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It's 2020: Some Surprises are in Store for Arbitration and the Financial Services Industry

By George H. Friedman*

Editor's Note: *Thanks to all* SAC *subsribers for your support and patronage over the years and, to all readers, a healthy, prosperous 2020! This edition of* SAC*, as our newsletter has become popularly known, completes Volume 2019. The first edition of* SAC *was printed and distributed in April 1988. Within six months of publication, we attracted over 200 subscribers, many of whom -- bless their loyalty (!) -- remain subscribers today. Those were heady times. We can think of no better way to mark this Volume's end and to begin 2020 than to lead with an article by George Friedman, newly Editor-in-Chief of SAC's* Securities Arbitration Alert*, focusing on predictions for securities arbitration in the coming year.*

G. Friedman

Introduction

With the new year here, it's time for my annual predictions. Among other things, 2020 will feature another SCOTUS decision on arbitration, more proposed federal laws – and a surprise enactment or two – curbing mandatory predispute arbitration, and of course another presidential election, complete with every House seat and several Senate seats up for grabs. What might this mean for arbitration and the financial services industry? I won't hazard a (public) prediction on the elections, but I will say this: some surprises are in store in the ADR world.

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Read on, my friends.

Some Iteration of the FAIR Act will Become Law; So Will Another Bill or Two

The *Forced Arbitration Injustice Repeal (FAIR) Act of 2019* – H.R. 1423 and S. 610 – is this Congress' iteration of the dear, departed, *Arbitration Fairness Act* or, as I call it, "The AFA on Steroids." If enacted, the *FAIR Act* would amend the Federal Arbitration Act ("FAA") to eliminate mandatory predispute arbitration agreements ("PDAA") for disputes involving consumer, investor, civil rights, employment, and antitrust. It definitely covers brokers and investment advisers; bars class action/collective action waivers in or out of a PDAA; extends to "digital technology" disputes; reserves for court determination any arbitrability or delegation issues "irrespective of whether the agreement purports to delegate such determinations to an arbitrator;" and clearly extends to sexual harassment claims. The *FAIR Act* would be retroactive, applying to *claims* made after the effective date.

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WELCOMING ROBERT PEARCE TO SAC's BOARD OF EDITORS

R. Pearce

Our practice since 1988, when we first formed the Board of Editors, has been to seek individuals to serve who have performed outstandingly in the field of securities/commodities arbitration and who have contributed, by their character, position, and inclinations to the development, integrity and advancement of the process. Bob Pearce has been practicing in the area of securities dispute resolution for as long as *SAC* has been a newsletter -- perhaps longer, since the earliest Award we have in SAC's Award Database reflecting Bob's name as an attorney is *Shevrin v. Broadchild Securities*, which was filed in May 1987, a month before *McMahon* issued.

Bob won that case for his client. It took two years, issuing at a time when the Ft. Laudedale firm of Lerner & Pearce, comprised of two former SEC attorneys, was just getting underway. Through the years, Bob has worked solo or teamed with one or two other attorneys in his practice. Today, the Law Offices of Robert Wayne Pearce, P.A. in Boca Raton, FL has one other lawyer. In the intervening years, Bob has honed his role as a securities attorney, representing clients in federal and state court, in arbitrations before the AAA, JAMS, NFA and the securities SRO forums, and defending industry parties before the SEC, FINRA, CFTC and the Florida Office of Financial Regulation.

Bob has served as a Federal court-appointed Receiver. He is qualified as a Certified Circuit Court Mediator and is a respected mediator in the FINRA Mediation Program. Because of his wide-ranging experience, he is often called upon to serve as an arbitrator, mediator or expert witness in complex securities and commodities and other investment disputes. SAC's Award Database now displays almost 100 Awards with Bob's name, either as Respondent's counsel or Claimant's counsel. In the SAC Database, Bob's first million-dollar-plus award occurred in 1991, on behalf of a trust, *Friedlander v. Margaretten Securities*, in NASD Arbitration.

There have been numerous others since, including two from Puerto Rico Panels in PR Bond cases. Most of his cases are situated in Florida, of course, but Bob has prosecuted arbitration claims to conclusion across the nation, including California, District of Columbia, Maryland, Michigan, Missouri, Pennsylvania and New York (where Bob began and has been a member of the Bar since 1980). He has received many accolades for his work, but an article featuring Bob in Florida's *Super Lawyers* Magazine article (first published in 2014 and updated in December 2019) reflects it all - a career of accomplishment, respect of colleagues, and a dedication to his field. For these reasons -- and because we value his candor and perspective -- we welcome Bob Pearce to the *SAC* Board of Editors.

-- Rick Ryder, SAC

MANAGING EDITOR .... **Richard P. Ryder**

SECURITIES ARBITRATION COMMENTATOR

Mailing Address: SAC, P.O. Box 112, Maplewood, N.J. 07040. Business Office: 590 Bloomfield Ave., Ste. 354, Bloomfield, NJ 07003. Tel: (973) 761-5880; 973-232-5698; 973-232-5032.

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Some Surprises in 2020 *cont'd from page 1*

The Act was approved by the House of Representatives on September 20 by a mostly party-line 225-186 vote. It has gone nowhere in the Senate; as of today – *as written* – it is stuck at 38 co-sponsors, with zero Republican support. But that doesn't mean it's dead. I predict that there will be a bipartisan effort to focus on procedural fairness. Why do I say this? The full Senate Judiciary Committee held an April 2019 hearing titled *Arbitration in America.* Based on the comments and questions from Committee members including Chair Lindsey Graham (R-SC) and former Chair Charles Grassley (R-IA), it seems to me there would be Republican support for some changes focused on procedural fairness. Senator Graham said:

> "The problems we will hear about today bother me…. What's good for business is not necessarily good for individuals…. It bothers me that when you sign up for a product or service you are giving away your rights. For the rest of this year this Committee will take a long and hard look at how arbitration can be improved. We will try to find some middle ground. We will find a way forward…. There have to be fairness standards."

Also, two Republican House members – Matt Gaetz, (FL) and Chris Smith (NJ) – voted in favor of the *FAIR Act,* as did recent GOP convert Jeff Van Drew (NJ).

The bottom line: look for passage of an amended *FAIR Act* bill that focuses less on banning PDAAs and more on ensuring procedural fairness – just as the name implies. How so?

Concerns Should be Addressed

I see many of the bills being well-intended but potentially troublesome overreactions to a legitimate concern. For example, I continue to think that retroactive nullification of existing PDAAs invites legal challenges based on the Constitution's Takings Clause.[1] And I chafe at the underlying assumption that arbitration is a bad thing.

On the other hand, procedural protections and improvements are needed, in my view. For example, I believe it is unfair to require a consumer to agree to a lop-sided version of arbitration when a contract is signed as a condition of the dominant party providing goods or services. Ditto for employees. It's not that the arbitration process is unfair, assuming basic standards of procedural fairness are maintained. It's that *perceptions* of fairness require a choice for the weaker party.[2]

Also, some of the arbitration systems imposed on consumers and employees – *not* those of the established ADR providers like AAA, FINRA, JAMS and CPR – have aspects that are not fair. For example, requiring consumers to travel hundreds of miles for a hearing involving relatively small amounts of money is not fair. Allowing the dominant party to select a captive ADR provider isn't fair. Burying the arbitration agreement in the midst of a dense contract is not fair.[3] There are better approaches, that: 1) address perceptions that it is not fair for a dominant party to force a consumer or employee to agree to a PDAA as a condition of obtaining goods or services or employment; and 2) ensure procedural fairness.

A Better Way?

Last year, I opined on this very subject;[4] the points still ring true today. Here's my plan. At a very high level, I propose fixes to the *FAIR Act* that provide:

- in a consumer contract, any predispute arbitration agreement must be separately signed or clicked by the consumer;
- a consumer cannot be denied goods or services if the consumer declines the arbitration option;
- in an employment contract that is not individually negotiated, any predispute arbitration agreement must be separately signed or clicked by the employee;
- a prospective or current employee cannot be denied employment if the employee declines the arbitration option;
- clear procedural fairness guidelines[5] be followed in any consumer or employment arbitration; and
- the law is prospective, applying to contracts entered into or revised after the effective date. This avoids Constitutional issues.

Et tu, Mr. President?

Would President Trump sign a bill curbing arbitration? Although the President is a big supporter of arbitration, he has *already signed* bills limiting the use of mandatory PDAAs – twice in 2019. For example, the *Taxpayer First Act* – H.R. 3151 – became law July 1. Nestled in the text of this omnibus bill is section 1405, which bans mandatory arbitration of IRS whistleblower claims. Also, the budget deal for the fiscal year ending September 30, 2020 (the *Consolidated Appropriations Act of 2020* – H.R. 1158) signed by the President on December 20 in section 8093 bars companies with federal defense contracts valued at over $1 million from mandating arbitration of Title VII or sexual harassment or assault claims. The law also prohibits enforcement of arbitration clauses in existing contracts.

Other Candidates for Enactment? Any proposed law perceived as protecting servicemembers will have bipartisan appeal. The Senate version of the *Justice for Servicemembers Act* (S. 2459) introduced September 10 by Sen. Murkowski (R-AK) and cosponsored by Sen. Graham (R-SC), is a clear harbinger of bipartisan support. Also, the *Ending Forced Arbitration of Sexual Harassment Act* (H.R. 1443) likewise has broad bipartisan support, and I don't think the President would risk a veto override in an election year.

SCOTUS Will Surprise Us in *GE Power*

On the Term's last day, SCOTUS granted *Certiorari* in an arbitration-centric case, *GE Energy Power Conversion France SAS v. Outokumpu Stainless USA LLC*, No. 18-1048.[6] The Petition for *Certiorari* was filed February 8,

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seeking review of *Outokumpu Stainless USA, LLC v. Converteam SAS*, 902 F.3d 1316 (11th Cir. 2018). The question presented in the Petition, which was granted June 28, asks: "Whether the *Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (the '*New York Convention*') permits a non-signatory to an arbitration agreement to compel arbitration based on the doctrine of equitable estoppel."

To review, FAA Chapter 2, which implements the *Convention*, enforces not only arbitration Awards, but also predispute arbitration agreements. It is hornbook law that a signatory to a broad PDAA is bound by its terms under FAA Chapter 1, and that sometimes such an arbitration agreement can be enforced by or against a non-signatory via equitable estoppel.[7] FAA Chapter 1, section 2, which in domestic transactions requires a written agreement to arbitrate, makes no mention of *signatures,* but the *Convention* does. Specifically:

> Article II, § 1: "Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship ….
>
> Article II, § 2: "The term 'agreement in writing' shall include an arbitral clause in a contract or an arbitration agreement, *signed by the parties* or contained in an exchange of letters or telegrams" (emphasis added).

SCOTUS has set oral argument for January 21. The December 9 Order List on page two shows that the Court has granted the Solicitor General's Motion to participate in the oral argument as *Amicus Curiae* on behalf of Petitioner, and for divided argument (ten minutes). Many *Amicus* Briefs have already been filed; they can be viewed here.

Why do I predict we may be in for a surprise in GE Power, given the Court's consistent support of arbitration and the FAA over the past half century? After all, there would appear to be a solid 5-4 pro-arbitration majority, and new Justices Neil Gorsuch and Brett Kavanaugh have already authored Opinions supporting arbitration. See for example *Henry Schein, Inc. v. Archer & White Sales, Inc*., 139 S. Ct. 524 (Jan. 8, 2019), where in the first Opinion written by Justice Kavanaugh, the Supreme Court held unanimously that there is no delegation carveout under the FAA for "wholly groundless" assertions of arbitrability. And recall that Justice Gorsuch authored the majority Opinion in *Epic Systems Corp. v. Lewis*, 138 S. Ct. 1612 (2018), reaffirming that the Federal Arbitration Act will prevail over another federal statute unless the latter expressly bars predispute arbitration agreements.

So, again, why this prediction? While it's probably way too early to be prognosticating, readers should note that Justices Gorsuch and Kavanaugh seem to be sticklers on statutory construction. Just read the Opinions in *Epic Systems* and *Henry Schein*. So, I would not at all be surprised by a decision saying essentially, "If Congress meant FAA Chapter 2 to deviate from the Convention's definition of an arbitration agreement it would have used language to that effect."

Repeal of Dodd-Frank is Still Kaput

In June 2017, the House of Representatives by a 233–186 strictly party-line vote approved the *Financial CHOICE Act*. Not a single Democrat voted "Yea" and only one Republican voted "Nay." Among other things, the 602-page Act (H.R. 10) would have repealed and replaced Dodd-Frank, and would have eliminated the authority granted to both the CFPB and SEC to limit or eliminate predispute arbitration agreements, or set conditions for their use. The Senate Banking Committee held hearings, but the full Senate did not act[8] and the bill expired with the old Congress in January 2019. I wrote a year ago that: "I very much doubt the new Democratic House would approve a reintroduced *FCA*," and indeed nothing happened in 2019. Repeal will remain kaput until at least the 117th Congress takes over in 2021.

The DOL will Finalize Its Fiduciary Rule, Coordinating with the SEC

On June 5 the SEC moved ahead with its own fiduciary standard rule, as authorized by Dodd-Frank section 913(g)(1). Specifically, the SEC voted 3-1 (Commissioner Jackson dissenting) to approve *Regulation Best Interest* (*Reg BI*) and three related proposed regulations at an open meeting held June 5. The revised, final package, which was accompanied by a Press Release containing a Fact Sheet and the massive final rulemaking package, was published that day. Two items were effective immediately on *Federal Register* publication in July: *Commission Interpretation Regarding Standard of Conduct for Investment Advisers* (84 FR 33669) and *Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion From the Definition of Investment Adviser* (84 FR 33681). Two other rules went into effect September 10, specifically *Reg BI* (84 FR 33318) and *Final Rule - Form CRS Relationship Summary and Form ADV Amendments* (84 FR 33492). Of key importance: "by June 30, 2020, registered broker-dealers must begin complying with Regulation Best Interest and broker-dealers and investment advisers registered with the Commission will be required to prepare, deliver to retail investors, and file a relationship summary."[9]

And the DOL Fiduciary Rule?

The Department of Labor's ("DOL") fiduciary standard rule for those offering retirement investment advice was invalidated by the Fifth Circuit in *Chamber of Commerce of the United States v. Department of Labor*, 885 F.3d 360 (5th Cir. 2018). The DOL in October 2018 issued its Fall Regulatory Agenda that included an item (RIN: 1210-AB82) on the now-defunct rule with this description: "On April 8, 2016, the Department replaced the 1975 regulation with a new regulatory definition [of fiduciary]. The new regulatory definition was vacated in toto in *Chamber of Commerce v. Department of Labor*…. The Department is considering regulatory options

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in light of the Fifth Circuit opinion." At that time, DOL projected a final rule by September 2019. The Department's Spring Regulatory Agenda included an update to RIN: 1210-AB82, indicating that the final rule would be proposed in December 2019. The Fall Agenda conveyed the same message.

So far there has been no rulemaking activity through today, but it's just a matter of time. And, in my mind there's no question that there will be coordination between the two Agencies. Then-DOL Secretary Alexander Acosta testified at a May 1 House Education and Labor Committee hearing titled, *Examining the Policies and Priorities of the U.S. Department of Labor*. Although not referenced in his prepared remarks, as reported by *InvestmentNews* and as seen in the hearing video, Secretary Acosta said of SEC coordination, "We are communicating with them, and based on our collaboration, we will be issuing new rules in this area." And a *Financial Adviser IQ* story reported: "In response to follow-up queries from *FA-IQ* about the new fiduciary rules, a DOL spokesperson said: 'The department's goal is to align our rules with the SEC's final rule and to the greatest extent possible to build off and harmonize with the work that they have done.'"[10]

The bottom line? I expect DOL to toe the line and come out with something consonant with Reg BI. While I don't predict this, I hope that DOL reiterates its recognition of the legitimacy of PDAAs in connection with fiduciary standards, given that some are ready to make the argument that a fiduciary using PDAAs faces a conflict of interest with the client.

More Smooth Sailing for President Trump's Nominees – and the Ninth Circuit will become Pro-arbitration (Really)

With a 53-47 GOP majority in the Senate, President Trump will again have a relatively easy time getting his judicial and agency head nominees approved by the next Senate. Last year, the President's nominee for the SEC Commissioner vacancy created by the departure of Democrat Kara M. Stein sailed through the Senate. Allison H. Lee was nominated in April, approved by the full Senate by voice vote on June 20, and sworn in on July 8. Democrat Robert L. Jackson, Jr. will be leaving the Commission on February 14,[11] and I have no doubts about his successor being approved swiftly and without resistance. As of this writing, there is media speculation that the nominee to replace Mr. Jackson will be SEC staff attorney Caroline Crenshaw.[12]

And the Courts?

President Trump has appointed and the GOP-controlled Senate confirmed a record number of federal judges in 2019, who for the most part are relatively young and conservative.[13] As of year's end:[14]

- President Trump appointed 102 federal judges in 2019 alone.

- The President has appointed 184 federal judges since becoming President, 50 of them circuit court judges.

- One in four federal circuit court judges are now Trump appointees.

- With 10 Trump appointees, the notoriously anti-arbitration Ninth Circuit has gone from a net majority of 11 Democrat appointees to just three, and the Second, Third, and Eleventh Circuits have "flipped" to majority Republican-appointees.

Already, I perceive a shift at the Ninth Circuit. For example, the Court in August denied a request for rehearing and rehearing *en banc* in *Dorman v. Charles Schwab Corp*., 934 F.3d 1107 (Aug. 20, 2019). The *Dorman* Court overruled a 35-year-old precedent, concluding that intervening Supreme Court rulings signify that Employee Retirement Income Security Act ("ERISA") claims are indeed arbitrable. The Ninth Circuit had held in *Amaro v. Continental Can Co*., 724 F.2d 747 (9th Cir. 1984), that claims asserted under ERISA could not be compelled to arbitration under the FAA. The unanimous *Dorman* Court holds:

> "In light of intervening Supreme Court case law, including … *Italian Colors* …, we conclude that our holding in *Amaro* is no longer good law…. Since *Amaro,* the Supreme Court has ruled that arbitrators are competent to interpret and apply federal statutes. See, e.g., *Am. Express Co*., 570 U.S. at 233 (holding that there is nothing unfair about arbitration -- even arbitration on an individual basis -- as long as individuals can vindicate their statutory rights in the arbitral forum). Recently, in *Munro v. Univ. of S. Cal*., 896 F.3d 1088 (9th Cir. 2018), we noted that 'there is considerable force' to the argument that *Amaro* has been overruled…. We agree" (some citations omitted).

There will undoubtedly be more federal judge nominations to come, and Leader McConnell will continue to work closely with the White House this year to confirm the President's nominees. Also, I'm certain if there are any further vacancies on the Supreme Court, Mr. Trump's nominees will be pro-arbitration and will eventually be approved by the Senate.[15]

Bonus: the Next President Will Be….

You really didn't think I'd be so bold as to predict *now* the outcome of the presidential election next *November*, did you? What I had in mind was offering insights on how the winner of the next election views arbitration, like "[Winner] will be supportive/critical/neutral/a blank slate about arbitration…" For example, as I've written before, I bet you didn't know that in 1994, a young attorney named Barack Obama argued successfully to enforce an NASD arbitration award in the Seventh Circuit? See *Baravati v. Josephthal, Lyon & Ross, Inc*., 28 F.3d 704 (7th Cir. 1994). Check back here after the election for my thoughts on the next President's arbitration views.

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Conclusion

I'm a bit reluctant to make so many bold predictions, given how wrong the pollsters and pundits were on election night 2016. On the other hand, my past predictions over the years have been pretty good.[16] Here's one prediction you can take to the bank: the arbitration world is constantly changing, and will evolve yet again next year. Doubtless there are some things that will happen in 2020 that I just don't see coming right now. And of course, some of my predictions may not come to pass, at least not yet. We will again compare notes in a year. In the meantime, see you in the future!

**George H. Friedman, Editor-in-Chief of the online* Securities Arbitration Alert *and an ADR consultant, retired in 2013 as FINRA's Executive Vice President and Director of Arbitration, a position he held from 1998. He also serves as non-executive Chairman of the Board of Directors of Arbitration Resolution Services. In his extensive career, he previously held a variety of positions of responsibility at the American Arbitration Association, most recently as Senior Vice President from 1994 to 1998. He is an Adjunct Professor of Law at Fordham Law School, and is also a member of the AAA's national roster of arbitrators. He holds a B.A. from Queens College, a J.D. from Rutgers Law School, and is a Certified Regulatory and Compliance Professional.*

Endnotes

1 U.S. Const. Art. 5.

2 See Black, Barbara & Gross, Jill, *When Perceptions Changes Reality: an Empirical Study of Investors' Views on the Fairness of Securities Arbitration,* 2008 J. Dispute Res. 349 (2009), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1118430##.

3 For a humorous take on this point, see *Wilson v. Huuuge, Inc.,* No. 18-36017 (9th Cir. Dec. 20, 2019) , where the unanimous Court says that playing "hide the-ball" (the Court's phrase) with the arbitration clause is not a good idea, where "the user would need Sherlock Holmes's instincts to discover the Terms" containing the PDAA.

4 See Friedman, George, *Surprise! Some of the Anti-Arbitration Bills Introduced in Congress this Year May Actually Become Law (One Already Has)*, 2019:5 SAC 1 (Sep. 2019).

5 The FINRA Code of Arbitration Procedure is a good example.

6 See the Securities Arbitration Commentator's July 1, 2019 blog post, *Certiorari Granted in Eleventh Circuit Case Holding that Non-Signatory Party Cannot Compel Arbitration Under the NY Convention.*

7 For a nice primer on equitable estoppel, see Law 360, *Courts' Love-Hate Relationship with Equitable Estoppel* (June 1, 2015).

8 Why the Senate failed to act during the lame duck session is a bit of a mystery. My guess is that with a slim 51-49 GOP Senate majority in the last Congress, the votes just weren't there.

9 Both the SEC and FINRA have made Reg BI core regulatory compliance objectives for 2020.

10 Senator Elizabeth Warren (D-MA) evidently believes the DOL intends to coordinate its rule with the SEC's. On December 11 she wrote to current DOL Secretary Eugene Scalia to voice her concerns that the DOL "may simply copy the wholly inadequate standards of conduct framework developed by the SEC in its recently-finalized Regulation Best Interest…." That, says Sen. Warren, would be a "costly mistake." The letter closed by posing eight questions – some with subparts – that were to be answered by December 18.

11 See *SEC Democratic Commissioner Jackson to Step Down Next Month* (Reuters Jan. 16, 2020).

12 See, e.g., *Exclusive: White House Expected to Nominate SEC Lawyer for Democratic Commissioner Seat – Sources* (WKZO, Dec. 20. 2019).

13 See, e.g., *Senate Confirms Avalanche of Trump-backed Judges Despite Impeachment* (NY Post Dec. 22, 2019), and *Trump Secures 50th Appellate Court Appointment, with Another 9th Circuit Judge Confirmed* (True Pundit, Dec. 11, 2019). Also, the December 11, 2019 Press Release issued by Leader McConnell.

14 See Fox News video, *How Trump is Filling the Liberal Ninth Circuit with Conservatives* (Dec. 26, 2019).

15 But no matter who the nominee is, the confirmation process will *not* be "smooth sailing"! I'm certain the Democrats will invoke "The Merrick Garland Precedent" and argue that there should be no SCOTUS vacancies approved in a Presidential election year. And if the vacancy is from one of the liberal wing Justices, expect a Battle Royale that will make the Kavanaugh proceedings look like they were conducted under the Marquess of Queensberry Rules.

16 Just ask my adult kids about our 2016 election wager. That was some steak dinner.

IN BRIEF

(*ed: This Section of the newsletter draws upon material previously published in the* Securities Arbitration Alert*, a supplemental e-mail service that is supplied to SAC Preferred subscribers weekly. A number of items in the relevant Arb Alerts do not appear here and those that do are often edited to bring them current to the date the newsletter goes to press. This "In Brief" column includes selected excerpts from SAAs that issued in recent months.)*

FINRA STATS, 11/19. DO NOVEMBER CASE FILINGS PRESAGE POTENTIAL TRENDLINE FOR 2020 CASELOAD? ***After the August surge in case filings and the drop back to yearly averages in September and October, we hoped the November numbers from FINRA's Office of Dispute Resolution ("FINRA-ODR") would suggest whether the year will finish strongly or with a fizzle.*** The latest monthly report is now available, and it indicates to us that the latter will be the case, with a middling final year-end tally.

Corrections, Surges & Signals

Let's start with an "Errata:" In reviewing the October 2019 FINRA statistical report at SAA 2019-45 (Nov. 27), we wrote: "In 2012, 4,299 new cases were filed; in 2018, the forum took in 4,325 new matters. 2019 will fall in between, begging the question, which way will 2020 go?" We should have written: "In 2012, 4,299 new cases were filed; in 2018, the forum took in 4,325 new matters. 2019 *will not approach these two case-filing bookends*, begging the question, which way will 2020 go?" Sandwiched between those two bookends are the lower case volume "quiet" years, a period lulled by a roaring bull market that has quieted the potential claims of many investors and rewarded others with serendipitous gains. The stock market's value soared some 30% in 2019, yet 2019 case-filing numbers at the FINRA arbitration forum have shown signs of strength. They popped in August to 500 for the month and, by October, looked capable of surpassing all five of the annual totals for the bracketed "quiet" years of 2013-2017.

November Signals New Lull

Then, the November new-case statistics were posted by FINRA-ODR just before the holidays, providing the latest indicator: 2019 will not show a recovery in case submissions by customers. FINRA reports 3,454 new matters filed with the arbitration facility during the first eleven months of the year. In October, there had been 317 new matters recorded, bringing the total for ten months to 3,203. The additional 251 cases filed in November now suggest that the year-end tally will be around 3,700. That number falls in the middle of the new-case figures for the quiet years. With the added information that the surge in August was due to a one-off event (see "Stats," SAA 2019-41 (Oct. 30)), 2019 appears ready to settle towards the bottom of the quiet pack.

Closed & Cases Pending

We'll sum up the prospects for 2020 when the December 2019 figures are released late in January. As of this writing, total new submissions are down 12% year-over-year, when compared to 2018's 3,937 tally. Dividing the total into customer and intra-industry claims, we find the former totaling 2,184 through November (2,507 in 2018), down 13% Y-O-Y, and the latter reaching 1,270, an 11% decrease from the 1,430 matters recorded through November 2018. Closed cases are up 7% Y-O-Y, with 3,699 cases concluded (3,444 in 2018) and pending or "Open" cases have subsided from earlier in the year to 4,817. That indicates much of the surge from last year has been absorbed and the decline in case inflow has begun to clear the pipeline somewhat. We might expect to see a further reduction in overall turnaround time averages (currently 14.1 months), as case traffic continues to lighten.

The Disappearing Arbitration Award

Speaking of lightening, we note with some dismay the marked shift away from trying cases, especially those brought by customers. Only 16% of all cases are being decided by arbitrators nowadays and that total includes the plethora of expungement cases in the pipeline -- and those have to be tried. Viewing customer-initiated claims solely, we find that percentage dropping to 13%. Many of the concluded cases are likely to be Puerto Rico Bond cases, as they comprise a large portion of FINRA-DR's case inventory. They reportedly settle at a 95%+ rate, so that particular "pig in the python" may be impacting the historically low numbers. When one reviews the particularly high win and recovery rates for the PR bond-related cases, though, and notes the escalating win rates overall for customers (47% vs. 40% Y-O-Y), especially in the higher-dollar cases (57% vs. 42%, All-Public Panels & Y-2-Y), higher-than-normal settlement rates seem almost anomalous. The climate for customers has rarely been better!! *(ed: Another seeming anomaly in the FINRA-ODR statistical report relates to the arbitrator roster numbers. We watched the ranks of Public and Non-Public arbitrators bloom and flourish over the past couple of years, a focused result of aggressive arbitrator recruiting by FINRA-ODR staff. Having almost broken the 8,000 mark earlier in the year, the Neutral Roster total receded to 7,814 (3,668 PAs & 4,146 NPAs) at November's end. There seemed to be a shake-out going on, primarily in the Non-Public ranks. As October registered a lower sum of 7,776 (3,653 & 4,123) than November, it may be that the trendline will return now to the positive.)* (SAC Ref. No. 2020-01-01)

THE OTHER SHOE DROPS: "INVESTOR CHOICE ACT" FINALLY REINTRODUCED IN HOUSE AND SENATE. WOULD AMEND 1934 ACT AND INVESTMENT ADVISERS ACT OF 1940 TO BAN MANDATORY PREDISPUTE ARBITRATION

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AGREEMENTS IN CUSTOMER AND SHAREHOLDER RELATIONSHIPS. ***It took a while, but joining the slew of anti-arbitration bills pending in Congress is the* Investor Choice Act, *identical versions of which were introduced in the House and Senate in early December.*** We reported in SAA 2019-12 (Mar. 20) that House and Senate Democrats had reintroduced several anti-mandatory arbitration bills in late **February** and early **March,** seeking to amend the Federal Arbitration Act ("FAA"), specific statutes like Dodd-Frank, or both. Most were reintroductions of bills that were not enacted by the last Congress. One of the old bills that had not yet been reintroduced was the *Investor Choice Act* ("ICA"), which would have amended the *Securities Exchange Act of 1934* and the *Investment Adviser Act of 1940* to ban the use of mandatory predispute arbitration agreements ("PDAA") by broker-dealers and investment advisers and would have guaranteed class action participation. We later reported in SAA 2019-15 (Apr. 17) that the ICA was reintroduced **March 28** in the House. The bill, however, was never formally introduced. That's no longer the case, because S. 2992 (introduced by Sen. **Jeff Merkley** (D-OR)), and H.R. 5336 (introduced by Rep. **Bill Foster** (D-IL)), were introduced within days of each other in early **December**.

New Bills are Almost Identical to the Old ICA…

The newly-introduced ICA is nearly identical to the old one (H.R. 585). The caption describes the proposed ICA as intending "to amend the Securities Exchange Act of 1934 and the Investment Advisers Act of 1940 to prohibit mandatory pre-dispute arbitration agreements, and for other purposes." Specifically, the bills would declare it unlawful for BDs, funding portals, municipal securities dealers, or investment advisers: "to enter into, modify, or extend an agreement with customers or clients of that entity with respect to a future dispute between the parties that -- (1) mandates arbitration for that dispute; (2) restricts, limits, or conditions the ability of a customer or client of that entity to select or designate a forum for resolution of that dispute; or (3) restricts, limits, or conditions the ability of a customer or client of that entity to pursue a claim relating to that dispute in an individual or representative capacity or on a class action or consolidated basis."

… But Different

This iteration of the ICA is essentially the same as the one introduced in the 115th Congress, except it adds a section amending the *Securities Act of 1933* to state: "A security may not be registered with the Commission if the issuer, in its bylaws, registration statement, or other governing documents mandates arbitration for any disputes between the issuer and the shareholders of the issuer." The bills also prohibit issuers from including shareholder arbitration agreements in IPO subscription agreements.

Retroactivity with One Exception

If enacted, the changes would be retroactive, rendering void a preexisting non-conforming arbitration agreement, except that pending, ongoing arbitrations would be allowed to continue. Specifically, a PDAA "shall not be void … if arbitration required by that provision was initiated by any party on or before the date of enactment of this Act." While this carveout would avoid chaos in pending cases, as we've said before, we think retroactivity – invalidating existing arbitration agreements – invites challenges as an impermissible taking under the Constitution.

*(ed: *The original bills were analyzed by SAC Editor-in-Chief and Fordham Law Professor George H. Friedman, who wrote a guest SAC Blog post we published in March,* Democrats Introduce Several Anti-Mandatory Arbitration Bills. What You Need To Know. *More recently, the Bates Group on April 25 published a nice analysis,* Federal Legislators Target Mandatory Arbitration, *focusing on potential impact on the financial services industry and regulators, and how they are reacting. **The added provision barring shareholder PDAAs to us is an effort to address this year's flap over Johnson & Johnson and an attempt to require arbitration to resolve shareholder disputes. See our coverage in SAA 2019-13 (Apr. 3). ***The forum designation clause is interesting. Of course, FINRA's Rules already bar class action waivers and permit customers to opt out of a PDAA commitment into class actions. ****The non-partisan Govtrack.us Website has not yet rated the chances of enactment, but we see them as very low.)* (SAC Ref. No. 2019-47-01)

MASSACHUSETTS ISSUES PROPOSED FINAL FIDUCIARY REGULATION. We reported in SAA 2019-24 (June 19) that, following the leads of Connecticut, Maryland, Nevada, and New Jersey, Massachusetts Secretary **William Francis Galvin** on **June 14** issued a *Preliminary Solicitation of Public Comments: Fiduciary Conduct Standard for Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representative*s, seeking "preliminary comment [on] a regulation to apply a fiduciary conduct standard on broker-dealers, agents, investment advisers, and investment adviser representatives when dealing with their customers and clients, respectively. We later reported in SAA 2019-30 (Aug. 7) that the comment period closed **July 26**, with over 50 comments posted on the Division's Website (*ed: see #30-02 for our analysis of the letters).* Secretary Galvin on **November 29** issued a Press Release stating: "Secretary of the Commonwealth William F. Galvin, the state's chief securities regulator, signed off today on new regulations that would impose a uniform fiduciary conduct standard on broker-dealers, agents, investment advisers, and investment adviser representatives when dealing with their customers and clients in Massachusetts."

The Reg has now been published on the Division's Website. Here are some further details:

The Proposed Reg in a Nutshell

The Webpage states that the Reg would: "Deem it an unethical or dishonest conduct or practice for a broker-dealer, agent, investment adviser, or investment adviser representative registered or required to be registered in Massachusetts to fail

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to act in accordance with a fiduciary duty to any customer or client… and [r]evise certain paragraphs in 950 CMR 12.204 and 950 CMR 12.205 to make clear that the existing suitability standard still applies to any relationships or transactions expressly excluded from the fiduciary standard." The plain English description in the Release is: "The proposed fiduciary conduct standard would require financial professionals to treat their customers and clients with utmost care and loyalty. Financial recommendations and advice would be required to be based on what is best for the customers and clients, without regard to the interests of the broker-dealer, advisory firm, and its personnel. The conduct standard is based on the common law fiduciary duties of care and loyalty."

The Details…

The guts of the four-page proposed final Reg, which is available in clean and redline versions, is a new 950 CMR 12.207, titled *Fiduciary Duty of Broker-Dealers, Agents, Investment Advisers, and Investment Adviser Representatives,* which creates a "non-exclusive list of practices by a broker-dealer, agent, investment adviser, or investment adviser representative which shall be deemed 'unethical or dishonest conduct or practices' for purposes of M.G.L. c. 110A, § 204(a)(2)(G)." Readers can peruse the long list of expected and prohibited conduct, but the gist is to make unlawful: "Failing to act in accordance with a fiduciary duty to a customer or client when providing investment advice or recommending an investment strategy, the opening of or transferring of assets to any type of account, or the purchase, sale, or exchange of any security, commodity, or insurance product." How is the duty defined? Says the proposed Reg: "The duty of care requires a broker-dealer, agent, investment adviser, or investment adviser representative to use the care, skill, prudence, and diligence that a person acting in a like capacity and familiar with such matters would use, taking into consideration all of the relevant facts and circumstances. For purposes of this paragraph, a broker-dealer, agent, investment adviser, or investment adviser representative shall make reasonable inquiry…."

Is there a Preemption Risk?

Although States are primary regulators of IAs with assets under management of less than $100 million, every time we've reported on State efforts to move ahead with their own fiduciary rules or laws, we've queried the potential preemptive effect of the SEC's Regulation Best Interest, which was finalized **July 2019**. Reg BI addresses this issue directly: "We note that the preemptive effect of Regulation Best Interest on any state law governing the relationship between regulated entities and their customers would be determined in future judicial proceedings based on the specific language and effect of that state law. We believe that Regulation Best Interest, Form CRS, and the related rules, interpretations and guidance that the Commission is concurrently issuing will serve as focal points for promoting clarity, establishing greater consistency in the level of retail customer protections provided, and easing compliance across the regulatory landscape and the spectrum of investment professionals and products." A footnote observes that "the preemptive effect on any state law would be determined in future judicial proceedings, and would depend on the language and operation of the particular state law at issue." On the other hand, the introduction seems to recognize that the States have some room to maneuver: "We emphasize that Regulation Best Interest is separate from any common law analysis of whether a broker-dealer has fiduciary duties."

*(ed: *Dates for the public hearing and comment period "will be announced at a later time." **Massachusetts is following the leads of Connecticut, Maryland, Nevada, and New Jersey, which have moved on establishing State fiduciary standards.)*
(SAC Ref. No. 2019-47-03)

VERY FEW COMMENTS ON FINRA's PROPOSED INACTIVE INDUSTRY PARTY ARBITRATION RULE. ***The comment period closed December 13th on FINRA's proposed rule to expand a customer's arbitration options when firms or APs become inactive, with just a few comments, all supportive but with most urging further steps be taken.*** We reported in SAA 2019-42 (Nov. 6) that FINRA had filed proposed rule, SR-FINRA-2019-027, on **November 5**, and in SAA 2019-44 (Nov. 20) that the SEC on **November 13th** had released that proposal for public comment in SEC Rel. No. 34-87557. This proposal, which would amend the FINRA *Code of Arbitration Procedure for Customer Disputes*, in order to "...Expand the Options Available to Customers if a Firm or Associated Person is or Becomes Inactive," was first floated in an **October 2017** Reg Notice, Regulatory Notice 17-33, after FINRA Board approval in **May 2017**. As the name implies, the proposal is aimed at expanding the customer's options when an industry party becomes inactive before or during a case. It is an added measure for reducing the incidence of unpaid Awards. As reported in SAA 2019-45 (Nov. 27), the proposal was published **November 22** in the *Federal Register* (Vol. 84, No. 226, Page 64581), making comments due **December 13**.

The Basics

Under the new proposed rule, customers with claims against inactive parties would be provided additional options in an expanded set of situations "where a firm becomes inactive during a pending arbitration, or where an associated person becomes inactive either before a claim is filed or during a pending arbitration." In those situations, the customer would have the option to amend the pleadings, as under the current rule, and also to postpone the proceedings, request default proceedings, or to withdraw the claims and receive a refund of the filing fees. Under the new provisions, the customer would also have the option to proceed in court, *rather than* filing a FINRA claim. FINRA would now advise the customer of the inactive party's "status change" and the customer would have 60 days to withdraw the claim "with or without prejudice." *(ed: why would one withdraw the complaint "with prejudice"? Doesn't this option just create confusion?)*

More Specifics on Customer Options

If the customer does not withdraw, FINRA believes that s/he

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should be able to adjust strategy based on the status change news. Although Rule 12309 will not permit the adding of parties between ranking and appointment stages, customers in this situation will have that privilege. Similarly, the customer may amend a pleading during a 60-day window from notification. Rule 12601 does not permit postponements without arbitrator approval, absent mutual agreement; here, customers will have the right to postpone, if the notification of the status change comes within 60 days prior to hearing. Finally, the right to default proceedings under Rule 12801 will be broadened under a technical change, so that any terminated associated person who fails to file an answer will trigger the request privilege.

Comments: Few, Supportive, But Most Say More Can be Done

Just five comments were posted on the Commission's Website as of the comment period's close on **December 13**. All were supportive, and four recommended additional investor protections. We commented in #44 that "it will be interesting to see if NASAA comments in its usual 'this is a good step, but more can be done' fashion." No NASAA comment has appeared, but the three institutional commenters – PIABA, SIFMA, and the Financial Services Institute – generally support the proposed rule but urge that more be done. Footnotes have been omitted.

PIABA: "PIABA supports the amendments contemplated in SR-FINRA-2019-027 (hereinafter 'the Notice') that expand options for customers in pursuing and attempting to collect money awarded to them against industry respondents in arbitration proceedings. However, as set forth below, PIABA believes that the proposed rule changes set forth in the Notice are insufficient to remedy the longstanding problem of unpaid arbitration awards, which disproportionately involve customer claims against inactive FINRA members and associated persons." The suggested changes (*presented essentially* verbatim)? Expand Customers' Ability to Withdraw Claims Without Prejudice and Amend Claims; Expand Customers' Ability to Adjourn Hearings and Obtain Refunds of Filing Fees; Streamline Default Proceedings; Do More to Solve the Problem of Unpaid Arbitration Awards (The letter concludes: "PIABA urges FINRA to establish a national investor recovery pool. While PIABA supports every measure taken to address the serious unpaid award problem, we reiterate our concern that FINRA's current proposal will not address in a meaningful way the millions of dollars in unpaid awards that make a mockery of FINRA arbitration as a means of recovering investor losses").

SIFMA: "SIFMA's support is predicated on FINRA's stated purpose of the Proposal – namely, to facilitate 'dealing with those member firms or associated persons who are responsible for most unpaid awards – firms and associated persons who are no longer in business either at the time the claim is filed or at the time of the award.' We agree that the Proposal would probably help address the issue of unpaid arbitration awards. To that end, to better achieve the purpose of the Proposal (i.e., help address unpaid arbitration awards), we recommended that the Proposal be expanded to apply not only to customer cases but also to intra-industry Cases."

Financial Services Institute: "FSI largely supports the Proposed Amendments as set forth in the Notice and the corresponding rule text.... However, as discussed more fully below, FSI is concerned that certain aspects of the Proposed Amendments have the unintended consequence of creating an unbalanced arbitration process and we make suggestions to address that concern." The letter raises the following concerns (*ed: presented essentially* verbatim): 1) The Proposed Amendments Are Not Likely to Address the Issue of Unpaid Arbitration Awards, But Instead Create an Imbalance in the Arbitration Process. 2) Amending Pleadings to Add Parties Should Be Subject to the Arbitration Panel's Approval.

Individual Commenters

Comments were also received from two individuals, **Steven B. Caruso**, Esq., Maddox, Hargett & Caruso, PC, and Professor **Benjamin P. Edwards** of the University of Nevada, Las Vegas William S. Boyd School of Law (in his individual capacity). Mr. Caruso's letter supports the proposed change without qualification. Professor Edwards supports the changes, but is also harshly critical of its shortcomings: "The proposal simply does not do enough to address the problem. It does not recognize that the industry bears collective responsibility for allowing the business practices that result in unpaid awards. With FINRA unwilling to meaningfully address the problem through its own initiative, the Commission should require FINRA to propose meaningful reforms. Ultimately, self-regulation will only succeed if the Commission requires the self-regulating brokerage industry to somehow internalize the cost of unpaid awards. If the industry were liable for the harms it generates, it would have a more meaningful incentive to police its own conduct."

*(ed: *Wonder if FINRA's response to comments will commit to further changes? **As we've noted before, the rule filing presumes throughout that any PDAA exercised by an inactive party will be invalidated by virtue of the inactivity -- so, for instance, the customer can now go to court. Actually, FINRA can't invalidate a PDAA. FINRA is "jawboning" a bit here; it can only deny its forum. It's perfectly feasible that a court might compel arbitration at an alternative forum under FAA section 5, for instance.) ***Professor Edwards attached to his letter his article,* The Dark Side of Self-Regulation, *85 U. CIN. L. REV. 573 (2017). ****We expected NASAA to comment and append its newly issued Report,* NASAA Broker-Dealer Section E&O Insurance Survey Report *(see below). *****What's next? Staff will analyze the comments and then send to the SEC a formal "response to comments" letter.)* (SAC Ref. No. 2019-48-01)

NASAA's "E&O INSURANCE SURVEY" MAKES CASE FOR E&O INSURANCE AS A TREATMENT FOR UNPAID AWARDS. ***Calling it a "key focus for the***

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North American Securities Administrators Association," NASAA's Broker-Dealer Section reports, in a 10-page Study released on December 11, 2019, that the problem of unpaid arbitration awards has led it to survey the economic and practical feasibility of E&O insurance coverage for FINRA members. That coverage for "errors and omissions" is too expensive and impractical to constitute a viable solution to the incidence of unpaid arbitration awards, particularly with respect to smaller broker-dealers, has been the stock reaction and repeated response to this suggested fix in the past. The Broker-Dealer Section and its Market Integrity and Regulatory Policy and Review Project Group decided to test the proposition.

To approach the problem in a deliberate way, the Section undertook to survey the frequency with which broker-dealers carry E&O insurance currently and the range in scope of policy coverage. The central objective aimed at finding the incidence of E&O insurance and how often it has paid awards or settlements in arbitration. The Report's findings: "[T]he survey results reveal that the majority of the responding firms had E&O insurance and that their policies have paid claims. Further, the results of the survey contradict the blanket assertion that E&O insurance is too expensive or too difficult."

The 64 firms in NASAA's survey were selected based on size and geographic location; small and mid-sized firms constituted 74% of the respondents of those surveyed. Among the small firms, 40% were not covered by E&O insurance, yet only 4% of that 40% cited cost as the reason for non-coverage. One firm specializing in the sale of Direct Participation Programs stated that insurance coverage was unavailable to it, while another, specializing in the sale of government securities, reasoned that it had never had a claim against it. Premium costs varied widely among the survey group, with the lowest premium falling under $4,000, another at $10,000, 17% claiming premium costs of $100,000 or more, and 4% claiming premiums exceeding $1 million. Four examples provided by NASAA reflected annual premiums constituting about 7%, 10%, 12%, and 30% of net capital. The data, according to the Report, show that "firms can obtain some measure of coverage at a reasonable cost."

NASAA also found that a surprising number (28) of insurance carriers offer E&O insurance to the sample and that the business was "evenly spread" -- not concentrated among a select few providers. Coverage limitations were also studied. Examples of exclusions from coverage were claims relating to fraud, alternative products, and unapproved securities activities. Some policies excluded specific reps from coverage, presumably to reduce premiums. Finally, the survey collected information about payouts by carriers; for instance, 23% of the firms reported at least one claim payout during the most recent coverage year, covering both claims filed and customer complaints that did not reach the filing stage. Whether any claims were refused coverage by the carrier was not specifically indicated, but NASAA does comment that "covered claims are generally being paid."

Summing up, NASAA states its primary conclusion that "small firms included in the survey could obtain E&O insurance at a reasonable cost." The Report's authors opine further that E&O insurance might help assure payments for some investors successful in arbitration. But, they also concede that, "because E&O insurance may not necessarily address awards against inactive firms or claims involving fraud or other excluded conduct, it is not a complete solution to the problem of unpaid arbitration awards."
*(ed: *NASAA does not cite the claims by FINRA that it too studied the feasibility of E&O insurance coverage for arbitration awards and found required coverage an imprudent proposition, but this Report clearly aims a shot across FINRA's bow with its findings that coverage is available, that it's not prohibitive in cost (in NASAA's view), and that, practically speaking, while fraud claims are commonly excluded from coverage, insurance carriers generally pay out when claims are made. **On this last point, we admit some discomfort with the Report's failure to deal with denied coverage and with the glib observation that "covered" claims are generally paid." Of course, covered claims are paid!! ***FINRA statistics, quoted in the Report, indicate that unpaid awards can be attributed to firms that were "inactive" at the time of the relevant arbitration filing 8-39% of the time and to individuals who were "inactive" at the time of filing 21-52% of the time. Such Respondents in arbitration would not have active insurance coverage, but, perhaps, some percentage of those becoming "inactive" during the arbitration would remain active, if E&O coverage were present, and, certainly, if coverage applied, fewer firms and individuals would be barred for non-payment. ****NASAA makes this observation in fn. 3 of the Report: "How this issue [of non-payment to successful clients in arbitration] relates to investment advisers is an area for further review." We would hope that "further review" would be hastened by the fact that NASAA's state regulators bear primary regulatory authority over nearly 18,000 RIAs. Would it not be a bold and persuasive move for the states to lead by example and demonstrate the effectiveness of E&O coverage in solving the problem of unpaid awards by imposing that requirement in a regime over which they have control and responsibility?)*
(SAC Ref. No. 2019-48-02)

SEC's OCIE RELEASES 2020 EXAM PRIORITIES – ARBITRATION AGAIN NOT ON THE LIST. The SEC's Office of Compliance Inspections and Examinations ("OCIE") issued its exam priorities for 2020. Once again, the Authority's dispute resolution program isn't mentioned. The 22-page OCIE Report issued January 7 announces several key exam priority categories (repeated verbatim): 1) Retail Investors, Including Seniors and Those Saving for Retirement; 2) Market Infrastructure; 3) Information Security; 4) Focus Areas Relating to Investment Advisers, Investment Companies, Broker-Dealers, and Municipal Advisors; 5) Anti-Money Laundering Programs; 6) Financial Technology (Fintech) and Innovation, Including Digital Assets and Electronic Investment Advice; and 7) FINRA and MSRB.

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Specific Priorities

SEC Chair Jay Clayton says in the Release: "OCIE's 2020 examination priorities identify key areas of risk, both existing and emerging, that we expect self-regulatory organizations (SROs), clearing firms, investment advisers and other market participants to identify and mitigate. I applaud OCIE's thoughtful, strategic and efficient focus, which is critical to the fulfillment of the SEC's mission and our service to Main Street investors." The specific priorities within the main categories are nicely summarized in a Press Release issued along with the Report (excerpted here verbatim):

Retail Investors, Including Seniors and Those Saving for Retirement: OCIE will continue its focus on the protection of retail investors, including the various intermediaries that serve and interact with retail investors and the investments marketed to, or designed for, retail investors.

Market Infrastructure: OCIE will continue its focus on entities that provide services critical to the functioning of our capital markets, including clearing agencies, national securities exchanges, alternative trading systems, and transfer agents. Particular attention will be focused on the security and resiliency of entities' systems.

Information Security: OCIE will continue to prioritize cyber and other information security risks across the entire examination program.

Focus Areas Relating to Investment Advisers, Investment Companies, Broker-Dealers, and Municipal Advisors: OCIE will continue its risk-based examinations for each type of these registered entities. In particular, examinations of registered investment advisers (RIAs) will focus on RIAs that have never been examined, including new RIAs and RIAs registered for several years that have yet to be examined…. Municipal advisor examinations will include review of registration and continuing education requirements and municipal advisor fiduciary duty obligations to municipal entity clients.

Anti-Money Laundering Programs: OCIE will continue to review for compliance with applicable anti-money laundering (AML) requirements, including whether entities are appropriately adapting their AML programs to address their regulatory obligations.

Financial Technology (Fintech) and Innovation, Including Digital Assets and Electronic Investment Advice: OCIE recognizes that advancements in financial technologies, methods of capital formation and market structures, as well as registered firms' use of new sources of data (often referred to as "alternative data"), warrant ongoing attention and review. OCIE also will continue to identify and examine SEC-registered firms engaged in the digital asset space, as well as RIAs that provide services to clients through automated investment tools and platforms, often referred to as "robo-advisers."

FINRA and MSRB: OCIE will continue its oversight of the Financial Industry Regulatory Authority (FINRA) by focusing examinations on FINRA's operations, regulatory programs, and the quality of FINRA's examinations of broker-dealers and municipal advisors. OCIE will also continue to examine the Municipal Securities Rulemaking Board (MSRB) to evaluate the effectiveness of its operations and internal policies, procedures, and controls.

And Arbitration?

As in recent years, arbitration is again not listed as a priority this year, although it is mentioned in passing on page 21 where the Report describes FINRA at a high level: "In addition, FINRA, among other things, provides a forum for securities arbitration and mediation…." Perhaps OCIE intends to examine the Office of Dispute Resolution where the Report states: "OCIE conducts risk-based oversight examinations of FINRA. It selects areas within FINRA to examine through a risk assessment process designed to identify those aspects of FINRA's operations important to the protection of investors and market integrity."

*(ed: *As usual, OCIE warns that the list is not exhaustive and that priorities may change as the year unfolds. **Last year's Report was just 12 pages long, and was referred to as a "Letter." ***FINRA's regulatory priories were announced January 9 and are analyzed directly below.)* (SAC Ref. No. 2020-02-01)

FINRA RELEASES 2020 RISK MONITORING AND EXAM PRIORITIES. KEY FOCUS IS ON REG BI. ARBITRATION AGAIN NOT ON THE LIST. FINRA announced its 2020 risk monitoring and exam priorities in a 15-page Risk Monitoring and Examination Priorities Letter, focusing heavily on Regulation Best Interest implementation. We report above that the SEC's Office of Compliance Inspections and Examinations ("OCIE") on January 7 issued its exam priorities for 2020. The 22-page OCIE Report issued January 7 announces several key exam priorities. Weighing in January 9 with some overlapping objectives is FINRA.

Focus on Reg BI

The Press Release, FINRA Releases 2020 Risk Monitoring and Examination Priorities Letter, announces: "New for this year is a focus on Regulation Best Interest (Reg BI) and Form CRS (Client Relationship Summary). In the first part of the year, FINRA will review firms' preparedness for Reg BI to gain an understanding of implementation challenges they may face. After the June 30, 2020 compliance date, FINRA will examine firms' compliance with Reg BI, Form CRS and related U.S. Securities and Exchange Commission guidance and interpretations." The Letter lists several areas of inquiry (ed: repeated verbatim):

- Does your firm have procedures and training in place to assess recommendations using a best interest standard?
- Do your firm and your associated persons apply a best interest standard to recommendations of types of accounts?

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- If your firm and your associated persons agree to provide account monitoring, do you apply the best interest standard to both explicit and implicit hold recommendations?
- Do your firm and your associated persons consider the express new elements of care, skill and costs when making recommendations to retail customers?
- Do your firm and your associated persons consider reasonably available alternatives to the recommendation?
- Do your firm and your registered representatives guard against excessive trading, irrespective of whether the broker-dealer or associated person "controls" the account?
- Does your firm have policies and procedures to provide the disclosures required by Reg BI?
- Does your firm have policies and procedures to identify and address conflicts of interest?
- Does your firm have policies and procedures in place regarding the filing, updating and delivery of Form CRS?

Other Focus Areas

The Press Release lists several other focus areas, which we repeat verbatim: Communications with the public, with a focus on private placement retail communications and communications via digital channels; cash management and bank sweep programs; direct market access controls; best execution; disclosure of order routing information; and Cybersecurity. The Letter adds that FINRA will "continue to review for firms' compliance in consistently important areas such as systems for supervision, sales practice risks, anti-money laundering and fraud, insider trading and manipulation across markets and products," and cautions that focus areas may evolve over the year.

Arbitration Again Doesn't Make the Cut

In 2017, the Office of Dispute Resolution ("ODR") was included in FINRA's regulatory priorities for the first time in three years. That was not the case this year, nor the two prior years. That's not necessarily a bad thing; if there were perceived problems with the program, we're sure it would be a focus area.

(ed: *Kudos again to FINRA for letting firms (and investors) know on what areas the Authority intends to focus. This year marks the Letter's 15th anniversary. **FINRA invites comments or suggestions on how it can improve the Priorities Letter. Send to: Steven Polansky, Member Supervision, at Steven.Polansky@finra.org. or Elena Schlickenmaier, Member Supervision, at Elena.Schlickenmaier@finra.org.) (SAC Ref. No. 2020-02-02)

BUSINESS GROUPS' CHALLENGE TO NEW CALIFORNIA LAW RESTRICTING EMPLOYMENT PDAA USE AND ENFORCEMENT. ***A coalition of business groups filed suit to prevent the planned January 1, 2020 effectiveness of California AB-51, which essentially bans mandatory arbitration of employment discrimination, sexual harassment, and wage law disputes.*** We reported in SAA 2019-40 (Oct. 23) that Governor **Gavin Newsom** last fall signed AB-51. The new law doesn't expressly bar predispute arbitration agreements ("PDAA"), but amends California Labor Code section 432.6(a) to provide: "A person shall not, as a condition of employment, continued employment, or the receipt of any employment-related benefit, or as a condition of entering into a contractual agreement, require any applicant for employment or any employee to waive *any right, forum, or procedure* for a violation of any provision of the California Fair Employment and Housing Act (Part 2.8 (commencing with Section 12900) of Division 3 of Title 2 of the Government Code) or this code, including the right to file and pursue a civil action or a complaint with, or otherwise notify, any state agency, other public prosecutor, law enforcement agency, or any court or other governmental entity of any alleged violation" (emphasis added). The statute also provides that an employer can't "threaten, retaliate or discriminate against, or terminate" an employee or job applicant who refuses to consent to waiver.

Preemption Avoidance Carveouts?

The statute has some carveouts seemingly included to avoid Federal Arbitration Act ("FAA") and federal securities acts preemption. From its introduction, the bill has had an SRO carveout: "This section does not apply to a person registered with a self-regulatory organization as defined by the Securities Exchange Act of 1934 (15 U.S.C. Sec. 78c) or regulations adopted under that act pertaining to any requirement of a self-regulatory organization that a person arbitrate disputes that arise between the person and his or her employer or any other person as specified by the rules of the self-regulatory organization." And the law provides that nothing contained in it "is intended to invalidate a written arbitration agreement that is otherwise enforceable under the Federal Arbitration Act (9 U.S.C. Sec. 1 et seq.)." Last, it does not invalidate existing PDAAs; it goes into effect **January 1, 2020**, for "contracts for employment entered into, modified, or extended" on or after that date. There are both civil and criminal penalties for violations.

The Legal Challenges Asserted

The suit, *Chamber of Commerce of the United States v. Becerra*, No. 2:19-at-01142 (E.D. Calif. Dec. 6, 2019), seeks declaratory and injunctive relief based on FAA preemption, specifically: "AB 51's limits on arbitration agreements conflict with federal law. Those limits are therefore preempted and invalid under the Supremacy Clause of the Constitution of the United States. Accordingly, Plaintiffs respectfully request that the Court (1) grant a declaratory judgment that AB 51 is invalid with respect to all arbitration agreements governed by the FAA and (2) issue an order permanently enjoining Defendants from enforcing it with respect to such arbitration agreements." The complaint brushes off the carveouts, focusing especially on the law's chilling effect on arbitration agreement use: "AB 51 singles out arbitration for disfavored treatment by imposing special restrictions on the formation of arbitration agreements, which do not apply to other types of contracts, and limit the ability of employers and workers to enter arbitration

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agreements. These requirements are not generally imposed to enter other provisions in employment contracts. Indeed, employers routinely condition employment on acceptance of other contractual terms.... AB 51 thus conflicts with --and also stands as an obstacle to -- Congress's objectives in enacting the FAA. It is therefore preempted."
*(ed: The other Plaintiffs are the California Association for Health Services at Home, the California Chamber of Commerce, the California Retailers Association, the Home Care Association of America, and the National Retail Federation. **The Court did issue the requested TRO and exrtended that TRO through the end of January, in prepration for preliminary injunctive hearings.)* (SAC Ref. No. 2019-48-03)

EEOC GIVES UP THE GHOST ON ANTI-ARBITRATION POLICY. ***The EEOC has formally rescinded a Clinton-era policy against mandatory arbitration of workplace discrimination claims.*** The Commission in 1997 issued a policy statement, *Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment,* stating: "The United States Equal Employment Opportunity Commission (EEOC or Commission), the federal agency charged with the interpretation and enforcement of this nation's employment discrimination laws, has taken the position that agreements that mandate binding arbitration of discrimination claims as a condition of employment are contrary to the fundamental principles evinced in these laws…. The use of unilaterally imposed agreements mandating binding arbitration of employment discrimination disputes as a condition of employment harms both the individual civil rights claimant and the public interest in eradicating discrimination. Those whom the law seeks to regulate should not be permitted to exempt themselves from federal enforcement of civil rights laws. Nor should they be permitted to deprive civil rights claimants of the choice to vindicate their statutory rights in the courts -- an avenue of redress determined by Congress to be essential to enforcement" (Policy no. 915.002, July 10, 1997).

SCOTUS Begged to Differ
In the more than two decades since the policy was adopted, the Supreme Court has made clear not only that there is a strong federal policy in favor of arbitration, but that employment claims – even statutory ones – may be the subject of mandatory predispute arbitration agreements. The Commission on **December 17** issued *Recission of Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment*, formally abrogating its 1997 policy "that had disapproved of the practice of requiring workers to enter into arbitration agreements to resolve workplace discrimination claims and instructed its staff to proceed with claims against employers despite the existence of such agreements." Why the change in policy? Says the EEOC: "Since its issuance, the Supreme Court has ruled that agreements to arbitrate employment-related disputes are enforceable under the Federal Arbitration Act (FAA) for disputes between employers and employees. *Circuit City Stores v. Adams*, 532 U.S. 105 (2001). In other arbitration-related cases it has decided since 1997, the Court rejected concerns with using the arbitral forum - both within and outside the context of employment discrimination claims. Those decisions conflict with the 1997 Policy Statement."

The Bottom Line: PDAAs are OK
The *Rescission Statement* has a long list of Supreme Court cases backing up its assertion, with the result that "the *Policy Statement on Mandatory Binding Arbitration* does not reflect current law, is rescinded, and should not be relied upon by EEOC staff in investigations or litigation." Citing *EEOC v. Waffle House, Inc.*, 534 U.S. 279 (2002), however, the revised policy notes that nothing therein "should be construed to limit the ability of the Commission or any other party to challenge the enforceability of a particular arbitration agreement."
(ed: As we said in SAA 2019-48, it's about time. We've had a hard time understanding how the EEOC, "the federal agency charged with the interpretation and enforcement of this nation's employment discrimination laws," could take a position contrary to those laws as defined by SCOTUS.) (SAC Ref. No. 2020-01-02)

ORAL ARGUMENT FOR CFPB-SEILA LAW SET FOR MARCH 3. SCOTUS has set March 3 as the date for oral argument in a case that will determine whether the Consumer Financial Protection Bureau's ("CFPB") structure is constitutional. The decision will resolve a split in the Circuits. As we reported in SAA 2019-40 (Oct. 23), SCOTUS on October 18 agreed to review *Consumer Financial Protection Bureau v. Seila Law LLC,* 923 F.3d 680 (9th Cir. May 6, 2019), a case dealing with the constitutionality of the CFPB's structure. There is currently a split in the Circuits on this issue (see our analysis in SAA 2018-36 (Sep. 26)).

Case Below
Alert readers may recall *PHH Corporation v. Consumer Financial Protection Bureau,* 881 F.3d 75 (D.C. Cir. 2018), where the *en banc* Circuit Court upheld the constitutionality of the CFPB's structure. That decision reversed *PHH Corporation v. Consumer Financial Protection Bureau,* 839 F.3d 1 (D.C. Cir. 2016), where a divided panel had held that the CFPB's structure, which has a single Director with virtually unlimited, unchecked authority, was unconstitutional (see our analysis in SAA 2018-05 (Jan. 31)). *PHH* was based in large part on *Humphrey's Executor v. United States,* 295 U.S. 602 (1935), where SCOTUS held that FTC commissioners could be removed only for "inefficiency, neglect of duty, or malfeasance in office," and, to a lesser extent, on *Morrison v. Olson,* 487 U.S. 654 (1988). Seeing "no need to re-plow the same ground," the Ninth Circuit, as we reported in SAA 2019-19 (May 15), unanimously adopted the *PHH* holding in *Seila Law*: "In short, we view *Humphrey's Executor* and *Morrison* as controlling here. Those cases indicate that the for-cause

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removal restriction protecting the CFPB's Director does not 'impede the President's ability to perform his constitutional duty' to ensure that the laws are faithfully executed…. The Supreme Court is of course free to revisit those precedents, but we are not."

Issue before the Court

And revisit SCOTUS shall. As we reported in SAA 2019-27 (Jul. 17), Seila Law on June 28 Petitioned the Court for *Certiorari*. The issue framed was: "Whether the vesting of substantial executive authority in the Consumer Financial Protection Bureau, an independent agency led by a single director, violates the separation of powers." The Court's Order granting *Certiorari* directs the parties to "brief and argue the following question: If the Consumer Financial Protection Bureau is found unconstitutional on the basis of the separation of powers, can 12 U.S.C. §5491(c)(3) be severed from the Dodd-Frank Act?" SCOTUS has posted its February-March oral argument calendar showing the case now set for argument on March 3.

*(ed: *The SCOTUS case is captioned* Seila Law LLC v. Consumer Financial Protection Bureau, *No. 19-7. **Many* Amici *Briefs have already been filed, including one from the House of Representatives.)* (SAC Ref. No. 2019-47-02)

SHORT BRIEFS:

FINRA ISSUES FAQ ON RULE 2081 AND EXPUNGEMENTS. FINRA already has published *Expanded Expungement Guidance*, and an FAQ on Rule 2080. We noticed a **November 22** Website posting, *Prohibited Conditions Relating to Expungement of Customer Dispute Information FAQ,* focusing on Rule 2081. This Rule provides: "No member or associated person shall condition or seek to condition settlement of a dispute with a customer on, or to otherwise compensate the customer for, the customer's agreement to consent to, or not to oppose, the member's or associated person's request to expunge such customer dispute information from the CRD system." Here are the four questions and the one-word answers (*ed: for further elaboration, consult the FAQ*): 1) **Is there a rule that addresses prohibited conditions relating to expungement of customer dispute information?** Yes. 2) **Does FINRA Rule 2081 apply only to settlements?** No. 3) **If I (or my employer) do not pay money or provide other consideration to a customer, can the parties' agreement to resolve a customer dispute include a provision that the customer consents to or does not oppose a request for expungement relief without violating FINRA Rule 2081?** No. 4) **Does an agreement, reached at any time, to release a customer from claims in exchange for the customer's agreement to consent to, or not to oppose, an expungement request violate FINRA Rule 2081?** Yes.

*(ed: *Clarity is good. **The FAQ refers readers to Regulatory Notice 14-31 for further info.)* (SAC Ref. No. 2019-46-04)

RADVOCATE ISSUES 3Q REPORT ON CONSUMER ARBITRATION: 1,500 CASES CONCLUDED, TAKING ABOUT 9 MONTHS. MOST SETTLE. The online consumer rights service Radvocate has published a report on consumer arbitration at AAA and JAMS for the third quarter. The data-filled **November 12** Report, *Latest Data: Consumer Claims Sent to Private Courts take 9 months to Resolve; Most Settled in Secret,* offers interesting but not surprising data (*ed: repeated essentially* verbatim): 1) a 25% increase in consumer claims resolved … [but] still, fewer than 1,500 claims (1,483) were processed in the quarter; 2) telecom & financial companies continue to face the most consumer claims (*ed: among the latter were American Express, Citibank; Credit One Bank; and Wells Fargo*); 3) most consumer claims (60.7%) were settled; 4) consumers mostly lost their arbitration claims (71% of "cases with final rulings:; 91% of "all cases not settled between the parties"); and 5) arbitration claims took an average of nine months to resolve. However, for claims that resulted in a final ruling (an award or dismissal), the average process took 11 months for the AAA and nearly 15 months for JAMS.

*(ed: *These results are not surprising; the stats are consistent with those provided to Congress recently by tech leaders; see the November 26 story in* The American Prospect, *"Tech Companies' Big Reveal: Hardly Anyone Files Arbitration Claims." **Of course FINRA's stats show a higher investor "win rate." ***Radvocate defines its role as follows: "Radvocate simplifies the process for consumers to resolve disputes with large corporations. We help you produce an official legal notice to the company, and then navigate to achieve a successful resolution of your complaint. If your complaint is not successfully resolved in a certain amount of time, we can also help bring your claim to an independent decision-maker through the consumer arbitration system.")* (SAC Ref. No. 2019-46-11)

SAVE THE DATE: NYSBA's "SECURITIES ARBITRATION 2020" PROGRAM IS MARCH 6. The New York State Bar Association will be holding *Securities Arbitration 2020: Deep Dive*, live and via Webcast, on **March 6th.** The program description says: "Trust established and trust breached. That is at the heart of almost every customer securities arbitration of merit that arbitrators must resolve. With the 'forum of equity' being supplanted by the 'forum of law,' how do practitioners get arbitrators to look beyond the law to the reality of the relationships between customers and financial advisers? How have FINRA's cases over the years reflected the different ways in which trust relationships were breached? How has the transition from transactional disputes to fiduciary advisory cases affected the kinds of cases brought? How can attorneys defend elder abuse, affinity fraud cases and other 'indefensible' conduct? How can aggressive discovery make or break a case? Ethical issues when customer attorneys solicit potential clients on the Internet and when defense attorneys represent brokerage firms and brokers in the same case?" The all-day seminar features an all-star faculty, moderated by co-chairs **David E. Robbins**, Esq., of Kaufmann Gildin & Robbins LLP, and **James D. Yellen,** Esq., of Yellen Arbitration & Mediation Services, and including **Richard Berry** and **Manly Ray** from FINRA. The program qualifies

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for 7.0 MCLE Credits (4.0 Skills; 2.0 Areas of Professional Practice; and 1.0 Ethics.) *(ed: *The seminar runs from 9:00 am - 4:45 pm Eastern, and will take place at Convene, 810 Seventh Avenue in Manhattan and will be Webcast. **Registration, which can be done online, ranges from $170 for NYSBA Commercial and Federal Litigation Section members to $195 for NYSBA members, to $295 for non-members.)* (SAC Ref. No. 2019-47-11)

FINRA BOARD APPROVES CHAIR ARBITRATOR HONORARIA INCREASES. We reported in SAA 2019-46 (Dec. 4) that FINRA's Board of Governors would be meeting **December 4-5**, and that the Agenda stated "the Finance, Operations and Technology Committee will review proposed amendments to the Codes of Arbitration Procedures to increase certain arbitration fees..." As usual, the description was somewhat cryptic, so we said "the specific fees being increased and by what amount will have to await the post-meeting memo and press release." "While the December 13th post-meeting memo from President and CEO **Robert W. Cook** and accompanying brief video and press release don't refer to the subject, we did some sleuthing and can report ..." that the Board has authorized staff to do a rule filing with the SEC increasing certain Chairperson honoraria. Readers may recall that, in SAA 2019-39 (Oct. 16), we reported on the Practising Law Institute's ***Securities Arbitration 2019*** program that took place in New York on **September 10th**. In describing FINRA-ODR Chief **Richard Berry's** remarks, we said: "Look for a raise in the Chair honorarium, relative to chairing IPHCs and the merits hearing. The Chair's hearing sur-payment could double." A FINRA spokesperson informs us that the Board indeed approved a proposal to increase the Chairperson honorarium for hearings on the merits from $125 to $250 per day (in addition to the standard $300 per session honorarium). It would also for the first time provide for a Chairperson honorarium of $125 for prehearing conferences (in addition to the standard $300 one-session honorarium). *(ed: *This is good news! $850 a day – $600 for two sessions plus $250 – is decent compensation, and the "extra" for IPHCs is fair. **FINRA has posted on its Website a nice FAQ on Chairperson honoraria. ***While the full 2020 schedule is not yet posted, the Website shows that the next meetings will take place March 11-12 and June 10-11. ****Our thanks to FINRA for answering our inquiry.)* (SAC Ref. No. 2019-48-06)

BUDGET DEAL MAINTAINS OBAMA-ERA REG BANNING SOME FEDERAL CONTRACTORS FROM REQUIRING ARBITRATION OF TITLE VII CLAIMS. We reported in SAA 2017-13 (Apr. 5) that President Trump in **March 2017** had signed into law a bill nullifying an Obama-era Executive Order and regulation barring companies with federal contracts valued at over $1 million from mandating arbitration of Title VII or sexual harassment or assault claims. Exercising its authority under the Congressional Review Act ("CRA"), 5 USC §§ 801-808, Congress had retroactively nullified and disapproved the Fair Pay & Safe Workplaces rule issued in **August 2016** (81 Fed. Reg. 58562). We thought that was the last we would hear about the topic, because once a regulation is rescinded under the CRA, a like reg in "substantially the same form" cannot be promulgated thereafter unless specifically authorized by Congress. It appears Congress has so acted – again. We reported in SAA 2018-13 (Apr. 4) that, buried in the 2,000+ page appropriations bill, the *Consolidated Appropriations Act of 2018* (H.R. 1625), signed into law **March 2018** was language essentially resurrecting the old regulation. Specifically, section 8095(a) stated that "[n]one of the funds appropriated or otherwise made available by this Act may be expended for any Federal contract for an amount in excess of $1,000,000, unless the contractor agrees not to -- (1) enter into any agreement with any of its employees or independent contractors that requires, as a condition of employment, that the employee or independent contractor agree to resolve through arbitration any claim under title VII of the Civil Rights Act of 1964 or any tort related to or arising out of sexual assault or harassment, including assault and battery, intentional infliction of emotional distress, false imprisonment, or negligent hiring, supervision, or retention…" The law also prohibited enforcement of arbitration clauses in existing contracts. The identical language is maintained in the new budget deal for the fiscal year ending **September 30, 2020,** signed by President Trump on **December 20**; it now appears in section 8093 of the *Consolidated Appropriations Act of 2020* -- H.R. 1158. *(ed: As we've opined before, we fear this approach will take us back to the old "intertwining" days, with some employment claims being arbitrable and some not.)* (SAC Ref. No. 2020-01-05)

DID YOU KNOW? THE AAA HAS SURVEYED ARBITRATORS ON LARGE CASE PROCESS EFFICIENCY. Did you know that the AAA in **July 2019** published a report analyzing *arbitrator* perceptions on the efficiency and cost-effectiveness of their AAA cases closed by Award. Says a Press Release: "The study incorporates views on every step of the arbitration process from more than 400 arbitrators who issued awards for large and complex cases with at least $1 million in claims or counterclaims. In particular, arbitrators were asked how well case participants and counsel cooperated, and how well they handled discovery, motion practice, and other aspects of arbitration. Arbitrators also commented on factors which they felt contributed most to the delay or rising cost of cases, and best practices for avoiding cost increases and time delays during arbitration." Spoiler alert: discovery and motion practice are the key offenders.

DID YOU KNOW? SAC's WEBSITE HAD A RECORD YEAR IN 2019. SAC's Webpage, www.SACarbitration.com, just concluded a record year. Here are some stats (2018 numbers are in parentheses): number of visits – 184,723 (129,571), unique visitors – 78,777 (57,560); pages viewed – 3,263,930 (1,680,104); "hits" – 3,506,444 (1,837,829); bandwidth – 29.71 GB (17.23 GB). By far, the most visited area of our Website was SAC's Blog. By any measure, then, 2019 was a very good year!

ARTICLES

As a regular feature, SAC summarizes articles and case decisions of interest in the field of securities/commodities arbitration law. If you find one we missed or are involved in a case that produces an interesting decision, please write and send us a copy. ***As it is our objective to cover all relevant decisions, we will sometimes include decisions in the current "Articles & Case Law" section that issued a year or more ago. We also summarize unpublished decisions and orders. For these reasons, readers are cautioned to cite-check cases to assure they have not been overruled and may be cited in accordance with local court rules.*** **We thank our readers who have contributed court opinions and who, by their efforts, help us all to keep informed. Credit is given to contributors at the end of the relevant case summaries.**

STORIES CITED

An Investor's Guide to Financial Regulatory Groups, **U.S. News and World Report (Dec. 12, 2019):** "The US financial industry is regulated by a baker's dozen of organizations, each with its own area of oversight. They cover the gamut from the behemoth Federal Reserve to the lesser-known Office of Thrift Supervision, which regulates the U.S. savings and loan (aka thrifts) industry. While every regulator has an impact on our economy and monetary system, there are four that play the biggest role in regulating the securities industry. The four regulatory groups every investor should know about are: the Securities and Exchange Commission (SEC); the Financial Industry Regulatory Authority (FINRA); the North American Securities Administrators Association (NASAA); and the Commodity Futures Trading Commission (CFTC)."

Arbitration Panel Rules in Favor of Merrill Lynch on Racketeering Claim, by Alex Padalka, FinancialAvisor-IQ (Jan. 16, 2020): Former Merrill Lynch Manager and his wife filed FINRA arbitration complaint alleging RICO claims predicated upon an offshore scheme that violated the law and caused Claimants damages in terms of lost compensation, worthless stock options and stock losses. The FINRA Panel dismissed the claims, which related back to 2010 on six-year eligibility grounds and declined to extend the start date to 2014, when Claimants averred that, due to a $16.65 billion regulatory settlement by Bank of America, they first learned of the scheme.

Broker Who Claimed RBC Treated Her Like a "CA" Loses Arbitration, **AdvisorHub (Dec. 27, 2019):** "A former broker at RBC Wealth Management who claimed she was treated 'as a client associate and/or sales assistant instead of as a financial advisor' at a branch near Houston has lost her attempt to avoid paying the firm almost $227,000 on her promissory notes…. A three-person Finra arbitration panel in Houston on Thursday granted RBC's motion to dismiss her claims 'in their entirety' on the grounds that Ripoll and the firm had no agreement to resolve disputes in arbitration, according to an award statement published on Thursday."

Brokerage Industry Opposes Massachusetts Fiduciary Rule Proposal at Hearing - Investor-protection Advocates Don't Expect State to Water Down Measure, **InvestmentNews (Jan. 7, 2020):** "Brokerage and insurance industry representatives on Tuesday criticized a Massachusetts proposal that would impose fiduciary duty on all financial advisers in the state, but investor-protection advocates are confident the state won't back down under industry pressure."

Can a Robojudge Be Fair?, **Kluwer Arbitration Blog (Dec. 16, 2019):** "At the latest ODR Forum which was held on 29-31 October 2019 in Williamsburg, Virginia, Dr. Anyu Lee presented on China's vision of online dispute resolution…. He discussed how far China has progressed in developing artificial intelligence ('AI') tools for online courts, arbitration and mediation. He also described the potential of AI in resolving disputes and in particular mentioned that, cross-border small value dissatisfactions which are difficult to resolve at present could be resolved smoothly and efficiently in the near future through AI. Dr. Lee concluded his presentation by arguing that the only way forward is to have these small value cross-border cases decided by robojudges/roboarbitrators/robomediators, and have their resolutions enforced by a social credit system."

Elderly Investor Wins $2.6 Million from Indie Firm in Finra Arbitration, **AdvisorHub (Jan. 8, 2020):** "A FINRA arbitration panel has ordered National Planning Corp. to pay $2.6 million to an octogenarian customer who bought fraudulent promissory notes, non-traded real estate investment trusts (REITs) and other unsuitable investments on the recommendation of a now-imprisoned former broker. The award from three public arbitrators in St. Louis includes $1.58 million in compensatory damages, $1 million in punitive damages and almost $46,000 in costs, according to the award statement published on Tuesday. It did not explain the panel's reasoning or their relatively rare granting of punitive damages."

FINRA Preps for New "Best Interest" Obligations - New Conduct Standards Top SRO's Compliance Agenda, **Investment Executive (Jan. 9, 2020):** "The U.S. industry self-regulatory organization, the Financial Industry Regulatory Authority (FINRA), will be testing firms' readiness to adopt new 'best interest' standards. In a letter setting out its compliance priorities for the coming year, FINRA said that it will initially focus on firms' preparedness for the U.S. Securities and Exchange Commission's (SEC) new best interest rules, known as Reg BI, 'to gain an understanding of implementation challenges they face.' After the new requirements kick in by June 30 of this year, FINRA will turn to reviewing firms' compliance with Reg BI, and related SEC rules and guidance."

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ARTICLES & CASE LAW *cont'd from page 19*

ARTICLES CITED

(SAC scours the Web for scholarly articles on the law, as it relates to our mission, using such legal resources as Lexology, SSRN.com, Securities Law Prof Blog and Google Scholar.)

Arbitration with Uninformed Consumers, by Egan, Mark and Matvos, Gregor and Seru, Amit, Harvard Business School Finance Working Paper No. 19-046 (June 2019).

Federal Court Blocks California's Ban On Mandatory Arbitration Agreements, FisherPhillips Blog (Dec. 30, 2019).

NLRB Reinstates Arbitral Deferral Standard**,** by Fiona W. Ong Shawe Rosenthal (Dec. 30. 2019)**.**

Mandatory Securities Arbitration's Impermissiblility Under State Corporate Law: An Analysis of the Johnson & Johnson Shareholder Proposal, by Jacob Hale Russell, SSRN.com (Feb. 24, 2019).

Ninth Circuit Vacates Arbitration Award Based on Later-Discovered Information that Creates a Reasonable Impressiion of Bias, Baker McKenzie, Lexology (Jan. 16, 2020)

Resolving Discrimination Complaints in Employment Arbitration: An Analysis of the Experience in Securities Arbitration, by J. Ryan Lamare & David B. Lipsky, LR Review (Jan. 12, 2018).

SDNY: Directors Not Liable for Whistleblower Claims Under SOX, Proskauer Rose, Lexology (Jan. 15, 2020).

Supreme Court Declines to Rule on ERISA Standard for ESOP Cases, Skadden Arps, Lexology (Jan. 14, 2020).

The Anatomy of Securities Class Action in China: A Functional and Comparative Approach**,** by Huang, (Robin) Hui and Hailong, Li and Lin, Gavin Yao, 46(4) Securities Regulation Law Journal 365-402 (2018)**.**

The Underlying Underwriter: An Analysis of the Spotify Direct Listing, by Benjamin J. Nickerson, 86 U. Chi L. Rev. 985 (2019).

CASES

(ed: The court decisions summarized below are arranged by major subject heading first and digested in a single sentence. This enables readers to quickly refer to the courts or topics that are of key interest. The decisions are then arranged in alphabetical order by Plaintiff and summarized more fully. Bold-type headnotes are added to facilitate quick scanning for topics of interest or for sorting decisions by major issues. Generally speaking, these case synopses were originally prepared for SAC's other newsletter service, Securities Online Litigation Alert (SOLA: www.saclitigation.com) *which more broadly covers court decisions in litigation concerning BDs & RIAs since 2000. Where our synopses have been written by one of* SOLA*'s Contributing Editors, the author's first initial and last name appear at the end of the summary, often with analysis. We thank our* SOLA *Board of Contributing Legal Editors for their valuable work in creating these case summaries.)*

SUMMARY OF DECISIONS

AWARD CHALLENGE: *Arbitrators did not exceed their powers or manifestly disregard the law in awarding attorney's fees and costs to firm when collecting the balance on a promissory note, because the note's arbitration clause included a cost- and fee-shifting provision.* **Ameriprise Financial Services, Inc. vs. Silverman** (S.D. N.Y., 12/11/19)

AWARD CHALLENGE: *Arbitrator's refusal to permit rebuttal witness to testify does not constitute refusal to hear material evidence sufficient to warrant vacatur under the FAA.* **Eaton Partners, LLC vs. Azimuth Capital Mgmt. IV, Ltd.** (S.D. N.Y., 10/18/19)

BREADTH OF AGREEMENT: *Where a non-signatory to an agreement containing a mandatory pre-dispute arbitration clause relies on other terms of the agreement to make claims, or the claims are intimately founded in, and intertwined with, the underlying contract obligations, principles of equitable estoppel may compel arbitration of, or entitle another non-signatory to compel arbitration of, the non-signatory's claims.* **Torlay vs. Nelligan** (D. N.J., 9/18/19)

CLIENT LOANS: *Trial court dismisses on statute of limitations grounds most of the causes of action asserted by estate of investor against his former financial and business advisor for allegedly improperly advising decedent to extend various loans.* **Lahey vs. Santinelli** (N.Y. Sup. Ct., Suffolk Cty., 9/18/19)

CONFIRMATION OF AWARD: *Neither arbitrator's refusal to compel discovery from Claimant or postpone hearing, nor panel's assisting a pro se Claimant during the hearing, warrant vacatur under New York's CPLR.* **R.M. Stark Co. vs. Owoyemi** (N.Y. Sup. Ct., NY Cty., 7/31/19)

CONFIRMATION OF AWARD: *Court grants motion to confirm arbitration award, denies motion to dismiss confirmation petition and denies motion for sanctions, finding that a party has an absolute right to seek confirmation of an arbitration award, if done within one year of the award being issued.* **Schusterman vs. Mazzone** (S.D. N.Y., 6/1819)

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ARTICLES & CASE LAW *cont'd from page 20*

CONFIRMATION OF AWARD: *District court's ruling confirming arbitration award which dismissed second arbitration proceeding was affirmed, where appellant failed to allege or prove arbitrator misconduct.* **Walker vs. Ameriprise Financial Services, Inc.** (5th Cir., 10/9/19)

NON-SIGNATORY TO AGREEMENT: *A nonsignatory can compel arbitration when the signatory to the contract containing the arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract.* **Story vs. Merrill Lynch, Pierce, Fenner & Smith, Inc.** (E.D. La., 12/13/19)

VACATUR OF AWARD: *District court will not vacate or modify FINRA arbitration award on "exceeding powers" grounds when it is clear parties agreed to submit the issues decided to the panel.* **Lawlor vs. Merrill Lynch, Pierce, Fenner & Smith, LLC** (E.D. N.Y., 11/22/19)

VACATUR OF AWARD: *Vacatur of an Award based upon a refusal to postpone is warranted only if the court finds that no reasonable basis exists to justify the Panel's decision.* **UBS Financial Services, Inc. & UBS Credit Corp. vs. Walzer** (S.D. Fla., 12/26/19)

Cases

Ameriprise Financial Services, Inc. vs. Silverman, No. 19-cv-7812 (S.D. N.Y., 12/11/19). **Attorney's Fees * Award Challenge * Confirmation of Award * FAA (Exceeding Powers) * Manifest Disregard of the Law * Arbitration Agreement * Disclosure Issues (Arbitrator Conflicts).** *Arbitrators did not exceed their powers or manifestly disregard the law in awarding attorney's fees and costs to firm when collecting the balance on a promissory note, because the note's arbitration clause included a cost- and fee-shifting provision.*

Petitioner Ameriprise brought a FINRA arbitration against Silverman, its former employee, after he resigned from the firm. Ameriprise sought to recover the balance on a promissory note evidencing the firm's loan to Silverman ("Note"). Petitioner also sought attorney's fees, as well as pre- and post-award interest. After a hearing, the panel awarded Ameriprise over $600,000, which included over $350,000 in compensatory damages and interest, and more than $200,000 in attorney's fees and $60,000 in costs. Ameriprise petitioned to confirm the award and Silverman cross-moved to vacate it.

The Court rejects Silverman's alleged grounds for vacatur. First, the district court concludes that the Panel did not exceed its authority in awarding the relief it did. The arbitration provision in the Note was broad, and expressly included a cost- and fee-shifting provision. The Court also rejects Silverman's argument that two of the panelists did not disclose their prior Awards, as that information was readily available in the Arbitrator Disclosure Report sent to the parties by FINRA. Finally, the Panel did not manifestly disregard the law in awarding attorney's fees to Ameriprise, as the Note plainly provided for their award to the prevailing party. Thus, the Court confirms the Award. *(J. Gross) (EIC: Other forums keep their Awards confidential or, when the law dictates, release information about the Awards, but, again, don't disclose them. Providing Awards to the parties during the arbitrator selection process not only places greater control in the parties' hands over their own fate (a good thing), it also protects the Award from later challenges of undisclosed conflicts.)* (SOLA Ref. No. 2020-02-02)

Eaton Partners, LLC vs. Azimuth Capital Mgmt. IV, Ltd., No. 18 Civ. 11112 (S.D. N.Y., 10/18/19). **Attorney's Fees * Award Challenge (Refusal to Hear Evidence) * Confirmation of Award * Manifest Disregard of the Law * FAA: Federal Arbitration Act (§10(a)(3).** *Arbitrator's refusal to permit rebuttal witness to testify does not constitute refusal to hear material evidence sufficient to warrant vacatur under the FAA.*

Eaton Partners, LLC, an investment placement agent ("Eaton"), and Azimuth Capital Management IV, Ltd., a private equity fund manager ("Azimuth"), entered into a Placement Agreement, pursuant to which Eaton agreed to use its best efforts to locate capital for Azimuth. When Azimuth stopped paying fees allegedly due under the Agreement, Eaton filed an arbitration claim in the American Arbitration Association against Azimuth, and Azimuth counterclaimed. At the time of the hearing, one of Azimuth's three witnesses listed on its witness list became unavailable due to his father's death. The parties tried to work out video testimony for him, but ultimately Azimuth voluntarily withdrew him as a witness.

Instead, Azimuth offered a new rebuttal witness to testify to some of the same matters about which the withdrawn witness would have testified. The Arbitrator refused to allow this rebuttal witness to testify, as the witness' offer of proof did not satisfy the criteria required in the Arbitrator's Procedural Order for the appearance of a rebuttal witness. After Eaton won the arbitration, it moved in district court to confirm the Award and Azimuth moved to vacate it. Azimuth argued that the Arbitrator committed misconduct in refusing to postpone the hearing to allow its withdrawn witness to testify and by refusing to permit its rebuttal witness to testify, and that she manifestly disregarded the law in her interpretation of the placement agreement.

The Court first finds that the Arbitrator did not commit misconduct. Instead, arbitrators have broad discretion to accept or refuse evidence under section 10(a)(3) of the Federal Arbitration Act and "need not allow every piece of evidence." The Court reasons that "even an improper exclusion of testimony does not constitute a denial of a fundamentally fair hearing," unless the witness is a "key witness."

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The withdrawn witness at issue here was going to testify on the same subjects as some of the other witnesses; therefore, Azimuth did not establish that a critical part of its case was left unrebutted. Moreover, Azimuth did not make a valid postponement request; rather, it voluntarily withdrew its witness. Additionally, the record belies Azimuth's suggestion that the Arbitrator favored Eaton by insisting on video deposition for the withdrawn witness.

As for the rebuttal witness, the Arbitrator has discretion to refuse to accept any evidence deemed cumulative, and she concluded that the rebuttal witness had nothing new to offer. Finally, the Court concludes that the Arbitrator did not manifestly disregard the law in her interpretation of terms of the placement agreement. The Court recognizes that it cannot disturb an arbitrator's determination on the merits of a dispute as long as there is a colorable justification for that determination. Accordingly, the Court confirms the Award and awards Eaton reasonable attorney's fees for having to oppose the motion to vacate. *(J. Gross)* (SOLA Ref. No. 2019-46-01)

Lahey vs. Santinelli, No. 19428-14, 2019 N.Y. Slip Op. 32757(U) (N.Y. Sup. Ct., Suffolk Cty., 9/18/19). **Pleading Requirements * Breach of Contract * Breach of Fiduciary Duty * Fraud * Timeliness Issues (Statute of Limitations) * Sales Practice/ Product Issues (Client Loans).** *Trial court dismisses on statute of limitations grounds most of the causes of action asserted by estate of investor against his former financial and business advisor for allegedly improperly advising decedent to extend various loans.*

David Lahey suffered a traumatic brain injury, recovered a monetary settlement, and deposited the proceeds into a brokerage account, with defendant Santinelli as his advisor. After Santinelli left the brokerage firm, he continued as Lahey's business and financial advisor pursuant to a "consulting agreement." After Lahey died, his estate brought numerous breach of fiduciary duty and fraud claims in New York state trial court against Santinelli and the brokerage firm, alleging they improperly advised him to extend loans in various amounts to friends and family of both Lahey and Santinelli.

The case against the broker-dealer defendant was stayed pending arbitration. After discovery, Santinelli moved for summary judgment on statute of limitations grounds. Lahey's estate cross-moved for summary judgment and to add an eighth cause of action against Santinelli. The Court dismisses five of seven causes of action on statute of limitations grounds. Applying the three year limitations period for breach of fiduciary duty claims that seek monetary damages, the Court finds that defendant advised Lahey to extend the various loans more than three years before the filing of the complaint.

The Court rejects plaintiff's argument that the six-year limitations period for fraud should apply, concluding that the fraud allegations were only incidental to the fiduciary duty claims and plaintiff only included the fraud claims to answer the statute of limitations defense. The Court also dismisses a sixth cause of action seeking to recover origination fees obtained by Santinelli, and punitive damages for charging origination fees. Defendant returned the only origination fee he received; therefore, he has nothing left to disgorge.

It also dismisses the punitive damages claim, as plaintiff did not show the conduct was part of a pattern directed at the public generally. The Court declines to dismiss a seventh cause of action against Santinelli for breach of the parties' consulting agreement with respect to two non-time-barred loans, finding factual issues exist as to whether Santinelli acted in good faith in carrying out his obligations under the agreement. It also grants plaintiff's request to add an eighth cause of action against Santinelli for breach of a loan, finding no prejudice to Santinelli. *(J. Gross) (EIC: So often, the prevalence of statutes of limitations defenses encourages a party to forego arbitration, but home runs are rare on timeliness challenges. Often, one just narrows the field of claims, but that ultimately doesn't save on expenses.)* (SOLA Ref. No. 2020-02-03)

Lawlor vs. Merrill Lynch, Pierce, Fenner & Smith, LLC, No. 19-cv-4145 (E.D. N.Y., 11/22/19). **Attorney's Fees * Award Challenge * Eligibility * Modification of Award * Vacatur of Award (Exceeding Powers).** *District court will not vacate or modify FINRA arbitration award on "exceeding powers" grounds when it is clear parties agreed to submit the issues decided to the panel.*

Petitioner Lawlor, a former employee of Respondent Merrill Lynch, filed a FINRA arbitration claim against Respondent for fraud, breach of fiduciary duty and RICO violations, all stemming from Merrill's grant of stock options to Lawlor in connection with his employment (the "Merits Claims"). Like it did for other arbitrations filed by similarly-situated former employees, Merrill challenged the arbitrability of Lawlor's Merits Claims in federal district court. The district court denied Merrill's arbitrability challenge. In a settlement reached in parallel actions in other districts, Merrill agreed to allow all similarly-situated former employees to pursue claims for costs and fees stemming from lawsuits filed by Merrill in federal court challenging the arbitrability of their employment-related claims.

As a result of that settlement agreement, which indisputably covered Lawlor's arbitration, Lawlor amended his FINRA arbitration claim to include claims for attorneys' fees, costs and punitive damages (the "Fees Claim") incurred by Lawlor in defending the federal court action. In the arbitration, Merrill then moved to dismiss Lawlor's Merits Claims under FINRA Rule 12206, which provides that a claim is not eligible for FINRA arbitration "where six years have elapsed from the occurrence or event giving rise to the claim." After the panel heard argument

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on Respondent's eligibility motion, during which Lawlor also argued his Fees Claims, the panel dismissed all of Lawlor's claims in their entirety.

Lawlor now moves to vacate the FINRA arbitration award on the grounds that the panel exceeded its powers in dismissing the Fees Claims in conjunction with the Rule 12206 dismissal. Lawlor argues in the alternative that the award should be modified to reflect that it does not cover Lawlor's Fees Claims because those claims were "not submitted" to the panel within the meaning of FAA § 11(b) (permitting a court to modify an award where the "arbitrators have awarded upon a matter not submitted to them"). The court denies Lawlor's motion. First, the court concludes that the panel clearly had the power to rule on the Fees Claims. The parties' arbitration agreement was broad in scope, as it covered "all controversies that may arise between us."

Second, the court finds that Lawlor submitted the Fees Claims to the panel through his amended statement of claim, and by arguing those claims during the hearing on the motion to dismiss. Moreover, the award separately addressed the Merits Claims and the Fees Claims, by granting the Rule 12206 motion for the Merits Claims in one paragraph and dismissing "any and all claims for relief not specifically addressed" in a second paragraph. Finally, the court rejects Lawlor's argument that Rule 12206 did not explicitly permit the panel to consider other claims at the same time as it considered the eligibility arguments. Rather, as the court notes, "one of the main benefits of arbitration is its embrace of efficient and practical decision-making, which often eschews procedural silos and ridged [sic] court rules." *(J. Gross)* (SOLA Ref. No. 2019-48-01)

R.M. Stark Co. vs. Owoyemi, No. 652065/2019, 2019 NY Slip Op 32339(U) (N.Y. Sup. Ct., NY Cty., 7/31/19). **Award Challenge * Confirmation of Award (Arbitrator Misconduct, Refusal to Postpone Hearings, Arbitrator Partiality) * Discovery Issues.** *Neither arbitrator's refusal to compel discovery from Claimant or postpone hearing, nor panel's assisting a pro se Claimant during the hearing, warrant vacatur under New York's CPLR.*

Claimant Owoyemi filed a FINRA arbitration *pro se* against Respondent R.M. Stark for unpaid commissions and unjust enrichment, among other things. During the pre-hearing process, the Arbitrators denied Respondent's motion to compel Claimant to produce certain documents about his financial and employment background. The Panel also refused to adjourn the hearing as a result of Claimant's alleged incomplete discovery responses. In addition, during the hearing, the Panel provided some assistance to the Claimant, who was not represented, in questioning a witness. After Claimant secured a $30,725.00 award plus interest, Respondent petitioned in New York state court to vacate the Award, citing both New York's and the FAA's grounds for vacatur. Claimant opposed the petition and asked the Court to confirm the Award instead. Citing New York's CPLR grounds, the Court denies the motion to vacate. First, the Court concludes that the Panel's denial of Respondent's discovery request was not arbitrator misconduct warranting vacatur. Arbitrators have wide discretion in managing the discovery process and the documents requested were not directly relevant to the Claimant's claims for unpaid commissions.

Second, even though the Panel assisted the Claimant with some procedures during the hearing, they were doing so because he was proceeding *pro se*. Thus, the Arbitrators did not commit misconduct. Furthermore, Respondent failed to preserve the objection to that assistance during the hearing and cannot raise it now. Accordingly, the Court confirms the award. *(J. Gross: Notably, NY Supreme Court bases its holding on New York's grounds for vacatur under the CPLR, even though the losing party cites to both New York and federal grounds. State courts are divided as to whether the FAA's grounds for vacatur or state grounds apply to a motion to vacate a FINRA arbitration Award brought in state court. Clearly a dispute filed in FINRA arbitration arises out of an agreement "involving commerce," and therefore the FAA governs the agreement to arbitrate. However, the Supreme Court has never held that FAA section 10, which is procedural and provides allowable grounds for vacatur, applies in state court.)* (SOLA Ref. No. 2019-47-02)

Schusterman vs. Mazzone, No. 19 Civ. 212 (PAE) (S.D. N.Y., 6/1819). **Award Challenge * Confirmation of Award * Defamation * FAA: Federal Arbitration Act (§ 9) * FRCP: Federal Rules of Civil Procedure (Rule 11 "Sanctions" and Rule 12(b)(6) "Claim for Relief") * Constitutional Issues (Mootness/Ripeness).** *Court grants motion to confirm arbitration award, denies motion to dismiss confirmation petition and denies motion for sanctions, finding that a party has an absolute right to seek confirmation of an arbitration award, if done within one year of the award being issued.*

Schusterman and Mazzone were both certified financial planners who jointly owned and operated a financial services group. Their business relationship had been memorialized in an agreement that required any disputes be resolved through FINRA arbitration. Upon the breakup of their group, Schusterman and Mazzone each filed separate FINRA arbitration claims. Schusterman argued Mazzone had breached their agreement by soliciting their joint clients and had also committed tortious interference and defamation in this endeavor. Schusterman also asserted Mazzone had assaulted her and falsely imprisoned her. Mazzone argued Schusterman had defamed her and battered her and also sought a declaration that Schusterman's $1 million payment to Mazzone to buy her interest in the

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group was proper and Schusterman was not entitled to recover that payment. Mazzone also sought sanctions against Schusterman, arguing that Schusterman had only filed the motion to confirm to "besmirch Mazzone's reputation."

Schusterman and Mazzone agreed to consolidate their two separate cases and, after 10 days of hearings, the FINRA Panel rendered an award mostly in favor of Schusterman. More specifically, the Panel found that Mazzone had breached the agreement in soliciting Schusterman's clients and awarded Schusterman just under $550,000. The Panel denied Schusterman's claims of tortious interference and defamation, finding those claims were not independent of the breach of contract claim. The Panel also ruled that Schusterman did not prove her claims of false imprisonment. Alternatively, the Panel ruled that Mazzone had proved her claim of battery and awarded her a $50,000 offset to the damages she owed Schusterman. The Panel also found Schusterman had defamed Mazzone, but Mazzone did not prove any damages related to that claim. Lastly, the Panel granted Mazzone's relief for Declaratory Judgment, finding that the $1 million payment was proper and Schusterman was not entitled to recover that payment.

Sometime after the Award was rendered, Schusterman filed an action to confirm the arbitration award. In response, Mazzone filed a motion to dismiss the motion to confirm the award, as well as a motion for sanctions against Schusterman. The Court notes that "[n]ormally, confirmation of an arbitration award is a summary proceeding …" and limited reasons exist for not confirming an arbitration award under the Federal Arbitration Act. In this case, Mazzone was not arguing that the award was flawed or the arbitrators had exceeded their authority. Rather, she argued "the matter is not ripe for confirmation because Schusterman's petition was filed before the deadline to comply with the Award had passed." Moreover, Mazzone has since paid the balance due under the Award, rendering the petition to confirm moot.

In denying Mazzone's motion to dismiss and confirming the award, the Court notes "payment does not negate the right of the prevailing party, Schusterman, to seek judicial confirmation of the arbitral decision." Rather, the Court explained, "[t]he issues of compliance and confirmation are distinct from each other." In the end, "parties retain an undisputed right to § 9 confirmation whatever the nature of an award *and the parties' degree of compliance with it*."

In denying the motion for sanctions, the Court rules that the sanctions request was not procedurally compliant, as Mazzone had failed to file it in a separate motion and had failed to give Schusterman the right to cure, as required under FRCP 11. Additionally, "Mazzone's motion fails on the merits." In order to impose sanctions, a court must find a party "acted with 'objective unreasonableness.'" There was nothing unreasonable about Schusterman exercising her right to confirm the award. *(S. Edwards)* (SOLA Ref. No. 2020-01-03)

Story vs. Merrill Lynch, Pierce, Fenner & Smith, Inc., No. 19-2301 (E.D. La., 12/13/19). **Non-Signatory to Agreement * Scope of Agreement (Arbitration) * Statutory Definitions ("Interdependent and Concerted") * Account Administration (Freeze Account) * Equitable Doctrine (Estoppel).** **A nonsignatory can compel arbitration when the signatory to the contract containing the arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract. **A nonsignatory can compel arbitration when each of a signatory's claims against a nonsignatory makes reference to or presumes the existence of a written agreement, and the signatory's claims arise out of and relate directly to the written agreement.*

Michael Zauner created a trust to benefit his wife, Tricia Story, and his children. The trust assets included an account at Merrill Lynch. After Zauner's death, Story became the trustee and she attempted to distribute the trust assets. Zauner's children objected to Story as trustee and so Merrill Lynch froze the accounts. Story then filed two suits in state court against Merrill Lynch and Bank of America, Merrill Lynch's parent. One suit asked the court to mandate the distribution of the funds and award Story damages. The other asked the court to grant Story authority over the accounts.

Defendants removed the suits to federal court, where they were consolidated. Merrill Lynch's motion to compel arbitration of the claim against it was granted. Initially, Bank of America did not move to compel arbitration, arguing instead that it was not a proper party to the dispute. It now moves to compel arbitration even though it was not a signatory to the Client Relationship Agreement that Story signed. Bank of America also argues that the dispute is now moot, because Story settled with the children after the suits were filed and the distributions were made. Story counters that the dispute is not moot, because she suffered damages on account of the freeze.

The Court grants the motion to compel arbitration. Bank of America asserts that it has the right to arbitrate the claim against it under the theory of estoppel. Estoppel permits a court to estop a signatory from avoiding arbitration with a nonsignatory, when the issues the nonsignatory is seeking to resolve in the arbitration are intertwined with the agreement that the estopped party has signed. This form of estoppel applies if one of two conditions is met. A nonsignatory can compel arbitration when the signatory to the contract containing the arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the nonsignatory and one or more of the signatories to the contract. Or a nonsignatory can compel arbitration when each of a signatory's claims against a nonsignatory makes reference to or presumes the existence of a written agreement, and the

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signatory's claims arise out of and relate directly to the written agreement.

Story's claims require arbitration under either condition. First, Story raises allegations of substantially interdependent misconduct against both Bank of America and Merrill Lynch. For example, in the pleadings she states she "has issued numerous directives to Merrill Lynch and Bank of America concerning the distribution of the funds." Second, Story's claims hinge on the Client Relationship Agreement. Story pleaded that, under this agreement, she received "access to a range of Accounts" and it was the denial of this access, which instigated her suits. Furthermore, allowing Bank of America to arbitrate prevents an otherwise perverse result. A contrary outcome would allow a plaintiff to circumvent an arbitration clause by suing a parent company whenever a dispute arose with a subsidiary. With respect to the issue of mootness, the parties agreed to send all grievances to arbitration. In such case, the issue of mootness is a question for the arbitrator. *(P. Dubow)* (SOLA Ref. No. 2020-02-01)

Torlay vs. Nelligan, No. 19-6589 (D. N.J., 9/18/19). **Agreement to Arbitrate * Arbitrability * Arbitration Agreement (Form U-4) * Compensation Issues * FRCP (Rule 56) * Injunctive Relief * Breadth of Agreement (Non-Signatory) * SRO Rules (FINRA Rule 13200 "Associated Person") * Stay of Litigation.** *Where a non-signatory to an agreement containing a mandatory pre-dispute arbitration clause relies on other terms of the agreement to make claims, or the claims are intimately founded in, and intertwined with, the underlying contract obligations, principles of equitable estoppel may compel arbitration of, or entitle another non-signatory to compel arbitration of, the non-signatory's claims.*

In response to the breach of contract action of plaintiff, a retired financial advisor, for defendants' alleged failure, after transferring to a new firm, to honor the customer non-solicitation terms of a five-year buy-out of his client book, defendants moved to compel arbitration. Plaintiff opposed the motion on the ground that none of the agreements at issue, or the arbitration clauses in them, were directly between plaintiff and defendants — plaintiff and defendants each having executed separate transition agreements with their former firm. Based on the intertwining obligations of the various agreements, plaintiff's use of them in bringing his claims, and applying common law principles of equitable estoppel, the Court grants the motion over plaintiff's objection.

As the Court first notes, though federal arbitration policy includes a strong presumption favoring arbitration, the presumption first requires proof under applicable state law that an enforceable agreement exists between the parties. Based on common law contract principles — in this instance, the laws of New York and New Jersey, which are indistinguishable on the issue -- the Court finds that two theories of equitable estoppel require plaintiff to arbitrate his claims. First, even though plaintiff is a non-signatory to defendants' agreement with their former firm, he is bound by the arbitration obligation in it, because his own claims sought to enforce, and benefit from, other parts of the agreement, including having pled the non-solicitation orders obtained by Morgan Stanley in earlier litigation from it. In the words of the Court, plaintiff may not, in an effort to avoid arbitration, "cherry-pick" or "strategically select" particular provisions of defendants' agreement.

Second, due to the intertwined contractual obligations and relationships of the parties, defendants, though non-signatories to plaintiff's agreement with Morgan Stanley, may enforce the arbitration obligations in it. As the Court notes, plaintiff specifically alleges that defendants denied him benefits due him under his Morgan Stanley agreement, plaintiff blurs the boundary lines between, and the revenues shared under, the two agreements, defendants' agreement specifically references plaintiff's agreement, and plaintiff's agreement designates defendants as the financial advisors servicing plaintiff's clients in retirement. Simply put, according to the Court, "plaintiff 'cannot have it both ways.'" *(D. Franceski: *It is also worth noting that the Court, absent evidence or affidavits establishing that each of the parties executed FINRA Form U-4 and are, therefore, subject to the arbitration obligations among industry professionals flowing from it, rejected defendants' additional argument that plaintiff should be compelled to arbitrate under FINRA Rule 13200. **Though, from time to time, this author's firm provides litigation services both to Morgan Stanley and to defendant Merrill Lynch, the firm did not participate in this litigation.)* (SOLA Ref. No. 2020-01-02)

UBS Financial Services, Inc. & UBS Credit Corp. vs. Walzer, No. 9:19-CV-81161 (S.D. Fla., 12/26/19). **Postponement, Refusal of * Award Challenge * Confirmation of Award * Simultaneous Proceedings * FAA (§10 "Exceeding Powers") * Choice of Law * State Statutes Interpreted (Fla. Arb. Code; Fla. Stat. § 682.13) * Evidentiary Standards (Best Evidence).** *Vacatur of an Award based upon a refusal to postpone is warranted only if the court finds that no reasonable basis exists to justify the Panel's decision.*

At seven different times during his UBS employment, and pursuant to seven different promissory notes, broker Howard Walzer received loans from Plaintiffs totaling $1.27 million. When Respondent Walzer resigned from the firm, he owed, according to Plaintiffs' joint claim before a FINRA arbitration Panel, almost $800,000 in unforgiven debt. Case No. 16-00888 was filed by UBS Financial and UBS Credit Corp. on March 25, 2016. A full three years later, on March 27, 2019, after four postponements granted at Respondent's request, the Panel refused a fifth request and proceeded with the hearing. The Majority Public Panel unanimously awarded full compensatory damages, pre-Award and post-Award interest,

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and attorney fees to the UBS entities. Counterclaims were withdrawn by mutual agreement and without prejudice.

Moving to vacate under the Florida Arbitration Code, broker Walzer charges the FINRA Panel with exceeding its authority and with refusing a postponement, when sufficient cause was demonstrated. That challenge is pending in Florida state court, while Plaintiffs have moved to confirm in federal court under the FAA. The Court begins its analysis by explaining how the two arbitration statutes interact: "When an arbitration agreement involves interstate commerce, the Federal Arbitration Act ('FAA') governs, supplemented by the Florida Arbitration Code ('FAC') to the extent that the FAC does not conflict with the FAA...." Here, the Court construes the objections made by Defendant to the Award "under the FAA's substantially identical provisions to the Florida statutes he cites...."

The basis for vacatur when a refusal to postpone is unwarranted requires that "no reasonable basis existed" for such refusal. While Mr. Walzer's claim of a medical condition was supported by a doctor's note and a proffer of a neurologist's testimony, the request to postpone was Defendant's fifth and was received 13 days before hearing, when 120 days' notice was provided. Moreover, the Panel accommodated Respondent by permitting a videoconference appearance and, when technical problems arose, the Panel delayed the hearing for 2 1/2 hours so that Mr. Walzer's counsel could appear personally.

An arbitrator's authority is so broad that challenges based on the "exceeding powers" clause in Section 10 of the FAA demand a clear showing that the arbitrators disregarded the contractual terms at issue. To the extent the Arbitrators interpret the contracts before them, whether or not they commit legal error, the courts may not conduct a review. The four arguments on which Defendant Walzer relies essentially charge legal error -- not a ground for vacatur. For example, the proposition that the Arbitrators wrongly permitted a non-member, UBS Credit, to assert its claim, in violation of FINRA rules, requires review of the arbitration clause and FINRA Rules. Yet, Defendant did not supply the Court with the promissory notes or the PDAA provisions, leaving the Court to second-guess the Arbitrators' interpretation of the arbitration rules. The Court confirms the Award and rejects the objections raised by Defendants. (SOLA Ref. No. 2020-01-01)

Walker vs. Ameriprise Financial Services, Inc., No. 18-11641 (5th Cir., 10/9/19). **Confirmation of Award * Award Challenge (Arbitrator Misconduct) * FAA: Federal Arbitration Act (§10(a)(3) & (4)) * Re-Litigation Issues * SRO Rules (FINRA Rule 13504).** *District court's ruling confirming arbitration award which dismissed second arbitration proceeding was affirmed, where appellant failed to allege or prove arbitrator misconduct.*

Appellant Walker was a former employee of appellee Ameriprise Financial Services, Inc. ("Ameriprise"). In 2015 Ameriprise sought a restraining order against Walker to prevent him from utilizing confidential customer information, and the dispute was submitted to FINRA arbitration (the "2015 Arbitration"). Ameriprise asserted several claims in the 2015 Arbitration, including theft of trade secrets and breach of contract. Walker was granted leave to amend his answer to "assert claims or defenses…including in bar or in mitigation of Claimants' claims," but was otherwise denied leave to amend counterclaims. At the final hearing, Walker was nevertheless permitted to argue his counterclaims. The 2015 Arbitration ended in an award for Ameriprise and against Walker, granting Ameriprise a permanent injunction, compensatory damages and attorney's fees. Walker did not challenge the injunction on appeal.

In 2017, Walker initiated a new FINRA arbitration (the "2017 Arbitration") in which he primarily alleged he was improperly enjoined by the 2015 Arbitration. Ameriprise moved for dismissal on the basis of FINRA Rule 13504(a)(6), which provides for dismissal of claims that were previously fully adjudicated on the merits and resolved with a final Award. Walker filed an initial and supplemental response to the motion and participated in a one-hour telephone evidentiary hearing attended by all parties and the full panel. Ameriprise's motion to dismiss was granted.

Walker sought vacatur in the district court, which affirmed the ruling. On appeal to the Fifth Circuit, Walker argued that the 2017 Arbitration Award should be vacated under the Federal Arbitration Act, 9 U.S.C. §10(a)(3), because the Arbitrators were guilty of misconduct in failing to allow him to present evidence and testimony, and under §10(a)(4), because the Arbitrators exceeded their powers by relying on FINRA Rule 13504 (a)(6) to dismiss the case. The Fifth Circuit noted that judicial review of an arbitration Award is exceedingly deferential, and it is not enough to show an error, even a serious error. A court may not vacate an award simply because it disagrees with the arbitrator's legal reasoning or would have reached a different conclusion. A party seeking to overturn an arbitration award faces a high hurdle.

In this case, Walker failed to make the required showing. The Arbitrators did allow him the opportunity to present evidence and testimony during the telephone hearing, negating his §10(a)(3) argument. And even if the Panel had incorrectly applied FINRA Rule 13504(a)(6) to the facts, this would not be grounds for vacatur under §10(a)(4), according to Fifth Circuit precedent. Instead, Walker would have had to show that the arbitration Panel acted contrary to express contractual provisions. Walker failed to even argue that the Panel violated the agreement to arbitrate, so this point fails as well. The 2017 Arbitration award dismissing Walker's claims is affirmed. *(J. Ballard)* (SOLA Ref. No. 2019-47-01)