

March 8, 2000

Katherine A. England, Esq.
Assistant Director
Division of Market Regulation
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

Re: **File No. SR-NASD-00-11** - Proposed Rule Change Relating to Mediation Fee Structure

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed is the above-numbered rule filing. Also enclosed is a 3-1/2" disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Louise Corso, Assistant General Counsel, Office of General Counsel, NASD Regulation, Inc., at (202) 728-6939; e-mail louise.corso@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Joan C. Conley
Senior Vice President
and Corporate Secretary

Enclosures

SECURITIES AND EXCHANGE COMMISSION

Washington, D. C.

Form 19b-4

Proposed Rule Change

by

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) under the Securities Exchange Act of 1934 (“Act”), the National Association of Securities Dealers, Inc. (“NASD” or “Association”), through its wholly owned subsidiary, NASD Regulation, Inc. (“NASD Regulation”), is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to the Code of Arbitration Procedure (“Code”) to encourage the use of mediation and increase revenue by adjusting mediation fee schedules, and to permit parties to agree to stay arbitrations in order to mediate the claim. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * *

Rule 10205. Schedule of Fees for Industry and Clearing Controversies

(a) - (i) No Change.

[(j)] Each party to a matter submitted to a mediation administered by the Association where there is no Association arbitration proceeding pending shall pay an administrative fee of \$250. The parties to a mediation administered by the Association shall pay all of the mediator's charges, including the mediator's travel and other expenses. The charges shall be specified in the Submission Agreement and shall be apportioned equally among the parties unless they agree otherwise. Each party shall deposit with the Association their proportional share of the anticipated mediator charges and expenses, as determined by the Director of Mediation, prior to the first mediation session. Mediator charges, except travel and other expenses, are as follows:

(1) Initial Mediation Session: \$600 or four (4) times the mediator's hourly rate agreed to by the parties and the mediator; and

(2) Additional Mediation Sessions: \$150 per hour, or such other hourly rate agreed to by the parties and the mediator.]

* * *

Rule 10332. Schedule of Fees for Customer Disputes

(a) - (h) No change.

[(i) Each party to a matter submitted to a mediation administered by the Association where there is no Association arbitration proceeding pending shall pay an administrative fee of \$150.

[(j) The parties to a mediation administered by the Association shall pay all of the mediator's charges, including the mediator's travel and other expenses. The charges shall be specified in the Submission Agreement and shall be apportioned equally among the parties unless they agree otherwise. Each party shall deposit with the Association their proportional share of the anticipated mediator charges and expenses, as determined by the Director of Mediation, prior to the first mediation session. Mediator charges, except travel and other expenses, are as follows:

(1) Initial Mediation Session: \$600 or four (4) times the mediator's hourly rate agreed to by the parties and the mediator; and

(2) Additional Mediation Sessions: \$150 per hour, or such other hourly rate agreed to by the parties and the mediator.]

* * *

Rule 10403. Arbitration Proceedings

(a) Unless the parties agree otherwise, the submission of a matter for mediation shall not stay or otherwise delay the arbitration of a matter pending under this Code. When all parties

agree to stay the arbitration in order to mediate the claim, the arbitration proceeding shall be stayed, notwithstanding any provision to the contrary in this Code.

(b) If mediation is conducted through NASD Regulation, no adjournment fees will be charged for staying the arbitration proceeding in order to mediate.¹

* * *

Rule 10407. Mediation Fees

(a) Filing Fees: Cases Filed Directly in Mediation

Each party to a matter submitted directly to a mediation administered by the Association shall pay an administrative fee to the Association in the amounts indicated in the schedule below, unless such fee is specifically waived by the Director of Mediation.

Amount in Controversy	Customer and Associated Person Fee	Member Fee	Total Fees
=====	=====	=====	=====
\$.01-\$25,000	\$ 50	\$150	\$200
\$25,000.01-\$100,000	\$150	\$300	\$450
Over \$100,000	\$300	\$500	\$800

(b) Filing Fees: Cases Initially Filed in Arbitration

When a matter is initially filed in arbitration and subsequently submitted to a mediation administered by the Association, each party shall pay an administrative fee to the Association in

¹ Note: The reference will be changed to NASD Dispute Resolution, Inc., when the new subsidiary becomes operational.

the amounts indicated in the schedule below, unless such fee is specifically waived by the Director of Mediation.

Amount in Controversy	Customer and Associated Person Fee	Member Fee	Total Fees
=====	=====	=====	=====
\$.01-\$25,000	\$ 0	\$ 0	\$ 0
\$25,000.01-\$100,000	\$100	\$150	\$250
Over \$100,000	\$250	\$500	\$750

(c) Mediator Fees and Expenses

The parties to a mediation administered by the Association shall pay all of the mediator's charges, including the mediator's travel and other expenses. The charges shall be specified in the Submission Agreement and shall be apportioned equally among the parties unless they agree otherwise. Each party shall deposit with the Association its proportional share of the anticipated mediator charges and expenses, as determined by the Director of Mediation, prior to the first mediation session.

* * *

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) The proposed rule change was approved by the Board of Directors of NASD Regulation at its meeting on January 26, 2000, which authorized the filing of the rule change

with the Commission. The Nasdaq Stock Market has been provided an opportunity to consult with respect to the proposed rule change, pursuant to the Plan of Allocation and Delegation of Functions by the NASD to its Subsidiaries. The NASD Board of Governors reviewed and approved the proposed rule change at its meeting on January 27, 2000. No other action by the NASD is necessary for the filing of the proposed rule change. Section 1(a)(ii) of Article VII of the NASD By-Laws permits the NASD Board of Governors to adopt amendments to NASD Rules without recourse to the membership for approval.

The NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 60 days following Commission approval. The effective date will be 30 days following publication of the Notice to Members announcing Commission approval.

(b) Questions regarding this rule filing may be directed to Louise Corso, Assistant General Counsel, NASD Regulation, Office of General Counsel, at (202) 728-6939.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

The proposed rule change is designed to encourage the use of mediation, especially in smaller cases, and to adjust mediation fee schedules. This adjustment is a first step to make the NASD Regulation Mediation Program ("Mediation Program") financially self-sustaining. The proposed rule change also permits parties to stay arbitrations by agreement in order to mediate the claim and eliminates the adjournment fees when parties conduct their mediation through NASD Regulation.

Background

In 1995, NASD Regulation initiated a mediation program to provide an additional dispute resolution option for parties. Mediation is an informal, non-binding, voluntary process in which an impartial person, trained in facilitation and negotiation techniques, helps the parties reach a mutually acceptable resolution. What distinguishes mediation from other forms of dispute resolution--principally, arbitration and litigation--is that the mediator does not impose a resolution on the parties, but rather works with the parties to create their own resolution. The resulting settlements often save the parties substantial time and expense.

The goal of the Mediation Program is to provide public customers, member firms, and associated persons with another effective way to resolve their disputes. Since its inception in 1995, over 3500 cases have been submitted to the Mediation Program. By 1999, parties in twenty percent of all arbitration cases filed with NASD Regulation used mediation to help resolve their disputes.

The Mediation Program has been extremely successful, both in terms of settlement rates and customer satisfaction. Approximately eighty percent of the mediations settle within 60 to 90 days of the parties' formal agreement to mediate. Parties who have used the Mediation Program consistently express satisfaction with their experience, even those who do not reach full agreement. Sometimes parts of a dispute are resolved in mediation, leaving fewer issues to be resolved in arbitration. During the mediation process, the parties and their representatives gain a better understanding of their case. Improved lines of communication often place the parties in a better position to settle the case at a later stage.

The attributes that have contributed to the success of the Mediation Program include:

- The mediators on the roster are highly qualified and experienced. Prior to admission to the roster, mediators are carefully screened by NASD Regulation staff and by members of the National Arbitration and Mediation Committee. Formal multi-day mediator training and experience as a mediator are requirements of service. NASD Regulation's 850 mediators represent a cross-section of people, diverse in culture, profession, and background. Many have extensive knowledge of securities law and industry practices, and many are also arbitrators with training and experience in resolving securities matters.
- NASD Regulation staff in the Office of Dispute Resolution ("ODR") performs a number of administrative services to facilitate the mediation. The staff works diligently to educate parties on the mediation process, to encourage them to mediate, to assist them in finding the best mediator for their case, and to ensure that the process runs smoothly. When one party expresses an interest in mediation, ODR will contact the other party or parties, explain the mediation process, and answer any questions. ODR staff is trained to explain the benefits of mediation and to help bring all parties to the table. After conferring with the parties, ODR will propose a list of neutrals consistent with the parties' needs from its roster of experienced mediators. The list is accompanied by a complete profile of each mediator. The parties may select their mediator from that list or ask for additional lists. The parties also may choose a mediator not on the list or from outside the Mediation Program roster. The staff works with the mediator and the parties to select a mutually convenient date and location for the mediation.

- The Mediation Program is completely voluntary. Parties choose whether, and at what point in the course of their case, to enter mediation.
- The Mediation Program is flexible and controlled by the parties. The parties control the process, scheduling and outcome of the dispute. Parties may mediate before filing a formal claim or pleading in arbitration, or at any stage of the arbitration process. They may submit all or some of the issues in dispute to mediation, including selected substantive or procedural issues such as the extent, nature, and schedule of discovery. The first session can be scheduled in a matter of days or weeks. Meetings can be conducted in person in over 50 cities in the United States and abroad, by telephone, video conference, or any other method agreeable to the parties and the mediator.
- Mediating through NASD Regulation is cost-effective. Most mediations are successfully concluded in less than a single day, resulting in lower attorney fees for the parties. Parties who choose to mediate also avoid hearing fees if they can settle before proceeding to a hearing. Finally, parties in mediation benefit by avoiding discovery costs typically associated with other forms of dispute resolution.

Operating the Mediation Program

The Mediation Program currently is subsidized. There are fifteen employees in ODR's mediation department located in five offices. For 1999, total direct expenses for the Mediation Program were approximately \$960,000 as compared to \$100,000 in direct revenues, resulting in an annual program deficit of \$860,000. Because the Mediation Program has continued to grow steadily, NASD Regulation believes that this is an appropriate time to change the mediation fee structure.

The objective of the proposed rule change is to take preliminary steps to make the Mediation Program financially self-sustaining while keeping mediation as a cost-effective alternative to arbitration for parties with claims of any dollar value. NASD Regulation estimates that the proposed mediation fee package will generate income of \$640,000 on an annual basis, assuming a level number of case filings. These funds will be used to help offset the operational costs of the Mediation Program and to ensure the continuation of this valuable service. In addition, the fee adjustments should add incentives for parties to mediate smaller cases.

In addition to this proposed rule change, NASD Regulation has recently instituted another measure that will increase revenues but did not require a change to the Code. Mediators on the roster of the Mediation Program individually set the fees they charge parties on each case. The rates are usually hourly and vary depending upon the mediators' background, experience, and reputation. NASD Regulation assesses a fee for each hour that the mediator bills the parties. The fee defrays a part of the costs of the case administration services that ODR provides to the mediators.

Formerly, NASD Regulation charged mediators a fee of \$25 for each hour the mediator billed the parties. This fee was significantly less than the charges of other dispute resolution providers, including the American Arbitration Association and JAMS, and will remain significantly less even with the enhanced fees. Effective April 3, 2000, NASD Regulation has eliminated the flat rate in favor of a sliding rate tied to the mediator's hourly compensation. This fee schedule, as well as other changes, is designed to encourage mediators to charge lower rates for small claims and to agree to handle some cases pro bono. The new rates are as follows:

Mediator's Hourly Rate =====	NASD Regulation Fee =====
Pro Bono	None
Up to \$99.99	\$25
\$100 to \$199.99	\$35
\$200 and over	\$50

Reduced Fees for Smaller Claims

NASD Regulation is committed to making mediation attractive to customers with smaller claims, that is, claims with less than \$25,000 in dispute. Mediation is especially well-suited to resolving smaller disputes. However, with most mediators' hourly rates at \$150 or more, mediation costs may exceed the parties' cost (exclusive of attorneys' fees) to arbitrate smaller claims. During 1997 and 1998, fewer than ten percent of all mediations involved claims of less than \$25,000.

NASD Regulation has recently asked its mediators to help reduce the cost of mediation for small cases by agreeing to charge reduced rates to mediate cases involving claims of \$25,000 or less. Specifically, it has suggested that mediators agree to charge \$50 an hour for mediations where the amount in dispute is less than \$25,000.

Mediators may set a limit on the number of reduced fee mediations they will conduct during a year. After a mediator serves the designated number of times, ODR staff will not propose his or her name for small claim mediations for the remainder of the year, unless the mediator is willing to serve on more cases at the reduced rate.

Summary of Proposed Rule Change

The rules setting mediation filing fees are currently contained in Rules 10205 and 10332 of the Code which primarily address intra-industry and customer arbitration fees, respectively. NASD Regulation proposes to delete the provisions relating to mediation fees from the arbitration sections of the Code, and include them in the Rule 10400 Series that pertains to mediation. Specifically, NASD Regulation would create a new rule, Rule 10407, entitled “Mediation Fees.”

The proposed rule change includes three components. First, Rule 10407(a) replaces the current flat fee with a sliding scale mediation case filing fee schedule. Second, Rule 10407(b) requires parties to pay a mediation case filing fee when they choose to use the Mediation Program after they have initiated arbitration. Third, changes to Rule 10403(a) make clear that the parties in arbitration can agree to stay the proceeding in order to mediate their claims, and new Rule 10403(b) provides an incentive to use the Mediation Program rather than an alternative forum when mediation takes place after an arbitration has been filed.

Mediation Case Filing Fees for Cases Filed Directly in Mediation: Rule 10407(a)

About fifteen percent of the 850 mediation cases filed annually are filed directly in mediation and result in a mediation administrative fee charged to parties. NASD Regulation currently charges \$150 per party for customer cases and \$250 per party for intra-industry cases, irrespective of the amount in dispute. These fees are found in Rules 10205(j) and 10332(i).

NASD Regulation proposes to replace the flat fee with a sliding scale fee schedule in new Rule 10407(a). The schedule has one column for customers and associated persons, and another

column for member firms. The filing fees are lowest for the smallest claims but increase as the amount in controversy gets larger.²

Customers in mediation whose cases involve up to \$25,000 in controversy would be charged only \$50, rather than the present filing fee of \$150. This is another measure that is intended to encourage the use of mediation for smaller claims. For claims between \$25,000 and \$100,000, customers pay a \$150 filing fee, the same as in the current model. However, when the claim exceeds \$100,000, customers will pay a \$300 filing fee. As noted, this same schedule also applies to claims made by associated persons.

Fees also are adjusted for members. Under the proposed rule, for cases up to \$25,000 in controversy, members will pay \$150, which is the current rate for a customer dispute, but is lower than the current \$250 rate for intra-industry disputes. For claims between \$25,000 and \$100,000, the charge for members increases to \$300, slightly higher than the intra-industry rate under the flat fee schedule. For claims exceeding \$100,000, the member fee will increase to \$500. For all claims, regardless of the amount in dispute, customers and members will pay less than the corresponding filing fees for arbitration.

Mediation Case Filing Fees for Cases Initially Filed in Arbitration: Rule 10407(b)

For cases first filed in arbitration that later go to mediation -- which amount to about eighty-five percent of all NASD Regulation mediations -- NASD Regulation currently waives all mediation case filing fees for the parties, as stated in Rules 10205(j) and 10332(i). NASD Regulation proposes to eliminate the fee waiver for all cases over \$25,000 and to charge mediation filing fees to parties choosing mediation after the arbitration case is already filed.

² NASD Regulation currently has a sliding scale schedule in place for arbitration fees. See the schedule of fees in Rules 10205 and 10332.

ODR's mediation staff incurs expenses that are distinct from those incurred by its arbitration staff. For cases filed in arbitration first, the mediation staff expends a great deal of time educating the parties about the mediation alternative and attempting to encourage the parties to agree to mediate. NASD Regulation staff expends these efforts to encourage parties to mediate because mediation generally saves them costs and time. Settlement rates are consistently high and parties report a high level of satisfaction with the process.

Arbitration fees cover arbitration case administrative tasks, but they do not cover the expenses of the mediation staff. Eliminating the fee waiver would cover some of the resources expended by the mediation staff in moving cases from arbitration to mediation.

In new Rule 10407(b), consistent with other efforts to increase incentives for parties to mediate claims under \$25,000, NASD Regulation does not impose any filing fee for converted small cases. NASD Regulation believes it is beneficial to resolve these claims through mediation because of the cost savings to the parties.

NASD Regulation proposes a reduced mediation filing fee for cases between \$25,000 and \$100,000 to induce members and investors to choose mediation. Members' filing fees for converted cases, found in Rule 10407(b), would be fifty percent less than for a case that is first filed in mediation, found in Rule 10407(a). Similarly, fees for customers would be reduced by \$50.

In matters involving more than \$100,000 in dispute, the proposed mediation filing fee for members is equal to the fee for a case that is first filed in mediation. Investors would get the benefit of a small reduction in fees for cases converted to mediation from the arbitration docket.

Mediator Fees and Expenses: Rule 10407(c)

The rule language regarding mediator fees and expenses contained in Rules 10205(j) and 10332(j) is moved to Rule 10407(c). The rule language is unchanged, with one exception. NASD Regulation proposes to delete the final sentence in Rules 10205(j) and 10332(j), respectively, which specifies mediator charges. NASD Regulation has found that mediators do not charge the parties fees for "mediation sessions," as indicated in the rule. Rather, mediators charge for the actual hours of services they provide. Therefore, NASD Regulation is deleting the final sentence in Rules 10205(j) and 10332(j) when it moves the other relevant language to new Rule 10407(c).

Proposed Changes to Rule 10403

NASD Regulation proposes to amend Rule 10403 of the Code in two ways. First, it adds language to Rule 10403(a) to make it clear that parties who agree to submit a matter for mediation can also agree to stay the arbitration. The parties can do so notwithstanding Rule 10319, the rule that gives arbitrators discretion whether to stay an arbitration proceeding. This rule change will benefit the parties by saving them time and money and by relieving them of the problems of proceeding in two arenas at the same time. Moreover, this change is consistent with the approach of other alternative dispute resolution providers.

Second, NASD Regulation proposes to add a new provision, Rule 10403(b), that encourages the use of the NASD Regulation Mediation Program. Whenever the mediation is conducted through NASD Regulation, the parties would avoid payment of arbitration adjournment fees.

(b) Statutory Basis

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that the Association'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. NASD Regulation believes that the proposed rule change is in the public interest because it will encourage the use of mediation, especially for small claims.

4. Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

6. Extension of Time Period for Commission Action

NASD Regulation does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibit

Completed notice of proposed rule change for publication in the Federal Register.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD Regulation has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD REGULATION, INC.

BY: _____
Joan C. Conley, Senior Vice President and
Corporate Secretary

Date: March 8, 2000

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-NASD-00-11)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Changes to the Mediation Fee Structure

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on , the National Association of Securities Dealers, Inc. (“NASD”), through its wholly owned subsidiary, NASD Regulation, Inc. (“NASD Regulation”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD Regulation. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS OF SUBSTANCE OF THE PROPOSED RULE CHANGE

NASD Regulation is proposing to amend Rule 10205, 10332 and 10403 of the Code of Arbitration Procedure (“Code”) of the National Association of Securities Dealers, Inc. (“NASD” or “Association”) and add Rule 10407 to the Code, to encourage the use of mediation and increase revenue by adjusting mediation fee schedules, and to permit parties to agree to stay arbitrations in order to mediate the claim.

Below is the text of the proposed rule change. Proposed new language is in italics; proposed deletions are in brackets.

* * *

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

Rule 10205. Schedule of Fees for Industry and Clearing Controversies

(a) - (i) No Change.

[(j) Each party to a matter submitted to a mediation administered by the Association where there is no Association arbitration proceeding pending shall pay an administrative fee of \$250. The parties to a mediation administered by the Association shall pay all of the mediator's charges, including the mediator's travel and other expenses. The charges shall be specified in the Submission Agreement and shall be apportioned equally among the parties unless they agree otherwise. Each party shall deposit with the Association their proportional share of the anticipated mediator charges and expenses, as determined by the Director of Mediation, prior to the first mediation session. Mediator charges, except travel and other expenses, are as follows:

(1) Initial Mediation Session: \$600 or four (4) times the mediator's hourly rate agreed to by the parties and the mediator; and

(2) Additional Mediation Sessions: \$150 per hour, or such other hourly rate agreed to by the parties and the mediator.]

* * *

Rule 10332. Schedule of Fees for Customer Disputes

(a) - (h) No change.

[(i) Each party to a matter submitted to a mediation administered by the Association where there is no Association arbitration proceeding pending shall pay an administrative fee of \$150.

[(j) The parties to a mediation administered by the Association shall pay all of the mediator's charges, including the mediator's travel and other expenses. The charges shall be

specified in the Submission Agreement and shall be apportioned equally among the parties unless they agree otherwise. Each party shall deposit with the Association their proportional share of the anticipated mediator charges and expenses, as determined by the Director of Mediation, prior to the first mediation session. Mediator charges, except travel and other expenses, are as follows:

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- (2) Additional Mediation Sessions: \$150 per hour, or such other hourly rate agreed to by the parties and the mediator.]

* * *

Rule 10403. Arbitration Proceedings

(a) Unless the parties agree otherwise, the submission of a matter for mediation shall not stay or otherwise delay the arbitration of a matter pending under this Code. When all parties agree to stay the arbitration in order to mediate the claim, the arbitration proceeding shall be stayed, notwithstanding any provision to the contrary in this Code.

(b) If mediation is conducted through NASD Regulation, no adjournment fees will be charged for staying the arbitration proceeding in order to mediate.³

* * *

Rule 10407. Mediation Fees

(a) Filing Fees: Cases Filed Directly in Mediation

³ Note: The reference will be changed to NASD Dispute Resolution, Inc., when the new subsidiary becomes operational.

Each party to a matter submitted directly to a mediation administered by the Association shall pay an administrative fee to the Association in the amounts indicated in the schedule below, unless such fee is specifically waived by the Director of Mediation.

Amount in Controversy	Customer and Associated Person Fee	Member Fee	Total Fees
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\$.01-\$25,000	\$ 50	\$150	\$200
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Over \$100,000	\$300	\$500	\$800

(b) Filing Fees: Cases Initially Filed in Arbitration

When a matter is initially filed in arbitration and subsequently submitted to a mediation administered by the Association, each party shall pay an administrative fee to the Association in the amounts indicated in the schedule below, unless such fee is specifically waived by the Director of Mediation.

Amount in Controversy	Customer and Associated Person Fee	Member Fee	Total Fees
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\$.01-\$25,000	\$ 0	\$ 0	\$ 0
\$25,000.01-\$100,000	\$100	\$150	\$250
Over \$100,000	\$250	\$500	\$750

(c) Mediator Fees and Expenses

The parties to a mediation administered by the Association shall pay all of the mediator's charges, including the mediator's travel and other expenses. The charges shall be specified in the Submission Agreement and shall be apportioned equally among the parties unless they agree otherwise. Each party shall deposit with the Association its proportional share of the anticipated mediator charges and expenses, as determined by the Director of Mediation, prior to the first mediation session.

* * *

II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its filing with the Commission, NASD Regulation included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NASD Regulation has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(1) **Purpose**

The proposed rule change is designed to encourage the use of mediation, especially in smaller cases, and to adjust mediation fee schedules. This adjustment is a first step to make the NASD Regulation Mediation Program ("Mediation Program") financially self-sustaining. The proposed rule change also permits parties to stay arbitrations by agreement in order to mediate

the claim and eliminates the adjournment fees when parties conduct their mediation through NASD Regulation.

Background

In 1995, NASD Regulation initiated a mediation program to provide an additional dispute resolution option for parties. Mediation is an informal, non-binding, voluntary process in which an impartial person, trained in facilitation and negotiation techniques, helps the parties reach a mutually acceptable resolution. What distinguishes mediation from other forms of dispute resolution--principally, arbitration and litigation--is that the mediator does not impose a resolution on the parties, but rather works with the parties to create their own resolution. The resulting settlements often save the parties substantial time and expense.

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The Mediation Program has been extremely successful, both in terms of settlement rates and customer satisfaction. Approximately eighty percent of the mediations settle within 60 to 90 days of the parties' formal agreement to mediate. Parties who have used the Mediation Program consistently express satisfaction with their experience, even those who do not reach full agreement. Sometimes parts of a dispute are resolved in mediation, leaving fewer issues to be resolved in arbitration. During the mediation process, the parties and their representatives gain a

better understanding of their case. Improved lines of communication often place the parties in a better position to settle the case at a later stage.

The attributes that have contributed to the success of the Mediation Program include:

- The mediators on the roster are highly qualified and experienced. Prior to admission to the roster, mediators are carefully screened by NASD Regulation staff and by members of the National Arbitration and Mediation Committee. Formal multi-day mediator training and experience as a mediator are requirements of service. NASD Regulation's 850 mediators represent a cross-section of people, diverse in culture, profession, and background. Many have extensive knowledge of securities law and industry practices, and many are also arbitrators with training and experience in resolving securities matters.
- NASD Regulation staff in the Office of Dispute Resolution ("ODR") performs a number of administrative services to facilitate the mediation. The staff works diligently to educate parties on the mediation process, to encourage them to mediate, to assist them in finding the best mediator for their case, and to ensure that the process runs smoothly. When one party expresses an interest in mediation, ODR will contact the other party or parties, explain the mediation process, and answer any questions. ODR staff is trained to explain the benefits of mediation and to help bring all parties to the table. After conferring with the parties, ODR will propose a list of neutrals consistent with the parties' needs from its roster of experienced mediators. The list is accompanied by a complete profile of each mediator. The parties may select their mediator from that list or ask for additional lists. The parties also may choose a

mediator not on the list or from outside the Mediation Program roster. The staff works with the mediator and the parties to select a mutually convenient date and location for the mediation.

- The Mediation Program is completely voluntary. Parties choose whether, and at what point in the course of their case, to enter mediation.
- The Mediation Program is flexible and controlled by the parties. The parties control the process, scheduling and outcome of the dispute. Parties may mediate before filing a formal claim or pleading in arbitration, or at any stage of the arbitration process. They may submit all or some of the issues in dispute to mediation, including selected substantive or procedural issues such as the extent, nature, and schedule of discovery. The first session can be scheduled in a matter of days or weeks. Meetings can be conducted in person in over 50 cities in the United States and abroad, by telephone, video conference, or any other method agreeable to the parties and the mediator.
- Mediating through NASD Regulation is cost-effective. Most mediations are successfully concluded in less than a single day, resulting in lower attorney fees for the parties. Parties who choose to mediate also avoid hearing fees if they can settle before proceeding to a hearing. Finally, parties in mediation benefit by avoiding discovery costs typically associated with other forms of dispute resolution.

Operating the Mediation Program

The Mediation Program currently is subsidized. There are fifteen employees in ODR's mediation department located in five offices. For 1999, total direct expenses for the Mediation Program were approximately \$960,000 as compared to \$100,000 in direct revenues, resulting in

an annual program deficit of \$860,000. Because the Mediation Program has continued to grow steadily, NASD Regulation believes that this is an appropriate time to change the mediation fee structure.

The objective of the proposed rule change is to take preliminary steps to make the Mediation Program financially self-sustaining while keeping mediation as a cost-effective alternative to arbitration for parties with claims of any dollar value. NASD Regulation estimates that the proposed mediation fee package will generate income of \$640,000 on an annual basis, assuming a level number of case filings. These funds will be used to help offset the operational costs of the Mediation Program and to ensure the continuation of this valuable service. In addition, the fee adjustments should add incentives for parties to mediate smaller cases.

In addition to this proposed rule change, NASD Regulation has recently instituted another measure that will increase revenues but did not require a change to the Code. Mediators on the roster of the Mediation Program individually set the fees they charge parties on each case. The rates are usually hourly and vary depending upon the mediators' background, experience, and reputation. NASD Regulation assesses a fee for each hour that the mediator bills the parties. The fee defrays a part of the costs of the case administration services that ODR provides to the mediators.

Formerly, NASD Regulation charged mediators a fee of \$25 for each hour the mediator billed the parties. This fee was significantly less than the charges of other dispute resolution providers, including the American Arbitration Association and JAMS, and will remain significantly less even with the enhanced fees. Effective April 3, 2000, NASD Regulation has eliminated the flat rate in favor of a sliding rate tied to the mediator's hourly compensation. This

fee schedule, as well as other changes, is designed to encourage mediators to charge lower rates for small claims and to agree to handle some cases pro bono. The new rates are as follows:

Mediator's Hourly Rate	NASD Regulation Fee
=====	=====
Pro Bono	None
Up to \$99.99	\$25
\$100 to \$199.99	\$35
\$200 and over	\$50

Reduced Fees for Smaller Claims

NASD Regulation is committed to making mediation attractive to customers with smaller claims, that is, claims with less than \$25,000 in dispute. Mediation is especially well-suited to resolving smaller disputes. However, with most mediators' hourly rates at \$150 or more, mediation costs may exceed the parties' cost (exclusive of attorneys' fees) to arbitrate smaller claims. During 1997 and 1998, fewer than ten percent of all mediations involved claims of less than \$25,000.

NASD Regulation has recently asked its mediators to help reduce the cost of mediation for small cases by agreeing to charge reduced rates to mediate cases involving claims of \$25,000 or less. Specifically, it has suggested that mediators agree to charge \$50 an hour for mediations where the amount in dispute is less than \$25,000.

Mediators may set a limit on the number of reduced fee mediations they will conduct during a year. After a mediator serves the designated number of times, ODR staff will not propose his or her name for small claim mediations for the remainder of the year, unless the mediator is willing to serve on more cases at the reduced rate.

Summary of Proposed Rule Change

The rules setting mediation filing fees are currently contained in Rules 10205 and 10332 of the Code which primarily address intra-industry and customer arbitration fees, respectively. NASD Regulation proposes to delete the provisions relating to mediation fees from the arbitration sections of the Code, and include them in the Rule 10400 Series that pertains to mediation. Specifically, NASD Regulation would create a new rule, Rule 10407, entitled “Mediation Fees.”

The proposed rule change includes three components. First, Rule 10407(a) replaces the current flat fee with a sliding scale mediation case filing fee schedule. Second, Rule 10407(b) requires parties to pay a mediation case filing fee when they choose to use the Mediation Program after they have initiated arbitration. Third, changes to Rule 10403(a) make clear that the parties in arbitration can agree to stay the proceeding in order to mediate their claims, and new Rule 10403(b) provides an incentive to use the Mediation Program rather than an alternative forum when mediation takes place after an arbitration has been filed.

Mediation Case Filing Fees for Cases Filed Directly in Mediation: Rule 10407(a)

About fifteen percent of the 850 mediation cases filed annually are filed directly in mediation and result in a mediation administrative fee charged to parties. NASD Regulation currently charges \$150 per party for customer cases and \$250 per party for intra-industry cases, irrespective of the amount in dispute. These fees are found in Rules 10205(j) and 10332(i).

NASD Regulation proposes to replace the flat fee with a sliding scale fee schedule in new Rule 10407(a). The schedule has one column for customers and associated persons, and another

column for member firms. The filing fees are lowest for the smallest claims but increase as the amount in controversy gets larger.⁴

Customers in mediation whose cases involve up to \$25,000 in controversy would be charged only \$50, rather than the present filing fee of \$150. This is another measure that is intended to encourage the use of mediation for smaller claims. For claims between \$25,000 and \$100,000, customers pay a \$150 filing fee, the same as in the current model. However, when the claim exceeds \$100,000, customers will pay a \$300 filing fee. As noted, this same schedule also applies to claims made by associated persons.

Fees also are adjusted for members. Under the proposed rule, for cases up to \$25,000 in controversy, members will pay \$150, which is the current rate for a customer dispute, but is lower than the current \$250 rate for intra-industry disputes. For claims between \$25,000 and \$100,000, the charge for members increases to \$300, slightly higher than the intra-industry rate under the flat fee schedule. For claims exceeding \$100,000, the member fee will increase to \$500. For all claims, regardless of the amount in dispute, customers and members will pay less than the corresponding filing fees for arbitration.

Mediation Case Filing Fees for Cases Initially Filed in Arbitration: Rule 10407(b)

For cases first filed in arbitration that later go to mediation -- which amount to about eighty-five percent of all NASD Regulation mediations -- NASD Regulation currently waives all mediation case filing fees for the parties, as stated in Rules 10205(j) and 10332(i). NASD Regulation proposes to eliminate the fee waiver for all cases over \$25,000 and to charge mediation filing fees to parties choosing mediation after the arbitration case is already filed.

⁴ NASD Regulation currently has a sliding scale schedule in place for arbitration fees. See the schedule of fees in Rules 10205 and 10332.

ODR's mediation staff incurs expenses that are distinct from those incurred by its arbitration staff. For cases filed in arbitration first, the mediation staff expends a great deal of time educating the parties about the mediation alternative and attempting to encourage the parties to agree to mediate. NASD Regulation staff expends these efforts to encourage parties to mediate because mediation generally saves them costs and time. Settlement rates are consistently high and parties report a high level of satisfaction with the process.

Arbitration fees cover arbitration case administrative tasks, but they do not cover the expenses of the mediation staff. Eliminating the fee waiver would cover some of the resources expended by the mediation staff in moving cases from arbitration to mediation.

In new Rule 10407(b), consistent with other efforts to increase incentives for parties to mediate claims under \$25,000, NASD Regulation does not impose any filing fee for converted small cases. NASD Regulation believes it is beneficial to resolve these claims through mediation because of the cost savings to the parties.

NASD Regulation proposes a reduced mediation filing fee for cases between \$25,000 and \$100,000 to induce members and investors to choose mediation. Members' filing fees for converted cases, found in Rule 10407(b), would be fifty percent less than for a case that is first filed in mediation, found in Rule 10407(a). Similarly, fees for customers would be reduced by \$50.

In matters involving more than \$100,000 in dispute, the proposed mediation filing fee for members is equal to the fee for a case that is first filed in mediation. Investors would get the benefit of a small reduction in fees for cases converted to mediation from the arbitration docket.

Mediator Fees and Expenses: Rule 10407(c)

The rule language regarding mediator fees and expenses contained in Rules 10205(j) and 10332(j) is moved to Rule 10407(c). The rule language is unchanged, with one exception. NASD Regulation proposes to delete the final sentence in Rules 10205(j) and 10332(j), respectively, which specifies mediator charges. NASD Regulation has found that mediators do not charge the parties fees for "mediation sessions," as indicated in the rule. Rather, mediators charge for the actual hours of services they provide. Therefore, NASD Regulation is deleting the final sentence in Rules 10205(j) and 10332(j) when it moves the other relevant language to new Rule 10407(c).

Proposed Changes to Rule 10403

NASD Regulation proposes to amend Rule 10403 of the Code in two ways. First, it adds language to Rule 10403(a) to make it clear that parties who agree to submit a matter for mediation can also agree to stay the arbitration. The parties can do so notwithstanding Rule 10319, the rule that gives arbitrators discretion whether to stay an arbitration proceeding. This rule change will benefit the parties by saving them time and money and by relieving them of the problems of proceeding in two arenas at the same time. Moreover, this change is consistent with the approach of other alternative dispute resolution providers.

Second, NASD Regulation proposes to add a new provision, Rule 10403(b), that encourages the use of the NASD Regulation Mediation Program. Whenever the mediation is conducted through NASD Regulation, the parties would avoid payment of arbitration adjournment fees.

(2) Statutory Basis

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that the Association'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. NASD Regulation believes that the proposed rule change is in the public interest because it will encourage the use of mediation, especially for small claims.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. DATE OF EFFECTIVENESS OF THE PROPOSED RULE CHANGE AND TIMING FOR COMMISSION ACTION

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- A. by order approve such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. 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 Room. Copies of such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

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

Jonathan G. Katz
Secretary