

Promissory Note Proceedings

SEC Approves Rule Establishing Expedited Procedures for Arbitrating Promissory Note Cases

Effective Date: September 14, 2009

Executive Summary

Effective September 14, 2009, FINRA will begin expediting the administration of cases that solely involve a brokerage firm's claim that an associated person failed to pay money owed on a promissory note. Under the new procedures, a single public arbitrator from the roster of arbitrators approved to hear statutory discrimination claims will decide such promissory note cases. FINRA amended Rules 13214 and 13600 of the Code of Arbitration Procedure for Industry Disputes to make conforming changes.

The SEC approved new FINRA Rule 13806 and amendments to FINRA Rules 13214 and 13600 relating to promissory note proceedings.¹ The text of the rules is set forth in Attachment A, and will apply to all promissory note cases filed on or after the effective date.

Questions concerning this *Notice* should be directed to:

- Richard W. Berry, Vice President and Director of Case Administration, FINRA Dispute Resolution, at (212) 858-4307 or richard.berry@finra.org; or
- Margo A. Hassan, Counsel, FINRA Dispute Resolution, at (212) 858-4481 or margo.hassan@finra.org.

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Notice Type

- Rule Amendment

Suggested Routing

- Compliance
- Legal
- Registered Representatives

Key Topic(s)

- Arbitration
- Associated Person
- Code of Arbitration Procedure
- Dispute Resolution
- Promissory Note

Referenced Rules & Notices

- FINRA Rule 13806
- FINRA Rule 13214
- FINRA Rule 13600

Background & Discussion

FINRA is amending its Code of Arbitration Procedure for Industry Disputes (Industry Code) to establish new procedures for administering cases that solely involve a firm's claim that an associated person failed to pay money owed on a promissory note. In the absence of additional allegations by firms or associated persons, promissory note cases involve straightforward contracts with few documents entered into evidence. Rule 13806 is limited to claims related to promissory notes with no additional allegations being made in the Statement of Claim. Rule 13806 provides that a single public arbitrator from the roster of arbitrators approved to hear statutory discrimination claims will serve on the arbitration panel hearing a promissory note case. FINRA is also amending Rules 13214 and 13600 of the Industry Code to make conforming changes.

The new procedures streamline the process for administering promissory note cases and reduce expenses for the parties while maintaining the procedural safeguards in the Industry Code for the associated person against whom a brokerage firm asserts a claim.

Specifically, under the new procedures:

- ▶ Parties choose a single public arbitrator from the roster of arbitrators approved to hear statutory discrimination claims. FINRA believes that the arbitrators on this roster are especially suited to resolve these disputes because of the depth of their experience and their familiarity with employment law.²
- ▶ If the associated person does not file an answer, simplified discovery procedures will apply and, regardless of the amount in controversy, the single arbitrator will render an award based on the pleadings and other materials submitted by the parties.
- ▶ If the associated person files an answer (but does not seek any additional relief or assert any counterclaims or third party claims), regular discovery procedures will apply and, regardless of the amount in controversy, the single arbitrator will hold a hearing.
- ▶ If the associated person files a counterclaim or third party claim, then regular discovery procedures will apply and the number of arbitrators will be based on the amount of the counterclaim or third party claim. If the counterclaim and/or third party claim is not more than \$100,000, exclusive of interest and expenses, the Director will appoint a single public arbitrator from the roster of arbitrators approved to hear statutory discrimination claims. If the counterclaim and/or third party claim is more than \$100,000, then the Director will appoint a three-arbitrator panel comprised of one public arbitrator from the roster of arbitrators approved to hear statutory discrimination claims who would serve as chairperson, one arbitrator from the public roster and one arbitrator from the non-public roster. If the counterclaim or third party claim is filed after the single arbitrator is appointed, and a three-arbitrator panel is required, the Director will retain the appointed arbitrator as chair and appoint two additional arbitrators (one public and one non-public arbitrator) to the panel.

Rule 13806(f) provides that FINRA will pay an arbitrator an honoraria of \$125 for each arbitration in which the associated person does not file an answer and the award is based on the arbitrator's review of the pleadings and other materials submitted by the parties. As these are expedited proceedings, FINRA is amending Rule 13214 (Payment of Arbitrators) to reflect that FINRA will not pay an honoraria for resolving a discovery-related motion without a hearing session or for resolving a contested motion concerning issuance of a subpoena without a hearing session. In instances where full discovery is conducted under the 13500 series of rules, FINRA will pay the honoraria prescribed in Rule 13214 for deciding these motions.

FINRA is also amending Rule 13600 (Required Hearings) to reflect that a hearing will not be held if the associated person does not file an answer. In such cases, the arbitrator will render the award on the pleadings and other materials submitted by the parties.

The amendments become effective on September 14, 2009, and apply to all arbitration cases filed on or after the effective date.

Endnotes

- 1 Exchange Act Release No. 60132 (June 17, 2009), 74 Federal Register 30191 (June 24, 2009) (File No. SR-FINRA-2009-015).
- 2 See Rule 13802(c)(3). These specially qualified arbitrators are attorneys familiar with employment law and who have at least ten years of legal experience. In addition, the arbitrator may not have represented primarily the views of employers or employees within the last five years. "Primarily" means 50 percent or more of the arbitrator's business or professional activities within the last five years.

Attachment A

New language is underlined; deletions are in brackets.

Code of Arbitration Procedure for Industry Disputes

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13806. Promissory Note Proceedings

(a) Applicability of Rule

This rule applies to arbitrations solely involving a member's claim that an associated person failed to pay money owed on a promissory note. To proceed under this rule, a claim may not include any additional allegations. Except as otherwise provided in this rule, all provisions of the Code apply to such arbitrations.

(b) Number of Arbitrators

(1) The Director will appoint one arbitrator if:

- the associated person does not file an answer;
- the associated person files an answer but does not allege any counterclaims or third party claims; or
- the associated person files an answer which includes any counterclaims or third party claims requesting money damages, and the amount of the counterclaims or third party claims is not more than \$100,000, exclusive of interest and expenses.

(2) The Director will appoint three arbitrators if the associated person files any counterclaims or third party claims and the amount of the counterclaims or third party claims is more than \$100,000, exclusive of interest and expenses, or is unspecified, or if the counterclaims or third party claims do not request money damages.

(c) Composition of Panel

(1) If the panel consists of one arbitrator, the arbitrator will be a public arbitrator qualified to resolve a statutory discrimination claim as set forth in Rule 13802(c)(3).

(2) If the panel consists of three arbitrators, one arbitrator will be a public arbitrator who meets the qualifications in Rule 13802(c)(3); one arbitrator will be selected from the roster of public arbitrators; and one arbitrator will be selected from the roster of non-public arbitrators. The arbitrator who meets the criteria in Rule 13802(c)(3) will serve as the chairperson of the panel.

(3) If the Director appoints a panel pursuant to (c)(1) above, and an associated person subsequently files a counterclaim or third party claim that requires appointment of a three-arbitrator panel, the appointed arbitrator will remain on the panel, and will serve as chairperson. In addition, one arbitrator will be selected from the roster of public arbitrators; and one arbitrator will be selected from the roster of non-public arbitrators.

(d) Discovery

(1) If the associated person does not file an answer, discovery will be conducted under Rule 13800(d) concerning Simplified Arbitration.

(2) If the associated person files an answer, discovery will be conducted under the 13500 series of rules.

(e) Hearings

(1) If the associated person does not file an answer, no initial prehearing conference or hearing will be held, and the arbitrator will render an award based on the pleadings and other materials submitted by the parties.

(2) If the associated person files an answer, a hearing will be held. If a hearing is held, the regular provisions of the Code relating to prehearing conferences and hearings, including fee provisions and payment of arbitrators, will apply.

(f) Arbitrator Honoraria

FINRA will pay the arbitrator an honorarium of \$125 for each arbitration administered under paragraph (e)(1).

13214. Payment of Arbitrators

(a) Except as provided in paragraph (b), [and] Rule 13800, and Rule 13806(f), FINRA will pay the panel an honorarium, as follows:

- \$200 to each arbitrator for each hearing session in which he or she participates;
- an additional \$75 per day to the chairperson for each hearing on the merits;
- \$50 for travel to a hearing session that is postponed pursuant to Rule 13601; and
- \$100 for each arbitrator if a hearing session other than a prehearing conference is postponed within three business days before a scheduled hearing session pursuant to Rules 13601(a)(2) and (b)(2).

(b) The Director may authorize a higher or additional honorarium for the use of a foreign hearing location.

(c) Payment for Deciding Discovery-Related Motions Without a Hearing Session

(1) FINRA will pay each arbitrator an honorarium of \$200 to decide a discovery-related motion without a hearing session. This paragraph does not apply to cases administered under Rule 13800 or pursuant to Rule 13806(d)(1).

(2) – (3) No Change.

(d) Payment for Deciding Contested Subpoena Requests Without a Hearing Session

(1) The honorarium for deciding one or more contested motions requesting the issuance of a subpoena without a hearing session shall be \$200. The honorarium shall be paid on a per case basis to each arbitrator who decides the contested motion(s). The parties shall not be assessed more than \$600 in fees under this paragraph in any arbitration proceeding. The honorarium shall not be paid for cases administered under Rule 13800 or pursuant to Rule 13806(d)(1).

(2) – (3) No change.

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13600. Required Hearings

(a) Hearings will be held, unless:

- The arbitration is administered under Rule 13800, [or] Rule 13801, or Rule 13806(e)(1);
- The parties agree otherwise in writing; or
- The arbitration has been settled, withdrawn or dismissed.

(b) – (c) No change.

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