International Assets Advisory
Member FINRA/MSRB/SIPC

Submitted via email to: pubcom@finra.org

April 30, 2026

Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1700 K Street, NW
Washington, DC 20006

Re: Regulatory Notice 26-06 — Request for Comment on Modernizing FINRA Arbitration Rules, Guidance and Processes

Dear Ms. Mitchell,

International Assets Advisory, LLC ("IAA") appreciates the opportunity to comment on Regulatory Notice 26-06 (the "Notice") to further FINRA's commitment to making changes to its rules, guidance and processes, and addressing challenging issues facing its arbitration forum.

IAA is a FINRA member retail broker/dealer that offers a variety of services and products to consumers, including traditional and alternative investments. FINRA must reevaluate its current arbitration rules and processes to bring it back to a forum that is a fair, efficient and cost-effective alternative to litigation for all participants. As explained in more detail in this letter, as currently structured, member firms are at a significant disadvantage in FINRA arbitrations. This structure does not promote the smooth functioning of our capital markets, nor does it promote investor protection. On the contrary, particularly for alternative investment cases involving accredited investors, the arbitration process has become fraught with distortions that are inconsistent with the law (that accredited investors do not need the protections afforded public offerings and are capable of withstanding the full risk of loss).

A. As currently structured, FINRA customer arbitration is not fair, efficient or cost effective for FINRA members.

While we understand that FINRA wants to encourage claimants who have legitimate claims to have access to the FINRA arbitration forum and a hearing on the merits, the actual result of these rules is that claimants and their counsel are not subject to any repercussions for filing unsubstantiated and frivolous claims, and in fact, are rewarded for doing so. The current structure encourages unsubstantiated and frivolous claims and is inherently unfair to member and associated person respondents.

As respondents have no meaningful way to of getting frivolous claims dismissed, claimants' counsel know that even a frivolous claim will often be settled because it is cheaper than defending at hearing. In addition, because of the FINRA disclosure requirements for registered personnel and, without any meaningful ability to get frivolous claims dismissed, the only way to get the disclosure removed is to go through the expungement process (which is expensive and unfairly tilted against the industry). This structure results in more unnecessary costs and expenses for registered personnel. Among other things, FINRA should reform the expungement process (FINRA went too far in its most recent rule changes) and it should also change the reporting level from $15,000 to at least $25,000. The reporting level was set in 1995 and has not changed in over 30 years despite inflation. In fact, $15,000 in 1995 equates to $32,500 today. Raising the threshold for disclosure to $25,000 would simply account for inflation over the last three decades.

1. Early resolution to arbitration claims should be encouraged, not discouraged.

Under FINRA Rule 12504(a), motions to dismiss prior to the "conclusion of a party's case in chief are discouraged in arbitration" and are not permitted prior to the filing an answer by the respondent. Furthermore, motions to dismiss may only be considered in very limited circumstances. These limitations were instituted in 2009 as a result of complaints of alleged excessive motion practice by respondents thereby delaying scheduled hearing sessions on the merits, increasing customers' costs, and intimidating less sophisticated customers. At the time, FINRA believed that the enforcement mechanisms in the rules would minimize parties' costs and ensure strict compliance with the rules. However, the result is that neither of these objectives have been met. The respondents' costs have grown exponentially and only the respondents are held to strict compliance with the rules.

Claimants' counsel are well aware of the limitations placed on respondents' ability to file motions to dismiss in FINRA arbitrations and take full advantage of this imbalance. In fact, the statement of claim filed will routinely include only generalized allegations and often does not even include the name of the investment that is the subject of the claim or when it was purchased—let alone any particularized allegation of wrongdoing (who, what, when, where). These generalized allegations would never survive a motion to dismiss in a court setting or even in any other arbitration forum. How is it fair to allow a claim for an unspecified investment purchased at a date uncertain to proceed against a member firm? This is especially true when claimants allege fraud but then are not required to provide any specificity as to their allegations—in direct contravention of case law across the country.

Because of this imbalance, claimants' counsel know that even a frivolous claim will often be settled because it is cheaper than defending at hearing. This structure is inherently unfair to the member firms. FINRA should change the timing and expand the circumstances under which the panel can act upon a prehearing motion to dismiss a party or claim. Among other things, prehearing motion practice should include the failure to plead claims with particularity and also to dismiss claims based on the applicable statutes of limitations or statutes of repose.

Unlike a court setting, under the current system, a consumer can make multiple unsubstantiated claims against a member and/or an associated person, including claiming fraud, without any

support for their claims. Instead of the claimant being required to provide evidence and factual support for his/her claims, it is up to the respondent to disprove the claims.

At a minimum, claimants and their counsel should be required to provide documents or other tangible evidence to support the allegations made in the statement of claim, including demonstrating actual damages. To level the playing field, there should be repercussions to claimants and their counsel who file unsubstantiated or frivolous claims in the same way that respondents face repercussions for filing frivolous motions. Without these safeguards, the abuse of the FINRA arbitration forum will continue.

2. The eligibility rule should be enforced and enforced consistently or eliminated in favor of state statutes of limitations and repose.

If the eligibility rule remains, FINRA must ensure that the rule is enforced consistently. As the eligibility rule is jurisdictional, the determination should be resolved by the Director or made at the earliest possible stage, such as before an answer is due. Additionally, as a jurisdictional rule, it should act as a statute of repose barring claims based on securities transactions that occurred more than six years before a claim is filed.

Unfortunately, due to the inconsistency of the application of the eligibility rule, claimants' counsel craft statements of claim to include generalized allegations of ongoing fraud and/or concealment of harm, quite often without any specific facts to support the claims. Often, these allegations lack any merit (e.g., when the investment-at-issue is illiquid and all of the claims concern occurrences or events at or before the point of sale). Additionally, in an effort to avoid clear 6-year eligibility issues, claimants' counsel routinely do not include the actual date or even the year that the investment was purchased or which product is the subject of the claim. How is it fair to allow a claim against a member firm well past the time period for the books and records retention requirements?

As the eligibility rule is jurisdictional, when the respondent files a motion to dismiss based on eligibility, the claimant would then have the opportunity to amend the SOC to include specific facts to support any alleged "ongoing fraud" and other claims against the respondent. If a claimant cannot provide specific facts to support the alleged ongoing fraud and other claims that would somehow extend the eligibility, then the claims should be dismissed.

Fairness runs both ways. Requiring respondents to defend against nebulous and generalized allegations including generalized allegations of fraud is not fair. Currently, claimants' counsel can, and do, file frivolous and unsubstantiated claims knowing that firms have to defend and often will settle for less than the cost of defense.

3. Certain categories of claims and customer dispute should be subject to different procedural requirements under FINRA rules.

Complex, high value and/or cases involving institutional, qualified and/or accredited investors and holders of institutional accounts should be subject to different procedural requirements. There should be a rebuttable presumption for any of these claimants to overcome since each is deemed

under the law to be capable to making their own investment decisions and accepting the risk of loss. Yet, accredited investors, in particular, often do not take responsibility and instead know that there are considerable costs for firms to defend cases, especially those that involve due diligence. Many of these cases lack merit and have nothing to do with investor protection.

Among other things, typically these claims concern alleged misconduct by the issuers. When the issuers fail, the claimants bar automatically files cases against brokerage firms *regardless* of the economic factors that caused the failure. In claim after claim, they misstate what happened and claim that investors wanted low risk investments despite claimants being accredited investors and receiving private placement memoranda and other documents that highlighted the risks. Effectively, the FINRA forum has turned broker-dealers—who only receive a small amount of compensation while the issuer receives the invested funds—into insurers for wealthy investors that the law deems to be able to fend for themselves. It is a broken system.

B. Arbitrators should be required to meet minimum requirements and should receive substantive training.

Arbitrators should have some business knowledge and background along with at least a four-year college degree. FINRA should also provide substantive training on the securities industry and products. One of the issues IAA has seen on a regular basis is that certain FINRA arbitrators do not have a basic understanding of the securities industry and its products. Unfortunately, this lack of knowledge is especially true when dealing with complex products and/or cases involving institutional, qualified and/or accredited investors and holders of institutional accounts.

Arbitrators should have basic training with respect to investment categories and products as well as core legal concepts. No one expects the arbitrators to have in-depth knowledge about complex products, but a basic understanding about the securities industry and the various products is currently lacking. How can we expect arbitrators to understand the parties' positions and arguments without an informed basis for evaluation? It is unfair to all parties when arbitrators are tasked with deciding a matter when they have no basic knowledge about the industry or the products.

C. Discovery

1. Sanctions should be applied equally to all parties.

Although both parties are required to provide discovery documents, the sanctions are not enforced evenly. Respondents are required to produce the documents and are penalized, but claimants are often not penalized. We are aware of cases where Panels have issued Orders for the nonproduction of documents but then fail to impose sanctions, even when those Orders are violated multiple times. Claimants' counsel know that their client will not be penalized, so they delay producing documents to the detriment of respondent firms. Sanctions for discovery abuses should be imposed equally.

2. Requiring members to produce documents concerning the existence and extent of any insurance coverage serves no legitimate purpose.

The existence and extent of any insurance coverage is not relevant to the underlying facts of the case nor is it relevant to liability. Even if produced confidentially, the fact that claimants' counsel would now know which members have coverage and the extent of that coverage would paint a target on those firms that act responsibly to the exclusion of those firms who do not have coverage or have insufficient coverage.

D. FINRA should require explained decisions in all arbitration cases.

IAA believes that explained decisions would increase transparency and improve the quality of decision-making and consistency among awards. As the ability to vacate or appeal arbitration awards is very limited, explained decisions should have little to no impact on the finality of arbitration awards.

Arbitrators should be required to provide additional detail in explained decisions and should include the factual and legal basis for the decision and the award. Requiring explained decisions could have a positive impact on the efficiency of the program and lead to more consistency among awards.

E. Form U5 Defamation Claims

FINRA should protect investors and the integrity of CRD/BrokerCheck disclosures by encouraging accurate and complete Form U5 reporting, and by discouraging unfounded U5 defamation claims.

The regulatory need for the reporting of complete and accurate information to CRD should be protected so that a false statement made in good faith, without malice or recklessness would not be sufficient for an arbitration award. An associated person's belief that the reported information is untrue or misleading should not be sufficient for an arbitration award.

In the current environment, firms who are diligent in making accurate and complete U5 filings nevertheless face unfounded U5 defamation claims, and increasingly awards, for money damages in FINRA arbitration. The proliferation of these claims further incentivizes the filing of even more frivolous defamation actions, given the potential for large, yet unfounded awards. It also incentivizes firms to make their U5 disclosures as narrow, limited and bare bones as possible (but consistent with regulatory requirements) to minimize their legal exposure.

A simple solution to this issue is for FINRA to specifically grant member firms a qualified privilege defense to U5 defamation claims. Privilege defenses were created in recognition of the public policy that under certain circumstances it is more important for the law to promote open and honest communication, even if it is defamatory, than to provide the subject of potentially defamatory statements an avenue for recovery. Most, if not all, states recognize at least a qualified privilege that protects member firms from defamation lawsuits for any Form U5 statements made unless the person knew or should have known at the time that the statement was made, that it was

false in a material respect or the person acted in reckless disregard of the statement's truth or falsity. In other words, a false statement made in good faith, without malice or recklessness, is not defamatory. Note: New York provides absolute privilege for Form U5 statements.

Unfortunately, FINRA arbitrators often focus their awards on simply whether the Form U5 disclosures are inaccurate or false, and not whether the claimant can satisfy the elements of a defamation claim or whether any type of privilege applies under state law.

Adopting the qualified privilege standard and requiring that the alleged defamatory statement meets the legal standard for defamation would protect investors and the integrity of CRD/BrokerCheck disclosures by encouraging accurate and complete Form U5 reporting, and by discouraging unfounded U5 defamation claims.

IAA appreciates FINRA's commitment to modernizing the rules governing arbitration and solicit comments on these issues.

Respectfully submitted,

Myra P. Nicholson

Myra P. Nicholson, Esquire
General Counsel