

## Arbitration

### Revised Discovery Guide and Document Production Lists for Customer Arbitration Proceedings

Effective Date: May 16, 2011

#### Executive Summary

FINRA is revising the Discovery Guide to expand the guidance it gives to parties and arbitrators on the discovery process and to update the Document Production Lists.<sup>1</sup> FINRA is consolidating the Document Production Lists from the 14 current Lists (two general Lists and 12 separate Lists for specific types of claims) to two lists of “presumptively discoverable” documents—one for firms/associated persons to produce and one for customers to produce. Many of the documents on the current Lists are included in the revised Discovery Guide. In addition, under the revised Guide, FINRA is requiring parties to produce additional types of documents that forum users have indicated they need to develop a case.

The amendments are effective on May 16, 2011, and will apply to all customer cases filed on or after the effective date. The amendments to Rules 12506 and 12508 are set forth in Attachment A, and the revised Discovery Guide is available on our website at [www.finra.org/arbitration/discoveryguide](http://www.finra.org/arbitration/discoveryguide).

Questions concerning this *Notice* should be directed to:

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- ▶ Margo A. Hassan, Assistant Chief Counsel, DR, at (212) 858-4481 or [margo.hassan@finra.org](mailto:margo.hassan@finra.org).

#### April 2011

##### Notice Type

- ▶ Rule Amendment

##### Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Registered Representatives
- ▶ Senior Management

##### Key Topics

- ▶ Arbitration
- ▶ Code of Arbitration Procedure
- ▶ Discovery

##### Referenced Rules & Notices

- ▶ FINRA Rule 12506
- ▶ FINRA Rule 12508
- ▶ NTM 99-90

## Background & Discussion

In 1999, FINRA adopted the Discovery Guide (Guide), which includes Document Production Lists (Lists), for use in customer arbitration proceedings.<sup>2</sup> The Guide provides direction on which documents parties should exchange without arbitrator or staff intervention, and the Lists specifically identify the documents parties should exchange before the hearing, depending on the type of dispute. After years of experience with the Guide, FINRA is revising it to expand the guidance given to parties and arbitrators on the discovery process and to update the Lists.

FINRA is replacing the current 14 Lists with just two Lists of presumptively discoverable documents: one for firms/associated persons to produce and one for customers to produce. As noted above, many of the documents on the current Lists are included in the revised Guide. In addition, the revised Guide requires parties to produce additional types of documents that users indicated they need to develop a case. Although each item on the Lists (with a few exceptions) will be presumptively discoverable in every customer case, the revised Guide encourages arbitrators to tailor the Guide to the facts and circumstances of each case. FINRA is also making conforming changes to Rules 12506 (Document Production Lists) and 12508 (Objecting to Discovery Requests; Waiver of Objection) that reflect the List consolidations.

## Discovery Guide Introduction

FINRA is revising the Guide's introduction to expand its guidance to parties and arbitrators on the discovery process generally, and to clarify how arbitrators should apply the Guide in arbitration proceedings. The revised introduction addresses, among other matters:

- ▶ **Flexibility:** The parties and arbitrators retain their flexibility in the discovery process. Arbitrators can:
  - ▶ order the production of documents not provided for by the Lists;
  - ▶ order that parties do not have to produce certain documents on the Lists; and
  - ▶ alter the production schedule.
- ▶ **Objections Based on Cost/Burden:** A party may object to producing a document on the List because of the cost or burden of production. If a party demonstrates that the cost or burden of production is disproportionate to the need for the document, the arbitrators should determine if the document is relevant or likely to lead to relevant evidence and, if so, the arbitrators should consider whether there are alternatives that can lessen the impact.

- ▶ **Requests for Additional Documents:** Arbitrators must use their judgment in considering requests for additional documents and may not deny document requests on the ground that the documents are not expressly listed in the Guide.
- ▶ **Party and Non-Party Production:** Only named parties must produce documents pursuant to the guidelines. Non-parties may be required to produce documents pursuant to a subpoena or an order of the arbitrator.
- ▶ **Consideration of Firm Business Models and Customer Claims:** Not all firms have the same business operations model and certain items on the Lists may not apply to a particular case when the firm's business model is considered. In addition, certain items on the Customer List may not apply to a particular case depending on the claims asserted.
- ▶ **Electronic Discovery:** Electronic files are "documents" within the meaning of the Guide.
- ▶ **Confidentiality:** When deciding contested requests for confidentiality orders, arbitrators should consider factors specified in the Guide including, among others, whether disclosure would constitute an unwarranted invasion of personal privacy, or whether the information contains proprietary confidential business plans and procedures or trade secrets.
- ▶ **Privilege:** Parties are not required to produce documents that are otherwise subject to an established privilege.
- ▶ **Affirmations:** If a party responds that there are no responsive documents in the party's possession, custody or control, the customer or the appropriate person in the brokerage firm who has knowledge must:
  1. state in writing that the party conducted a good faith search;
  2. describe the extent of the search; and
  3. state that, based on the search, there are no requested documents in the party's possession, custody or control.
- ▶ **No Obligation to Create Documents:** Parties are not required to create documents in response to items on the Lists.
- ▶ **Admissibility:** Production of documents in discovery does not create a presumption that the documents are admissible at the hearing.

## Documents the Firm/Associated Persons Shall Produce in All Customer Cases (List 1)

Document Production List 1 specifies the presumptively discoverable documents that firms/associated persons are required to produce in customer cases. Subject to the limited exceptions specified in certain List items, firms/associated persons are required to produce every document in every case unless the required production is narrowed either by party agreement or by order of the arbitrator. Highlights of the items follow. See the attached Guide for the full details and requirements of each item, including relevant time frames.

- Item 1:** Account record information for the customer parties, documents concerning the customer parties' risk tolerance and agreements with the customer parties.
- Item 2:** Correspondence sent to the customer parties or received by the firm/associated persons, and advertising materials sent to customers of the firm.
- Item 3:** Documents evidencing any investment or trading strategies used or recommended in the customer parties' accounts.
- Item 4:** For claims alleging unauthorized trading, all documents the firm/associated persons relied upon to establish that the customer parties authorized the transactions at issue, all documents relating to the customer parties' authorization of the transactions and all order tickets for the transactions.
- Item 5:** Materials the firm and/or associated persons prepared or used and/or provided to the customer parties relating to the transactions or products at issue, and worksheets or notes indicating that the associated persons reviewed or read such documents.
- Item 6:** Notes the firm/associated persons made relating to the customer parties and/or the customer parties' claims, accounts, transactions or products or types of products at issue.
- Item 7:** Notes or memoranda evidencing supervisory, compliance or managerial review of the customer parties' accounts or transactions, or of the associated persons assigned to the customer parties' accounts; and correspondence between the customer parties and firm/associated persons relating to the customer parties' claims, accounts, transactions or products or types of products at issue bearing indications of managerial, compliance or supervisory review.
- Item 8:** Recordings, telephone logs and notes of telephone calls or conversations about the transactions at issue that occurred between the associated persons and the customer parties, and/or between the firm and the associated persons.

- Item 9:** Writings reflecting communications between the associated persons assigned to the customer parties' accounts at issue and members of the firm's compliance department relating to the securities/products at issue and/or the customer parties' claims, accounts or transactions.
- Item 10:** Forms RE-3, U4 and U5 and Disclosure Reporting Pages for the associated persons assigned to the customer parties' accounts at issue, customer complaints identified in the forms, and customer complaints filed against the associated persons.
- Item 11:** Sections of the firm's manuals relating to the claims alleged, including separate or supplemental manuals governing the duties and responsibilities of the associated persons and supervisors, bulletins the firm issued and the table of contents/index to the manuals/bulletins.
- Item 12:** Analyses and reconciliations of the customer parties' accounts, including those relating to reviews of the customer parties' claims, accounts, transactions or the product or types of products at issue.
- Item 13:** Exception reports, supervisory activity reviews, concentration reports, active account runs and similar documents produced to review for activity in the customer parties' accounts related to the allegations. For claims alleging failure to supervise, the firm/associated persons must produce the documents listed in this Item that were produced to review for activity in customer accounts handled by associated persons and related to the allegations.
- Item 14:** Portions of internal audit reports for the branch in which the customer parties maintained accounts that concern associated persons or the accounts or transactions at issue and discussed alleged improper behavior in the branch against other individuals similar to the improper conduct alleged.
- Item 15:** Records of disciplinary action taken against associated persons by any regulator or employer for all sales practice violations or conduct similar to the conduct alleged.
- Item 16:** Investigations, charges, or findings by any regulator and the firm/associated persons' responses.
- Item 17:** Portions of examination reports or similar reports following an examination or inspection conducted by any regulator that focused on the associated persons or the customer parties' claims, accounts or transactions, or the product or types of products, or that discussed alleged improper behavior in the branch against other individuals similar to the conduct alleged.

- Item 18:** Documents related to the case that the firm/associated persons received by subpoena or by document request directed to third parties.
- Item 19:** For the transactions at issue, documentation showing the compensation, gross and net, to the associated persons.
- Item 20:** For claims related to solicited trading activity, a record of all compensation, including, but not limited to, monthly commission runs for the associated persons.
- Item 21:** A record of all agreements pertaining to the relationship between the associated persons and the firm, summarizing the associated persons' compensation arrangement or plan with the firm.
- Item 22:** For allegations regarding an insurance product that includes a death benefit, information concerning the customer parties' insurance holdings and recommendations, if any, regarding insurance products.

### Documents the Customer Parties Shall Produce in All Customer Cases (List 2)

Document Production List 2 specifies the presumptively discoverable documents that customer parties are required to produce in customer cases. Subject to the limited exceptions specified in certain List items, customer parties are required to produce every document in every case unless the required production is narrowed either by party agreement or by order of the arbitrator. Highlights of the items follow. See the attached Guide for the full details and requirements of each item, including relevant time frames.

- Item 1:** Customer party federal income tax returns, limited to pages 1 and 2 of Form 1040; Schedules A, B, D and E; and the IRS worksheets related to these schedules, redacted to delete the customer parties' Social Security numbers. Customer parties may redact information relating to medical and dental expenses and names of charities on Schedule A unless the information is related to allegations in the Statement of Claim.
- Item 2:** Financial statements, including statements within a loan application, or similar statements of the customer parties' assets, liabilities and/or net worth.
- Item 3:** Documents the customer parties received from the firm/associated persons and from entities in which the customer parties invested through the firm/associated persons, including account opening documents and/or forms, prospectuses, research reports, annual and periodic reports, and correspondence.
- Item 4:** Account statements for each non-party securities firm where the customer parties maintained an account.

- Item 5:** Documents, including agreements and forms, relating to accounts at the firm or transactions with the firm.
- Item 6:** Account analyses and reconciliations prepared by or for the customer parties relating to the customer parties' accounts at the firm or transactions with the firm.
- Item 7:** Notes, including entries in diaries or calendars, relating to the accounts at the firm or the transactions at issue.
- Item 8:** Recordings and notes or logs of telephone calls or conversations about the customer parties' accounts or transactions at issue that occurred between the associated persons and the customer parties, and telephone records evidencing telephone contact between the customer parties and the firm/associated persons.
- Item 9:** Correspondence the customer parties sent or received relating to the accounts or transactions at issue.
- Item 10:** Previously prepared written statements by persons with knowledge of the facts and circumstances related to the accounts or transactions at issue.
- Item 11:** Complaints/Statements of Claim and answers filed in civil actions involving securities and securities arbitration proceedings in which the customer parties have been a party, and all final decisions or awards or non-confidential settlements entered in these matters. If a person is a party to a confidential settlement agreement that by its terms does not preclude identification of the existence of the agreement, the party shall identify the documents comprising the agreement.
- Item 12:** Documents showing the customer parties' ownership in or control over any business entity. If the customer parties are trustees, documents showing the accounts over which the customer parties have trading authority.
- Item 13:** Documents the customer parties received, including documents found through the customer parties' own efforts, relating to the investments at issue.
- Item 14:** For claims alleging unauthorized trading, documents the customer parties relied upon to show that they did not know about or consent to the transactions at issue.
- Item 15:** Materials the customer parties received or obtained relating to the claims, transactions or products at issue, and materials received relating to other investment opportunities.

- Item 16:** Customer parties' resumes.
- Item 17:** Existing descriptions of the customer parties' educational and employment background if not set forth in resumes.
- Item 18:** Documents related to the case that the customer parties received by subpoena or by document request directed to third parties.
- Item 19:** To the extent that an insurance product that provides a death benefit is included in the Statement of Claim, information received from an insurance sales agent or securities broker relating to such insurance.

## Effective Date

The amendments are effective on May 16, 2011, and will apply to all customer cases filed on or after the effective date.

## Endnotes

- 1 Exchange Act Release No. 64166 (April 1, 2011), 76 Federal Register 19155 (April 6, 2011) (File No. SR-FINRA-2010-035).
- 2 *See Notice to Members (NTM) 99-90* (November 1999).

## Attachment A

Deletions are in brackets.

### Code of Arbitration Procedure for Customer Disputes

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#### 12506. Document Production Lists

##### (a) Applicability of Document Production Lists

When the Director serves the statement of claim, the Director will notify parties of the location of the FINRA Discovery Guide and Document Production Lists on FINRA's Web site, but will provide a copy to the parties upon request. Document Production Lists 1 and 2 describe the documents that are presumed to be discoverable in all arbitrations between a customer and a member or associated person. [Other Document Production Lists may also apply, depending on the specific cause(s) of action alleged.]

##### (b) Time for Responding to Document Production Lists

(1) Unless the parties agree otherwise, within 60 days of the date that the answer to the statement of claim is due, or, for parties added by amendment or third party claim, within 60 days of the date that their answer is due, parties must either:

- Produce to all other parties all documents in their possession or control that are described in [the] Document Production Lists 1 and 2[, and any other Document Production List that is applicable based on the cause(s) of action alleged];
- Identify and explain the reason that specific documents described in Document Production Lists 1 and 2[, and any other Document Production List that is applicable based on the cause(s) of action alleged,] cannot be produced within the required time, and state when the documents will be produced; or
- Object as provided in Rule 12508.

(2) No change.

(c) No change.

\* \* \*

**12508. Objecting to Discovery; Waiver of Objection**

(a) If a party objects to producing any document described in Document Production Lists 1 or 2[, any other applicable Document Production List,] or any document or information requested under Rule 12507, it must specifically identify which document or requested information it is objecting to and why. Objections must be in writing, and must be served on all other parties at the same time and in the same manner. Objections should not be filed with the Director. Parties must produce all applicable listed documents, or other requested documents or information not specified in the objection.

(b)-(c) No change.

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