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SHOWING THE LOVE: FINRA ADOPTS MANY TASK FORCE RECOMMENDATIONS TO IMPROVE THE DISPUTE RESOLUTION FORUM

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FINRA formed a task force in June 2014 (the "Task Force") to consider possible improvements to FINRA's dispute resolution forum. In December 2015, the Task Force issued a Final Report making 51 recommendations to improve FINRA's arbitration and mediation processes for industry disputes. So far, FINRA has taken action on 35 of the 51 recommendations. On February 8, 2017, FINRA issued a Status Report providing an update on the implementation of the Task Force's recommendations. The following is a brief summary of some of the highlights of FINRA's progress, mostly as they relate to intra-industry disputes:

Motions to Dismiss Are Permissible Where a Dispute Was Previously Adjudicated

Generally, motions to dismiss are disfavored in FINRA arbitrations except for a limited number of circumstances identified in the FINRA Rules. In reviewing the FINRA forum, however, the Task Force identified an additional situation in which it concluded that motions to dismiss should be considered. The Task Force recommended a rule change to allow motions to dismiss in customer disputes before the conclusion of a party's case in chief in situations where the dispute has been previously adjudicated and memorialized in an order, judgment, award, or decision.[1] FINRA agreed with the Task Force's recommendation, however, it also determined that the rule change should apply to intra-industry disputes. FINRA's rule proposal, which was approved by the Securities and Exchange Commission (SEC) in November 2016, provided that arbitrators may decide motions to dismiss a party or claim prior to the conclusion of a party's case in chief if the non-moving party previously brought a claim against the same party that had already been fully adjudicated and memorialized in an order, judgment, award, or decision. The new Rules 12504 (Customer Code) and 13504 (Industry Code) reflecting this change went into effect on January 23, 2017.[2]

Pending SEC Approval: Expungement Requests Will Be Reported to State Securities Regulators

The process to obtain an expungement has grown increasingly more difficult over the past few years. On many occasions, FINRA has expressed its concerns about expungements, with a focus on ensuring the protection of investors. Keeping this focus in mind, the Task Force reviewed FINRA's expungement procedures to identify areas of improvement. It noted that, while an arbitration

[1] *See* The Task Force's Final Report at p. 38 (Previously Adjudicated Cases).
[2] *See* FINRA's Status Report at p. 2.

Panel may make a determination on an expungement request, many state regulators do an independent review of the request, as well. To support the state regulators' assessment, the Task Force recommended a review of the procedures for notifying state regulators of expungement requests. Agreeing with that recommendation, the FINRA Board approved amendments to Rules 12805 (Customer Code) and 13805 (Industry Code) to require notice to appropriate state securities regulators of all expungement requests.[3]

Pending SEC Approval: Limited Telephonic Hearings for Claims of $50,000 or Less

Currently, claims filed in FINRA of $50,000 or less ("small claims") are adjudicated through a simplified arbitration procedure with one arbitrator and a decision made solely on the parties' written submissions, unless the claimant requests a hearing.[4] While decisions made solely on the papers may lessen the time and expense of arbitration, the Task Force noted that matters adjudicated through the simplified procedure led to the most dissatisfied users of the FINRA forum.[5] It further noted that, from the arbitrator's perspective, deciding the merits of cases solely on written submissions was problematic. This dissatisfaction led to the Task Force's recommendation to adopt an intermediate form of adjudication, providing something more than a decision on the papers but less than a full hearing. FINRA agreed and proposed to amend Rules 12800 (Customer Code) and 13800 (Industry Code) to provide an option for a limited telephonic hearing, called the Special Proceeding for Simplified Arbitration, for small claims. FINRA confirmed that its proposal will be filed with the SEC for comment.

Revisions to the *Initial Pre-Hearing Conference* (IPHC) Script: Technology and Phantom Experts

The use of technology is pervasive in our society, and it only continues to increase. However, many arbitrations in the FINRA forum continue to proceed with limited to no technology at the hearings. The Task Force expressed concerns that the minimal use of technology at hearings was the result of some arbitrators' reluctance to permit its use. In the interest of increasing efficiency and the cost-effectiveness of arbitration, the Task Force suggested that FINRA amend its IPHC script to include express permission to the parties to use technology at hearings.[6] Acknowledging the legitimacy of that concern, FINRA amended its IPHC script to *encourage* parties' use of technology in the facilitation of hearings. It further allows parties to modify the hearing procedures by agreement to promote efficiency and cost-effectiveness.[7]

The Task Force also recommended a change to the IPHC script to discourage the practice of phantom retention of experts, where parties identify an expert witness during the 20-day exchange without actually retaining the expert. FINRA agreed with this recommendation and amended its IPHC script, urging parties to avoid that practice. FINRA also issued an article in *The Neutral Corner* identifying the potential consequences of the disfavored practice, including unnecessary arbitrator recusals, miscalculation of the duration of the hearing, and needless retention of a rebuttal expert by an opponent.[8]

[3] *See* FINRA's Status Report at p. 2.
[4] *See* FINRA Rules 12800 (Customer Code) and 13800 (Industry Code).
[5] *See* The Task Force's Final Report at p. 28 (Small Claims).
[6] *See* The Task Force's Final Report at p. 42 (Use of Technology).
[7] *See* FINRA's Status Report at p. 7.
[8] *See The Neutral Corner*, Volume 2, 2016 at p. 1.

Implementation of Procedure to Monitor and Prevent Late Arbitrator Recusals

The Task Force identified last minute arbitrator recusals as a significant problem causing scheduling difficulties for parties and delays. The Task Force recommended a number of actions to alleviate some of the issues caused by late arbitrator recusals.[9] FINRA recognized late arbitrator recusals as a problem and issued an article in *The Neutral Corner* providing guidance for arbitrators and urging them to remain available to attend all hearings to which they have committed. FINRA further enhanced its case management system to issue reports and allow staff to track and monitor late arbitrator recusals.[10]

Improve Functionality of the DR Portal

The online DR Portal continues to evolve as features are added and users become more familiar with its interface. The Task Force confirmed its support for increased functionality of the Portal. To that end, it recommended that FINRA develop a feature to allow parties to view all costs on an on-going basis.[11] FINRA confirmed that it is in the process of programming system changes that will allow parties to view, in real time, costs assessed to a case.[12]

Explained Decisions

Explained decisions was a hot issue that the Task Force considered. The Task Force believed that the use of explained decisions could increase the transparency of, and confidence in, the FINRA arbitration system. It recommended an amendment to the FINRA Rules making explained decisions the default.[13] Under the Task Force's proposed rules, if a party wanted to opt-out of the explained decision, it would need to notify the arbitrators prior to the IPHC. FINRA did not agree with that proposal. While it recognized the possible increased transparency of explained decisions, it noted that many forum users expressed concerns about making them the default.[14] For example, users felt that explained decisions could put the finality of arbitration awards at risk of motions to vacate based on the explanations. Demonstrating its understanding of both positions, FINRA elected to compromise by waiving the $400 fee to obtain an explained decision while it continues monitoring the feasibility of making explained decisions the default award type.

The above summaries represent a small selection of the 35 actions FINRA has taken in response to the Task Force's considerations and recommendations. Industry professionals and their attorneys should review FINRA's entire Status Report and all subsequent reports to ensure compliance with applicable new rules implemented at the suggestion of the Task Force.

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[9] *See* The Task Force's Final Report at p. 41 (Last-Minute Recusals).
[10] *See* FINRA's Status Report at p. 8.
[11] *See* The Task Force's Final Report at p. 42 (DR Portal).
[12] *See* FINRA's Status Report at p. 8.
[13] *See* The Task Force's Final Report at p. 43-44 (Public Availability of Information).
[14] *See* FINRA's Status Report at p. 9.