SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54320; File No. SR-NYSE-2005-18)

August 15, 2006

Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Approving Proposed Rule Change and Amendments No. 1 and 2 Thereto Regarding NYSE Rule 619 to Clarify That Failure to Appear or Produce Documents in Arbitration May Be Deemed Conduct Inconsistent with Just and Equitable Principles of Trade

## I. Introduction

On February 17, 2005, the New York Stock Exchange, Inc. ("NYSE" or the "Exchange") filed with the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] a proposed rule change to amend Rule 619 to clarify that it may be deemed conduct or proceeding inconsistent with just and equitable principles of trade for purposes of NYSE Rule 476(a)(6) for a member, member organization, allied member, approved person, registered or non-registered employee of a member or member organization or person otherwise subject to the jurisdiction of the Exchange (each, a "responsible party") to fail to appear or fail to produce any document in its possession or control as directed pursuant to applicable provisions of the NYSE Arbitration Rules. On July 27, 2005, the Exchange filed Amendment No. 1 to the proposed rule change.[3] On February 15, 2006, the Exchange filed Amendment No. 2 to

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 In Amendment No. 1, which replaced the original filing, the Exchange clarified that Rule 619 also applies to a "person otherwise subject to the jurisdiction of the Exchange."

the proposed rule change.[4] The proposed rule change was published for comment in the Federal Register on April 11, 2006.[5] The Commission received five comment letters on the proposal.[6] This order approves the proposed rule change as amended.

## II. Description of the Proposal

NYSE Rule 476 allows disciplinary sanctions to be imposed upon a responsible party who is adjudged guilty of certain enumerated offenses, including "conduct or proceeding inconsistent with just and equitable principles of trade." The proposal would amend Rule 619 to clarify that it may be deemed conduct or proceeding inconsistent with just and equitable principles of trade for purposes of NYSE Rule 476(a)(6) for a responsible party to fail to appear or fail to produce any document in its possession or control as directed pursuant to provisions of the NYSE Arbitration Rules.

The Exchange is aware of allegations that member organizations have not fulfilled their discovery obligations as prescribed by NYSE Arbitration Rules. The NYSE believes that the express authority for the NYSE to bring a disciplinary action under NYSE Rule 476(a)(6) will improve the efficacy of the arbitration process by

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[4] Amendment No. 2, which replaced the first amended rule filing, conformed the proposed rule to reflect the list of persons subject to disciplinary action under NYSE Rule 476.

[5] See Exchange Act Release No. 53599 (Apr. 4, 2006), 71 FR 18401 (Apr. 11, 2006).

[6] See email from David Plimpton, Plimpton & Esposito, to rule-comments@sec.gov, dated April 27, 2006 ("Plimpton"); letter from Robert S. Banks, Jr., Public Investors Arbitration Bar Association, dated April 25, 2006 ("PIABA"); email from A. Daniel Woska, A. Daniel Woska & Associates, PC, to rule-comments@sec.gov, dated April 23, 2006 ("Woska"); email from Les Greenberg, Law Offices of Les Greenberg, to rule-comments@sec.gov, dated April 20, 2006 ("Greenberg"); letter from Steven B. Caruso, Maddox Hargett Caruso, P.C., dated April 11, 2006 ("Caruso").

facilitating the Exchange's ability to ensure more fully and forcefully the cooperation of a responsible party who is a party to an arbitration proceeding. By explicitly providing that the failure to appear or to produce documents in one's possession or control may be deemed conduct or proceeding inconsistent with just and equitable principles of trade, the NYSE believes that the proposed amendment would provide the Exchange with a clear mechanism to pursue disciplinary action pursuant to NYSE Rule 476 in response to such conduct.

## III. Summary of Comments

The Commission received five comment letters on the proposal.[7] Commenters generally supported the proposal.[8] As discussed below, however, some raised concerns with certain aspects of it.

Proposed Rule 619(h) states in relevant part that "[i]t may be deemed conduct or proceeding inconsistent with just and equitable principles of trade for purposes of Rule 476(a)(6) [for a responsible party] to fail to appear or to produce any document in their possession or control *as directed pursuant to provisions of the NYSE Arbitration Rules."* (Emphasis added.) One commenter stated that the emphasized language could be misconstrued to require the prior direction or an order of an arbitration panel before the NYSE could charge the party with a violation of Rule 476.[9] The commenter also suggested that the proposed rule be amended to clarify that it does not affect an

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[7] See id.

[8] For example, one commenter supported the proposed rule because, in the commenter's view, members that violate discovery rules do not regard their conduct as serious unless sanctions are imposed. PIABA. See also Woska.

[9] See Caruso.

arbitrator's current authority under Rules 604 (dismissal of proceedings) and 621 (enforcement of rulings).[10]

Two commentators believed that the proposed rule does not adequately address what the commenters' view are ongoing problems with arbitrator conflicts of interest.[11] One of these commenters stated that a securities arbitrator may be reluctant to impose sanctions on a party for fear that the party may not select the arbitrator to serve on future NYSE arbitration panels.[12]

## IV. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change, as amended, is consistent with the Act and, in particular, with Section 6(b)(5) of the Act, which requires, among other things, that the NYSE's rules 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.[13] The Commission also finds that the proposal is consistent with Section 6(b)(6) [14] of the Act, which

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[10] Id. Two commentators stated that arbitrators need to better enforce existing procedures, particularly Rule 604(b), which allows an arbitrator to impose sanctions against a party that willfully and intentionally fails to comply with an arbitrator's order if lesser sanctions have proven ineffective. Greenberg and PIABA.

[11] See Greenberg (stating that monetary sanctions on attorneys might be a more effective deterrent) and Plimpton (questioning whether NYSE arbitrators are independent enough to take action to curb discovery abuse).

[12] See Greenberg. To address concerns about arbitrator reluctance to sanction a party, the commenter suggested that the proposal require arbitrators to refer all contested discovery orders to NYSE.

[13] 15 U.S.C. 78f(b)(5).

[14] 15 U.S.C. 78f(b)(6).

requires, among other things, that the rules of an exchange provide that members and persons associated with its members be appropriately disciplined for violating the Act, the rules or regulations under the Act, or the rules of the exchange.

In particular, the Commission believes that by expressly authorizing the NYSE to bring an action against a member under Rule 476 for failing to appear or to produce any document in its possession or control in an arbitration proceeding, the proposal will enable NYSE to appropriately discipline such members. Moreover, the Commission believes the proposed rule could reduce discovery abuses by alerting parties to the importance of complying with NYSE Rule 619.

One commenter stated that the proposal could be misconstrued to require an order of an arbitration panel before NYSE could charge a party with violating Rule 476.[15] NYSE staff confirms that the proposed rule does not require an arbitration panel to issue an order before the NYSE could bring an action under Rule 476. Indeed, the proposal does not require any action from the arbitration panel before the NYSE may bring such an action. Moreover, the proposal authorizes the NYSE to bring an action under Rule 476 against a party during an arbitration proceeding if the NYSE believes such action is warranted.[16]

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[15] Caruso.

[16] Telephone conversation between Karen Kupersmith, Director of Arbitration, NYSE, and Richard Strasser, Attorney Fellow, SEC (Aug. 1, 2006). The commenter also suggested that the proposed rule be amended to clarify that it does not affect the power of an arbitrator to impose sanctions under Rules 604 (dismissal of proceedings) and 621 (enforcement of rulings). In the telephone call referenced above, NYSE staff stated that nothing in the proposal is intended to affect arbitrators' current authority under existing NYSE arbitration rules.

Some commenters raised broader concerns about arbitrator conflicts of interest and the need for arbitrators to better enforce existing arbitration procedures.[17] The Commission believes these comments are beyond the scope of the current proposal.

## VI. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act[18] that the proposed rule change (SR-NYSE-2005-18), as amended, be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[19]

Nancy M. Morris
Secretary

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17 See, e.g., Greenberg and Plimpton.

18 15 U.S.C. 78s(b)(2).

19 17 CFR 200.30-3(a)(12).