



June 25, 2021

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FINRA
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Re: Comment on FINRA Regulatory Notice 21-17

To Whom it May Concern:

Thank you for the opportunity to comment on FINRA's role in diversity and inclusion in the broker-dealer industry in response to FINRA Regulatory Notice 21-17.¹ The Notice requests comments "on any aspect of [FINRA's] rules, operations and administrative processes that may create unintended barriers to greater diversity and inclusion in the broker-dealer industry or have unintended disparate impacts on those within the industry."² This comment focuses on the steps FINRA should take to improve diversity and inclusion in one aspect of the broker-dealer industry, FINRA's arbitration forum.

My interest in this issue and its application to the FINRA arbitration forum is both professional and personal. I am a law professor who teaches business and securities law courses. My recent scholarship focuses specifically on consumer investors' experiences in FINRA arbitration.³ I previously directed a law school securities arbitration clinic and supervised law students representing investors with smaller claims against their brokers in the FINRA arbitration forum. I am the chair of FINRA's National Arbitration and Mediation Committee (NAMC). I am also a Mexican-American woman with her own non-retirement investment accounts. These experiences provide me a unique lens through which to view FINRA's diversity and inclusion efforts as they relate to the FINRA Dispute Resolution forum.⁴

¹ FINRA Regulatory Notice 21-17, *Diversity and Inclusion* (April 29, 2021) available at <https://www.finra.org/sites/default/files/2021-04/Regulatory-Notice-21-17.pdf>.

² *Id.* at 4.

³ See, e.g., Nicole Iannarone, *Structural Barriers to Inclusion in the Securities Arbitrator Pool*, __ WASH. L. REV. __ (forthcoming 2021) (hereinafter "*Structural Barriers*") available at <https://ssrn.com/abstract=3873407> (examining whether FINRA's efforts to diversify its arbitrator pool results in more diverse arbitrators hearing smaller claims brought by consumers); Charlotte Alexander and Nicole G. Iannarone, *Winning Defined? Text Mining Arbitration Awards*, __ CARDOZO L. REV. __ (forthcoming 2021), available at <https://ssrn.com/abstract=3546266> (examining impact of differing measures of success in arbitration awards); Nicole G. Iannarone, *Finding Light in Arbitration's Dark Shadow*, 4 NEV. LAW J. FORUM 1 (2020) (recommending study of promise and limits of FINRA forum transparency).

⁴ This comment is written in my personal capacity and represents my own views and not necessarily the views of my employer or any groups with which I am affiliated.

FINRA should be applauded for recognizing that work remains to be done notwithstanding the positive steps it has already taken to improve diversity and inclusion. To eliminate barriers to diversity and inclusion, FINRA should first expand its current inquiry to ensure all relevant constituents are included and considered. Second, Dispute Resolution should continue the work it has already begun to diversify its arbitrator pool. Finally, FINRA should increase the transparency of information related to arbitrator demographics and selection so that the impact of its meaningful and sustained efforts to diversify the arbitrator pool can be fully studied and remaining barriers to inclusion uncovered and eliminated.

I. FINRA's Diversity and Inclusion Review Should Mirror its Mission

As an initial matter, FINRA should expand how it defines its diversity and inclusion focus to ensure that all constituencies it serves feel part of, participate in, and are considered in the review process. Regulatory Notice 21-17's call for comments could be interpreted as FINRA only looking inward at members of the broker-dealer industry.⁵ However, the Notice recognizes that FINRA's statutory mandate and authority "focuses on investor protection and market integrity."⁶ By keying its diversity and inclusion examination to the "broker-dealer industry" and "those within the industry," the Notice itself appears to frustrate greater inclusion as it seems to exclude the beneficiaries of broker-dealer services, the investing public, from the inquiry.⁷ Market integrity is served by ensuring that consumers of broker-dealer services are not disparately impacted by FINRA rules and procedures. Similarly, FINRA's investor protection mission is impacted by barriers to inclusion: how can investors be protected if structural barriers to diversity and inclusion adversely impact their engagement with FINRA and its members?

Thus, though the Notice intends to include investors as part of FINRA's inquiry due to the request for feedback on "on any aspects of our rules, operations and administrative processes," not specifically including and listing all who are impacted by FINRA rules and procedures is itself a barrier to inclusion. A reframing of FINRA's diversity and inclusion focus will ensure that the intended beneficiaries of FINRA's regulatory efforts are adequately represented. This is imperative because many FINRA rules and regulations that raise diversity and inclusion concerns impact investors in addition to broker-dealers or the industry. For example, FINRA administers the largest forum for the resolution of securities disputes.⁸ The FINRA Dispute Resolution program has been recognized as crucial to investor trust and market integrity.⁹ Because most

⁵ See, e.g., *id.* at 3 ("FINRA requests comment to ensure that FINRA's rules, operations and administrative processes do not create unintended barriers to greater diversity and inclusion in the broker-dealer industry or have unintended disparate impacts on those within the industry."); *id.* 4 ("FINRA seeks comment on any aspects of our rules, operations and administrative processes that may create unintended barriers to greater diversity and inclusion in the broker-dealer industry or that might have unintended disparate impacts on those within the industry.").

⁶ *Id.* at 2.

⁷ See, e.g., *supra* n 5.

⁸ See *FINRA Dispute Resolution Services*, available at <https://www.finra.org/arbitration-mediation> ("FINRA operates the largest securities dispute resolution forum in the United States").

⁹ See, e.g., Iannarone, *Structural Barriers*, *supra* n. 3 at 11 (describing consumer trust and market integrity functions of fair process for consumers to resolve disputes with brokers).

investors are required to submit to FINRA arbitration if they have a dispute with their broker, investors are bound by those FINRA rules and procedures and any rule or procedure that disparately impacts them must be part of FINRA's review of diversity and inclusion efforts.¹⁰ Accordingly, FINRA should begin its examination of barriers to inclusion by ensuring that all subject to its rules, regulations, and mission are included within the review process.

II. FINRA Dispute Resolution Services Should Continue its Diversification Efforts

FINRA Dispute Resolution Services staff has undertaken significant efforts to increase the diversity of members of its arbitration roster and has been committed to building an arbitrator roster reflective of society. As a public member and now chair of NAMC, I have been pleased when staff have shared the details of the strategic work they have taken to increase diversity and inclusion in the neutral roster. Dispute Resolution Services should further be commended for sharing the progress it has made in diversifying the arbitrator pool while also recognizing that much more work needs to be done.¹¹ As a Latina, the lack of diversity within the FINRA arbitrator pool has long been a concern to me. According to the U.S. Census Bureau, 18.5% of the American population is Hispanic or Latino/a.¹² The FINRA arbitrator pool does not currently mirror the United States population, with only 4% of FINRA's arbitrator pool identifying as Hispanic or Latino/a, a percentage that has remained static since 2016.¹³ Similarly, FINRA's arbitrator pool has diversified with regard to arbitrators identifying as Black or African-American¹⁴ or Asian¹⁵ in the past five years, but the percentage of such arbitrators within the arbitrator pool still falls below the percentage that each of these groups represent within the country as a whole.¹⁶ FINRA has increased the percentage of women on its arbitrator roster from 24% to 30% in the past five years,¹⁷ though women are 50.8% of the total U.S. population.¹⁸ Investor trust, and derivatively, market integrity, may suffer if members of diverse groups are required to arbitrate claims in a forum whose neutrals are not representative of them or the American population. While FINRA has made progress in recruiting more diverse arbitrators to its neutral roster, it is imperative that work continue and the hardworking FINRA staff who have undertaken these gains continue to be

¹⁰ See, e.g., Barbara Black, *Can Behavioral Economics Inform Our Understanding of Securities Arbitration?*, 12 TENN. J. BUS. L. 107, 107 (2011) ("virtually all disputes involving customers, brokerage firms, and their registered representatives are arbitrated before the Financial Industry Regulatory authority ("FINRA") forum.").

¹¹ FINRA, *Our Commitment to Achieving Arbitrator and Mediator Diversity at FINRA*, available at <https://www.finra.org/arbitration-mediation/our-commitment-achieving-arbitrator-and-mediator-diversity-finra>.

¹² United States Census Bureau, *Quick Facts*, available at <https://www.census.gov/quickfacts/fact/table/US/RHI725219>.

¹³ FINRA, *Our Commitment to Achieving Arbitrator and Mediator Diversity at FINRA*, available at <https://www.finra.org/arbitration-mediation/our-commitment-achieving-arbitrator-and-mediator-diversity-finra>.

¹⁴ *Id.* (Black or African-American arbitrators increasing from 5% to 9% of total arbitrator pool from 2016-2020).

¹⁵ *Id.* (Asian arbitrators increasing from 1% to 2% of total arbitrator pool from 2016-2020).

¹⁶ United States Census Bureau, *Quick Facts*, available at <https://www.census.gov/quickfacts/fact/table/US/RHI725219> (measuring Black or African American as 13.4% of population; Asian as 5.9% of population).

¹⁷ FINRA, *Our Commitment to Achieving Arbitrator and Mediator Diversity at FINRA*, available at <https://www.finra.org/arbitration-mediation/our-commitment-achieving-arbitrator-and-mediator-diversity-finra>.

¹⁸ United States Census Bureau, *Quick Facts*, available at <https://www.census.gov/quickfacts/fact/table/US/RHI725219>.

given the support they need to pursue their important work until the arbitrator pool reflects society.

III. FINRA Dispute Resolution Should Increase its Transparency so that its Efforts to Diversify can be Fully Assessed and Barriers to Inclusion Identified and Eliminated

Among dispute resolution forums, FINRA is significantly more transparent, particularly as to the information provided concerning the members of the neutral roster and the cases over which they preside.¹⁹ Yet, the current transparency does not go far enough. First, FINRA should provide information sufficient for investors to assess arbitrator pool diversity as applied to their circumstances. Second, FINRA should provide sufficient transparency so that the impact of its diversification efforts can be fully assessed and additional barriers to inclusion, if any, can be eliminated.

A. Increasing Transparency for Consumer Investor Trust

FINRA takes the rare steps to show not only the current demographics of its arbitrator pool but how it has changed as a result of the significant efforts FINRA has already taken to diversify the pool. That transparency goes a long way to cultivate public trust, though more can and should be done to ensure investor trust and identify areas where more focused diversification efforts are needed. Were an investor to have a dispute with a broker, that investor can only now see the aggregate demographic statistics of FINRA's arbitrator pool. It is not possible to tell from the publicly available information what the demographic makeup of the arbitrator pool is in each of the 69 FINRA hearing locations. This lack of specificity can cause investors to wonder if the arbitrator pool in their hearing location would reflect their background and experiences and, absent such information, potentially lead them to mistrust their sole means for resolving a dispute with their broker, leading to market integrity concerns. Providing data as to the demographic make up of the public, non-public, and public-chair arbitrator rosters by hearing location would increase trust in FINRA arbitration. It would also allow outside stakeholders to target their arbitrator recruitment efforts and focus on areas with the greatest need. The investors I have had the pleasure to represent in FINRA proceedings are investors with claims of a dollar amount deemed small by the industry, but that are vitally important to them. These claimants – those who seek less than \$100,000 – have their cases heard by public arbitrators who have been qualified to serve as public chairs due to their experience serving as one of three arbitrators in either one or two prior proceedings seeking more than \$100,000. Without knowing the demographic breakdown of arbitrators by their classification and hearing location, an investor with a smaller claim cannot trust that even a fully diversified arbitrator pool matching U.S. demographics means that the customer will have access, in their hearing location, to diverse public chair-qualified arbitrators. Providing such detailed information would also assist FINRA in underscoring the need when staff recruit applicants for service as arbitrators in particularly underserved areas. FINRA should increase its transparency to provide better information to investors across the

¹⁹ See, e.g., Iannarone, *Structural Barriers*, *supra* n. 3 at 5 (comparing FINRA arbitrator roster transparency to AAA and JAMS).

country about the diversity of the arbitrator pool in their area and broken down by the three classifications of arbitrators: public, non-public, and public chair.

B. FINRA Should Increase Transparency to Study the Impact of Diversification Efforts and Identify Barriers to Inclusion

Finally, FINRA should provide sufficient transparency so the impact of its diversification efforts can be more fully evaluated and additional barriers to inclusion identified. Because FINRA takes the rare step of making publicly available all awards, some study of the impact of efforts to diversify its arbitrator roster are possible, with limitations. Last summer, I took steps to determine if arbitrators added to FINRA's neutral roster in the past five years, who on the whole are more diverse than the prior pool, had been able to obtain the necessary qualification to preside as chairs over smaller claims.²⁰ My study, forthcoming in the *Washington Law Review*, was based on the hypothesis that two structural barriers made it likely that investors with smaller claims were unlikely to obtain the benefit of FINRA's diversity recruitment efforts: (1) FINRA's public chair qualification rule; and (2) the list selection procedures for three arbitrator cases whereby arbitrators already qualified as chairs have two opportunities to appear on lists compared to non-chair public arbitrators only having one opportunity to appear on a list.²¹ From the publicly available awards, I was able to determine that in smaller claims that concluded via hearing from 2014-2019, only 0.98% were decided by public chair qualified arbitrators who first appeared in FINRA's awards database as an arbitrator in a case filed after December 31, 2014.²² The data indicate that virtually no customers in small cases whose proceeding concluded with an award after a hearing benefitted from the increased diversity FINRA achieved in the overall pool from 2015-2019, suggesting that the hypothesis was correct and two FINRA rules serve as barriers to inclusion.²³ The study also showed that longer serving arbitrators far outnumbered new entrants. Over half of the arbitrators who presided over small claims in the study period first appeared in the FINRA awards database more than 20 years ago.²⁴ Over 80% first appeared in the awards database before chair qualification was a prerequisite to presiding over smaller claims.²⁵ In addition, more than one-third of the arbitrators studied first appeared in cases filed before 1998, the date before which parties had no ability to select arbitrators in FINRA proceedings.²⁶

As more fully described in the article, the transparency FINRA currently makes available concerning the members of its arbitrator roster is an insufficient basis upon which to fully assess whether FINRA's arbitrator diversification efforts result in inclusion.²⁷ Transparency in the form of arbitrator disclosure reports listing the date the arbitrator joined FINRA's roster, the hearing location(s) where the arbitrator is willing to hear cases, the number of times the arbitrator has

²⁰ See generally Iannarone, *Structural Barriers*, *supra* n 3.

²¹ *Id.*

²² *Id.* at 45.

²³ *Id.* at 46.

²⁴ *Id.*

²⁵ *Id.*

²⁶ *Id.* at 47.

²⁷ *Id.* at 47-49.

been included on a list, the number of times the arbitrator has been chosen to serve in an arbitration, and issuing public awards for cases that have concluded via settlement are necessary for third parties to independently assess FINRA's arbitrator pool diversification efforts and definitively state whether structural barriers or party behavior and biases drive the low number of small claims presided over by new entrants to the arbitrator pool. Such transparency is required to fully assess whether there are barriers to inclusion within FINRA's arbitrator pool and eliminate any identified barriers. Nevertheless, the extremely small number of new arbitrators hearing smaller claims that conclude in an award in the past five years suggests that FINRA should immediately take steps to remove the double selection preference currently provided to existing public chairs. FINRA should also provide greater opportunities for diverse arbitrators to be named on a list. Taking dual steps of increasing transparency so that FINRA's arbitrator pool diversification efforts can be independently evaluated while also easing back rules that disparately advantage existing, long-serving arbitrators will help FINRA fulfill its mission of investor protection and market integrity.

Conclusion

Thank you for the opportunity to comment on FINRA Regulatory Notice 21-17. FINRA as a whole, and FINRA Dispute Resolution Services specifically, have taken significant steps to improve diversity and inclusion in the broker-dealer industry. This comment has identified areas in which concrete steps can be undertaken to continue the work that FINRA has already begun by including investors in the conversation, providing public transparency so that FINRA's efforts can be externally assessed, and dismantling preexisting barriers that prevent inclusion.

Please do not hesitate to contact me if I may answer any questions or provide any assistance.

Best regards,

/s/ Nicole G. Iannarone

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