Financial Industry Regulatory Authority

August 14, 2014

Kevin O'Neill
Deputy Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

RE: Notice of Filing of Partial Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change, as Modified by Partial Amendment No. 1, Relating to Broadening Arbitrators' Authority to Make Referrals During an Arbitration Proceeding (FINRA-2014-005); Response to Comments

Dear Mr. O'Neill:

On January 29, 2014, Financial Industry Regulatory Authority, Inc. ("FINRA") filed a proposed rule change to amend Rule 12104 of the Code of Arbitration Procedure for Customer Disputes ("Customer Code") and Rule 13104 of the Code of Arbitration Procedure for Industry Disputes ("Industry Code") (together, "Codes") to broaden arbitrators' authority to make referrals during an arbitration proceeding.[1] The Securities and Exchange Commission ("SEC") received eleven comment letters on the proposed rule change.[2] On May 19, 2014, FINRA responded to the comments[3] ("May 2014 Response"), and filed Partial Amendment No. 1 to require that a party file a recusal request for the referring arbitrator no later than three days after the Director notifies the parties of the referral, or forfeit the right to request recusal based on the mid-case

[1] See Securities Exchange Act Rel. No. 71534 (Feb. 12, 2014), 79 FR 9523 (Feb. 19, 2014) (File No. SR-FINRA-2014-005).

[2] See Comments on FINRA Rulemaking, Notice of Proposed Rule Change to Amend the Codes of Arbitration Procedure to Permit Arbitrators to Make Mid-case Referrals, available at http://www.sec.gov/comments/sr-finra-2014-005/finra2014005.shtml.

[3] See letter to Lourdes Gonzalez, Assistant Chief Counsel for Sales Practices in the Division of Trading and Markets, SEC, from Mignon McLemore, Assistant Chief Counsel, FINRA Dispute Resolution, Response to Comments, dated May 19, 2014. Jenice L. Malecki, Esq. submitted a comment on the proposed rule change after FINRA filed its letter. The comment supports the goal of the proposed rule change, but expresses concern about certain provisions. See comment submitted by Jenice L. Malecki, Malecki Law, May 20, 2014 ("Malecki Comment"). FINRA will respond to and cite to the Malecki Comment in this letter, where applicable and appropriate.

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referral.[4] On May 20, 2014, the SEC published a Notice of Filing of Partial Amendment No. 1 and Order Instituting Proceedings ("Notice") to determine whether to approve or disapprove the proposed rule change, as modified by Partial Amendment No. 1, relating to broadening arbitrators' authority to make referrals during an arbitration proceeding.[5]

In its Notice, the SEC solicited feedback[6] on any issues related to the changes made to the proposed rule change by Partial Amendment No. 1 and whether the proposed rule change, as modified by Partial Amendment No. 1, would be consistent with Section 15A(b)(6) of the Securities Exchange Act of 1934.[7] The Notice also requested comment on the issues raised by the May 2014 Response.[8] In addition, the Notice sought comment on questions raised by commenters about the potentially adverse consequences of the proposal for retail investors whose cases may be delayed or disrupted by a mid-case referral.[9] The questions were: (1) would the proposal adversely affect retail investors? If so, how?; (2) should FINRA propose a different standard for referral? If so, what standard(s) would be appropriate?; and (3) does Partial Amendment No. 1 ameliorate commenters' concerns that notifying parties of a mid-case referral could lead to adverse consequences to the claimant, including requests for recusal and challenges to an award? If not, should FINRA amend the proposal to preclude the Director, or anyone else, from notifying the parties of a referral?[10] The SEC received eight comment letters on its Notice.[11]

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[4] See Response to Comments and Partial Amendment No. 1, filed on May 19, 2014, available at http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p508484.pdf.

[5] See Securities Exchange Act Rel. No. 72196 (May 20, 2014), 79 FR 30206 (May 27, 2014) (File No. SR-FINRA-2014-005).

[6] Id. at 30208.

[7] 15 U.S.C. 78o-3(b)(6).

[8] See supra note 5.

[9] Id.

[10] Id.

[11] Comments on the Notice were submitted by: George H. Friedman, Esquire, George H. Friedman Consulting, LLC, Jun. 9, 2014 ("Friedman Comment"); Nicole G. Iannarone, Esq., Assistant Clinical Professor; Patricia Uceda, Student Intern, Investor Advocacy Clinic, Georgia State University College of Law, Jun. 20, 2014 ("GSU Comment"); Guillermo Gleizer, Esq., June 25, 2014 ("Gleizer Comment"); Jason Doss, President, Public Investors Arbitration Bar Association (PIABA), Jun. 26, 2014 ("PIABA Comment"); Ellen Liang, Student Intern; Elissa Germaine, Supervising Attorney; and Jill Gross, Director; Pace Investor Rights Clinic, Jun. 26, 2014 ("PACE Comment"); Richard P. Ryder, Esq., President, Securities Arbitration Commentator, Inc., Jun. 26, 2014 ("Ryder Comment"); Andrea Seidt, President, North American Securities Administrators

Hereinafter, FINRA refers to the proposed rule change as the "January proposal," and to Partial Amendment No. 1 as "Partial Amendment No. 1." Further, FINRA refers to the January proposal and Partial Amendment No. 1, collectively, as the "amended current proposal."

FINRA is hereby responding to the comments received on the Notice, as they discuss issues related to the amended current proposal. The eight commenters' positions break down as follows: one supports the amended current proposal;[12] two support the goal of the amended current proposal, but express concern about certain provisions;[13] and five oppose the amended current proposal.[14]

Comments that Support the Amended Current Proposal

The Friedman comment states that the amended current proposal with his suggested changes (discussed below) would enhance the investor protection mission of FINRA and the SEC, and urges its approval. Two other commenters support FINRA's efforts to identify and stop ongoing securities market schemes that could harm investors by authorizing arbitrators to make mid-case referrals.[15] They express concerns, however, about the potential impacts that the amended current proposal could have on individual claimants and suggest further changes that, in their view, would minimize the negative impact of the amended current proposal.[16]

As FINRA stated in its May 2014 Response, it "has carefully considered the impact that its proposed rules could have on an individual investor claimant. However, its obligations as a regulator require that it also weigh the potential effect that inaction could have on a large group of investors. In developing the January proposal, FINRA weighed the risk of potentially increasing the costs of an individual investor against the harm of significant losses to a larger group of investors. In balancing the potential outcomes, FINRA determined that the January proposal would help FINRA detect serious, ongoing or imminent threats to investors at an earlier stage than would otherwise occur; this early warning could help curb financial losses of a potentially large group of investors. FINRA believes, therefore, that providing additional protection to public

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Association and Ohio Securities Commissioner, Jun. 27, 2014 ("NASAA Comment"); and Steven B. Caruso, Esq., Maddox Hargett & Caruso, P.C., Jul. 2, 2014 ("Caruso Comment").

[12] Friedman Comment.

[13] PACE Comment and NASAA Comment.

[14] GA State Comment, Gleizer Comment, PIABA Comment, Ryder Comment, and Caruso Comment.

[15] PACE Comment and NASAA Comment. See also Malecki Comment (supporting the goal of the proposed rule change).

[16] Id.

investors generally by strengthening its regulatory structure outweighs the potential increased costs to an investor party."[17]

Comments that Oppose or Suggest Changes to the Amended Current Proposal

In its Notice, the SEC asked three questions to focus the commenters' thoughts and direct the discussion on the amended current proposal.[18] Most of the commenters who oppose[19] or recommend changes[20] to the amended current proposal did so when responding to these questions.

Question One - "Would the proposal adversely affect retail investors? If so, how?"

In response to this question, most of the commenters cite to their prior letters to explain their concerns about how the retail investor would incur increased costs and delays in the arbitration, if an arbitrator made a mid-case referral.[21] Other commenters raise concerns about the adverse effects that a recusal request would have on an investor's arbitration case, as well as the resulting motion to vacate that a respondent would file, if the referring arbitrator denied a recusal request.[22]

Commenters raised similar concerns about the January proposal.[23] In its May 2014 Response, FINRA explained the options parties have to control the costs parties could incur if an arbitrator makes a mid-case referral, as well as the options FINRA has to mitigate such costs under the Codes.[24] FINRA also explained that, while a denial of a recusal request could result in a motion to vacate, courts have found that such actions do not provide parties with valid bias grounds on which to challenge an award.[25] Further, FINRA noted that, if the SEC approved the January proposal, FINRA would use the Regulatory Notice to, among other things, emphasize that arbitrators are not required to grant a recusal request based on making a mid-case referral as well as provide guidance on the courts' findings on what constitutes grounds for evident partiality.[26] This guidance, FINRA believes, could further mitigate the effect of these motions. FINRA believes that its current policies, procedures, and case law address these concerns; thus,

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[17] See supra note 3, "Response to Comments" at 4.

[18] See supra note 5 at 30208.

[19] See supra note 14.

[20] PACE Comment, NASAA Comment, and Friedman Comment. See also Malecki Comment.

[21] See, e.g, PIABA Comment, Ryder Comment, and PACE Comment.

[22] PACE Comment, Ryder Comment, and Caruso Comment.

[23] See supra note 2.

[24] See supra note 3, "Effect of arbitrators granting recusal request" at 12-13.

[25] See supra note 3, "Effect of arbitrators declining recusal request" at 14-17.

[26] See supra note 3, "Arbitrator training and guidance" at 20.

the relevant sections of its May 2014 Response are incorporated by reference and serve as FINRA's response.

Two commenters also contend that the retail investor should not be expected to incur the costs that could arise if an arbitrator made a mid-case referral.[27] These commenters suggest that the costs that result from a mid-case referral should be borne by the party seeking recusal or by FINRA.[28]

Commenters raised similar concerns about the January proposal.[29] In its May 2014 Response, FINRA explained that the Codes do not require a moving party to pay all parties' costs that result from a recusal request.[30] FINRA noted that the Code permits the panel to determine the amount of costs and expenses incurred by the parties, and which party or parties will pay the costs and expenses.[31] Moreover, FINRA explained alternative approaches for aggrieved parties to seek recovery of costs and expenses in the event a mid-case referral resulted in increased costs and delays.[32] FINRA believes its current policies and procedures address these concerns; thus, the relevant section of its May 2014 Response is incorporated by reference and serves as FINRA's response.

Question Two – "Should FINRA propose a different standard for referral? If so, what standard(s) would be appropriate?"

The PIABA Comment reflects its belief that a different standard of referral under proposed Rule 12104(b) would not insulate the claimant from the adverse impacts of the proposed rule, as described in PIABA's response to Question One. The Caruso Comment contends that the standard may be inadequate for those arbitrators who are not attorneys and not trained in the nuances of legal system. Further, the Ryder Comment suggests that the standard is designed to assure that the rule is rarely invoked, but he does not believe it would prevent arbitrators from making an unnecessary and wrongly-based referral.

In its May 2014 Response, FINRA declined to amend the standard for referral in proposed Rule 12104(b), believing instead that "the current wording provides arbitrators with more guidance on how the rule should be applied."[33] Also, in the section discussing "a mid-case referral based on the reasonable belief standard," FINRA stated that it "believes the reasonable belief standard is appropriate for arbitrators to use in its forum because it would allow them to use their judgment, based on their assessment of the facts,

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[27] PIABA Comment and Malecki Comment (citing PIABA Comment, dated February 26, 2014, at 1-2).

[28] Id.

[29] See supra note 2.

[30] See supra note 3, "Require moving party to pay all costs of recusal request" at 11-12.

[31] Rule 12902(c). See also Rule 13902(c).

[32] See supra note 30.

[33] See supra note 3, "Comments that Support the Proposal" at 5.

evidence, and testimony, when making decisions during an arbitration."[34] Further, in its May 2014 Response, FINRA agreed to provide training for arbitrators on the mid-case referral rule and how it should be applied.[35] The PACE Comment, which supports the standard for referral as well as FINRA's proposed training, provides that the standard along with the training should help prevent arbitrators from making unnecessary mid-case referrals, and facilitate a smoother transition for them to learn how to apply the rule. FINRA agrees, and, for reasons provided in its May 2014 Response, believes the proposed standard is appropriate and should remain unchanged.

The Friedman comment suggests that FINRA remove the last sentence of proposed Rule 12104(b), as he believes the phrase "nearing completion" is vague and would invite inconsistent interpretation.

Another commenter made the same suggestion in a comment submitted on the January proposal when it was filed in January 2014.[36] This commenter and the Friedman Comment suggest that FINRA remove the option for the arbitrator to wait until the case concludes to make a mid-case referral, if the case is nearing completion and investor protection would not be materially harmed by the delay. In its May 2014 Response, FINRA explained that it "included this option for arbitrators to permit them to protect a party from the effects that a mid-case referral could have on a person's case, if the facts and circumstances support waiting until the case concludes."[37] FINRA's rationale from its May 2014 Response addresses this concern. Therefore, FINRA declines to change the amended current proposal because the criteria in this sentence provide additional guidance to the arbitrators as well as added protections to investors.

Question Three – "Does Partial Amendment No. 1 ameliorate commenters' concerns that notifying parties of a mid-case referral could lead to adverse consequences to the claimant, including requests for recusal and challenges to an award? If not, should FINRA amend the proposal to preclude the Director, or anyone else, from notifying the parties of a referral?"

Partial Amendment No. 1

In response to the question of whether Partial Amendment No. 1 ameliorates the commenters' concerns about notifying parties of a mid-case referral, three commenters believe that it does not.[38]

For example, PIABA contends that the substance of Partial Amendment No. 1 would not minimize the negative consequences of the proposed rule. The commenter believes that if the respondent inadvertently or purposefully fails to file a recusal request

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[34] See supra note 3, "A mid-case referral based on the reasonable belief standard" at 8-9.

[35] See supra note 3, "Arbitrator training and guidance" at 20-21.

[36] See supra note 2 for Caruso Comment, dated March 4, 2014.

[37] See supra note 3, "Comments that Support the Current Proposal" at 5.

[38] PIABA Comment, PACE Comment and GA State Comment.

within three days of being notified about the referral, this failure to comply with the rule would serve as basis for a subsequent motion to vacate an award.[39] The PACE Comment indicates that Partial Amendment No. 1 does not ameliorate its concerns because the amended current proposal contains an explicit reference to recusal.[40] The commenter argues that a mid-case referral should not provide any grounds for recusal or for a motion to vacate an award.[41] In addition, the NASAA Comment suggests that FINRA expressly state in the rule language that mid-case referral is not grounds for recusal. Finally, in the opinion of the GA State Comment, Partial Amendment No. 1 does not ameliorate its concerns about the effect that notifying the parties would have on the claimant's case, namely that a mid-case referral would result in a recusal request and a motion to vacate if the subject of mid-case referral loses the request or case.

Commenters raised similar concerns about the January proposal.[42] First, in its May 2014 Response, FINRA explained that, based on case law, denial of a recusal request would not be sufficient evidence to establish evident partiality by an arbitrator.[43] Further, the courts have not found that an arbitrator acting on evidence learned during a hearing rises to the level of evident partiality.[44] Moreover, a party's inadvertent or deliberate failure to comply with a forum's rules is not grounds, under the Federal Arbitration Act, for vacating an arbitration award.[45]

Second, in response to the concern that the amended current proposal contains an explicit reference to recusal,[46] FINRA notes that amended current proposal does not create a right to make a recusal request.[47] That right exists in any arbitration case.[48] However, the proposed rule acknowledges that such a request could occur after a mid-case referral and attempts to address the consequences.

Last, in response to the GA State Comments, FINRA notes that disclosure of a mid-case referral could prompt a party to make a recusal motion. In its May 2014 Response, FINRA explained that a party currently may make such a request under the Codes.[49] FINRA also explained that its rules do not currently dictate the grounds for

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[39] PIABA Comment.

[40] See also Malecki Comment.

[41] PACE Comment.

[42] See supra note 2.

[43] See supra note 3, "Effect of arbitrators declining recusal request" at 14-17.

[44] Id.

[45] See 9 U.S.C. §10(a).

[46] PACE Comment and Malecki Commemt.

[47] See supra note 3, "Require moving party to pay all costs of recusal request" at 12.

[48] Rules 12406 and 13409.

[49] See supra note 3, "Remove the notice requirement and ability to request recusal" at 9-10.

granting recusal requests and do not require specific decisions by arbitrators in response to such requests.[50] In response to the commenter's concern about the subject of a mid-case referral filing a motion to vacate if the request is denied or case is lost, FINRA believes its response to the same concerns raised under Question One above also addresses this concern. FINRA believes that its current policies, procedures, and case law address these concerns; thus, the relevant sections of its May 2014 Response are incorporated by reference and serve as FINRA's response.

Eliminating Notice Requirement

The commenters' positions are evenly split, in response to the SEC's inquiry about precluding the Director or anyone else from notifying the parties of the referral. Three commenters believe that the amended current proposal should retain the notification requirement.[51] As one commenter notes, the amended current proposal should retain the notification provision as this is consistent with the current obligations of arbitrators to provide full disclosure to help ensure fairness in the arbitration process.[52] Three other commenters suggest that it should be removed,[53] with one commenter advocating for confidential referrals from arbitrators.[54]

Commenters raised similar concerns about the January proposal.[55] In its May 2014 Response, FINRA emphasized the forum's policies encouraging arbitrator disclosures and its rules which require arbitrators to make disclosures when appointed to a FINRA arbitration, at any stage of the arbitration, or as circumstances dictate.[56] Further, FINRA noted that, in addition to its rules and practices, case law has established a broad requirement that arbitrators make full disclosures,[57] and, that a failure to do so, could provide a party with grounds to challenge an award by claiming evident partiality against the arbitrator.[58] For the reasons provided in its May 2014 Response, FINRA declined to remove the notice requirement, and its position remains unchanged.

The Caruso Comment suggests that providing the subject of a mid-case referral advance notice of a potential investigation could negatively impact the subsequent criminal or regulatory investigations. For example, the commenter believes that such

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[50] Id.

[51] PACE Comment, Ryder Comment, and Friedman Comment.

[52] PACE Comment.

[53] GA State Comment, NASAA Comment, and Caruso Comment.

[54] NASAA Comment.

[55] See supra note 2.

[56] See supra note 3, "Remove the notice requirement and ability to request recusal" at 9-10.

[57] Id.

[58] See supra note 3, "Effect of arbitrators declining recusal request" at 14-17.

notice could lead to destruction of evidence and obstruction of the investigation.[59] FINRA believes knowledge of behavior that would warrant a mid-case referral if revealed during a hearing, would likely not be a revelation to the wrongdoer. However, that disclosure during a hearing would serve as notice to the wrongdoer that the matter or conduct is on the verge of public exposure. Once that exposure is noted, the wrongdoer could begin to engage in the behavior described by the commenter, regardless of whether arbitrators act on the information and make a mid-case referral. FINRA believes that, in these instances, disclosure of a mid-case referral would give regulators advance notice of a serious threat that is likely to harm investors, and, thus, permit them to take immediate action instead of waiting until the end of the case. Otherwise, if the regulators did not learn of the referral until after the case closes, there is a risk that the wrongdoer would have extra time to destroy evidence.

Forwarding the Mid-case Referral to Director

Finally, in response to Question Three, two commenters suggest removing the provision that would require forwarding the mid-case referral to the President or Director for review.[60] One commenter believes the referral could be forwarded directly to the regulatory or enforcement department of FINRA.[61] The other commenter suggests expanding the direct referral concept to include the SEC, state securities regulators, or local or federal law enforcement.[62]

Commenters raised similar concerns about the January proposal.[63] In its May 2014 Response, FINRA explained that it modeled this provision after the current practice used when an arbitrator makes a post-case referral.[64] FINRA also stated that the purpose of the Director's review is to determine which FINRA division should receive the referral, and whether other divisions or regulators should be notified.[65] Based on the relevant section of the May 2014 Response, which is incorporated by reference, FINRA believes that this provision would result in an efficient use of its resources, and, thus, declines to change the amended current proposal as suggested.

Other Issues Raised Concerning the Amended Current Proposal

Explicit reference to recusal

Two commenters contend that the explicit reference to recusal in the amended current proposal suggests implicitly that an arbitrator could be biased after the person has

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[59] Caruso Comment.

[60] Friedman Comment and NASAA Comment.

[61] Friedman Comment.

[62] NASAA Comment.

[63] See supra note 2.

[64] See supra note 3, "Director's review after referral" at 20.

[65] Id.

heard enough evidence of wrongdoing.[66] The PACE Comment opines that finding liability based on evidence presented does not mean that the arbitrator is sufficiently biased against the wrongdoer to justify good cause for recusal. The Malecki Comment compares the amended current proposal to the Federal laws, which, according to the commenter, are less stringent and do not expressly provide for recusal. This commenter contends that, by inserting language in the amended current proposal to explain the availability of a recusal request even though it is available in other parts of the Codes, FINRA is seeking to make its rules more stringent than the Federal laws.

First, FINRA notes that the amended current proposal does not create a right to make a recusal request. That right exists in any arbitration case.[67] However, this rule acknowledges that such a request could occur after a mid-case referral and attempts to address the consequences. Second, FINRA disagrees with the PACE Comment that the explicit reference implies bias on the part of an arbitrator who has heard enough evidence of wrongdoing. Last, the Federal laws, to which the Malecki Comment refers, relate to grounds for recusal. The reference in this proposed rule is not about the grounds for recusal. As FINRA explained in its May 2014 Response, arbitrators are expected to make decisions based on evidence presented during a hearing, and such decisions alone have been insufficient to support a showing of evident partiality.[68] Thus, FINRA has made it clear that the act of making a mid-case referral is not evidence of bias, whether implied or overt. The forum's rules are designed to guide parties and staff in the administration of arbitration cases. FINRA believes its rules are more effective when procedures are expressly incorporated in the arbitration rules; this transparency results in the efficient administration of cases and consistent application of the rules.

Rely on current referral process

Three commenters suggest that FINRA rely on the current process for referring actions or matters for further investigation.[69] Specifically, when an arbitration claim is filed, FINRA's Central Review Group (CRG) receives a copy of statements of claims and pleadings and reviews them to determine if referral to Enforcement is warranted. These commenters believe FINRA should use this process to detect wrongdoing rather than rely on the arbitrators to enforce the rules and, thus, create issues of bias and impartiality.[70]

Commenters raised similar concerns about the January proposal.[71] In its May 2014 Response, FINRA explained that enforcement procedures conducted by CRG prior

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[66] PACE Comment and Malecki Comment.

[67] See supra note 47.

[68] See supra note 3, "Effect of arbitrators declining recusal request" at 14-17, and "Remove the notice requirement and ability to request recusal" at 9-10.

[69] GA State Comment, PIABA Comment, and Malecki Comment.

[70] Id.

[71] See supra note 2.

to an arbitration hearing would not be an effective substitute for arbitrator action taken during a hearing based on evidence presented.[72] FINRA noted that analysis by Enforcement employees conducted on the claims and pleadings permit FINRA to monitor and analyze volumes of data through various market data systems to detect evidence of wrongdoing.[73] However, expanding these Enforcement procedures would not necessarily address the same concerns discovered by arbitrators, who learn of a serious threat during a hearing after consideration of evidence.[74] For the reasons provided in the relevant section of its May 2014 Response, which is hereby incorporated by reference, FINRA declines to expand its enforcement procedures as suggested.

No evidence to support the need for the amended current proposal

Three commenters contend that FINRA did not provide evidence to support the need for the amended current proposal or that it would prevent ongoing fraud or losses for investors.[75]

Commenters raised similar concerns about the January proposal.[76] In its May 2014 Response, FINRA explained that its assessment of its regulatory structure as well as its determination that its rules would be strengthened by closing a gap that currently permits arbitrators to make post-case referrals only, justify the need for the amended current proposal.[77] FINRA believes that its assessment of the issue and rationale for the January proposal address this concern; thus, the relevant section of its May 2014 Response is incorporated by reference and serves as FINRA's response.

Amended current proposal would deputize arbitrators

Three commenters express concern that the amended current proposal would deputize arbitrators as examiners, who would be required to evaluate and report rule violations.[78] They believe this role would conflict with an arbitrator's duty, which is to serve as an arbiter of a dispute to achieve the best resolution in a manner that serves the interests of the parties.[79]

Commenters raised similar concerns about the January proposal.[80] In its May 2014 Response, FINRA explained that its rules require arbitrators to be impartial and free

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[72] See supra note 3, "Expand Enforcement's role" at 7-8.

[73] Id.

[74] Id.

[75] GA State Comment, Malecki Comment, and Caruso Comment.

[76] See supra note 2.

[77] See supra note 3, "Purpose of current proposal not defined" at 6-7.

[78] Ryder Comment, Gleizer Comment, and Malecki Comment.

[79] Id.

[80] See supra note 2.

from conflicts that could hinder their ability to decide a case fairly.[81] Further, case law supports FINRA's position that arbitrators would not compromise their neutrality by making a mid-case referral, because, in doing so, arbitrators would be performing one of the duties that is expected of arbitrators.[82] FINRA believes that its current rules, case law, and the Code of Ethics for Arbitrators in Commercial Disputes address these concerns; thus, the relevant section of its May 2014 Response is incorporated by reference and serves as FINRA's response.

FINRA notes that the Malecki Comment refers to arbitrators as "an arm of FINRA," [83] when describing the arbitrator's role in helping FINRA enforce its rules, and, thereby, assisting FINRA in achieving its investor protection mandate. FINRA agrees that the arbitrators' role in helping FINRA achieve its mission is important. However, FINRA believes that describing arbitrators as "an arm of FINRA" could be interpreted as classifying them as employees. Thus, to clarify any misperceptions, FINRA notes that arbitrators are not FINRA employees; they are independent contractors.[84]

Monitor effectiveness and provide statistics to SEC

Two commenters urge FINRA to monitor the effects of the amended current proposal on individual investors and disclose statistics periodically to the SEC on the number of mid-case referrals that arbitrators make.[85] Currently, FINRA has implemented procedures to track post-case referrals. If the amended current proposal is approved, FINRA would update its procedures to track the number of mid-case referrals made after the amended current proposal becomes effective. FINRA would provide this data to the SEC a year after the effective date, and thereafter at the SEC's request. FINRA would monitor the effects of the amended current proposal to determine whether further action would be necessary.

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[81] See supra note 3, "Compromises to arbitrators' neutrality and the arbitration process" at 18-19.

[82] Id.

[83] See Malecki Comment at 3.

[84] See FINRA, Arbitration and Mediation, Honorarium, Frequently Asked Questions, available at http://www.finra.org/web/groups/arbitrationmediation/@arbmed/@arbtors/documents/arbmed/p122407.pdf.

[85] NASAA Comment and PACE Comment.

FINRA believes that the foregoing, along with its May 2014 Response, responds to the issues raised by the commenters. If you have any questions, please contact me on 202-728-8151 or mignon.mclemore@finra.org.

Sincerely,

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FINRA Dispute Resolution, Inc.