

June 2, 2016

Via Email Only

Brent J. Fields
Office of the Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
rule-comments@sec.gov

RE: SR-FINRA-2016-014: Proposed Rule Change to Amend FINRA Regulation, Inc. By-Laws Relating to National Adjudicatory Council Composition, Member Terms and Election Procedures

Dear Secretary Fields,

I write to support SR-FINRA-2016-014. The proposed rule amends FINRA by-laws to alter the appointment process and service terms for FINRA's National Adjudicatory Council (NAC). The proposed rule changes will affect the NAC in three ways: (i) expanding the size of the NAC and requiring that it include a majority of non-industry members; (ii) extending the terms of office for future NAC members; and (iii) modernizing the selection process to be implemented for contested nominations and elections for certain industry-affiliated members of the NAC. These changes will improve the NAC.

The NAC plays a vital role. It reviews initial decisions from FINRA disciplinary and membership proceedings, giving it the power to shape how FINRA exercises its authority. Its decisions provide important guidance to FINRA member firms about their obligations and FINRA's priorities.

I. The Proposed Changes Will Improve the NAC

(i) Proposal to Change the Composition and Size of the NAC:

Under the current by-laws, the NAC contains fourteen members, evenly split between industry and non-industry members.¹ The proposal will shift the balance by requiring a majority of non-industry members.

The NAC's current composition may interfere with its ability to act to protect investors in instances where investor and industry interests diverge. For example, if the Industry and Non-Industry Members of the NAC disagree, the current committee may not be able to act effectively.

¹ See FINRA Regulation, Inc. By-Laws, Art. V., Sec. 5.2 (Number of Members and Qualifications), paragraph (a).

Furthermore, FINRA's legitimacy partially depends on whether the NAC is viewed as an impartial and fair adjudicatory body. Altering the NAC's composition to include a majority of non-industry members should enhance its reputation for impartiality and reduce the possibility of deadlock.

(ii) Proposal to Change NAC Member Terms:

Under the current by-laws, NAC members are divided into three classes, with members serving three-year terms of office that commence and expire on a staggered, annual basis.² These short terms drive significant annual turnover. Four NAC members' terms will expire on January 1, 2017 (*Burton, Polanin, Santaniello, and Muschalek*).³ Five members' terms will expire on January 1, 2018 (*Mandelbaum, Tull, Sale, Wyderko, and Kohn*).⁴ And the remaining five members' terms will expire on January 1, 2019 (*Bergers, Hurt, McDonald, Williams, and Rodgers*).⁵

This yearly turnover, about one-third of the NAC members, compromises the NAC's effectiveness. Freshly appointed NAC members may not be as effective as more experienced members. In any event, unseasoned members lack the same institutional knowledge as members that have spent a more significant amount of time on the NAC. Extending NAC member terms will likely improve the NAC's functioning.

(iii) Proposal to Change the NAC Selection Process:

The proposed rule change also updates an outdated NAC member selection process. For example, the current by-laws seem to suggest that members may only vote via paper ballots. The proposed rule will allow FINRA to move to more efficient procedures and implement electronic balloting.⁶

II. The NAC Appointment Process Remains Flawed

While the proposed changes to the NAC will do some good, the modest changes will not fully ensure the NAC's independence and impartiality. Persons that meet the technical requirements for "Non-Industry" members may remain susceptible to pressure because they may have material business relationships with the industry.

Under the current structure, persons with significant industry connections may qualify as "Non-Industry" members. Consider the technical requirements to qualify for a Non-Industry Member position on the NAC:

² See FINRA Regulation, Inc. By-Laws, Article V, Section 5.6 (Term of Office), paragraphs (a) and (b).

³ See FINRA Election Notice - 12/17/13, (2013).

⁴ See FINRA Election Notice - 12/05/14, (2014).

⁵ See FINRA Election Notice - 12/18/15, (2015).

⁶ The proposal will also eliminate a provision that allows NAC candidates or their representatives to demand to personally observe ballot tabulation. Because FINRA uses an independent agent to tabulate ballots, there does not seem to be any good reason to maintain this special, additional protection for the elected NAC positions.

[A] "Non-Industry Member" means a NAC or committee member who is (1) a Public Member; (2) an officer or employee of an issuer of securities listed on a market for which FINRA provides regulation; (3) an officer or employee of an issuer of unlisted securities that are traded in the over-the-counter market; or (4) any other individual who would not be an Industry Member.⁷

This broad definition for non-industry members permits persons with material business relationships with the industry to serve as non-industry members. The current by-laws and the proposed amendments, only require FINRA to include three "Public Members" on the NAC. Public Members are non-industry members with "no material business relationship with a broker or dealer or a self-regulatory organization registered under the Act."⁸ Even with the proposal's improvements, the majority of non-industry NAC members may have material business entanglements with industry members.

FINRA should closely examine its appointment processes to ensure that non-industry appointees are both qualified and independent. If possible, FINRA should strive to increase the number of Public Member appointees to something significantly above the current three-member minimum.

I thank the Securities and Exchange Commission for considering this comment letter.

Respectfully submitted,

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⁷ See FINRA Regulation, Inc. By-Laws, Article I, paragraph (ee).

⁸ See FINRA Regulation, Inc. By-Laws, Article I, paragraph (hh).