



December 11, 2014

Brent J. Fields  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

**Re: File No. SR-FINRA-2014-028 – Order Instituting Proceedings to Determine Whether to Approve or Disapprove Proposed Rule Change Relating to Revisions to the Definitions of Non-Public Arbitrator and Public Arbitrator; Response to Comments**

Dear Mr. Fields:

On October 1, 2014, the SEC published its Order Instituting Proceedings (“Notice”) to Determine Whether to Approve or Disapprove Proposed Rule Change Relating to Revisions to the Definitions of Non-Public Arbitrator and Public Arbitrator.<sup>1</sup> On November 24, 2014, the Financial Industry Regulatory Authority, Inc. (“FINRA”) responded to the comments the SEC received on the Notice. FINRA is submitting this letter to further describe why it believes that if the SEC approves the proposed rule change, FINRA will have a sufficient number of public arbitrators to serve the immediate needs of forum users.

**Arbitrator Recruitment**

In its November 24<sup>th</sup> letter, FINRA stated that it recognizes that the proposed rule change will necessitate aggressive arbitrator recruitment and that FINRA is committed to ensuring that the forum has a sufficient number of public arbitrators to serve the needs of forum users in each of its hearing locations. As an example of its recruitment efforts, FINRA explained how it managed an influx of cases in Puerto Rico concerning bond fund disputes. FINRA staff conducted recruitment activities in Puerto Rico and also asked arbitrators in hearing locations in the Southeast Region and Texas if they would be willing to serve in Puerto Rico. FINRA’s recruitment efforts resulted in almost 200 applications from Puerto Rico residents to serve on our roster. In total, approximately 800 arbitrators have agreed to hear cases in Puerto Rico.

The recent arbitrator recruitment in Puerto Rico is only one example of FINRA’s on-going effort to increase the number of arbitrators on its roster. FINRA currently dedicates two full-time staff members to arbitrator recruitment. Staff concentrates its recruitment efforts on the hearing locations with the lowest number of arbitrators on the roster in comparison with the number of open

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<sup>1</sup> See Securities Exchange Act Rel. No. 73277 (October 1, 2014), 79 FR 60556 (October 7, 2014)(file No. SR-FINRA-2014-028).

cases in the location. In addition, since FINRA amended its rules to allow any party in a customer case to select an all public panel, staff has targeted for recruitment those individuals whom FINRA would likely classify as public. Between January 1, 2014 and November 11, 2014, 634 individuals applied to become FINRA arbitrators. This is a substantial increase from 2013, when 445 individuals submitted applications (a 42.5 percent increase). If the SEC approves the proposed rule change, FINRA will focus its efforts on the hearing locations most impacted by the rule change. If the need arises, FINRA will assign additional staff to recruitment.

### **Arbitrator Retention**

In addition to arbitrator recruitment, FINRA has taken steps to enhance arbitrator retention at the forum. FINRA recently amended its Codes of Arbitration Procedure for Customer and Industry Disputes (“Codes”) to increase the honoraria arbitrators receive for participating in hearing sessions, serving as a chairperson, deciding contested subpoena motions, and deciding simplified arbitration cases.<sup>2</sup> This is the first increase to the honoraria payments to arbitrators in fifteen years. For example, FINRA raised the honorarium for a full day of hearings from \$400 to \$600 per day.<sup>3</sup> FINRA also increased the honorarium for administering a claim under the Simplified Arbitration rules from \$125 to \$350.

As a further measure to retain arbitrators, on December 3, 2014, FINRA’s Board of Governors authorized FINRA to file with the SEC proposed amendments to the Codes to increase the late cancellation fees which are assessed against the parties when they postpone or cancel a hearing at the last minute.<sup>4</sup> Arbitrators have raised concerns about last minute cancellations, and FINRA believes that they are a barrier to arbitrator retention. The proposed amendments would address this arbitrator concern.

### **Number of Arbitrators on the Roster**

FINRA believes that if the SEC approves the proposed rule change, it will have a sufficient number of public arbitrators to serve the immediate needs of forum users despite the anticipated reclassification of arbitrators from the public roster to the non-public roster. FINRA bases this belief, in part, on a comparison between the number of open cases FINRA is administering at the forum today, and the number of cases handled in earlier years. For example, at the end of 2003, FINRA had over 11,900 open cases and almost 6,900 arbitrators on its roster. As of October 2014, FINRA has approximately 4,700 open cases and nearly 6,400 arbitrators on its roster. FINRA’s open caseload is 60 percent less than the caseload we administered in 2003. The roster is just seven percent lower.

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<sup>2</sup> FINRA announced the amendments in Regulatory Notice 14-49. The amendments are effective on December 15, 2014 for cases filed on or after the effective date.

<sup>3</sup> A hearing session is a meeting between the parties and arbitrators of four hours or less, and includes a hearing or a pre-hearing conference. Typically, parties hold two hearing sessions per day with a lunch break in between.

<sup>4</sup> See FINRA Rules 12601 and 13601.

In addition, FINRA frequently hears from arbitrators that despite completing all required training, and updating their arbitrator disclosure statements, they are not selected often enough to arbitration panels. Parties select their arbitrators from lists randomly generated by FINRA's Neutral List Selection System. However, the fact that arbitrators regularly ask about how they can serve on panels more frequently is further indicia that FINRA has a sufficient number of arbitrators on its roster.

FINRA operated effectively when the docket ballooned to about 1.7 cases per available arbitrator. Therefore, FINRA staff is confident that it will also operate effectively with a docket reduced to less than half the number of cases per available arbitrator. While FINRA acknowledges that in 2003 parties could not select an all-public panel, given the substantial decrease in the caseload between 2003 and 2014, and the fact that parties continue to select non-public arbitrators in many cases, the case statistics support a finding that FINRA would have a sufficient number of public arbitrators on its roster.

### **Conclusion**

FINRA believes that the foregoing, along with its September 30, 2014 and November 24, 2014 letters, responds to the issues raised by the commenters. If you have any questions, please contact me on (212) 858-4481 or by email at [margo.hassan@finra.org](mailto:margo.hassan@finra.org).

Very truly yours,



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