

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-84418; File No. SR-FINRA-2018-026)

October 12, 2018

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving a Proposed Rule Change to Amend the Arbitrator Payment Rule to Pay Each Arbitrator a \$200 Honorarium to Decide Without a Hearing Session a Contested Subpoena Request or a Contested Order for Production or Appearance

I. Introduction

On July 13, 2018, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Exchange Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend FINRA Rule 12214(c) of the Code of Arbitration Procedure for Customer Disputes (“Customer Code”) and FINRA Rule 13214(c) through (e) of the Code of Arbitration Procedure for Industry Disputes (“Industry Code” and together, “Codes”), to provide that FINRA will pay each arbitrator a \$200 honorarium to decide without a hearing session a contested subpoena request or a contested order for production or appearance.

The proposed rule change was published for comment in the Federal Register on July 30, 2018.<sup>3</sup> The public comment period closed on August 20, 2018. The Commission received four comment letters in response to the Notice, all supporting the proposed rule change.<sup>4</sup> On October

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Exchange Act Release No. 83699 (Jul. 24, 2018), 83 FR 36647 (Jul. 30, 2018) (File No. SR-FINRA-2018-026) (“Notice”).

<sup>4</sup> See Letter from Steven B. Caruso, Maddox Hargett Caruso, P.C., dated July 25, 2018 (“Caruso Letter”); letter from Ryan K. Bakhtiari, Aidikoff, Uhl and Bakhtiari, dated July 31, 2018 (“Bakhtiari Letter”); letter from Glenn S. Gitomer, McCausland, Keen and Buckman, dated August 1, 2018 (“Gitomer Letter”); and letter from Andrew Stoltmann, President, Public Investors Arbitration Bar Association (“PIABA”), dated August 15,

5, 2018, FINRA responded to the comment letters received in response to the Notice.<sup>5</sup> On August 23, 2018, FINRA extended the time period in which the Commission must approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change to October 26, 2018.<sup>6</sup> This order approves the proposed rule change.

## II. Description of the Proposed Rule Change<sup>7</sup>

### **Background**

Parties to an arbitration typically exchange documents and information with each other to prepare for the arbitration through the discovery process.<sup>8</sup> If one party objects to a discovery request, the party seeking the documents or information, or appearance may file a motion requesting that the arbitrator issue a subpoena<sup>9</sup> or an order compelling discovery.<sup>10</sup> The

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2018 (“PIABA Letter”). Comment letters are available on the Commission’s website at <https://www.sec.gov>.

<sup>5</sup> See Letter from Mignon McLemore, Assistant Chief Counsel, FINRA, to Mr. Brent J. Fields, Secretary, U.S. Securities and Exchange Commission, dated October 5, 2018 (“FINRA Letter”). The FINRA Letter is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA, at the Commission’s website at [http://www.finra.org/sites/default/files/rule\\_filing\\_file/SR-FINRA-2018-026-response-to-comments.pdf](http://www.finra.org/sites/default/files/rule_filing_file/SR-FINRA-2018-026-response-to-comments.pdf), and at the Commission’s Public Reference Room.

<sup>6</sup> See Letter from Mignon McLemore, Assistant Chief Counsel, FINRA, to Lourdes Gonzalez, Assistant Chief Counsel – Sales Practices, Division of Trading and Markets, Securities and Exchange Commission, dated August 23, 2018.

<sup>7</sup> The subsequent description of the proposed rule change is substantially excerpted from FINRA’s description in the Notice. See Notice, 83 FR at 36648-36649.

<sup>8</sup> See FINRA Rules 12505 and 13505.

<sup>9</sup> See FINRA Rules 12512 and 13512.

<sup>10</sup> See FINRA Rules 12513 and 13513.

opposing party may oppose the filing party's motion, contesting the request for a subpoena<sup>11</sup> or order compelling discovery.

### **Subpoena for Appearance**

Currently, under FINRA Rule 12214(d),<sup>12</sup> each arbitrator who decides one or more contested subpoenas without a hearing session receives a one-time honorarium of \$250 during the life of the arbitration case.<sup>13</sup> The rule caps the total amount that the parties could pay the arbitrators to decide contested subpoena requests without a hearing in any one case at \$750.<sup>14</sup> The panel allocates the cost of the honorarium to the parties in the award.<sup>15</sup> Arbitrators do not receive an honorarium for deciding unopposed requests to issue a subpoena.<sup>16</sup>

### **Order for Production or Appearance**

The Codes do not expressly provide an honorarium for arbitrators who decide requests for orders for production or appearance without a hearing session. FINRA does, however,

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<sup>11</sup> See FINRA Rules 12512(c) and 13512(c).

<sup>12</sup> See also FINRA Rule 13214(d).

<sup>13</sup> See FINRA Rules 12214(d)(1) and 13214(d)(1).

If a hearing session is required to decide the motion, each arbitrator who participates in the hearing session will receive a \$300 honorarium instead. See FINRA Rules 12214(a) and 13214(a).

<sup>14</sup> See FINRA Rules 12214(d)(1) and 13214(d)(1). The chairperson of a three-person panel will decide the contested subpoena request without a hearing session, for which the chairperson would be paid \$250. The honorarium for contested subpoena requests could increase in \$250 increments, if, for example, the chairperson recuses or withdraws from the panel and the replacement chairperson must decide another contested subpoena request without a hearing session. In this instance, the replacement chairperson would receive a \$250 honorarium for this work. In no event would the parties be charged more than \$750 per case. See Notice at 36648, note 14.

<sup>15</sup> See FINRA Rules 12214(d)(3) and 13214(d)(3).

<sup>16</sup> See Notice at 36648.

provide arbitrators a \$200 honorarium to decide discovery-related motions without a hearing.<sup>17</sup> Accordingly, FINRA categorizes requests to issue orders for production as discovery-related motions and pays \$200 honorarium for each arbitrator deciding the order, regardless of whether it is contested. FINRA does not pay the honorarium, however, for an order for appearance, regardless of whether it is contested or unopposed.<sup>18</sup>

### **Proposed Rule Change**

FINRA is proposing to amend FINRA Rules 12214(c) and 13214(c) to provide that FINRA would pay each arbitrator an honorarium of \$200 to decide, without a hearing session: (i) a discovery-related motion;<sup>19</sup> (ii) a motion that contains one or more contested subpoena requests<sup>20</sup> or contested orders for production or appearance; or (iii) a motion that contains one or more contested subpoena requests and contested orders for production or appearance.<sup>21</sup>

### **Contested Subpoena**

Specifically, the proposed rule change would reduce the honorarium that an arbitrator receives to decide a contested subpoena request from \$250 to \$200; however, it would also

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<sup>17</sup> FINRA Rules 12214(c) and 13214(c) provide that FINRA will pay each arbitrator an honorarium of \$200 to decide a discovery-related motion without a hearing session.

<sup>18</sup> See Notice at 36648-36649.

<sup>19</sup> Under the proposed rule change, FINRA would add a contested subpoena request and a contested order for production or appearance to the discovery-related motions rule; however, FINRA would not change the rule language explaining what constitutes a discovery-related motion. See Notice at 36649, note 27.

<sup>20</sup> The proposal would retain what constitutes a contested subpoena by moving the description from FINRA Rule 12214(d)(2) to FINRA Rule 12214(c)(2)(ii). See Notice at 36649, note 28.

<sup>21</sup> See Notice at 36649.

remove the per-case cap on these payments. Thus, under the proposed rule change, an arbitrator would receive a \$200 honorarium for each contested subpoena request that he or she decides.<sup>22</sup>

### **Contested Orders for Production or Appearance**

In addition, the proposed rule change would now expressly provide a \$200 honorarium for arbitrators deciding a contested order for production or appearance without a hearing session. Specifically, FINRA would not need to categorize requests to issue orders for production as discovery-related motions. Similarly, arbitrators would receive an honorarium for deciding without a hearing session, a contested arbitrator order for appearance as well as for production. Under the proposal, however, arbitrators would no longer receive an honorarium for deciding unopposed requests to issue an order for production<sup>23</sup>

The proposed rule change would describe what constitutes a contested order for production or appearance by modeling the description on that of a contested subpoena request. Specifically, proposed FINRA Rule 12214(c)(2)(iii) would provide that a contested order for production or appearance shall include a motion requesting the issuance of an order for production or appearance, a written objection from the party opposing the issuance of the order, and any other documents supporting a party's position.<sup>24</sup>

Moreover, like a contested subpoena request, a party would be permitted to request the issuance of one or more orders in one motion,<sup>25</sup> and if one or all of the arbitrator orders become

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<sup>22</sup> See id. As is current practice, arbitrators would not receive an honorarium for an unopposed subpoena request. See Notice at 36649, note 29.

<sup>23</sup> See Notice at 36649.

<sup>24</sup> Id.

<sup>25</sup> The proposed rule change would also permit parties to request the issuance of one or more subpoenas in the same motion or a combination of subpoena and order requests. See Notice at 36649, note 30.

contested, each arbitrator who decides the motion would receive one honorarium payment of \$200.<sup>26</sup>

### **Additional Proposed Changes**

The proposed rule change would also amend Rules 12214(a) and 13214(a) to make a few non-substantive changes.<sup>27</sup>

### III. Comment Summary

#### **Supportive Comments**

As noted above, the Commission received four comment letters on the proposed rule change, supporting the proposal.<sup>28</sup> All four commenters support the proposal and believe that it represents a fair and reasonable approach to helping ensure that arbitrators are compensated according to the time and effort they devote to deciding a motion.<sup>29</sup> Specifically, one commenter states that “removing the per-case cap on [honorarium for contested subpoena requests] would provide consistency and fairness to the arbitrator payment rules by ensuring that the payment arbitrators receive for deciding these requests is commensurate with the time and effort spent on each motion.”<sup>30</sup> Two other commenters believe that the proposal would help FINRA retain and recruit qualified arbitrators to its arbitration forum.<sup>31</sup> In particular, one commenter states that

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<sup>26</sup> See Notice at 36649.

<sup>27</sup> See id.

<sup>28</sup> See supra note 4.

<sup>29</sup> See Caruso Letter, Bakhtiari Letter, Gitomer Letter, and PIABA Letter; see also FINRA Letter.

<sup>30</sup> Caruso Letter; see also Gitomer Letter (stating that the proposal would provide “reasonable compensation for the time and effort spent in deciding these important requests.”).

<sup>31</sup> See Bakhtiari Letter and PIABA Letter.

“paying arbitrators fair honoraria commensurate with the time and effort required for deciding motions tends to encourage qualified arbitrators to serve on cases and as Chair.”<sup>32</sup>

### **Additional Guidance**

One commenter also suggests that FINRA take additional action regarding the assessment of fees related to discovery-related motions for subpoenas and orders. Specifically, the commenter suggests that FINRA should “informally advise arbitrators to consider assessing all fees to the non-prevailing party on contested discovery motions, where in the arbitrators’ view the non-prevailing party’s position lacked merit.”<sup>33</sup> Otherwise, the commenter suggests arbitrators may “naturally” split fees between the parties which could encourage “spurious” motion practice.<sup>34</sup>

In response, FINRA states that its arbitration forum already provides a mechanism for parties to argue their positions regarding the assessments of fees associated with an arbitration proceeding.<sup>35</sup> Specifically, FINRA states that in the absence of an agreement between the parties governing the allocation of these fees, FINRA Rules 12902(c) and 13902(c) give arbitrators discretion to determine how these fees should be allocated in an award.<sup>36</sup> FINRA also states, however, that “[p]arties may argue their positions regarding the appropriate assessment of fees

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<sup>32</sup> PIABA Letter; see also Bakhtiari Letter (stating that “fairly compensate[ing] arbitration Chairpersons for deciding contested subpoenas and orders of production and appearance” would help FINRA recruit and retain qualified arbitrators to preside over its forum.).

<sup>33</sup> PIABA Letter.

<sup>34</sup> See id.

<sup>35</sup> See supra note 5.

<sup>36</sup> See FINRA Letter.

and expenses in their motion papers or responses thereto the panel.”<sup>37</sup> Accordingly, FINRA rejects the notion that formal guidance on a panel’s authority is necessary.<sup>38</sup>

#### IV. Discussion and Commission Findings

After careful review of the proposed rule change and the comment letters, the Commission finds that the proposal is consistent with the requirements of the Exchange Act and the rules and regulations thereunder that are applicable to a national securities association.<sup>39</sup> Specifically, the Commission finds that the proposed rule change is consistent with Section 15A(b)(6) of the Exchange Act,<sup>40</sup> which requires, among other things, that FINRA rules 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, and Exchange Act Section 15A(b)(5) of the Exchange Act,<sup>41</sup> which requires, among other things, that FINRA rules provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system that FINRA operates or controls.

The Commission agrees with FINRA and the commenters that the proposed rule change would protect investors and the public interest by improving the FINRA arbitration forum for the parties that use it and the arbitrators who preside over claims.<sup>42</sup> Currently, the FINRA rules governing fees and corresponding honoraria for the resolution of discovery-related subpoenas and orders in arbitration vary. As stated above, an arbitrator who decides one or more contested

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<sup>37</sup> FINRA Letter.

<sup>38</sup> See FINRA Letter.

<sup>39</sup> In approving this rule change, the Commission has considered the rule’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>40</sup> 15 U.S.C. 78o-3(b)(6).

<sup>41</sup> 15 U.S.C. 78o-3(b)(5).

<sup>42</sup> See supra note 28; see also FINRA Letter.



subpoenas without a hearing receives \$250. An arbitrator receives no honorarium, however, for: (i) deciding an unopposed request to issue a subpoena; or (ii) deciding requests for orders for appearance without a hearing. Furthermore, FINRA states that arbitrators only receive honorarium for deciding requests for orders for production without a hearing (for which an arbitrator would receive no honorarium) because FINRA typically characterizes them as discovery-related motions without a hearing so that it can pay \$200 honorarium to each arbitrator for deciding the motion.<sup>43</sup>

The proposal would make the rules more transparent and consistent for both parties and arbitrators by providing for payments to each arbitrator of an honorarium of \$200 to decide, without a hearing session: (i) a discovery-related motion; (ii) a motion that contains one or more contested subpoena requests or contested orders for production or appearance; or (iii) a motion that contains one or more contested subpoena requests and contested orders for production or appearance.<sup>44</sup> According to FINRA, the existing structure for payments to arbitrators for deciding requests to issue subpoenas or orders without a hearing session has been difficult for parties and arbitrators to understand due to the differences between when, and under what circumstances, arbitrators will receive payments.<sup>45</sup> For example, parties can incur different fees, and arbitrators can receive different honoraria, for contested and unopposed requests to issue subpoenas and orders.<sup>46</sup>

The Commission believes the proposal would also help FINRA retain and recruit qualified arbitrators to its forum by helping ensure arbitrators are paid honoraria commensurate

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<sup>43</sup> See supra notes 17 and 18.

<sup>44</sup> See Notice at 36649.

<sup>45</sup> See Notice at 36650; see also Notice at 36650, note 34.

<sup>46</sup> See Notice at 36650.

with the time and effort they devote to deciding each request. As stated in the Notice, arbitrators must review several documents related to contested discovery-related requests: the motions requesting the issuance of the order or subpoena; the draft order or subpoena; and, any written objections to the motion. Arbitrators must then consider the arguments before making decisions on the merits of the request.<sup>47</sup> Despite the similar type and amount of work necessary to decide certain discovery-related requests for orders and subpoenas without a hearing, the rules expressly provide honoraria to arbitrators for deciding a contested subpoena but not for deciding a contested order.

The Commission believes that by structuring the arbitrator honorarium rules so that arbitrators receive the same amount of honorarium for each contested subpoena request or contested request for an order for production or appearance they decide without a hearing, the proposed rules would align the payment of honoraria to arbitrators based on the amount of time and effort required to resolve certain discovery-related motions rather than based on the characterization of those requests.<sup>48</sup> The Commission also believes that simplifying the rules governing the payment of honorarium would help improve arbitrators' understanding of the honorarium structure.

The Commission acknowledges that the proposed rule change could increase fees for certain parties. For example, under the proposed rule change parties would be subject to fees for contested requests to issue orders of appearance without a hearing session; and, the proposal would remove the per-case cap on fees for contested subpoena requests so that parties would be assessed additional fees if they submit multiple contested requests for subpoenas.

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<sup>47</sup> See Notice at 36648.

<sup>48</sup> See Notice at 36649.

The Commission also acknowledges that the proposed rule change could lower fees for certain parties. For example, the proposal would: (i) eliminate payment of honoraria to arbitrators deciding an unopposed order for production; and (ii) lower the amount of honoraria paid to arbitrators for deciding a contested subpoena request from \$250 to \$200. In addition, the proposal would permit a party or parties to use one motion to request the issuance of one or more contested subpoenas or orders so that parties could mitigate their fees.<sup>49</sup> The Commission also acknowledges, however, that the proposal would eliminate the per-case cap honoraria so arbitrators could receive additional payments for multiple contested requests for subpoenas.<sup>50</sup>

On balance, the Commission believes that the proposed rule change is designed to protect investors and the public interest. Notwithstanding the potential increase in fees to some parties in arbitration, the Commission believes that the proposal would improve the FINRA arbitration forum for its users.<sup>51</sup>

In addition, notwithstanding the potential decrease in honoraria in some cases, the Commission believes that the proposal would help FINRA retain and recruit qualified arbitrators to its forum.<sup>52</sup> In particular the Commission believes that reducing the honoraria for contested subpoena requests while removing the per-case cap on these payments would help ensure that the honoraria arbitrators receive for deciding contested requests for orders and subpoenas without a hearing would be more commensurate with their time and effort to consider the requests.<sup>53</sup>

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<sup>49</sup> See Notice at 36649 and 36651.

<sup>50</sup> See id.

<sup>51</sup> The Commission also notes that the proposal would help parties mitigate any potential fee increase by allowing parties to request one or more contested subpoenas or orders in one motion.

<sup>52</sup> The Commission also notes that the proposal would mitigate these decreases by removing the per-case cap on these honorarium payments.

<sup>53</sup> See supra note 29.

Furthermore, the Commission believes that retaining and recruiting qualified arbitrators is an essential element to operating an effective arbitration forum.<sup>54</sup>

The Commission acknowledges one commenter's request that FINRA provide additional guidance to arbitrators regarding their authority to assess all fees to the non-prevailing party on contested discovery motions, where in the arbitrators' view the non-prevailing party's position lacked merit.<sup>55</sup> However, the Commission notes FINRA's statement that a mechanism for checking arbitrators' assessments of fees associated with an arbitration proceeding already exists.<sup>56</sup> Accordingly, the Commission acknowledges FINRA's decisions not to provide additional formal guidance to its arbitrators.<sup>57</sup>

V. Conclusion

IT IS THEREFORE ORDERED pursuant to Section 19(b)(2) of the Exchange Act<sup>58</sup> that the proposal (SR-FINRA-2018-026), be and hereby is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>59</sup>

Eduardo A. Aleman  
Assistant Secretary

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<sup>54</sup> See Notice at 36650; see also supra note 32.

<sup>55</sup> See supra notes 33 and 34.

<sup>56</sup> See supra note 37.

<sup>57</sup> See supra note 38.

<sup>58</sup> 15 U.S.C. 78s(b)(2).

<sup>59</sup> 17 CFR 200.30-3(a)(12).