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BACKGROUNDER

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Reforming FINRA

David R. Burton

Abstract
FINRA is a regulator of central importance to the functioning of U.S. capital markets. It is neither a true self-regulatory organization nor a government agency. It is largely unaccountable to the industry or to the public. Due process, transparency, and regulatory-review protections normally associated with regulators are not present, and its arbitration process is flawed. Reforms are necessary. FINRA itself, the SEC, and Congress should reform FINRA to improve its rule-making and arbitration process. This Heritage Foundation Backgrounder *outlines alternative approaches that Congress and the regulators can take to improve FINRA, and provides specific recommended reforms.*

Key Points

- FINRA is a regulator of central importance to the functioning of U.S. capital markets. It is neither a true self-regulatory organization nor a government agency.
- FINRA does not provide the due process, transparency, and regulatory-review protections normally associated with regulators, and its arbitration process is flawed. Reforms are necessary.
- FINRA arbitrators should be required to make findings of fact based on the evidentiary record, and to demonstrate how those facts led to the award given. These written FINRA arbitration decisions should be subject to SEC review and limited judicial review.
- FINRA rules have played a key role in the decline in the number of small broker-dealers. This has an adverse impact on entrepreneurial capital formation.
- Congress and the SEC need to provide greater oversight of FINRA.

An Introduction to FINRA

The Financial Industry Regulatory Authority (FINRA) is the primary regulator of broker-dealers.[1] It regulates 3,895 broker-dealers and 641,761 registered representatives.[2] The Securities Exchange Act requires that a broker-dealer be a member of a registered "national securities organization,"[3] and FINRA is the only extant registered "national securities association."[4] Thus, broker-dealers must be members of FINRA in order to do business, and if FINRA revokes their membership, they may not do business.

In 2015, FINRA levied $94 million in fines against broker-dealers, took 1,512 disciplinary actions against broker-dealers, and ordered $97 million in restitution to harmed investors.[5] FINRA conducts the arbitration of almost all disputes between a customer and a broker-dealer as well as the arbitration of intra-industry disputes.[6] Investors are generally barred from pursuing relief in state

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or federal courts.[7] As discussed below, if conducted fairly, arbitration can be a cost-effective means of resolving disputes.

FINRA maintains an Office of the Ombudsman to resolve investor, broker-dealer and other complaints about FINRA operations.[8] This office handles more than 500 inquiries annually.[9]

FINRA is a Delaware not-for-profit corporation that is tax exempt under section 501(c)(6) of the Internal Revenue Code.[10] The Securities and Exchange Commission (SEC) is responsible for the oversight of FINRA.[11] In 2015, FINRA had 3,500 employees.[12] In fiscal year (FY) 2015, the SEC had 4,300 employees.[13] FINRA has an annual budget of $1 billion,[14] and has $2 billion in cash and investments on hand.[15] The SEC has an annual budget of $1.6 billion.[16] FINRA contracts to perform regulatory functions for a wide variety of exchanges. The fees it receives from these contracts account for $126 million of its annual revenues.[17]

FINRA was formed when the regulatory functions of the New York Stock Exchange (NYSE) and the National Association of Securities Dealers (NASD) were merged and given to FINRA[18] as part of a series of transactions in which both the NYSE and NASDAQ[19] became public, investor-owned enterprises.[20] These changes were approved by the SEC on July 26, 2007.[21]

FINRA is commonly called a self-regulatory organization (SRO) by both commentators and the SEC.[22] By "SRO," commentators typically mean an organization whereby the industry regulates itself. Although FINRA's predecessor organizations (the NASD and the NYSE's regulatory arm) were once true SROs,[23] FINRA is not.[24] FINRA is governed by a 23-member board.[25] Under the eighth article of its articles of incorporation, the number of its "public governors" (those not chosen by industry) "shall exceed the number of Industry Governors."[26] Industry governors are those elected by the industry. Currently, there are 10 board members who are industry governors. There are 12 public governors. In addition, FINRA's CEO, Robert Cook, also serves on its board. Thus, the industry controls only 10 of 23 governors, 43 percent of the board.[27] Because the industry does not control FINRA, it is inappropriate to regard FINRA as an SRO.

The Potential Virtues of Self-Regulation. Private individuals have the right to conduct their business, within the law, as they see fit. Firms should be free to hold themselves to higher standards than the law requires, or to establish standards, procedures, and practices by mutual agreement that improve the functioning of a market. True self-regulation by industry is one way to do that, and has potential merit.[28] Self-regulation may be thought of as spontaneous private legal ordering.[29]

Law professors William Birdthistle and Todd Henderson argue that "[i]ndustry professionals have strong incentives to police their own, since many of the costs of misbehavior are born by all members of the profession, while the benefits inure only to the misbehaving few. So long as the few do not control the regulatory process, self-regulation could in theory work as well or better than external regulation."[30] Industry representatives often have greater expertise than government regulators and are closer to the market. They may be able to more rapidly respond to changing circumstances and their regulatory response may be more proportional or scaled.[31] When the "self-regulator" becomes intertwined with government, however, self-regulation presents potential conflicts of interest and is often a guise for erecting barriers to entry in a market to protect incumbent firms and to extract economic rents at the expense of customers or clients.[32]

Why Reform Is Necessary

FINRA is an unusual entity. FINRA is a key regulator with a budget nearly two-thirds the size of the SEC's budget and a staff numbering more than 80 percent that of the SEC, but it is not a government agency. While critical to the functioning of the finance industry, and having industry representation on its board, it is not controlled by the industry. While it serves a governmental function and has coercive power, including the ability to completely bar firms and individuals from the marketplace,[33] it is not subject to any of the normal transparency, regulatory review, or due-process protections normally associated with government. It is not, for example, subject to the notice-and-comment provisions of the Administrative Procedure Act,[34] the Freedom of Information Act,[35] the Regulatory Flexibility Act,[36] the Sunshine Act,[37] the Paperwork Reduction Act,[38] or cost-benefit-analysis requirements.[39] In contrast to a court, FINRA's arbitration and disciplinary hearings are not generally open to the public.[40] Its arbitrators are not usually required to provide reasons for their decisions.[41] Its rule-making is generally done in private,[42] and its Board of Governors meetings are closed.

Unless FINRA is ultimately held to be a state actor, constitutional due-process protections, either for broker-dealers or for investors, do not apply.[43] In *Jackson v. Metropolitan Edison Co.*, the Supreme Court held that in determining whether the actions of a private party constitute state action, "the inquiry must be whether there is a sufficiently close nexus between the State and the challenged action of the regulated entity so that the action of the latter may be fairly treated as that of the State itself."[44] In *Blum v. Yaretsky*, the Supreme Court held that "a State normally can be held responsible for a private decision only when it has exercised coercive power or has provided such significant encouragement, either overt or covert, that the choice must in law be deemed to be that of the State. [T]he required nexus may be present if the private entity has exercised powers that are 'traditionally the exclusive prerogative of the State.'"[45]

In an unpublished[46] 2015 opinion, the Second Circuit held that FINRA is not a state actor.[47] In a similarly unpublished 2011 opinion, the Eleventh Circuit raised, and then side-stepped, the issue by finding that even if FINRA were a state actor, FINRA had provided due process in the case being considered.[48] Courts determining whether FINRA's predecessor organizations, the NASD and the NYSE, were a state actor were divided (although a majority found in most contexts relating to due process that they were not).[49] These cases, however, are of uncertain relevance given the differences between FINRA and NASD or NYSE governance structures, the monopoly status that FINRA enjoys, changes in the statutory and regulatory structure over time, and evolution in the judicial state action doctrine and the Supreme Court's separation of powers jurisprudence.

The IRS, however, has found that "FINRA is a corporation serving as an agency or instrumentality of the government of the United States" for purposes of determining whether FINRA fines are deductible as a business expense.[50] A "penalty paid to a government for the violation of any law" is not deductible under Internal Revenue Code section 162(f).

Furthermore, courts have routinely held that FINRA and its predecessor organizations *are* government actors for purposes of immunity from private lawsuits against them.[51] For example, in *Standard Investment Chartered Inc. v. National Association of Securities Dealers*,[52] the Second Circuit held that:

> There is no question that an SRO and its officers are entitled to absolute immunity from private damages suits in connection with the discharge of their regulatory responsibilities. This immunity extends both to affirmative acts as well as to an SRO's omissions or failure to act.... It is patent that the consolidation that transferred NASD's and NYSE's regulatory powers to the resulting FINRA is, on its face, an exercise of the SRO's delegated regulatory functions and thus entitled to absolute immunity.... The statutory and regulatory framework highlights to us the extent to which an SRO's bylaws are *intimately intertwined with the regulatory powers delegated to SROs by the SEC* and underscore our conviction that immunity attaches to the proxy solicitation here.[53] (Emphasis added.)

Thus, when dealing with FINRA, the many protections afforded to the public when dealing with government are unavailable, and the recourse that one would normally have when dealing with a private party—both access to the courts and the ability to decline to do business—is also unavailable. Like Schrödinger's cat, simultaneously dead and alive, FINRA is, under current rulings, both a state actor (for purposes of barring liability and for tax purposes) and, generally, not a state actor (for purposes of absolving it of due process and other requirements and for liability purposes).

Professors Birdthistle and Henderson have written that:

> SROs have been losing their independence, growing distant from their industry members, and accruing rulemaking, enforcement, and adjudicative powers that more closely resemble governmental agencies such as the Securities and Exchange Commission and the Commodity Futures Trading Commission.... This process by which these self-regulatory organizations shed their independence for an increasingly governmental role is highly undesirable from an array of normative viewpoints. For those who are skeptical of governmental regulation, deputizing private bodies to increase governmental involvement is clearly problematic.[54]

Former SEC Commissioner Daniel M. Gallagher has raised similar concerns:

> This decrease in the "self" aspect of FINRA's self-regulatory function has been accompanied by an exponential increase in its regulatory output. As FINRA acts more and more like a "deputy" SEC, concerns about its accountability grow more pronounced.[55]

Law professor Emily Hammond refers to FINRA's current status as "double deference" and argues that "the combination of oversight agencies' deference to SROs and judicial deference to oversight agencies undermines both the constitutional and regulatory legitimacy of SROs" and that reforms would "better promote accountability and guard against arbitrariness not only for SROs but also for the modern regulatory state."[56]

The U.S. Chamber of Commerce, referring to FINRA and the proxy adviser firm Institutional Shareholder Services, wrote:

> Despite their tremendous influence over the workings of the capital markets, these organizations are generally subject to few or none of the traditional checks and balances that constrain government agencies. This means they are devoid of or substantially lack critical elements of governance and operational transparency, substantive and procedural standards for decision making, and meaningful due process mechanisms that allow market participants to object to their determinations.[57]

It is also unclear how well FINRA is discharging its core mission of preventing fraud, misappropriation of funds, and other misconduct by those it regulates.[58] A recent empirical analysis found:

> Roughly 7% of advisers have misconduct records. At some of the largest financial advisory firms in the United States, more than 15% of advisers have misconduct records. Prior offenders are five times as likely to engage in new misconduct as the average financial adviser. Firms discipline misconduct: approximately half of financial advisers lose their job after misconduct.... [O]f these advisers, 44% are reemployed in the financial services industry within a year.[59]

Some of the largest firms have committed multibillion dollar frauds with few consequences for the individuals who committed this fraud.[60] There is bipartisan, bi-ideological concern about FINRA enforcement.[61] It is, of course, possible that the high level of advisers with misconduct records is due to aggressive FINRA enforcement, and that the high level (44 percent) of re-employment in the financial industry of advisers with misconduct records is because the misconduct involved was minor. Given the information currently available to the public and policymakers, it is simply impossible to know.

FINRA's Office of the Chief Economist[62] has conducted research on FINRA enforcement. In August 2015, it released a working paper that found that the "20% of brokers with the highest ex-ante predicted probability of investor harm are associated with more than 55% of investor harm events and the total dollar harm in our sample."[63] Thus, the one-fifth of brokers that FINRA's algorithm predicts have the highest likelihood of misconduct do, in fact, account for over half of the misconduct. Presumably, FINRA's Enforcement Department is taking this predictive algorithm into account when assessing its enforcement priorities. The study also found that "[w]ith respect to the impact of releasing additional non-public CRD information on BrokerCheck, we find that HAC [harm associated with co-workers] leads to an economically meaningful increase in the overall power to predict investor harm."[64] HAC is FINRA jargon that means if a firm employs or has employed brokers that engage in misconduct, other brokers at that firm are more likely to engage in misconduct, presumably because of the culture at the firm or poor internal controls. Releasing additional CRD information, then, may allow the public to better assess whether their broker, or a broker whom they are considering, is likely to harm them by engaging in misconduct. Among other things, unreleased information includes complaints, test scores, felonies, and bankruptcies, and some of the information is quite old. Release of unadjudicated complaint information where there has been no finding of fault by the broker-dealer is probably not warranted. FINRA should evaluate whether additional information should be released.

The bottom line is this. FINRA has a monopoly. It is the only SRO for broker-dealers. Broker-dealers must be a member of FINRA in order to do business. Quitting FINRA is not an option given the legal requirement to be a member of an SRO. FINRA is virtually immune to legal challenges to its regulatory decisions. Thus, the normal recourse when dealing with a private party is not available. FINRA also has a virtual monopoly on arbitration of disputes between FINRA members and between a FINRA member and investors. Both investors and broker-dealers are generally barred from accessing the courts. FINRA has coercive authority over its members and investors. The federal government has effectively delegated regulatory and dispute-resolution authority to a private organization. When they are dealing with FINRA, neither broker-dealers nor investors enjoy the many protections that the law affords in dealing with government regulators in any court[65] or in the regulation formulation process. Furthermore, it is far from clear that FINRA is doing an adequate job of policing fraud, misappropriation, and other serious misconduct. FINRA is not adequately accountable to Congress, to the public, or to those it regulates. Reforms, discussed below, are necessary.

FINRA's Constitutionality

It is an open question whether FINRA, as currently constituted, is constitutional.[66] It is arguably unconstitutional for at least two reasons: (1) the separation of powers, and (2) the Fifth Amendment due-process clause and the associated private non-delegation doctrine. No matter how the courts ultimately rule on the constitutionality of FINRA's current structure, the due-process, transparency, accountability, and governance questions raised are policy questions that Congress should address.

The Supreme Court in *Free Enterprise Fund v. Public Company Accounting Oversight Board*[67] held the dual "for cause" provisions[68] in the section of Sarbanes–Oxley creating the Public Company Accounting Oversight Board (PCAOB)[69] to be unconstitutional on separation-of-powers grounds.

In *Free Enterprise*, the Supreme Court asked: "May the President be restricted in his ability to remove a principal officer, who is in turn restricted in his ability to remove an inferior officer, even though that inferior officer determines the policy and enforces the laws of the United States?"[70]

The Supreme Court's answer:

> We hold that such multilevel protection from removal is contrary to Article II's vesting of the executive power in the President. The President cannot "take Care that the Laws be faithfully executed" if he cannot oversee the faithfulness of the officers who execute them. Here the President cannot remove an officer who enjoys more than one level of good-cause protection, even if the President determines that the officer is neglecting his duties or discharging them improperly.[71]

Because FINRA is tasked with enforcing the securities laws,[72] and its board and officers are not removable by the President, and SEC Commissioners are only removable for cause, it is quite possible that a court would conclude that FINRA, as currently structured, violates the separation-of-powers clause. The Supreme Court, however, did distinguish the PCAOB from "private self-regulatory organizations in the securities industry—such as the New York Stock Exchange."[73] So the central question becomes whether FINRA is exercising "executive power" within the meaning of the Constitution, or whether it is a truly private self-regulatory organization.[74]

Discussing the Supreme Court's private non-delegation doctrine in another context, Heritage Foundation Legal Research Fellow Paul Larkin wrote:

> The Fifth Amendment Due Process Clause ensures that the actors in each department cannot evade the Framers' carefully constructed regulatory scheme by delegating their federal lawmaking power to unaccountable private parties, individuals beyond the direct legal and political control of superior federal officials and the electorate. That is, the due process requirement that federal government officials act pursuant to "the law of the land" when the life, liberty, or property interests of the public are at stake prohibits the officeholders in any of those branches from delegating lawmaking authority to private parties who are neither legally nor politically accountable to the public or to the individuals whose conduct they may regulate.[75]

In *Todd & Co. v. SEC*[76] and *R. H. Johnson & Co. v. Securities & Exchange Commission*,[77] two circuits ruled the Maloney Act[78] delegation to the NASD (FINRA's predecessor organization) to be constitutionally compliant. The *Todd* court, however, explicitly disclaimed making a ruling on the

1975 amendments to the Securities Act,[79] let alone changes since FINRA was created.[80] As discussed above, the NASD and the NYSE were controlled by members of the organizations, while FINRA is not. Moreover, at the time of those decisions, the NYSE and NASDAQ were mutualized. Furthermore, the decisions predate the SEC's role in approving all SRO rules. Finally, the courts' state action and separation-of-powers jurisprudence has evolved considerably since the *Todd* and *R.H. Johnson* courts considered the issue.

Three Paths to Reform

There are three basic approaches to reforming FINRA. First, it could be changed back into a truly private SRO, controlled by the industry, with the SEC resuming its traditional regulatory role. This would, in effect, be a return to the regulatory environment before the NYSE and NASD handed off their regulatory function to FINRA.[81] Second, FINRA could be incorporated into the SEC. FINRA's status as a "national securities organization" would be terminated, its employees would have the option of becoming government employees,[82] and FINRA's regulatory functions would be discharged by the SEC, presumably by its Division of Trading and Markets. Those educational functions not conducted by its foundation and perhaps its market surveillance[83] and intra-industry dispute resolution functions could be retained. As discussed below, ideally, its arbitration function would be spun off. This approach would provide the transparency, due-process protections, and congressional oversight typically associated with government. Significant changes to the Securities Exchange Act provisions governing national securities organizations would be required. Third, the existing framework could be substantially reformed. This latter, incremental, approach is likely to have the best chance of success in the current policy environment.

In August 2016, Robert Cook became president and CEO of FINRA, and chairman of the FINRA Investor Education Foundation.[84] Jack Brennan was named FINRA's chairman.[85] Previously, Richard Ketchum had been both chairman and CEO. In addition, Bob Muh, the CEO of Sutter Securities, Inc., was elected in September as a small-firm governor on a platform of reducing the regulatory burden on small broker-dealers.[86] With new leadership may come a new openness to reform.

Incremental Reforms. Incremental—although major—reforms that would address the most substantial problems with FINRA's current structure are outlined below. In principle, many of these reforms could be implemented by FINRA itself, with SEC approval. Alternatively, Congress could amend § 15A and § 19 of the Securities Exchange Act, such that a national securities association (that is, an SRO) must meet the outlined requirements as a condition of registration. Current law already imposes more than 20 requirements.[87]

Transparency. Given FINRA's importance to U.S. financial markets, and the effective delegation to it of key regulatory functions by the SEC and Congress, openness and transparency in its regulatory and adjudicatory functions is entirely appropriate. FINRA should comply with a set of rules substantially similar to the requirements imposed on government agencies under the Freedom of Information Act.[88]

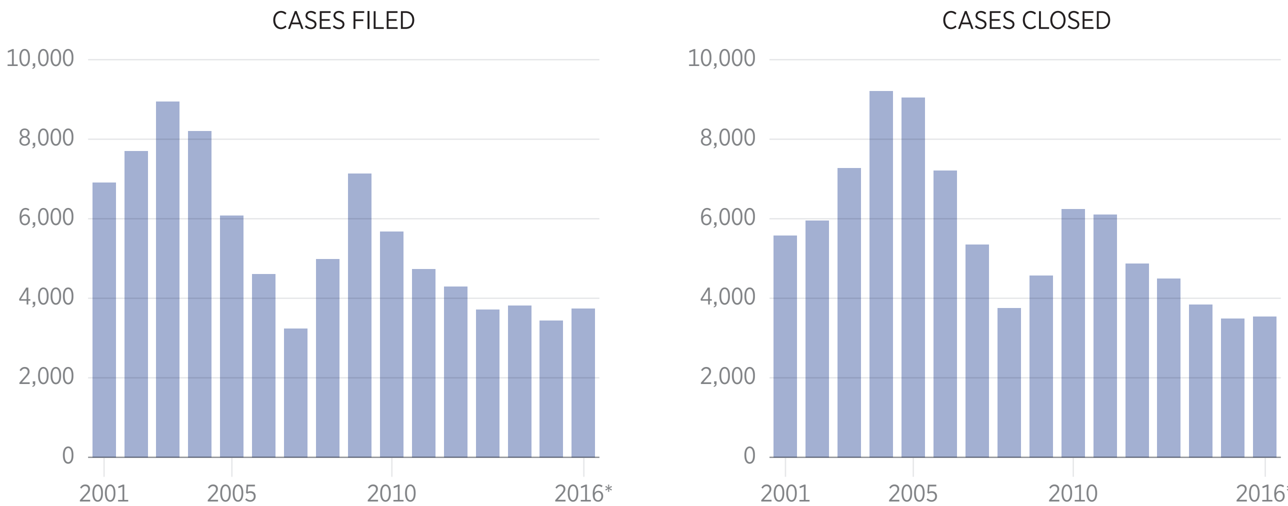
FINRA's Board of Governors meetings should be open to the public, unless the board votes to meet in executive session. The criteria for whether they can close the meeting should be established in advance and carefully circumscribed. FINRA currently does not make available in advance rule-makings that the FINRA board is expected to consider.[89] The complete board agenda should be made available to the public in advance, and board minutes describing actions taken should be published with alacrity. Such requirements are analogous to, but less stringent than, the requirements imposed on government agencies by the Sunshine Act.[90]

Given that under current law FINRA proceedings supplant a civil trial and there is no means of accessing the courts, FINRA arbitration hearings should be open to the public and reported. This is analogous to the public-trial requirement in the Sixth Amendment and the long-standing presumption that *all* court proceedings in the United States are open to the public.[91] Just as trials in criminal and civil courts and hearings in administrative courts are open to the public, so should disciplinary hearings.

In 1884, Oliver Wendell Holmes, then a justice on the Massachusetts Supreme Court, held in *Cowley v. Pulsifer*[92] that members of the public enjoy a right of access to civil trials. This right, he said, is rooted in democratic principles:

CHART 1

FINRA Arbitration Cases



* Projected.
SOURCE: Financial Industry Regulatory Authority, "Dispute Resolution Statistics," http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics (accessed December 22, 2016).

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> It is desirable that the trial of [civil] causes should take place under the public eye…not because the controversies of one citizen with another are of public concern, but because it is of the highest moment that those who administer justice should always act under the sense of public responsibility, and that every citizen should be able to satisfy himself with his own eyes as to the mode in which a public duty is performed.

Although proceedings are not public, adverse results in many disciplinary matters are made public via a database called Broker-Check.[93] Broker-Check, however, reports only some of the information available on FINRA's Central Registration Depository. FINRA's Office of the Chief Economist has found that the unreported information is relevant to predicting broker misconduct.[94] Other than unauthenticated complaint data,[95] FINRA should consider whether this information should be made public. As discussed below, FINRA's rule-making process should also be made more transparent.

Arbitration and Dispute Resolution. FINRA handles about 4,000 arbitration cases annually. About 70 percent of these involve customer complaints, and the remainder consist of intra-industry cases.[96]

Arbitration can be a lower cost, fair way of resolving disputes.[97] However, for the reasons discussed below in detail, FINRA's arbitration system is flawed and should be improved.

Alternatively, Congress should consider a different approach. It could create a specialized court, analogous to the Tax Court, to hear intra-industry and customer-securities cases. This could be a specialized Article III court with limited jurisdiction, or a non-Article III court, such as the U.S. Tax Court[98] or the U.S. Court of Federal Claims.[99] It should have a small claims division like the Tax Court and many state courts so that small claims can be handled in a less-formal and less-expensive manner. The small-claims division should be open to *pro se* litigants, and judges should take a more active role in fact finding. Such an approach would have two primary advantages. First, there would be no doubt about its impartiality as there is in the case of FINRA. These doubts arise because, although not controlled by industry, FINRA certainly has strong industry influence. Second, its judges would develop expertise in securities-law cases. Often, neither an Article III court of general jurisdiction nor current FINRA arbitrators have expertise in securities cases.

Due Process. Due process may be summarized as providing to a person who may suffer loss of life, liberty, or property "notice, an opportunity to be heard, and a determination by a neutral decision-maker"[100] in an open forum. In the words of the Supreme Court:

> Secrecy is not congenial to truthseeking.... No better instrument has been devised for arriving at truth than to give a person in jeopardy of serious loss notice of the case against him and opportunity to meet it. Nor has a better way been found for generating the feeling, so important to a popular government, that justice has been done.[101]

Due-process protections would, at a minimum, include (1) adequate notice of the charges or complaint; (2) the right to be present at a hearing or trial; (3) a public forum; (4) the right to be heard and to present evidence; (5) the right to retain counsel; (6) trial by jury or, at least, an impartial, neutral decision maker; (7) an adequate ability to compel the opposing party to disclose facts and documents that are material to the dispute (adequate discovery); (8) an adequate ability to call witnesses and to cross-examine witnesses called by the opposing party; (9) a requirement that findings of fact are made and legal reasons are given for a decision; and (10) an adequate review by an impartial party of the triers' decision to ensure that it is not arbitrary or capricious and has a rational basis in law and in fact (adequate appeal rights). Each of these is addressed in turn below.

1. Notice. FINRA appears to provide adequate notice both in disciplinary hearings and in its arbitrations.[102]

2. The Right to be Present. FINRA allows the parties to be present during proceedings.[103]

3. Public Forum. FINRA does not generally provide a public forum. Its proceedings are generally closed to the public.[104] As discussed above under "Transparency," these proceedings should generally be open to the public.[105]

4. The Right to Be Heard and Present Evidence. FINRA provides the opportunity for parties to be heard and to present evidence. As discussed below, however, parties' rights to present and obtain evidence are circumscribed, and the federal rules of evidence do not apply.[106]

5. The Right to Retain Counsel. The right to retain and be represented by counsel is preserved in FINRA proceedings.[107]

6. Impartial Decision Maker. FINRA does not provide the right to a trial by jury as is guaranteed in federal court by the Seventh Amendment[108] and in state courts by most state constitutions.[109] FINRA arbitration chairpersons are not judges. Although there are some requirements for arbitration chairpersons, there is no requirement that arbitrators have any special expertise in finance or the law. In fact, FINRA actively recruits from outside those fields.[110] FINRA arbitrators must be approved by FINRA and complete 13.5 hours of FINRA training.[111] FINRA maintains a list of 6,000 approved arbitrators[112] and generates a random list of arbitrators (typically 10 public arbitrators, 10 non-public arbitrators, and 10 chairpersons) from which the parties can choose.[113] FINRA changed its rules in 2011,[114] however, so that in arbitrations involving a dispute between customers and a firm, the customer may elect to have the arbitration panel composed of entirely public arbitrators rather than industry representatives.[115]

7. Adequate Discovery. FINRA discovery rules differ depending on the type of proceeding.[116] Discovery is more limited than it would be in a federal court.[117] In particular, the ability to depose witnesses is severely circumscribed.[118] This may make it more difficult for a party to pursue a claim. FINRA discovery is, however, more extensive than discovery made under American Arbitration Association rules.[119] Excess discovery costs are one of the primary reasons why conventional litigation is so expensive, and controlling dispute resolution costs is one of the primary advantages of arbitration.[120] Controlling costs is one of the core rationales underlying the Federal Arbitration Act,[121] which generally requires courts to enforce arbitration awards and bars access to courts when the parties have entered into a pre-dispute arbitration agreement[122] (as would be the case in virtually every customer-broker agreement). Whether FINRA discovery rules should be modified should be studied further.

8. Calling Witnesses and Witness Cross-Examination. Witnesses may generally be called, and opposing witnesses cross-examined. The limits on conducting witness deposition discussed above make it much more difficult to adequately rebut surprise testimony or to impeach a witness.

9. Findings of Fact and Law. In general, FINRA arbitrators need not explain their reasoning or make findings of fact or law. If, however, all parties agree in advance,[123] they may request and pay $400 for an "explained decision."[124] But even an explained decision need not include "legal authorities and damage calculations."[125] Thus, neither the parties nor anyone reviewing the arbitrators' decision can meaningfully assess how much, or how little, thought or analysis about the facts or the law went into deciding the case or the amount, if any, of the award. Neither the parties nor anyone else can meaningfully assess whether the arbitrators' reasoning was flawed or sound. In contrast to very high compensation for FINRA employees,[126] arbitrators are paid between $300 (for a session up to four hours) and $600 (for a session lasting up to a day).[127] This amounts to $75 per hour—and substantially less than that, once the time traveling to and from the hearing and preparation time is considered. In contrast, the reimbursement rate for attorneys under the Equal Access to Justice Act is about $190 per hour.[128] Arbitrators are not paid for time spent on preparation, analysis, or discussion outside the actual arbitration session. Thus, they have every incentive to make a quick decision rather than a well-reasoned decision.

Administrative-law courts are required to make "findings and conclusions, and the reasons or basis therefore, on all the material issues of fact, law, or discretion presented on the record."[129] FINRA arbitrators should be required to do the same for those cases where more than $100,000[130] is at stake or severe disciplinary sanctions are possible. This may be difficult for many existing FINRA arbitrators who do not have training in finance or in the law. If raising FINRA arbitrator honoraria is necessary in order to attract those with the requisite skills, FINRA should do so.

10. Adequate Review of Arbitration Decisions. Either party can appeal the result of a disciplinary hearing to the National Adjudicatory Council (NAC).[131] The NAC is a FINRA committee[132] with 14 members.[133] Any governor may request that FINRA's Board of Governors review the decision of the NAC.[134] A respondent may ask the SEC to review a final FINRA decision.[135] The SEC's decision, in turn, is subject to limited judicial review.[136]

There is no comparable review in customer or intra-industry arbitrations. The arbitrators' decisions are final.[137] The combination of arbitrators not needing to provide reasons for their decision and the near-total lack of review for customer or intra-industry arbitrations is fundamentally unfair and affords no recourse to either customers or firms that are the victims of poorly reasoned, unjust, or arbitrary decisions. Some of these disputes, of course, involve modest amounts of money. But others involve substantial sums and can, in the case of customers, involve their life savings. Similarly, a firm that is forced to unjustly pay an award has no recourse.

FINRA arbitrators should be required to make findings of fact based on the evidentiary record and to demonstrate how those facts led to the award given. These written FINRA arbitration decisions should be subject to SEC review and limited judicial review. Policymakers should carefully evaluate whether the current practice in disciplinary proceedings is sufficient to provide adequate review. Specifically, those reviewing the outcome in a disciplinary decision should be able to assess whether the findings of fact actually have an adequate basis, and to assess a written finding of how, in light of those facts, a specific FINRA rule or provision in the securities law was violated.

Improved Oversight. The Government Accountability Office (GAO) has found the SEC's oversight of FINRA to be insufficient.[138] In response, in October 2016, the SEC started a new office called the FINRA and Securities Industry Oversight (FISIO) group, designed to enhance its oversight of FINRA.[139] The new FISIO should issue annual reports describing its oversight of FINRA and addressing the issues raised in this *Backgrounder*.

Congressional oversight of FINRA has been light. To improve oversight, Congress should:

- Require that FINRA submit an annual report to Congress with detailed, specified information about its budget and fees; its enforcement activities (including sanctions and fines imposed by type of violation and type of firm or individual); its dispute resolution activities; and its rule-making activities;
- Conduct annual oversight hearings on FINRA, its budget, its enforcement activities, its dispute resolution activities, and its rule-making activities;
- Require an annual GAO review of FINRA with respect to its budget, its enforcement activities, its dispute resolution activities, and its rule-making activities and a separate review of the SEC's oversight of FINRA; and

CHART 2

FINRA Regulated Firms and Registered Representatives

SOURCES: Financial Industry Regulatory Authority, "Annual Reports and Financials, 2007–2010," http://www.finra.org/about/annual-reports-financials (accessed December 22, 2016), and Financial Industry Regulatory Authority, "Statistics," http://www.finra.org/newsroom/statistics (accessed December 22, 2016). Note: FINRA data for 2008–2010 are approxmiate.

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- Consider making FINRA, the Municipal Securities Rulemaking Board (MSRB),[140] and the National Futures Association (NFA)[141] each a "designated federal entity"[142] and establishing an inspector general with respect to financial SROs, including FINRA, the MSRB, and the NFA or, alternatively, placing FINRA, the MSRB, and the NFA within the ambit of an existing inspector general.[143]

Small Broker-Dealer Relief. As Chart 2 shows, the number of broker-dealers has declined by nearly 13 percent over the past five years (2011–2016), and 23 percent in the nine years since FINRA was created in 2007.[144]

Since 2009, the number of registered representatives who work for broker-dealers has remained fairly constant, but the number of firms has continued to decline. This reflects the concentration in the market and the decline in the number of small broker-dealers. The registered representatives that once worked for these smaller firms have found employment with the remaining firms.

A similar phenomenon is occurring in the banking sector.[145] The number of small banks has declined by 28 percent since 2000, and small banks' share of total domestic deposits has declined from 40 percent to less than 22 percent.[146] There are many reasons for the decline in small broker-dealers and small banks, but one obvious factor common to both banks and broker-dealers is the ever-increasing rise in the regulatory burden on small broker-dealers and small banks. FINRA rules are a major component of that regulatory burden for broker-dealers. Regulatory compliance costs do not increase linearly with size, and place a disproportionate burden on small firms, making them less competitive in the marketplace.[147] Small broker-dealers are more willing to underwrite the offerings of small and start-up businesses. The decline in the number of small broker-dealers impedes the ability of entrepreneurs to raise capital.

FINRA needs to undertake a systematic review of it rules and regulatory practices comparable to the small-entity impact review required of federal agencies under the Regulatory Flexibility Act.[148] This review should include the impact of stress tests, the nature of FINRA audits, FINRA rules relating to the interaction between research and corporate finance, FINRA rules and practices relating to sanctions for inadequate policies and procedures or failure to supervise, the operation of "remedial" sanctions imposed without a hearing,[149] and other matters. FINRA needs to be open to experimentation and financial-technological innovation that most commonly occurs in small firms.

Budget and Finance. FINRA fees are not voluntary. As a matter of economics, though not law, they are effectively a tax. And, at $789 million in 2015, they are substantial.[150] The businesses that pay these fees must recover the costs.[151] Before raising these fees, FINRA should be required to obtain an affirmative vote by Congress or, at least, by the SEC.

The fines leveled by FINRA in 2015 ($94 million) were 263 percent higher than the $25.9 million in fines levied in 2008, its first full year of operation.[152] Average fines per member were $5,286 in 2008, and $23,755 in 2015, a 349 percent increase.[153] It is difficult to judge the appropriateness of FINRA fines without additional information, but FINRA should not have a budgetary incentive to impose fines. Currently, it is FINRA policy that FINRA fines are used to fund "capital expenditures and specified regulatory projects."[154] Revenues from fines imposed ($97 million in FY 2015)[155] should go to either a newly established investor reimbursement fund[156] or to the Treasury, not to FINRA's budget.

Congress should consider making FINRA "on budget" for purposes of the federal budget, along with various other government-sponsored enterprises, quasi-governmental entities, agency-related nonprofit organizations, and the like that currently escape congressional oversight during the budget process.[157] The Securities Protection Investors Corporation and the PCAOB are District of Columbia not-for-profit organizations but are on budget.[158] The MSRB and NFA are not.[159]

Regulatory Process. FINRA's rule-making process should also be made more transparent. Currently, it solicits comments from the public for many of its rules.[160] But this solicitation is not required. Its committee process is opaque and its Board of Governors' meetings, where final rules decisions are made, are closed. The proposed rules are subject to public scrutiny once they are submitted to the SEC for approval.[161] But, by this juncture, it is unusual for changes to be made, and the SEC rarely disapproves a rule proposed by FINRA.[162] In its rule-making process, FINRA should comply with a set of rules substantially similar to the requirements imposed on government agencies relating to the notice-and-comment provisions of the Administrative Procedure Act.[163]

Although FINRA made improvements in the economic analysis of its rules by creating its Office of the Chief Economist in 2013, its efforts are still relatively rudimentary compared to those of the SEC and most other government agencies.[164] FINRA should also examine whether its rules have a disproportionate impact on small, more entrepreneurial broker-dealers.[165]

Conclusion

FINRA is a key regulator of central importance to the functioning of U.S. capital markets. It is neither a true self-regulatory organization nor a government agency. It is largely unaccountable to the industry or to the public. Due process, transparency, and regulatory-review protections normally associated with regulators are not present, and its arbitration process is flawed. Reforms are necessary. FINRA itself, the SEC, and Congress should reform FINRA to improve it rule-making and arbitration process. Congress should amend § 15A and § 19 of the Securities Exchange Act such that a national securities association (FINRA) must meet the reforms outlined in this *Backgrounder* as a condition of registration.

*—**David R. Burton** is Senior Fellow in Economic Policy in the Thomas A. Roe Institute for Economic Policy Studies, of the Institute for Economic Freedom, at The Heritage Foundation.*

Endnotes

1. Financial Industry Regulatory Authority, "What We Do," http://www.finra.org/about/what-we-do (accessed December 9, 2016).
2. Financial Industry Regulatory Authority, "Statistics," September 2016 data, http://www.finra.org/newsroom/statistics (accessed December 9, 2016).
3. Securities Exchange Act sections 15(b)(8) ("It shall be unlawful for any registered broker or dealer to effect any transaction in, or induce or attempt to induce the purchase or sale of, any security (other than commercial paper, bankers' acceptances, or commercial bills), unless such broker or dealer is a member of a securities association registered pursuant to section 78o–3 of this title or effects transactions in securities solely on a national securities exchange of which it is a member.") and 15(b)(11(A)(i). ("A broker or dealer may not register under this paragraph unless that broker or dealer is a member of a national securities association registered under section 15A(k).")
4. FINRA is registered pursuant to Securities Exchange Act section 15A [15 U.S. Code § 78o–3].
5. Financial Industry Regulatory Authority, *FINRA 2015 Year in Review and Annual Financial Report*, p. 3, http://www.finra.org/sites/default/files/2015_YIR_AFR.pdf (accessed December 9, 2016).
6. Financial Industry Regulatory Authority, "Arbitration and Mediation," https://www.finra.org/arbitration-and-mediation (accessed December 9, 2016), and Financial Industry Regulatory Authority, *Final Report and Recommendations of the FINRA Dispute Resolution Task Force*, December 16, 2015, http://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf (accessed December 9, 2016). For a discussion of the history of securities-dispute arbitration in the U.S., see Jill Gross, "The Historical Basis of Securities Arbitration as an Investor Protection Mechanism," *Journal of Dispute Resolution*, Vol. 171 (2016), pp. 171–186, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2728978 (accessed December 9, 2016). For statistics on FINRA arbitrations, see Financial Industry Regulatory Authority, "Dispute Resolution Statistics," http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics (accessed December 9, 2016).
7. This is because virtually all brokers require customers to sign a mandatory arbitration agreement, and FINRA's decisions are final in most cases. The Supreme Court has upheld the mandatory arbitration clauses in customer agreements. See *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987), and *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 131 S. Ct. 1740, 179 L.Ed. 2d 742 (2011). Under FINRA Rule 12904(b) (approved by the SEC), "[u]nless the applicable law directs otherwise, all awards rendered under the Code are final and are not subject to review or appeal." Code in this context means the FINRA Code of Arbitration Procedure for Customer Disputes, FINRA Rules 12000 et seq., http://finra.complinet.com/en/display/display_viewall.html?rbid=2403&element_id=4096&record_id=5174&filtered_tag (accessed December 9, 2016). See also the arbitration discussion below, in the section titled "Arbitration and Dispute Resolution."
8. FINRA, "Office of the Ombudsman," http://www.finra.org/about/office-ombudsman (accessed January 4, 2017).
9. FINRA, *Office of the Ombudsman 2014 Report*, p. 3 http://www.finra.org/sites/default/files/Office_Ombudsman_Report_072815.pdf (accessed January 4, 2017).
10. Foundation Center, IRS Form 990, http://990s.foundationcenter.org/990_pdf_archive/521/521959501/521959501_201312_990O.pdf (accessed December 9, 2016); Delaware Department of State: Division of Corporations, Entity Search, https://icis.corp.delaware.gov/Ecorp/EntitySearch/NameSearch.aspx (accessed December 9, 2016); and FINRA Articles of Incorporation, http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=4589 (accessed December 9, 2016).
11. Securities Exchange Act section 19 [15 U.S. Code § 78s]; 17 C.F.R. §§ 240.19b-4-240.19h-1; Securities and Exchange Commission, "Self-Regulatory Organization Rulemaking," https://www.sec.gov/rules/sro.shtml (accessed December 9, 2016); Government Accountability Office, "SEC Can Further Enhance Its Oversight Program of FINRA," April 2015, GAO–15–376, http://gao.gov/assets/670/669969.pdf (accessed December 9, 2016). In October 2016, the SEC started a new office called the FINRA and Securities Industry Oversight (FISIO) group designed to enhance its oversight of FINRA. The SEC will also be reducing the number of examiners dedicated to broker-dealer examinations. See Marc Wyatt, "Inside the National Exam Program in 2016," Securities and Exchange Commission, keynote address at National Society of Compliance Professionals conference, Washington, DC, October 17, 2016, https://www.sec.gov/news/speech/inside-the-national-exam-program-in-2016.html (accessed December 9, 2016); Elizabeth Dilts, "SEC Says to Monitor Partner Regulator's Brokerage Oversight," Reuters, October 17, 2016, http://www.cnbc.com/2016/10/17/reuters-america-sec-says-to-monitor-partner-regulators-brokerage-oversight.html (accessed December 9, 2016); and "SEC Launches Dedicated FINRA Oversight Unit: Watching the Detectives," *National Law Review*, October 27, 2016, http://www.natlawreview.com/article/sec-launches-dedicated-finra-oversight-unit-watching-detectives (accessed December 9, 2016).
12. Financial Industry Regulatory Authority, *2015 Year in Review and Annual Financial Report*, p. 13, http://www.finra.org/sites/default/files/2015_YIR_AFR.pdf (accessed December 9, 2016).
13. On a full-time-equivalent (FTE) basis. FY 2017 SEC Congressional Budget Justification, p. 14.
14. *FINRA 2015 Year in Review and Annual Financial Report*, p. 14.
15. Ibid., p. 15.
16. Securities and Exchange Commission, *FY 2017 Congressional Budget Justification, FY 2017 Annual Performance Plan, FY 2015 Annual Performance Report*, p. 15, https://www.sec.gov/about/reports/secfy17congbudgjust.pdf (accessed December 9, 2016).

17. FINRA performs market regulation under contract for the New York Stock Exchange LLC (NYSE); NYSE Arca, Inc. (NYSE Arca); NYSE MKT LLC (NYSE MKT); The Nasdaq Stock Market LLC (NASDAQ); Nasdaq BX, Inc. (Boston); Nasdaq PHLX LLC (Philadelphia); BATS Global Markets, Inc. (the BZX, BYZ, EDGA and EDGX exchanges, collectively referred to as BATS); the International Securities Exchange, LLC (ISE, ISE Gemini, and ISE Mercury); the Chicago Board Options Exchange and the C2 Options Exchange (CBOE and C2); and other exchanges. See *FINRA 2015 Year in Review and Annual Financial Report*, pp. 12 and 19.
18. News release, "NASD and NYSE Member Regulation Combine to Form the Financial Industry Regulatory Authority–FINRA," Financial Industry Regulatory Authority, July 30, 2007, http://www.finra.org/newsroom/2007/nasd-and-nyse-member-regulation-combine-form-financial-industry-regulatory-authority (accessed December 9, 2016); and Securities and Exchange Historical Society, "Creation of FINRA," http://www.sechistorical.org/museum/galleries/sro/sro06g.php (accessed December 9, 2016).
19. NASDAQ was originally the acronym for National Association of Securities Dealers Automated Quotations.
20. The NYSE is owned by Intercontinental Exchange Inc. traded on the NYSE under the symbol ICE. Nasdaq, Inc. is traded on NASDAQ under the symbol NDAQ. Previously, NYSE and NASDAQ had been member (broker-dealer) owned (sometimes called "mutualized" exchanges).
21. "Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Approving Proposed Rule Change To Amend the By-Laws of NASD To Implement Governance and Related Changes To Accommodate the Consolidation of the Member Firm Regulatory Functions of NASD and NYSE Regulation, Inc.," Notices, *Federal Register*, Vol. 72, No. 147 (August 1, 2007), pp. 42169–42190 and 42190-42192, https://www.gpo.gov/fdsys/pkg/FR-2007-08-01/pdf/E7-14855.pdf (accessed December 14, 2016).
22. For more on the history of securities SROs and FINRA in particular, see Roberta S. Karmel, "Should Securities Industry Self-Regulatory Organizations Be Considered Government Agencies?" *Stanford Journal of Law, Business & Finance*, Vol. 14, No. 1 (Fall 2008), pp. 163 and 164, http://brooklynworks.brooklaw.edu/cgi/viewcontent.cgi?article=1376&context=faculty (accessed December 9, 2016); Hester Peirce, "The Financial Industry Regulatory Authority: Not Self-Regulation after All," Mercatus Center *Working Paper*, January 2015, https://www.mercatus.org/system/files/Peirce-FINRA_0.pdf (accessed December 9, 2016); and Jonathan Macey and Caroline Novogrod, "Enforcing Self-Regulatory Organization's Penalties and the Nature of Self-Regulation," *Hofstra Law Review*, Vol. 40 (2012), pp. 963–1003, http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=5671&context=fss_papers (accessed December 9, 2016).
23. However, aspects of the NASD's regulatory function had left industry control as early as 1996. See Karmel, "Should Securities Industry Self-Regulatory Organizations Be Considered Government Agencies?" In addition, the NYSE regulatory function was no longer under industry control by the 1990s. For a discussion of the history of the evolution of SROs, see Daniel M. Gallagher, "U.S. Broker-Dealer Regulation," Chapter 6 in Hester Peirce and Benjamin Klutsey, eds., *Reframing Financial Regulation*, (Arlington, VA: Mercatus Center at George Mason University, 2016) https://www.mercatus.org/system/files/peirce_reframing_web_v1.pdf (accessed January 4, 2017).
24. See, for example, Peirce, "The Financial Industry Regulatory Authority: Not Self-Regulation After All," and William A. Birdthistle and M. Todd Henderson, "Becoming a Fifth Branch," *Cornell Law Review*, Vol. 99, No. 1 (2013), pp. 1–69, http://cornelllawreview.org/files/2013/11/99CLR1.pdf (accessed December 9, 2016).
25. Financial Industry Regulatory Authority, "FINRA Board of Governors," http://www.finra.org/about/finra-board-governors (accessed December 9, 2016).
26. Financial Industry Regulatory Authority, "Restated Certificate of Incorporation of Financial Industry Regulatory Authority, Inc.," Eighth Article, subsection (b), paragraph 2, http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=4589 (accessed December 14, 2016), and Financial Industry Regulatory Authority, "By-Laws, Article VII, Board of Governors," http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4628 (accessed December 14, 2016).
27. Financial Industry Regulatory Authority, "FINRA Board of Governors."
28. Neil Gunningham and Joseph Rees, "Industry Self-Regulation: An Institutional Perspective," *Law & Policy*, Vol. 19, No. 4 (October 1997), http://onlinelibrary.wiley.com/doi/10.1111/1467-9930.t01-1-00033/epdf (accessed December 9, 2016).
29. Anthony Ogus, "Self-Regulation (9400)," in Boudewijn Bouckaert and Gerrit De Geest, eds., *Encyclopedia of Law and Economics*, *Vol. I. The History and Methodology of Law and Economics* (Cheltenham, PA: Edward Elgar, 2000), http://encyclo.findlaw.com/9400book.pdf (accessed December 9, 2016).
30. Birdthistle and Henderson, "Becoming a Fifth Branch," p. 10.
31. See Securities and Exchange Commission, "Foundations of Self-Regulation" section in "Concept Release Concerning Self-Regulation," *Federal Register*, Vol. 69, No. 235 (December 8, 2004), pp. 71256–71282, https://www.gpo.gov/fdsys/pkg/FR-2004-12-08/pdf/04-26154.pdf (accessed December 9, 2016).
32. SEC Commissioner Luis A. Aguilar, "The Need for Robust SEC Oversight of SROs," Securities and Exchange Commission, May 8, 2013, https://www.sec.gov/News/PublicStmt/Detail/PublicStmt/1365171515546 (accessed December 9, 2016); Ogus, "Self-Regulation (9400)"; Birdthistle and Henderson, "Becoming a Fifth Branch," pp. 11 and 12; and Andrew F. Tuch, "The Self-Regulation of Investment Bankers," *George Washington Law Review*, Vol. 83, No. 1 (December 2014), pp. 101–175, http://www.gwlr.org/wp-content/uploads/2015/03/83-Geo-Wash-L-Rev-101.pdf (accessed December 9, 2016). Occupation licensing is often controlled by SROs or quasi-governmental organizations. On occupation licensing generally as a barrier to entry, see The White House, "Occupational Licensing: A Framework for Policymakers," July 2015, https://www.whitehouse.gov/sites/default/files/docs/licensing_report_final_nonembargo.pdf (accessed December 9, 2016), and Dick M. Carpenter et al., "License to Work: A National Study of Burdens from Occupation Licensing," Institute for Justice, May 2012, https://www.ij.org/images/pdf_folder/economic_liberty/occupational_licensing/licensetowork.pdf (accessed December 9, 2016).

33. "One cannot deal in securities with the public without being a member of FINRA. When a member fails to pay a fine levied by FINRA, FINRA can revoke the member's registration, resulting in exclusion from the industry." See *Fiero v. Financial Industry Regulatory Authority*, 660 F.3d 569, 576 (2d Cir. 2011).
34. 5 U.S. Code § 553.
35. 5 U.S. Code § 552.
36. 5 U.S. Code §§ 601–612.
37. 5 U.S. Code § 552b.
38. 44 U.S. Code §§ 3501–3531.
39. See, for example, Executive Orders 12866 and 13563 and Office of Management and Budget (OMB) Circular A-4.
40. FINRA Manual, Code of Arbitration Procedure for Customer Disputes, FINRA Rule 12602, Attendance at Hearings. See also FINRA Rules 9261 and 9265.
41. See detailed discussion below, in the section titled "Due Process."
42. However, once a rule is finalized by FINRA and submitted to the SEC for approval, the SEC does make the rule available for public comment. Dodd–Frank required that the SEC conduct its review of FINRA rules within 45 days. In FY 2015, only 63 percent were approved or disapproved within 45 days. Securities and Exchange Commission, *FY 2015 Annual Performance Report*, p. 25, https://www.sec.gov/about/reports/sec-fy2015-fy2017-annual-performance.pdf (accessed December 9, 2016).
43. Karmel, "Should Securities Industry Self-Regulatory Organizations Be Considered Government Agencies?" pp. 151–197; Michael Deshmukh, "Is FINRA a State Actor? A Question that Exposes the Flaws of the State Action Doctrine and Suggests a Way to Redeem It," *Vanderbilt Law Review*, Vol. 67, No. 4 (2014), pp. 1173–1211, https://www.vanderbiltlawreview.org/wp-content/uploads/sites/89/2014/06/Is-FINRA-a-State-Actor.pdf (accessed December 9, 2016); and Steven Irwin et al., "Self-Regulation of the American Retail Securities Markets–An Oxymoron for What Is Best for Investors?" *University of Pennsylvania Journal of Business Law*, Vol. 14, No. 4 (2012), pp. 1055–1084, http://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=1421&context=jbl (accessed December 9, 2016).
44. *Jackson v. Metropolitan Edison Co.*, 419 U.S. 345, 351, 95 S.Ct. 449, 42 L.Ed.2d 477 (1974).
45. *Blum v. Yaretsky*, 457 U.S. 991, 1004-05, 102 S.Ct. 2777, 73 L.Ed.2d 534 (1982).
46. See Federal Rules of Appellate Procedure (FRAP) 32.1, and John Szmer, Robert K. Christensen, and Ashlyn Kuersten, "The Efficiency of Federal Appellate Decisions: An Examination of Published and Unpublished Opinions," *The Justice System Journal*, Vol. 33, No. 3 (2012), p. 319, http://spia.uga.edu/faculty_pages/rc/law_pa_files/Pub12_JSJ_EfficiencyFedAppCourts.pdf (accessed December 9, 2016), finding that three-quarters of federal appellate decisions are now unpublished (unreported) and given that FRAP 32.1, after January 1, 2007, allows attorneys to cite opinions "designated as 'unpublished,' 'not for publication,' 'non-precedential,' 'not precedent,' or the like," unpublished opinions are of greater importance.
47. *Santos-Buch v. Financial Industry Regulatory Authority, Inc.*, U.S. Court of Appeals for the Second Circuit, No. 14-2767-cv, January 30, 2015, http://www.leagle.com/decision/In%20FCO%2020150130104/SANTOS-BUCH%20v.%20FINANCIAL%20INDUSTRY%20REGULATORY%20AUTHORITY,%20INC (accessed December 9, 2016).
48. *Busacca v. S.E.C*, U.S. Court of Appeals for the Eleventh Circuit, No. 10-15918, December 28, 2011, unpublished opinion, https://www.sec.gov/litigation/opinions/2010/34-63312-appeal.pdf (accessed December 9, 2016).
49. *D'Alessio v. S.E.C.*, 380 F.3d 112, 120 n.12 (2d Cir. 2004) [discussing whether the NASD is a state actor, but asserting that a determination of that issue was not necessary in that case]; *D.L. Cromwell Investments v. NASD Regulation*, 279 F.3d 155 (2d Cir. 2002) [finding that NASD is not a state actor]; *Desiderio v. NASD*, 191 F.3d 198, 206 (2d Cir. 1999) [finding that NASD is not a state actor but recognizing that "private entities may be held to constitutional standards if their actions are 'fairly attributable' to the state"]; *Gold v. SEC*, 48 F.3d 987 (7th Cir. 1995) [finding that due process was provided and side-stepping the state action issue]; and *Intercontinental Industries, Inc. v. American Stock Exchange*, 452 F.2d 935 (5th Cir. 1971) ["The intimate involvement of the [American Stock] Exchange with the Securities and Exchange Commission brings it within the purview of the Fifth Amendment controls over governmental due process."]. The American Stock Exchange was acquired by the NYSE in 2008 and since 2012 has been called NYSE MKT. See also *Saad v. SEC*, 718 F. 3d 904 (D.C. Cir. 2013) [finding that the commission abused its discretion in failing to address several potentially mitigating factors when upholding a FINRA lifetime bar].
50. Internal Revenue Service, Memorandum No. 201623006, Office of Chief Counsel, June 3, 2016, http://brokeandbroker.com/PDF/IRSFINRAFines.pdf (accessed December 9, 2016).
51. "The NYSE, as a[n] SRO, stands in the shoes of the SEC in interpreting the securities laws for its members and in monitoring compliance with those laws. It follows that the NYSE should be entitled to the same immunity enjoyed by the SEC when it is performing functions delegated to it." See *D'Alessio v. New York Stock Exchange, Inc.*, 258 F.3d 93 (2d Cir. 2001). See also *Sparta Surgical Corp. v. National Association of Securities Dealers, Inc.*, 159 F.3d 1209 (9th Cir. 1998), and *Weissman v. Nat'l Association of Securities Dealers, Inc.*, 500 F.3d 1293 (11th Cir. 2007).
52. 637 F.3d 112 (2d Cir. 2011), cert. denied January 17, 2012. Citations omitted. Both progressive organizations and free-market groups filed amicus briefs urging the Supreme Court to grant *certiorari*.
53. Ibid.
54. Birdthistle and Henderson, "Becoming a Fifth Branch" (quote is from the introductory abstract).

55. Gallagher, "U.S. Broker-Dealer Regulation." See also Commissioner Daniel M. Gallagher, "Market 2012: Time for a Fresh Look at Equity Market Structure and Self-Regulation," Securities and Exchange Commission, October 4, 2012, https://www.sec.gov/News/Speech/Detail/Speech/1365171491376 (accessed December 9, 2016).
56. Emily Hammond, "Double Deference in Administrative Law," *Columbia Law Review*, Vol. 116, No. 7 (November 2016), http://columbialawreview.org/content/double-deference-in-administrative-law/ (accessed December 9, 2016).
57. Center for Capital Markets Competitiveness, "U.S. Capital Markets Competitiveness: The Unfinished Agenda," Summer 2011, p. 5, https://www.uschamber.com/sites/default/files/legacy/reports/1107_UnfinishedAgenda_WEB.pdf (accessed December 9, 2016).
58. For the first nine months of 2016, FINRA statistics show the following misconduct-controversy types in customer arbitrations: Breach of Fiduciary Duty (1,572); Negligence (1,465); Failure to Supervise (1,417); Misrepresentation (1,300); Suitability (1,239); Breach of Contract (1,207); Omission of Facts (1,086); Fraud (1,010); Unauthorized Trading (279); Violation of State Blue Sky Laws (254); Churning (201); Manipulation (191); Margin Calls (62); Errors-Charges (44); and Transfer (28). See Financial Industry Regulatory Authority, "Top 15 Controversy Types in Customer Arbitrations," http://www.finra.org/arbitration-and-mediation/dispute-resolution-statistics (accessed December 9, 2016).
59. Mark Egan, Gregor Matvos, and Amit Seru, "The Market for Financial Adviser Misconduct," SSRN, March 2016, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2739170 (accessed December 9, 2016).
60. David Burton, "No Get-Out-of-Jail-Free Card for Bankers," *Newsweek*, February 28, 2015, http://www.newsweek.com/no-get-out-jail-free-card-bankers-310256 (accessed December 9, 2016).
61. See, for example, letter by Senators Elizabeth Warren (D–MA) and Tom Cotton (R–AR) to FINRA, May 11, 2016, https://www.warren.senate.gov/files/documents/2016-5-11_Warren-Cotton_Letter_to_FINRA.pdf (accessed December 9, 2016).
62. FINRA created its Office of the Chief Economist in 2013: Financial Industry Regulatory Authority, "Office of the Chief Economist," http://www.finra.org/industry/chief-economist (accessed December 9, 2016).
63. Hammad Qureshi and Jonathan Sokobin, "Do Investors Have Valuable Information About Brokers?" FINRA Office of the Chief Economist *Working Paper*, August 2015, p. 21, http://www.finra.org/sites/default/files/OCE-Working-Paper.pdf (accessed December 9, 2016), and Qureshi and Sokobin, "Do Investors Have Valuable Information About Brokers?" non-technical summary, August 2015, http://www.finra.org/sites/default/files/OCE-Non-technical-Summary.pdf (accessed December 9, 2016).
64. Ibid., *Working Paper*, p. 4.
65. Including "regular" Article III courts, Article II courts like the Tax Court, federal administrative law courts or, for that matter, any state court.
66. Joseph McLaughlin, "Is FINRA Constitutional?" *Engage*, Vol. 12, No. 2 (September 2011), pp. 111–114, http://www.fed-soc.org/publications/detail/is-finra-constitutional (accessed December 9, 2016).
67. 561 U.S. 477, 130 S. Ct. 3138, 177 L. Ed. 2d 706 (2010).
68. 15 U.S. Code § 7211(e)(6).
69. Public Company Accounting Oversight Board, "About the PCAOB," https://pcaobus.org/About/pages/default.aspx (accessed December 9, 2016).
70. 561 U.S. 477, 483–484.
71. 561 U.S. 477, 484.
72. The Free Enterprise decision found that the PCAOB being charged with enforcement of Sarbanes–Oxley was of central importance to determining if it was exercising executive power. FINRA is statutorily charged with enforcing the securities laws. See Securities Exchange Act § 15A(b)(2). See also FINRA By-Law Article XI ("to carry out the purposes of the Corporation and of the Act, the Board is hereby authorized to adopt such rules for the members and persons associated with members"). "The Act" is defined in FINRA By-Law Article I as the Securities Exchange Act of 1934.
73. 561 U.S. 477, 484.
74. McLaughlin, "Is FINRA Constitutional?" pp. 113–114. McLaughlin argues that FINRA does exercise executive power. For a discussion of these issues, also see *PHH Corporation v. Consumer Financial Protection Bureau* (DC Cir., October 11, 2016), https://www.cadc.uscourts.gov/internet/opinions.nsf/AAC6BFFC4C42614C852580490053C38B/$file/15-1177-1640101.pdf (accessed December 9, 2016). ("Applying the Supreme Court's separation of powers precedents, we therefore conclude that the CFPB is unconstitutionally structured because it is an independent agency headed by a single Director.")
75. Paul J. Larkin, Jr., "The Dynamic Incorporation of Foreign Law and the Constitutional Regulation of Federal Lawmaking," *Harvard Journal of Law & Public Policy*, Vol. 38, No. 1 (2015), pp. 416 and 417, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2556440 (accessed December 9, 2016).
76. 557 F.2d 1008 (3d Cir. 1977).
77. 198 F.2d 690 (2d Cir.), cert. denied, 344 U.S. 855, 73 S. Ct. 94, 97 L.Ed. 664 (1952).
78. The Maloney Act, Public Law No. 75–719 (June 25, 1938), created section 15A of the Securities Exchange Act and extended the role of SROs beyond exchanges. The NASD was created as a result, and it registered as an SRO on August 7, 1939. The Maloney Act is available at http://www.sechistorical.org/collection/papers/1930/1938_0625_MaloneyAct.pdf (accessed December 9, 2016). For more on the history of SROs and links to many historical documents, see Securities and Exchange Commission Historical Society, "The Institution of Experience: Self-Regulatory Organizations in the Securities Industry, 1792–2010, Self Help and the New Deal," http://www.sechistorical.org/museum/galleries/sro/sro04b.php (accessed December 9, 2016).

79. Securities Acts Amendments of 1975, Public Law No. 94–29, 89 Stat. 97 (1975), https://www.gpo.gov/fdsys/pkg/STATUTE-89/pdf/STATUTE-89-Pg97.pdf (accessed December 9, 2016). These amendments made a wide variety of changes to the Exchange Act provisions governing national securities associations, their members, and hearings conducted by SROs.
80. 557 F.2d 1008 (3d Cir. 1977) at footnote 6. ("There are some changes in the amendments as they apply to hearings before the Commission, e.g., under the 1934 Act, the S.E.C. is to make its decision 'upon consideration of the record before the association and such other evidence as it may deem relevant…' The 1975 amendment, on the other hand, states '…which hearing may consist solely of consideration of the record before the self-regulatory organization and opportunity for the presentation of supporting reasons to affirm, modify, or set aside the sanction …' Our consideration of this case is confined to the 1934 act, and we do not intimate any view on the constitutionality of the 1975 amendment.")
81. However, some of the governance changes made by the NASD and the NYSE in 1996 before FINRA's creation were important steps away from truly private, self-regulatory status. See Karmel, "Should Securities Industry Self-Regulatory Organizations Be Considered Government Agencies?" p. 163, n. 58, discussing NASD bylaw changes.
82. The details of this conversion process and the degree to which the SEC would preserve the right to not hire FINRA employees would need to be decided.
83. It is possible that an organization with strong industry representation could be more effective in discharging this function. The issue would need to be evaluated carefully.
84. Liz Moyer, "Finra Names Robert Cook Its Chief Executive," *The New York Times*, June 13, 2016, http://www.nytimes.com/2016/06/14/business/dealbook/finra-names-robert-cook-its-chief-executive.html?_r=0 (accessed December 9, 2016).
85. News release, "John J. Brennan Elected Chairman of FINRA Board of Governors," Financial Industry Regulatory Authority, July 15, 2016, http://www.finra.org/newsroom/2016/john-j-brennan-elected-chairman-finra-board-governors (accessed December 9, 2016).
86. David Michaels, "FINRA Board Seat Goes to Ex-Bear Stearns Partner in Tight Race," *The Wall Street Journal*, September 19, 2016. Bob Muh is quoted as saying: "So many small firms are angry over the huge increase in compliance costs to meet the many new rules."
87. Securities Exchange Act § 15A(b)-(d).
88. 5 U.S. Code § 552.
89. FINRA, "Board of Governors Meetings," http://www.finra.org/industry/governors-meetings (accessed January 4, 2017).
90. 5 U.S. Code § 552b.
91. *Richmond Newspapers, Inc. v. Virginia*, 448 U.S. 555, 580 n. 17 (1980) ("Whether the public has a right to attend trials of civil cases is a question not raised by this case, but we note that historically both civil and criminal trials have been presumptively open."); *Press-Enterprise Co. v. Superior Court*, 478 U.S. 1 (1986); *Press-Enterprise v. Superior Court*, 464 U.S. 501 (1984); and *Globe Newspaper Co. v. Superior Court*, 457 U.S. 596 (1982). See also *Gannett Co. v. DePasquale*, 443 U.S. 368 (1979) ("The experience in the American Colonies was analogous. From the beginning, the norm was open trials.... If the existence of a common-law rule were the test for whether there is a Sixth Amendment public right to a public trial, therefore, there would be such a right in civil as well as criminal cases.... Indeed, many of the advantages of public criminal trials are equally applicable in the civil trial context."). See also Jeanne L. Nowaczewski, "The First Amendment Right of Access to Civil Trials after Globe Newspaper Co. v. Superior Court," *University of Chicago Law Review*, Vol. 51, No. 1 (1984), pp. 286–314, http://chicagounbound.uchicago.edu/uclrev/vol51/iss1/10 (accessed December 9, 2016).
92. 137 Mass. 392 (1884), http://masscases.com/cases/sjc/137/137mass392.html (accessed December 9, 2016).
93. Financial Industry Regulatory Authority, BrokerCheck, http://brokercheck.finra.org/ (accessed December 9, 2016).
94. Qureshi and Sokobin, "Do Investors Have Valuable Information About Brokers?" *Working Paper*, p. 4. The nature of this unreported information is not entirely clear.
95. A mere complaint where there is no finding of wrong-doing, no award, no fine, or any adverse disciplinary action does not imply misconduct.
96. Financial Industry Regulatory Authority, "Dispute Resolution Statistics."
97. Securities Industry and Financial Markets Association, "White Paper on Arbitration in the Securities Industry," October 2007, http://www.sifma.org/uploadedfiles/societies/sifma_compliance_and_legal_society/whitepaperonarbitration-october2007.pdf (accessed December 9, 2016), and Barbara Black, "The Irony of Securities Arbitration Today: Why Do Brokerage Firms Need Judicial Protection?" *University of Cincinnati Law Review*, Vol. 72 (2003), http://digitalcommons.pace.edu/lawfaculty/16 (accessed December 9, 2016).
98. The Tax Court was created in 1942 as the successor to the U.S. Board of Tax Appeals. Major changes were made in 1969. For a history of the Tax Court and a discussion of its constitutional status, see Harold Dubroff and Brant J. Hellwig, *The United States Tax Court, An Historical Analysis*, 2nd ed. (Washington, DC: Government Printing Office, 2014), https://www.ustaxcourt.gov/book/Dubroff_Hellwig.pdf (accessed December 9, 2016). See also 26 U.S. Code § 7441, and *Freytag v. Commissioner*, 501 U.S. 868 (1991).
99. United States Court of Federal Claims, "The People's Court," http://www.uscfc.uscourts.gov/sites/default/files/USCFC%20Court%20History%20Brochure_0.pdf#overlay-context=about-court (accessed December 9, 2016).
100. Edward J. Eberle, "Procedural Due Process: The Original Understanding," *Constitutional Commentary*, Vol. 4 (1987), pp. 339–362 and 339, http://docs.rwu.edu/cgi/viewcontent.cgi?article=1057&context=law_fac_fs (accessed December 9, 2016).
101. *Joint Anti-Fascist Refugee Committee v. McGrath*, 341 U.S. 123, 171-172 (1951).

102. FINRA Rule 9212; FINRA Rule 12302; and FINRA Rule 13302.
103. FINRA Rule 9261; FINRA Rule 12602; and FINRA Rule 13602.
104. FINRA Rule 9265; FINRA Rule 12602; and FINRA Rule 13602.
105. This, of course, means that the date, time, and place of the proceeding must be made public. In addition, documents (notably pleadings) pertaining to the hearings should generally be made public as in court proceedings, perhaps using a database similar to the Public Access to Court Electronic Records (PACER), https://www.pacer.gov/ (accessed December 9, 2016).
106. FINRA Rule 12604(a).
107. FINRA Rule 9141; FINRA Rule 12208; and FINRA Rule 13208.
108. See also Federal Rule of Civil Procedure 38.
109. Margaret L. Moses, "What the Jury Must Hear: The Supreme Court's Evolving Seventh Amendment Jurisprudence," *The George Washington Law Review*, Vol. 68 (2000), pp. 183–257, http://lawecommons.luc.edu/cgi/viewcontent.cgi?article=1301&context=facpubs (accessed December 9, 2016).
110. Financial Industry Regulatory Authority, "FINRA Arbitrators," http://www.finra.org/arbitration-and-mediation/finra-arbitrators (accessed December 9, 2016).
111. Financial Industry Regulatory Authority, "Required Basic Arbitrator Training," http://www.finra.org/arbitration-and-mediation/required-basic-arbitrator-training (accessed December 9, 2016).
112. Financial Industry Regulatory Authority, "FINRA Arbitrators."
113. FINRA Rule 12403.
114. FINRA Notice 11-05, "Customer Option to Choose an All Public Arbitration Panel in All Cases," effective February 1, 2011, http://finra.complinet.com/en/display/display.html?rbid=2403&element_id=9973 (accessed December 9, 2016).
115. By striking all of the non-public (industry) arbitrators during the arbitrator-selection process; see FINRA Rule 12403.
116. For disciplinary proceedings, see FINRA Rules 9251–9253; for customer disputes, see FINRA rules 12505–12512; and for intra-industry disputes, see FINRA Rules 13505–13512.
117. See Federal Rules of Civil Procedure 26–37.
118. See FINRA Rule 12510. Federal administrative law courts permit depositions; see 5 U.S. Code § 556(c)(4).
119. American Arbitration Association, "Consumer Arbitration Rules: R-22. Exchange of Information between the Parties," 2016, https://www.adr.org/aaa/ShowProperty?nodeId=/UCM/ADRSTAGE2021425&revision=latestreleased (accessed December 9, 2016).
120. Steven Shavell, "Alternative Dispute Resolution: An Economic Analysis," *The Journal of Legal Studies*, Vol. 24, No. 1 (1995), pp. 1–28; Christopher R. Drahozal and Samantha Zyontz, "An Empirical Study of AAA Consumer Arbitrations," *Ohio State Journal on Dispute Resolution*, Vol. 25, No. 4 (2010), pp. 843–930, https://kb.osu.edu/dspace/bitstream/handle/1811/76944/OSJDR_V25N4_0843.pdf?sequence=1 (accessed December 9, 2016); and Theodore J. St. Antoine, "Mandatory Arbitration: Why It's Better than It Looks," *University of Michigan Journal of Law Reform*, Vol. 41, No. 4 (2008), pp. 783–812, http://repository.law.umich.edu/cgi/viewcontent.cgi?article=1466&context=articles (accessed December 9, 2016).
121. United States Arbitration Act, Public Law 68–401, 43 Stat. 883, February 12, 1925, codified at 9 U.S. Code §§ 1-16.
122. *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220, 107 S.Ct. 2332, 96 L.Ed.2d 185 (1987), and *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 131 S. Ct. 1740, 179 L.Ed. 2d 742 (2011).
123. FINRA Rule 12514(d).
124. FINRA Rule 12904(g).
125. FINRA Rule 12904(g)(2).
126. In 2015, FINRA had 3,500 employees with compensation, including benefits, of $688.7 million. This amounts to *average* compensation of $196,771 per employee: *FINRA 2015 Year in Review and Annual Financial Report*, p. 20. FINRA's compensation for arbitrators, making the unrealistic assumption that they worked every work day with two weeks of vacation, amounts to the equivalent of $150,000 annually ($600 per day times 50 weeks times five days).
127. Financial Industry Regulatory Authority, "What to Expect: Honorarium," http://www.finra.org/arbitration-and-mediation/what-expect-training-case-service-and-honorarium (accessed December 9, 2016).
128. "Statutory Maximum Rates Under the Equal Access to Justice Act," Ninth Circuit Court of Appeals, http://www.ca9.uscourts.gov/content/view.php?pk_id=0000000039 (accessed December 9, 2016), and 28 U.S. Code § 2412 (d)(2)(A). The DC Circuit is $190 per hour; see *Security Point Holdings, Inc. v. TSA*, September 2, 2016, p. 12, https://www.cadc.uscourts.gov/internet/opinions.nsf/FEEE2F100B567F3F85258022004E9F5F/$file/13-1068-1633546.pdf (accessed December 9, 2016).
129. 5 U.S. Code § 557(c).
130. This is the threshold for a three-arbitrator panel under current FINRA rules. See FINRA Rule 12401.
131. FINRA Rule 9311.

132. Financial Industry Regulatory Authority, "National Adjudicatory Council," http://www.finra.org/industry/nac (accessed December 9, 2016).
133. Financial Industry Regulatory Authority, "NAC Committee Members," http://www.finra.org/industry/nac-committee-members (accessed December 9, 2016).
134. FINRA Rule 9351.
135. FINRA Rule 9370, and Securities Exchange Act section 19(d)(2).
136. "The SEC reviews sanctions imposed by the NASD to determine whether they 'impose any burden on competition not necessary or appropriate' or are 'excessive or oppressive.'" *Siegel v. SEC*, 592 F.3d 147, 155 (DC Cir. 2010) (quoting 15 U.S. Code § 78s(e)(2)). "This court reviews the SEC's conclusions regarding sanctions to determine whether those conclusions are arbitrary, capricious, or an abuse of discretion," *Saad v. SEC*, 718 F. 3d 904 (DC Cir. 2013).
137. FINRA Rule 12904(b), and FINRA Rule 13904(b).
138. Government Accountability Office, "Opportunities Exist to Improve SEC's Oversight of the Financial Industry Regulatory Authority," GAO–12–625, May 30, 2012, http://www.gao.gov/products/GAO-12-625 (accessed December 9, 2016), and Government Accountability Office, "SEC Can Further Enhance Its Oversight Program of FINRA," GAO–15–376, April 30, 2015, http://www.gao.gov/products/GAO-15-376 (accessed December 9, 2016).
139. Wyatt, "Inside the National Exam Program in 2016"; Elizabeth Dilts, "SEC Says to Monitor Partner Regulator's Brokerage Oversight," Reuters, October 17, 2016, http://www.cnbc.com/2016/10/17/reuters-america-sec-says-to-monitor-partner-regulators-brokerage-oversight.html (accessed December 9, 2016); and "SEC Launches Dedicated FINRA Oversight Unit: Watching the Detectives," *National Law Review*.
140. Municipal Securities Rulemaking Board, "About the MSRB," http://www.msrb.org/About-MSRB.aspx (accessed December 9, 2016).
141. The National Futures Association, "Who We Are," http://www.nfa.futures.org/nfa-about-nfa/index.HTML (accessed December 9, 2016).
142. See §8G(a)(2) of the Inspector General Act of 1978, https://www.law.cornell.edu/uscode/html/uscode05a/usc_sup_05_5_10_sq2.html (accessed December 9, 2016).
143. Council of the Inspectors General on Integrity and Efficiency, "The Inspectors General," July 14, 2014, https://www.ignet.gov/sites/default/files/files/IG_Authorities_Paper_-_Final_6-11-14.pdf (accessed December 9, 2016). For the Inspectors General Act of 1978, as amended, see https://www.ignet.gov/sites/default/files/files/igactasof1010(1).pdf (accessed December 9, 2016).
144. For years 2011 to 2016, see FINRA, Statistics, http://www.finra.org/newsroom/statistics (accessed December 9, 2016), and FINRA Annual Reports 2007–2010, http://www.finra.org/about/annual-reports-financials (accessed December 9, 2016). For the years 2008–2010, FINRA provides only approximate numbers.
145. Hester Peirce and Stephen Matteo Miller, "Small Banks by the Numbers, 2000–2014," Mercatus Center, March 17, 2015, https://www.mercatus.org/publication/small-banks-numbers-2000-2014 (accessed December 9, 2016); Hester Peirce, Ian Robinson, and Thomas Stratmann, "How Are Small Banks Faring Under Dodd–Frank?" Mercatus Center, February 27, 2014, https://www.mercatus.org/publication/how-are-small-banks-faring-under-dodd-frank (accessed December 9, 2016); and Roisin McCord, Edward Simpson Prescott, and Tim Sablik, "Explaining the Decline in the Number of Banks Since the Great Recession," Federal Reserve Bank of Richmond, March 2015, https://www.richmondfed.org/-/media/richmondfedorg/publications/research/economic_brief/2015/pdf/eb_15-03.pdf (accessed December 9, 2016).
146. Peirce and Miller, "Small Banks by the Numbers, 2000–2014."
147. Goldman Sachs CEO Lloyd Blankfein, for example, recently said: "More intense regulatory and technology requirements have raised the barriers to entry higher than at any other time in modern history. This is an expensive business to be in, if you don't have the market share in scale. Consider the numerous business exits that have been announced by our peers as they reassessed their competitive positioning and relative returns." See "Regulation Is Good for Goldman," *The Wall Street Journal*, February 11, 2015, http://www.wsj.com/articles/regulation-is-good-for-goldman-1423700859?KEYWORDS=Regulation+Is+Good+for+Goldman (accessed December 9, 2016); Craig M. Lewis, "The Future of Capital Formation," Chief Economist and Director of the Division of Economic and Risk Analysis, MIT Sloan School of Management's Center for Finance and Policy's Distinguished Speaker Series, April 15, 2014, http://www.sec.gov/News/Speech/Detail/Speech/1370541497283#.VITmIsmwU0Q (accessed December 9, 2016); Jeff Schwartz, "The Law and Economics of Scaled Equity Market Disclosure," *Journal of Corporation Law*, Vol. 39 (2014); and C. Steven Bradford, "Transaction Exemptions in the Securities Act of 1933: An Economic Analysis," *Emory Law Journal*, Vol. 45 (1996), pp. 591–671, http://digitalcommons.unl.edu/cgi/viewcontent.cgi?article=1088&context=lawfacpub (accessed December 9, 2016). See also Securities and Exchange Commission, "Economic Analysis, Proposed Rule Amendments for Small and Additional Issues Exemptions Under Section 3(b) of the Securities Act," *Federal Register*, Vol. 79, No. 15 (January 23, 2014), pp. 3972–3993 [Release Nos. 33-9497, 34-71120, and 39-2493; File No. S7-11-13], http://www.gpo.gov/fdsys/pkg/FR-2014-01-23/pdf/2013-30508.pdf (accessed December 9, 2016).
148. 5 U.S. Code § 603.
149. For a discussion of these issues, see Barbara Black, "Punishing Bad Brokers: Self-Regulation and FINRA Sanctions," *The Brooklyn Journal of Corporate, Financial & Commercial Law*, Vol 8 (2013), pp. 23–55, http://scholarship.law.uc.edu/cgi/viewcontent.cgi?article=1221&context=fac_pubs (accessed December 9, 2016).
150. Regulatory revenues ($445 million); user revenues ($218 million); and contract services revenues ($126 million) in FY 2015 for a total of $789 million (excluding fines, dispute resolution, and other revenues). See *FINRA 2015 Year in Review and Annual Financial Report*, p. 19.

151. As with any tax, barring extreme assumptions about elasticities, the incidence of the tax is borne partially by shareholders and partially by consumers (and potentially by employees).
152. *FINRA 2008 Year in Review and Annual Financial Report: Reforming Regulation to Better Protect Investors*, p. 10, http://www.finra.org/sites/default/files/Corporate/p119061.pdf (accessed December 9, 2016).
153. The figures in the previous sentence divided by the number of members in Chart 2 (3,957 in 2015 and 4,900 in 2008).
154. Financial Industry Regulatory Authority, "Fines Policy," http://www.finra.org/industry/fines-policy (accessed December 9, 2016).
155. *FINRA 2015 Year in Review and Annual Financial Report*, p. 3.
156. Such a fund would reimburse consumers when sufficient funds cannot be recovered from the firm or individual committing the misconduct.
157. Kevin R. Kosar, "The Quasi Government: Hybrid Organizations with Both Government and Private Sector Legal Characteristics," Congressional Research Service, June 22, 2011, https://www.fas.org/sgp/crs/misc/RL30533.pdf (accessed December 9, 2016).
158. See appendix of *Budget of the U.S. Government, FY 2017*.
159. Ibid.
160. Financial Industry Regulatory Authority, "Requests for Comments," http://www.finra.org/industry/requests-comments (accessed December 9, 2016).
161. See §19(b) of the Securities Exchange Act.
162. It is the understanding of the author that the SEC staff has a major role in formulating FINRA rules and informally reviews proposed rules before they are formally submitted to the SEC.
163. 5 U.S. Code § 553.
164. Financial Industry Regulatory Authority, "Office of the Chief Economist," http://www.finra.org/industry/chief-economist (accessed December 9, 2016); Financial Industry Regulatory Authority, "Framework Regarding FINRA's Approach to Economic Impact Assessment for Proposed Rulemaking," September 2013, http://www.finra.org/sites/default/files/Economic%20Impact%20Assessment_0_0.pdf (accessed December 9, 2016); RSFI and OGC, "Current Guidance on Economic Analysis in SEC Rulemakings," *Memorandum*, March 16, 2012, https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf (accessed December 9, 2016); Executive Order 12866; and Office of Management and Budget Circular A-4.
165. This is analogous to Small Business Regulatory Enforcement Fairness Act (SBREFA) requirements that amended the Regulatory Flexibility Act, 5 U.S. Code §§ 601 et seq. See also Executive Order 13272.