

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * <input type="text" value="24"/>	SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 Form 19b-4	File No.* SR - <input type="text" value="2013"/> - * <input type="text" value="003"/>	Amendment No. (req. for Amendments *) <input type="text"/>
---	--	---	--

Filing by Financial Industry Regulatory Authority
Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * <input checked="" type="checkbox"/>	Amendment * <input type="checkbox"/>	Withdrawal <input type="checkbox"/>	Section 19(b)(2) * <input checked="" type="checkbox"/>	Section 19(b)(3)(A) * <input type="checkbox"/>	Section 19(b)(3)(B) * <input type="checkbox"/>
			Rule		
Pilot <input type="checkbox"/>	Extension of Time Period for Commission Action * <input type="checkbox"/>	Date Expires * <input type="text"/>	<input type="checkbox"/> 19b-4(f)(1)	<input type="checkbox"/> 19b-4(f)(4)	
			<input type="checkbox"/> 19b-4(f)(2)	<input type="checkbox"/> 19b-4(f)(5)	
			<input type="checkbox"/> 19b-4(f)(3)	<input type="checkbox"/> 19b-4(f)(6)	

Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010 Section 806(e)(1) <input type="checkbox"/> Section 806(e)(2) <input type="checkbox"/>	Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934 Section 3C(b)(2) <input type="checkbox"/>
--	---

Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>
---	---

Description

Provide a brief description of the action (limit 250 characters, required when Initial is checked *).

Proposed rule change to amend FINRA's Customer and Industry Codes of Arbitration Procedure to revise the public arbitrator definition.

Contact Information

Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.

First Name * <input type="text" value="Margo"/>	Last Name * <input type="text" value="Hassan"/>
Title * <input type="text" value="Assistant Chief Counsel, FINRA Dispute Resolution"/>	
E-mail * <input type="text" value="margo.hassan@finra.org"/>	
Telephone * <input type="text" value="(212) 858-4481"/>	Fax <input type="text" value="(301) 527-4761"/>

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

(Title *)

Date <input type="text" value="01/04/2013"/>	<input type="text" value="Senior Vice President and Chief Counsel, FINRA Dispute Resolution"/>
By <input type="text" value="Kenneth Andrichik"/>	<input type="text" value="Kenneth Andrichik"/>

NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFF website.

Form 19b-4 Information *

Add Remove View

The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change *

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies

Add Remove View

The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

Add Remove View

Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

Add Remove View

Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

Add Remove View

The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

Add Remove View

The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

Add Remove View

If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ the Financial Industry Regulatory Authority, Inc. (“FINRA”) is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to amend the Customer and Industry Codes of Arbitration Procedure (“Codes”) to revise the definition of “public arbitrator” to exclude persons associated with a mutual fund or hedge fund from serving as public arbitrators and to require individuals to wait for two years after ending certain affiliations before they may be permitted to serve as public arbitrators. FINRA believes that the proposed amendments to the public arbitrator definition would improve investors’ perception about the fairness and neutrality of FINRA’s public arbitrator roster.

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

Customer Code

12100. Definitions

* * * * *

(u) Public Arbitrator

The term "public arbitrator" means a person who is otherwise qualified to serve as an arbitrator and:

(1) is not engaged in the conduct or activities described in paragraphs

(p)(1)–(4);

(2) was not engaged in the conduct or activities described in paragraphs

¹ 15 U.S.C. 78s(b)(1).

(p)(1)–(4) for a total of 20 years or more;

(3) is not an investment adviser, or associated with, including registered through, a mutual fund or hedge fund;

(4) is not an attorney, accountant, or other professional whose firm derived 10 percent or more of its annual revenue in the past two years from any persons or entities listed in paragraphs (p)(1)–(4);

(5) is not an attorney, accountant, or other professional whose firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to any persons or entities listed in paragraph (p)(1) relating to any customer disputes concerning an investment account or transaction, including but not limited to, law firm fees, accounting firm fees, and consulting fees;

(6) is not employed by, and is not the spouse or an immediate family member of a person who is employed by, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business;

(7) is not a director or officer of, and is not the spouse or an immediate family member of a person who is a director or officer of, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business; and

(8) is not the spouse or an immediate family member of a person who is engaged in the conduct or activities described in paragraphs (p)(1)–(4). For purposes of this rule, the term immediate family member means:

- (A) a person's parent, stepparent, child, or stepchild;
- (B) a member of a person's household;
- (C) an individual to whom a person provides financial support of more than 50 percent of his or her annual income; or
- (D) a person who is claimed as a dependent for federal income tax purposes.

A person whom FINRA would not designate as a public arbitrator because of an affiliation under subparagraphs (3)-(7) shall not be designated as a public arbitrator for two calendar years after ending the affiliation.

For purposes of this rule, the term "revenue" shall not include mediation fees received by mediators who are also arbitrators, provided that the mediator acts in the capacity of a mediator and does not represent a party in the mediation.

* * * * *

Industry Code

13100. Definitions

* * * * *

(u) Public Arbitrator

The term "public arbitrator" means a person who is otherwise qualified to serve as an arbitrator and:

(1) is not engaged in the conduct or activities described in paragraphs (p)(1)–(4);

(2) was not engaged in the conduct or activities described in paragraphs (p)(1)–(4) for a total of 20 years or more;

(3) is not an investment adviser, or associated with, including registered through, a mutual fund or hedge fund;

(4) is not an attorney, accountant, or other professional whose firm derived 10 percent or more of its annual revenue in the past two years from any persons or entities listed in paragraphs (p)(1)–(4);

(5) is not an attorney, accountant, or other professional whose firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to any persons or entities listed in paragraph (p)(1) relating to any customer disputes concerning an investment account or transaction, including but not limited to, law firm fees, accounting firm fees, and consulting fees;

(6) is not employed by, and is not the spouse or an immediate family member of a person who is employed by, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business;

(7) is not a director or officer of, and is not the spouse or an immediate family member of a person who is a director or officer of, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business; and

(8) is not the spouse or an immediate family member of a person who is engaged in the conduct or activities described in paragraphs (p)(1)–(4). For purposes of this rule, the term immediate family member means:

(A) a person's parent, stepparent, child, or stepchild;

- (B) a member of a person's household;
- (C) an individual to whom a person provides financial support of more than 50 percent of his or her annual income; or
- (D) a person who is claimed as a dependent for federal income tax purposes.

A person whom FINRA would not designate as a public arbitrator because of an affiliation under subparagraphs (3)-(7) shall not be designated as a public arbitrator for two calendar years after ending the affiliation.

For purposes of this rule, the term "revenue" shall not include mediation fees received by mediators who are also arbitrators, provided that the mediator acts in the capacity of a mediator and does not represent a party in the mediation.

* * * * *

- (b) Not applicable.
- (c) Not applicable.

2. Procedures of the Self-Regulatory Organization

At its meeting on April 18, 2012, the FINRA Board of Governors authorized the filing of the proposed rule change with the SEC. No other action by FINRA is necessary for the filing of the proposed rule change.

FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 30 days following publication of the Regulatory Notice announcing Commission approval.

Questions regarding this rule filing may be directed to Margo Hassan, Assistant Chief Counsel, FINRA Dispute Resolution, at (212) 858-4481.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Background

FINRA classifies arbitrators under the Codes as either “non-public” or “public” (non-public arbitrators are often referred to as “industry” arbitrators). Non-public arbitrators are affiliated with the securities industry either through their current or former employment in a securities business, or because they provide professional services to securities businesses. Public arbitrators do not have any significant affiliation with the securities industry; nor are they related to anyone with a significant affiliation to the securities industry.

To improve investor confidence in the neutrality of FINRA’s public arbitrator roster, FINRA has amended its arbitrator definitions a number of times over the years. In 2004, FINRA amended the definitions of public arbitrator and non-public arbitrator to:

- Increase from three years to five years the period for transitioning from a non-public to public arbitrator after leaving the securities industry;
- Clarify that the term "retired" from the industry includes anyone who spent a substantial part of his or her career in the industry;
- Prohibit anyone who has been associated with the industry for at least 20 years from ever becoming a public arbitrator, regardless of how long ago the association ended;
- Exclude from the public arbitrator roster attorneys, accountants, or other

professionals whose firms have derived 10 percent or more of their annual revenue in the previous two years from clients involved in securities related activities; and

- Provide that investment advisers may not serve as public arbitrators, and may only serve as non-public arbitrators if they otherwise qualify as non-public.²

In 2007, FINRA revised the public arbitrator definition to exclude individuals who were employed by, or who served as an officer or director of, a company in a control relationship with a broker/dealer. Individuals were also excluded if their spouse or immediate family member served in such a capacity. In this rule change, FINRA also made it clear that people registered through a broker/dealer could not be public arbitrators even if they are employed by a non-broker/dealer (such as a bank).³

Finally, in 2008, FINRA revised the public arbitrator definition to add a dollar limit to the 2004 10 percent rule. This precluded an attorney, accountant, or other professional from serving as a public arbitrator if the individual's firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to

² See Securities Exchange Act Rel. No. 49573 (April 16, 2004), 69 FR 21871 (April 22, 2004) (File No. SR-NASD-2003-95)(Order Granting Approval to a Proposed Rule Change Relating to Arbitrator Classification and Disclosure in NASD Arbitrations). The changes were announced in Notice to Members 04-49 (June 2004).

³ See Securities Exchange Act Rel. No. 54607 (Oct. 16, 2006), 71 FR 62026 (Oct. 20, 2006) (File No. SR-NASD-2005-094)(Order Approving Proposed Rule Change and Amendment No. 1 Thereto Relating to Amendments to the Classification of Arbitrators Pursuant to Rule 10308 of the NASD Code of Arbitration Procedure). The changes were announced in Notice to Members 06-64 (November 2006).

certain industry entities relating to customer disputes concerning an investment account or transaction.⁴

Proposal to Amend the Arbitrator Definition

Recently, FINRA investor representatives raised concerns that they do not perceive certain arbitrators on the public roster as public because of their background or experience. To respond to this perception, FINRA is proposing to amend the public arbitrator definition to exclude persons associated with a mutual fund or hedge fund from serving as public arbitrators and to require individuals to wait for two years after ending certain affiliations before FINRA permits them to serve as public arbitrators.

The public arbitrator definition does not expressly prohibit individuals associated with mutual funds and hedge funds from serving as public arbitrators. However, because of their association with the financial services industry, Staff believes that these individuals should not serve as public arbitrators. Therefore, Staff's current practice is to exclude these individuals from the public arbitrator roster until they terminate their affiliation with the hedge fund or mutual fund. For example, FINRA removed a public arbitrator from the roster because he was serving as a director of a mutual fund. FINRA is proposing to amend Rules 12100(u)(3) and 13100(u)(3), which exclude investment advisers from serving as public arbitrators, to exclude also persons associated with, including registered through, a mutual fund or hedge fund. The proposed rule change would respond to questions and concerns raised about arbitrator service by persons associated with mutual funds and hedge funds.

⁴ See Securities Exchange Act Rel. No. 57492 (March 13, 2008), 73 FR 15025 (March 20, 2008) (File No. SR-NASD-2007-021)(Order Approving Proposed Rule Change To Amend the Definition of Public Arbitrator). The changes were announced in Regulatory Notice 08-22 (May 2008).

FINRA is also proposing to amend the public arbitrator definition to add a two-year “cooling off” period before FINRA permits certain individuals to serve as public arbitrators. Currently under the Codes, an individual may not serve as a public arbitrator if he or she is:

- an investment adviser;
- an attorney, accountant, or other professional whose firm derived 10 percent or more of its annual revenue in the past two years from certain financial industry entities;
- an attorney, accountant, or other professional whose firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to certain financial industry entities relating to any customer disputes concerning an investment account or transaction;
- employed by, or is the spouse or an immediate family member of a person who is employed by, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business; or
- a director or officer of, or is the spouse or an immediate family member of a person who is a director or officer of, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business.

However, as soon as the individual ends the affiliation that was the basis for the exclusion from the public roster, the individual may begin serving as a public arbitrator.

In one instance, an individual applying to be a public arbitrator had retired one month

earlier from a lengthy career at a law firm that represented securities industry clients. Rule 12100(u)(5) provides that a public arbitrator may not be an attorney, accountant, or other professional whose firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to specified securities industry clients relating to any customer disputes concerning an investment account or transaction. The applicant confirmed that the firm derived revenue of at least \$50,000 during the past two years from clients in the securities industry relating to customer disputes. If the individual applied while employed at the firm, FINRA would not have approved the application. However, since the applicant left the firm one month earlier, and the rule does not include a cooling off period, the applicant was permitted to join the public arbitrator roster.

FINRA is proposing to amend Rules 12100(u) and 13100(u) to provide that a person whom FINRA would not designate as a public arbitrator because of an affiliation under subparagraphs (3)-(7) (the exclusions detailed in the bullets above) shall not be designated as a public arbitrator for two calendar years after ending the affiliation. As stated above, FINRA is proposing to add persons associated with mutual funds and hedge funds to Rules 12100(u)(3) and 13100(u)(3). Therefore, the two-year cooling off period would apply to these individuals as well. FINRA believes that the cooling off period would improve its constituents' perception about the neutrality of the arbitrators on the public roster.

As noted in Item 2 of this filing, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice to be published no later than 60 days following Commission approval. The effective date will be no later than 30 days following publication of the Regulatory Notice announcing Commission approval.

(b) Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁵ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed amendments to the public arbitrator definition would benefit investors by addressing concerns raised about the fairness and neutrality of FINRA's public arbitrator roster. By prohibiting persons associated with mutual funds or hedge funds from serving on the public roster, the proposed amendments further restrict the professional affiliations that a public arbitrator may have with the securities industry. The proposed two-year cooling off period ensures that potential arbitrators have sufficient separation from their affiliations to the securities industry. These restrictions would improve investors' perception of fairness and neutrality of the public roster.

4. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

⁵ 15 U.S.C. 78o-3(b)(6).

6. Extension of Time Period for Commission Action

FINRA does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.⁶

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibits

Exhibit 1. Completed notice of proposed rule change for publication in the Federal Register.

⁶ 15 U.S.C. 78s(b)(2).

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-FINRA-2013-003)

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change Relating to Amendments to the Customer and Industry Codes of Arbitration Procedure to Revise the Public Arbitrator Definition

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on January 4, 2013, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend the Customer and Industry Codes of Arbitration Procedure (“Codes”) to revise the definition of “public arbitrator” to exclude persons associated with a mutual fund or hedge fund from serving as public arbitrators and to require individuals to wait for two years after ending certain affiliations before they may be permitted to serve as public arbitrators. FINRA believes that the proposed

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

amendments to the public arbitrator definition would improve investors' perception about the fairness and neutrality of FINRA's public arbitrator roster.

The text of the proposed rule change is available on FINRA's website at <http://www.finra.org>, at the principal office of FINRA and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Background

FINRA classifies arbitrators under the Codes as either "non-public" or "public" (non-public arbitrators are often referred to as "industry" arbitrators). Non-public arbitrators are affiliated with the securities industry either through their current or former employment in a securities business, or because they provide professional services to securities businesses. Public arbitrators do not have any significant affiliation with the securities industry; nor are they related to anyone with a significant affiliation to the securities industry.

To improve investor confidence in the neutrality of FINRA's public arbitrator roster, FINRA has amended its arbitrator definitions a number of times over the years.

In 2004, FINRA amended the definitions of public arbitrator and non-public arbitrator to:

- Increase from three years to five years the period for transitioning from a non-public to public arbitrator after leaving the securities industry;
- Clarify that the term "retired" from the industry includes anyone who spent a substantial part of his or her career in the industry;
- Prohibit anyone who has been associated with the industry for at least 20 years from ever becoming a public arbitrator, regardless of how long ago the association ended;
- Exclude from the public arbitrator roster attorneys, accountants, or other professionals whose firms have derived 10 percent or more of their annual revenue in the previous two years from clients involved in securities related activities; and
- Provide that investment advisers may not serve as public arbitrators, and may only serve as non-public arbitrators if they otherwise qualify as non-public.³

In 2007, FINRA revised the public arbitrator definition to exclude individuals who were employed by, or who served as an officer or director of, a company in a control relationship with a broker/dealer. Individuals were also excluded if their spouse or

³ See Securities Exchange Act Rel. No. 49573 (April 16, 2004), 69 FR 21871 (April 22, 2004) (File No. SR-NASD-2003-95)(Order Granting Approval to a Proposed Rule Change Relating to Arbitrator Classification and Disclosure in NASD Arbitrations). The changes were announced in Notice to Members 04-49 (June 2004).

immediate family member served in such a capacity. In this rule change, FINRA also made it clear that people registered through a broker/dealer could not be public arbitrators even if they are employed by a non-broker/dealer (such as a bank).⁴

Finally, in 2008, FINRA revised the public arbitrator definition to add a dollar limit to the 2004 10 percent rule. This precluded an attorney, accountant, or other professional from serving as a public arbitrator if the individual's firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to certain industry entities relating to customer disputes concerning an investment account or transaction.⁵

Proposal to Amend the Arbitrator Definition

Recently, FINRA investor representatives raised concerns that they do not perceive certain arbitrators on the public roster as public because of their background or experience. To respond to this perception, FINRA is proposing to amend the public arbitrator definition to exclude persons associated with a mutual fund or hedge fund from serving as public arbitrators and to require individuals to wait for two years after ending certain affiliations before FINRA permits them to serve as public arbitrators.

⁴ See Securities Exchange Act Rel. No. 54607 (Oct. 16, 2006), 71 FR 62026 (Oct. 20, 2006) (File No. SR-NASD-2005-094)(Order Approving Proposed Rule Change and Amendment No. 1 Thereto Relating to Amendments to the Classification of Arbitrators Pursuant to Rule 10308 of the NASD Code of Arbitration Procedure). The changes were announced in Notice to Members 06-64 (November 2006).

⁵ See Securities Exchange Act Rel. No. 57492 (March 13, 2008), 73 FR 15025 (March 20, 2008) (File No. SR-NASD-2007-021)(Order Approving Proposed Rule Change To Amend the Definition of Public Arbitrator). The changes were announced in Regulatory Notice 08-22 (May 2008).

The public arbitrator definition does not expressly prohibit individuals associated with mutual funds and hedge funds from serving as public arbitrators. However, because of their association with the financial services industry, Staff believes that these individuals should not serve as public arbitrators. Therefore, Staff's current practice is to exclude these individuals from the public arbitrator roster until they terminate their affiliation with the hedge fund or mutual fund. For example, FINRA removed a public arbitrator from the roster because he was serving as a director of a mutual fund. FINRA is proposing to amend Rules 12100(u)(3) and 13100(u)(3), which exclude investment advisers from serving as public arbitrators, to exclude also persons associated with, including registered through, a mutual fund or hedge fund. The proposed rule change would respond to questions and concerns raised about arbitrator service by persons associated with mutual funds and hedge funds.

FINRA is also proposing to amend the public arbitrator definition to add a two-year "cooling off" period before FINRA permits certain individuals to serve as public arbitrators. Currently under the Codes, an individual may not serve as a public arbitrator if he or she is:

- an investment adviser;
- an attorney, accountant, or other professional whose firm derived 10 percent or more of its annual revenue in the past two years from certain financial industry entities;
- an attorney, accountant, or other professional whose firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to

certain financial industry entities relating to any customer disputes concerning an investment account or transaction;

- employed by, or is the spouse or an immediate family member of a person who is employed by, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business; or
- a director or officer of, or is the spouse or an immediate family member of a person who is a director or officer of, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business.

However, as soon as the individual ends the affiliation that was the basis for the exclusion from the public roster, the individual may begin serving as a public arbitrator. In one instance, an individual applying to be a public arbitrator had retired one month earlier from a lengthy career at a law firm that represented securities industry clients. Rule 12100(u)(5) provides that a public arbitrator may not be an attorney, accountant, or other professional whose firm derived \$50,000 or more in annual revenue in the past two years from professional services rendered to specified securities industry clients relating to any customer disputes concerning an investment account or transaction. The applicant confirmed that the firm derived revenue of at least \$50,000 during the past two years from clients in the securities industry relating to customer disputes. If the individual applied while employed at the firm, FINRA would not have approved the application. However, since the applicant left the firm one month earlier, and the rule does not include a cooling off period, the applicant was permitted to join the public arbitrator roster.

FINRA is proposing to amend Rules 12100(u) and 13100(u) to provide that a person whom FINRA would not designate as a public arbitrator because of an affiliation under subparagraphs (3)-(7) (the exclusions detailed in the bullets above) shall not be designated as a public arbitrator for two calendar years after ending the affiliation. As stated above, FINRA is proposing to add persons associated with mutual funds and hedge funds to Rules 12100(u)(3) and 13100(u)(3). Therefore, the two-year cooling off period would apply to these individuals as well. FINRA believes that the cooling off period would improve its constituents' perception about the neutrality of the arbitrators on the public roster.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁶ which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed amendments to the public arbitrator definition would benefit investors by addressing concerns raised about the fairness and neutrality of FINRA's public arbitrator roster. By prohibiting persons associated with mutual funds or hedge funds from serving on the public roster, the proposed amendments further restrict the professional affiliations that a public arbitrator may have with the securities industry. The proposed two-year cooling off period ensures that potential arbitrators have sufficient separation from their affiliations to the securities industry.

⁶ 15 U.S.C. 78o-3(b)(6).

These restrictions would improve investors' perception of fairness and neutrality of the public roster.

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2013-003 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2013-003. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You

should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2013-003 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁷

Elizabeth M. Murphy
Secretary

⁷ 17 CFR 200.30-3(a)(12).