrators could voluntarily prepare written opinions. Exchange Act Rel. No. 26805, Part III. H. (May 10, 1989) (File Nos. SR-NYSE-88-29, SR-NYSE-88-8, SR-NASD-88-29, SR-NASD-88-51, SR-NASD-89-19; and SR-AMEX-88-29), 54 Fed. Reg. 21144, 21151-52 (May 16, 1989).

ATTACHMENT A

Text Of Amendments

(Note: New text is underlined; deletions are in brackets.)

3000. RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS, EMPLOYEES, AND OTHERS' EMPLOYEES

* * *

3080. Disclosure to Associated Persons When Signing Form U-4

A member shall provide an associated person with the following written statement whenever the associated person is asked to sign a new or amended Form U-4.

The Form U-4 contains a predispute arbitration clause. It is in item 5 on page 4 of the Form U-4. You should read that clause now. Before signing the Form U-4, you should understand the following:

(1) You are agreeing to arbitrate any dispute, claim or controversy that may arise between you and your firm, or a customer, or any other person, that is required to be arbitrated under the rules of the self-regulatory organizations with which you are registering. This means you are giving up the right to sue a member, customer, or another associated person in court, including the right to a trial by jury, except as provided by the rules of the arbitration forum in which a claim is filed.

(2) A claim alleging employment discrimination, including a sexual harassment claim, in violation of a statute is not required to be arbitrated under NASD rules. Such a claim may be arbitrated at the NASD only if the parties have agreed to arbitrate it, either

before or after the dispute arose. The rules of other arbitration forums may be different.

(3) Arbitration awards are generally final and binding; a party's ability to have a court reverse or modify an arbitration award is very limited.

(4) The ability of the parties to obtain documents, witness statements and other discovery is generally more limited in arbitration than in court proceedings.

(5) The arbitrators do not have to explain the reason(s) for their award.

(6) The panel of arbitrators may include arbitrators who were or are affiliated with the securities industry, or public arbitrators, as provided by the rules of the arbitration forum in which a claim is filed.

(7) The rules of some arbitration forums may impose time limits for bringing a claim in arbitration. In some cases, a claim that is ineligible for arbitration may be brought in court.

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10000. CODE OF ARBITRATION PROCEDURE

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10200. INDUSTRY AND CLEARING CONTROVERSIES

10201. Required Submission

(a) Except as provided in paragraph (b) or Rule 10216, a dispute, claim, or controversy eligible for submission under the Rule 10100 Series between or among members and/or associated persons, and/or certain others, arising in connection with

the business of such member(s) or in connection with the activities of such associated person(s), or arising out of the employment or termination of employment of such associated person(s) with such member, shall be arbitrated under this Code, at the instance of:

- (1) a member against another member;
- (2) a member against a person associated with a member or a person associated with a member against a member; and
- (3) a person associated with a member against a person associated with a member.

* * *

10202. Composition of Panels

(a) In disputes subject to arbitration that arise out of the employment or termination of employment of an associated person, and that relate exclusively to disputes involving employment contracts, promissory notes or receipt of commissions, the panel of arbitrators shall be appointed as provided by paragraph (b)(1) or (2) or Rule 10203, whichever is applicable. In all other disputes arising out of the employment or termination of employment of an associated person, the panel of arbitrators shall be appointed as provided by Rule 10212, 10302 or [Rule] 10308, whichever is applicable.

* * *

10210. Statutory Employment Discrimination Claims

The Rule 10210 Series shall apply only to disputes that include a claim alleging employment discrimination, including a sexual harassment claim, in violation of a statute. The

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Rule 10210 Series shall supersede any inconsistent Rules contained in this Code.

10211. Special Arbitrator Qualifications for Employment Discrimination Disputes

(a) Minimum Qualifications for All Arbitrators

Only arbitrators classified as public arbitrators as provided in Rule 10308 shall be selected to consider disputes involving a claim of employment discrimination, including a sexual harassment claim, in violation of a statute.

(b) Single Arbitrators or Chairs of Three-Person Panels

(1) Arbitrators who are selected to serve as single arbitrators or as chairs of three-person panels should have the following additional qualifications:

(A) law degree (Juris Doctor or equivalent);

(B) membership in the Bar of any jurisdiction;

(C) substantial familiarity with employment law; and

(D) ten or more years of legal experience, of which at least five years must be in either:

(i) law practice;

(ii) law school teaching;

(iii) government enforcement of equal employment opportunity statutes;

(iv) experience as a judge, arbitrator, or mediator; or

(v) experience as an equal employment opportunity offi-

cer or in-house counsel of a corporation.

(2) In addition, a chair or single arbitrator with the above experience may not have represented primarily the views of employers or of employees within the last five years. For purposes of this Rule, the term "primarily" shall be interpreted to mean 50% or more of the arbitrator's business or professional activities within the last five years.

(c) Waiver of Special Qualifications

If all parties agree, after a dispute arises, they may waive any of the qualifications set forth in paragraph (a) or (b) above.

10212. Composition of Panels

For disputes involving a claim alleging employment discrimination, including a sexual harassment claim, in violation of a statute:

(a) Each panel shall consist of either a single public arbitrator or three public arbitrators qualified under Rule 10211, unless the parties agree to a different panel composition.

(b) A single arbitrator shall be appointed to hear claims for \$100,000 or less.

(c) A panel of three arbitrators shall be appointed to hear claims for more than \$100,000, unless the parties agree to have their case determined by a single arbitrator.

10213. Discovery

(a) Necessary pre-hearing depositions consistent with the expedited nature of arbitration shall be available.

(b) The provisions of Rule 10321 shall apply to proceedings under this Rule 10210 Series.

10214. Awards

The arbitrator(s) shall be empowered to award any relief that would be available in court under the law. The arbitrator(s) shall issue an award setting forth a summary of the issues, including the type(s) of dispute(s), the damages or other relief requested and awarded, a statement of any other issues resolved, and a statement regarding the disposition of any statutory claim(s).

10215. Attorneys' Fees

The arbitrator(s) shall have the authority to provide for reasonable attorneys' fee reimbursement, in whole or in part, as part of the remedy in accordance with applicable law.

10216. Coordination of Claims Filed in Court and in Arbitration

(a) Option to Combine Related Claims in Court

(1) (A) If a current or former associated person of a member files a statutory discrimination claim in court against a member or its associated persons, and asserts related claims in arbitration at the Association against some or all of the same parties, a respondent who is named in both proceedings shall have the option to move to compel the claimant to bring the related arbitration claims in the same court proceeding in which the statutory discrimination claim is pending, to the full extent to which the court will accept jurisdiction over the related claims.

(B) The respondent shall notify the claimant in writing, before the time to answer under Rule 10314 has expired, that it is exercising this option and shall file a copy of such notification with the Director. If the respondent files an answer without having exercised this option, it shall have waived its right to move to compel the claimant to assert related claims in court, except as provided in paragraph (b).

(2) (A) If a member or current or former associated person of a member ("party") has a pending claim in arbitration against a current or former associated person of a member and the current or former associated person thereafter asserts a related statutory employment discrimination claim in court against the party, the party shall have the option to assert its pending arbitration claims and any counterclaims in court.

(B) The party shall notify the current or former associated person in writing, before filing an answer to the complaint in court, that it is exercising this option and shall file a copy of such notification with the Director. If the party files an answer in court without having exercised this option, it shall have waived its right to assert the pending arbitration claim in court.

(C) The party may not exercise this option after the first hearing has begun on the arbitration claim.

(b) Option Extended When Claim is Amended

(1) If the claimant files an amended Statement of Claim adding new claims not asserted in the

original Statement of Claim, a respondent named in the amended Statement of Claim shall have the right to move to compel the claimant to assert all related claims in the same court proceeding in which the statutory discrimination claim is pending, to the full extent that the court will accept jurisdiction over the related claims, even if those related claims were asserted in the original Statement of Claim.

(2) The respondent shall notify the claimant in writing, before the time to answer the amended Statement of Claim under Rule 10314 has expired, that it is exercising this option and shall file a copy of such notification with the Director. If the respondent files an answer to the amended Statement of Claim without having exercised this option, it shall have waived its right to move to compel the claimant to assert related claims in court.

(c) Requirement to Combine All Related Claims

If a party elects to require a current or former associated person to assert all related claims in court, the party shall assert in the same court proceeding all related claims that it has against the associated person to the full extent to which the court will accept jurisdiction over the related claims.

(d) Right of Respondent to Remain in Arbitration

(1) If there are multiple respondents and a respondent has exercised an option under paragraph (a) or (b), but another respondent wishes to have the claims against it remain in arbitration, then any remaining party may apply for a stay of the arbitration proceeding.

(2) The arbitration shall be stayed unless the arbitration panel determines that the stay will result in substantial prejudice to one or more of the parties. If a panel has not been appointed, the Director shall appoint a single arbitrator to consider the application for a stay. Such single arbitrator shall be selected using the Neutral List Selection System (as defined in Rule 10308) and is not required to have the special employment arbitrator qualifications described in Rule 10211.

(e) Pre-Filing Certification

(1) Prior to or concurrently with filing a Statement of Claim, a claimant may file with the Director a certification that it had communicated unsuccessfully with the respondent concerning the consolidation of all claims in court prior to filing a Statement of Claim, in an effort to save the expense of arbitration fees. A copy of such certification shall be sent to the respondent at the same time and in the same manner as the filing with the Director.

(2) If, after a certification has been filed, all the respondents later exercise the option to consolidate all claims in court, the Director will return the claimant's filing fee and any hearing session deposits for hearings that have not been held, but will retain the member surcharge and any accrued member process fees. If there are any remaining respondents, the filing fee and any hearing deposits will be adjusted to correspond to the claims against the remaining respondents.

(f) Motion to Compel Arbitration

If a member or a current or former associated person of a member files in court a claim against a member or a current or former

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associated person of a member that includes matters that are subject to mandatory arbitration, either by the rules of the Association or by private agreement, the defending party may move to compel arbitration of the claims that are subject to mandatory arbitration.

(g) Definitions

For purposes of this Rule:

(1) The term "related claim" shall mean any claim that arises out of the employment or termination of employment of an associated person.

(2) The term "statutory discrimination claim" means a claim alleging employment discrimination, including a sexual harassment claim, in violation of a statute.

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