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Mission Statement

We publish *The Neutral Corner* to provide arbitrators and mediators with current updates on important rules and procedures within securities dispute resolution. FINRA's dedicated neutrals better serve parties and other participants in the FINRA forum by taking advantage of this valuable learning tool.

Curveballs: Unexpected Situations That Arise During a Hearing

By Julie Jason



FINRA arbitrators who serve as chairpersons bear an added responsibility during the hearing. Not only do they need to understand the applicable rules and procedures, they also need to set the right tone and manage the parties' behavior—all while remaining fair, impartial and judicious. For this reason, we are republishing the following article authored by Julie Jason, and originally published in Volume 5—2008 of this newsletter.

Curveballs are intended to surprise. A batter does not have much time to adjust to a ball that loses trajectory after he begins to swing. In an arbitration hearing, parties' representatives can sometimes pitch curveballs to the chairperson inadvertently—or purposefully—to gain tactical advantage over an opponent. The chairperson must be alert to curveballs and address them with strength and conviction, while balancing the goal of fairness. Parties have a right to a fair hearing, and the chairperson must not allow any behavior that distracts from that objective.

The secret is to be prepared for surprises and to know how to deal with them. They may be anything out of the ordinary, including a misstep by parties, parties' representatives, witnesses or other panelists. This article will review some possible curveballs and provide suggestions for addressing them.

The Sidebar Discussion

Sometimes a party's attorney and an associate engage in a private discussion during the testimony of a witness, which can be distracting to the witness, opposing counsel and panel. The chairperson should ask counsel to cease the conversation and if counsel does not comply, the chairperson should call a recess. The panel should excuse the parties and the witnesses and advise counsel that if such behavior continues, the panel may ask the associate to leave the hearing room.

Year-End Message to Neutrals

FINRA is proud to provide dispute resolution services to the securities community—investors, broker-dealers and their employees. We could not provide the fair and impartial forum that FINRA has become known for without our dedicated arbitrators. Each of you is an integral part of the dispute resolution process at FINRA. We value the commitment and skill you bring to the process, and we want to thank you for your dedicated service in 2011 and wish you a very happy new year.

The Unprepared Advocate

Occasionally, party representatives may be distracted or have difficulty organizing their cases at the hearing for any number of reasons; for example, a missed train or traffic delay. The chairperson should be alert to these types of situations and call a short recess to allow counsel to organize their presentations for the hearing to proceed.

If, however, a faltering presentation is due to lack of preparation, there is no perfect solution. This creates a significant problem for the other parties and is an imposition on the panel, as it tries to understand the elements of each party's case. In such instances, it may help to have a conference with both counsel to discuss how they plan to present their case to determine the best way to proceed.

The Zealous Advocate

Zealous advocates may have their clients' best interest at heart. However, an advocate who conducts hostile cross-examinations, interrupts witnesses with "speaking objections," interrupts counsel or asks leading questions on direct examination, does little to advance a party's case. The chairperson should control these situations before they escalate into an unproductive hearing. The chairperson should ask the parties to focus on the facts by presenting testimony and evidence without getting bogged down in histrionics.

Allegations of Arbitrator Bias

More serious curveballs may challenge the impartiality of the panel. For example:

1. After the parties accept the panel and the hearing is underway, counsel questions the composition of the panel and suggests that one of the arbitrators has a conflict, but refuses to identify the arbitrator or the conflict. (Arbitrators will find it helpful to read [Volume 4—2011 of *The Neutral Corner*](#).)
2. An attorney objects to an arbitrator's questions, comments or demeanor and remarks that, "One of the panelists smiled from time to time on the first day of testimony." The attorney may refer to this occurrence as evidence of arbitrator bias, showing that the arbitrator agreed with the testimony and ostensibly with the presenting party's case at the outset of the hearing.

The chairperson should not try to guess *which* undisclosed panelist is the subject of the attorney's objection. An effective chairperson will want to clear the air—by removing witnesses and parties from the hearing room—and direct counsel to state the objection with specificity, finding out if counsel is requesting that the particular panelist recuse himself/herself. If, instead, a party is challenging an arbitrator for failure to disclose a conflict at the time of appointment, counsel may file a request with the Director of FINRA Dispute Resolution to remove the panelist.¹

If counsel is unable to clearly state how he/she would like to proceed, the panel should give counsel the opportunity to withdraw the objection, and move forward with the hearing. While it is important to note that a sole allegation of appearance of bias is probably insufficient to establish evident partiality, the panel should always take an objection seriously because it could result in the appearance of bias.

Allegations of Bias in the Arbitration Process

Another serious curveball is a challenge to the process itself, as in the following examples.

1. Counsel states during closing statements that his client did not have a fair hearing. Counsel may have a valid ground for filing a motion to vacate the award; therefore, the panel should take this allegation seriously. The panel should ask counsel to place his/her objections on the record and seek details about why the party does not believe that he/she had a fair hearing.

Generally, it is difficult for a party to successfully overturn a panel's award. The arbitration process is founded on a contract (opting out of the court system into a non-judicial forum); therefore, the courts do not "allow a disappointed party to bring his dispute into court by the back door, arguing that he is entitled to appellate review of the arbitrators' decision."²

2. The courts may, however, vacate an award if a party presented clearly applicable law to the arbitrators and the arbitrators nevertheless chose to disregard it.³ Some lawyers may declare that it would be a manifest disregard of the law if the panel rules against their client.

The chairperson should ask counsel to explain his/her position and the reasoning behind such a conclusion—that the arbitrators knew the law and disregarded it. Opposing counsel should be given an opportunity to respond.

Message From the Editor

We are changing the publication frequency of *The Neutral Corner* (TNC). Currently, TNC is published on a bi-monthly basis, resulting in six issues each year. Starting in 2012, we will be publishing TNC on a quarterly basis. Each of the four issues will be published at the end of each quarter.

Comments, Feedback and Suggestions

Please send your suggestions and comments to:

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The chairperson may also request posthearing briefs on the issue. The panel should keep in mind that arbitration is a forum of equity in which arbitrators are committed to serve justice as they deem appropriate for particular factual situations. Their evaluation of the facts will not generally be second-guessed by the courts.

Conclusion

While a chairperson cannot be prepared for every surprise that comes up, he/she should expect the unexpected. Within this context, it is imperative to remember that there are two sides to every controversy, and that fairness is paramount during an arbitration proceeding. When faced with a curveball, the chairperson should exert dignified, but firm, leadership and ensure that all sides are treated fairly.

The views expressed in this article are solely the views of the author and do not necessarily reflect the views or policies of FINRA.

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Endnotes

- 1 Code of Arbitration Procedure Rules 12407 and 13407 provide that, after the first hearing session begins, the director may remove an arbitrator based only on information required to be disclosed under Rules 12405 and 13405 that was not previously known by the parties when the arbitrator was selected. This provision is intended to prevent parties from raising challenges late in the process that could have been raised at the outset. Rules 12407 and 13407 also provide that the director's authority under this subparagraph may only be exercised by the director or by the president of FINRA Dispute Resolution.
- 2 *Baravati v. Josephthal, Lyon & Ross, Inc.*, 28 F.3d 704, 706 (7th Cir. 1994).
- 3 This non-statutory, "common law" ground for judicial review is an exception to the four statutory grounds for review under §10 of the Federal Arbitration Act (FAA). Since the Supreme Court case, *Hall Street Associates v. Mattel*, 552 U.S. 52 (2008), the courts have been split on the viability of manifest disregard as a ground for vacating an arbitration award.

Dispute Resolution and FINRA News

Case Filings and Trends



Arbitration case filings from January through November 2011 reflect a 17 percent decrease compared to cases filed during the same 11-month period in 2010 (from 5,242 cases in 2010 to 4,359 cases in 2011). Customer-initiated claims decreased by 19 percent through November 2011, as compared to the same time period in 2010.

From January through November 2011, arbitration cases filed identified the following securities (listed in order of decreasing frequency): common stock, mutual funds, preferred stock, annuities, options, corporate bonds, variable annuities, limited partnerships, auction rate securities, derivative securities and certificates of deposit. The top two causes of action alleged were breach of fiduciary duty and negligence.

Update on the Optional All Public Panel Rule

On February 1, 2011, FINRA implemented the Optional All Public Panel rule, which permits customers to have a panel consisting of three public arbitrators rather than two public and one non-public arbitrator. From February 1 through November 30, there have been 2,353 eligible cases filed under the Optional All Public Panel rule. Customers in 76 percent of eligible cases have chosen the all public panel option. Customers choosing the all public panel option have chosen to rank one or more non-public arbitrator on the list in 34 percent of the cases (421 of the 1,234 cases) in which parties have completed the ranking process. Customers in 14 percent of cases proceeding under the all public panel option have ranked four or more non-public arbitrators. For more information about the Optional All Public Panel rules, please review the [Notice to Parties—New Optional All Public Panel Rules](#) on our website.

Updated Hearing Scripts with Additional Disclosure Guidance

We recently updated the [Initial Prehearing Conference](#) and regular hearing scripts ([single arbitrator](#) and [three-member](#) panels) to emphasize the importance of the arbitrator's ongoing duty to disclose actual and potential conflicts of interest. We encourage arbitrators to review the revised scripts as they prepare to conduct upcoming hearings.

Increase in Meal Allowance for Arbitrators

Effective January 1, 2012, FINRA will increase the meal allowance for arbitrators from \$20 to \$25 for most reimbursement categories for expenses incurred on or after January 1, 2012. FINRA will publish the updated [Guidelines for Arbitrator Reimbursement](#) before the new rates go into effect in January.

Updated: New Account Application Template

FINRA recently updated the [New Account Application Template](#) to reflect FINRA's new suitability rule. Designed for firms to use when creating their own account applications, this voluntary template uses plain English to highlight key disclosures and related investor education information. Arbitrators may expect to see this new form as they serve on upcoming arbitration cases.

SEC Rule Filing

Whistleblower Claims in Arbitration

On November 21, 2011, FINRA filed with the Securities and Exchange Commission (SEC), a proposal to amend Rule 13201 of the Code of Arbitration Procedure for Industry Disputes (Industry Code). The proposed amendment provides that disputes arising under a whistleblower statute that prohibit the use of a predispute arbitration agreement would not be required to be arbitrated. The proposal would align the rule with statutes, such as The Dodd-Frank Wall Street Reform and Consumer Protection Act that would invalidate predispute arbitration agreements for whistleblower claims.

The notice was published in the *Federal Register* on December 6. The comment period ends on January 3, 2012. Please visit our website for more information about [FINRA-2011-067](#).



Questions and Answers

Promissory Note Cases

Question: I was recently assigned to a promissory note case in which the respondent did not submit an answer. Are there special procedures I should follow?

Answer: Yes. Because the respondent did not file an answer, simplified discovery procedures outlined in [FINRA Rule 13800\(d\)](#) will apply; and regardless of the amount in controversy, you as the single arbitrator assigned to the case, will render an award based on the pleadings and other materials submitted by the parties. No hearing will be held. If you need additional documentary information from the parties to render your decision, contact the staff member assigned to the case. Do not contact the parties directly.

When you are ready to render your decision, you should complete the [Promissory Note Case Checklist](#) (rather than the usual Award Information Sheet). When completing the Promissory Note Case Checklist, please keep in mind the following:

- You must answer each of the eight questions. Some of the subparts are mutually exclusive so you may need to answer only one of the questions.
- If you award interest, you must state when the interest begins to accrue and when it ceases to accrue. For example, you might award “5 percent interest per annum from January 1, 2010, to January 1, 2011, or from January 1, 2010, until the date of payment of the award.”
- If you award punitive damages, you must include the basis for the award of punitive damages. If you need additional information to determine the basis for the punitive damage award (*e.g.*, case law or federal or state statute), you should ask the parties to brief the issue to help you determine whether both factual and legal bases exist for the punitive damage award.
- If you award attorneys’ fees, you must specify the amount as well as the legal authority for the attorneys’ fees award. Examples of the authority you may cite include federal or state statutes and attorneys’ fees provisions which may be contained in the promissory note.

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, you will hold a hearing.

Please review [*Regulatory Notice 09-48*](#) for further guidance on procedures for promissory note cases.

Arbitrator Immunity From Liability

Question: Can I be held liable for actions taken while serving as an arbitrator in FINRA arbitrations?

Answer: No. Arbitrators have immunity from civil liability that may arise out of their conduct as arbitrators. With respect to testimony, arbitrators generally have a quasi-judicial privilege from discussing the basis for a decision. The arbitrator's immunity from post-award questioning can be waived, however, if an arbitrator voluntarily discusses the case and discloses his or her reasoning, or discloses communications that occurred with other panel members, to someone outside of the arbitration panel. Breaching confidentiality not only waives the protection for that arbitrator, but it may also waive protection for the other panel members, even if they did not breach confidentiality. Problems concerning arbitrator confidentiality seldom arise; however, should such a problem occur, FINRA will provide legal representation to arbitrators who are sued or subpoenaed for actions that arise from their service on an arbitration case.

Arbitrators are not, however, immune from liability for criminal misconduct that is punishable by law, such as fraud or corruption. Arbitrators can be liable for acts they commit while serving as arbitrators that are not related to their roles as arbitrators, and FINRA will not provide representation under these circumstances.

For additional information about arbitrator confidentiality and immunity, please review the article, "[Maintaining Arbitrator Confidentiality](#)" in the April 2007 issue of *The Neutral Corner*.

Mediation Update



From January through November 2011, parties initiated 631 mediation cases. FINRA also closed 707 mediation cases during the same 11-month period. Approximately 82 percent of these cases concluded with successful settlements, and the average case turnaround time was 97 days.

Mediation Settlement Month

FINRA hosted its annual Mediation Settlement Month event during October, offering incentives designed to promote mediation and to educate potential parties about the benefits of the program. The majority of mediators on FINRA's roster agreed to reduce their normal fees for Mediation Settlement Month, allowing FINRA to offer substantial savings to parties. This year, more than 80 mediation cases were filed during Mediation Settlement Month.

Mediation Settlement Day

The 11th annual Mediation Settlement Day took place on October 20, 2011, with a kick-off event on October 18, at the New York City Bar Association. Mediation Settlement Day is an annual event designed to raise awareness about the benefits of mediation and to provide resources to parties. Organizations coordinate efforts to promote mediation on the same day each year. On this day and throughout the month of October, organizations conduct special programs to encourage parties to try mediation for the first time and to reinforce its value and effectiveness to those who have benefitted from it before.

Mediation Outreach Efforts

Mediation staff visited the new Investors Rights Clinic at the University of Miami School of Law in preparation for the opening in January 2012. Staff also lectured at the Albany Law School Securities Arbitration Clinic and conducted mock mediations and arbitrations at St. John's Law School Securities Arbitration Clinic and at Florida International University Law School's Investor Advocacy Clinic.

Arbitrator Training



Arbitrator Disclosure

Arbitrator disclosure is essential to maintaining the integrity of the arbitration process. To ensure that arbitrators have ample guidance on how to make proper and timely disclosures, we are providing the following training opportunities.

Neutral Workshop: Arbitrator Disclosure

The October 31 Neutral Workshop provides an overview of arbitrator disclosure. Workshop faculty Kenneth Andrichik, Senior Vice President, Chief Counsel and Director of Mediation and Strategy, and Barbara Brady, Vice President and Director of Neutral Management, discuss:

- when disclosure is required;
- examples of the information and circumstances to disclose; and
- consequences for not disclosing information.

The following links are referenced during the workshop:

- [Arbitrator Information Update Form](#)
- [Volume 4—2011 of *The Neutral Corner*](#)
- [The Code of Arbitration Procedure](#)
- [The Arbitrator’s Guide](#)
- [Initial Prehearing Conference Arbitrator’s Script](#)
- [Hearing Procedure Script](#)

Please send any questions or comments to FINRADRcall-inworkshop@finra.org.

Note: FINRA’s neutral workshops are pre-recorded, which allows neutrals to pause and playback the audio file.

Updated Arbitrator Disclosure Checklist

To better facilitate arbitrator disclosure, we recently updated the [Arbitrator Disclosure Checklist](#) that all arbitrators must complete, with the Oath of Arbitrator, at the outset of cases on which they are serving. The checklist ensures that you have considered all possible disclosures and have provided a complete explanation of any possible conflict to the parties.

Below is a summary of the changes we made to the checklist. We clarified the questions by:

- using more straight-forward and consistent language;
- grouping the questions by topic and providing a road map; and
- adding new questions to seek information about name changes, non-securities accounts, opinions formed about the case, ongoing relationships with former firms, current litigation or arbitration, unsatisfied judgments or liens and any additional disclosure not captured by the questions.

We hope that the updated checklist will provide greater clarity about your duty to disclose. Please contact your assigned staff member if you have any questions about arbitrator disclosure.

New and Improved Online Arbitrator Training: Your Duty to Disclose

We created a new and improved version of our online arbitrator training course on disclosure to provide additional guidance on proper disclosure. The new course is available on FINRA's [Learning Management System](#).

Even if you successfully completed the previous version of the disclosure course, we strongly encourage you to complete the new course, which provides additional valuable information not available in the previous course.

The disclosure course—like all of FINRA Dispute Resolution's [online arbitrator courses](#)—is available free of charge, and completion of the course will be noted on your Arbitrator Disclosure Report.

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