

NASD OFFICE OF HEARING OFFICERS

DEPARTMENT OF ENFORCEMENT,

Complainant,

v.

Respondent.

Disciplinary Proceeding No.
2005001449202

Hearing Officer—Andrew H. Perkins

INTERIM SCHEDULING AND CASE MANAGEMENT ORDER

The Hearing Officer held a Pre-Hearing Conference (“Conference”) in this proceeding on May 8, 2007, to: (1) refine the issues in dispute; (2) set the hearing format and schedule; and (3) institute procedural guidelines to expedite the hearing.

Having considered the comments and proposals of the parties submitted at the Conference, together with the comments and proposals the parties submitted following the first two conferences in this case, the Hearing Officer ORDERS:

1. Refinement of Issues

a) Intent to Violate Rules and Regulations

The Department does not allege, and does not intend to present evidence to show, that Respondent intended to violate any applicable rules or regulations, or that it intended to mislead or defraud arbitration claimants by not providing emails in response to discovery demands between October 2001 and March 2005. The Department contends that Respondent acted recklessly. Accordingly, the pleadings are deemed amended to reflect this clarification.

b) Affirmative Defenses

Respondent asserted 14 affirmative defenses in its Answer. The Department filed a motion to strike seven of the affirmative defenses on the grounds that they are legally and factually insufficient.¹ On April 30, 2007, the Hearing Officer issued an order that prohibited the parties from filing other dispositive motions until a comprehensive pre-hearing schedule could be set for the case. The Hearing Officer also granted Respondent an extension of time to respond to the Department's Motion to Strike Affirmative Defenses.

Based upon careful consideration of the Department's Motion to Strike Affirmative Defenses and Respondent's Answer, the Hearing Officer directed Respondent to file an Amended Answer that includes only those affirmative defenses that are warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law. By filing the Amended Answer with the Office of Hearing Officers, counsel is certifying that to the best of the person's knowledge, information, and belief, formed after an inquiry reasonable under the circumstances, the affirmative defenses are not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation; and the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation.²

¹ The Department requested that the First, Second, Third, Fourth, Fifth, Ninth, and Fourteenth affirmative defenses be stricken.

² *Cf.* Fed. R. Civ. P. 11.

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Respondent shall articulate with reasonable specificity the factual and legal bases for each alleged defense. "Reasonable detail" means a factual and legal description sufficient to allow the Department to understand the substance and basis of the defense and to address it at the hearing, or, if appropriate, in a motion for partial summary disposition. Affirmative defenses that do not meet this standard shall be stricken.

Respondent shall file its Amended Answer no later than May 22, 2007.

c) Discovery (Pre-Complaint Rule 8210 Requests for Information)

The Department served Respondent with a Request for Information on October 17, 2006 ("Rule 8210 Request"). In general terms, the Rule 8210 Request called for the production of four categories of documents:

1. All documents and/or communications from [Respondent] to its opposing parties relating to requests for e-mail communications, which requests were sent from September 30, 2001 through March 30, 2005.
2. All discovery requests for the production of e-mail in NASD arbitration proceedings brought by [Respondent] customers open as of or after September 11, 2001, and closed prior to April 30, 2005.
3. All e-mails in the New Repository which (1) were subject to a discovery demand or obligation as described in para. 2 above; (2) which constitute communication between the customer(s) whose accounts are the subject of any arbitration proceeding described in para. 2 above and any employee, registered representative, principal or agent of [Respondent]; or (3) involve the subject matter of any such arbitration.
4. All pre-June 7, 2002 e-mails that were provided to arbitration claimants or their counsel during the period of September 30, 2001 through April 30, 2005 in connection with any arbitration proceeding described in para. 2 above.³

On January 5, 2007 the Department modified the Rule 8210 Request by withdrawing item 3(3) and clarifying the scope of production required under item 3(1).

³ Identification of Outstanding Rule 8210 Request filed May 4, 2007.

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To date, the parties have identified between approximately 1200 and 1700 arbitrations in which claimants made discovery demands upon Respondent. Respondent is in the process of searching for the documents covered by the Rule 8210 Request, but both sides concede that it will be impossible to ever identify with certainty and recover all of the relevant emails. Each side also has indicated that the hearing schedule will be dependent on the completion of this search process unless the scope of the Rule 8210 Request is modified further.

The Department contends that the requested emails are relevant and material because they demonstrate the "scope" of the alleged violations from a quantitative perspective.

Based upon the parties' representations and the Department's proffer regarding its intended use of the subject emails, the Hearing Officer determined that the information requested pursuant to the Rule 8210 Request could best be quantified through stipulations. Accordingly, the Hearing Officer ORDERS the parties to meet and confer no later than May 29, 2007, in an effort to resolve the outstanding issues pertaining to the Rule 8210 Request. The parties shall thereafter promptly report their progress to the Hearing Officer. If the parties are unable to agree to appropriate stipulations and a plan to resolve all of the outstanding issues presented by the Rule 8210 Request, the Hearing Officer will schedule a pre-hearing conference to review the outstanding issues.

Given the uncertain nature of some of the subject facts, the parties are encouraged to consider admissions not only of facts of which each party has personal knowledge, but also of those that can be established from facts known by others. Facts of the latter type can be shown as "uncontested," "uncontroverted," or "conceded" rather than admitted.

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By stipulating that certain facts are uncontroverted, the parties are not conceding the facts admissibility or weight. The parties retain the right to object to the relevance of an uncontroverted fact or to contest its probative value.

2. Hearing Format and Schedule

After careful consideration of the parties' Joint Submission Regarding Scheduling Order, the Hearing Officer ORDERS that the hearing will be conducted in three stages:

a) Information Technology Issues (Stage 1)

During Stage 1, the parties will offer evidence and argument related to Respondent's pre- and post-September 11, 2001, email systems (including archive and backup systems); how the events of September 11, 2001, affected those systems; how Respondent's information technology staff responded to the events of September 11, 2001 (including the restoration of Respondent's email systems); and related technology issues. Stage 1 is set for the week of October 15, 2007.

b) Liability Issues (Stage 2)

During Stage 2, the parties will offer evidence and argument related to the violations alleged in the Complaint and Respondent's defenses, including Respondent's policies and practices with respect to the disclosure of email to regulators and arbitration claimants; the nature of Respondent's understanding regarding the preservation of pre-September 11, 2001 emails; Respondent's policies and practices regarding record keeping; Respondent's supervisory policies, procedures, and systems regarding emails; and related issues. Stage 2 is set for the week of October 29, 2007.

c) Sanction Issues (Stage 3)

During Stage 3, the parties will offer evidence and argument related to the impact Respondent's handling of pre-September 11, 2001 email had on arbitration claimants and

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regulators; and related factors that impact the appropriate sanctions if any violations are found. Stage 3 is set for the weeks of December 3 and 10, 2007.⁴

3. Procedural Issues

a) Motions to Amend the Pleadings

Motions to amend or supplement the pleadings shall be filed no later than June 1, 2007.

b) Motions for Summary Disposition

No motions for summary disposition shall be filed without prior leave of the Hearing Officer.

c) Expert Witnesses

The parties shall obtain leave to call an expert witness to testify at the hearing. Motions for leave to call an expert witness shall identify the nature of the expert's proposed testimony in sufficient detail to enable the Hearing Officer to determine whether the testimony will be necessary and appropriate.

Andrew H. Perkins
Hearing Officer

Dated: May 9, 2007

⁴ Stage 2 and 3 could be consolidated if the parties resolve the outstanding issues related to the Rule 8210 Request.