

All-public panels are a hit with investors, Finra says

Popularity of new program could quell calls to end mandatory arbitration

By Dan Jamieson

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After nearly a full year, the Financial Industry Regulatory Authority Inc.'s program to let investor plaintiffs exclude industry arbitrators from hearing panels has proved more popular than expected.

So popular is the program, in fact, that it could ease concerns about industry bias and help quell calls to end mandatory arbitration.

From the start of the all-public program in February 2011 through Jan. 26, more than three-quarters (76%) of investors chose the all-public option, which allows them to strike industry arbitrators from proposed lists of panelists.

That figure was up from a 54% opt-in rate during a 27-month pilot program, according to Finra.

Normally, investor cases are heard by three-person panels that include an "industry" arbitrator who works in or is associated with the financial industry.

The popularity of the all-public program is a "bit surprising, because the pilot numbers were lower," said Linda Fienberg, head of Finra's arbitration program.

Observers said a growing familiarity with the all-public option by plaintiff's attorneys is driving its widespread use.


The pilot also was limited to customer cases against a select group of firms and applied only to those cases where an individual broker was not named. The permanent program includes all firms, as well as cases against brokers.

"The program has given everyone an option" to use in a larger number of cases, said Ryan Bakhtiari, a partner at Aidikoff Uhl & Bakhtiari, and president of the Public Investors Arbitration Bar Association, which represents plaintiff's attorneys.

The Securities Industry and Financial Markets Association also supports the program.

"We also think it's quite important that an industry panelist remains an option for investors," Kevin

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Carroll, associate general counsel at the trade group, wrote in an e-mail.

SIFMA was smart to support all-public panels, said David Robbins, a plaintiff's lawyer and partner at Kaufmann Gildin Robbins & Oppenheim LLP.

The program has eased concerns about industry bias and helped counter the push by the plaintiff's bar and state regulators to end mandatory arbitration, he said.

"Finra had to respond this way because ... they were fearful they would be out of [the arbitration] business," Mr. Robbins said.

Finra "wanted to assuage customer's attorneys [about the process] and it's worked," he said.

"I do believe this [program] has removed the one issue [critics] could use to claim the [Finra arbitration] forum wasn't as fair as it might be," Ms. Fienberg said.

Data from the pilot program are inconclusive as to whether investors did better when they opted into the program.

Of 49 pilot program awards issued by all-public panels, investors were awarded damages in 26 of 40 cases, or 65% of the time, according to Finra. Another 23 pilot program awards were issued by panels with one nonpublic arbitrator, and in these instances, investors got relief 13 times, for a 62% win rate.

In nonpilot cases, win rates were lower: In 2009, arbitrators awarded damages to investors in 49% of cases; in 2010, the win rate was 48%.

However, Finra said that the award data are insufficient to draw meaningful conclusions about whether all-public panels tend to favor investors — a conclusion that others share.

"Talk to me in a year" about win rate data, Ms. Fienberg said.

"We'll have a better idea then" whether customers do better with all-public panels, she said.

The growing use of the all-public option has worried some industry arbitrators, who insist that they can be as tough, if not tougher, on industry malefactors as public panelists.

"I've noticed inquiries for me [to sit on panels] have dried up," said Neal Tourdo, national sales director at Mastrapasqua Asset Management Inc., who serves as an industry arbitrator.

Eliminating industry panelists "is a mistake," he said.

"Finra doesn't do a good job of educating [public] arbitrators about investments," Mr. Tourdo said.

For more technical products, such as derivatives, "the public arbitrators are generally unprepared," said Joseph Stineman, a partner and chief compliance officer at Fogel Neale Partners LLC, who is also an industry arbitrator.

He added, however, that his own caseload of four potential customer cases is heavier than ever.

Of the 1,431 cases in the permanent program that have ranked panelists, investors have chosen to strike all the industry people in 66% of the cases, according to Finra.

Despite the success of the all-public option, the plaintiff's bar and state regulators still want an

end to mandatory pre-dispute arbitration agreements.

“We think choice is working with the all-public program, and we think choice is the way to go in arbitration” overall, Mr. Bakhtiari said.

If arbitration were made optional, “I think [the industry] would improve the customer protection aspect of it,” such as providing for attorney’s fees and written decisions, said John Cronin, Vermont’s securities director and chairman of the North American Securities Administrators Association Inc.’s broker-dealer section.

The Dodd-Frank reform law gave the Securities and Exchange Commission authority to prohibit mandatory arbitration in brokerage contracts.

The commission hasn’t yet acted on that authority.

Mr. Robbins doesn’t think that will happen, due in large part to the all-public option.

Customers “are winning” in Finra arbitrations, he said.

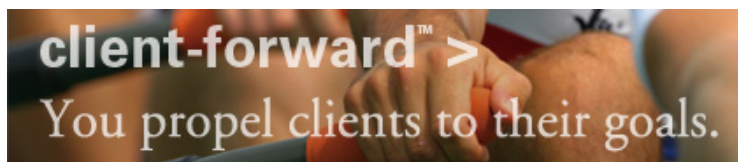
“Why kill a system where you can prevail?” Mr. Robbins said.

The SEC doesn’t have a timetable for looking into the arbitration issue, Ms. Fienberg said.

“My best guess ... is, they are mightily working to do [other] things with a time requirement first,” she said.

Meanwhile, Republican control of the House and recent Supreme Court decisions make legislation prohibiting mandatory pre-dispute agreements less likely, Ms. Fienberg said.

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