SIFMA
Securities Industry and
Financial Markets Association

May 27, 2008

BY EMAIL TO: pubcom@finra.org

Ms. Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1500

Re: FINRA Regulatory Notice 08-20,
Proposed Changes to Forms U4 and U5

Dear Ms. Asquith:

The Arbitration Committee of the Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to comment on the above-referenced proposal. SIFMA generally supports the proposed changes to Forms U4 and U5 as changes that are designed to ensure greater consistency and fairness in reporting of customer complaints against registered persons. SIFMA suggests, however, that there are several supplemental measures that FINRA could implement to further advance the goals of consistency, fairness, and compliance in customer complaint reporting. Our recommendations are as follows:

I. The Dollar Threshold For Reporting Settlements of Customer Complaints Should Be Raised From $10,000 to $25,000

SIFMA agrees with FINRA's proposal to raise the current $10,000 threshold for reporting settlements of customer complaints. That threshold was set more than a decade ago and it has never been adjusted. It is logical, however, for such dollar benchmarks to either be indexed for inflation or adjusted from time to time. In this case, FINRA suggests that the threshold should increase from $10,000 to $15,000.

FINRA concedes, however, that the relevant "inflation" rate at which the $10,000 threshold should be adjusted is *not* the general rate of inflation but rather, inflation of "the business criteria (including the cost of litigation) firms consider when deciding to settle claims."[2] It should be noted that during the ten

[1] SIFMA brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

[2] FINRA Regulatory Notice 08-20 (April 2008) at 6.

year period from 1991 to 2001, the percentage increase in the individual index for legal costs (48%) far exceeded the percentage increase in the general consumer price index (30%).[3] Further, since 1996 (the time the $10,000 threshold was set), member firms have also experienced significant forum cost increases. For example, in July 1997, FINRA substantially increased the surcharge on members named as parties to arbitration proceedings.[4] Additionally, in January 1998, FINRA adopted a new process fee for member firms named as parties to arbitration proceedings.[5] Fourteen months later, in March 1999, FINRA substantially increased the filing fees and hearing session deposits required for customer and member arbitrations.[6] Thus, during the twelve-year period between 1996 and today, firms' legal fees and arbitration forum fees have increased significantly, and at a far greater pace than inflation generally. Accordingly, SIFMA recommends that the reporting threshold be increased to at least $25,000 to more accurately reflect the reality of these business cost increases, which directly factor into firms' settlement decisions. As far back as 1998, FINRA tacitly recognized $25,000 as the appropriate small claim amount when it increased the ceiling for simplified arbitration cases from $10,000 to $25,000.[7] FINRA should do the same for the threshold for reporting settlements of customer complaints.

II. FINRA Should Adopt Reasonable Measures to Promote Responsible Pleading

The CRD system captures – and makes publicly available – all written customer complaints irrespective of merit or factual basis. The CRD system in fact has no analog in any other industry or professional field in the comprehensive manner in which it captures and publishes unsubstantiated complaints. As a result, the system – and registered persons – are subject to potential abuses by disgruntled customers or unscrupulous claimant's counsel. Experience shows that many claims and complaints contain a litany of alleged wrongful acts, including fraud, churning, unauthorized trading and conversion of funds, without prior sufficient knowledge of all facts to substantiate the claim. Accordingly, FINRA should implement meaningful safeguards to ensure that claimants and/or lawyers who engage in such practice understand the significant consequences of what they are doing and have a reasonable, good faith basis for naming the particular registered person. We suggest that claimants and their counsel be required to attest at the time the statement of claim is filed that there is a good-faith basis for naming the registered person(s) (whether in the caption or in the body of the claim).[8]

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[3] Best's Review, *Battling rising prices: increases in costs of key components in claims drive price indexes for the property/casualty industry's major business lines* (Sep. 1, 2003), available online at http://goliath.ecnext.com/coms2/gi_0199-3124007/Battling-rising-prices-increases-in.html.

[4] *See* SR-NASD-97-40.

[5] *See* FINRA Notice to Members 98-01 (January 1998).

[6] *See* FINRA Notice to Members 99-23 (March 1999).

[7] See FINRA Notice to Members 98-90 (November 1998).

[8] This could be accomplished by either: (i) modifying the Uniform Submission Agreement to include a separate signature line, whereby a claimant would certify to a good-faith basis for naming the individual registered person as a respondent; or (ii) requiring that claimants attest in writing that they have read the materials provided by FINRA and have a good-faith basis for naming an individual respondent.

We also suggest that FINRA provide additional investor education material in the initial packet of information that is sent to customers preparing to file a claim. This additional material would explain the potentially damaging implications of naming a registered person (whether in the caption or in the body of the claim). The foregoing measures would help promote more responsible pleading practice, improve the quality of information in the CRD system, and thereby enhance the integrity of the CRD system, upon which regulators, firms and investors rely.

III. FINRA Should Provide Firms With Further, Specific Guidance On Firms' Reporting Obligations

The proposed changes to Forms U4 and U5 will require firms to make additional, subjective determinations concerning their U4 and U5 reporting obligations. Accordingly, it would be beneficial for FINRA to provide firms with further guidance on firms' reporting obligations with respect to registered persons who are referenced in an arbitration claim. For example, what is a firm's reporting obligations with respect to a registered person named in an arbitration claim, but whose alleged misconduct is entirely unrelated to the substance of the claim? What is a firm's reporting obligation if one of its registered persons is referenced in an arbitration claim against a different firm, and how will the firm find out? What is a firm's reporting obligation where the arbitration claim mentions the names of numerous individuals in the chain of command from the broker and branch manager up to the compliance officer the chief executive officer?

FINRA currently maintains a webpage with "Form U4 and U5 Interpretive Questions."[9] Given FINRA's proposed changes to Forms U4 and U5, this webpage will already need to be revised. Along with these revisions, SIFMA suggests that FINRA provide the additional guidance requested above. Such guidance will minimize subjectivity in making reporting determinations, and thereby enhance consistency and compliance in reporting customer complaints.

IV. FINRA Should Ensure That Its Proposed Changes Do Not Treat Registered Persons Disparately

When a registered person is named as a party in an arbitration claim, that individual has the opportunity to be dismissed or to settle out of the case. These outcomes are reported as final dispositions on the DRP and the matter is concluded – there is finality. However, when a registered person is not named as a party but is referenced in the body of the claim, the registered person cannot exit the case by dismissal or settlement. In addition, none of the findings in the arbitration, or the terms of any settlement, would apply to such a non-party, registered person. The current DRP form for arbitrations, however, does not adequately provide a way to report these facts, or to report the finality of the matter with respect to the registered person. Accordingly, FINRA should revise the DRP form, and provide specific guidance for reporting these unique complaints, so that registered persons receive fair reporting treatment regardless of whether they are named in the caption, or merely named in the body.

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[9] The webpage is available at: http://www.finra.org/RegulatorySystems/CRD/FilingGuidance/p005243.

Finally, the rule proposal should make clear that registered persons who are only named in the body of a claim are afforded the opportunity to clear their CRD records – and their professional reputations – by seeking expungement of the complaint.

Thank you for giving SIFMA's Arbitration Committee the opportunity to comment on the proposed changes to Forms U4 and U5. If you have any questions regarding this comment letter, please contact the Committee's staff advisor, Kevin Carroll, at 202.962.7382 (kcarroll@sifma.org).

Sincerely,

Edward G. Turan
Chair, SIFMA Arbitration Committee

cc: Richard E. Pullano, Associate Vice President, Registration and Disclosure