NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION, INC.
750 First Street N.E., Suite 1140
Washington, D.C. 20002
202/737-0900
Fax: 202/783-3571
www.nasaa.org

NASAA

February 26, 2015

The Honorable Keith Ellison
U.S. House of Representatives
2263 Rayburn House Office Building
Washington, DC 20515

Re: H.R. 1098, the Investor Choice Act of 2015

Dear Congressman Ellison:

On behalf of the North American Securities Administrators Association (NASAA),[1] I am writing to applaud you for re-introducing legislation that prohibits the use of mandatory pre-dispute agreements by broker-dealers and investment advisers that limit investors' ability to pursue recourse in any forum. Your legislation will greatly benefit the public and give investors access to our judicial system. It will further the legislative intent of Congress and ensure that mandatory pre-dispute arbitration provisions are statutorily prohibited under the securities laws.

NASAA has long been concerned with the widespread use of mandatory pre-dispute arbitration clauses in customer contracts used by broker-dealers and, most recently, investment advisers. NASAA believes that investors must have a choice of forum when it comes to resolving disputes with their investment professionals. Investor confidence in fair and equitable recourse is critical to the stability of the securities markets and long-term investments by retail investors. NASAA has argued that participation by "mom and pop" investors in our capital markets, and, by extension, job growth, is directly tied to their level of trust in having a reasonable avenue to seek recovery if they are victimized by securities fraud or other unethical conduct.

Consumer disputes are typically resolved in court or through alternative dispute resolution processes (i.e., negotiation, mediation, arbitration, etc.). Investor disputes against broker-dealers, however, are resolved in only one forum: arbitration administered by the Financial Industry Regulatory Authority (FINRA). Investors are required to submit to FINRA arbitration and are denied access to the courts because almost all broker-dealer contracts require that their customers agree to binding, pre-dispute (i.e., before a dispute or loss is known) arbitration. Increasingly, investment advisers are also requiring that their customers agree to

[1] The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc. (NASAA) was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

mandatory pre-dispute arbitration as a precondition to becoming a customer of the advisory firm.[2] NASAA considers these "take-it-or-leave-it" clauses (also known as "contracts of adhesion" or "form contracts") to be detrimental to the public interest.

Section 921 of the Dodd-Frank Wall Street Reform and Consumer Protection (Dodd-Frank) Act, enacted on July 21, 2010, was included in response to Congressional concern that mandatory pre-dispute arbitration agreements were unfair to investors.[3] During deliberation, lawmakers observed the following with regard to mandatory pre-dispute arbitration clauses in broker-dealer contracts:

> For too long, securities industry practices have deprived investors of a choice when seeking dispute settlement, too. In particular, pre-dispute mandatory arbitration clauses inserted into contracts have limited the ability of defrauded investors to seek redress. Brokerage firms contend that arbitration is fair and efficient as a dispute resolution mechanism.
>
> Critics of mandatory arbitration clauses, however, maintain that the brokerage firms hold powerful advantages over investors. Brokerages often hide mandatory arbitration clauses in dense contract language. Moreover, arbitration settlements generally remain secret, preventing other investors from learning about the performance of a particular brokerage firm.
>
> If arbitration truly offers investors the opportunity to efficiently and fairly settle disputes, then investors will choose that option. But investors should also have the choice to pursue remedies in court, should they view that option as superior to arbitration. For these reasons, H.R. 3817 [the precursor to Section 921] provides the SEC with the authority to limit, prohibit or place conditions on mandatory arbitration clauses in securities contracts.[4]

Section 921 of the Dodd-Frank Act gives the U.S. Securities and Exchange Commission (SEC) explicit rulemaking authority to prohibit, condition or limit the use of mandatory pre-dispute arbitration agreements if it finds that doing so is in the public interest and for the protection of investors. Although Congress gave the SEC an important tool to act in this area, in the nearly five years since the Dodd-Frank Act was enacted, the SEC has not exercised its authority to conduct rulemaking or even examine the impact of mandatory pre-dispute arbitration clauses on investors and the public. In NASAA's Legislative Agenda for the 114th Congress,[5]

---

[2] Letter from Secretary William F. Galvin of the Commonwealth of Massachusetts to SEC Chair Elisse B. Walter and SEC Commissioners Tory A. Paredes, Luis A. Aguilar, and Daniel M. Gallagher (Feb. 12, 2013), *available at* http://www.sec.state.ma.us/sct/sctarbitration/arbitration-letter.pdf (citing a Massachusetts Securities Division survey to 710 state-registered Massachusetts investment advisers, which indicated that of the over 50% surveys received, nearly half of the investment advisers included a binding pre-dispute arbitration clause in their advisory contracts).

[3] Congress considered the following concerns about the arbitration process: "high upfront costs; limited access to documents and other key information; limited knowledge upon which to base the choice of arbitrator; the absence of a requirement that arbitrators follow the law or issue written decisions; and extremely limited grounds for appeal." AARP, letter to Senators Chris Dodd (D-CT) and Richard Shelby (R-AL), November 19, 2009. *See also* Senate Committee on Banking, Housing, and Urban Affairs on S. 3217, S. Rep. No. 111-176, at 110.

[4] House Committee on Financial Services on H.R. 3817, H.R. Rep. No. 111-687, Part 1, at 50.

[5] *Available at*: http://www.nasaa.org/wp-content/uploads/2011/08/NASAA-Legislative-Agenda-114th-Congress-Final.pdf.

we recommend Congressional action to codify Section 921 by prohibiting the use of mandatory pre-dispute arbitration clauses, and we urge Congress to exercise its oversight authority and investigatory responsibility to require the SEC to gather quantitative and qualitative data that would establish the analytical foundation for future rulemaking. In the absence of action by the SEC, we continue to support the Investor Choice Act as a necessary step in protecting investors and ensuring access to every available forum.

The time is ripe for the SEC to take action under its Section 921 authority, and in the absence of such action, for Congress to advance the underlying intent and spirit of Section 921 of the Dodd-Frank Act by amending the securities laws as applicable to broker-dealers and investment advisers to statutorily prohibit the use of any mandatory pre-dispute agreement that erodes class action or other investor rights to seek redress in the most appropriate forum of his or her choosing—H.R. 1098 accomplishes that goal.

Your bill ensures that investors will not be forced into arbitration or any other forum that could foreclose their ability to obtain relief. NASAA strongly supports H.R. 1098 and thanks you for recognizing that the inclusion of mandatory pre-dispute arbitration agreements in broker-dealer and investment adviser contracts undermines investor faith in the markets that Congress is trying to jump start. H.R. 1098 will ensure that investors have a meaningful choice and an unencumbered right to seek redress in the appropriate and desired forum.

For the reasons summarized above, NASAA applauds you for introducing the Investor Choice Act of 2015, and we look forward to working with you to ensure the legislation's timely enactment.

Sincerely,

William Beatty
NASAA President and Washington Securities Director