FINRA

Financial Industry Regulatory Authority

March 11, 2013

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: File No. SR-FINRA-2013-003 – Proposed Rule Change Relating to Amendments to the Customer and Industry Codes of Arbitration Procedure to Revise the Public Arbitrator Definition

Dear Ms. Murphy:

The Financial Industry Regulatory Authority, Inc. ("FINRA") hereby responds to the comment letters received by the Securities and Exchange Commission ("SEC") with respect to the above rule filing. In this rule filing, FINRA is proposing to amend the Customer and Industry Codes of Arbitration Procedure ("Codes") to revise the definition of public arbitrator to exclude persons associated with a mutual fund or hedge from serving as public arbitrators and to require individuals to wait for two years after ending certain affiliations before they may be permitted to serve as public arbitrators.[1]

The SEC received 45 comment letters on the proposed rule change.[2] All but three of the commenters express support for the proposal to exclude persons

[1] See Securities Exchange Act Rel. No. 68632 (January 11, 2013), 78 FR 3925 (January 17, 2013) (File No. SR-FINRA-2013-003).

[2] Comment letters were submitted by Steven B. Caruso, Esq., Maddox Hargett & Caruso, P.C., dated January 16, 2013 ("Caruso letter"); David Neuman, Stoltmann Law Offices, dated January 16, 2013 ("Neuman letter"); Richard M. Layne, Law Office of Richard M. Layne, dated January 28, 2013 ("Layne letter"); Seth E. Lipner Professor of Law, Zicklin School of Business, Baruch College, Member Deutsch & Lipner, dated January 29, 2013 ("Lipner letter"); Carl J. Carlson, Attorney, Tousley Brain Stephens PLLC, dated January 29, 2013 ("Carlson letter"); David Harrison, Esq., Law Offices of David Harrison, dated January 29, 2013 ("Harrison letter"); Philip M. Aidikoff, Esq., Attorney, dated January 29, 2013 ("Aidikoff letter"); Scott L. Silver, Esq., Silver Law Group, dated January 30, 2013 ("Silver letter"); Robert A. Uhl, Esq., Adjunct Professor of Law, Securities Arbitration and Director Pepperdine Investor Advocacy Clinic, Partner Aidikoff, Uhl & Bakhtiari, dated January 30, 2013 ("Uhl letter"); Andrew A. Lipkowitz, Student Intern, and Christine Lazaro, Acting Director, St. John's Law School Securities Arbitration Clinic, dated February 4, 2013 ("St. John's Letter"); Robert C. Port, Cohen Goldstein Port Gottlieb, LLP, dated February 5, 2013 ("Port letter"); Lisa A. Catalano, Esq., dated February 5, 2013 ("Catalano letter"); Scott R. Shewan, Pape Shewan, LLP, dated February 6, 2013 ("Shewan letter"); Jon C. Furgison, Law Offices of Jon C. Furgison, dated

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associated with a mutual fund or hedge fund from serving as public arbitrators.[3] However, commenters express concerns about the proposed "cooling off" period that would require certain individuals to wait for two years before FINRA would permit them to serve as public arbitrators. Several commenters recommend that FINRA implement a five-year cooling off period[4] and two commenters recommend a 10 year cooling off period.[5] Several commenters state that the two-year cooling off period is

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February 6, 2013 ("Furgison letter"); Steven J. Gard, Esquire, Reznicsek Fraser White & Shaffer, P.A., dated February 6, 2013 ("Gard letter"); Michael S. Edmiston, Jonathan W. Evans Associates, dated February 6, 2013 ("Edmiston letter"); Robert Savage, Esquire in his individual capacity and as Visiting Assistant Clinical Professor, Florida International University College of Law, dated February 7, 2013 ("Savage letters"); James A. Dunlap, Jr., James A. Dunlap Jr. & Associates LLC, dated February 7, 2013 ("Dunlap letter"); Diane Nygaard, Attorney, dated February 7, 2013 ("Nygaard letter"); W. Scott Greco, Partner, Greco & Greco, P.C. dated February 7, 2013 ("Greco letter"); A. Heath Abshure, NASAA President and Arkansas Securities Commissioner, dated February 7, 2013 ("NASAA letter"); Robert S. Banks, Jr., Banks Law Office, P.C., dated February 7, 2013 ("Banks letter"); Dale Ledbetter, Esq., Ledbetter and Associates, dated February 7, 2013 ("Ledbetter letter"); Scott C. Ilgenfritz, President, Public Investors Arbitration Bar Association ("PIABA"), dated February 7, 2013, ("PIABA letter"); Elizabeth Zeck, Attorney, Willoughby & Hoefer, PA,, dated February 7, 2013 ("Zeck letter"); James A. Sigler, dated February 7, 2013 ("Zigler letter"); Robert W. Goehring, Esquire, dated February 7, 2013 ("Goehring letter"); William S. Shepherd, Shepherd Smith Edwards and Kantas, LLP, dated February 7, 2013 ("Shepherd letter"); Leonard Steiner, dated February 7, 2013 ("Steiner letter"); Joseph Fogel, Fogel & Associates, dated February 7, 2013 ("Fogel letter"); Richard A. Lewins, Esq., dated February 7, 2013 ("Lewins letter"); Jenice L. Malecki, Esq., Malecki Law, dated February 7, 2013 ("Malecki letter"); Mark E. Sanders, Attorney, Halling & Cayo, S.C., dated February 7, 2013 ("Sanders letter"); Jeffrey Sonn, Esq., Sonn & Erez PLC, dated February 7, 2013 ("Sonn letter"); Thomas C. Costello, dated February 7, 2013 ("Costello letter"); Barry D. Estell, Esq., Attorney, Dated February 7, 2013 ("Estell letter"): Royal Lea, dated February 7, 2013 ("Lea letter"); Peter Mougey, Levin, Papantonio, Thomas, Mitchell, Rafferty & Proctor, P.A., dated February 7, 2013 ("Mougey letter"); William A. Jacobson, Associate Clinical Professor, Cornell Law, School and Director, Cornell Securities Law Clinic, dated February 7, 2013 ("Jacobson letter"); David T. Bellaire, Esq., Executive Vice President and General Counsel, Financial Services Institute, dated February 7, 2013 ("FSI letter"); Theodore M. Davis, Esquire, dated February 8, 2013 ("Davis letter"); Nicholas J. Guiliano, Esquire, The Guiliano Law Firm, dated February 8, 2013 ("Guiliano letter"); Mitchell Ostwald, Attorney at Law, dated February 8, 2013 ("Ostwald letter"); and Charles Michael Tobin, The Tobin Law Firm LLC, dated February 22, 2013 ("Tobin letter").

[3] The Harrison letter asserts that persons associated with mutual funds and hedge funds should be treated as non-public arbitrators. The Gard and FSI letters are silent as to this aspect of the proposed rule change.

[4] See the Caruso, Neuman, Layne, Harrison, Silver, St. John's, Catalano, Zeck, Shepherd, Malecki, Costello, Estell, Jacobson, and Guiliano letters.

[5] See the Carlson and Edmiston letters.

too short, but they do not recommend a specific time frame for the waiting period.[6] Other commenters argue that the cooling off period is misguided,[7] is unfair to investors,[8] or should be extended in certain instances.[9] Finally, several commenters suggest that FINRA should permanently bar individuals with prior securities industry affiliations from serving as public arbitrators.[10]

Some commenters believe that FINRA should add new categories of individuals to the non-public arbitrator roster.[11] In the subject rule filing, FINRA is not proposing to amend the non-public arbitrator definition. Therefore, these comments

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[6] See the Lipner, Shewan, Greco, Steiner, and Sanders letters.

[7] See the Aidikoff and Furgison letters.

[8] See the Port, Dunlap, Nygaard, Banks, and Goehring letters.

[9] The Gard letter raises concerns about individuals who were previously registered with or employed by broker dealers for less than twenty years but did not retire from such firms. The PIABA letter recommends that FINRA subject attorneys, accountants, and other professionals and family members of persons directly affiliated with the securities industry, to a longer cooling off period.

[10] The Port, Edmiston, Sonn, and Mougey letters ask FINRA to bar any persons with a previous industry affiliation. Other commenters identify certain persons who FINRA should bar. The Harrison letter suggests that FINRA should prohibit anyone who was associated with the industry for at least 20 years from ever serving as a public arbitrator. The Banks, NASAA, Fogel, and Davis letters assert that persons associated with mutual funds or hedge funds should never be classified as public arbitrators. The Davis and Jacobson letters state that persons who have spent many years affiliated with security industry entities should never be classified as public. The PIABA letter states that persons who have worked for more than a de minimis period of time as a stockbroker or investment advisor should be precluded from ever being classified as a public arbitrator and that persons with more than a de minimis length of affiliation with a member firm, an investment advisory firm, a hedge fund, a mutual fund, or an issuer, sponsor, marketer, or seller of securities or investment products with embedded securities should also be excluded from ever serving as public arbitrators. The Lewins letter recommends excluding anyone who has ever been securities licensed, or anyone who depended on the securities industry for more than a de minimis amount of their livelihood for any appreciable length of time. The Zeck letter states that mutual fund and hedge fund professionals should be permanently excluded if they retired from, or spent a substantial party of their career engaging in mutual fund or hedge fund activities.

[11] The NASAA letter suggests that FINRA classify industry-affiliated persons, including those who have been away from the industry for several years, as non-public. Similarly, the Steiner and Ostwald letters state that FINRA should classify persons who are connected to the brokerage industry because of their education, training, or work experiences as non-public. Finally, the Malecki letter recommends adding persons associated with mutual funds and hedge funds to the non-public arbitrator roster.

are outside the scope of the proposed rule change. Others assert that FINRA should add new categories of individuals to the list of those who may not serve as public arbitrators.[12] For reasons explained below, FINRA is not proposing to add additional categories of persons who may not serve as public arbitrators at this time.

As FINRA stated in the proposed rule change, the purpose of the proposal is to respond to investor representatives' concerns that they do not perceive certain arbitrators on the public roster as public because of their background and experience. This rule proposal affects persons whose job precludes them from being classified as a public arbitrator but does not qualify the person as a non-public arbitrator. Upon leaving that job for a new position that would not otherwise disqualify them for service, the proposed rule would require the person to wait two years before being eligible to join the public roster. FINRA maintains that the proposed cooling off period responds to the concerns raised by investor representatives and is a positive step toward enhancing investors' perception of fairness at the forum. Therefore, FINRA is not proposing additional amendments to the public arbitrator definition at this time. However, FINRA intends to conduct a comprehensive review under the auspices of the National Arbitration and Mediation Committee ("NAMC"),[13] of both the public and non-public arbitrator definitions[14] with a view towards clarifying the definitions and reviewing the additional issues raised in the comment letters as described above.

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[12] The Gard letter raises concerns about individuals who were previously registered with or employed by broker dealers for less than twenty years but did not retire from such firms. The PIABA letter suggests that FINRA exclude from the public roster individuals who are affiliated with issuers or sponsors of private placements, non- traded REITs, variable products, and other investment products that may arise in the future; and individuals who are affiliated with entities which act as sponsors, issuers, marketers, or sellers of securities or other investment products with embedded securities. The FSI letter avers that FINRA should exclude attorneys whose firms derived $50,000 or 10 percent or more of their annual revenue in the prior two years from professional services to claimants relating to customer disputes. Finally, the Davis letter asserts that FINRA should exclude individuals who were employed by securities industry trade organizations. The Davis letter characterizes former FINRA employees as being among those employed by a securities industry trade organization. FINRA, a self-regulatory organization that is the largest independent regulator for all securities firms doing business in the United States, is not a trade organization. FINRA classifies former regulators from federal and state regulatory entities, as well as former regulators from self-regulatory organizations, as public arbitrators. FINRA distinguishes former regulators from persons formerly associated with organizations that serve the interests of securities industry entities and persons associated with such entities.

[13] The National Arbitration and Mediation Committee (NAMC) is composed of investor, industry, and neutral (arbitrator and mediator) representatives. It provides policy guidance to FINRA's Dispute Resolution staff. A majority of the NAMC members and its chair are public.

[14] The non-public arbitrator definition enumerates the categories of persons who may serve as non-public arbitrators at the forum. To be included on the non-public arbitrator roster, an individual must be affiliated with the securities industry, either through current or former

The comment letters express broad support for excluding persons associated with mutual funds and hedge funds from serving as public arbitrators. The primary concerns raised about the proposed rule change relate to application of a cooling off period. FINRA requests that the SEC approve the proposed rule change, as written, as a significant measure that addresses the perception issue outlined in the rule filing. The proposed rule change should improve investors' perception about the fairness and neutrality of FINRA's public arbitrator roster, enhancing the forum for its users.

If you have any questions, please contact me by telephone at (212) 858-4481 or by email at margo.hassan@finra.org.

Very truly yours,

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employment in a securities business, or because the person provides professional services to a securities business. The definition of public arbitrator operates differently. Instead of listing categories of persons who may serve as public arbitrators, the public arbitrator definition states who may *not* serve as a public arbitrator. In some instances, a potential arbitrator may not be eligible to serve in either a non-public or a public capacity. For example, FINRA does not allow a person to serve as a public arbitrator if that person's family member is registered through a broker/dealer. FINRA would also exclude this person from the non-public roster if he or she did not meet the criteria enumerated in the non-public definition.