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August 4, 2016

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

Re: *SR-FINRA-2016-022*
Proposed Rule Changes for FINRA Rule 12403 Regarding Selection of Public Arbitrators in Customer Disputes

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 the rules Financial Industry Regulatory Authority ("FINRA") promulgates to govern the conduct of securities firms and their representatives. In particular, our members and their clients have a strong interest in the fairness of the arbitration process, including the important step of the selection of arbitrators.

Pursuant to SR-FINRA-2016-022, FINRA sought comment on proposed changes to Rule 12403 regarding the selection of public arbitrators in customer disputes. Specifically, the rule change proposal would increase the number of proposed public arbitrator candidates from 10 to 15, as well as increase the number of strikes each party would have for each arbitrator candidate list from 4 to 6. FINRA made these rule change proposals after the FINRA Dispute Resolution Task Force recommended that parties be offered a new list of 10 additional potential public arbitrators if parties strike the non-public arbitrators.

PIABA generally supports this rule change proposal, but it also wants to alert the Commission to overarching problems with the arbitrator selection process that threaten to undermine and overshadow the process, even when otherwise sound modifications are made. Therefore, in addition to a few comments specific to the proposed rule change, PIABA suggests that other measures that should be undertaken as soon as possible to promote fairness in the arbitrator selection process.

The Rule Proposal May Help Limit Instances of "Cram-Down" Arbitrators

PIABA is generally supportive of the rule change proposal. First, it provides a total of 30 public arbitrator candidates to be ranked instead of the 20 now available when the non-public arbitrators are stricken. In theory, having the ability to consider more candidates helps both claimants and respondents. Second, by increasing the number of qualified public arbitrators to be ranked, the proposed rule change may help limit instances of "cram-down"[1] arbitrators appointed to panels when the parties strike all the proposed arbitrators. In an instance where there is one claimant and one respondent and the parties select an all-public arbitration panel (by collectively striking all the non-public list names), the rule proposal would guarantee that at least three public arbitrators would be ranked by the parties, as opposed to the current system that guarantees only two arbitrators would be ranked.

With the proposed rule change, in a perfect world where all three of the mutually ranked arbitrators from the initial list are initially qualified, willing and able to serve as arbitrators, FINRA would still have one "alternate" arbitrator the parties have already ranked that could be appointed in the too-common event one of the prior ranked and appointed arbitrators later becomes unavailable or is otherwise disqualified, unwilling, or unable to serve on the panel. Thus, the proposed rule change would hopefully help parties avoid instances where they may get a cram down arbitrator or have to utilize a "short-list" of new arbitrators from which FINRA will appoint one mutually acceptable to the parties (if that arbitrator is available).

While increasing the number of candidates from 10 to 15 for each of the chair-qualified and public lists sounds good in theory, in practice, it will likely lead to disastrous results for investors.

Additional Recommendations to Promote Transparency and Fairness in the Arbitrator Selection Process

While adding additional public arbitrator candidates to the ranking lists stands to improves the process by decreasing the chances of cram-down or short-list arbitrator appointments, there is fundamental problem with the current list selection process that must be addressed if it is ever to become more fair for the participants, and especially investors.

When FINRA changed the Rule 12100 definitions of "non-public" and "public" arbitrators for customer cases effective in June 2015, it substantially reduced the number of arbitrators eligible to serve as chairpersons and public arbitrators.[3] Accordingly, and especially in the smaller and moderately sized cities, there are insufficient numbers of local candidates for the chair-qualified and public lists. Many, if not most, arbitrators on the chair-qualified lists today are from outside the state where the investors reside and where the dispute arose.[4] In all but the largest metropolitan cities, PIABA's members, who practice in FINRA's arbitration forum daily, have seen a

[1] A "cram-down" arbitrator is a colloquial term for arbitrators who FINRA selects without the advance notice, disclosure or selection of the parties. Like all arbitrators, these arbitrators are supposed to be randomly selected from the arbitrator pool.
[3] Regulatory Notice 15-18, regarding amendments to revise the definitions of Non-Public and Public Arbitrator in FINRA Rules 12100 and 13100, effective June 26, 2015.
[4] While this problem has been noticed more often by PIABA members with chair-qualified arbitrators, it is not exclusive to them. It is not uncommon for customer cases, even in major metropolitan cities, to nonetheless have a majority of the arbitrators on the list be out-of-state names on chair qualified and public lists.

disturbing trend by which local chair-qualified candidates are not appearing on the chair-qualified list, but instead, those lists are comprised primarily of foreign (*i.e.*, out-of-state or "traveling") arbitrators.

FINRA's regular use of foreign arbitrators as chairpersons has a dramatic impact on investor rights. For one thing, many investor claims are based upon violation of state securities laws, which vary from jurisdiction to jurisdiction. PIABA's members have experienced a trend whereby the foreign arbitrators have what appear to be histories of awards that substantially favor the industry, compared to the local arbitrators' records that tend to be more investor-friendly. Our members have also seen that, all too often, foreign arbitrators are less familiar with, and have less regard for, the laws of the forum state where the arbitration is taking place. Accordingly, investors are too often being denied rights afforded to them by their state legislatures.

PIABA members' concern about the effect of importing so many arbitrators is well founded. Since Rule 12100 and the definition of "public" arbitrators were amended (effective June 26, 2015), the percentage of awards in which customers were awarded damages decreased from 47% in 2015 to 38% in 2016 in cases with three "public" arbitrators. *See* FINRA Arbitration Statistics Through June (https://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics#arbitrationstats , last visited July 27, 2016).

PIABA is concerned that the increase of proposed arbitrators to the public arbitrator selection list, without other necessary modifications to list generation and arbitrator selection, will only serve to further exacerbate the alarming increase of out-of-state arbitrators appearing on ranking lists. This is particularly a significant problem for locations in the country that have limited available chair-qualified and public arbitrators *(i.e.*, areas with "shallow" arbitrator pools).

Given the foregoing, rather than increasing the parties' overall satisfaction with the arbitration process, the proposed rule change will likely only increase customers' view that the mandatory arbitration process is not fair to them. Therefore, PIABA recommends that FINRA redouble its efforts to recruit suitable *local* individuals to serve as public and chair-qualified arbitrators. Having more local public arbitrators should increase the chances that arbitrators will take into account and apply their state's particular laws, including applicable "blue sky" laws, securities regulations, common law, and administrative rules. PIABA also urges FINRA to monitor and review the frequency of appearances of out-of-state arbitrators on chair-qualified and public lists in various localities to evaluate and measure the success of the recruitment efforts and whether the current arbitration selection rules are affording investors a fair selection process.

PIABA also urges FINRA to increase transparency regarding the list selection process including, but not limited to, the methods employed by the Neutral List Selection System to ensure that the inclusion of traveling out-of-state arbitrators in candidate lists is random (as FINRA has repeatedly represented), is a justified necessity given the number of local people in a specific locality's arbitrator pool, and actually results in the neutral selection of arbitrators. PIABA's members have long sought this same information with respect to local arbitrators that seem to disproportionately appear again and again on certain locations' selection lists. Now, the lack of transparency in the list selection process is also eroding PIABA members' confidence that FINRA's appointment of arbitrators from out-of-state is the result of a neutral and random process. While FINRA has steadfastly maintained that the list generation system is, in fact, random, pulling back the curtain on the process would go a long way toward promoting investor confidence in the system.

In sum, PIABA generally supports the implementation of SR-FINRA-2016-022, subject to concerns and recommendations set forth herein. Under no circumstances does PIABA want the implementation of the proposed rule change to make the arbitrator selection problem worse for investors, which seems to be a real possibility if not an outright certainty. Thank you for the opportunity to comment.

Sincerely,

Hugh Berkson, President
PIABA