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April 9, 2008

BY EMAIL TO: rule-comments@sec.gov
Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: File No. SR-FINRA-2007-021
Proposal Amending Rules 12206 and 12504 of the NASD Customer Code and Rules 13206 and 13504 of the NASD Industry Code to Address Motions to Dismiss

Dear Ms. Morris:

Morgan Stanley & Co. Inc. ("Morgan Stanley") appreciates the opportunity to comment on the above-referenced rule proposal (the "Proposal") submitted to the Commission by Financial Industry Regulatory Authority, Inc. ("FINRA").

Morgan Stanley acknowledges that the right to obtain dismissal of legally deficient claims prior to an evidentiary hearing must be balanced against FINRA's dual objectives of deterring abusive motion practices and assuring that legitimate claims receive a timely evidentiary hearing. As currently drafted, however, proposed Rules 12504(a)(6) and 13504(a)(6), which address "motions to dismiss prior to conclusion of case in chief," would virtually eliminate prehearing dispositive motions by allowing them to be filed in only two highly limited instances, namely, when the non-moving party released the claims in dispute or when the moving party was not associated with the account, securities or conduct at issue.[1]

[1] The Proposal also provides for the dismissal of claims that are ineligible for arbitration under Rules 12206 and 13206 (the "six-year rule"). Under such circumstances, the dismissal is not claim-dispositive and the parties are free to litigate their claims in court. This comment letter focuses on the Proposal as it relates to dispositive motions to dismiss that are not based on eligibility.

This drastic step is unjustified and unnecessary in light of separate provisions included in the proposed amendments to Rules 12504(a) and 13504(a) which fully address FINRA's concerns regarding abusive motion practices. These new provisions are designed to curb abusive motion practices by, among other things: (i) eliminating delays as a result of motions to dismiss (by requiring a party to file an answer before any motion to dismiss and requiring all motions to dismiss to be filed well in advance of a scheduled hearing); (ii) eliminating costs to non-movants associated with motions to dismiss (by requiring panels to assess forum fees against parties who file unsuccessful motions); (iii) requiring such motions to be decided by the full panel at a recorded hearing in which any award of dismissal is unanimous and accompanied by a written explanation; and (iv) providing sanctions for frivolous motions (including, but not limited to, the assessment of attorney's fees against the filing party).

FINRA and the SEC should first afford these new provisions reasonable time to deter the abusive motion practices which prompted the Proposal. Only if abuses are shown to persist after these amendments are adopted should the more drastic step of limiting the substantive grounds for prehearing dispositive motions be considered.

FINRA's broader proposal is unnecessary and would have negative consequences. For instance, the Proposal as currently drafted eliminates a respondent's right to file prehearing dispositive motions based on statutes of limitations. Such a rule may lead claimants to file patently time-barred claims in arbitration because the cost of defending these legally deficient claims through discovery and an evidentiary hearing will create settlement value where it did not previously exist. Without prehearing dispositive motions, a respondent will be forced to undertake the burden of preparing for a full arbitration not knowing if its motion, however sound, will be granted at the conclusion of claimant's case in chief. By then, discovery motions will already have been fought over and decided, fact witnesses will already have been subjected to trial preparation, expert witnesses will already have billed for the preparation of their reports, and travel expenses will already have been incurred for counsel and witnesses. FINRA administrators and arbitrators will similarly be unnecessarily burdened, as they will have handled discovery issues, administrative conferences, and full evidentiary hearings in cases that were facially deficient. And for what purpose? Both sides will have been forced to prepare their cases for arbitration despite lost witnesses, faded memories and missing documents that accompany the litigation of stale cases. These are the very policy concerns which support application of statutes of limitations in the first place, and they justify allowing panels to dismiss time-barred claims before the conclusion of the claimant's case-in-

chief. The Proposal will strip the arbitrators of their power to avoid these inefficiencies by dismissing such claims (and others that are legally barred) when there are no material facts in dispute.

I. SUMMARY

Morgan Stanley respectfully opposes the adoption of those portions of the Proposal that limit the substantive grounds for prehearing dispositive motions (*i.e.* Rules 12504(a)(6) and 13504(a)(6)) for the following reasons:

- Prehearing dispositive motions serve a primary goal of arbitration, namely, the efficient resolution of disputes. Where a sound basis for a dispositive motion exists, so long as each party receives a sufficient opportunity to be heard and there are no disputed factual issues that require holding a full evidentiary hearing, the moving party that meets its burden of proof should be entitled to the dismissal of legally deficient claims against it, thereby relieving all parties of the burden and expense of preparing for and attending a full evidentiary hearing.

- Prior governmental and regulatory analyses of securities arbitration endorse the use of prehearing dispositive motions. Numerous courts have affirmed arbitrators' awards granting prehearing dismissals on dispositive motions and found that such dismissals are fundamentally fair if handled appropriately. The Proposal represents an unjustifiable shift in arbitration policy which lacks prior legal, regulatory or governmental support.

- The concerns advanced in support of the Proposal regarding abusive motion practices are appropriately addressed by separate provisions within the Proposal, which would eliminate delays, prohibit a party from refiling a denied motion, and provide for cost and fee shifting as well as sanction mechanisms. These new rules, if adopted, will deter parties from filing dispositive motions for an improper purpose.

- The stated concern that dispositive motions increase the cost of or delay arbitrations is unsupported. Many counsel who represent claimants do so on a contingency fee basis. These claimants pay nothing or, at most, *de minimis* fees to their counsel to oppose prehearing dispositive motions. Moreover, if granted, dispositive motions relieve both sides of the time and expenses associated with discovery, trial preparation, and an

evidentiary hearing. Additionally, concerns regarding delays arising from prehearing dispositive motions are addressed by the new provisions that will require a party to file a full answer before moving to dismiss and submit any dispositive motion well in advance of the scheduled hearing date.

- The only conceivable rationale for preventing arbitration panels from considering most prehearing dispositive motions would be data demonstrating that arbitrators have acted improperly in granting such motions. **Yet, FINRA presents no data to support this. Courts and** commentators have repeatedly upheld arbitrators' competence to decide difficult factual and legal issues. FINRA has offered nothing to suggest that its arbitrators are somehow less than competent when deciding threshold legal issues where there are no disputed factual issues.

- The Proposal's prohibition of all but two substantive grounds for prehearing dispositive motions is unnecessarily overbroad and would eliminate entirely appropriate grounds for such motions, most notably, motions based on statutes of limitations. The Proposal would similarly prevent panels from dismissing claims prior to an evidentiary hearing based on such fundamental legal doctrines as *res judicata* and legal impossibility.

- Finally, the Proposal is one-sided. While removing a respondent's ability to obtain prehearing dismissals of demonstrably deficient claims, the Proposal contains no corresponding rule to deter or prevent a claimant from filing such claims. Thus, the Proposal may encourage the filing of legally deficient, frivolous, harassing, or stale claims because panels will be powerless to dismiss them until the conclusion of the claimant's case-in-chief.

II. PREHEARING DISPOSITIVE MOTIONS FURTHER A FUNDAMENTAL PURPOSE OF ARBITRATIONS, NAMELY, THE EFFICIENT RESOLUTION OF DISPUTES

Prehearing dispositive motions serve a primary goal of the arbitration process by furthering the efficient resolution of disputes. Where a sound basis for a dispositive motion exists, so long as each party receives a sufficient opportunity to be heard and

there are no factual issues in dispute that would require holding a full evidentiary hearing, the moving party that meets its burden should be entitled to an order of dismissal.

Far from increasing costs, prehearing motions to dismiss demonstrably deficient claims, if granted, relieve the parties of the substantial burden and expense of preparing for and attending a full evidentiary hearing on such claims. Even motions that are granted in part serve to promote efficiency by narrowing the scope of subsequent evidentiary hearings to claims with legal merit. Respondents are not the only beneficiaries of these cost savings. Dismissals also benefit claimants by relieving them of costs *not* covered by contingency fee agreements, for example, forum fees and expert witness costs, which can be substantial.

III. REGULATORS AND OTHER AUTHORITIES HAVE PREVIOUSLY ENDORSED THE USE OF PREHEARING DISPOSITIVE MOTIONS IN ARBITRATIONS

Regulators and others who have previously considered the issue have endorsed the use of prehearing dispositive motions in arbitration. Acceptance of dispositive motions, specifically dispositive motions based on statutes of limitations, appears in various analyses of securities arbitration. Moreover, numerous courts which have considered challenges to arbitrators' awards granting prehearing dismissals have confirmed such awards based on findings that the underlying proceedings were fair. The Proposal represents an unjustifiable shift in policy that has no prior support.

In September 1994, the Board of Governors of NASD appointed the Arbitration Policy Task Force to study the securities arbitration process administered by NASD and make suggestions for its reform. In January 1996, the Arbitration Policy Task Force, headed by former SEC Chairman David S. Ruder, published "Securities Arbitration Reform: Report of the Arbitration Policy Task Force" (the "Ruder Report"). According to NASD, the Ruder Report "represented the most comprehensive proposal to revamp securities industry arbitration since it was established to resolve investor disputes more than a century earlier." ("The Arbitration Policy Task Force Report – A Report Card" at 5, July 27, 2007). More importantly, the Ruder Report's recommendations "*formed the framework that currently guides NASD Dispute Resolution policy and rulemaking.*" *Id.*[2]

So far as relevant here, the Ruder Report recommended:

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[2] All emphasis is supplied unless otherwise indicated.

> NASD should institute procedures to provide *early resolution of statute of limitations issues in arbitration.* Specifically, the NASD should codify procedures to permit parties to move to dismiss claims or counterclaims on statutes of limitations grounds *prior to the merits hearing.* These motions, as well as any other dispositive motions, should be decided by the arbitration panel selected by the parties.

Ruder Report at 14. To assist arbitrators in deciding dispositive motions based on statutes of limitations:

> The Task Force recommends that the NASD Code be amended to provide express directions to arbitrators that, *in deciding whether claims are time barred, they must apply the applicable statutory or common law statutes of limitations.* In addition to codifying this decision in the NASD Code, the instructions should be set forth in the Arbitrator's Manual with examples.

Id. at 15.

The Ruder Report also recommended: "Because of the importance to the parties of decisions on dispositive motions, we urge that these motions be decided by the entire panel, as is the current practice, and not solely by the panel chair." *Id.* at 14-15. Further, the Ruder Report proposed that "the arbitrators consider dispositive motions to dismiss as *early as practicable in the process*, as frequently is done in civil litigation," and "anticipate[d] that this would be *well before a hearing on the merits in many cases.*" *Id.* at 15. The Ruder Report also recommended that "[t]he arbitrators should be required to provide the reasons for their decision to grant or to deny the motion to dismiss on the basis of statute of limitations in writing. The written statement should include reference to the law on which the arbitrators relied in reaching a determination." *Id.*[3] The Ruder Report's recommendations, made after an extensive examination of the securities

[3] In connection with its recommendations in support of motions to dismiss based on statutes of limitations, the Ruder Report also recommended a temporary three-year suspension of the eligibility rule, which it concluded was initially adopted "to serve the same purposes as a statute of limitations, that is, to eliminate stale claims." *Id.* at 12. After noting that the eligibility rule "was designed to provide certainty and to render the arbitration process faster and less costly," the Report concluded that the rule "has fostered extensive litigation...." *Id.* Under such circumstances, the goals of arbitration could be best advanced through the early application of statutes of limitations.

arbitration process, support the principle that motions to dismiss can be highly useful if accompanied by appropriate procedural safeguards such as those that have been included in the Proposal to prevent delay, unnecessary costs and abusive motion practices.

The Ruder Report was followed by another study conducted by the U.S. General Accounting Office (n/k/a the U.S. Government Accountability Office) (the "GAO"). On April 11, 2003, the GAO issued a report titled "Follow-up Report on Matters Relating to Securities Arbitration" (the "GAO Report") (GAO-03-162R). The GAO Report was prepared at the behest of Congress to evaluate issues relating to securities arbitration policy and processes, and in that capacity, the GAO made recommendations to improve various aspects of securities arbitration.

Importantly, after consideration of "concern about the use of motions to dismiss and motions for summary judgment to terminate NASD-administered arbitrations," GAO Report at 1, the GAO Report made *no* recommendations to change (or otherwise limit) dispositive motion practice in arbitrations. To the contrary, the GAO Report concluded that dispositive motions are consistent with NASD practice:

> NASD arbitration rules do not specifically provide for dismissal motions or for motions for summary judgment. However, nothing in the rules prohibits the parties from filing motions or precludes panels from granting them. *NASD rules are consistent with the practice of disposing of claims by motion. NASD rules allow prehearing conferences at which the presiding person can require the briefing of contested issues and address "any other matters which will expedite the arbitration cases."*

GAO Report at 7 (citing Former Code of Arbitration Rule 10321).

The commentary authored by the SEC and NASD in response to the GAO Report further endorsed the GAO Report's findings with respect to dispositive motions. In particular, the SEC noted: "GAO [] observed that motions to dismiss are not used with great frequency. *Used sparingly, as the draft report reflects, such motions can be used effectively to conserve the parties' resources or direct parties to a correct forum outside of arbitration.*" Letter from Annette Nazareth, Director of the Division of Market Regulation, SEC, to William O. Jenkins, Jr., U.S. General Accounting Office, at 1 (March 28, 2003) (Enclosure I to GAO Report).

NASD Dispute Resolution similarly has recognized the use of prehearing dispositive motions in NASD arbitrations, emphasizing that each side receives a sufficient opportunity to be heard on such motions:

> We fully agree with the GAO Report that parties deserve to be fully and fairly heard. NASD attempts to provide procedural safeguards by administratively managing this motion practice to ensure that each side gets a fair opportunity to be heard on any matter presented to the arbitrators. Our administrative procedures and arbitrator training focus on providing that opportunity to be heard on any matter presented to the arbitrators. While arbitrators may address such motions prior to the beginning of a hearing, the arbitrators always accept arguments from all sides, either through written submissions or oral argument, before ruling. Further, the full panel is always involved in these decisions. We allow parties to practice advocacy as they choose and try to provide a fair and efficient mechanism to assist the parties in reaching a resolution.

Letter from Linda D. Feinberg, President, NASD Dispute Resolution, to William O. Jenkins, Jr., U.S. General Accounting Office, at 11-12 (March 26, 2003) (Enclosure II to GAO Report).

The GAO Report also found that "[t]he case law consistently has recognized the authority of arbitrators to grant prehearing motions to dismiss." *Id.* at 7. Indeed, the authors of the GAO Report stated, "[w]e have not found any cases that do not recognize arbitrators' authority to grant prehearing motions to dismiss." *Id.* at 8.

In addition to the above authorities, numerous courts have confirmed arbitrators' awards granting prehearing dispositive motions, including motions based on statutes of limitations. In these cases, the courts have determined that the arbitrators provided each side with a fundamentally fair hearing before dismissing all claims on a prehearing motion to dismiss. *See, e.g., Sheldon v. Vermonty*, 269 F.3d 1202, 1206 (10th Cir. 2001) ("[W]e hold that a NASD arbitration panel has full authority to grant a prehearing motion to dismiss with prejudice based solely on the parties' pleadings so long as the dismissal does not deny a party fundamental fairness."); *Tricome v. Success Trade Securities*, NO. CIV.A. 05-4746, 2006 WL 1451502, at *3 (E.D. Pa. May 25, 2006) (holding that "arbitrators may grant a motion to dismiss without holding a full evidentiary hearing"); *Wise v. Wachovia Securities, LLC*, 2005 WL 1563113, at *3 (N.D. Ill. May 4, 2005)

("[A]lthough NASD did not conduct a formal evidentiary hearing, the Plaintiffs received an otherwise fundamentally fair proceeding.") *aff'd* 450 F.3d 265 (7th Cir. 2006); *Warren v. Tacher*, 114 F. Supp. 2d 600, 602-03 (W.D. Ky. 2000) ("Petitioners were given adequate opportunity to respond to Bear Sterns' motion to dismiss and they did so. They were represented by counsel at oral arguments. Plaintiffs cite to no authority that they were automatically entitled to a full-blown evidentiary hearing following discovery, and the court is aware of none.").[4]

IV. FINRA'S CONCERNS REGARDING ABUSIVE AND REPETITIVE MOTION FILINGS ARE ADEQUATELY ADDRESSED THROUGH SEPARATE PROVISIONS OF THE RULE PROPOSAL

FINRA's concerns regarding abusive and repetitive dispositive motion practice, as well as delays arising from such practice, can be addressed and resolved fully through the adoption of amendments that do not unnecessarily limit the substantive grounds for prehearing motions to dismiss.

For example, the Proposal permits an arbitration panel to issue sanctions if it determines that a party filed a motion in bad faith. Proposed Rules 12504(a)(11) and 13504(a)(11). The Proposal further *requires* the panel to award reasonable costs and attorneys' fees to a party that opposed a motion to dismiss deemed frivolous by the panel. *Id.* at 12504(a)(10) and 13504(a)(10). Furthermore, the Proposal *requires* the panel to assess forum fees associated with hearings on motions to dismiss against the filing party if the panel denies the motion. *Id.* at 12504(a)(9) and 13504(a)(9). These aspects of the Proposal more than adequately address FINRA's concerns regarding abusive motion practices.

Addressing FINRA's related concern regarding repetitive or duplicative filings, the Proposal prohibits a party from re-filing a denied motion to dismiss unless specifically permitted by a panel order. *Id.* at 12504(a)(8) and 13504(a)(8). Moreover,

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[4] Moreover, consistent with prior NASD practice, other arbitral fora recognize the utility of and approve prehearing dispositive motions. For example, under American Arbitration Association Commercial Arbitration Rule R-30(b), the arbitrators have discretion to "conduct the proceedings with a view to expediting the resolution of the dispute and may direct the order of proof, bifurcate the proceedings and direct the parties to focus their presentations on issues the decision of which could dispose of all or part of the case." *See* Rule R-30(b) (http://www.adr.org/sp.asp?id=22440#R30). Likewise, Comprehensive Arbitration Rule 18(a), "Summary Disposition of a Claim or Issue," governing Judicial Arbitration and Mediation Services, Inc. ("JAMS") arbitrations vests arbitrators with authority to "permit any Party to file a Motion for Summary Disposition of a particular claim or issue, either by agreement of all interested Parties or at the request of one Party, provided other interested Parties have reasonable notice to respond to the request." *See* Rule 18(a) (http://www.jamsadr.com/rules/comprehensive.asp#Rule%2018).

FINRA's concerns about delays arising from prehearing dispositive motions are addressed in its proposed amendments requiring an Answer to be filed before any motion to dismiss and requiring motions to dismiss to be filed 60 days before a scheduled hearing. *Id.* at 12504(a)(2) and (a)(3) and 13504(a)(2) and (a)(3).

Finally, the Proposal contains new rules to further ensure fairness in the process for hearing and deciding dispositive motions. These new rules include precluding a panel from granting a motion to dismiss unless the panel holds an in-person or telephonic prehearing conference on the motion, requiring a unanimous decision by the panel to grant a motion to dismiss and requiring a written explanation of the decision to grant a motion to dismiss in the award. *Id.* at 12504(a)(4), (a)(5), and (a)(7), and 13504(a)(4), (a)(5), and (a)(7).

These new amendments, if adopted, will effectively deter the filing of abusive or repetitive dispositive motions. Assuming, as FINRA does, that certain parties previously filed inappropriate motions, these measures will reduce the future volume of prehearing motions to dismiss. The new amendments will also ensure procedural fairness in the process for hearing and deciding dispositive motions.

Since these new amendments will most likely fully address all of FINRA's concerns regarding abusive motion practices, the adoption of additional rules is unnecessary. At a minimum, FINRA and the SEC should first see if the new amendments eliminate the abuses that prompted FINRA to make the Proposal. Thereafter, only if the abuses are shown to persist should the more drastic step of limiting the substantive grounds for prehearing dispositive motions be considered.

V. FINRA HAS PROVIDED NO RATIONALE FOR ITS PROPOSAL TO LIMIT THE SUBSTANTIVE GROUNDS FOR PREHEARING DISPOSITIVE MOTIONS; FINRA ARBITRATORS ARE CAPABLE OF FAIRLY DECIDING SUCH MOTIONS

The only conceivable rationale for drastically restricting the substantive grounds for prehearing dispositive motions to two narrow grounds would be data demonstrating that FINRA arbitrators have previously acted improperly in granting prehearing dispositive motions on other substantive grounds (e.g., statutes of limitations). Yet, the Proposal contains no data to support this. Nor does the Proposal present data or other information demonstrating that FINRA arbitrators are incapable of properly deciding such motions. Arbitrators qualified to render awards at the conclusion of a case are, by definition, equally qualified to decide dispositive legal issues at an earlier (prehearing)

stage. Indeed, FINRA has never expressed concern over the quality of its arbitrators' decisions on dispositive motions.

Rather, the Proposal appears to be based solely on allegations of abuse and a recent rise in the volume of dispositive motions filed. As discussed in Section IV above, concerns about the volume of abusive motions are *fully addressed* by the separate provisions within the Proposal that, among other things, impose attorney's fees for frivolous filings and permit additional sanctions for motions filed in bad faith. By proposing to eliminate previously accepted *substantive* grounds for prehearing dispositive motions (such as statutes of limitations) without even a scintilla of proof that motions based on these accepted substantive grounds have been improperly decided – the Proposal is overbroad and unnecessary. Further, whether an intended consequence or not, a rule divesting arbitrators of the authority to decide most prehearing dispositive motions would communicate to the public that arbitrators cannot be trusted to fairly adjudicate prehearing legal issues. This could undermine public confidence in the fairness and quality of the entire arbitration process.

VI. THE PROPOSAL TO LIMIT THE SUBSTANTIVE GROUNDS FOR DISPOSITIVE MOTIONS IS OVERBROAD IN THAT IT WOULD ELIMINATE THE AUTHORITY OF ARBITRATORS TO ADJUDICATE APPROPRIATE LEGAL ISSUES AT AN EARLY STAGE

The Proposal would eviscerate longstanding and well-accepted substantive grounds for prehearing dispositive motions in arbitrations, most notably, motions based on statutes of limitations. The Proposal would also prevent panels from dismissing claims prior to an evidentiary hearing based on the doctrines of *res judicata* and legal impossibility. Finally, as presently drafted, the Proposal could be construed (improperly in our view) as prohibiting panels from granting early motions to dismiss senior executives who have no personal knowledge of the claim and who are named as respondents for improper purposes.

A. Time-Barred Claims

FINRA has long recognized the enforceability of statutes of limitations in arbitrations. For example, the 1996 NASD Panel Member Course Preparation Guide makes clear that claims barred by the applicable statute of limitations must be dismissed: "The statute of limitations refers to a prescribed time limit after which a cause of action or claim may not be brought. If the arbitration is brought after the statute of limitations had run and the time period cannot be tolled, the claim should be dismissed with prejudice...." The 2005 NASD Arbitrator Training, Panel Course Preparation Guide

contains the same instruction to arbitrators to dismiss claims barred by the applicable statutes of limitations. (v. 1.3 (2005)).

The recently published new NASD Code of Arbitration Procedure ("NASD Code") similarly recognizes the importance of disallowing stale claims and expressly directs that statutes of limitations are to be applied and enforced in FINRA arbitrations. Specifically, NASD Code 12206 states that a claim must be filed within six years of the conduct at issue in order for it to be "eligible" for arbitration with the caveat that this "eligibility" provision "does not extend applicable statutes of limitations." *See also* NASD Arbitrator's Manual (January 2007 at p. 8) ("The arbitrators should also be aware that a statute of limitations may preclude the awarding of damages even though the claim is eligible for submission to arbitration.").

Proposed Rules 12504(a)(6) and 13504(a)(6), if adopted, would preclude respondents from filing prehearing dispositive motions based on expiration of statutes of limitations. Instead, respondents will be forced to absorb the cost of evidentiary hearings against parties with demonstrably time-barred claims. Nothing in the Proposal justifies the removal of arbitrators' historically recognized authority to dismiss time-barred claims under applicable law prior to a full evidentiary hearing.

Divesting arbitrators of their longstanding authority to summarily dismiss time-barred claims will have substantial adverse consequences. Claimants with patently stale claims may commence arbitrations because the cost of defending these claims through an evidentiary hearing will create settlement value, despite their legal deficiency. The parties, FINRA administrators and FINRA arbitrators will be forced to try, administer, and hear a full-blown arbitration without regard to whether the claims are legally barred based on the undisputed facts. While not all statutes of limitations issues may be appropriate for summary resolution, there certainly are instances in which arbitrators can be satisfied based on the record before them that claims are legally barred regardless of the evidence a claimant intends to introduce. In such cases, the Proposal's requirement that such facially flawed claims proceed through a full arbitration would result in wasteful litigation against the interests of the parties, the forum and the arbitrators.

B. *Res Judicata* or Arbitration and Award

Claims subject to dismissal based on the doctrine of *res judicata* also illustrate the injustice of the Proposal. Even if the parties have litigated a matter to final resolution in court or in an arbitration that proceeded to a final award, the Proposal would seemingly allow a party to refile its claims in arbitration and receive full discovery and an

evidentiary hearing before the claims could be dismissed. While under the Proposal the arbitrators would have the opportunity to dismiss such a claim after claimant's case in chief, the respondent in that matter would again be forced to expend the resources to prepare for and attend the hearing of an obviously invalid claim.

C. Legal Impossibility

Prehearing dismissals based on legal impossibility (failure to state a claim) would also be foreclosed, thus allowing specious claims to proceed to an evidentiary hearing even if the arbitrators believe that there is no dispute over the material facts and no need to resolve any credibility issues. One example of a "legally impossible" claim would be a registered representative's Form U-5 defamation claim in the state of New York. On March 29, 2007, New York's highest court held in *Rosenberg v. Metlife, Inc.*, that statements made by a brokerage firm in a Form U-5 Termination Notice are subject to an absolute privilege in a suit for defamation. *See Rosenberg v. Metlife, Inc.*, 8 N.Y.3d 359, 368 (2007). Yet, under the Proposal, a respondent defending a claim based on this "legally impossible" ground would be forced to bear the costs of discovery, trial preparation and an evidentiary hearing even if the arbitrators have concluded that they would dismiss all claims as a matter of well-settled law regardless of the evidence presented at the final hearing.

D. Senior Executives

Proposed Rules 12504(a)(6)(B) and 13504(a)(6)(B) permit a panel to consider a prehearing motion to dismiss a party who "was not associated with the account(s), security(ies), or conduct at issue." Clarification is necessary regarding whether FINRA intended these rules to permit prehearing dismissals of senior executives who have no knowledge of the claimants or the allegations in the claim. If FINRA did not intend for Rules 12504(a)(6)(B) and 13504(a)(6)(B) to cover senior executives in such circumstances, it should so state and the SEC should reject FINRA's position.

Such a rule would require senior executives to attend arbitration hearings rather than run their firm's business and would thus adversely impact the shareholders of member firms. Established law authorizes the dismissal of senior executives who have no meaningful connection to the claim and who were named as defendants/respondents solely to increase the *in terrorem* effect or settlement value of a claim. When this occurs, courts and arbitrators alike have granted prehearing dispositive motions to dismiss senior executives from proceedings. *See, e.g., Rich v. Maidstone Financial, Inc.*, 2001 WL 286757 (S.D.N.Y. March 23, 2001) (dismissing claim against officer of brokerage

company because the complaint offered no factual details in support of its general allegations of officer's involvement in alleged misconduct); *Cascardo v. A.G. Edwards & Sons, Inc., et al.*, 2007 WL 3022844 (FINRA Oct. 2, 2007) (ordering prehearing dismissal of Chief Executive Officer Robert L. Bagby); *Goldsmith v. Merrill Lynch, et al.*, 2005 WL 524733 (NASD Feb. 15, 2005) (ordering prehearing dismissal of Chief Executive Officer E. Stanley O'Neal); *Soofi v. American Express Financial Advisors, et al.*, 2003 WL 22462637 (NASD Oct. 24, 2003) (ordering prehearing dismissal of Chief Executive Officer Kenneth I. Chenault); *Woody v. Morgan Stanley DW Inc., et al.*, 2003 WL 22881023 (NASD Nov. 17, 2003) (ordering prehearing dismissal of Chief Executive Officer Philip J. Purcell); *Ganguly v. Charles Schwab & Co., Inc.*, 2004 WL 213016, at *2 (S.D.N.Y. February 4, 2004) (hearing panel dismissed brokerage firm's CEO despite allegations of his nominal involvement in purportedly improper practices).

If the Proposal is adopted, senior executives and their corresponding firms will be deprived of such necessary prehearing relief.

VII. THE PROPOSAL TO LIMIT THE SUBSTANTIVE GROUNDS FOR DISPOSITIVE MOTIONS IS ONE-SIDED

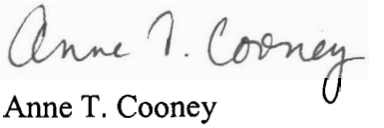
Finally, the Proposal is unfairly one-sided in its application. While proposed Rules 12504(a)(6) and 13504(a)(6) largely eliminate a party's ability to dismiss deficient claims at the prehearing stage, the Proposal contains no corresponding rule to deter or prevent a party from *filing* a deficient or frivolous claim. This inequity may actually encourage the filing of legally deficient, frivolous, harassing or stale claims because panels will be powerless to dismiss them until the conclusion of the claimant's case-in-chief. Such an open playing field for claimants without any concomitant vehicle for respondents to dismiss deficient claims serves no legitimate purpose and will only increase the costs of arbitrations for both sides, while reducing FINRA's ability to effectively serve those claimants who file legitimate claims.

VIII. CONCLUSION

Morgan Stanley respectfully urges against the adoption of proposed Rules 12504(a)(6) and 13504(a)(6) which, as drafted, unjustifiably limit the substantive grounds for prehearing dispositive motions. FINRA's concerns regarding abusive motion practices are adequately addressed through its other proposed rule amendments. Before

taking the drastic step of limiting the substantive grounds for prehearing dispositive motions, FINRA and the SEC should first determine whether FINRA's concerns regarding abusive motion practices are fully corrected through its separate proposed rule amendments.

Respectfully submitted,



Anne T. Cooney
Managing Director

cc: Linda D. Fienberg, President, FINRA Dispute Resolution
George H. Friedman, Executive Vice President, FINRA Dispute Resolution