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Via E-Mail

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F. Street, NE
Washington, DC 20549-1090

Re: File Number SR-FINRA-2007-021

Dear Ms. Morris:

I appreciate the opportunity to comment on proposed revisions to Rules 12206 and 12504 of the NASD Code of Arbitration Procedure regarding motions to dismiss (the "Proposed Rules"). In my practice, I frequently represent broker-dealers and brokers in disputes with customers. Although imperfect, arbitration is an effective, efficient and balanced method of resolving conflicts between brokerage firms and their customers. Because the proposed rules are not necessary, are not calibrated to address the perceived problem, and ultimately may impair the integrity of the FINRA arbitration process, the amendments should not be adopted.

1. The Increasing use of Motions to Dismiss is an Appropriate Response to the Declining Quality of Claims.

Motions to dismiss have undoubtedly increased in recent years. But, in my experience, that increase in motion practice is directly related to the increasing number of legally baseless claims brought by the claimants' bar. The data is clear that as a result of the sustained growth in the markets after the correction in 2000-2001, the number of claims filed by investors has declined sharply. Less well documented, but equally apparent to myself and other practitioners in this area, is that the quality of cases brought by counsel for investors has declined even more steeply. Claimants' counsel are increasingly bringing cases that are beyond the relevant statute of limitations, that invoke laws that are facially not applicable to securities disputes, and that seek "damages" that do not exist.

The proper method of addressing such claims is through a motion to dismiss, empowering the arbitrators to determine early the same legal issues they would ultimately be required to resolve

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at the end of the case. Arbitrators are obligated to apply the law and, in many cases, the law requires the dismissal of a claim prior to a full evidentiary hearing. Indeed, in the case of statutes of limitations, arbitrators are trained by FINRA to dismiss claims that are not timely under applicable law. Like most respondents' counsel and respondents, I make selective use of motions to dismiss to seek the early dismissal of cases or claims that plainly lack a legal basis.[1] A balanced concern for the fairness of the arbitration process would welcome, not discourage, the increased efforts by respondents to terminate claims that fail on their face at an early stage.

FINRA's proposed rule is unwarranted because FINRA has no basis to believe that the increase in motion practice is driven by the appropriateness of the motions, not the quality of the claims by investors. Claimants' counsel would obviously prefer to proceed to hearings without ever having to defend the legal adequacy of their claim. Accordingly, they allege that the rise in dispositive motions is driven by "frivolous" pleadings. FINRA appears prepared to accept this claim, based on anecdotal evidence and "focus groups." But the release supporting the new rules and other published information regarding this issue reveal absolutely no attempt by FINRA to evaluate the merits of the motions or the cases at issue. Were FINRA to do so, I believe that FINRA would find that the vast majority of motions are brought against claims that are stale, assert inapplicable legal claims, involve parties that are immune from civil liability, or otherwise involve cases that lack a legal basis. To proceed with any modification of the rules without some qualitative analysis of the quality of the cases to which motions to dismiss have been directed is inherently unfair.

2. <u>Under the Current System, Claims are Not Being Improperly Dismissed.</u>

The current process for resolving motions to dismiss is fair and does not require modification. Some letter comments suggest that motion to dismiss practice in arbitration somehow impairs the "due process" rights of investors. In fact, there is a clear and well defined body of law that establishes the due process requirements of a motion to dismiss. That case law requires a full

[1] Commenters from the claimants' bar have suggested that motions to dismiss are filed for the improper purpose of "climitizing" a panel or setting a favorable legal framework for the case. To the extent a motion to dismiss has this effect, it is no basis for criticism. Establishing early the legal principles that will control a case is a positive step. Of course, claimants are always given an opportunity to respond to motions, and accordingly the ability to establish the legal framework is mutual. In any event, the suggestion that respondents file such motions solely for that purpose is simply wrong. Respondents have the opportunity to file an Answer and are free to set forth the legal framework they believe controlling in that document, without the clear opportunity for a reply from claimants. The suggestion that respondents would bear the expense of doing in a motion to dismiss that they can do more directly in an Answer is baseless.

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and fair opportunity for the claimants to be heard. In every proceeding in which I have been involved, claimants have been given an opportunity to fully brief the legal issues and argue the matter in a hearing, whether in person or by phone. Such an opportunity meets the due process standard easily and, exceeds the procedural opportunities provided in courts. If the process by which motions to dismiss are resolved is the real concern, the rules should directly provide more structure in that regard. The proposed rules would, if anything, needlessly diminish the due process rights of respondents with no corresponding gain to claimants.

But there is a more telling fact that confirms that FINRA arbitrators do not unfairly resolve motions against claimants. Although dozens of lawyers from the claimants' bar have filed comment letters complaining about the unfairness of motions to dismiss, not a single comment letter that I have reviewed asserts that a motion to dismiss has been improperly granted, divesting a public investor of a claim that had merit. They do not make such claims, no doubt, because they cannot. Thus, the real arguments in favor of the new rules relate solely to the interests of claimants' counsel, which they describe as concerns of "efficiency," not the fairness of the proceedings for public investors.

3. <u>Motions to Dismiss Impose No Hardship on Claimants.</u>

Respondents are not unaware of the frequency with which motions to dismiss are granted. As a result, the claims that respondents file serial, baseless dispositive motions simply to delay cases or impose costs on claimants ring particularly hollow. In my experience, respondents are acutely aware of the costs of motion practice, whether allocating scarce internal resources or paying my hourly fees. But most claimants' lawyers work on a contingency basis and accordingly most claimants, unlike most respondents, face no direct cost from additional early briefing. The purported concerns about efficiency have nothing to do with the public investors, in most cases. The concern for the effort necessary to respond to a motion to dismiss is a concern only of the advocates, who want the opportunity to subject respondents to a potential hearing with as little effort as possible. As counsel for claimants well know, curtailing motions to dismiss would not preserve resources, it would only maximize uncertainty.

Dispositive motions need not cause delay. Panels currently endeavor to schedule hearings within nine months. Generally, the compounded schedules of three arbitrators, two sets of counsel, and experts control the scheduling of hearings. I have not participated in a case where the hearing schedule has been extended to resolve a motion to dismiss, nor need they be. The briefing and hearing for a motion to dismiss can run parallel to the discovery process, as they have in every case in which I have filed a dispositive motion. In cases where multiple motions are filed, including motions close to the hearing date, the panel should consider those facts in ruling on the motion.

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Preventing a motion to dismiss spares no resources. Ultimately, if there are valid legal defenses, they will be presented to the Panel before the hearing is resolved. Whether this occurs in the respondent's answer, a motion to dismiss, a hearing brief, or closing arguments, both sides need to research and present the law and the legal issues must be examined by the panel. The only issue is the timing of that presentation. Deferring briefings and hearings until trial does not preserve any resources, it only ensures that more resources will be expended by both sides before legal issues are resolved. Such a process is inherently wasteful and does not advance the interests of investors or member firms.

4. <u>The Proposed Rules Improperly Limit Substantive Rights to Resolve Procedural Concerns.</u>

As set forth above, I believe that the claims that respondents routinely file frivolous motions to dismiss are exaggerated and the assumption that such motion practice imposes more costs on claimants than respondents is false. But whether it is the motions to dismiss or the claims themselves that are unfounded, the solution reflected in the proposed rules does not address the perceived problem. The concerns raised are procedural in nature. The only complaints from any corner are that motions to dismiss cause delay or inhibit efficiency; no one claims that panels wrongly decide those motions. Accordingly, the resolution should address – at least in the first instance – the procedural concerns raised by FINRA and lawyers for public investors. Before stripping respondents of substantive legal rights, the first step, if any, ought to be applying the procedural requirements set forth in the Proposed Rules before any limitation on the grounds for which dismissal can be granted.

5. <u>Limiting Motions to Dismiss is Fundamentally Unfair to Member Firms.</u>

FINRA suggests that the amendments are appropriate because it believes that disputes should be resolved by hearings. That position is inappropriate, as member firms should not be subject to full hearings for claims that are barred as a matter of law. Arbitration hearings are undoubtedly supposed to be more efficient than trials, and they are. But nothing in the goal of efficiency compels results that are not rooted in the law. Claimants should not be allowed to bring claims that have no basis in a substantive legal right. Panels are more than capable of resolving such issues and, only when a claim should clearly be dismissed, does it ever happen. There is no justification for requiring a respondent to fully litigate a claim that is facially deficient or legally barred.

And the widespread support among the claimants' bar for the Proposed Rules has nothing to do with a desire for more hearings on the merits. If a claim is legally flawed, and if a panel is inclined to dismiss a claim based on that legal flaw, a public investor would like the hearing on the legal issue to be heard as quickly possible. No investor would want to spend the time to participate in several days of hearings and potentially pay an expert in addition to hearing fees if

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the panel believes a legal issue bars the investor's claims regardless of the facts adduced at a hearing. The championing of the Proposed Rules by lawyers for public investors is rooted not in a desire for more (futile) hearings, but in a desire for the most procedural uncertainty for the longest amount of time. The majority of filed arbitrations are resolved without a hearing. Claimants' lawyers know that full hearings are resource-intensive for member firms, whether handled by inside or outside counsel, and that the threat of an expensive hearing is the best leverage for a favorable resolution to a meritless claim. Claimants' lawyers would like nothing better than to avoid the burden of responding to solid motions to dismiss and proceeding directly to a conversation about the cost to respondents of participating in a full trial. Precluding motions to dismiss, far from increasing the fairness of the process, will only serve to increase filings of claims that would otherwise be subject to appropriate motions to dismiss and potentially terminated prior to a hearing.

Undoubtedly, these are cases where public investors are legitimately injured and FINRA members responsible for those harms should be efficiently held accountable. But the reality is that years of strong markets have made it even harder for claimants' lawyers to claim that their clients have suffered a legally cognizable harm. Rather than filing fewer cases, they hope to perpetuate their business model by stripping away procedural checks and balances and increasing the number of cases in which they can potentially subject members firms to expensive litigation. FINRA and the SEC should not respond to the increase in baseless claims by limiting the mechanism by which those claims can be most fairly and efficiently resolved. The proposed rule should not be adopted.

Sincerely,

Christian T. Kemnitz

CTK:nlv