Public Investors Arbitration Bar Association

June 18, 2012

Via Email Only
chairmanoffice@sec.gov

Mary L. Schapiro, Chairman
Securities Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: Amendments to Form ADV

Dear Chairman Schapiro:

I am writing in my capacity as President of the Public Investors Arbitration Bar Association ("PIABA"). PIABA is national bar association comprised of attorneys, including law school professors and regulators, both former and current, who devote a significant portion of their practice to the representation of public investors in securities arbitrations. On April 1, 2011 our colleague Bob Banks wrote to you with concerns about amendments to Form ADV and the disclosure of arbitration awards. In your response dated April 20, 2011 you stated that you believed the issue warranted further evaluation. Copies of the correspondence are attached for your convenience.

On October 12, 2010, the amendments to Form ADV became effective. At the time, the Commission considered whether it should require disclosure of arbitration awards and claims. In the federal release, No. IA–3060, File No. S7–10–00, the Commission noted that some commenters objected, "with some reasoning that arbitration claims are easy to make and that arbitration settlements and awards may not necessarily include findings of wrongdoing (*i.e.*, parties may settle arbitration proceedings and/or arbitration awards may be granted even in the absence of legal violations)." The Commission decided that it would not require disclosure of arbitration awards in the client brochure. The Commission cautioned that investment advisers should consider whether particular arbitration awards or settlements do, in fact, involve or implicate wrongdoing or reflect on the integrity of the adviser, and should be disclosed to clients in the brochure or through other means.

The rationale offered by the Commission for not requiring disclosure is troubling. First, arbitration claims are not easy to make. The costs associated with filing arbitration claims are not insignificant, and in fact, are often substantially higher than filing a claim in court. In addition, attorneys are subject to the same ethical rules whether they file an arbitration claim or a court

proceeding. Second, arbitration awards typically do not contain explicit findings of wrongdoing because FINRA's Code of Arbitration Procedure (CAP) does not require an explained decision. FINRA's CAP contemplates an explained decision only if all parties jointly request one. This rarely happens.

If the Commission has concerns about the legitimacy of the arbitration process, those concerns should be addressed to FINRA, and the process should be fixed or eliminated. The Commission has approved all of FINRA's rules, including those related to the arbitration process. In addition, virtually every brokerage firm customer is subject to mandatory arbitration at FINRA. It is troubling that the Commission is expressing concerns about the legitimacy of the process, but has done nothing to change it. Pursuant to section 921 of Dodd-Frank, the Commission is to issue rules, as it deems appropriate, addressing agreements that require customers or clients of any broker, dealer or investment adviser to arbitrate disputes. However, to date, the Commission has not enacted any rules. The Commission continues to list this issue under "dates still to be determined" on its Dodd-Frank agenda. As long as arbitration is the only way to resolve customer disputes, the Commission should not undermine the legitimacy of arbitration awards to customers.

Moreover, arbitration claims and awards are disclosable on an associated person's CRD. If the rationale offered by the Commission was valid, it would not have permitted FINRA to adopt rules requiring that this information be disclosed when it pertains to an associated person. The Commission may permit the investment adviser to provide an explanation of an arbitration claim or award as it does for associated persons. However, failing to mandate disclosure is another example of inconsistent standards for investment advisers and broker-dealers, when it is clear that investors do not understand the difference between the two. Investment advisors should be subject to the same disclosure obligations as brokers.

Further, according to its website, the Commission is the "Investor's Advocate". It provides information on its website educating investors about how they may protect themselves. It instructs investors as follows:[1]

> Before you invest or pay for any investment advice, make sure your brokers, investment advisers, and investment adviser representatives have not had disciplinary problems or been in trouble with regulators or other investors.
> ...
> To find out about an investment adviser and whether it is properly registered, read its registration form, called "Form ADV." Form ADV has two parts. Part 1 contains information about the adviser's business and whether the adviser has had problems with regulators or clients. Part 2 sets out the minimum requirements for a written disclosure statement, commonly referred to as the "brochure," which advisers must provide to prospective clients initially and to existing clients annually. The brochure describes, in a narrative format, the adviser's business practices, fees, conflicts of interest,

[1] http://sec.gov/investor/brokers.htm

and disciplinary information. Before you hire an investment adviser, always ask for and carefully read both parts of the Form ADV.

These instructions imply that an investor will receive complete information if he or she follows the steps outlined. However, that may not be the case. By failing to require disclosure of arbitration claims and awards, investors have no way of ensuring that they have complete information about whether the investment advisor has "been in trouble with other investors."

Cautioning investment advisers that they may be required to disclose information about particular arbitration awards or settlements that involve or implicate wrongdoing and/or reflect on the integrity of the adviser is not sufficient protection to ensure that an investor is receiving full and fair disclosure. On the one hand, the Commission's position is that arbitration claims are easy to make and that arbitration awards may be granted even in the absence of legal violations. On the other, the Commission is of the view that an award or settlement may implicate wrongdoing. It is difficult to imagine the situation in which an arbitration award is granted against an investment advisor that does not implicate some wrongdoing. Based on the Commission's own rationale, it seems an investment advisor would have a valid ground to argue that, notwithstanding an adverse award, the advisor did nothing wrong. The presumption should always favor disclosure.

Accordingly, we request that the Commission reconsider its position, and harmonize the Form ADV with the Forms U4 and U5 to require disclosure of both arbitration claims and awards. To require anything less would not be in the best interest of investor protection.

Very truly yours,

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April 1, 2011

Via Email chairmanoffice@sec.gov

The Honorable Mary Schapiro
Chairperson
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

RE: New Reporting Requirements Permitting Omission of Arbitration Awards on Form ADV

Dear Mary:

I received a call from a reporter from *The Oregonian* newspaper today asking for a comment on the SEC's decision not to require investment advisors to disclose arbitration awards issued against them on Form ADV. I originally said that he was mistaken, until he showed me the Federal Register at http://www.sec.gov/rules/final/2010/ia-3060fr.pdf and directed me to the SEC comments on page 49234. I learned that the SEC has indeed decided that financial advisors may conceal FINRA arbitration awards actually entered against them on their Form ADV Disclosure Reporting Page.

One rationale the SEC used for non-disclosure is that "arbitration claims are easy to make." Arbitration awards in favor of investors, when they occur, are hardly rubber stamped. Those claims are decided by a panel of three arbitrators, all of whom have successfully completed a lengthy application process, rigorous training, an examination, and background screening by FINRA. They study the pleadings, attend pre-hearing conferences, and sit through hearings that typically last 3-5 days, considering all of the evidence from both sides. If they issue an award in favor of the investor, it is because the arbitrators have found wrongdoing. Claims are not "easy to make" and they are harder to win. If experienced arbitrators issue an award against an advisor, that is a material event that any reasonable investor inquiring into an advisor's background would want to know.

Another basis for the SEC's decision to allow concealment of adverse arbitration awards is that the awards "may not include findings of wrongdoing." That reasoning is equally flawed.

As you may remember, under FINRA rules, arbitrators do not give the reason for their decisions in the award unless all parties agree to it. As an investor attorney, I am always in favor of a reasoned award, but I have never had a case in which the industry has agreed to one. They don't want any record of findings made against them. When the advisor does not consent to an explained decision, he or she should not be able to avoid disclosure because the award lacks explanation!

To me, it is ironic that the very agency that is responsible for the integrity of the FINRA arbitration process would decide that arbitration awards issued by FINRA are not sufficiently reliable to require disclosure. Given your previous role at FINRA, I hope that you would agree. I know that you are a fair person, and I respectfully request that you personally review and reopen the issue for further comment. I don't believe that PIABA or many other investor advocates were aware of this issue, or they would have commented on it.

Thank you for your consideration.

Very truly yours,

Bob Banks

Robert S. Banks, Jr.

RSB:ms

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

THE CHAIRMAN

April 20, 2011

Mr. Robert S. Banks, Jr.
Investment Litigation
1300 SW Fifth Avenue
Suite 2135
Portland, OR 97201

Dear Mr. Banks:

Thank you for your letter of April 1, 2011, relating to the disclosure of arbitration awards in Form ADV, Part 2 disclosures ("brochures") provided to clients and prospective clients of advisers registered under the Investment Advisers Act of 1940. I understand that your inquiry was referred to the Division of Investment Management, which in turn provided a response describing certain staff views on this issue.

In light of the critical disclosure purposes that our brochure rule seeks to fulfill and the fact that arbitration proceedings represent a vigorous process by which investors can seek redress for harm they experience, I believe that the issues you raise warrant further evaluation. Consequently, I am writing to let you know that I have asked the staff to more closely focus on this issue and to consider the circumstances under which disclosure of an arbitration award should be made in an adviser's brochure.

Thank you again for your letter. Please contact me or Jennifer McHugh at (202) 551-2100 or mchughj@sec.gov, if we can be of further assistance.

Sincerely,

Mary L. Schapiro

cc: Robert Plaze