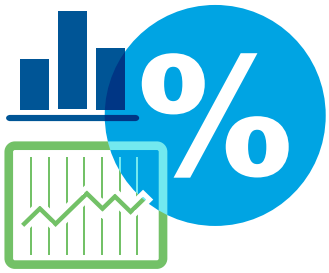
SEYFARTH SHAW



Financial Services Employment Arbitration Q&A

FINRA Arbitration Task Force Issues Recommendations on Key Issues

By Robert Whitman, Cameron Smith, and Samuel Sverdlov

FINRA's Arbitration Task Force, a group of 13 industry experts convened in July 2014, has issued a host of recommendations intended to improve the transparency, impartiality and efficiency of FINRA arbitration. The Task Force report, entitled *Interim Summary of Key Issues*, does not propose specific rule changes to the Code of Arbitration Procedure. But it makes broad-based policy suggestions that, if ultimately adopted by the FINRA Board of Governors and incorporated into rule amendments, would have a significant effect on the conduct and scope of FINRA arbitrations.

Of the Task Force's 13 proposals, the following 6 would be especially pertinent in FINRA arbitrations of employment-related claims:

1. *"Class action waivers should not be allowed in broker-dealers' Pre-Dispute Arbitration Agreements ("PDAAs") and the FINRA policy set forth in Schwab is strongly endorsed."*

Class action waivers in PDAAs have long been a source of dispute at FINRA, and recent decisions have left the viability of such provisions subject to question for member firms. In April 2014, in *Dep't of Enforcement v. Charles Schwab & Co.*, the Board of Governors held that, in light of Rule 12204, which provides that customer class actions may not be arbitrated at FINRA, and notwithstanding the Supreme Court's approval of class action waivers in PDAAs under the Fedearl Arbitration Act, member firms may not restrict public investors from bringing class actions in court. Then, on June 30, 2015, the Second Circuit in *Cohen v. UBS Fin. Servs., Inc.*, an employment case, held that Rule 13204 (the counterpart to the above rule for intra-industry cases) does not prohibit the use of class action waivers in PDAAs. To the contrary, the court said, the rule allows parties to enter into additional agreements beyond the scope of the Industry Code. Quoting from *Schwab*, the *Cohen* court explained, "there are no restrictions upon firms regarding the content of pre-dispute arbitration agreements with employees."

Perhaps not for long. If the Arbitration Task Force has its way, FINRA would impose an explicit prohibition on class action waivers in PDAAs for member firms. It is unclear, however, whether the Task Force's recommendation would apply to employment cases or only in the customer context. Because *Schwab* focused entirely on the Customer Code rather than the Industry Code (which governs employment cases), it is possible that the Task Force's recommendation is restricted to

strengthening and clarifying FINRA's rules prohibiting the use of class action waivers in PDAAs for customers only. But in light of *Cohen*, which stated that the existing rules under the FINRA Industry Code do not preclude the use of class action waivers, it is also possible that the Board of Governors could take a broader approach and embrace the Task Force's recommendation for all intra- industry disputes – including employment claims -- as well.

2. *In rules pertaining to arbitrator selection and disclosure: "Develop a rationale and procedure for voir dire of panel members and provide examples of appropriate questions… Propose modifications to the list selection process in light of the all-public panel options… Monitor the application of the recently adopted definitions of public and non-public arbitrators in light of concerns that individuals with substantial process and subject matter expertise are stricken from the lists… Strengthen disclosure requirements to highlight potential conflicts when arbitrators are assigned to multiple cases with the same witnesses, experts, documents, etc."*

The Task Force is hoping to strengthen disclosure requirements and develop a process for *voir dire* so that parties can have more access to information regarding arbitrators.

In June 2015, FINRA revised the definition of a "public" arbitrator, which now generally excludes anyone who worked in the financial services industry for any part of his or her career and those who represent investors or the industry as a significant part of their business. (See our blog post on this change *here*.) The Task Force said it is aware of concerns that the recently changed definition may significantly shrink the pool of qualified individuals who could be selected as public arbitrators and recommends that FINRA study the issue. However, it is unclear whether FINRA will respond to these concerns by increasing honoraria to recruit additional arbitrators or undertake other recruiting efforts.

3. *"Expand the grounds for Motions to Dismiss Prior to Conclusion of Case in Chief to include situations where the dispute was previously adjudicated by an order, judgment, award or decision."*

Under the existing rules, only three grounds are available for Motions to Dismiss prior to the conclusion of te claimant's case-in-chief: naming the wrong respondent, the six-year eligibility rule, and an executed release among the parties. The Task Force has recommended allowing respondents to bring an early motion to dismiss if the dispute was previously adjudicated to a final decision or award, essentially incorporating the doctrine of *res judicata* into the Code.

4. *"Explained Decisions. The FINRA rule should be amended to require explained decisions unless either party notifies FINRA, prior the IPHC, that it does not want an explained decision"*

Currently, parties seeking an explained decision from a panel must submit a joint request no later than the 20-day pre-hearing exchange. The Task Force hopes to retain the current "brief, fact-based format of the explanation" for arbitration decision, but seeks to add "some summary explanation of the reasons behind any damage calculation." To achieve this result, FINRA is expected to "develop and administer a training program on how to write explained decisions," which "chairs must comple… promptly after they are notified that an explained decision is expected in an assigned case." However, the Task Force has recommended that explained decisions be mandatory unless the parties decide, at the outset of the case, that they don't want one. Under the proposed new framework, the parties would have make this important strategic decision before any discovery takes place.

5. *"FINRA should seriously consider the adoption of a mandatory set of procedures for large claims, i.e., matters where the actual damages sought are at least $20 million, exclusive of consequential or punitive damages and attorneys' fees… The rules would, in general, give parties flexibility to set up alternative procedures to the FINRA rules, including an alternative method of selecting arbitrators. Limited use of depositions would be expressly authorized."*

This recommendation builds off the Large Case Pilot Program that FINRA established in 2012, which gives parties the leeway to choose other administrative procedures and take broader discovery than is permitted under FINRA rules if the case involves damage claims of at least $10 million. Under the proposed framework, the Large Case Pilot Program would become mandatory for claims that involve damages claims of at least $20 million. The most salient change under the Large Case Pilot Program is that depositions would be expressly authorized on a limited basis. Of course, at this point it is unclear to what extent depositions will be permitted, but the Task Force seems inclined to explore the use of depositions in larger cases.

6. *"Expungement. … The Task Force will give further consideration to the creation of a Special Arbitration Panel consisting of specially trained arbitrators to decide requests for expungement."*

The Task Force declined to make a recommendation on expungement, noting that FINRA and the North American Securities Adminstrators Association are currently "in discussions with respect to the expungement process." While it is difficult to glean how expungement proceedings might change based on the limited statement quoted above, the possibility of a Special Arbitration Panel for expungement cases poses some interesting questions. In cases requiring the resolution of multiple issues, one of which is expungement, a Special Arbitration Panel could mean that parties must engage in a duplicative parallel-track arbitration for the expungement issue separate from the other claims

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As always, we will continue to follow and keep you informed of any developments with regard to these recommendations as they make their way to the Board of Governors. Please direct any questions of concerns you may have concerning FINRA arbitration to our experienced team of attorneys.

Robert Whitman is a partner in Seyfarth's New York office, *Cameron Smith* is an associate in the firm's New York office, and Samuel Sverdlov is a senior fellow in the New York office. If you would like further information, please contact your Seyfarth Shaw LLP attorney, Robert Whitman at *rwhitman@seyfarth.com*, Cameron Smith at *casmith@seyfarth.com*, or Samuel Sverdlov at *ssverdlov@seyfarth.com*.