

Time to Revamp FINRA

By Richard Roth

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News that Susan Merrill, the Financial Industry Regulatory Authority (FINRA) Enforcement Chief, was stepping down from her position, has led to immediate thoughts on who will be her successor. While the enforcement chief is a key job for FINRA, now is the time for a much broader discussion than a simple leadership change. FINRA should be looking to make wholesale changes in how it operates. What it needs is to revamp its entire system.

In recent years, FINRA has focused on the 'slap on the wrist' violations, and has been afraid of challenging the large scale perpetual violators. FINRA should have as much, if not more, egg on its face from the Madoff scandal than the SEC. Yet somehow it has escaped the criticism that it rightly deserved.

One recent case that I worked on highlights the deficiency of FINRA's current approach to enforcement actions. In an almost unprecedented appellate reversal this past August, the National Adjudicatory Counsel overturned a FINRA enforcement panel's decision which provided for a lifetime bar of two stockbrokers from the industry. One of the brokers was charged with fraud and violating section 10b-5 of the Securities and Exchange Act and both were accused of

violating FINRA's "recommendation rule" which provides that FINRA member-firms must conduct a review of certain financial information prior to recommending over-the-counter securities to customers. In the matter, no customers ever complained in writing or orally about conduct of the brokers and, by the time of the hearing, each and every customer submitted an affidavit which was submitted to FINRA detailing that the brokers did nothing wrong and that the customers continued to use the brokers.

After a lengthy hearing before a FINRA enforcement panel, the brokers were barred for life from the securities industry. That is, they were literally thrown out of the business *even though there was no customer complaint*. The brokers appealed the entire decision to the NAC, the National Adjudicatory Counsel, that hears appeals of NASD/FINRA decision. The appeal was of including all findings of fact and sanctions imposed. And the NAC, on appeal, threw out each and every claim against both brokers.

In its twenty-six page appellate decision, the NAC blasted the FINRA enforcement panel -- reversing findings of fact and, most importantly, the draconian sanctions imposed. Overnight, the brokers went from

barred for life from their chosen profession to having nothing on their record regarding this matter.

Unfortunately, these run-away train cases against the smaller players in the industry, the ones who don't have the deep pockets to mount a costly defense of themselves, are not so unusual. Now is the time for reform. FINRA's leadership should use the opportunity of appointing a new enforcement chief to take a hard look at the entire spectrum of FINRA enforcement. This is a good time to right a sinking ship.

*Civil litigation and enforcement-defense attorney **Richard Roth** from the **Roth Law Firm**, has litigated hundreds of commercial and securities disputes in his career, with clients including large broker-dealers, clearing firms, and investment and financial institutions. **Mr. Roth** hosts *The Roth Roundtable* – an annual forum attended by securities experts and professionals which is supported and accredited by the New York State CLE Board. **Mr. Roth** can be reached at rich@rrothlaw.com*

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The Roth Law Firm, PLLC
295 Madison Avenue, Floor 22
New York, NY (212) 542-8882
www.rrothlaw.com