

January 31, 2002

Florence Harmon
Senior Special Counsel
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

Re: File No. SR-NASD-2002-15 – Default Procedures for Claims against Terminated
Members and Associated Persons

Dear Ms. Harmon:

Pursuant to Rule 19b-4, enclosed please find 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 Jean I. Feeney, Associate Vice President and Chief Counsel, NASD Dispute Resolution, Inc., at (202) 728-6959; e-mail jean.feeney@nasd.com. The fax number is (202) 728-8833.

Very truly yours,

Linda D. Fienberg
President

Enclosures

File No. SR-NASD-2002-15
Consists of 23 Pages

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 Dispute Resolution, Inc. (“NASD Dispute Resolution”), is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to the NASD Code of Arbitration Procedure to provide default procedures for situations in which a suspended, terminated or otherwise defunct member or associated person fails to answer or participate in an arbitration proceeding, and the claimant nevertheless elects to pursue arbitration. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * *

CODE OF ARBITRATION PROCEDURE

10314. Initiation of Proceedings

Except as otherwise provided herein, an arbitration proceeding under this Code shall be instituted as follows:

(a) Statement of Claim

Unchanged.

(b) Answer - Defenses, Counterclaims, and/or Cross-Claims

(1) Unchanged.

(2) (A) - (B) Unchanged.

(C) A Respondent, Responding Claimant, Cross-Claimant, Cross-Respondent, or Third-Party Respondent who fails to file an Answer within 45 calendar days from receipt of service of a Claim, unless the time to answer has been extended pursuant to subparagraph (5), below, may, in the discretion of the arbitrators, be barred from presenting any matter, arguments, or defenses at the hearing. Such a party may also be subject to default procedures as provided in paragraph (e) below.

(3) - (4) Unchanged.

(5) Unchanged.

(c) - (d)

Unchanged.

(e) Default Procedures

(1) A Respondent, Cross-Respondent, or Third-Party Respondent that fails to file an Answer within 45 calendar days from receipt of service of a Claim, unless the time to answer has been extended pursuant to paragraph (b)(5), may be subject to default procedures, as provided in this paragraph, if it is:

(A) a member whose membership has been terminated, suspended, canceled, or revoked;

(B) a member that has been expelled from the NASD;

(C) a member that is otherwise defunct; or

(D) an associated person whose registration is terminated, revoked, or suspended.

(2) If all Claimants elect to use these default procedures, the Claimant(s) shall notify the Director in writing and shall send a copy of such notification to all other parties at the same time and in the same manner as the notification was sent to the Director.

(3) If the case meets the requirements for proceeding under default procedures, the Director shall notify all parties.

(4) The Director shall appoint a single arbitrator pursuant to Rule 10308 to consider the Statement of Claim and other documents presented by the Claimant(s). The arbitrator may request additional information from the Claimant(s) before rendering an award. No hearing shall be held, and the default award shall have no effect on any non-defaulting party.

(5) The Claimant(s) may not amend the claim to increase the relief requested after the Director has notified the parties that the claim will proceed under default procedures.

(6) An arbitrator may not make an award based solely on the non-appearance of a party. The party who appears must present a sufficient basis to support the making of an award in that party's favor. The arbitrator may not award damages in an amount greater than the damages requested in the Statement of Claim, and may not award any other relief that was not requested in the Statement of Claim.

(7) If the Respondent files an Answer after the Director has notified the parties that the claim will proceed under default procedures but before an

award has been rendered, the proceedings under this paragraph shall be terminated and the case will proceed under the regular procedures.

* * *

(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 Dispute Resolution at its meeting on October 24, 2001, which authorized the filing of the rule change with the SEC. Counsel for The Nasdaq Stock Market, Inc. and NASD Regulation, Inc. have 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 had an opportunity to review the proposed rule change at its meeting on October 25, 2001. 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.

NASD Dispute Resolution will announce the effective date of the proposed rule change in a Notice to Members following Commission approval. The effective date will be at least 30 days after publication of the Notice to Members.

(b) Questions regarding this rule filing may be directed to Jean I. Feeney, Associate Vice President and Chief Counsel, NASD Dispute Resolution, Inc., at (202) 728-6959; e-mail jean.feeney@nasd.com.

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

(a) Purpose

NASD Dispute Resolution proposes to provide default procedures for situations in which a suspended, terminated or otherwise defunct member or associated person fails to answer or participate in an arbitration proceeding, and the claimant nevertheless elects to pursue arbitration. The procedures are designed to make it easier for claimants to obtain an award against a defunct party, which award can then be enforced in court.

The United States General Accounting Office (GAO) issued a report in June 2000 expressing concern over the number of unpaid arbitration awards issued in connection with arbitration proceedings in the securities industry arbitration forums, and making several recommendations for improvements.¹ The GAO Report observed that most of the unpaid awards resulted from broker/dealers that were no longer in business.² In a May 25, 2000, letter to the GAO,³ the NASD committed to undertake several initiatives to address the issue of unpaid awards. The proposed rule change will complete NASD Dispute Resolution's implementation of all initiatives.

The GAO initiatives are listed below with a description as to the actions already taken. The last item is the proposed rule change.

¹ The report is entitled, "Securities Arbitration: Actions Needed to Address Problem of Unpaid Awards" ("GAO Report"), Report No. GAO/GGD-00-115 (June 2000), available online at www.gao.gov.

² GAO Report at 8.

³ The letter is reprinted in the GAO Report at page 66.

Require member firms and associated persons to notify NASD Dispute Resolution when they have satisfied an award.

NASD Dispute Resolution issued Notice to Members 00-55, effective September 18, 2000, which requires members to certify that they have paid or otherwise complied with an award against them or their associated persons within 30 days after service of the award. Beginning September 18, 2000, NASD Dispute Resolution has been sending two new letters when awards are served. One letter is sent only to members and associated persons against whom an award has been rendered. It requires members to inform NASD Dispute Resolution whether they or their associated persons have paid awards against them. Associated persons who have changed members since the complaint was filed are required to notify NASD Dispute Resolution directly.⁴ NASD Dispute Resolution begins the suspension process if the 30-day period has passed and there has been no notice that the member or associated person has paid the award.

Request in the award service letter that claimants notify NASD Dispute Resolution if the award has not been paid within an established number of days of service.

Notice to Members 00-55 also invites claimants to inform NASD Dispute Resolution if their awards against members or associated persons have not been paid, so that the non-summary suspension process can be commenced. The second letter implemented September 18, 2000 is sent to all parties with service of their award. It restates the requirement to pay awards within 30 days of service, and requests parties who have prevailed against a member or associated person to inform NASD Dispute Resolution if their award has not been paid.

⁴ The respondent may also provide a justification for non-payment: for example, that the parties have agreed to installment payments, that the award has been modified or vacated by a court, that a motion to vacate or modify the award has been timely filed with a court of

Propose to the NASD Board and to the SEC a rule amendment that a firm that has been terminated, suspended, or barred from the NASD, or that is otherwise defunct, cannot enforce a predispute arbitration agreement against a customer in the NASD forum.

The Boards of NASD Dispute Resolution and the NASD approved this proposal at their meetings on December 6 and 7, 2000. The SEC approved the rule change on April 6, 2001.⁵ Notice to Members 01-29, announcing the SEC's approval, was published on May 10, 2001, and the rule change was effective for all claims served on or after June 11, 2001.

Advise claimants in writing of the status of a firm or associated person (e.g., terminated, out of business, bankrupt) so they can evaluate whether to continue with arbitration.

This procedure was implemented on June 11, 2001, in connection with the previous item.

Propose to the NASD Board and to the SEC a rule amendment to provide streamlined default proceedings where the terminated or defunct member or associated person does not answer or appear, but the claimant affirmatively elects to pursue arbitration.

This is the present proposed rule change. It would provide an expedited default procedure for certain cases in which a respondent is an associated person whose registration is terminated, revoked, or suspended; a member whose membership has been terminated, suspended, canceled, or revoked; a member that has been expelled from the NASD; or a member that is otherwise defunct (collectively referred to in this rule filing as "defunct"). If a defunct respondent fails to answer the claim in a timely manner, the claimant may elect to proceed under optional default procedures as to that respondent. If there are several

competent jurisdiction and such motion has not been denied by that court, that there is a pending bankruptcy petition, or that the award has been discharged in bankruptcy.

⁵ Exchange Act Release No. 44158 (April 6, 2001) (File No. SR-NASD-01-08), 66 Federal Register 19267 (April 13, 2001).

claimants, all must agree to use default procedures. The default procedures may be used against one or more defunct respondents while the rest of the initial arbitration proceeds against any remaining respondents.⁶

If the claimant opts to use default procedures, the case will proceed with a single arbitrator without a hearing. Under the default procedures, the arbitrator will make an award based upon the Statement of Claim and any other material submitted by the claimant. The arbitrator may request additional information from the claimant before rendering an award. In keeping with the streamlined nature of the procedures, neither the claimant nor the single arbitrator will have the option to ask that two additional arbitrators be appointed to decide the case (as is sometimes done in other single-arbitrator cases).

The procedures have several provisions to safeguard the integrity of the process and discourage abuses:

- The claimant may not amend the claim to increase the relief requested after the staff has notified the parties that the claim will proceed under default procedures.
- An arbitrator may not make an award based solely on the non-appearance of a party. The party who appears must present a sufficient basis to support the making of an award in that party's favor.
- The arbitrator may not award damages in an amount greater than the damages requested in the Statement of Claim, and may not award any other relief that was not requested in the Statement of Claim.

⁶ If a case is to be bifurcated and handled under two different procedures, regular and default, each proceeding will be assigned a separate case number to avoid confusion. Proposed Rule 10314(e) provides that the default award will have no effect on any non-defaulting party.

The proposed rule provides, however, that the default award will have no effect on the non-defaulting parties. The proposed rule would apply to all types of claimants, whether they are customers, associated persons, or member firm claimants, that are bringing a claim against a suspended or terminated member or associated person. In line with the GAO's recommendations, the proposal is designed to make it easier to obtain an award against any defunct member or associated person.

Finally, if a respondent thought to be defunct belatedly files an answer or otherwise begins to participate after the staff has notified the parties that the claim will proceed under default procedures but before an award has been rendered, the default procedures will be suspended, and the case will proceed under the regular procedures.

(b) Statutory Basis

NASD Dispute Resolution 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 Dispute Resolution believes that the proposed rule change will protect investors and the public interest by making it faster and less expensive for investors and other claimants to obtain awards against defunct members and associated persons, which awards can then be enforced in court and through the NASD suspension process, while containing several provisions to safeguard the integrity of the process and discourage abuses.

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

NASD Dispute Resolution 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 Dispute Resolution 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. Exhibits

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

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

NASD DISPUTE RESOLUTION, INC.

BY: _____
Linda D. Fienberg, President

Date: January 31, 2002

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-NASD-2001-)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Default Procedures for Claims against Terminated Members and Associated Persons

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 Dispute Resolution, Inc. (“NASD Dispute Resolution”) 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 Dispute Resolution. 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 Dispute Resolution is proposing to provide default procedures for situations in which a suspended, terminated or otherwise defunct member or associated person fails to answer or participate in an arbitration proceeding, and the claimant nevertheless elects to pursue arbitration. 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).

CODE OF ARBITRATION PROCEDURE

10314. Initiation of Proceedings

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Unchanged.

(b) Answer - Defenses, Counterclaims, and/or Cross-Claims

(1) Unchanged.

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(3) - (4) Unchanged.

(5) Unchanged.

(c) - (d)

Unchanged.

² 17 CFR 240.19b-4.

(e) Default Procedures

(1) A Respondent, Cross-Respondent, or Third-Party Respondent that fails to file an Answer within 45 calendar days from receipt of service of a Claim, unless the time to answer has been extended pursuant to paragraph (b)(5), may be subject to default procedures, as provided in this paragraph, if it is:

(A) a member whose membership has been terminated, suspended, canceled, or revoked;

(B) a member that has been expelled from the NASD;

(C) a member that is otherwise defunct; or

(D) an associated person whose registration is terminated, revoked, or suspended.

(2) If all Claimants elect to use these default procedures, the Claimant(s) shall notify the Director in writing and shall send a copy of such notification to all other parties at the same time and in the same manner as the notification was sent to the Director.

(3) If the case meets the requirements for proceeding under default procedures, the Director shall notify all parties.

(4) The Director shall appoint a single arbitrator pursuant to Rule 10308 to consider the Statement of Claim and other documents presented by the Claimant(s). The arbitrator may request additional information from the Claimant(s) before rendering an award. No hearing shall be held, and the default award shall have no effect on any non-defaulting party.

(5) The Claimant(s) may not amend the claim to increase the relief requested after the Director has notified the parties that the claim will proceed under default procedures.

(6) An arbitrator may not make an award based solely on the non-appearance of a party. The party who appears must present a sufficient basis to support the making of an award in that party's favor. The arbitrator may not award damages in an amount greater than the damages requested in the Statement of Claim, and may not award any other relief that was not requested in the Statement of Claim.

(7) If the Respondent files an Answer after the Director has notified the parties that the claim will proceed under default procedures but before an award has been rendered, the proceedings under this paragraph shall be terminated and the case will proceed under the regular procedures.

* * *

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 Dispute Resolution 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 Dispute Resolution 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

(a) Purpose

NASD Dispute Resolution proposes to provide default procedures for situations in which a suspended, terminated or otherwise defunct member or associated person fails to answer or participate in an arbitration proceeding, and the claimant nevertheless elects to pursue arbitration. The procedures are designed to make it easier for claimants to obtain an award against a defunct party, which award can then be enforced in court.

The United States General Accounting Office (GAO) issued a report in June 2000 expressing concern over the number of unpaid arbitration awards issued in connection with arbitration proceedings in the securities industry arbitration forums, and making several recommendations for improvements.³ The GAO Report observed that most of the unpaid awards resulted from broker/dealers that were no longer in business.⁴ In a May 25, 2000, letter to the GAO,⁵ the NASD committed to undertake several initiatives to address the issue of unpaid awards. The proposed rule change will complete NASD Dispute Resolution's implementation of all initiatives.

The GAO initiatives are listed below with a description as to the actions already taken. The last item is the proposed rule change.

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Request in the award service letter that claimants notify NASD Dispute Resolution if the award has not been paid within an established number of days of service.

Notice to Members 00-55 also invites claimants to inform NASD Dispute Resolution if their awards against members or associated persons have not been paid, so that the non-summary suspension process can be commenced. The second letter implemented September 18, 2000 is sent to all parties with service of their award. It restates the requirement to pay awards within 30 days of service, and requests parties who have prevailed against a member or associated person to inform NASD Dispute Resolution if their award has not been paid.

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The Boards of NASD Dispute Resolution and the NASD approved this proposal at their meetings on December 6 and 7, 2000. The SEC approved the rule change on April 6, 2001.⁷ Notice to Members 01-29, announcing the SEC's approval, was published on May 10, 2001, and the rule change was effective for all claims served on or after June 11, 2001.

Advise claimants in writing of the status of a firm or associated person (e.g., terminated, out of business, bankrupt) so they can evaluate whether to continue with arbitration.

This procedure was implemented on June 11, 2001, in connection with the previous item.

Propose to the NASD Board and to the SEC a rule amendment to provide streamlined default proceedings where the terminated or defunct member or associated person does not answer or appear, but the claimant affirmatively elects to pursue arbitration.

This is the present proposed rule change. It would provide an expedited default procedure for certain cases in which a respondent is an associated person whose registration is terminated, revoked, or suspended; a member whose membership has been terminated, suspended, canceled, or revoked; a member that has been expelled from the NASD; or a member that is otherwise defunct (collectively referred to in this rule filing as "defunct"). If a defunct respondent fails to answer the claim in a timely manner, the claimant may elect to proceed under optional default procedures as to that respondent. If there are several

competent jurisdiction and such motion has not been denied by that court, that there is a pending bankruptcy petition, or that the award has been discharged in bankruptcy.

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claimants, all must agree to use default procedures. The default procedures may be used against one or more defunct respondents while the rest of the initial arbitration proceeds against any remaining respondents.⁸

If the claimant opts to use default procedures, the case will proceed with a single arbitrator without a hearing. Under the default procedures, the arbitrator will make an award based upon the Statement of Claim and any other material submitted by the claimant. The arbitrator may request additional information from the claimant before rendering an award. In keeping with the streamlined nature of the procedures, neither the claimant nor the single arbitrator will have the option to ask that two additional arbitrators be appointed to decide the case (as is sometimes done in other single-arbitrator cases).

The procedures have several provisions to safeguard the integrity of the process and discourage abuses:

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- The arbitrator may not award damages in an amount greater than the damages requested in the Statement of Claim, and may not award any other relief that was not requested in the Statement of Claim.

⁸ If a case is to be bifurcated and handled under two different procedures, regular and default, each proceeding will be assigned a separate case number to avoid confusion. Proposed Rule 10314(e) provides that the default award will have no effect on any non-defaulting party.

The proposed rule provides, however, that the default award will have no effect on the non-defaulting parties. The proposed rule would apply to all types of claimants, whether they are customers, associated persons, or member firm claimants, that are bringing a claim against a suspended or terminated member or associated person. In line with the GAO's recommendations, the proposal is designed to make it easier to obtain an award against any defunct member or associated person.

Finally, if a respondent thought to be defunct belatedly files an answer or otherwise begins to participate after the staff has notified the parties that the claim will proceed under default procedures but before an award has been rendered, the default procedures will be suspended, and the case will proceed under the regular procedures.

(a) Statutory Basis

NASD Dispute Resolution 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 Dispute Resolution believes that the proposed rule change will protect investors and the public interest by making it faster and less expensive for investors and other claimants to obtain awards against defunct members and associated persons, which awards can then be enforced in court and through the NASD suspension process, while containing several provisions to safeguard the integrity of the process and discourage abuses.

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

NASD Dispute Resolution 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