

What to Expect: FINRA’s Dispute Resolution Process

It is rare for most firms to find themselves in a dispute with a customer, an employee, or another firm that escalates to a point where FINRA’s dispute resolution services are needed. However, this can occur, so it is important that you know what to expect in the event that you are involved in one.

It is typically less costly and faster to use arbitration or mediation as a way to settle a dispute than to take a case to court. In arbitration, a single arbitrator or panel of three arbitrators—depending on the amount of money in controversy—hears all sides of the issues, studies the evidence, and then decides how the matter should be resolved. In mediation, a mediator facilitates negotiations between disputing parties to help them develop and agree upon a resolution.

FINRA operates the largest securities dispute resolution forum in the world, and has extensive experience in providing a fair, efficient and effective place to handle claims. Broker-dealers, registered representatives, other associated persons, and investors can resolve disputes by arbitrating or mediating through FINRA’s dispute resolution program. Roughly one-third of FINRA’s cases are industry disputes, meaning they do not involve customer claims. And the forum is neutral. Staff members who coordinate the process are FINRA employees, but they are not involved in rendering judgments, and are separate from FINRA’s Examination and Enforcement departments. FINRA cannot offer legal advice or legal representation to anyone.

FINRA’s dispute resolution forum is neutral. While FINRA staff members coordinate the dispute resolution process, they are not involved in rendering judgments.

Parties can file an arbitration claim or request mediation when there is a dispute involving the business activities of a brokerage firm or an associated person, including claims by investors and disputes involving employee compensation or termination. Generally, the claim must be about an incident that took place within the last six years.

Arbitration

Arbitration is similar to the courts, but is usually faster, cheaper and less complex. Parties present the issues through the use of witness testimony and documentary evidence much as they would in court. Instead of a judge, there is either a single arbitrator or a panel of three arbitrators. The arbitrator or panel studies the evidence and decides how to resolve the matter much as a judge makes a ruling in a court case, but the legal rules of evidence do not strictly apply. Arbitrators are guided by the underlying policies of the law but can interpret legal concepts with more flexibility than judges.

The arbitration process differs depending on the claim size. Larger claims involve an in-person hearing decided by a panel of three arbitrators, with one serving as the chair. Smaller claims are decided by one arbitrator. The smallest claims may be decided through what is called a Simplified Arbitration Process. This is when the arbitrator decides the case by reading all of the materials provided by the parties without an in-person hearing.

The first step for parties who want to file an arbitration is to submit the request to FINRA along with the required paperwork. One required document is called a Statement of Claim. This is submitted by the person filing the claim and includes a description of the dispute, the parties involved and the monetary size of the claim.

Another required document is the FINRA Submission Agreement, previously known as the Uniform Submission Agreement. This lists the parties in the arbitration case and confirms that FINRA will administer it. It also establishes that, if the case ends with a hearing, the parties all agree to abide by the arbitrators’ decisions. FINRA also requires that the claimant submit the appropriate filing fees to begin the case.

Requirements for Filing an Arbitration

- ▶ Statement of Claim
- ▶ FINRA Submission Agreement
- ▶ Filing Fees

When FINRA receives the required documents and fees, it analyzes the claim, looking for things like the claim’s size to decide how many arbitrators will be needed, the nature of the dispute and the type of securities involved. Then, FINRA assigns a case number and informs the parties how to contact FINRA staff about the case.

Firms often ask if FINRA staff can dismiss frivolous claims. Because FINRA staff serves as the impartial provider of the arbitration forum, staff members have no authority to evaluate the strengths and weaknesses of claims or defenses. That job is reserved for the arbitrators.

If your firm is named in a claim as a respondent, FINRA notifies your firm’s representative by mail. You will receive a case packet that has a copy of the Statement of Claim. The packet will also include a detailed letter highlighting important rules and response deadlines outlined in FINRA’s Code of Arbitration Procedure. And it also contains a blank FINRA Submission Agreement that your firm must fill out, sign and return.

The cover letter will contain the city in which the hearings for the case will take place and how to contact FINRA if you have questions. Usually, the hearing will take place in the FINRA hearing location nearest to where the claimant lived at the time of the original dispute. If the parties agree on a different hearing location, FINRA will try to accommodate the request. There is at least one, and as many as three, hearing locations in every state, plus the District of Columbia, Puerto Rico and London—over 70 in total.

Each respondent is given 45 days to research the claim and to prepare and serve a response. In it, the respondent can outline the defenses the firm or broker plans to argue and any exhibits that support this position. FINRA will analyze this information to see if there are counterclaims (which are claims by the respondent against the claimant) or cross claims (which are claims by the respondent against another respondent). If so, FINRA checks to make sure the parties submitted the right fees, and looks for any newly named parties. FINRA also checks to see whether the respondent completed the FINRA Submission Agreement properly.

Then, the parties select their arbitrators. FINRA provides identical lists of possible arbitrators for the case to both sides of the dispute. A computer generates the names randomly. FINRA also provides both sides with a detailed report on each arbitrator’s background, called a disclosure report. The disclosure report resembles a résumé, and includes the arbitrator’s employment background, education and training. FINRA also provides a list of cases in which each of the arbitrators has issued a final decision, called an award. You can view awards for free on FINRA’s website or obtain them from FINRA in hard copy.

Both sides are allowed to remove, or strike, some of the arbitrators on the list from consideration and to rank the remaining names in order of their preference. This process gives both parties a say in who the arbitrators will be.

Arbitrators are not FINRA employees but work on a case-by-case basis as contractors. They must apply to be arbitrators, and FINRA evaluates their education, professional licenses and employment. They also must take required training to arbitrate in FINRA’s forum. FINRA divides arbitrators into two categories: those who have a connection to the securities industry and those who do not. FINRA refers to the arbitrators who have a connection as non-public arbitrators and all others as public arbitrators. FINRA strives to include people who represent different professions and backgrounds for both categories of arbitrators. For people who chair arbitration panels, FINRA requires special training and experience with previous arbitrations.

A public arbitrator serves as the sole arbitrator on smaller claims involving customers. A three-arbitrator panel hears the larger customer claims. Customers in cases that proceed with three arbitrators have the option to have an all-public arbitration panel or a majority-public panel decide their claim.

Disputes between firms are decided exclusively by non-public arbitrators. Smaller disputes between firms and their employees are decided by a single public arbitrator. Larger disputes between firms and their employees are decided by a three-arbitrator panel comprised of two public arbitrators and one non-public arbitrator. Disputes involving statutory discrimination claims use all public panels with specially qualified chairs.

In all cases, arbitrators are required to make decisions based on the facts and merits of the cases they hear, and they take an oath to remain neutral. FINRA constantly monitors arbitrators to ensure that they meet necessary standards and, if they fail to meet them, FINRA removes them from the pool of arbitrators.

Once the parties select their arbitrators, the arbitration panel has an initial pre-hearing conference with the party representatives—typically over the telephone. During the call, the arbitrators and party representatives—usually lawyers—discuss procedural issues, the mediation alternative and the scheduling of the in-person hearing. So, at this conference, FINRA recommends that the representatives have their calendars available. And they should also raise any issues that they think the arbitrators will need to address at this time.

The next stage is Discovery. This is when parties exchange documents and identify their witnesses. FINRA’s website contains detailed rules for parties and their representatives to follow during the discovery process. Also, all parties in a customer case should be familiar and comply with a document called the Discovery Guide. It lists the documents that should be produced by both the claimant and respondent in all customer arbitrations.

Once the parties complete the Discovery phase of the case, it is time for the in-person hearings. This is when each party presents its case to the arbitrators.

Arbitration Hearing Process

After all the parties arrive, the arbitrators invite the parties, their counsel and witnesses into the hearing room. If either side has fact witnesses, they may be asked to wait in a waiting room until they are called in to testify. Expert witnesses are generally permitted to remain in the hearing room, while fact witnesses will be called in when it is their turn to testify.

The arbitrators sit at the head of the table, and respondents and claimants sit with their groups on opposite sides. Usually, the arbitrators reserve seats near them for witnesses. It will take a little while for everyone to bring in all of their materials and to get them set up. While everyone gets settled, the parties should not have conversations with the arbitrators.

Once everyone is ready, the chairperson will call the hearing to order. The arbitrators will identify themselves, and then so will all those in attendance. The chair will then swear in all of the parties and witnesses in attendance who will testify. The claimant’s side is given the opportunity to make an opening statement, followed by a statement from the respondent’s side. These statements provide a brief outline of the issues and what the party will try to prove. This is not the appropriate time to present evidence.

After the opening statement, the claimants present the details of their case. For example, they present witnesses and introduce any relevant documents. If the arbitrators did not swear a witness in at the beginning of a hearing, they will administer the oath before that person testifies. The other side can cross-examine any witness who testifies, that is, ask questions of the witness. The arbitrators may also ask the witnesses questions. After the claimant’s side has completed presenting its case, then it is the respondent’s turn to present its case.

Each party can object to any evidence being presented before the arbitrators receive it. Following an objection, the arbitrators will decide if they will accept the evidence. You should also know that hearings are digitally-recorded, usually on a device operated by the arbitrators. And, sometimes a party will arrange for a court reporter to be present at the hearing.

Once the parties have offered all witnesses and evidence, they present closing arguments. This allows them the opportunity to summarize what they believe they have proven. Either side can rebut the other side’s closing arguments if they choose.

Post Hearing

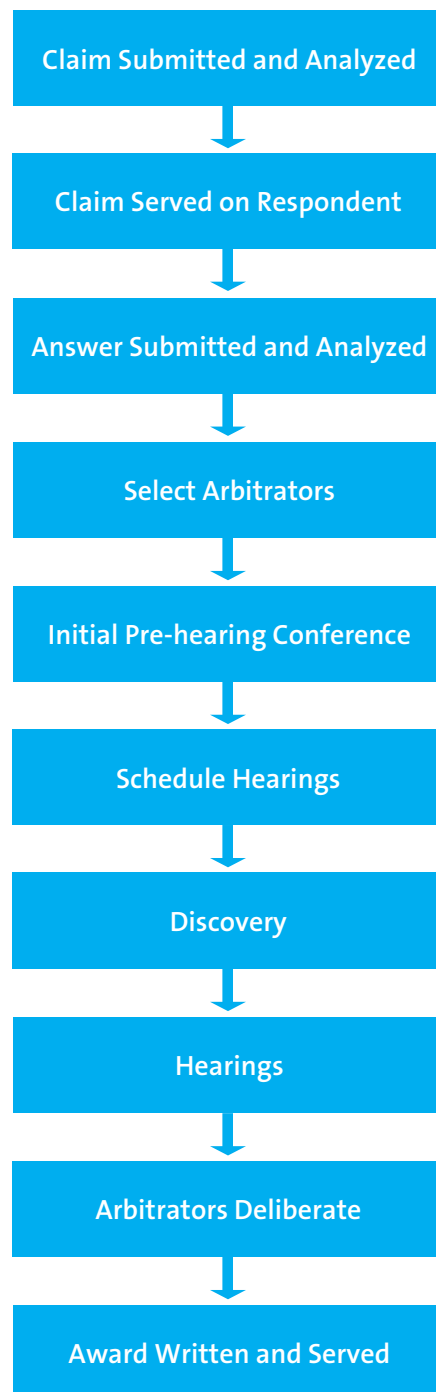
After the hearing, the arbitrators consider the evidence and make a decision on the case—also called rendering an award—typically within 30 days. All of the arbitrators have an equal vote, with the majority deciding the outcome. But, most awards in the FINRA forum are unanimous.

The decision is put in writing and signed by the arbitrators. This decision is called the arbitration award, and is sent to the parties. In the award, the arbitrators decide the claims and counterclaims presented by the parties, and will also decide how to allocate FINRA forum fees. If the decision requires your firm to take any action, like making a payment to the other side, then your firm must comply with it, or move in court to vacate the award (which means to ask the court to set the award aside as void) within 30 days after you receive the award. Firms that do not comply in a timely manner risk FINRA suspension. You can find all of the arbitration decisions from our forum on FINRA’s website.

Once the panel renders an award, it is legally binding and final, except in very limited situations in which a party can challenge it in court. Also, there is no internal appeals process at FINRA.

Arbitration cases that settle are typically resolved in a little over a year. When an arbitration case goes to hearing, it typically takes 16 months. In either case, arbitration is usually faster than most court cases. Since arbitration cases are resolved more quickly, and there is only limited court review of arbitration decisions, the related costs, such as attorney fees and other expenses, are typically lower in arbitration than in cases that go to court.

Arbitration Case Flow



Mediation

While arbitration is a fast, economical and fair way to resolve disputes, it is not the only way. Mediation is another way that you can resolve a dispute. If you are involved in an arbitration, you may request or agree to mediation at any time before the arbitrators issue an award. Or, you may agree to mediation from the beginning of the dispute as the way to resolve your conflict.

A mediator does not act like a judge or an arbitrator. Instead, the mediator is a facilitator who helps the parties negotiate an agreed-upon solution. It is a voluntary process, so either party may decide to stop at any time. However, over 80 percent of mediations end up with a settlement.

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To mediate through FINRA’s program, one or both parties will first tell FINRA staff that they are interested in mediation. FINRA will then contact the other side to see if they agree to mediate the dispute. However, if you do not want FINRA to tell the other side that you expressed interest in mediation, FINRA staff will see if they are interested in mediation without revealing any interest by the opposing party. FINRA staff members also contact parties in some cases from the arbitration docket to elicit interest in mediation.

If both parties agree to mediation, FINRA’s mediation administrators can assist in the selection of a mediator. FINRA provides a list of mediators to choose from along with a disclosure report for each mediator. The parties have full say in who their mediator is, and select a mediator who they all agree to work with.

Like arbitrators, mediators are not FINRA employees. They are carefully screened and represent a cross-section of diverse people. Many have extensive knowledge of the securities laws and industry practices. And, like arbitrators, they are required to follow ethical standards.

Once the parties agree on a mediator, FINRA staff sends a Mediation Submission Agreement to the parties that indicates the terms for the mediation. All parties, their representatives and the mediator must sign this document before the mediation can take place. The purpose of the Mediation Submission Agreement is to protect the parties involved and prevent any misunderstandings about the process. It includes the requirement that everything that takes place in mediation remain confidential. It also shows the mediator’s fees and how the parties will divide those fees. FINRA’s mediation administrators can work with both parties to find mutually agreeable conditions for the mediation.

Before mediation starts, most mediators will ask the parties to provide a written statement with their side of the story. Mediators indicate up front whether they will share this statement with the other side or keep it confidential.

The mediator may ask your firm to indicate what it hopes to get out of the process. It is important for you to think about what you want to achieve and what your firm is willing to offer to resolve the case before you go to the mediation. If you think about a range of possible solutions and know your bottom line, it will help you prepare for mediation. Your attorney can represent and help you with this process.

FINRA’s staff will help you schedule the mediation date and coordinate the location.

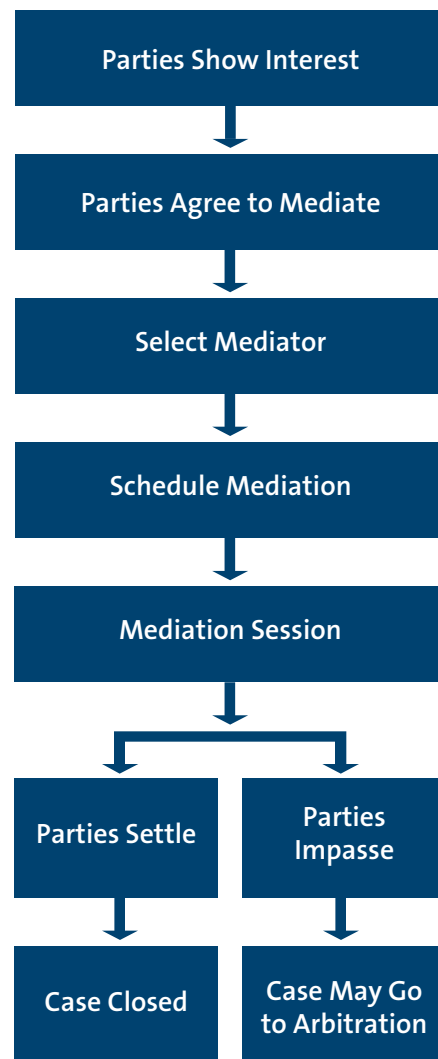
Then the actual mediation session for the parties to work toward a possible settlement occurs. The location of these sessions is selected in the same way as arbitration hearing locations are selected.

Mediation Session Process

The mediator begins the mediation session with introductions. After that, the mediator will make some opening remarks and set the ground rules. Next, the claimant’s attorney explains their position and interests. Then, the respondent’s attorney does the same. The parties continue to discuss the issues with the mediator’s guidance. At some point, the mediator may meet with each side privately. Sometimes, parties are more open in these separate sessions and the mediator will maintain confidences when asked.

Four out of five times, this process helps the parties reach a settlement. If the parties agree to settle, their representatives draft enforceable agreement, which both parties sign. The parties only sign the settlement agreement if they agree with its terms. You can stop the mediation process at any time. If settlement is not reached, then the claimant can file an arbitration case, or, if one was previously filed, request that it continue.

Mediation Case Flow



Choosing Between Arbitration and Mediation

You might want to pursue mediation if your firm wants to quickly resolve a claim. Arbitrations usually take a bit longer than a year to resolve, but most mediations take a little over three months to complete. Arbitration hearings last about four days, but mediations are typically resolved in one session that lasts about eight hours. As a result, mediations usually are less costly. Mediation can also be less adversarial and is something to consider if your firm prefers a less formal setting to resolve disputes. However, choosing to mediate is entirely your decision, and you always have the right to go through the full arbitration process.

Simply put, you can think of arbitration as presenting your case and having someone else decide it, versus mediation, where someone assists you with negotiating a solution to your case.

Working with an Attorney

Most parties are represented by a lawyer when they are involved in an arbitration or a mediation. But, we realize that some firms may not have relationships with legal counsel or know counsel with securities arbitration or mediation experience.

As we mentioned earlier, FINRA staff does not give legal advice, and we cannot recommend any specific lawyers. But they can suggest ways to find an attorney.

You can also ask contacts at other firms for suggestions, or locate and work with legal referral services offered by bar associations to find lawyers who specialize in securities issues. FINRA’s website has a link to a nationwide network of legal referral services.

Additional Resources

FINRA Dispute Resolution

www.finra.org/ArbitrationMediation/index.htm

What Disputes Are Eligible for Arbitration?

www.finra.org/ArbitrationMediation/Parties/Overview/ArbitrationProcedures/P009533

Statement of Claim (part of pdf document: “Uniform Forms Guide”)

www.finra.org/web/groups/arbitrationmediation/@arbmed/@tools/documents/arbmed/p007954.pdf

FINRA Submission Agreement

www.finra.org/web/groups/arbitrationmediation/@arbmed/@neutrl/documents/arbmed/p009438.pdf

Filing Fee Calculator

apps.finra.org/ArbitrationMediation/ArbFeeCalc/1/

Dispute Resolution Regional Offices & Hearing Locations

www.finra.org/ArbitrationMediation/Contacts/DRRegionalOfficesHearingLocations/p085899

Awards Database Online

finraawardsonline.finra.org

Notice to Parties – Discovery Rules and Procedures

www.finra.org/ArbitrationMediation/Parties/ArbitrationProcess/NoticesToParties/P009517

Discovery Guide

www.finra.org/web/groups/arbitrationmediation/@arbmed/@arbrul/documents/arbmed/p009420.pdf

Mediation Submission Agreement

www.finra.org/web/groups/arbitrationmediation/@arbmed/@party/documents/arbmed/p018658.pdf

How to Find an Attorney

www.finra.org/ArbitrationMediation/Parties/Overview/HowToFindAnAttorney/index.htm