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April 10, 2008

Ms. Nancy Morris  
Secretary  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, DC 20549

**Re: File No. SR-FINRA-2007-021**

Dear Ms. Morris:

I welcome this opportunity to comment upon the proposed Rule Change referenced above addressing the use of Motions to Dismiss under FINRA Arbitration Rules. Because the proposed rule stands to eliminate one form of abusive motion practice by unnecessarily replacing it with another form of inappropriate motion practice, which is likely to be as abusive as the current practice, if not more so, I respectfully urge that the rule not be adopted in its present form.

## **I. BACKGROUND & EXPERIENCE**

I am an attorney with close to 25 years of experience in civil litigation. I have been representing investors in court and arbitration cases for over 15 years, and my representation of investors is a major focus of my practice. I have lectured on the topic of SRO arbitration on numerous occasions at securities seminars sponsored by industry regulators and bar associations. I have considerable practical experience with Motions to Dismiss, both in court and in arbitration. I have closely followed the controversy and debate over the years attaching to the use of Motions to Dismiss in FINRA arbitration, and I am very well acquainted with the wide range of viewpoints on this issue, as represented within the comment letters filed to date on this proposed rule change. I specifically contacted a majority of the authors of the comment letters submitted on behalf of the interests of FINRA member firms to discuss with the authors their expressed beliefs that Motions to Dismiss should be permitted under the FINRA Arbitration Rules.

## **II. MOTIONS TO DISMISS AND MOTIONS FOR DIRECTED VERDICT**

The proposed rule would be effective in curtailing an existing abusive practice identified by FINRA, which is the excessive and inappropriate filing of pre-hearing Motions to Dismiss by

FINRA member firms. Pre-hearing Motions to Dismiss, raising hyper-technical questions of law, have no place in the FINRA arbitration system. FINRA does not require its arbitrators to be attorneys nor have any formal training in law. FINRA does not provide training to its arbitrators consistent with their being asked to rule upon formal court-like Motions involving the adjudication of complex issues of law.

While FINRA's proposed rule properly identifies and seeks to eliminate an abusive practice within its arbitration system, the proposed rule at the same time inexplicably creates a new and equally inappropriate motion practice in its place. The proposed rule approves the use of Motions to Dismiss filed at the conclusion of the customer's case, which in court are more commonly known as "Motions for Directed Verdict." (The authors of the industry comment letters with whom I spoke agreed with this interpretation of the proposed rule.) Inasmuch as pre-hearing Motions to Dismiss are inappropriate for FINRA arbitration and subject to being abused by FINRA members, these same observations and conclusions are even more applicable to Motions for Directed Verdict.

The legal grounds that may support a pre-hearing Motion to Dismiss are relatively limited, because they arise solely from the customer's statement of claim. Yet, as FINRA has acknowledged, the use of these Motions has grown to abusive levels. The greatest increase in the use of pre-hearing Motions to Dismiss occurred *after* FINRA adopted rules governing motion practice, though Motions to Dismiss were not specifically approved, sanctioned, nor mentioned in the current rules. There can be little doubt that if FINRA were to adopt a rule specifically approving the use of Motions for Directed Verdict, the use and abuse of this form of motion practice will equal or surpass the existing abuse of pre-hearing Motions to Dismiss.

While the grounds supporting pre-hearing Motions to Dismiss are relatively limited, as being addressed to the customer's statement of claim, the universe of technical legal points that may be raised in a Motion for Directed Verdict is, for all practical purposes, limitless. Motions for Directed Verdict are designed to compare the adequacy of legal proof, determined by compliance with formal rules of evidence, with the elements that must be proven in connection with any formal legal cause of action. In its commentary, FINRA acknowledges that this new Motion that is to be formally sanctioned under the proposed rule can be used to raise any legal grounds for dismissing a customer's claim.

FINRA's proposal to formalize Motions for Directed Verdict within its Arbitration Rules is completely antithetical to its arbitration system. FINRA arbitration administrators defend FINRA arbitration by touting the advantage for customers that their claims need not satisfy the legal formalities of a court of law. This supposed feature of FINRA arbitration is held out as one of its principal virtues as compared to court. The proposed rule, in formalizing Motions for Directed Verdict, is a road map for eliminating this espoused virtue of the FINRA system. The SEC should consider that FINRA members have abused pre-hearing Motions to Dismiss under circumstances where such Motions were never formally approved by the FINRA arbitration rules. The current rule proposal does formally approve Motions for Directed Verdict. If the industry abused Motions to Dismiss without formal FINRA approval of that

practice, can there be any doubt that the industry will in the same manner abuse Motions for Directed Verdict if such a motion practice were to be formally approved?

### III. FINRA ARBITRATION IS NOT A COURT OF LAW

The real danger of the proposed rule is not that customers will now encounter technical court-like motions that did not previously exist. The proposed rule acknowledges that this problem already exists. Under the proposed rule, however, the arbitrators will be instructed by FINRA for the first time that it is their express duty to sit as a court of law and give due consideration to technical, court-like motions, which require that they adjudicate complex issues of law, which are very likely to be beyond their competence and training to decide. I have on more than one occasion represented investors in FINRA arbitration hearings where there was not a single attorney on the three-member panel. On two such occasions, my case represented the chairperson's very first case – one a retired physician and the other a retired English teacher. Even where there is an attorney on the panel, these attorneys may nonetheless have no education or experience in securities law or litigation practice, both of which take years to learn and master.

The FINRA arbitration system is defensible only insofar as the securities industry is a highly regulated industry and is subject to very specific uniform rules and regulations, which govern all investor accounts and transactions. These industry rules and regulations are simple enough for untrained, lay arbitrators to understand and apply. In an informal arbitration system where customers can present their claims to an arbitration panel that includes a member of the industry, by reference to rules and regulations that universally apply to all members of the industry, the absence of formal legal training and experience among the arbitrators alone need not hinder the ability of investors to obtain an equitable resolution of their claims. In this respect, however, the industry still reaps enormous benefits from compelling investors to litigate claims within an informal equity forum, because in court investors have available to them damages that are fixed by law, which cannot be reduced by the equitable defenses raised by the industry in FINRA arbitration proceedings.

Presently, the industry's abusive motion practice, while an annoyance, rarely impacts the outcome of investor cases, because the industry's motions are for the most part ignored by the arbitrators. The arbitrators seem to generally appreciate that the FINRA arbitration system is intended to be an informal process, where they are not bound to either understand or follow formal legal procedures as exist in court. It is also my experience, however, that arbitrators attempt to follow, as best they can, the limited procedural rules that do exist, as well as the training and instruction provided to them by FINRA. *If for the first time, FINRA now instructs its arbitrators that they must, to the best of their ability, decide formal courtroom motions, then the lack of formal legal training and experience amongst the arbitrators may very well cause serious damage to investor claims.*

As an experienced litigator representing investors, I have no need of the FINRA arbitration system in seeking justice for my clients. The rigors and legal requirements of a court of law are not a threat to my clients. When FINRA touts that customers need not abide by legal

formalities in its arbitration system this represents no advantage to my clients, because the law as it exists is more than sufficient to protect investors. The industry alone favors mandatory FINRA arbitration for reasons of its own self-interest. Mandatory FINRA arbitration is opposed by every pro-consumer group that has addressed this issue, which is why the "Arbitration Fairness Act" pending before Congress seeks to abolish it. If an investor is to be unfairly restricted to the FINRA arbitration system, without choice to go to court, then at the very least that system should operate as intended within the practical limits of the training, experience and competence of FINRA arbitrators.

#### **IV. THE INDUSTRY'S ERRONEOUS CASE FOR "MOTIONS TO DISMISS."**

##### **A. Eliminating Substantive Motions to Dismiss is "Unfair."**

A review of the comment letters filed on behalf of the interests of the industry regarding Motions to Dismiss all express a common theme: it is unfair to deprive industry members of motion practice available in court proceedings to eliminate "frivolous" or legally unsustainable claims. First, the proposed rule does not eliminate all pre-hearing Motions to Dismiss. The proposed Rule properly eliminates only those Motions that require technical and complex interpretation and application of law, which on their face are inappropriate for an informal arbitration system, as explained above.

Second, if there were any truth or validity to the argument that FINRA arbitration is unfair to industry members because it deprives them of remedies available in court to avoid frivolous customer claims, then there is a very simple remedy for that malady. The industry could make participation in FINRA arbitration voluntary and elective, instead of imposing it upon its customers without any choice to go to court. If participation in FINRA arbitration were voluntary, industry firms could elect on a case-by-case basis to agree to arbitrate or proceed in court where they wish to retain the right to seek court dismissal of frivolous claims. Whatever disadvantage it may be to the industry to forgo formal court procedures, it is not so great as to overcome the overall advantage the industry enjoys by imposing a system an arbitration system upon its customers that is operated by its own trade association.

In short, the industry could avoid the unfairness that it claims would result if formal Motions to Dismiss are barred in FINRA arbitration by making the choice to proceed in FINRA arbitration voluntary for both parties. This cure for the industry's complaint regarding fairness is supported by the North American Association of Securities Administrators ("NAASA"), the Public Investors Arbitration Bar Association ("PIABA"), and it is the remedy being pursued in legislation pending before Congress, the "Arbitration Fairness Act" sponsored by Senator Russ Feingold. Insofar as the absence of Motions to Dismiss is "unfair" to the securities industry, the industry need only permit each side to choose arbitration on a voluntary basis, as contemplated by Senator Feingold's Bill to reform consumer arbitration. Yet the industry steadfastly resists the Arbitration Fairness Act and all other efforts to make participation in FINRA arbitration voluntary.

## B. The Industry's Motions to Dismiss Would be Granted in Court.

Most of the comment letters filed on behalf of the industry assert that the Motions to Dismiss that the firms wish to maintain and pursue only concern cases where such motions would be granted by a court of law. This argument is demonstrably false. There is a very simple means by which the SEC or FINRA can test the truth and validity of the industry's claim in this respect. If this claim were true, then the industry and its member firms should have no objection under such circumstances to provide the customer with the option of shifting the case to court. Providing such an option to the customer where a Motion to Dismiss is pursued would ensure that the firm is, in fact, correct that the case is legally defective under standards that would be applied by a court of law, which has the training, experience and the resources to make such legal judgments. If the SEC puts this question to the industry associations and its firms, as I have already done on numerous occasions, it will find that they will oppose such a condition. It is evident that when challenged on this point, the industry and its firms have no confidence that their Motions to Dismiss would be accepted by a court of law.

For example, in each and every instance where I have received a Motion to Dismiss in an NASD or FINRA case, and I have made the offer to opposing counsel to have the case voluntarily dismissed by the arbitrators under NASD/FINRA Rule 10305, without prejudice for referral to court, so that a court would decide the motion to dismiss, the industry members have declined the offer. This offer is always prefaced by inquiring of counsel whether they have a good faith belief that a court would grant their Motion to Dismiss, to which they universally respond: "yes." This claim of having a good faith belief in the Motion is belied, however, by their unwillingness to put that belief to the test by having the matter decided in court.

To provide an even more specific case example in a case against a large and prominent Wall Street brokerage firm, the firm filed a motion in arbitration raising multiple legal grounds to have the case dismissed on the merits. Opposing counsel had unwittingly included in his Motion, however, that the case was ineligible for arbitration under NASD/FINRA 10304. Rule 10304 had recently been amended to provide that where a case is dismissed for reasons of this eligibility rule, it is without prejudice for the customer to re-file the case in court. In response to the firm's Motion to Dismiss, I filed my own Motion to Dismiss under NASD/FINRA Rule 10305, which also provides for a dismissal without prejudice to re-file the case in court. Moreover, I pointed out to the panel that where both parties request dismissal, the panel has no discretion and must dismiss the case under Rule 10305 without prejudice, which it did. When I then re-filed this case in court, which according to the firm's original Motion to Dismiss should be dismissed outright as lacking any legal merit, not only did the firm not reassert its Motion to Dismiss in court, it agreed to settle the case for \$250,000, where my elderly widow client had lost less than \$200,000 in her account. Such is a testament to the lack of validity to the claim that Motions to Dismiss in FINRA arbitration represent *bona fide* efforts to terminate frivolous or legally unsustainable cases. This example also explains why the industry desperately seeks to prevent investors from gaining access to court. My client would never have obtained a recovery of \$250,000 in FINRA arbitration system. Such a recovery was

only possible because the courts and the law provide far superior protections to investors than exist in the FINRA arbitration.

### CONCLUSION

The only reason that the proposed rule is supported by some pro-investor groups and attorneys is (1) they wish to eliminate the existing abusive practice involving pre-hearing Motions to Dismiss and (2) they recognize that the securities industry's very strong influence over the FINRA rule-making process makes compromise necessary. As such, they view the trade-off of eliminating the abusive pre-hearing Motion to Dismiss practice (a known evil) in exchange for allowing the industry to obtain formal approval of a mid-hearing Motion for Directed Verdict practice (an unknown future problem) as the best they can achieve under the circumstances.

It is not the function of the SEC, however, to eliminate a known inappropriate and abusive practice, which is not suitable for FINRA arbitration, only upon condition that the securities industry be provided with a similarly inappropriate practice in its place. For the reasons set forth above, court-like motion practice is inappropriate for FINRA arbitration, whether it takes place pre-hearing or mid-hearing. Such a practice is all the more dangerous when it has a formal stamp of approval within the FINRA Arbitration Rules. For these reasons, I respectfully urge that the proposed rule not be adopted in its present form.

Very truly yours,



Thomas P. Willcutts

cc: Hon. Russell D. Feingold,  
United States Senate

Ralph A. Lambiase, Director  
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PIABA