

Notice to Members

MARCH 2007

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KEY TOPICS

Arbitration
Code of Arbitration Procedure
Dispute Resolution
Subpoenas

GUIDANCE

Code of Arbitration Procedure

SEC Approves Amendments to NASD Code of Arbitration Procedure Concerning Subpoenas and Payment of Arbitrators; **Effective Date: April 2, 2007**

Executive Summary

The Securities and Exchange Commission (SEC) has approved amendments to the subpoena rule as set forth in Rule 10322 of the NASD Code of Arbitration Procedure (Code)¹ to allow only arbitrators to issue subpoenas, whether for discovery in arbitration or for appearance at a hearing before the arbitrators.² The SEC also approved an amendment to the payment of arbitrators rule as set forth in IM-10104 to provide for the payment of a \$200 honorarium per case for each arbitrator who considers contested motions for the issuance of subpoenas.³

The text of Rule 10322 and IM-10104, as approved, are set forth in Attachment A of this *Notice*. The changes to Rule 10322 will become effective on April 2, 2007, and will apply to subpoenas issued on or after that date, regardless of when the case was filed. The changes to IM-10104 will apply to decisions rendered on a contested subpoena request on or after April 2, 2007.

Questions/Further Information

Questions regarding this *Notice* may be directed to Jean I. Feeney, Vice President and Chief Counsel, Dispute Resolution, at (202) 728-6959; or Mignon McLemore, Assistant Chief Counsel, Dispute Resolution, at (202) 728-8151.

Background and Discussion

Under current Rule 10322(a) of the Code of Arbitration Procedure (Code), both arbitrators and counsel of record to the arbitration have the power to issue a subpoena, as provided by law. In the course of preparing their cases, attorneys sometimes issue subpoenas to non-parties requesting the production of documents in advance of an arbitration hearing. Disputes regarding the propriety or scope of these subpoenas to non-parties occasionally arise, raising the question of whether the subpoenaed materials should be produced. Currently, the Code does not contain any rules that specifically address the issuance of subpoenas to non-parties or the resolution of disputes involving such subpoenas. Thus, parties may bring their disputes to the arbitrators or, if arbitrators have not yet been appointed, then they may resort to litigation in court. This process may be expensive and confusing to parties.

Under amended Rule 10322, only arbitrators will be permitted to issue subpoenas for both parties and non-parties, whether for discovery or for appearance at a hearing. Parties will send their requests for issuance of a subpoena to the NASD Director of Arbitration and to all other parties at the same time and in the same manner. The request must be in the form of a written motion and must include a draft subpoena.⁴ The requesting party may not serve the motion or draft subpoena on a non-party.

If another party objects to the scope or propriety of the subpoena, that party must—within 10 calendar days of service of the motion—file written objections with the Director, with an additional copy for the arbitrator, and must serve copies on all other parties at the same time and in the same manner as on the Director. The party that requested the subpoena may respond to the objections within 10 calendar days of receipt of the objections. After considering timely objections, the arbitrator responsible for deciding discovery-related motions will rule promptly on the issuance and scope of the subpoena.⁵ Arbitrators will use their discretion to determine whether or not to issue a subpoena, and whether or not to limit the scope of a subpoena before it is issued.

After the requesting party receives subpoenaed documents from a non-party, the requesting party must notify all other parties within five calendar days of receipt. If another party requests copies of documents that were received in response to a non-party subpoena, the party that requested the documents must provide the copies within ten calendar days. The arbitration panel has authority to determine the amount of costs incurred as a result of subpoenaed documents and by whom such costs should be borne.

NASD believes that providing arbitrators with greater control over the issuance of subpoenas will help to protect investors, associated persons and other parties from abuse in the discovery process. In addition, the establishment of a uniform, nationwide rule will reduce potential confusion for parties and their counsel regarding whether they have the ability to issue subpoenas, minimize gamesmanship in the subpoena process and make the rule easier to administer.

Payment of Arbitrators for Deciding Contested Subpoena Requests

In 2005, NASD amended IM-10104 to provide arbitrators with an honorarium of \$200 to decide discovery-related motions without a hearing session. The revised rule did not discuss whether a contested motion concerning a subpoena constitutes a discovery-related motion. NASD recognizes that arbitrators may spend a significant amount of time and effort deciding contested subpoena motions and believes that arbitrators should be compensated for this work. Therefore, NASD has amended the payment of arbitrators rule to provide a \$200 honorarium for each arbitrator who decides contested motions for subpoenas.

Under most circumstances, the chairperson will be the only arbitrator to consider the subpoena requests based on the documents supplied by the parties. If a party requests that the entire panel decide the contested motion, each arbitrator who participates in the decision on the subpoena will receive an honorarium of \$200. The honorarium will be paid on a per case basis, regardless of the number of contested subpoena motions considered by an arbitrator or panel during the case. Furthermore, the maximum amount that will be paid by the parties for any one case will be \$600, irrespective of any changes to the composition of the panel.⁶ NASD believes that structuring the honorarium in this manner will limit the arbitration costs for parties while at the same time compensating arbitrators for the time that they spend considering contested subpoena requests.

Endnotes

- 1 Rule 10322 will be renumbered as Rule 12512 in the NASD Code of Arbitration Procedure for Customer Disputes (Customer Code) and Rule 13512 in the NASD Code of Arbitration Procedure for Industry Disputes (Industry Code) when those Codes become effective on Apr. 16, 2007. Similarly, IM-10104 will be renumbered as Rules 12214 and 13214. See *Notice to Members 07-07* (Feb. 2007).
- 2 Exchange Act Release No. 55038 (Jan. 3, 2007), 72 FR 1353 (Jan. 11, 2007) (File No. SR-NASD-2005-079).
- 3 Exchange Act Release No. 55108 (Jan. 16, 2007), 72 FR 2914 (Jan. 23, 2007) (File No. SR-NASD-2006-101).
- 4 Motions are not required to be in any particular format. They may take the form of a letter, legal motion or any other format that the panel decides is acceptable. NASD anticipates that the motion accompanying a subpoena will provide the panel with relevant information that would not be obvious from the draft subpoena itself, such as the rationale for the request.
- 5 Normally, the chair will issue subpoenas. In customer cases, the parties are given an opportunity to agree on their chairperson, who is almost always a public arbitrator, and if they cannot agree, then the highest-ranked public arbitrator is appointed as the chairperson. See NASD Rule 10308(c)(5). In intra-industry cases, the chair may be a public or non-public arbitrator, as appropriate to the type of case. Under the amendments to the Code that will be effective on April 16, 2007, parties will select their chair from a list of chair-qualified arbitrators; see the Rule 12400 and 13400 Series.
- 6 If more than three arbitrators decide contested subpoena motions in a particular case because of changes in the panel, NASD will absorb the cost of any honorarium that exceeds \$600.

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ATTACHMENT A

New language is underlined. Deleted language is in brackets.

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NASD Code of Arbitration Procedure¹

IM-10104. Arbitrators' Honorarium

(a) - (e) No change

(f) Payment for Deciding Contested Subpoena Requests Without a Hearing Session

(1) The honorarium for deciding one or more contested motions requesting the issuance of a subpoena without a hearing session shall be \$200. The honorarium shall be paid on a per case basis to each arbitrator who decides the contested motion(s). The parties shall not be assessed more than \$600 in fees under this paragraph in any arbitration proceeding. The honorarium shall not be paid for cases administered under Rules 10203 or 10302.

(2) For purposes of paragraph (f)(1), a contested motion requesting the issuance of a subpoena shall include a motion requesting the issuance of a subpoena, the draft subpoena, a written objection from the party opposing the issuance of the subpoena, and any other documents supporting a party's position.

(3) The panel will allocate the cost of the honorarium under paragraph (f)(1) to the parties pursuant to Rules 10205(c) and 10332(c).

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10322. Subpoenas and Power to Direct Appearances

(a) [Subpoenas

The arbitrators and any counsel of record to the proceeding shall have the power of the subpoena process as provided by law. All parties shall be given a copy of a subpoena upon its issuance. Parties shall produce witnesses and present proofs to the fullest extent possible without resort to the subpoena process.] To the fullest extent possible, parties should produce documents and make witnesses available to each other without the use of subpoenas. Arbitrators shall have the authority to issue subpoenas for the production of documents or the appearance of witnesses.

(b) A party may make a written motion requesting that an arbitrator issue a subpoena to a party or a non-party. The motion must include a draft subpoena and must be filed with the Director, with an additional copy for the arbitrator. The requesting party must serve the motion and draft subpoena on each other party, at the same time and in the same manner as on the Director. The requesting party may not serve the motion or draft subpoena on a non-party.

(c) If a party receiving a motion and draft subpoena objects to the scope or propriety of the subpoena, that party shall, within 10 calendar days of service of the motion, file written objections with the Director, with an additional copy for the arbitrator, and shall serve copies on all other parties at the same time and in the same manner as on the Director. The party that requested the subpoena may respond to the objections within 10 calendar days of receipt of the objections. After considering all objections, the arbitrator responsible for deciding discovery-related motions shall rule promptly on the issuance and scope of the subpoena .

(d) If the arbitrator issues a subpoena, the party that requested the subpoena must serve the subpoena at the same time and in the same manner on all parties and, if applicable, on any non-party receiving the subpoena.

(e) Any party that receives documents in response to a subpoena served on a non-party shall provide notice to all other parties within five days of receipt of the documents. Thereafter, any party may request copies of such documents and, if such a request is made, the documents must be provided within 10 calendar days following receipt of the request.

(f) [Power to Direct Appearances and Production of Documents

An arbitrator] The arbitrator(s) shall be empowered without resort to the subpoena process to direct the appearance of any person employed by or associated with any member of the Association and/or the production of any records in the possession or control of such persons or members. Unless an arbitrator directs otherwise, the party requesting the appearance of a person or the production of documents under this Rule shall bear all reasonable costs of such appearance and/or production.

1 The text of these rules as renumbered by the Customer and Industry Codes can be found on the NASD Web site. While the new Codes generally apply to claims filed on or after April 16, 2007, amended Rules 12214 and 13214 will apply to decisions rendered on a contested subpoena request on or after April 2, 2007; and the changes to Rules 12512 and 13512 are effective on April 2, 2007, for subpoenas issued on or after that date.