PUBLIC INVESTORS ARBITRATION BAR ASSOCIATION
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June 13 2016

Robert W. Errett
Deputy Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: SR-FINRA-2016-015; Proposed Rule Changes for FINRA
Rules 12904 and 13904 Regarding Offsetting Damages

Dear Mr. Errett:

I write on behalf of the Public Investors Arbitration Bar Association ("PIABA"), an international bar association comprised of attorneys who represent investors in securities arbitrations. Since its formation in 1990, PIABA has promoted the interests of the public investor in all securities and commodities arbitration forums, while also advocating for public education regarding investment fraud and industry misconduct. Our members and their clients have a strong interest in rules promulgated by the Financial Industry Regulatory Authority ("FINRA") to govern the conduct of securities firms and their representatives. In particular, our members and their clients have a strong interest in FINRA rules relating to the information provided to investors and those that affect the fairness of FINRA's dispute resolution forum.

FINRA has proposed changes to Rules 12904 and 13904 regarding offsetting damages, in arbitration awards where arbitrators have awarded damages to both sides. In particular, the proposal would require that when opposing parties are each awarded monetary compensation, then the monetary awards offset each other, and the party that owes the larger amount shall pay the net difference, absent any specification to the contrary in the award. PIABA generally supports this rule proposal and believes that it makes common sense.

For example, in the context of a broker-dealer versus former broker case, the arbitrators may award damages to the broker-dealer if a broker failed to pay money pursuant to a promissory note but may also award a lesser amount to the broker as part of a counterclaim (such as for commissions withheld). In the event that the broker is unable to pay the award, the broker-dealer may still have to pay money to the broker pursuant to the counterclaim award, even where the broker-dealer is awarded more money. If the broker-dealer fails to pay (even though it is the net "winner"), it could be suspended under FINRA Rules. Requiring one party to pay money to the other, when the first party would actually be owed if the awards were offset creates an inequitable result.

FINRA has also indicated that this can occur in the context of a customer versus broker-dealer case involving margin balances. However, FINRA also notes that this only occurred in one case during 2013 and 2014 (out of 8,375 cases which were resolved during that timeframe).

While this rule seems to primarily fix an issue for intra-industry cases, it is a significant problem when a member firm or associated person cannot pay an award to a customer party. For example, the issue of an offset may also arise in a case where a customer leaves the broker-dealer with a debit balance accrued as a result of the complained of trading. A panel in that instance could issue an award in favor of the customer, but also order that the customer repay the lesser debit balance. If the broker-dealer were to go out of business, the customer could potentially find themselves (as the net "winner") being pursued by that firm's creditors and the like if there were no offset.

Courts have embraced the practice of offsetting damages. For example, the United States Supreme Court and Second Circuit Court of Appeals have recognized the right to a setoff:

> It makes little sense to have [Party A] pay [Party B] money that [Party B] will immediately return to [Party A]. Allowing [Party A] to pay just its *net* obligation avoids "the absurdity of making A pay B when B owes A."

ST Microelectronics, N.V. v Credit Suisse Sec. (USA) LLC, 648 F3d 68, 82 (2d Cir 2011) (quoting the United States Supreme Court decision in *Studley v. Boylston Nat'l Bank of Boston*, 229 U.S. 523, 528 (1913)).

The *ST Microelectronics* Court also astutely noted the potential for significant prejudice and inefficiency if there were no setoff:

> Such an arrangement also avoids the possibility — however remote it might be — that [Party B] might not immediately return the $75 million it would owe [Party A], forcing [Party A] to pursue enforcement efforts against [Party B] in Switzerland.

ST Microelectronics, N.V., 648 F3d at 82.

Additionally, a number of States address the issue in their statutes. For example, New York's Debtor Creditor Law, Sec. 151, *et seq*., states in relevant part:

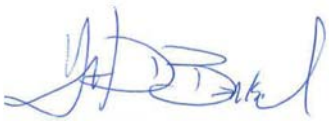
> Every debtor shall have the right upon: . . . (b) the making of an assignment by a creditor for the benefit of its creditors; . . . to set off and apply against any indebtedness, whether matured or unmatured, of such creditor to such debtor, any amount owing from such debtor to such creditor.

PIABA encourages FINRA to follow suit. This rule proposal also highlights the inequities that exist with unpaid arbitration awards, whether the claimant is an investor, broker, or broker-dealer. As highlighted by PIABA's study of arbitration awards involving customers during 2013, over $62 million of arbitration awards went unpaid, which amounts to 1 out of 3 cases, or nearly 1 out of every 4 dollars awarded. The large number of unpaid awards undermines the integrity of the securities arbitration process and must be corrected.

While the concerns addressed by the rule proposal may more generally benefit FINRA's members, rather those members' customers, what's good for the goose is good for the gander. FINRA needs to use this opportunity to not only address a problem with unpaid awards for intra-industry disputes, but to address unpaid awards for investors as well. PIABA urges FINRA to implement a national recovery pool to address this important problem.

In sum, PIABA supports the rule proposal but asks that FINRA take more steps in ensuring that all arbitration awards are paid, regardless of whether they are customer or intra-industry disputes. Thank you for the opportunity to comment.

Sincerely,



Hugh Berkson