SECURITIES ARBITRATION ALERT 2023-20 (5/25/23)

George H. Friedman, Editor-in-Chief

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- **Iannarone, Nicole G., *A Model for Post-Pandemic Remote Arbitration?,* STETSON LAW REVIEW, Vol. 52, 2023 (Aug. 1, 2022)**
- ***FINRA Expels Firm Over Reg BI Violations,* Think Advisor (May 15, 2023)**
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- ***The FINRA Process about How to Go about Recovering Your Investment Losses*, TechBullion (May 16, 2023)**
- ***Finra Panel Orders Fidelity to Pay Options Trader Nearly $4M for Account Liquidation*, FA Magazine (May 17, 2023)**
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DID YOU KNOW?

- **Arbitration was Used to Resolve a Dispute Between the U.S. and England Arising Out of the Civil War**

Enjoy a safe and healthy Memorial Day weekend
Due to the holiday, we will be publishing on Friday next week

SQUIBS: IN-DEPTH ANALYSIS

THIRD CIRCUIT FINALLY RULES ON J&J'S REJECTION OF SHAREHOLDERS' ARBITRATION PROPOSAL. ***The issue of shareholder arbitration is in the news again, this time another court decision on Johnson &***

Johnson's rejection of a shareholder proposal. This one has quite a history, so we borrow heavily from our past coverage. We reported in SAA 2019-07 (Feb. 13) that then-SEC Chairman **Jay Clayton** in **February 2019** issued a formal Public Statement backing a staff decision to issue a "no-action letter" on Johnson & Johnson's decision to omit a shareholder proposal on arbitration. J&J had asked SEC staff for informal guidance: "on whether, under Rule 14a-8(i)(2), the company may omit from its proxy statement a shareholder proposal relating to mandatory arbitration of shareholder claims arising under the federal securities laws."

Recent History

The more recent history can be adduced by quoting the Third Circuit's Opinion in *The Doris Behr 2012 Irrevocable Trust v. Johnson & Johnson*, No. 22-1657 (3rd Cir. May 9, 2023). "Plaintiffs are shareholders of Defendant. In 2019, they submitted a proposal for inclusion in Defendant's proxy materials that would have directed the board of directors to adopt a bylaw requiring shareholders to arbitrate securities claims against the Defendant or its officers or directors. Concerned that the bylaw would violate federal and New Jersey law, Defendant informed the U.S. Securities and Exchange Commission (SEC) staff that Defendant planned to exclude the proposal and requested a no-action letter. The New Jersey Attorney General urged the SEC staff to grant no-action relief, opining that New Jersey law forbade Plaintiffs' proposed bylaw. In support of that view, the Attorney General relied on a recent Delaware Court of Chancery decision invalidating a similar bylaw. See App. 76–77 (discussing *Sciabacucchi v. Salzberg*, No. 2017-0931-JTL, 2018 WL 6719718 (Del. Ch. Dec. 19, 2018)). Treating the Attorney General's position as authoritative, the SEC staff issued a no-action letter. In reliance on that letter, Defendant omitted Plaintiffs' proposal from its 2019 proxy materials.

"Plaintiffs then sued Defendant in the District Court, seeking both a declaratory judgment confirming the legality of their proposed bylaw under both New Jersey and federal law and an injunction requiring Defendant to include the proposal in its proxy materials. As the parties litigated this suit, the Delaware Supreme Court reversed the Chancery Court opinion that the New Jersey Attorney General had relied upon before the SEC. See App. 27 (citing *Salzberg v. Sciabacucchi*, 227 A.3d 102 (Del. 2020)). Following that decision, Defendant relented in its opposition to Plaintiffs' proposal and agreed to include the proposal in future proxy materials.

"Plaintiffs subsequently resubmitted their proposal twice—once in 2022 and again in 2023. On both occasions, Defendant included the proposal in its proxy materials, but Plaintiffs withdrew their proposal before the shareholder vote.

"Defendant moved to dismiss Plaintiffs' suit for lack of subject matter jurisdiction. The District Court granted that motion and Plaintiffs timely appealed."

Third Circuit Affirms

On appeal, a unanimous Third Circuit affirms in *The Doris Behr 2012 Irrevocable Trust v. Johnson & Johnson*, No. 22-1657 (3rd Cir. May 9, 2023). The Court holds that the

Shareholders' claims are not justiciable because they are not ripe and are moot: "Plaintiffs argue that Defendant could exclude their proposal again. But Defendant's repeated inclusion of Plaintiffs' proposal in its proxy materials belies any reasonable expectation that Defendant will do so. Instead, 'the inescapable fact is—as [Plaintiffs'] speculation about [Defendant's] future actions reflects—they cannot make a reasonable showing that they will again be subjected to the alleged illegality'" (brackets in original). *(ed: We suspect this is not the last we've heard of this issue.)*
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COURT DECLINES EFFORT AT PARTIAL VACATUR OF FINRA PANEL'S $50+ MILLION AWARD AGAINST HEDGE FUND AND EXECS. ***A former D.E. Shaw money manager, who prevailed to the tune of $52.1 million in his defamation claim against the firm and four senior executives, fails in his attempt to have the Court vacate the part of the Award denying his $14 million claim for statutory and other damages.*** We reported in SAA 2022-26 (Jul. 7) that a former D.E. Shaw money manager prevailed to the tune of $52.1 million in his defamation claim against the firm and four senior executives (see *Michalow v. D.E. Shaw & Co., L.P.*, FINRA ID No. 18-03174 (New York, NY, Jun. 29, 2022)). Although he had prevailed in what, according to the SAC Award Database, was the tenth largest award in any type of dispute in any forum and the eighth largest compensatory damages award, former money manager Dan Michalow sought to vacate the part of the Award denying his claim for an additional $14 million in damages for violation of New York Labor Law § 193; breach of contract; and unjust enrichment. The Court in *Michalow v. D.E. Shaw & Co., L.P.*, No. 653480/2022 (Sup. Ct., N.Y. Cty. May 15, 2023), denies the motion to partially vacate. Borrowing heavily from our past coverage, we analyze the case below.

Claims Asserted
In Michalow's Statement of Claim: "Claimant asserted the following causes of action: defamation; gender discrimination; violation of New York Labor Law §§ 193, 198 et. seq.; breach of contract; and unjust enrichment. In the Amended Statement of Claim, Claimant asserted the following causes of action: defamation; violation of New York Labor Law §§ 193, 198 et. seq.; breach of contract; and unjust enrichment."

Damages Sought
Michalow sought: "defamation damages of $600,000,000.00; discrimination damages of $600,000,000.00; damages emanating from Respondents' failure to provide Claimant with his deferred compensation, and his 2018 compensation; punitive damages of $600,000,000.00; and such other and further relief, including but not limited to, statutory interest, attorneys' fees, filing fees, and costs. In the Amended Statement of Claim, Claimant requested defamation damages of $600,000,000.00; damages from Respondents' failure to provide Claimant with his deferred compensation and 2018 prorated compensation with statutory interest; liquidated damages to which he is entitled under New York Labor Law § 198; litigation costs, including attorneys' fees;

punitive damages; and such other relief as deemed just and proper, including but not limited to, interest, filing fees, and costs. or additional relief and damages which the Panel deemed to be just and equitable."

Respondents' Answer

Respondents: "requested an award dismissing all of Claimant's claims; ordering Claimant to pay Respondents' costs and attorneys' fees; attorneys' fees and costs in defending the defamation claim; and all other and further relief as deemed just and proper."

The Award

The Panel found the Respondents jointly and severally liable for $52,125,000 in compensatory damages for defamation. The Panel also: "specifically finds that Claimant did not commit sexual misconduct." The $93,150 in hearing session fees were assessed as follows: $46,575 against Claimant and $46,575 jointly and severally against Respondents. All other claims were denied.

Partial Vacatur Effort Fails

The *Michalow* Court states: "Daniel Michalow's motion to vacate … a portion of his $52,125,000 FINRA Award (hereinafter defined) which was granted only in respect of his defamation (first cause of action) cause of action must be denied. Simply put, Mr. Michalow has not established by clear and convincing evidence that the arbitrators' refusal to grant him relief in respect of his violation of New York Labor Law § 193 (second cause of action), (iii) breach of contract (third cause of action), and (iv) unjust enrichment (fourth cause of action) causes of action manifestly disregarded the law or otherwise violated public policy…. [T]his Court … can not [sic] conclude that Mr. Michalow has met his burden by clear and convincing evidence that the arbitrators manifestly disregarded the law."

(ed: Label us skeptics, but we think we haven't seen the last of this one.)

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SHORT BRIEFS: CONCISE NEWS YOU NEED TO KNOW

FINRA ISSUES NEW "INDUSTRY SNAPSHOT." NOTHING ABOUT ARBITRATION, BUT STILL INTERESTING NONETHELESS. FINRA on **May 4** issued the *2023 FINRA Industry Snapshot,* which: "provides a high-level overview of the industry, ranging from the number of FINRA-registered individuals to the overall revenues of firms, and from trading activity to how firms market their products and services." The 60-page publication, which was first issued in **2018**, is laden with charts, graphs, and data, and is a treasure trove of information. An accompanying Press Release, *FINRA Publishes 2023 Industry Snapshot: Options Trading Activity, Demographic Changes for FINRA-Registered Representatives Among New Data Available in this Year's Snapshot,* says that the new *Snapshot*: adds new data about options trading activity, and certain demographic changes of FINRA-registered representatives.... This year's Industry Snapshot incorporates several new topics including: Options trading activity by account owner type; Demographic changes in FINRA-registered representatives by year and firm size; Supplementary liquidity schedule providers by type

and size, and sources of liquidity; and Taxable investment account ownership data from the FINRA Foundation's National Financial Capability Study."
(ed: There's nothing about dispute resolution, but kudos to FINRA. This is a wonderful demonstration of transparency.)
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SCOTUS DENIES *CERTIORARI* IN DELEGATION CASE. The Supreme Court on **May 22** denied *Certiorari* in *Petrobras America Inc. v. Transcor Astra Group S.A.*, No. 22-518, which had sought review of *Transcor Astra Group S.A. v. Petrobras America Inc.,* No. 20-0932 (Tex. Apr. 29, 2022). We covered the case below in a "Quick Take" in SAA 2022-19 (May 19), where the Texas Supreme Court held: "At a minimum, reading the arbitration agreement and the subsequent settlement agreement together, we cannot conclude that a presently enforceable arbitration agreement clearly and unmistakably exists. We thus conclude that courts, rather than the arbitrator, must decide whether an agreement to arbitrate claims regarding the 2006 stock-purchase agreement presently exists, and for the reasons we have explained, we conclude it does not.[] In the absence of an arbitration agreement, the trial court properly decided whether the 2012 settlement agreement bars the claims Petrobras asserted in the arbitration proceeding." The **November 2022** Petition had presented this question: "Whether, when parties have entered a contract with an arbitration clause that delegates to the arbitrator questions of arbitrability, the arbitrator—rather than a court—must decide whether the contract has been superseded by a subsequent contract."
*(ed: We're not surprised. **The case appears on page 2 of the May 22 Order List.)*
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ANOTHER NJ APPELLATE COURT RULES STRICT *ATALESE* STANDARD DOESN'T APPLY TO PDAA BETWEEN SOPHISTICATED BUSINESS PARTIES. We reported in SAA 223-09 (Mar. 2) on *County of Passaic v. Horizon Healthcare Services, Inc*., No. A-0952-21 (N.J. Super., App. Div. Feb. 8. 2023) (*per curiam*). There, in a case of first impression, a unanimous New Jersey Appellate Division held that the strict "waiver of jury trial" requirement for predispute arbitration agreements ("PDAA") involving consumers articulated in *Atalese v. U.S. Legal Services Group L.P*., 219 N.J. 430 (2014), *Cert. den.* 540 U.S. 938 (2015), and its progeny does not apply to PDAAs between sophisticated parties of relatively equal bargaining positions. *Atalese* tells us that, to be enforced in New Jersey, a PDAA in a consumer context must contain a clear, unambiguous waiver of the right to a jury trial. That standard was later extended to employment matters. But the *Horizon* ruling holds that the *Atalese* test does not apply to a commercial transaction involving sophisticated business parties. Add to the list of similar holdings *Arbor Green Condo. Ass'n, Inc. v. Start 2 Finish Restoration & Bldg. Servs., LLC,* No. A-2056-21 (N.J. Super., App. Div. Apr. 24, 2023) (*per curiam*). Says the Court: "The arbitration provision here is plainly written and expressly advises the reader to select how to resolve their dispute. The agreement sets forth the rules that would apply in arbitration and the finality of an arbitration award. Plaintiff is a sophisticated party, having entered a multi-million-dollar transaction for restoration of large residential buildings, contracted for managing agents to oversee the association, and retained experts

to review defendant's work. The record lacks any evidence of an unequal bargaining power between the parties, a lack of sophistication, or of other evidence supporting plaintiff's claims it did not understand it had to arbitrate its claims against defendant." (*ed: Seems right to us.)*

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QUICK TAKES: CASES AND AWARDS WORTH READING

***Mundiales v. Bolivarian Republic of Venezuela*, No. 2019-0046 (D. D.C. May 15, 2023)**: "Plaintiffs Valores Mundiales and Consorcio Andino (together, Valores) brought this action to recognize and enforce an arbitral award issued against the Bolivarian Republic of Venezuela under the International Convention on the Settlement of Investment Disputes between States and Nationals of Other States. The Court referred the case to Magistrate Judge Robin M. Meriweather for a Report & Recommendation on four motions, two regarding a default that the Clerk entered on October 23, 2020, and cross motions for summary judgment.[] On August 3, 2022, Judge Meriweather recommended that the Court set aside the default and confirm the arbitral award and Report. Valores does not object to setting the default motion aside, but Venezuela objects to the Court confirming the arbitral award. Valores has responded to Venezuela's Objections, and Venezuela has replied.[] Upon consideration of the Report of the Report and Recommendation, the Objections, the applicable case law, and the entire record, the Court over-rules the Objections. Venezuela's Motion for Summary Judgment is **DENIED**, and Valores's Motion for Summary Judgment is **GRANTED**. Without objection, Venezuela's Motion to Set Aside Default is **GRANTED**, and Valores's Motion for Default Judgment is **DENIED** as moot (emphasis in original; footnote and internal cites omitted). (*ed: An* Alert *h/t to Editorial Board member Peter R. Boutin, Esq., of Keesal, Young & Logan, for alerting us to this decision*.)

***Rice v. Gulfstream Aerospace Corporation*, No. B316079 (Calif. Ct. App. 2 May 9, 2023)**: "Robert Rice was laid off from his employment at Gulfstream Aerospace Corporation (Gulfstream) on May 1, 2020. He sued Gulfstream for wrongful termination, age discrimination, retaliation, violation of wage and hour laws, and various other employment-related claims. Gulfstream moved to compel arbitration, arguing Rice had agreed to arbitration when he signed an employment application stating applicants were bound by the company's dispute resolution policy. In opposition, Rice disputed that a valid agreement to arbitrate was formed but argued that, even if he had agreed to arbitrate, the agreement was unconscionable. The court denied the motion, concluding the agreement was unconscionable. We affirm."

***Lennar Homes of Tex. Land & Construction, Ltd. v. Whiteley*, No. 21-0783 (Tex. May 12, 2023)**: "With respect to the subsequent purchaser, we hold that she was bound by the arbitration clause in the purchase-and-sale agreement under the doctrine of direct-benefits estoppel. As to the subcontractors, we agree with the court of appeals that the trial court did not vacate the award against them. They later intervened in the trial court, and our record contains no ruling on any motion to confirm or vacate the arbitration award with respect to the subcontractors. Accordingly, we reverse in part, render judgment

confirming the award against the purchaser, and remand to the trial court for further proceedings."

***Bowden v. Merrill Lynch*, FINRA ID No. 22-02238 (Boca Raton, FL, Mar. 31, 2023)**: An Arbitrator grants a broker's request for expungement of a complaint from his CRD record despite the objection of the customer involved. *Provided courtesy of SAC's ARBchek facility (www.arbchek.com).*

***Cowan v. Ayre*, FINRA ID No. 23-00602 (Los Angeles, CA, Apr. 7, 2023)**: In this Rule 12801 default case, a non-appearing broker is held liable to a customer for compensatory damages relating to the purchase of Foresight Energy LP stock. *Provided courtesy of SAC's ARBchek facility (www.arbchek.com).*
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ARTICLES OF INTEREST: RECENT NEWS FROM THE ADR FRONT

Iannarone, Nicole G., *A Model for Post-Pandemic Remote Arbitration?*, STETSON LAW REVIEW, Vol. 52, 2023 (Aug. 1, 2022): "Is Remote Justice Still Justice? This Article approaches the question posed in this symposium edition by looking to the future, beyond the pandemic emergency use of remote arbitration proceedings. It zooms in on one mandatory arbitration forum–the Financial Industry Regulatory ('FINRA') securities arbitration forum–describing the steps that FINRA took to evaluate remote arbitration; outlining the resulting changes to its policies, resources, and rules; and illuminating features of the FINRA forum that may position it as a model for evaluating post-pandemic remote arbitration in other mandatory arbitration forums. The Article makes several contributions to the literature on mandatory consumer arbitration."

***FINRA Expels Firm Over Reg BI Violations*, Think Advisor (May 15, 2023)**: "The Financial Industry Regulatory Authority has expelled broker-dealer SW Financial for 'multiple violations' related to Regulation Best Interest.[] FINRA found that between January 2018 and December 2021, New York-based SW Financial and Thomas Diamante, the firm's co-owner, made material misrepresentations and omitted material information in connection with the sale of private placement offerings of pre-IPO securities in violation of both FINRA rules and Reg BI's Disclosure Obligation."

***SEC Charges Red Rock Secured, Three Executives in Fraud Scheme Targeting Retirement Accounts*, www.sec.gov (May 15, 2023)**: "The Securities and Exchange Commission today announced charges against El Segundo, California-based Red Rock Secured LLC, its CEO, Sean Kelly, and two of its former Senior Account Executives, Anthony Spencer and Jeffrey Ward, in connection with a fraudulent scheme that involved convincing hundreds of investors to sell securities in their retirement accounts to buy gold and silver coins at prices that included markups far greater than the defendants had promised."

***The FINRA Process about How to Go about Recovering Your Investment Losses*, TechBullion (May 16, 2023)**: "In the ever-changing world of investments, even the most

experienced investors occasionally suffer unexpected losses. Whether brought on by market turbulence, false advice, or dishonest business practices, investment losses can have catastrophic financial and emotional effects. The Financial Industry Regulatory Authority or FINRA, is a structure that exists to assist those who have suffered investment losses, offering a clear and structured path toward potential recovery.[] However, understanding the intricacies of this process, and knowing how to navigate it effectively can be daunting for individuals unfamiliar with the regulatory landscape."

Finra Panel Orders Fidelity to Pay Options Trader Nearly $4M for Account Liquidation**, FA Magazine (May 17, 2023)**: "Fidelity Brokerage Services and its affiliate, National Financial Services, have been ordered to pay nearly $4 million to an options trader who claimed the firms improperly liquidated his account, resulting in substantial losses, following the market downturn amid the pandemic in March 2020.[] A Financial Industry Regulatory Authority arbitration panel awarded Rotem Perelmuter of San Francisco, Calif., $3,976,048.00 in compensatory damages after nine days of testimony, according to the award document" (*ed: link to Award added by the* Alert.)

FINRA Warns Recommendations Might Trip Reg BI Enforcements, Even Though Murkiness Exists**, Financial Planning (May 18, 2023)**: "When does listing investment options for a client cross the line into becoming a recommendation?[] That's one of the big questions regulators at the second day of the Financial Industry Regulatory Authority's annual conference in Washington, D.C., said broker-dealers should be asking themselves. James Wrona, vice president and associate general counsel for the broker-dealer industry's self-regulator, said a lot of firms try to march right up to the edge of giving a recommendation without going over."
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DID YOU KNOW?

ARBITRATION WAS USED TO RESOLVE A DISPUTE BETWEEN THE U.S. AND ENGLAND ARISING OUT OF THE CIVIL WAR. Ever hear of the *Alabama Claims of 1862 – 1872*? Neither had we. It seems that after the Civil War the United States asserted claims against England, whose shipbuilders had supplied warships to the Confederacy. Things got serious. According to History Central: "at one point, a claim was made that Britain was responsible for half the cost of the war, and that the U.S. would consider Canada proper payment. This shocked the British and they realized they had better come to some agreement soon." The dispute was submitted to arbitration in accordance with the *Treaty of Washington*. The arbitration was held in Geneva before a five-person arbitration tribunal consisting of Arbitrators designated by the heads of state of Britain, the United States, Brazil, Italy, and Switzerland. How did it turn out? Although in the end they got to keep Canada, Britain had to pay the U.S. $15,500,000 in gold – over $385 million today – and say they were sorry. Here's the Award.
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