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OFFICE OF THE SECRETARY

Nancy M. Morris
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: **File Number SR-FINRA-2007-021 Proposed Rule Changes to FINRA Code of Arbitration Relating to Motions to Dismiss**

Dear Ms. Morris:

Charles Schwab & Co. Inc. ("Schwab") welcomes the opportunity to comment on SR-FINRA-2007-021, the FINRA's proposal governing motions to dismiss (the "Proposed Rules"). Schwab recognizes that any rule relating to the arbitration process potentially affects the interests of several different parties, including public investors, FINRA member firms and their associated persons, and Schwab commends FINRA for its ongoing efforts to enhance the arbitration process.

Schwab, however, does not support the Proposed Rules because they effectively eliminate pre-hearing motions to dismiss. Schwab believes that the Proposed Rules will have a negative impact on the arbitration process by forcing the parties including claimants to incur additional expense in cases where there is no legal or factual basis for a claim which warrants a hearing on the underlying merits and which will be lost at hearing in any event.

As an initial matter, pre-hearing motions to dismiss are rarely granted. Arbitration panels recognize the importance to investors to have their claims heard. To effectively remove a panel's discretion to grant pre-hearing motions to dismiss where the circumstances warrant unfairly and unnecessarily calls into question a panel's judgment.

FINRA's stated reasons for the Proposed Rules are abusive and duplicative filings by respondents in arbitrations. Specifically, it references comments received almost exclusively from the claimants' bar which assert that respondents use pre-hearing motions to dismiss as a delay tactic, to increase investors' costs, and to intimidate less sophisticated parties. Schwab strongly disagrees with these comments and is not aware of any empirical evidence to support them. To the extent that abuses do exist, there clearly are better, more direct ways to handle

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them. Parties could be limited to filing only one such motion in a proceeding and within a timeframe which does not cause any delay in a scheduled hearing. Motions deemed frivolous by the panel could be subject to sanctions and an award of attorney's fees against the losing party.

FINRA filed a previous rule proposal which would have permitted a panel to grant a dispositive motion prior to an evidentiary hearing only under "extraordinary circumstances." That proposal was withdrawn because it did not provide effective guidance on how such motions would be handled in the forum. The Proposed Rules offer to remedy that lack of guidance by affirmatively stating that there are only two grounds on which a panel may grant a motion to dismiss: (1) a signed settlement and/or written release and; (2) factual impossibility.

Rather than provide guidance by stating two extraordinarily narrow grounds for granting such motions, Schwab submits that it would benefit the arbitration process to establish certain grounds when a pre-hearing motion to dismiss should not be granted. One commentator has suggested that these grounds should be where: (1) credibility is an issue; (2) disputed issues of material fact exist; and (3) the panel believes a hearing is necessary in the interests of justice. Schwab agrees with this approach.

By stating broad grounds where a pre-hearing motion to dismiss should not be granted is preferable to attempting to enumerate the instances in which such a motion can be granted. The particular facts and circumstances of any given case make it virtually impossible to compile such an affirmative list.

As they stand, the Proposed Rules would only permit motions to dismiss where there is a signed settlement and/or written release and factual impossibility. The Proposed Rules completely ignore the fact that there are any number of situations in which a claimant cannot legitimately prevail.

For instance, nothing in the Proposed Rules would prevent a claimant from filing multiple arbitrations on the basis of facts which have been adjudicated by a prior arbitration panel. If a claimant brings a claim in arbitration and loses, he can refile the same claim and try again before another panel. This clearly undermines a fundamental purpose for arbitration – an expeditious and final resolution of claims.

Respondents would also be forced to a hearing where the law clearly bars the recovery sought by a claimant. The six-year eligibility rule was never intended to supplant statutes of limitation. Granted, most statements of claim do not set forth specific causes of action under the law or plead claims with the particularity required in courts, nor should they be required to do so. Nevertheless, there are clear cut instances where any conceivable interpretation of a claim would be barred by a statute of limitation which is shorter than the six-year period under existing rules.

There are instances where the substantive law clearly bars the relief sought by a claimant. For example, certain states bar claims for damages for alleged defamation on a U-5 filing. If damages are the only relief sought in such a case, no good purpose would be served to hold a hearing on the merits. The law is well-settled that where a clearing firm merely performs its contractual functions as a clearing broker - - without more - - it is not liable for a transaction. Also, where a brokerage firm merely serves as the custodian for a self-directed account and holds securities purchased at another firm, no liability attaches. Under the terms of a contract where responsibility for the suitability of trades is assigned by a customer to a third party, such as an independent investment advisor or power of attorney, and the brokerage firm is not responsible for monitoring account activity, it would not be fair to force the brokerage firm to a hearing on the merits on a pure suitability claim.

There are also cases in which the material facts are not in dispute. For example, a customer brings a suitability claim based upon the use of margin in a self-directed account. The brokerage firm can conclusively demonstrate that no securities were purchased on margin. Rather, the margin debit balance was created by the customer who wrote checks on the account. There is no basis to hold the brokerage firm liable when the market precipitously declines causing the liquidation of securities in the account. No one would conclude that it is the responsibility of the brokerage firm to tell a customer how to spend his money.

The scenarios recited above are not hypothetical, they are based on actual cases. The common thread throughout all of them is that in each case the Proposed Rules would require a full hearing on the merits. Such a hearing would be a waste of time and money for all parties involved.

The Proposed Rules would also preclude the filing of pre-hearing motions to dismiss which would dispose of some, but not all of the claims in an arbitration proceeding. There are instances where a claimant names multiple individuals at a brokerage firm, from the chief executive officer on down, as respondents in arbitration. It would not be factually impossible that these individuals would not have some percipient knowledge of the claims made. However, in most all instances they have no such knowledge and have been named in error or merely to harass. It is not fair to these individuals to have to wait until the end of a hearing to be dismissed from a case.

Where a claimant files multiple claims in one proceeding, there could be some claims which are valid and others which have no legitimate basis in fact or law. Again, if a claimant files an arbitration based on X transaction and an arbitration panel denies his claim after a hearing, he should not be able to bring another arbitration based upon X, Y, and Z transactions. Two of the claims are new but the other was already decided.

In each of these cases, the inability to dismiss individually named respondents or to eliminate patently meritless claims within a larger proceeding results in a waste of time and money for all parties. The scope of discovery is determined by the claims made and the individuals named as respondents. The additional cost this entails, including the delays resulting from discovery and additional disputes, is contrary to the underlying principles of arbitration. It undermines the efficiency and cost-effectiveness of the arbitration process.

In sum, Schwab believes that the myriad of factual and legal circumstances which can arise in any given arbitration case demonstrates that FINRA's approach to pre-hearing motions charles SCHWAB

to dismiss as set forth in the Proposal Rules is misguided. Rather than create narrow categories where arbitration panels are permitted to consider such motions, the rules should establish broad guidelines where such motions will not be allowed, coupled with sanctions in the case of frivolous motions. This approach will permit an arbitration panel to exercise its sound discretion to rule on the facts and circumstances of each case and to impose sanctions as warranted.

FINRA's suggestion that a respondent's ability to bring a motion to dismiss at the conclusion of a party's case *in chief on any theory* balances the competing interests of claimants to present their case and the respondents to challenge a claim they believe lacks merit is illusory. It does virtually nothing as a practical matter to address the competing interests of the parties to a hearing. By the time a party concludes its case in chief, the parties have already incurred the costs associated with discovery, the preparation of witnesses including experts, and travel.

If, however, FINRA's approach to pre-hearing motions to dismiss is adopted, then the Proposal Rules need to be expanded to include other categories of claims which can be the subject of such motions. Failure to do so would result in an imbalance which would be *inefficient, costly,* and fundamentally unfair to all parties.

Schwab submits that these additional categories should at a minimum include:

(1) claims barred by applicable statutes of limitation;
(2) legal impossibility;
(3) clearing brokers, named solely for their role in clearing a trade;
(4) where a contract clearly assigns liability to a third party other than a brokerage firm;
(5) where a prior governing arbitration award or court judgment exists, and;
(6) where there is no possibility that the claimant can prevail on a claim.

Thank you for considering Schwab's comments on this important issue.

Very truly yours,

Curt H. Mueller

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Vice President and
Associate General Counsel
Charles Schwab & Co., Inc.

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