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Second Circuit Holds Forum Selection Clause Supersedes FINRA's Mandatory Arbitration Rule

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In Goldman, Sachs & Co. v. Golden Empire Schools Financing Authority, No. 13-797-cv, 2014 WL 4099289 (2d Cir. Aug. 21, 2014), the United States Court of Appeals for the Second Circuit held that a forum selection clause in a broker-dealer agreement superseded FINRA's mandatory arbitration rule. FINRA Rule 12200 compels members to arbitrate disputes if (1) the customer requests arbitration and (2) the dispute arises in connection with the member's business activities. In Golden Empire, the Second Circuit ruled that a broad forum selection clause, requiring "all actions and proceedings" related to the parties' transactions to be brought in court, trumped Rule 12200. As discussed more fully below, Golden Empire marks a growing circuit split over the availability of mandatory FINRA arbitration in light of such a broad, all-inclusive forum selection clause. It also raises several important issues for future litigation.

The Second Circuit's decision disposed of two related cases originating in the Southern District of New York: Goldman, Sachs & Co. v. Golden Empire Sch. Fin. Auth., 922 F. Supp. 2d 435 (S.D.N.Y. 2013); Citigroup Global Mkts. Inc. v. N.C. E. Mun. Power Agency, No. 13 CV 1703 10 (S.D.N.Y. May 10, 2013). In each case, public financing authorities retained financial services firms as underwriters and broker-dealers in connection with the issuance of auction rate securities ("ARS"). The parties entered into broker-dealer agreements containing effectively the same forum selection clause:

The parties agree that all actions and proceedings arising out of this Broker–Dealer Agreement or any of the transactions contemplated hereby shall be brought in the United States District Court in the County of New York and that, in connection with any such action or proceeding, submit to the jurisdiction of, and venue in, such court.

The agreements also included a merger clause stating that they "contain the entire agreement between the parties relating to the subject matter hereof."

After the public financing authorities commenced FINRA arbitrations pursuant to Rule 12200, the financial services firms brought actions for declaratory and injunctive relief dismissing the arbitrations. In each case, the District Court granted the firm's motion for preliminary injunction on the grounds that the forum selection clause trumped FINRA's mandatory arbitration rule. The public financing authorities appealed.

On appeal, the Second Circuit affirmed the rulings below. The Court observed that, under Circuit precedent, a subsequent agreement containing a forum selection clause supersedes a prior agreement to arbitrate if the clause "specifically precludes arbitration." For example, in Bank Julius Baer & Co. v. Waxfield Ltd., 424 F.3d 278 (2d Cir. 2005), the Second Circuit held that a forum selection clause, providing that a bank's customer "submits to the jurisdiction of any New York State or Federal court" and "agrees that any Action may be heard" in such court, did not supersede an arbitration agreement because the provision did not specifically preclude arbitration. Id. at 282 (emphasis in original). By contrast, in Applied Energetics, Inc. v. NewOak Capital Markets., LLC, 645 F.3d 522 (2d Cir. 2011), the Second Circuit held that an agreement, stating that "[a]ny dispute arising out of this Agreement shall be adjudicated in" New York courts, and that the related agreements "constitute the entire understanding and agreement" of the parties, did supersede a prior agreement to arbitrate because the forum selection clause's "all-inclusive" and "mandatory" language specifically precluded arbitration, even though it did not mention arbitration. Id. at 525. Applying this precedent to Golden Empire's and NCEMPA's claims, the Court found the forum selection clause in the two appeals indistinguishable from the provision in Applied Energetics. Accordingly, the Court held that these provisions require "disputes arising out of the broker-dealer agreements [to] be adjudicated in the Southern District of New York, and they thus supersede the background FINRA arbitration rule."

Notably, in affirming the district court's rulings, the Second Circuit rejected the argument that the phrase "all actions and proceedings" does not include arbitrations, observing that "[a]rbitrations are regularly described as 'proceedings' by the United States Supreme Court, our Circuit, New York state courts, the C.P.L.R., and the FINRA rules."

The Second Circuit's decision in Golden Empire signals a growing circuit split over the availability of mandatory FINRA arbitration in the presence of a forum selection clause precluding arbitration. On one side of the split are the Second Circuit and United States Court of Appeals for the Ninth Circuit, with the United States Court of Appeals for the Fourth Circuit on the other. Compare Goldman, Sachs & Co. v. City of Reno, 747 F.3d 733 (9th Cir. 2014) (holding that a broad forum selection clause superseded FINRA Rule 12200), with UBS Fin. Servs., Inc. v. Carilion Clinic, 706 F.3d 319 (4th Cir. 2013) (reaching the opposite result with respect to a nearly identical clause).

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