# NASD and NYSE Investigations from Start to "Wells" Type Notices: Working with Regulators in Your Client's Best Interest

**Susan Light**
**NYSE Division of Enforcement**

**Bill Singer**
**Gusrae, Kaplan, Bruno & Nussbaum PLLC**

**Michael Solomon**
**UBS Financial Services, Inc.**

**Ben Indek**
**Morgan, Lewis & Bockius LLP**
**(Moderator)**

**American Conference Institute**
**Broker / Dealer Enforcement Actions**
**New York, NY**
**October 25, 2005**

## I. INTRODUCTION[1/]

Over the last several years, the enforcement staffs of the NASD and NYSE have commenced numerous investigations into the activities and conduct of broker/dealers and their employees. In this unprecedented environment, it is critical for counsel to understand the SRO investigative processes and procedures to effectively represent firms and individuals in these high-stakes matters. This outline reviews the following important aspects of SRO investigations: (i) document requests and responses; (ii) witness preparation; (iii) cooperation with regulators; (iv) Fifth Amendment rights in SRO proceedings; and (v) considerations regarding litigating or settling an SRO matter.

## II. DOCUMENT REQUESTS AND RESPONSES

Regulators routinely request numerous categories of documents from broker/dealers during the course of investigations. The following are several practical considerations for counsel to keep in mind upon receiving and responding to document requests.

Upon receipt of the document request, counsel should attempt to ascertain what documents the Company has in its possession, what documents can be obtained for production and determine when such production can reasonably begin. At this stage, where appropriate, counsel should also confirm that procedures are in place so that responsive documents are neither altered nor destroyed.

Where counsel determines that it cannot reasonably obtain or produce documents called for by a regulator, the lawyer should consider developing a concrete counter-proposal for production and begin the process of discussing this issue with the enforcement staff. At this time, counsel and the staff should also negotiate any modifications to the request, including extensions of time where appropriate. Consideration should be given to memorializing any such modifications in writing.

As the document production process continues, it is critical for counsel to keep the enforcement staff apprised of the progress of such efforts.

## III. WITNESS PREPARATION

### A. COUNSEL'S REVIEW AND ORGANIZATION OF RELEVANT DOCUMENTS, INCLUDING:

1. Letter requesting testimony

2. Documents referring or relating to the witness which were produced in the case, non responsive key documents, and documents concerning the nature

---

[1/] Unless otherwise noted, this outline was drafted by Ben A. Indek of Morgan, Lewis & Bockius LLP. The views expressed are his own and do not necessarily constitute those of his firm, the other panelists or their companies or organizations.

and scope of the witness' duties (e.g., job descriptions organizational charts, etc.)

3. References to the witness in the prior testimony of other individuals involved in the case

4. Exhibits marked for identification at the testimony of others

5. Chronology or outline of facts and issues the witness is likely to be confronted with

**B. DISCUSS WITNESS WITH COMPANY PERSONNEL**

1. Discuss the activities, responsibilities and character of the witness with others in the Company who are familiar with the witness

2. Obtain and review prior disciplinary proceedings, complaints or lawsuits and transcripts of testimony. Search data bases of other depositions and documents that refer to witness

**C. ASCERTAIN SCOPE OF TESTIMONY**

1. Attempt to ascertain the anticipated scope of the testimony

   a. Gather intelligence from counsel for other witnesses if that can be done without compromising confidentiality

   b. Elicit information from SRO counsel, if possible, about the areas to be covered. An informed witness can be an informative witness, assuming its in the client's interest to shed light on events in question.

**D. CONSIDER PREPARING AN OUTLINE OF COUNSEL'S OWN EXAMINATION**

1. Consider the pros and cons of this exercise

**E. CONSIDER DOING A MEMO TO THE FILES ABOUT THE INTERVIEW**

1. Consider the pros and cons of this exercise

**F. THE PREPARATION SESSION: BACKGROUND INFORMATION AND REVIEWING THE FACTS**

1. Ensure that the witness is comfortable

   a. Two of counsel's most important responsibilities are to put the witness at ease and make him/her feel confident

b. This is purely a matter of style and personality; counsel should do what is natural and attempt to "connect" with the witness

2. Explain the nature of the case

   a. Describe the background, nature and scope of the case

   b. Explain the role of the witness in the case and identify, as appropriate, others who have testified or will testify

   c. Outline, in general terms, the possible ramifications of the case

3. Review the role of counsel

   a. Explain and review counsel's role in the case

   b. Confirm that the witness understands the attorney-client relationship and the nature and scope of the representation, including:

      (i) The right to counsel

      (ii) Responsibility of witness to be open and forthcoming with counsel

      (iii) Possibility of conflicts arising – joint representations issues

      (iv) Attorney-client privilege

      (v) Use of information learned from witness by management

4. Ascertain personal, educational and employment background

   a. It is critical for counsel to ascertain a complete understanding of the personal, educational and employment background of the witness

   b. Particular attention should be paid to prior terminations and civil or criminal actions

      (i) Develop a strategy for answering these types of questions where the witness will be required to provide "yes" answers

      (ii) Explain importance of managing embarrassing information

5. Review and develop the facts of the case

   a. Review the witness' understanding of the facts

(i) A chronological progression of the facts is often most useful and efficient

(ii) References to the relevant documents, testimony (by verbally apprising the witness of other testimony) and exhibits should be made[2]

(a) This must be done on a case by case basis; as a general rule, a witness with a limited role in a situation should not be provided with a lot of detail

(b) Counsel must also determine how and when to refresh the witness' recollection

b. Assume that the witness' recollection is not influenced by counsel's assessment of the facts or that of other potential witnesses

c. Determine whether the witness is uncomfortable about any aspect of his/her testimony or is concerned with any issues that have arisen during the review of the facts

d. Keep an open mind and pay attention to what the witness is trying to say, especially if it appears discomforting to the witness. Be attuned to body language. Look at the witness and assess how his/her demeanor will affect the testimony. Consider a videotape practice session.

e. Ascertain if the witness has any additional documents or information that may be relevant to the matters

(i) Counsel may discover that additional materials or information is available by simply prodding the witness from time to time during the preparation session

(a) Diaries, calendars, logs, missing or forgotten files often spring to a witness' mind with gentle prodding

f. Do not be formalistic in asking questions; counsel may miss information because he/she and the witness are not speaking the same language

---

[2] Counsel must keep in mind that time enforcement staff may ask the witness about the documents he/she reviewed in preparation for testimony. Counsel should deflect such an inquiry by asserting the protections afforded by the attorney work product doctrine and attorney-client privilege.

g. Decide on overall strategy for the testimony and discuss it with the witness. Adapt to the strengths and weaknesses of the witness as well as his or her posture in the case. What does he/she stand to gain or lose, i.e., to what extent is there exposure and how can this witness best handle the testimony

h. Counsel and the witness may find it helpful if counsel jotted down a short list of the key facts or themes they decide the witness should try to hit during the testimony

(i) Counsel could refer to this list at breaks or before taking the opportunity to ask clarifying questions at the end of the testimony

## G. PRIVILEGE ISSUES

1. Evaluate whether the testimony is likely to evoke answers that could be privileged and discuss with the witness how to approach

a. Attorney-Client Privilege

b. Spousal Privilege

c. Confessor-Penitent Privilege

d. Self-Critical Analysis

2. Do follow-up research to ensure an understanding of the scope of privilege, its application, the ramifications of waiver and impact that assertions may have on case, witness' employment status, etc. Explain issues carefully to the witness.

## H. THE PREPARATION SESSION: RULES OF TESTIFYING

Once counsel has completed the substantive portion of the preparation session, he/she should turn to perhaps the most important part – the rules of the road.

1. Describe length and setting of the testimony

a. Provide the witness with an estimate of the length of the testimony

b. Paint a mental picture of the testimony room for the witness

c. Inform the witness that he/she should not bring any items to the testimony (including files, notepads or papers)

2. List attendees at the testimony

a. Counsel that will be present

(i) This often provides counsel with a good opportunity to describe tendencies of the counsel involved

b. Court stenographer

(i) Inform the witness that a court stenographer will be present so that an accurate record of the testimony is made and a transcript produced

c. Other attendees

3. Caution the witness not to discuss the facts of the investigation with anyone other than counsel

a. Witnesses who do so run the risk of having to testify about those conversations

4. Discuss with the witness any searches he or she has undertaken to comply with regulatory requests for documents and prepare the witness to be able to describe such efforts

5. Rules of the road for testifying

a. The witness must tell the truth

b. Listen to the question carefully

c. The witness should wait until the examiner has completed his/her entire question before answering

(i) Keeps the record clean

(ii) Avoids answering the wrong question

d. Think about the answer before actually answering

e. Answer the specific question asked

f. Upon completion of the answer by the witness, the examiner may wait a second or two before posing the next question; the witness should not try to fill up the silence

g. The witness must not attempt to answer a question he/she does not understand

h. The witness should not guess

(i) Speculation is inappropriate; if the witness does not know the answer to a question, he/she should simply say so

i. The witness has the right to speak to counsel

(i) The witness should ask to speak to counsel and then discuss any concerns with counsel either outside the testimony room or in a whispered conversation

j. The witness should carefully review an exhibit handed to him/her by the examiner

k. The witness has the right to take a break during the testimony

(i) The witness should ask the staff for a break when needed

## I. THE PREPARATION SESSION: CONCLUSION

a. Ask the witness if he/she has any remaining questions or concerns

(i) confirm that he/she is comfortable and ready to go forward

b. Set up a time and place to meet prior to the beginning of the testimony

(i) Because schedules change (due to business or personal problems) it may be advisable for counsel and the witness to exchange home and cell numbers in the case of an emergency

## J. AFTERMATH

a. At the conclusion of the testimony, but before leaving, evaluate whether any material corrections should be made so that the record accurately reflects the witness' best recollection as counsel understood it going in

b. Consider whether additional information (by affidavit or otherwise) should be submitted after the fact. Counsel should keep in mind the difference between depositions and investigative testimony.

c. Review the transcript carefully and ask the witness to do the same. Transcription errors and other mistakes should be corrected promptly.

d. Develop a strategy to follow-up if it is in the best interest of the witness to do so.

## IV. COOPERATION WITH REGULATORS[3]

Cooperation, or the lack thereof, in regulatory investigations has been the subject of heightened interest.[4] In remarks in April 2004, Stephen Cutler, then Director of the SEC's Division of Enforcement said

> If, for example, an entity -- whether public company, accounting firm, or regulated entity -- or its counsel is recalcitrant during an investigation, misleads the staff, or fails unreasonably to comply with Commission processes, the staff is very likely to seek a penalty in settlement. The penalty is likely to be particularly substantial if the violator's underlying conduct has also resulted in significant investor harm.
>
> As you would expect, the provision of extraordinary cooperation, on the other hand, including self reporting a violation, being forthcoming during the investigation, and implementing appropriate remedial measures (including, in the case of an entity, appropriate disciplinary action against culpable individuals), can contribute significantly to a conclusion by the staff that a penalty recommendation should be more moderate in size or reduced to zero.[5]

To provide some background, in October 2001, the SEC issued a Section 21(a) report (commonly referred to as the "Seaboard Report") that articulated a broad framework for evaluating a company's cooperation and determining whether and how to charge violations of the federal securities laws.[6] The Seaboard Report established certain criteria that the Commission indicated it would consider in determining "whether, and how much, to credit self-policing, self-reporting, remediation and cooperation – from the extraordinary step of taking no enforcement action to bringing reduced charges, seeking lighter sanctions, or including

---

[3] This section was drafted in connection with the 2004 SIA Compliance & Legal Division Regional Seminar in Washington, D.C. Mr. Indek is grateful for the input provided by his co-panelists (Susan Merrill, James Shorris and Linda Chatman Thomsen) who participated on the SEC and S.R.O. Enforcement Priorities panel.

[4] See Phyllis Diamond, SEC Demand for 'Cooperation' Seen Raising Due Process Concerns, BNA Securities Law Daily (June 14, 2004).

[5] Stephen M. Cutler, Remarks to 24th Annual Ray Garrett Jr. Corporate & Securities Law Institute (April 29, 2004) <http://www.sec.gov/news/speech/spch042904smc.htm>.

[6] See Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Release No. 34-44969 (October 23, 2001) <http://www.sec.gov/litigation/ investreport/34-44969.htm>.

mitigating language in documents [used] to announce and resolve enforcement actions."[7] Those criteria were set forth in the Seaboard Report as follows:

> 1. What is the nature of the misconduct involved? Did it result from inadvertence, honest mistake, simple negligence, reckless or deliberate indifference to indicia of wrongful conduct, willful misconduct or unadorned venality? Were the company's auditors misled?
>
> 2. How did the misconduct arise? Is it the result of pressure placed on employees to achieve specific results, or a tone of lawlessness set by those in control of the company? What compliance procedures were in place to prevent the misconduct now uncovered? Why did those procedures fail to stop or inhibit the wrongful conduct?
>
> 3. Where in the organization did the misconduct occur? How high up in the chain of command was knowledge of, or participation in, the misconduct? Did senior personnel participate in, or turn a blind eye toward, obvious indicia of misconduct? How systemic was the behavior? Is it symptomatic of the way the entity does business, or was it isolated?
>
> 4. How long did the misconduct last? Was it a one-quarter, or one-time, event, or did it last several years? In the case of a public company, did the misconduct occur before the company went public? Did it facilitate the company's ability to go public?
>
> 5. How much harm has the misconduct inflicted upon investors and other corporate constituencies? Did the share price of the company's stock drop significantly upon its discovery and disclosure?
>
> 6. How was the misconduct detected and who uncovered it?
>
> 7. How long after discovery of the misconduct did it take to implement an effective response?
>
> 8. What steps did the company take upon learning of the misconduct? Did the company immediately stop the misconduct? Are persons responsible for any misconduct still with the company? If so, are they still in the same positions? Did the company promptly, completely and effectively disclose the existence of the misconduct to the public, to regulators and to self-

---

[7] Id.

regulators? Did the company cooperate completely with appropriate regulatory and law enforcement bodies? Did the company identify what additional related misconduct is likely to have occurred? Did the company take steps to identify the extent of damage to investors and other corporate constituencies? Did the company appropriately recompense those adversely affected by the conduct?

9. What processes did the company follow to resolve many of these issues and ferret out necessary information? Were the Audit Committee and the Board of Directors fully informed? If so, when?

10. Did the company commit to learn the truth, fully and expeditiously? Did it do a thorough review of the nature, extent, origins and consequences of the conduct and related behavior? Did management, the Board or committees consisting solely of outside directors oversee the review? Did company employees or outside persons perform the review? If outside persons, had they done other work for the company? Where the review was conducted by outside counsel, had management previously engaged such counsel? Were scope limitations placed on the review? If so, what were they?

11. Did the company promptly make available to our staff the results of its review and provide sufficient documentation reflecting its response to the situation? Did the company identify possible violative conduct and evidence with sufficient precision to facilitate prompt enforcement actions against those who violated the law? Did the company produce a thorough and probing written report detailing the findings of its review? Did the company voluntarily disclose information our staff did not directly request and otherwise might not have uncovered? Did the company ask its employees to cooperate with our staff and make all reasonable efforts to secure such cooperation?

12. What assurances are there that the conduct is unlikely to recur? Did the company adopt and ensure enforcement of new and more effective internal controls and procedures designed to prevent a recurrence of the misconduct? Did the company provide our staff with sufficient information for it to evaluate the company's measures to correct the situation and ensure that the conduct does not recur?

13. Is the company the same company in which the misconduct

> occurred, or has it changed through a merger or bankruptcy reorganization?[8]

The NASD Sanction Guidelines also highlight the importance of cooperation. One of the factors set forth in the Principal Considerations In Determining Sanctions states that Adjudicators should consider:

> Whether the respondent provided substantial assistance to NASD Regulation in its examination and/or investigation of the underlying misconduct, or whether the respondent attempted to delay NASD Regulation's investigation, to conceal information from NASD Regulation, or to provide inaccurate or misleading testimony or documentary information to NASD Regulation.[9]

The NYSE has not published similar sanction guidelines or the equivalent to the Seaboard Report, but it has on a number of occasions included language in settlements indicating that cooperation is taken into account in resolving matters. In the last several months, senior officials of the NYSE's Division of Enforcement have also publicly described the factors that the staff takes into account in considering the sanctions that it may seek in connection with resolving its investigations. The first factor identified by the staff was "credit for cooperation."

## V. FIFTH AMENDMENT RIGHTS IN SRO PROCEEDINGS

The NYSE and NASD apparently do not permit individuals to invoke their Fifth Amendment right against self-incrimination in connection with regulatory investigations.

The most recent discussion of this increasingly important issue can be found in last year's NASD disciplinary case against Frank Quattrone. See In re Dep't of Enforcement v. Quattrone, NASD Disc. Proceeding No. CAF030008, 2004 WL 2692229 (N.A.S.D.R. November 22, 2004). In this case, the NASD's National Adjudicatory Council handed down an appellate decision affirming (and increasing) an administrative penalty against Frank Quattrone, former head of the Technology Group of CS First Boston. Quattrone had been asked for and had given testimony to the NASD staff in connection with investigations into "spinning" and analyst conflicts of interest. After receiving a Wells notice from the NASD staff, Quattrone was put on administrative leave by CSFB after the company announced that it was conducting an investigation into the circumstances surrounding an email he had sent regarding CSFB's document retention policy. A federal criminal investigation into the matter was opened on the same day. That event prompted a fresh NASD request for testimony, which Quattrone first tried to delay but ultimately declined, asserting his Fifth Amendment privilege. NASD commenced a case seeking to bar Quattrone for non-cooperation, leading to a decision that suspended him for one year subject to a potential bar from the industry if he continued to fail to cooperate. Subsequent to his criminal conviction relating to the email, Quattrone gave the NASD the

---

[8] Id. (footnote omitted from item number 11).

[9] NASD Sentencing Guidelines, Principal Consideration No. 12.

testimony requested. Nevertheless, on appeal of the suspension, the NAC affirmed the hearing panel decision and stiffened the penalty to a lifetime bar. Quattrone has appealed this decision as to the SEC.

## VI. DECIDING WHETHER TO SETTLE OR LITIGATE[10]

In deciding whether to settle or litigate and enforcement action with an SRO, the following issues must be considered:

### A. PUBLICITY

Complaints issued by the NASD are publicized – often through a press release. In contrast, the NYSE does not generally make any public statement about the initiation of litigated disciplinary actions. Consideration must be given to whether the respondent can endure the negative publicity surrounding the issuance of an NASD complaint and the collateral affects on a firm's or an individual's ongoing business activities. In addition, litigation might involve two waves of publicity (upon the filing of a complaint and at the conclusion of a case) as opposed to a settlement, which generally is covered in the media only at the resolution of the matter.

### B. REGULATORY FILINGS

Upon the issuance of complaints, firms and individuals are required to disclose the nature of the disciplinary action through the CRD system. The filing of forms disclosing regulatory complaints must be considered when deciding whether to litigate or settle.

### C. REPUTATIONAL RISKS

Publicity and/or regulatory filings can adversely affect a firm's or an individual's reputation and standing in the securities industry and the national or local community. The reputational risks associated with litigating disciplinary actions must be carefully weighed. Of course, firms and individuals may wish to vindicate their position through litigation rather than settle on unfavorable or inaccurate terms.

### D. COLLATERAL CONSEQUENCES

Respondents must consider the collateral consequences of a litigated decision. These consequences include collateral estoppel in connection with private litigation or arbitration involving the same facts that can arise from fully litigating an SRO matter. In contrast, SRO settlements are resolved without admitting or denying the facts and are less likely to raise collateral estoppel issues in related litigation or arbitration.

---

[10] This section was drafted in connection with the 2005 SIA Compliance & Legal Division Annual Seminar. Mr. Indek received a substantial assistance and input on this section from his co-panelists (Daniel Taub, Suzanne Auletta, Daniel Kramer and Bob Lehman) who participated on the Litigating with S.R.O.s panel.

## E. REGULATORY RELATIONSHIPS

For firms, litigating with their SROs can lead to, at a minimum, a perception that the broker-dealer is not committed to cooperating with the regulatory process. Because firms will have to continue to work with and be examined by SROs on an ongoing basis, broker-dealers must consider the potential damage to regulatory relationships arising out of litigating with their regulators.

## F. SANCTIONS

Generally speaking, there is a perception within the industry that firms or individuals can settle with regulators on terms that may be more advantageous than the sanctions levied at the conclusion of a litigated case. Consideration to the types of charges, fines, undertakings and language available in a settlement must be weighed against those that can be obtained by an SRO in litigation.

## G. DISTRACTION

Firms and individuals can be distracted from their business activities while litigating with an SRO. The time, effort and disruption that can come with a protracted and contentious litigation must be considered before deciding to fight a disciplinary action.

## H. COSTS

Litigation (in any context) can be a costly endeavor. Legal fees and expert witness fees, to name two costs, can be significant and the money spent in litigating must be considered before deciding to do so.

## I. PROCEDURAL ISSUES AND DIFFERENCES

There are various materials available on the NASD and NYSE websites that describe the SRO disciplinary hearing process. These include:

1. NASD's Guide: Disciplinary Hearing Procedures.
2. NASD's Answers to Frequently Asked Questions for Respondents in ASD Disciplinary Proceedings.
3. NYSE's Hearing Board Procedures Outline

Some of the key procedural issues and differences between litigating with the two main SROs (the NASD and NYSE) can best be seen using the following chart.

| | NASD | NYSE |
|---|---|---|
| **Pleadings** | • Cases are initiated by the staff serving a Complaint. Complaints issued by the NASD are publicized. (NASD Rule 9211 and IM-8310-2)<br><br>• The Complaint must "specify in reasonable detail the conduct alleged to constitute the violative activity" and the rule(s) alleged to have been violated. Enforcement may amend a Complaint once as of right before submission of an Answer. (NASD Rule 9212)<br><br>• Answers must admit, deny or state that the Respondent does not have sufficient information to admit or deny, each allegation. Affirmative defenses must be included in the Answer. Answers may be amended with the permission of the Hearing Officer. (NASD Rule 9215) | • The staff commences an action by issuance of a Charges Memorandum. (NYSE 476(d)) There is no publicity for a Charge Memorandum.<br><br>• The Charge Memorandum must contain a statement of alleged facts and the charges being asserted. The charges should be set forth with "precision and clarity." (NYSE Hearing Board Outline)<br><br>• Answers must admit or deny the assertions of fact and charges and "shall also contain any specific facts in contradiction of the charges and any affirmative defenses." (NYSE Rule 476(d)) A general denial may be considered a failure to file an Answer. (NYSE Hearing Board Outline) |
| **Panel Composition** | • Three Hearing Panel members preside over most cases. Under NASD rules, Hearing Panels are led by an independent Hearing Officer, and also include two industry panelists. (NASD Rule 9231(b))<br><br>• In cases involving "market quality" matters, Hearing Panels may include one panelist who was or is on the Market Regulation Committee. (NASD Rules 9231(b) and (c) and 9232(b)) | • Generally, three Hearing Panel members decide a case; Hearing Panels are led by an independent Hearing Officer; two industry panelists also sit on the panel. (NYSE Rule 476(b))<br><br>• In cases involving members, member organizations, allied members or approved persons, at least one of the industry panelists, "to the extent reasonably possible," must be engaged in similar activities as the Respondent. (NYSE Rule 476(b)) |

| | NASD | NYSE |
|---|---|---|
| **Discovery** | • The Respondent is entitled to inspect and copy documents prepared or obtained by the NASD staff in connection with the investigation that led to the proceeding. (NASD Rule 9251)<br><br>• The Respondent may make a motion for the production of witness statements of individuals whom the staff has called, or is expected to call, to testify in the proceeding. To compel production, the Hearing Officer must find that the statement pertains to the witnesses' direct testimony. (NASD Rule 9253) | • Parties are encouraged to engage in "voluntary mutual discovery." (NYSE Hearing Board Outline) The Hearing Officer may require the staff to permit the Respondent to inspect and copy documents that are "material to the preparation of the defense or are intended for use" by the staff at the hearing. (NYSE Rule 476(c)) |
| | • The NASD may withhold certain documents, including privileged or work product materials, documents prepared by the staff that will not be offered into evidence or materials that may disclose staff procedures or the identity of a confidential source. (NASD Rule 9251(b)) | • The rules do not authorize discovery of various internal NYSE documents (including "reports, memoranda, or other internal Exchange documents prepared . . . in connection with the proceeding.") (NYSE Rule 476(c)) |
| | • The Respondent may request that the staff compel the production of documents or testimony at the hearing from persons over whom the NASD has jurisdiction. (NASD Rule 9252) | • Upon request, the Hearing Officer may direct the appearance or testimony of an individual subject to the NYSE's jurisdiction. (NYSE Hearing Board Outline) |

| | NASD | NYSE |
|---|---|---|
| **Motions** | • The Respondent or the staff may make a motion for summary disposition prior to the hearing. After the hearing starts, the Respondent or staff must receive Hearing Officer leave to move for summary disposition. (NASD Rule 9264)<br>• A party may move to disqualify the Hearing Officer or a Hearing Panelist for conflict of interest, bias or where circumstances exist that call into question the fairness of a Hearing Panel member. (NASD Rules 9233 and 9234)<br>• The Respondent may make a motion for a more definite statement of specified matters of fact or law as described in the Complaint. (NASD Rule 9215(c))<br>• The Respondent may make a motion for an order limiting or prohibiting the disclosure of confidential information. The Hearing Officer must find that disclosure would have "a demonstrated adverse effect on the [moving party] or would involve an unreasonable breach of [such person's] privacy." (NASD Rule 9146(k)) | • While there is no specific provision for motions in the NYSE rules, the Hearing Officer is empowered to "resolve any and all procedural and evidentiary matters." (NYSE Rule 476(c)) In practice, motions on many issues can and are made by counsel. |

| | NASD | NYSE |
|---|---|---|
| **Hearing Process** | • The Respondent may request that a hearing be held; such requests must be granted. (NASD Rule 9221) | • Disciplinary proceedings are conducted at a hearing. (NYSE Rule 476(b)) Hearings are private; the public is ordinarily not permitted to attend. (NYSE Hearing Board Outline) |
| | • The case is presented by submission of relevant documents and witness testimony. (NASD Rule 9261) | • Both parties may present witnesses and other evidence. (NYSE Rule 476(b)) |
| | • Persons subject to NASD jurisdiction must testify under oath or affirmation. (NASD Rule 9262) Customers and others testifying are urged to do so under oath. (7/97 NASD letter to SEC) | • An oath or affirmation is administered for all witnesses. (NYSE Hearing Board Outline) |
| | • The formal rules of evidence do not apply in NASD disciplinary proceedings. (NASD Rule 9145) "The Hearing Officer shall receive relevant evidence and may exclude all evidence that is irrelevant, immaterial, unduly repetitious, or unduly prejudicial." (NASD Rule 9263) The NASD has indicated, however, that Hearing Officers "will refer to the law and precedent set forth in the circuit courts, SEC administrative decisions, and Association and other SRO proceedings regarding evidentiary matters, including the use of hearsay, telephone testimony, and videotaped testimony." (7/97 NASD letter to SEC) | • "The Hearing Panel is not bound by formal rules of evidence. The Hearing Officer decides the admissibility into evidence of testimony and documents." (NYSE Hearing Board Outline) |

| | NASD | NYSE |
|---|---|---|
| **Decisions/ Sanctions** | • NASD charges must be proven by a preponderance of the evidence.<br>• NASD Hearing Panels may impose one or more of the following sanctions: censure, fine, suspension, expel or cancel membership of a member or revoke or cancel a person's registration bar or "any other fitting sanction." (NASD Rule 8310)<br>• The NASD also has the authority to impose temporary and permanent cease and desist orders.<br>• NASD disciplinary actions are "unified" proceedings. There are no distinct liability and sanction phases.<br>• Hearing Panels refer to the NASD Sanction Guidelines in determining the kinds and levels of sanctions. | • The staff must prove its charge by a preponderance of the evidence.<br>• NYSE rules permit a Hearing Panel to impose one or more of the following sanctions: expulsion, suspension, limitation on activities, functions and operations (including suspension cancellation, registration or assignment of a stock), fine, suspension or bar from association with a member firm, or "any other fitting sanction." (NYSE Rule 476(a))<br>• The NYSE does not have cease and desist power.<br>• The NYSE uses a "bifurcated" process. There is a liability phase, and if the Respondent is found guilty of a charge, a sanction phase is subsequently held.<br>• Cases are the most relevant precedent for Hearing Panels. |

| | NASD | NYSE |
|---|---|---|
| **Appeals and Reviews** | • There are three levels of appeal in NASD disciplinary actions: NAC, SEC and US Court of Appeals. (NASD Rule 9300 Series)<br><br>• Under new rules, enforcement staff may appeal. (NASD Rule 9311)<br><br>• An appeal to the NAC stays sanctions except bars and expulsions. (NASD Rule 9370)<br><br>• The NAC may call a decision for review. (NASD Rule 9312) | • The Respondent may appeal to the NYSE's Board of Directors or Board of Executives, SEC and US Court of Appeals. (NYSE Rule 476(f))<br><br>• The NSYE enforcement staff may appeal a decision to the Board of Directors or Board of Executives. (NYSE Rule 476(f))<br><br>• In most cases where an appeal is made, any penalty imposed is stayed. (NYSE Rule 476(e))<br><br>• Any member of the Board of Directors or Board of Executives of the NYSE may require a review of any decision. (NYSE Rule 476(f)) |