



February 6, 2018

The Honorable Richard W. Sears, Jr.
Chair, Senate Judiciary Committee
115 State Street
Montpelier, VT 05633-5501

RE: Senate Bill 105 – Arbitration

Dear Chair Sears and Members of the Senate Judiciary Committee:

The Financial Industry Regulatory Authority (“FINRA”) appreciates the opportunity to comment on S.105 which seeks to limit arbitration clauses in contracts and establishes data collection and disclosure requirements regarding arbitrations. The bill is pending before the Senate Judiciary Committee.

FINRA respectfully requests an exemption from the provisions for arbitrations conducted through the forum that FINRA operates. As detailed below, the FINRA Customer and Industry Codes of Arbitration Procedures (FINRA Codes) have important safeguards that protect investors, thereby distinguishing the FINRA forum from other arbitration forums. Legislatures in other states—including Arizona, California, District of Columbia, Maryland, Nevada and West Virginia—have exempted FINRA from bills that conflict with the FINRA Codes.

Background

FINRA is dedicated to investor protection and market integrity. It regulates one critical part of the securities industry—brokerage firms doing business with the public in the United States. FINRA, overseen by the Securities and Exchange Commission (SEC), writes rules, examines for and enforces compliance with FINRA rules and federal securities laws, registers broker-dealer personnel and offers them education and training, and informs the investing public. In addition, FINRA provides surveillance and other regulatory services for equities and options markets, as well as trade reporting and other industry utilities. FINRA also administers a dispute resolution forum for investors and brokerage firms and their registered employees. More specifically, FINRA administers more than 99% of securities-related arbitrations and mediations between and among investors, brokerage firms and individual brokers through its FINRA Codes, attached hereto: <https://www.finra.org/arbitration-and-mediation/code-arbitration-procedure>.

SEC oversight requires FINRA to file each rule, including those in its arbitration codes, with the SEC for approval. The SEC review process includes a public comment period and FINRA is required to respond to each comment submitted. In order to approve a FINRA rule, the SEC must find it to be in the public interest and may approve, deny, modify or even abrogate FINRA rules.

FINRA’s arbitration program has important safeguards that distinguish it from other arbitration forums. Benefits to FINRA arbitration include significantly lower forum fees, the right to have an all-public panel in customer cases (where none of the arbitrators is affiliated with the securities industry), and convenient venues in 72 hearing locations, including at least one in each state. We provide new and continuing training to the arbitrators and are committed to making sure the arbitration roster is filled with a diverse roster of highly qualified individuals. In addition, FINRA suspends a firm or broker’s membership for failure to pay arbitration awards or agreed-upon settlements. The FINRA Codes also provide for sanctions for frivolous or abusive motion practices, thereby ensuring that parties are given an opportunity to fully present their cases.

FINRA Codes state that all awards shall be in writing and signed by a majority of the arbitrators or as required by applicable law. Arbitration awards are published online on FINRA's Arbitration Awards Online database (AAO)¹ and also made available through BrokerCheck², which is searchable by firm and broker. Arbitrations related to other industries (i.e. credit cards, telephone services, hospitals and nursing homes) are conducted in a variety of forums and are not likely to be subject to the same level of government oversight and procedural safeguards.

FINRA strives continually to improve the arbitration process for investors. To ensure that the forum meets the evolving needs of parties, FINRA formed a task force to consider possible enhancements to its arbitration and mediation forum. The task force, which was composed of individuals representing a broad range of interests in securities dispute resolution, issued a report in December 2015 and action has been taken on most of its recommendations. The task force and its subcommittees—which included counsel representing investors, securities firms, arbitrators, a mediator, a state regulator, an academic and a consumer advocate—met over a period of 14 months and solicited written comments from a wide array of interested organizations and individuals.³ After the Task Force recommended that FINRA adopt a policy of promoting, to the maximum extent possible, transparency about its dispute resolution forum, FINRA expanded the statistics updated monthly on the FINRA website and updated charts to display case filing volume for the 15 most often cited controversy and security types over a five-year period. The information is further distinguished between customer cases and intra-industry cases. FINRA also added a map that provides the number of cases and arbitrators (by type) in each arbitration hearing location.⁴

The legislatures of Arizona, California, District of Columbia, Maryland, Nevada and West Virginia have also recognized the importance of FINRA's carefully vetted rules and oversight by the SEC by providing exemptions for arbitrations conducted through FINRA. Those legislatures amended their bills to exempt arbitrations conducted by self-regulatory organizations approved by the SEC under federal law. If S.105 is enacted as written, Vermont will be the only state to impose non-uniform and unnecessary requirements on FINRA's forum.

Finally, it is important to note that where FINRA Codes have conflicted with state statutes, federal and state courts have held that the Codes have preemptive force over conflicting state law, as illustrated in the following two cases:

¹ FINRA's Arbitration Awards Online database enables users to perform Web-based searches for FINRA and historical NASD arbitration awards free of charge, seven days a week. For more information and to access the database, visit <http://www.finra.org/arbitration-and-mediation/arbitration-awards>.

² BrokerCheck is a free tool from FINRA that allows the investing public to research the professional backgrounds of brokers and brokerage firms, as well as investment adviser firms and advisers. For more information and to access BrokerCheck, visit <https://brokercheck.finra.org/>.

³ More information about the task force, its recommendations and related status updates can be found at <https://www.finra.org/arbitration-and-mediation/finra-dispute-resolution-task-force>.

⁴ For more information, visit <http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics>.

Credit Suisse First Boston Corp. v. Grunwald, 400 F.3d 1119 (9th Cir. 2005), and

Jevne v. Superior Court, 35 Cal. 4th 935 (Cal. 2005).

FINRA Concerns with S.105

First, section 6055(a)(1) of S.105 differs from the Uniform Arbitration Act (UAA) and the Revised Uniform Arbitration Act (RUAA), which form the basis of most if not all state arbitration codes, and FINRA Codes in a significant way. Section 6055(a)(1) would require that an arbitration take place in the county where the individual claimant resides or where the contract was consummated. Of FINRA's 72 hearing locations, only one is located in Vermont (Montpelier, Washington County). FINRA Rules 12213 (Customer Code) and 13213 (Industry Code) state that the Director of FINRA's Office of Dispute Resolution will decide which of FINRA's hearing locations will be the hearing location for the arbitration. Generally, in customer arbitrations, the Director will select the hearing location closest to the customer's residence at the time of the events giving rise to the dispute, unless the hearing location closest to the customer's residence is in a different state, in which case the customer may request a hearing location in the customer's state of residence at the time of the events giving rise to the dispute.

In intra-industry cases involving an individual broker, the Director will generally select the hearing location closest to where the individual broker was employed at the time of the events giving rise to the dispute, unless the hearing location closest to the individual broker's employment is in a different state, in which case the individual broker may request a hearing location in his or her state of employment at the time of the events giving rise to the dispute. However, in cases involving more than one individual broker, the Director will consider a variety of factors, including:

- The parties' signed agreement to arbitrate, if any;
- Which party initiated the transaction or business in issue; and
- The location of essential witnesses and documents.

Second, section 6055(a)(5) of S.105 differs from the UAA, the RUAA and FINRA Codes in a significant way. It would require FINRA to set a different fee schedule for Vermont than as enumerated in the Codes and risk de-standardizing its program among 50 states, the District of Columbia and Puerto Rico. FINRA Rules 12900 (Customer Code) and 13900 (Industry Code) each provide a sliding scale for filing fees based on the amount of damages claimed. As mentioned above, FINRA arbitration includes significantly lower forum fees than other forums. FINRA also endeavors to provide access to arbitration for customers regardless of their inability to pay a filing fee; parties may submit a written request and supporting documentation to FINRA for a fee waiver stating the reasons that would make payment of the filing fee a financial hardship.

FINRA Rules 12901 (Customer Code) and 13901 (Industry Code) provide that a member surcharge fee is assessed against each member that is named as a party to arbitration; therefore, industry parties are responsible for approximately 85 percent of arbitration fees annually. Moreover, FINRA Rules 12902 (Customer Code) and 13902 (Industry Code) provide that the allocation of fees is determined by the arbitration panel, which allows for parties to request for reimbursement and reallocation of fees.

Third, section 5667 of S.105 differs from the UAA, the RUAA and FINRA Codes in a significant way. It would require FINRA to publish details about arbitrations that did not go into award (i.e., settled or dismissed) and to revise its awards template. FINRA Rules 12904 (Customer Code) and 13904 (Industry Code) state that all awards shall be made publicly available and must contain the following elements:

- The names of the parties;
- The name of the parties' representatives, if any;
- An acknowledgement by the arbitrators that they have each read the pleadings and other materials filed by the parties;
- A summary of the issues, including the types of any security or product, in controversy;
- The damages and other relief requested;
- The damages and other relief awarded;
- A statement of any other issues resolved;
- The allocation of forum fees and any other fees allocable by the panel;
- The names of the arbitrators;
- The dates the claim was filed and the award rendered;
- The number and dates of hearing sessions;
- The location of the hearings; and
- The signatures of the arbitrators.

As noted above, arbitration awards are published on AAO and also made available through BrokerCheck. Through AAO, users can access FINRA arbitration awards from January 1989 through the present. In addition, users can access all New York Stock Exchange (NYSE) arbitration awards, as well as the awards of all arbitration programs absorbed over the years by FINRA (which include the American Stock Exchange, Chicago Board Options Exchange, International Stock Exchange, Philadelphia Stock Exchange, and Municipal Securities Rulemaking Board) and NYSE (which includes Pacific Exchange/NYSE ARCA). The database provides users with instantaneous access to awards and the ability to search for awards by using multiple criteria, such as by case number, keywords within awards, arbitrator names, date ranges set by the user, and any combination of these features. FINRA also includes in customer awards information about the panel selection method and panel composition.

Suggested Language to Amend S.105

FINRA respectfully requests that the bill be amended to state the following, or something substantially similar:

THIS ARTICLE DOES NOT APPLY TO AN ARBITRATION CONDUCTED OR ADMINISTERED BY A SELF-REGULATORY ORGANIZATION AS DEFINED BY THE SECURITIES EXCHANGE ACT OF 1934 (15 U.S.C. SECTION 78C) OR REGULATIONS ADOPTED UNDER THAT ACT.

Conclusion

FINRA's arbitration program, which is subject to strict oversight by the SEC, has far-reaching protections in place that distinguish it from other arbitration forums that administer disputes involving consumer goods and services. FINRA's program has been nationally recognized for its training, neutrality and transparency. FINRA's extensive information about its arbitration program is publicly available. In light of these factors, we respectfully request an amendment exempting arbitrations conducted through FINRA's dispute resolution forum from S. 105.

If you have any comments or need additional information, please contact Nancy Doyal at (616) 485-8287 or Kristine Vo at (212) 858-4106. Thank you for consideration of this request.

Sincerely,


Gregory Dean
Senior Vice President
Office of Government Affairs

cc: Michael S. Pieciak, Commissioner, Vermont Department of Financial Regulation

FINRA Rule 12213:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4119

FINRA Rule 13213:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4216

FINRA Rule 12900:

http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=4188

FINRA Rule 13900:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4288

FINRA Rule 12901:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4189

FINRA Rule 13901:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4289

FINRA Rule 12902:

http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=4190

FINRA Rule 13902:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4290

FINRA Rule 12904:

http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=4192

FINRA Rule 13904:

http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4292