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October 23, 2008

Ms. Florence Harmon  
Deputy Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090  
**(rule-comments@sec.gov)**

Re: **File Number SR-FINRA-2008-047**  
**Proposed rule change to amend Rule 12401 of the Customer Code**  
**and Rule 13401 of the Industry Code to raise the amount in**  
**controversy heard by a single chair-qualified arbitrator to**  
**\$100,000.**

Dear Ms. Harmon:

Charles Schwab & Co., Inc. ("Schwab") welcomes the opportunity to comment on SR-FINRA-2008-047, FINRA's proposal to change its arbitration rules to have all claims of \$100,000 or less heard by a single chair-qualified arbitrator ("the Proposed Rule"). Schwab recognizes that any rule relating to the arbitration process potentially affects the interests of several different parties, including public investors, FINRA member firms and their associated persons, and Schwab commends FINRA for its ongoing efforts to enhance the arbitration process.

Nevertheless, Schwab does not support the Proposed Rule, which FINRA says will "increase efficiencies and decrease costs for parties and FINRA." The only reasons given for this change to a long-standing and important element of arbitration procedure are purely administrative in nature – namely, easier scheduling of pre-hearing conferences and hearings, reduced forum fees for parties, and reduced copying and mailing costs for parties and FINRA.

On the other hand, the Proposed Rule offers no substantive reasons for this change. Nor does the Proposed Rule discuss, or even mention, the impact this change would have on the quality of the awards issued by FINRA panels. Schwab believes the Proposed Rule will diminish the quality of the decision making process in FINRA arbitrations by eliminating the collaborative, deliberative process that occurs with three arbitrator panels. For that reason, Schwab urges the Securities and Exchange Commission (SEC) not to approve the Proposed Rule.

### **A. The Proposed Rule Places Administrative Form Over Substance**

The Proposed Rule is wholly based on FINRA's tenuous premise that it will increase efficiency and decrease costs. Regarding increased efficiency, FINRA notes, among other things, that parties will save time by vetting fewer prospective arbitrators and will enjoy reduced case processing times because it will be easier to schedule conference calls and hearing dates. It is undeniably true that reviewing eight potential arbitrators instead of twenty four would take less time, but that is hardly a sufficient reason to remove two arbitrators from arbitrations where up to \$100,000 may be at stake.<sup>1</sup> And while it may also be true that parties will experience marginally faster scheduling of pre-hearing conferences and hearings, Schwab doubts that having a single arbitrator will reduce case processing times to such an extent as to justify a fundamental change to the arbitration process.

FINRA's decreased costs rationale is also open to question. First, the reduced hearing session fees highlighted in the proposal are relatively small – a maximum savings of \$600 per day according to FINRA. Such small savings do not justify a wholesale change to FINRA arbitration procedure. This is all the more true given that the costs at issue are more often than not split between the parties, resulting in a savings of \$300 per party per day. In addition, parties to the majority of cases would not see these minor savings multiplied over numerous hearing sessions because most cases are resolved without a hearing.<sup>2</sup> Second, FINRA's observations that parties and FINRA would save on photocopying costs, and FINRA would enjoy some limited savings on its mailing costs, are far from compelling reasons to allow single arbitrators to decide cases of up to \$100,000. FINRA's analysis should focus on whether parties to these cases will get better or worse decisions, not whether their copying costs will be marginally reduced. We suggest that the highly deleterious effect the Proposed Rule will have on a balanced, equitable and fair decision making process can not be justified by minimal administrative cost saving.

### **B. The Proposed Rule Will Degrade the Decision Making Process for FINRA Awards**

In contrast to the myriad administrative reasons given by FINRA to support the Proposed Rule, FINRA has not offered a single substantive reason why this change should be made. Schwab submits that there are no such reasons. In fact, there are several reasons to conclude that the proposed change will degrade the decision making process and, by extension, the quality of the awards rendered by FINRA panels.

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<sup>1</sup> The same would be true for cases of \$101,000 or \$1,000,000. Presumably FINRA is not proposing a similar change for cases of over \$100,000 because it recognizes that three person panels are appropriate for those cases.

<sup>2</sup> According to statistics posted on [www.finra.org](http://www.finra.org), approximately 80% of cases resolved since 2005 have been resolved without a hearing.

As any FINRA arbitrator knows, the process of arriving at an award is a fluid, collaborative process, with each arbitrator offering his or her view of the facts, the evidence presented, and how the case should be decided. I am an NASD/FINRA arbitrator, and I have witnessed this process first-hand. Each arbitrator brings his or her perspective and experience to the deliberations, and the decision is almost always a unanimous decision reflecting the views of all of the arbitrators. By the same token, one arbitrator's inaccurate view of a case can be nullified by his colleagues' majority ruling. The Proposed Rule would do away with this important safeguard.

The Proposed Rule will eliminate this deliberative process and will instead put the power to render an award of up to \$100,000 in the hands of a single arbitrator.<sup>3</sup> That is simply too much money to allow one arbitrator to award (or refuse to award), and it poses an unacceptable threat to both parties' rights to a full and fair hearing. Until now, NASD/FINRA has agreed. Indeed, the current process assigns a three arbitrator panel to any case for over \$50,000 and, importantly, to any case over \$25,000 if one party so requests.<sup>4</sup> Thus, FINRA itself acknowledges that three person panels are appropriate for larger dollar cases, and, by implication, single arbitrators are not.

FINRA has offered no compelling reason for this change. The fact that case filings are rising this year - or that the proposal will bring the percentage of cases heard by a single arbitrator back to what it was in 1998 - is wholly irrelevant to the debate.<sup>5</sup> These are simply more administrative facts being used as cover for a substantive policy change. The real question is how many arbitrators should decide cases of between \$25,000 and \$100,000, and in that regard FINRA's long-standing policy has been correct all along - three person panels should decide these cases.

The Proposed Rule represents a fundamental change in FINRA arbitration procedure and, yet, is being justified on purely administrative grounds. Arbitration policy should be based on more than that, and the consequences of this change - for both Claimants and Respondents - are more significant than just increased efficiencies and decreased costs. For all these reasons, Schwab respectfully urges the SEC not to approve the Proposed Rule.

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<sup>3</sup> The Proposed Rule will also result in the removal of the industry arbitrator from a large portion of FINRA arbitrations without any public comment or debate. This unstated change highlights another anomaly of the Proposed Rule - that FINRA will now have a two-tiered system where industry arbitrators are used in some cases but not others.

<sup>4</sup> The Proposed Rule eliminates this procedure and would only allow a three person panel if one was requested by all parties.

<sup>5</sup> See FINRA press release September 26, 2008. Moreover, the abnormally low case filings of 2007 are a poor basis for comparison.

Thank you for considering Schwab's comments on this important issue.

Very truly yours,

A handwritten signature in black ink, appearing to read 'G. Scanlon', with a large, sweeping flourish extending to the right.

Gregory M. Scanlon  
Vice President & Associate General Counsel  
Charles Schwab & Co., Inc.