SECURITIES ARBITRATION ALERT 2023-01 (1/5/23)

George H. Friedman, Editor-in-Chief

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- ***Beco v. Fast Auto Loans, Inc.*, No. G059382 (Calif. Ct. App. 4 Dec. 14, 2022)**
- ***Githaiga v. TD Ameritrade,* FINRA ID No. 22-00240 (Washington, DC, Nov. 16, 2022)**
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DID YOU KNOW?

- **A Guest "Did You Know?" Courtesy of SCOTUS**

WE ARE BACK: SO MUCH HAPPENING! *We are back after a quarterly break, and the news, court decisions and awards have been piling up in our absence. We kick off the year with news of a late-year rule filing aimed at implementing the recommendations in the independent investigator's report on the "rigged panels" accusation. We also report on the results of the December FINRA Board meeting, which includes proposed arbitrator selection changes. We also offer an analysis of FINRA-DRS' through-*

November stats, which feature more signs of a strong finish to the year in arbitration filings. And we have our usual collection of Short Briefs, Quick Takes, and Articles of Interest. In other words, a jam-packed new issue of the Alert!

SQUIBS: IN-DEPTH ANALYSIS

FINRA FILES RULE CHANGE PROPOSAL IMPLEMENTING "RIGGED PANELS" INVESTIGATION REPORT RECOMMENDATIONS. ***On the eve of the year-end holiday break, FINRA filed a rule change proposal that would implement recommendations resulting from the outside investigation of allegations that the arbitrator selection process was rigged*****.** First, some background. As summarized in SAA 2022-38 (Oct. 13), FINRA in **June 2022** released a 37-page *Report of the Independent Review of FINRA's Dispute Resolution Services – Arbitrator Selection Process*, which was announced in a corporate Press Release and a separate statement from the Audit Committee. The investigation was directed by **Christopher Gerold**, a partner in Lowenstein Sandler LLP's Securities Litigation and Corporate Investigations & Integrity Practice Groups.

Recommended Changes

After discussing methodology and the operation of the Neutral List Selection System, the Report concluded that there were no irregularities, and it closed with recommendations for improvement. The core recommendations were (*ed: presented* verbatim *from the Release*):

- Implementing ongoing, mandatory training for staff;
- Requiring written explanations, upon a party's request, of approval or denial of a causal challenge to the selection of an arbitrator or an arbitrator removal by the DRS Director for cause;
- Conducting an updated external procedural review of the arbitrator selection algorithm to determine if it is still the most effective means for creating random, computer-generated arbitrator lists; and
- Updating the DRS Manual and rules to clarify staff roles and procedures, and to ensure consistency and transparency.

FINRA's Follow-up: A Dedicated Webpage and a Rule Filing

FINRA's management accepted all recommendations, and now posts on its Website a live progress report on implementation. *Status Report on Lowenstein Sandler LLP Recommendations* shows that most items have been implemented or were "in progress." The latest step was accomplished on **December 23**, when FINRA filed with the SEC SR-FINRA-2022-033, *Proposed Rule Change to Amend the Codes of Arbitration Procedure.* The filing describes it as: "a proposed rule change to amend the Code of Arbitration Procedure for Customer Disputes ('Customer Code') and the Code of Arbitration Procedure for Industry Disputes ('Industry Code') (together, 'Codes') to make changes to provisions relating to the arbitrator list selection process in response to recommendations in the report of independent counsel Lowenstein Sandler LLP. The proposed rule change also makes clarifying and technical changes to requirements in the Codes for holding prehearing conferences and hearing sessions, initiating and responding to claims, motion

practice, claim and case dismissals, and providing a hearing record." We will provide more detail in a future *Alert.*
(ed: The rule filing's progress can be tracked here.)
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FINRA BOARD MET LAST MONTH. ARBITRATOR SELECTION RULE CHANGES APPROVED. ***FINRA's Board met in mid-December and among other matters approved changes to the arbitrator listing process.*** FINRA's Board of Governors met in person **December 14 – 15.** As reported in SAA 2022-47 (Dec. 15), the agenda had a somewhat mysterious dispute resolution-related item: "review amendments to the Codes of Arbitration Procedure to make various clarifying, technical and procedural changes." At that time we were stumped as to what this meant.

Clarity Provided by FINRA …
The post-meeting memo sheds further light on the subject: "The Board approved the submission to the SEC of proposed amendments to the Codes of Arbitration Procedure to make clarifying, technical and procedural changes to the arbitrator selection process. The amendments would codify current practices and guidance relating to arbitrator selection *and increase selection opportunities for public arbitrators who are not chair-qualified*" (emphasis added). While this description is still somewhat cryptic, we have a good read on the highlighted planned changes to the arbitrator list selection process.

… and the *Alert*
In a letter to the editor published in SAA 2022-48 (Dec. 22), Dispute Resolution Services' Associate Director, Recruitment and Training, **Nicole Haynes** said: "In addition to current recruitment efforts to bolster the forum's neutral roster, in 2023, FINRA will propose changes to the arbitrator selection process to provide new and more diverse public arbitrators with greater opportunities to serve. Currently, public chairpersons have two opportunities to appear on a list. Chairpersons not appointed to the chairperson list also appear in the public arbitrator pool along with the public arbitrators in each hearing location for possible inclusion on the list, thereby giving eligible public chairpersons an advantage. To correct this imbalance, the proposal would provide non-chair qualified public arbitrators with two opportunities to appear on the public list. Chair-qualified arbitrators would have one opportunity to appear on the public list, as they already had one opportunity to be selected on the chairperson list. The goal of the proposal is to provide new and more diverse public arbitrators with greater opportunities to serve, to gain experience and ultimately become eligible to join the chairperson roster."

And … Early Release of Regulatory Targets
The Board also previewed the *2023 Report on FINRA's Examination and Risk Monitoring Program*, "which will provide firms with insight into findings from recent oversight activities of FINRA's Regulatory Operations to help inform the development and operation of firms' compliance programs." The memo added that FINRA plans to release the report early in the new year, which is much earlier than in recent years.

*(ed: *This would be a good rule change. We'll be on the lookout for a Reg Notice seeking comments, or a rule filing with the SEC. **This was the last meeting for 2022. Next year's schedule is: March 9–10; May 17–18; July 12–13; September 13–14; and December 6–7.)*
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CFPB ISSUES SEMI-ANNUAL REPORT (SCANT MENTION OF ARBITRATION). DIRECTOR CHOPRA APPEARED BEFORE CONGRESS LAST MONTH. ***The CFPB has issued its Semi-annual Report to Congress, with just a passing reference to arbitration. Also, Director Chopra in December appeared before committees of both houses of Congress.*** We reported in SAA 2022-21 (Jun. 2) that the Consumer Financial Protection Bureau ("CFPB" or "Bureau") seemed disinclined to act on arbitration. We based this surmise on Director **Rohit Chopra**'s semi-annual report to Congress in **April**, when neither he nor any Senate Banking Committee members mentioned arbitration. The Committee's two-hour hearing, *The Consumer Financial Protection Bureau's Semi-Annual Report to Congress,* was held **April 26**. Perusal of the hearing video (available here) and Director Chopra's five-page prepared remarks shows that the term "arbitration" was not mentioned.

Still the Same
The CFPB recently published its *Semi-Annual Report to Congress* for the period running **October 1, 2021** through **March 31, 2022**. Like its predecessors, the Report makes scant reference to arbitration, referring to it just twice in connection with litigation brought by the Bureau. Also, the *Spring 2022 Agency Rule List*, which delineates regulatory initiatives the Bureau: "reasonably anticipates having under consideration during the period from June 1, 2022 to May 31, 2023," has five items listed, but arbitration is not one of them: 1) Consumer Access to Financial Records; 2) Amendments to FIRREA Concerning Automated Valuation Models; 3) Property Assessed Clean Energy Financing; 4) Small Business Lending Data Collection Under the Equal Credit Opportunity Act; and 5) Adverse Information in Cases of Human Trafficking Under the Debt Bondage Repair Act.

No Surprise to Us
As we've said before, given past events and resource limitations, arbitration's absence from the CFPB's priorities is not surprising. Recall that *Dodd-Frank* section 1028 directs the CFPB to study the use of PDAAs in contracts for consumer financial products and services, to later report to Congress, and to ban, limit or impose conditions on their use if such action: "is in the public interest and for the protection of consumers." *Alert* readers may recall that the CFPB did indeed issue the required report to Congress and later promulgated a rule banning class action waivers. However, before it became effective, the Final Rule was retroactively nullified in **November 2017**, when **President Trump** signed into law H.J. Res. 111, a *Joint Disapproval and Nullification Resolution* (see SAA 2017-41). Congress had exercised its authority under the *Congressional Review Act*, ("*CRA*"), 5 USC §§ 801 *et seq*., which allows that body to legislatively nullify any regulation within 60 legislative/session days of its publication. Under the *CRA*, a

substantially similar reg cannot be reintroduced without the express permission of Congress.

Chairman Chopra Goes to Congress
Chairman Chopra made back-to-back appearances at Congressional committee hearings last month. Specifically, Mr. Chopra testified before the House Financial Services Committee at a **December 14** hearing titled: *Consumers First: Semi-Annual Report of the Consumer Financial Protection Bureau*; and a **December 15**, Senate Banking Committee hearing, *The Consumer Financial Protection Bureau's Semi-Annual Report to Congress*." Arbitration was not discussed at either hearing or as part of his prepared remarks. The House majority staff memo likewise is silent about arbitration.
(ed: We are not surprised that arbitration is not a CFPB priority.)
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SHORT BRIEFS: CONCISE NEWS YOU NEED TO KNOW

FINRA DRS POSTS STATS THROUGH NOVEMBER: LOOKS LIKE A STRONG END TO THE YEAR. FINRA Dispute Resolution Services ("DRS") has posted case statistics through **November**, with recent trends suggesting a strong end to the year in arbitration filings. We offer these headlines: 1) overall arbitration filings through the eleven-month mark – 2,473 cases – are down 11% for the year (but up from minus 14% in October); 2) cumulative customer claims declined by 14% (up from -18% in October); and 3) industry arbitration filings are down 5% (-6% in October). That all three case filing figures are again improved over the previous month indicates to us that – for the fifth month in a row – arbitration filing declines have definitely rebounded. Overall arbitration turnaround times were 18.2 months, with hearing cases now taking 19.8 months (both figures are barely changed from the past two months). There were 716 mediation cases in agreement, a 27% increase (but way down from May's torrid plus 137% pace). The mediation settlement rate remains very high at 91%. There are now 8,383 DRS arbitrators, 4,036 public and 4,347 non-public. Pending cases stand at 3,084, a decline of 65 from October.
*(ed: *Despite the recent mini-surge in arbitration case filings, if the trend holds the 2,423 arbitrations filed through November straight-lines to only about 2,650 yearly arbitration filings, a weak year by any measure. Ten years ago, the 2012 stats showed 4,299 yearly arbitration case filings. The all-time high-water mark was 2003, when that post tech-wreck figure was 8,945 cases. **As we said before, it seems to us the rebound in customer claims will continue. ***Past year stats can be found here.)*
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EXPUNGEMENT UPDATE: JUST ONE REBUTTAL ON FINRA'S AMENDED PROPOSAL. BALL IS IN SEC'S COURT. The comment period closed **December 21** for rebuttal comments on FINRA's proposed changes to its expungement rule filing, with just one rebuttal being posted on the Commission's Website. We analyzed in SAA 2022-47 (Dec. 15) the comments received from NASAA, PIABA, and SIFMA. We described them in a **December 16** blog post, *Expungement Update: Few Comments on Amended Proposal. PIABA and NASAA Supportive, But SIFMA Urges Disapproval*, as falling into

one of three categories: support fully (PIABA); support but recommend improvements (NASAA); and urge disapproval (SIFMA). Comments on the amended rule and potential disproval were due **December 7**, and rebuttals by **December 21.**
(ed: The ball is now squarely in the SECs court. After all this effort, we can't see the Commission disapproving the proposal. More likely, there will be approval with suggestions for further improvements.)
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NEW BUDGET DEAL BARS SOME FEDERAL CONTRACTORS FROM REQUIRING ARBITRATION OF TITLE VII OR SEXUAL HARASSMENT AND ASSAULT CLAIMS. Buried in the 1,600+ page appropriations bill, the *Consolidated Appropriations Act of 2023* (H.R. 2617), signed into law **December 29**, is language that bars companies with federal defense contracts valued at over $1 million from mandating or enforcing arbitration of Title VII or sexual harassment or assault claims. Specifically, the text of section 8089(a) states that: "None 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 prohibits enforcement of arbitration clauses in existing contracts.
(ed: The Act complements the Ending Forced Arbitration of Sexual Assault and Sexual Harassment Act of 2021 ("EFASASHA"), which the President signed into law on March 3. As we have reported many times, EFASASHA expressly amended the Federal Arbitration Act ("FAA") to make predispute arbitration agreements and class action waivers voidable at the option of the victim. The new law has been codified as FAA Chapter 4. It consists of § 401 (definitions) and § 402 (no validity or enforceability).)
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SEC AWARDS MORE THAN $20 MILLION TO WHISTLEBLOWER. The SEC on **December 12** announced via press release an award of more than $20 million to an individual whistleblower: "who provided information and assistance that significantly contributed to a successful enforcement action. The whistleblower provided new information, met with Enforcement Division staff multiple times, and remained cooperative throughout the investigation." The Commission stresses that whistleblower awards are: "made out of an investor protection fund, established by Congress, which is financed entirely through monetary sanctions paid to the SEC by securities law violators. No money has been taken or withheld from harmed investors to pay whistleblower awards." Whistleblower awards: "can range from 10 to 30 percent of the money collected when the monetary sanctions exceed $1 million."
*(ed: *This is one of the larger such awards in our memory. **For more information about the program, visit www.sec.gov/whistleblower.)*
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DEADLINE FAST APPROACHING: ICC SEEKING LAW SCHOOL APPLICANTS FOR VIS PRE-MOOT. The International Chamber of Commerce on **December 16** posted a notice encouraging law schools to participate in the *ICC Vis Pre-Moot* taking place in-person **March 6 - 8** at its headquarters in Paris. The event's purpose is to help teams prepare for the virtual *30th Willem C. Vis International Commercial Arbitration Moot* taking place in Vienna in early **April**. The notice states that the Pre-Moot will enable teams to: "measure up against and interact with other students from a wide range of different jurisdictions and legal systems; receive comments from and interact with arbitrators from different professional, cultural and legal backgrounds; practice and improve your advocacy skills; and refine and adjust your oral arguments just before participating in the Vis Moot in Vienna."
*(ed: *Unlike last year, there is no online participation option. **Applications are done online. The deadline is January 8, and only one team per university may apply. ***Contact iccpremoot@iccwbo.org for further information. ****The 2020 Moot was cancelled due to the pandemic.)*
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QUICK TAKES: CASES AND AWARDS WORTH READING

***Suski v. Coinbase, Inc.*, No. 22-1520 (9th Cir. Dec. 16, 2022)**: "The district court concluded that a delegation clause in the Coinbase User Agreement did not delegate to the arbitrator the issue of which contract governed the dispute. The district court further ruled that, under state law principles of contract interpretation, the Official Rules superseded the Coinbase User Agreement and, therefore, that the User Agreement's arbitration clause did not apply.... The district court correctly ruled that because the User Agreement and the Official Rules conflict on the question whether the parties' dispute must be resolved by an arbitrator or by a California court, the Official Rules' forum selection clause supersedes the User Agreement's arbitration clause."

***Lloyd v. Argent Trust Co.*, No. 22-cv-4129, 2022 U.S. Dist. LEXIS 219964 (S.D.N.Y. Dec. 6, 2022)**: "[T]he plaintiffs argue that the arbitration clause in the WBBQ Plan is not enforceable because it prohibits claimants from asserting certain statutory rights, and from seeking certain statutory remedies. In particular, the plaintiffs argue that the Plan's limitations on equitable relief preclude them from seeking certain forms of equitable relief authorized by ERISA, including 'removal of [a] fiduciary.' 29 U.S.C. § 1109(a). The plaintiffs also point to the Plan's limitations on damages remedies, which only allow damages to compensate an individual claimant. By contrast, ERISA allows claimants to bring representative actions, seeking relief on behalf of the plan as a whole…. The plaintiffs are correct; the Plan's arbitration clause may not be enforced. The Plan's arbitration procedures prohibit representative actions seeking relief on behalf of a plan even though ERISA expressly provides for such actions. Id. Additionally, the Plan prohibits arbitral remedies with 'the purpose or effect of providing additional benefits or monetary relief' to other claimants. This provision imposes a limitation on relief that ERISA does not contain, and precludes remedies that ERISA expressly authorizes, such as the removal of a fiduciary" (citation omitted).

***Beco v. Fast Auto Loans, Inc*., No. G059382 (Calif. Ct. App. 4 Dec. 14, 2022)**: "Taken together, the fee and cost-shifting limits, the restriction on limitations periods, and the limits on discovery create substantial substantive unconscionability. These provisions are entirely one-sided and serve to benefit only FastAuto, not its employees. The removal of statutory fee-shifting provisions undoubtedly makes it more difficult to find an attorney willing to take an employee's case. The removal of the ability to recover costs, including expert witness costs, makes pursuing a case more difficult and expensive for the employee. Potentially shifting all the costs of arbitration to the employee after one day creates uncertainty and leaves the employee wondering if he or she could wind up even worse off than before because he or she tried to seek the protection of the law. The limitations on discovery – indeed, the prospect that no discovery at all might be allowed – make it that much harder for an employee to meet his or her burden of proof before an arbitrator. And the incredibly short limitations period, anywhere from months to years shorter than the statutory equivalent, can leave an employee with no relief at all. When added to the adhesive nature of the agreement and the oppression present in its execution, we find the trial court had substantial evidence from which it could determine the entire agreement was unconscionable and unenforceable." (*ed: An* Alert *h/t to Editorial Board member Peter R. Boutin, Esq., of Keesal, Young & Logan, for alerting us to this decision.*)

***Githaiga v. TD Ameritrade*, FINRA ID No. 22-00240 (Washington, DC, Nov. 16, 2022)**: A customer alleging that an unauthorized trade occurred in his securities account in error and seeking rescission of the trade loses his case against Respondent broker-dealer. *Provided courtesy of SAC's ARBchek facility (www.arbchek.com).*

***Destigter v. Beliakov*, FINRA ID No. 21-02686 (Omaha, NE, Nov. 18, 2022)**: Despite being granted his Motion for Default Judgment pursuant to FINRA Rule 12801 of the Code, a customer (on behalf of his IRA) loses his case against the only remaining Respondent in this matter. The customer's claim involved an allegation that he was overcharged for commissions and placed in unsuitable real estate investment trusts. *Provided courtesy of SAC's ARBchek facility (www.arbchek.com).*
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ARTICLES OF INTEREST: RECENT NEWS FROM THE ADR FRONT

Jose Pereyó, *Avoiding Res Judicata – Collateral Estoppel Pitfalls in Multi-Fora Disputes*, Kluwer Arbitration Blog (Dec. 19, 2022): "A slate of recent cases reminded us how important are the doctrines of res judicata and/or collateral estoppel. Put simply, res judicata is known as claim preclusion because a judicial judgment or arbitral award deciding a particular 'claim' will be binding on the parties who participated in that proceeding, whereas collateral estoppel is known as issue preclusion because a party is prevented from re-litigating with another party an issue of fact or law that was previously addressed and dealt with in a prior litigation. Both doctrines, as we will see in this post, are instrumental in multi-fora disputes: that is when parties or related parties engage in separate proceedings (either in parallel or in sequence) on related issues and claims."

***Finra Fines Edward Jones $1.1M for Missing Phone Records*, Financial Advisor IQ (Dec. 15, 2022)**: "The Financial Industry Regulatory Authority says it has ordered Edward Jones to pay $1.1 million for failing to produce phone records the industry self-regulator requested in 10 separate investigations over a period of nearly four years.[] In February 2017, the St. Louis-based broker-dealer implemented a policy of purging call-detail records older than 18 months from its internal storage, according to a letter of acceptance, waiver and consent filed Monday."

***New FINRA Foundation Research Examines Changing Investor Demographics, Preferences And Attitudes*, Mondo Visione (Dec. 15, 2022)**: "A substantial proportion of investors joined the market relatively recently, younger investors are more likely to engage in riskier investment behaviors and a third of investors are considering investing in cryptocurrencies. These are just some of the findings contained in new research released today by the FINRA Investor Education Foundation (FINRA Foundation).[] The study, 'Investors in the United States: The Changing Landscape,' reveals a new generation of younger and less experienced investors that is vastly different from older generations in their investment behaviors and attitudes."

***Arbitration Statistics 2021 – Have the Numbers of Arbitration Proceedings Reached their Ceiling?*, Baker & McKenzie Blog (Nov. 23, 2022)**: "As every year, we have taken a closer look at the statistics that are available for arbitration proceedings at some of the most important arbitral institutions.[] Over the last four years, the picture has always been the same: the number of proceedings was rising – in Europe, in the Americas as well as in Asia. This picture seems to have changed in 2021: some institutions have achieved new records, such as the ICSID. However, most of the institutions did not achieve new records, despite having had a good year. The number of new cases has dropped at the ICC, SCC, SIAC, HKIAC, DIS.[] Do we see a turning point or a ceiling? Probably not. The numbers remain impressively high" (footnotes omitted).

***Finra Tweaks Remote Inspection Proposal to Pacify Critics*, AdvisorHub (Dec. 19, 2022)**: "The Financial Industry Regulatory Authority, in an attempt to address criticisms from state regulators and investor advocates, among others, has amended its proposal to allow brokerages to complete their internal inspection obligations remotely beyond year-end 2023…. Finra's tweaks would call for brokerages to consider more risk factors when determining if locations are eligible for remote inspections. Finra specifically wants firms to evaluate a location based on its trade volume, the complexity of the products it sells, the vulnerabilities of its clients, and the risk-levels of its brokers, including if any are under heightened supervision."

***SCOTUS Set to Resolve Circuit Split over Stays Pending Arbitration Appeal*, Lexology (Dec. 23, 2022)**: "The Supreme Court recently granted certiorari in a case to resolve a circuit split that has serious implications for companies who are unsuccessful in their efforts to enforce arbitration provisions in federal district courts.[] In *Coinbase, Inc. v. Bielski*, No. 22-105, the defendant moved to compel arbitration in two putative class

actions. The motions to compel were denied, and the defendant sought stays while it appealed the denials—which the Federal Arbitration Act gives defendants an automatic right to do. See 9 U.S.C. § 16. Both motions to stay were denied, and the Ninth Circuit affirmed both decisions.[] Federal appellate courts are divided over whether litigation must be stayed when a defendant appeals a denial of its motion to arbitrate."

***Morgan Stanley to Pay $800K for Overcharging Clients*, ThinkAdvisor (Dec. 28, 2022)**: "Morgan Stanley agreed to pay restitution of $802,483 plus interest to settle allegations its supervisory system mistakenly failed to provide more than 2,000 clients with mutual fund sales charge waivers and fee rebates to which they were entitled, according to the Financial Industry Regulatory Authority.[] As a result of the error, the affected clients paid about $802,000 in excess sales charges and fees between January 2015 and December 2021, FINRA said. Therefore, Morgan Stanley violated FINRA Rules 3110 (governing supervision) and 2010 (governing standards of commercial honor and principles of trade), according to the regulator."
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DID YOU KNOW?

A GUEST "DID YOU KNOW?" COURTESY OF SCOTUS. We came across this item on the SCOTUS landing page. We repeat it *verbatim:* "**Did You Know … Congress Authorizes Funds for a New Supreme Court Building**: On December 20, 1929, Congress authorized $9,740,000 for the construction of the Supreme Court Building. The Supreme Court Building Commission, chaired by Chief Justice William Howard Taft, was charged with overseeing construction of the building.[] Since its completion in 1935, the Supreme Court Building has been the setting for many significant events in American life. Its monumental character provides an appropriate stage for the Court to fulfill its essential role in ensuring the Rule of Law in the United States, and the Building has become a symbol recognized around the world for the high principle of the words carved above its entrance, 'EQUAL JUSTICE UNDER LAW.'"
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