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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.

Arbitrator Best Practices for the Prehearing Phase

By Scott Carfello, Associate Vice President and Regional Director for the Midwest Region, FINRA Dispute Resolution



The Dispute Resolution Section of the New York State Bar Association has published guidance to help arbitrators as they navigate an increasingly complex and costly prehearing phase. Although FINRA arbitrations are governed by the Code of Arbitration Procedure, much of the guidance provided in the brochure—[Guidelines for the Arbitrator's Conduct of the Pre-Hearing Phase of Domestic Commercial Arbitrations and Guidelines for the Arbitrator's Conduct of the Pre-Hearing Phase of International Arbitrations](#)—transcends the rules of any one forum and focuses on practical, common-sense tactics arbitrators can use to increase efficiency. This article touches briefly on some of the key guidelines and how they can be applied to FINRA arbitrations.

Good Judgment

The brochure emphasizes that there is no one correct approach to arbitration, as each case is different. Fundamental to any arbitration, however, is the experience and judgment of the arbitrator. Although FINRA provides the structure for the arbitration process, arbitrators and their decisions, demeanor and treatment of the parties are crucial for success. Arbitrators must adapt to the unique circumstances and facts of each case.

Discovery

The brochure also focuses on discovery and specific discovery devices. The brochure urges arbitrators to set “ambitious hearing dates and aggressive interim deadlines” for discovery and to strictly enforce these deadlines. As FINRA arbitrators know, discovery plays a big role in FINRA's prehearing phase. The discovery rules ([12505-12514](#)) under the Code explicitly state that parties should cooperate to the fullest extent practicable and review the [FINRA Discovery Guide](#).¹ The Discovery Guide contains lists of documents that parties should exchange without the intervention of the arbitrators and FINRA. However, discovery issues arise, and the brochure advises arbitrators to set limits and keep the process moving.

Comments, Feedback and Suggestions

Please send your suggestions and comments to:

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The brochure specifically addresses depositions—testimony taken under oath before the hearing and presented at the hearing in lieu of live testimony. It recognizes that depositions can be costly, and not necessary in every case. For those cases where arbitrators believe depositions would be appropriate, a brief sample order is referenced. At FINRA, depositions are used in only limited situations under [Rule 12510](#). While the brochure's guidance is not determinative in FINRA arbitrations, arbitrators may review this section and consider its utility.

One newer area for discovery issues is electronic discovery or e-discovery. The brochure provides a brief overview of e-discovery and its potential issues and includes some possible language for e-discovery orders. FINRA is considering specific changes to the Discovery Guide on e-discovery to guide arbitrators and parties.

Specific Motions

Another issue the brochure discusses is specific motions that arise before the hearing, particularly adjournments and dispositive motions. The brochure provides guidance and factors to consider when addressing these challenging issues. In particular, the segment on dispositive motions acknowledges the potential cost and delay of dispositive motions but also points out the possible benefits to focused motions. The guide suggests that parties submit a brief summary of any dispositive motion before the arbitrators will consider the motion. Dispositive motions in FINRA arbitrations are addressed in FINRA [Rules 12504](#) and [12206](#) and were developed to bring consistency when parties file dispositive motions and limit potential abuses of the motion process.

Conclusion

In some instances, the guidance in the brochure may not apply to FINRA arbitration and should not be followed in lieu of FINRA rules and procedures. Overall, the brochure provides practical advice to arbitrators in any dispute resolution forum and addresses key issues that are common to most arbitrations. Arbitrators can review the entire brochure on the New York State Bar Association website.

Endnote

- 1 The Discovery Guide is being reviewed by FINRA's Discovery Task Force to update relevant sections and include guidance on new areas. On June 3, 2013, FINRA filed a proposed amendment ([SR-FINRA-2013-024](#)) to the Discovery Guide to provide general guidance on electronic discovery (e-discovery) issues and product cases. Please see Rule Filings under DR News.

To reinforce the importance of disclosure, FINRA recently sent a broadcast email to arbitrators reminding them to consider all aspects of their professional and personal lives when making disclosures. The notice included a reminder to disclose relationships involving broker-dealers, memberships in professional organizations and disclosures concerning the nature of a case.

Are You Forgetting to Make Necessary Disclosures?

Barbara L. Brady, Vice President and Director of FINRA Neutral Management



As we have stated previously in [The Neutral Corner](#), arbitrator disclosure is the cornerstone of FINRA arbitration. Arbitrators must reflect on all aspects of their professional and personal lives when considering disclosures, keeping in mind that disclosures can arise from any relationship or experience that may affect an arbitrator's ability to be impartial. However, the disclosure standard does not end there: Arbitrators must not only be impartial in fact, but must also *appear* to be impartial. Parties must believe an arbitrator is able to render a fair decision.

Consider the Subject Matter and the Nature of the Claim

When making disclosures, arbitrators should consider all aspects of their professional and personal lives. Most arbitrators know they must disclose all ties between or among themselves, the parties, the parties' representatives and witnesses. But, did you know that arbitrators must also consider the nature of the matter in dispute and the causes of action claimed?

For example, suppose you are serving on an arbitration case that alleges breach of fiduciary duty and you were recently named as a party in a civil action, having nothing to do with securities, which also alleged breach of fiduciary duty. Would you need to disclose this to FINRA? The answer is yes.

The fact that both the civil action you are personally involved in and the arbitration case contain the same type of allegation is material and must be disclosed, even if the subject matter of each case is very different. Failure to make this type of disclosure has been successfully asserted to vacate an arbitration award.

For example, a California superior court vacated the FINRA arbitration award in *Larry Hagman et al. v. Citigroup Global Markets, Inc.* because the arbitrator failed to disclose that two years earlier he had been involved in a dispute alleging breach of fiduciary duty—the same allegation claimed in the arbitration case to which the arbitrator had been assigned.¹

Consider the Nature of Your Professional Practice, Your Clients and Your Professional Associations

When you applied to FINRA's arbitrator roster, you were required to disclose all known conflicts/disclosures and the nature of these conflicts/disclosures. For example, the arbitrator application required you to disclose any work performed for, or against, broker-dealers, the date of such work and whether such work is ongoing or has concluded. You were also asked to disclose all of your professional associations.

Given that you agreed to fulfill your continuing obligation to make updates and disclosures, have you recently considered the following questions from the application?

- Have you ever represented or served as counsel for a broker-dealer in an arbitration, litigation, or other matter? If so, please list the broker-dealer(s).
- Have you ever represented or served as counsel for a party adverse to a broker-dealer in an arbitration, litigation, or other matter? If so, please list the broker-dealer(s).
- Are you, or were you previously, a member of any professional organization (include bar associations)? If so, please list the organizations.

Answers to these questions are, by nature, fluid and frequently changing. Accordingly, these are often the hardest disclosures to keep current. However, it is your responsibility as a FINRA arbitrator to make all reasonable efforts to consider these questions and to keep your Arbitrator Disclosure Report up-to-date.

Involvement in Social Media

Finally, arbitrators were required in their application to disclose their publications, including books, articles, blogs, Twitter feeds and other such forms of social media. Given our fast-paced digital world, have you remembered to disclose your latest publications?

Many parties conduct extensive research on potential arbitrators during the arbitrator selection process, and **after** an arbitrator renders the award. It is not uncommon for parties to research arbitrators through online search engines such as Google to review websites associated with an arbitrator and/or an arbitrator's employer and search social media sites. Accordingly, arbitrators should strive for consistency between their publicly available information and the information they provide in their Arbitrator Disclosure Report.

As a reminder, if you are active on social media websites, such as Facebook, Twitter or LinkedIn, you should not correspond with anyone connected to an arbitration case to which you are, or have been, assigned. You should not add attorneys or parties who have appeared before you in an arbitration case as "friends" or "connections."

Conclusion

For additional information on arbitrator disclosure, and for information on how to update your Disclosure Report, please see the [Arbitrator Disclosure](#) section of our website or contact the [Department of Neutral Management](#).

Endnote

- 1 *Larry Hagman et al. v. Citigroup Global Markets, Inc.*, No. BS128800, 2011 WL 975535 (Cal. Superior Feb. 9, 2011) (Trial Order).

Dispute Resolution and FINRA News

Case Filings and Trends



Arbitration [case filings](#) from January through May 2013 reflect a 20 percent decrease compared to cases filed during the same five-month period in 2012 (from 2,003 cases in 2012 to 1,604 cases in 2013). Customer-initiated claims decreased by 14 percent through May 2013, as compared to the same time period in 2012.

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

Resources for Investors Representing Themselves in FINRA Arbitrations and Mediations

FINRA has created a [resource page](#) for investors representing themselves in FINRA arbitrations and mediations. The Web page consolidates information and tools helpful to self-represented investors.

Financial Capability Survey

The FINRA Investor Education Foundation released results of America's [State-by-State Financial Capability Survey](#). The Survey was developed in consultation with the U.S. Department of the Treasury, other federal agencies and the President's Advisory Council on Financial Capability to compare the financial capabilities of Americans across all 50 states and the nation as a whole. The data were collected through an online survey of 25,509 American adults (approximately 500 per state, plus D.C.), over a four-month period, July – October 2012.

PLI Securities Arbitration 2013

On August 1, FINRA will participate in the Practising Law Institute's (PLI) Securities Arbitration 2013 program. The program will feature FINRA staff, FINRA arbitrators, noted academics and experienced attorneys who represent both customers and industry parties. Among other topics, the

program will discuss tips for practicing in FINRA's forum, proposed changes to FINRA's arbitration rules and enhancements to the arbitration hearing process.

Please visit [PLI's website](#) for more information about the Securities Arbitration 2013 program.

Securities Arbitration & Mediation Hot Topics 2013

On June 4, FINRA participated on the panel at the Securities Arbitration Mediation Hot Topics program at the New York City Bar Association. The panel of experienced practitioners and senior representatives from FINRA examined rule changes and provided practical advice on arbitrating and mediating claims at FINRA.

American Bar Association

In April, FINRA participated in a panel discussion on ethics in securities arbitration and mediation during the ABA's Section of Dispute Resolution Spring Conference held in Chicago, IL.

SEC Rule Filings

One Panel Composition Method

On June 3, 2013, FINRA filed two proposed rule changes with the Securities and Exchange Committee (SEC). The first filing proposed an amendment to Rule 12403 regarding panel composition in customer cases with three arbitrators. Under the proposed rule change, FINRA would no longer require a customer to elect a panel selection method, and parties in all customer cases with three arbitrators would get the same selection method. FINRA would provide all parties with lists of 10 chair-qualified public arbitrators, 10 public arbitrators, and 10 non-public arbitrators and permit them to strike four arbitrators on the chair-qualified public list and on the public list. However, any party could select an all-public arbitration panel by striking all of the arbitrators on the non-public list.

Please visit FINRA's website for more information about [SR-FINRA-2013-023](#).

Discovery Guide to Include General Guidance on Electronic Discovery and Product Cases

The second proposal would amend the Discovery Guide used in customer arbitration proceedings to provide general guidance on electronic discovery (e-discovery) issues and product cases and would clarify the existing provision relating to affirmations made when a party does not produce documents specified in the Guide.

Please visit FINRA's website for more information about [SR-FINRA-2013-024](#).

SEC Rule Approval

Amendment to FINRA's Customer and Industry Codes of Arbitration Procedure to Revise the Public Arbitrator Definition

Effective July 1, 2013, the definition of public arbitrator will exclude persons associated with a mutual fund or hedge fund from serving as public arbitrators and will require individuals to wait for two years after ending certain affiliations before they may be permitted to serve as public arbitrators. FINRA believes that the amendments to the public arbitrator definition will improve investors' perception about the fairness and neutrality of FINRA's public arbitrator roster.

We urge arbitrators to review the amended definition in [Rules 12100\(u\)](#) and [13100\(u\)](#) and [Regulatory Notice 13-21](#) to determine if the changes affect your ability to serve on FINRA's arbitrator roster.

Public Arbitrator Survey

To ensure that FINRA properly classifies arbitrators in accordance with the amended public arbitrator definition, we are surveying some members of our public arbitrator roster. Note that we did not send the survey to every public arbitrator on our roster. The survey requires arbitrators to answer several questions regarding their potential affiliations with hedge funds and mutual funds as well as the timeframe in which they were associated with entities involved in the securities business. Arbitrators who receive this survey must complete and return it by July 1 in order to remain active on the roster.

Please visit our [website](#) for more information about these amendments to the public arbitrator definition.



Questions and Answers

DR Portal

Question I received an invitation to the DR Portal. Should I register now?

Answer Yes. You should register with the portal as soon as possible. Currently, neutrals can review and update their profile information, print their disclosure reports, view the status and details of their cases and view a history of case assignments and honorarium earned. This fall, the portal will include even more enhancements for case management.

When the new enhancements become available, neutrals will be able to view case documents in the portal, allowing them to immediately access time-sensitive documents. They will also be able to schedule prehearings and regular hearings in the portal. By registering early and becoming accustomed to the portal, you will be prepared to take advantage of the portal's efficiencies.

407 Letters

Question I am trying to open a brokerage account, and the brokerage firm has asked me to obtain a 407 letter from FINRA because the brokerage firm believes I am associated with a self-regulatory organization (SRO). What is a 407 letter, and how do I get one?

Answer A 407 letter refers to [NYSE Rule 407](#), which requires member firms to obtain written approval from the NYSE before opening accounts for its employees or employees of other member firms. Although the rule does not apply to FINRA employees, some brokerage firms may request such a letter whenever an employee of FINRA seeks to open an account; FINRA will advise the firm that such a letter is not required. As an arbitrator, however, you are an independent contractor, not an employee, of FINRA. Therefore, you are not required to provide a 407 letter prior to opening a brokerage account. In fact, since arbitrators are not FINRA employees, FINRA will not issue such a letter to them.

Expungements in Intra-Industry Disputes

Question Does FINRA Rule 2080 apply to intra-industry expungement requests?

Answer No. FINRA [Rule 2080](#) (Obtaining an Order of Expungement of Customer Dispute Information from the Central Registration Depository (CRD)) does not apply to intra-industry disputes, unless the information to be expunged involves customer dispute information (customer complaints, arbitration claims and court filings made by customers and arbitration awards or court judgments that may result from those claims or filings).

For intra-industry disputes, arbitrators are not required to address the standards set forth in FINRA Rule 2080 when determining whether or not to grant expungement relief. If the arbitrators award expungement relief, FINRA will expunge the referenced information if the award is confirmed by a court of competent jurisdiction.

If the arbitrators award expungement relief and also determine that the information is **defamatory in nature**, FINRA will expunge the information without a court order. When requesting expungement in these situations, parties should present evidence to the arbitrators that proves the defamatory nature of the information in a broker's CRD record. If the arbitrators are satisfied that the party requesting expungement has proven its defamation claim, they must clearly state in the award that they are ordering expungement relief based on the defamatory nature of the information in CRD. Arbitrators, however, are not required to state explicitly in the award that they found all elements required to satisfy a claim in defamation under governing law, have been met.

For additional information about expungement of information in intra-industry disputes, please review John Nachmann's article in [Volume 2—2010 of *The Neutral Corner*](#). Please also review [Notice to Members 99-09](#) and [99-54](#).

Mediation Update

Mediation Statistics



From January through May 2013, parties initiated 221 mediation cases. FINRA also closed 240 mediation cases during this period. Approximately 77 percent of these cases concluded with successful settlements, and the average case turnaround time was 88 days.

Annual Membership Fee Due September 1, 2013

FINRA mediators must submit their \$200 annual membership renewal fee by September 1 to remain active on the roster. All active FINRA mediators will receive email notices by mid-August with instructions on how to pay the annual fee. Please contact [Marilyn Molena](#) if you have questions regarding your mediator availability status.

Mediation Outreach

This spring, mediation staff visited St. John's University's School of Law Securities Arbitration Clinic and spoke to students about FINRA's arbitration and mediation programs. Staff also visited Florida International University's Investor Advocacy Clinic and conducted a mock arbitration with the students.

Education and Training

Neutral Workshop—Tips for Conducting Efficient Hearings

During the [May 16, 2013 Neutral Workshop](#), Linda Fienberg, president of FINRA Dispute Resolution, discusses proposed rule changes to the Customer Option Rule and the Discovery Guide. Also, Barbara Brady, vice president and director of Neutral Management, moderates a discussion about strategies for conducting prehearing conferences and hearings with experienced FINRA arbitrators Jill Gross, professor of Law and director of Legal Skills at Pace University School of Law, and David Robbins, partner at Kaufmann, Gildin, Robbins & Oppenheim LLP.

Arbitrator Tip: Serving in Secondary Hearing Locations



FINRA assigns each arbitrator to one primary hearing location, which is the closest in-state hearing location to an arbitrator's primary residence. Arbitrators often split their time between two residences and request to serve in an additional, or secondary, hearing location.

If FINRA approves an arbitrator's request to serve in a secondary hearing location, arbitrators agree to pay their own travel and accommodation costs associated with serving in this hearing location. More importantly, arbitrators must have the availability and flexibility to serve in secondary hearing locations without causing a delay in the hearing process. They must respect the parties' need for an expeditious hearing and honor their commitment to keep the scheduled hearing dates. Additionally, FINRA encourages arbitrators to note—in the business backgrounds of their disclosure reports—in which hearing location they plan to spend certain months of the year, so parties are aware of any potential scheduling conflict at the start of the proceedings.

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