September 10, 2010

BY EMAIL TO: **rule-comments@sec.gov**

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549

Re: File No. SR-FINRA-2010-035
Proposed amendments to the Discovery Guide
and rules 12506 and 12508 of the Code

Dear Ms. Murphy:

The Arbitration Committee of the Securities Industry and Financial Markets Association (SIFMA)[1] appreciates the opportunity to comment on the SEC Release regarding FINRA's proposed amendments to the Discovery Guide (the Release).[2] We understand that FINRA's proposal is intended to expand the guidance FINRA gives to parties and arbitrators on the discovery process and to streamline the Document Production Lists (Lists) from fourteen down to two. SIFMA generally supports expanded guidance and streamlining the discovery process.

Our underlying concern, however, is that streamlining the Lists will not result in streamlined discovery but rather, in increasingly voluminous, burdensome, and expensive discovery and motion practice in every case. For example, as discussed more fully below, the production of full sets of commission runs in every case involving "solicited

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

[2] Notice of Filing of Proposed Rule Change Amendments to the Discovery Guide (Aug 3, 2010), Release No. 34-62584; File No. SR-FINRA-2010-035, available at http://edocket.access.gpo.gov/2010/pdf/2010-18999.pdf.

trading activity" (the lion's share of cases) serves no useful purpose. While a more limited subset of such information may be relevant in cases containing allegations of churning, unauthorized trading or unauthorized discretionary trading, this information is not relevant in suitability and misrepresentation cases. Simply put, that a broker sold the same securities to unrelated clients has no bearing whatsoever on whether those securities were suitable for the claimant. Making such information "presumptively discoverable" in all cases defeats one of the fundamental purposes of arbitration, namely, to achieve justice in a manner that is less costly, burdensome and time-consuming than a court proceeding, and will lead to unnecessary motion practice in those cases where such information is presumptively irrelevant.

In furtherance of our collective goal of improving the discovery process, we offer the following additional comments and recommendations:

I. General Comments

1. Distinguish "customers" from "claimants." The text of the Release draws a clear distinction between "customers who are parties to an arbitration [known as "claimants"] and other customers of a brokerage firm." The text of the actual Lists, however, uses only the term "customer" – which creates unnecessary ambiguity, lends itself to differing interpretations as to what documents are called for, and raises serious concerns that firms would be asked to produce non-party customers' personal and private information in contravention of their privacy obligations, discussed in greater detail below. Accordingly, the text of the Lists should likewise distinguish between customers and claimants. In doing so, and in order to avoid a construction that renders the Lists over-broad and unduly burdensome, it seems clear that virtually all of the references in the Lists should be to the "claimant(s)" – and not to the "customer(s)." Specifically, all references in the Lists that currently read "customer(s)" should be changed to read "claimant(s)," provided that the term "customer(s)" may be appropriately retained in the following two items: List 1, Item 10 (the final three references to customer), and List 1, Item 20(b).

2. Include a reference to clearing firms in the introduction. The fifth paragraph of the introduction to the new Discovery Guide reads, in part, "not all firms have the same business operations model and certain items on the Lists may not be relevant in a particular case when the firm's business model (e.g. full service firm, discount broker, or online broker) is taken into consideration." The parenthetical should appropriately add "clearing firm" as an example of a firm with a clearly distinguishable business model that should be taken into account in determining which items on the Lists are relevant.

3. Define a reasonable time period or scope for all List items. Some, but not all, of the items on the draft Lists have a defined time period. Items that are undefined and unlimited in terms of time scope are inherently over-broad and unduly burdensome, and should be amended to include a defined time period. In particular, List

1, Items 2 (relating to advertising material), 3 (investment strategies) and 21 (broker/firm agreements) should be limited to the time period during the transactions at issue.

4. The Lists should not limit the scope of subpoenas to non-parties. The Release does not distinguish between documents produced by a claimant and documents produced by a non-party in response to a subpoena – but it should. Documents obtained from a non-party – a prior or contemporaneous brokerage firm, for instance – do not involve any burden on the claimant. The clearest example is monthly statements, where the proposed List would require a claimant to produce only three years worth of statements, in part because of the burden of requiring the claimant to find and copy older records. That consideration does not come into play when those documents are requested from another member firm via subpoena; six or more years of statements can be produced with no additional effort by the claimant.

The fourth paragraph of the introduction to the new Discovery Guide, however, states that "the arbitrators may use the Lists as guidance for discovery issues involving non-parties." We believe this statement should be removed or, in the alternative, that FINRA should clarify that the Discovery Guide should not be used as a sword to limit the scope of documents that respondent firms can obtain by subpoena from third parties. Without this change, many arbitrators presiding over the issuance of a subpoena will take the path of least resistance and reject any document request in a proposed subpoena that is not in strict conformity with the List requests. This will result in denying respondent firms access to highly relevant, if not critical, evidence.

Using the example provided above, the arbitrator will deny a request in a proposed subpoena for account statements pre-dating the three-year period called for under the Guide. Similarly, the omission of account documentation from List 2, Item 4 will lead to arbitrators precluding respondent firms from obtaining a claimant's account records from a non-party brokerage firm, which records memorialize such information as the claimant's investment objective, risk tolerance and financial wherewithal – all vital pieces of information in a suitability case. These are but two examples of the wide variety of potentially relevant documents in the possession of non-member firms that are not specified in the Guide and, therefore, would be rendered unavailable to respondent firms. For all of these reasons, it is illogical to apply the Discovery Guide, crafted with the burden of production in mind, to third party discovery. To avoid attempts by claimants or their counsel to use the Guide as a sword and to unfairly restrict discovery from third parties, FINRA should make clear that the Guide is not intended to limit the scope of discovery that may be obtained from third parties.

5. Maintain the privacy of non-party customer information. Several of the List items appropriately and explicitly recognize that certain non-party customer information may be redacted from document productions. *See, e.g.*, List 1, Items 10 (RE-3s, et al.) and List 1, Item 20(b) (commission runs). These references to third party privacy rights, however, are by no means uniform or comprehensive throughout and among the List items. Regardless, we are mindful of our commitment, and indeed legal obligation, to maintain the privacy of non-party customers' "personally identifiable

financial information," including the fact that a named individual is a customer of a firm. As the SEC explained, the customer relationship is "personally identifiable," within the meaning of Reg. S-P, "because it identifies the individual as a customer of the institution" and it is "financial" because it reveals a financial relationship with the institution and the receipt of financial products or services from the institution."[3]

II. List One

List 1, Item 2 (advertising materials). The term "advertising material" is undefined and will be argued to encompass a wide variety of communications. As such, compliance would be unreasonably burdensome and its fruits scarcely relevant. While it may be fairly straightforward for a broker or his branch office to identify what the broker at issue or those under his control sent to the claimant, it would be much more time consuming, prone to inaccuracy, and generally unhelpful, to produce all advertising materials generated from the home office – and every other branch office – and sent to any customer of the firm. Many firms simply don't maintain advertising records in a centralized manner or otherwise in a manner conducive to identification and production in any given arbitration. Moreover, what would be the general relevance? Does the fact that a claimant complains about the suitability of various investments in his Roth IRA make the firm's promotional materials about Roth IRAs relevant in the case? Certainly not. Accordingly, "advertising material" should not be deemed presumptively discoverable unless, at a minimum, the claimant alleges that she was misled by or relied to her detriment on certain of the firm's advertising materials. In addition, the scope of this item should be reasonably and appropriately limited to advertising materials that were actually delivered to the claimant.

List 1, Item 9 (communications with compliance). This item calls for the production of "communications between the associated persons … and members of the firm's compliance department relating to," inter alia, "the securities/products at issue." The production should be limited to the accounts, transactions and customers in issue (excluding, of course, documents subject to an established privilege, many of which may fall within this item). Otherwise a claim that an account was unsuitably weighted toward equities would require any communication about any stock, an unduly burdensome and irrelevant exercise.

List 1, Items 7, 13(a) & 13(b) (distinguish customers from claimants, exception reports for non-party accounts). Per our general comment (discussed above) to distinguish between customers and claimants, it appears that the term "customers'" is intended to mean "claimants'" under items 7 and 13(a). If so, these items are generally unobjectionable. If not, then these items are grossly overbroad, unduly burdensome, and unlikely to lead to relevant evidence.

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[3] *See* Regulation S-P, Privacy of Consumer Financial Information, 17 C.F.R. 248 (Nov. 13, 2000), available at http://www.sec.gov/rules/final/34-42974.htm#P208_76535.

Under item 13(b), on the other hand, it appears that the term "customers" is in fact intended to mean "customers." As a result, item 13(b) is grossly overbroad, unduly burdensome, and unlikely to lead to relevant evidence. The apparent limitation – production limited to those "related to the allegations in the statement of claim" – is illusory. It is impossible to know without significant additional investigation whether other accounts on an exception report are so "related." Moreover, the discovery would be of scant probative value. The firm's supervision of the claimant's account should stand or fall on the unique circumstances of the claimant and the nature of management's conduct with respect to the claimant. Thus, the adequacy of management's supervision can be evaluated based on the quality of management's response to exception reports, if any, generated for the claimant's account, and management's other conduct with respect to the account that is not captured in an exception report.

On the other hand, if the production of exception reports for unrelated third parties were permitted, respondent firms would be in an impossible position – they would either have to let the panel draw an unfair and adverse inference from the exception reports, or they would have to defend their supervision of multiple non-party accounts. The latter would involve a "mini trial" to prove, for each non-party customer, that their account activity was appropriately supervised given each customer's investment objectives, risk tolerance, net worth and investment experience. This would not only be a distracting sideshow, it would require significant litigation over a non-party's personal and private information, in derogation of the firm's privacy obligations, as discussed above.

List 1, Item 18 (third-party documents). This item requires production of "[a]ll documents related to the case at issue that respondent received by subpoena under Rule 12515 or by document request directed to third parties at any time during the case." This request is overly broad and unduly burdensome to the extent it calls for documents that may have no relevance to or bearing on the case (e.g., documents produced by a third-party in connection with an informal interview, documents produced pursuant to a FOIA request, etc.). Such documents may also be protected from disclosure based on the attorney work product doctrine, limited solely to the obligation to produce the documents during the pre-hearing exchange if they are intended to be used at the hearing. In fairness, the parties should be entitled to receive only documents received by counterparties pursuant to a subpoena and documents that counterparties intend to use at the hearing (produced in the 20-day exchange). Accordingly, we recommend that the second clause of Item 18 be stricken. This comment applies with equal force to the parallel customer List provision (List 2, Item 18); see discussion *infra*.

List 1, Item 19 (broker compensation). This item requires production of all gross and net compensation per associated person and whether each trade entered by that associated person was solicited or unsolicited. First and foremost, this item would create a significant redacting project in each case in order for the firm to satisfy its privacy obligations to its non-party customers (see privacy discussion *supra*). Second, as drafted, this item would be generally unduly burdensome, costly, and time consuming to produce.

Thus, we recommend that this item be strictly limited to cases in which there are churning or frequent trading allegations.

List 1, Item 20 (claims re: solicited trading). This item requires (for all claims related to solicited trading activity) production of all compensation, including monthly commission runs, for the associated person. This request is generally overbroad, unduly burdensome, and unlikely to lead to relevant evidence.

First, virtually every case involves "solicited" trading activity claims. It is unclear why this item should be presumptively discoverable in every case. This item should require at least some minimal showing of relevance, or otherwise be limited to cases involving churning, unauthorized trading or unauthorized discretion. In other words, there are rare cases in which the timing of recommendations to other clients may be highly relevant. With respect to a particular stock, there may be a dispute as to whether the stock was the customer's idea or the broker's. A commission run for transactions in that stock by the broker's other customers may well be relevant; the presence or absence of such purchases at the time of the claimant's purchase may be decisive. The point is that these cases are a tiny minority of the cases brought, and their existence does not justify the extraordinary burden of production in every case.

Second, this item's carte blanche approach to the discoverability of cross-holding information merits further reasonable limitations. At a minimum, in the limited sub-set of cases in which this information may be relevant, the records to be produced should be appropriately limited to trades occurring on the same date, or within a reasonable time (e.g., three days), and in the same securities, as those alleged in the Statement of Claim.

Third, this item calls for the production of a few items that are not generally maintained or readily available in the form requested among a firm's usual business records, including (i) whether a trade was solicited or unsolicited, and (ii) the type of account (IRA, 401(k), etc.). We recommend either removing these clauses, or including additional guidance (supplementing the general guidance) that respondents are not required to create documents to respond to these items.

Fourth, if not modified, the burden imposed by this item is gargantuan. This item, as presently formulated, purports to require production of *every* trade for *every* customer account for the entire life of the claimant's accounts (plus six months.) Multiply the firms' current obligation (claimant only) by the number of customers serviced by the associated person. Thus, for an associated person with 100 customers, the burden increases 100 fold.

Fifth, if not modified, the information generated by this exercise is of very limited relevance or probative value. Different clients have different investment objectives, risk tolerance, levels of experience, financial resources, and portfolios – none of which differences are apparent from the commission run. As with item 13(b), there would be a "mini trial" for each non-party customer trade that a claimant's lawyer wanted to query. There would be no way to prepare for a hearing after such a production – potentially

thousands of trades for hundreds of customers might be in issue. Firms would be unaware of a claimant's attempt to question a non-party trade until the hearing.

Sixth, there is no justification for requiring the production of private information regarding the associated person's trading in every case. This is an invasion of the associated person's privacy. It is also completely irrelevant. Unlike the customer, who puts his or her financial life in issue by bringing the claim, the associated person has not put his or her financial life on trial. The associated person has different investment objectives and experience, different risk tolerance, different financial resources and different investment sophistication.

List 1, Item 21 (broker / firm agreements). By expanding the language of the existing request, which reads "[d]ocuments *sufficient to describe or set forth* the basis upon with the Associated Person(s) was compensation during the years in which the transaction(s) or occurrence(s) in question occurred, including . . . " (emphasis supplied), this item greatly expands the universe of potentially responsive documents to include irrelevant agreements covering benefit plans, loans, etc. To identify, locate and produce such documents is burdensome and unnecessary. Accordingly, the language from the existing request calling for "documents sufficient to describe" how the associated person was compensated should be retained. In addition, this item is undefined and unlimited in terms of time scope, rendering the request over-broad and unduly burdensome. It should be appropriately limited to the time period during the transactions at issue. Otherwise years of compensation information would be required for long-term associated persons with short-term claimant customers.

III. List Two

General comment – affiliated accounts. Increasingly, customers maintain both bank and brokerage relationships with their full service firms. In many cases, the affiliate may possess bank statements showing cash/CD holdings, documents relating to investment accounts managed by the bank, and loan documents reflecting the customer's financial situation, net worth, income, etc. Accordingly, where customers are required to produce presumptively discoverable documents received from the respondent firm, they should likewise be required to produce such documents for their other accounts at the firm's affiliates.

General comment – persons acting on behalf of the claimant. As is done in List 2, Item 8(a), the claimant should be required to produce documents and records generated not only by the claimant, but also by "any person purporting to act on behalf of the [claimant]."

List 2, Item 4 (third-party account statements). The proposed Discovery Guide imposes far greater burdens on firms than on customers. Nowhere is this disparate treatment more apparent than in Item 4, which limits claimant's production of other brokerage accounts to account statements for a brief three year time period. While firms are asked to produce "all advertising material" sent to any customer of the firm (List 1,

Item 2), the claimant is not required to produce correspondence he received from another brokerage firm. While firms are asked to produce discipline against any associated person of the firm, unlimited in time (List 1, Item 15), claimants may withhold monthly statements older than thirty-six months. While firms are asked to produce solicited/unsolicited information for thousands of trades for hundreds of non-party customers (List 1, Item 20(a)), claimants are not obliged to make that information available in discovery. Burden is not the issue – if the customer does not have the documents, they can be obtained via authorization or subpoena from the other member firm. There is simply no reason to deprive the panel of vital information in filling out the picture of the claimant's investment experience and objectives, risk tolerance and assets.

Suitability information. Information regarding the claimant's investment objectives, risk tolerance, investment experience, and financial condition which are on file at other securities firms are highly relevant to the claims brought by the claimant against a respondent firm or associated person. The Lists should be revised to include "All account statements, new account forms, correspondence, and any other documents and information received from or maintained by each securities firm where the customers have maintained an account for the three years prior to . . . "

Claimants and firms often disagree about the accuracy of the firm's suitability profile of the claimant. Every firm records customer suitability information – net worth, investment objectives and experience, risk tolerance, etc. Suitability information recorded by another member firm is undoubtedly useful to an Arbitration Panel in its deliberations. Parties and arbitrators should not be deprived of this critical information, particularly when it is *required to be kept* by all member firms and is *easily retrievable* by the third party firms, if not in the possession of the claimant. Little if any burden is placed on the claimant, since compliance with the item can be accomplished via the use of a third party authorization if the documents are not in the files of the claimant.

Account statements. The proposed Guide inappropriately limits claimant's obligation to produce account statements to the period up to three years before the transactions at issue. The three-year period is unreasonably short (e.g., the credit crisis started three years ago) and arbitrary, and would eliminate the production of highly relevant evidence. Claimants routinely allege a lack of investment experience and understanding for the investments or trading strategies they claim are unsuitable. Evidence that claimants owned or traded the same or similar securities at other firms may be relevant to refute such allegations. The probative value of such evidence is not diminished by the fact that such investments or trading occurred more than three years before the transactions at issue. Moreover, the Claimant would not suffer an undue burden by having to collect these documents; they can be obtained by subpoena or authorization.

Account correspondence. Customers often receive correspondence from other member firms, including specific correspondence about the activity in the account. Respondent firms should receive voluntarily from the claimant their correspondence with

their predecessor or contemporaneous firms, including letters regarding the activity in the account.

Account/commission runs. The proposed Guide concedes the relevance of whether a claimant's trade was solicited or not. List 1, Item 20(a). But that concession does not apply to accounts that claimant maintained at other firms. Respondent firms deserve the right to discover whether a claimant's trading at another firm was unsolicited, if necessary by authorization or subpoena of that firm. Such discovery might also obviate the need for testimony from that other member firm.

List 2, Item 7 (notes). As discussed above, claimants should also be required to produce such notes relating to accounts at the respondent firm's affiliates or at third party firms. Again, such documents would be directly relevant to the claimant's suitability profile.

List 2, Item 11 (other litigation). This item should make clear the need to disclose related class actions to ensure claimant is not pursuing a claim arising from the same facts in a different forum. *See* FINRA Code of Arbitration Procedure 12204. Also in addition to "securities matters," claimants should disclose whether they have pursued other actions against service providers, for instance, professional malpractice actions.

List 2, Item 12 (business entity control / ownership). The use of the term "trustee" is unduly restrictive. The second sentence should be stricken in its entirety and replaced as follows, "Provide document showing any accounts over which the claimants have trading authority."

List 2, Item 18 (third-party documents). This item requires production of "[a]ll documents related to the case at issue that the [claimant] received by subpoena under Rule 12515 or by document request directed to third parties at any time during the case." As discussed above under List 1, Item 18, this request is overly broad and unduly burdensome to the extent it calls for documents that may have no relevance to or bearing on the case (e.g., documents produced by a third-party in connection with an informal interview; documents produced pursuant to a FOIA request, etc.). In fairness, the parties should be entitled to receive only documents received by counterparties pursuant to a subpoena and documents that counterparties intend to use at the hearing (produced in the 20-day exchange). Accordingly, we recommend that the second clause of Item 18 be stricken.

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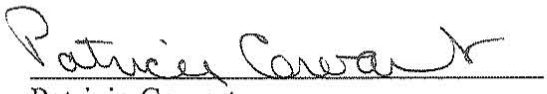
Thank you for giving SIFMA's Arbitration Committee the opportunity to comment on the proposed amendments to the Discovery Guide. If you have any questions regarding this comment, please contact the Committee's staff advisor, Kevin Carroll, at 202.962.7382 (kcarroll@sifma.org).

Sincerely,



Patricia Cowart
Chair, SIFMA Arbitration Committee

cc: Linda D. Fienberg, President, FINRA Dispute Resolution
George H. Friedman, Executive Vice President, FINRA Dispute Resolution
Robert W. Cook, Director, Division of Trading and Markets, SEC