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Firms Have Roadmap for Expanding Litigation of Customer Disputes After Second Circuit Holds Forum Selection Clauses Trump FINRA's Mandatory Arbitration Rule

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In the recent decision, *Goldman Sachs & Co. v. Golden Empire Sch. Fin. Auth.*, 764 F.3d 210 (2d Cir. 2014), the Second Circuit held that nearly-identical forum selection clauses in broker-dealer agreements between the broker-dealers/underwriters of auction rate securities ("ARS") and the public financing authorities who issued the ARS superseded the Financial Industry Regulatory Authority, Inc. ("FINRA") rule mandating arbitration between a customer and member. In so holding, the Second Circuit potentially has opened an avenue for firms seeking to litigate – rather than arbitrate – customer disputes subject to FINRA's mandatory arbitration rule.

In *Golden Empire*, the Second Circuit decided two district court cases, *Goldman Sachs & Co. v. Golden Empire Sch. Fin. Auth.*, 922 F. Supp. 2d 435 (S.D.N.Y. 2013) and *Citigroup Global Mkts. Inc. v. N.C. E. Mun. Power Agency*, No. 13 CV 1703 (S.D.N.Y. May 10, 2013). In those cases, the parties' broker-dealer agreements ("BDAs") included a forum selection clause providing that, "all actions and proceedings arising out of this [BDA] 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." In 2012, the municipal authorities instituted separate FINRA arbitrations in connection with the ARS market collapse during the financial crisis. Goldman Sachs and Citibank then sought to enjoin those arbitrations in the Southern District of New York. In both cases, the district court found that the forum selection clauses in the BDAs superseded FINRA's Rule 12200 governing arbitration.

In affirming the decisions below, the Second Circuit noted that whether similar forum selection clauses supersede the mandatory obligation to arbitrate under FINRA Rule 12200 "has been the subject of litigation in multiple circuits, with decidedly mixed results," highlighting the Ninth Circuit decision, *City of Reno v. Goldman Sachs & Co.*, 747 F.3d 733 (9th Cir. 2014), holding that "such a forum selection clause supersedes Rule 12200," and contrasting the Fourth Circuit decision, *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319 (4th Cir. 2013), holding that "a nearly identical forum selection does not supersede Rule 12200." The Second Circuit held that "an agreement to arbitrate is superseded by a later-executed agreement containing a forum selection clause if the clause specifically precludes arbitration, but there is no requirement that the forum selection clause mention

arbitration."

The Second Circuit also distinguished an earlier case, *Bank Julius Baer & Co. v. Waxfield Ltd.,* 424 F.3d 278 (2d Cir. 2005), where it held that "an arbitration agreement was not superseded by an agreement providing that a bank's customer submit to the jurisdiction of any New York State or Federal court' and 'agrees that any Action may be heard' in such court" by holding that the "subsequent agreement was not exclusive of any rights or remedies provided under any other agreements."

The Second Circuit also rejected the municipal authorities' arguments that the BDAs did not cover their entire relationship with the broker-dealers/underwriters and that, in any event, the language in the forum selection clause, "all actions and proceedings," did not include arbitrations. The Second Circuit explained that the forum selection clauses in the BDAs were broadly worded and plainly included the ARS issuances and held that "all actions and proceedings" must be interpreted based on its plain meaning; arbitrations are regularly described as "proceedings" by the U.S. Supreme Court, the Second Circuit, New York state courts and the FINRA rules. The Second Circuit concluded by noting its disagreement with the Fourth Circuit's conclusion in *Carilion Clinic*, rejecting that District's reasoning that "if 'all actions and proceedings' includes arbitration proceedings, then 'the paragraph becomes nonsensical' because it would require arbitration proceedings to be 'brought' in federal court."

On September 4, 2014, the municipal authorities filed a motion to stay issuance of the mandate for 90 days to file a petition for a writ of certiorari with the U.S. Supreme Court with the Second Circuit, which was granted on September 16, 2014. In their motion, the municipal authorities argued that their writ of certiorari would present three substantial questions to the Supreme Court:

1. the Second Circuit's opinion conflicts with opinions from other circuits that apply a presumption in favor of arbitration when a party claims a broad arbitration agreement is waived or superseded through a subsequently executed forum selection clause that does not specifically reference arbitration;

2. the Second Circuit's "recognized" split with the Fourth Circuit decision; and

3. the Second Circuit's opinion is contrary to Supreme Court precedent and pro-arbitration policies of the Federal Arbitration Act.

Notably, the municipal authorities in *City of Reno* had previously filed a petition for a writ of certiorari with the Supreme Court on August 7, 2014, making arguments similar to those raised by the municipal authorities in *Golden Empire*. Supreme Court Case No. 14-146. On November 10, 2014, the Supreme Court denied that petition. Though the *Golden Empire* municipal authorities have until December 15, 2014 to file their petition for a writ of certiorari with the Supreme Court, it seems unlikely that the Supreme Court will grant their petition so soon after denying the petition for a writ of certiorari in *City of Reno*.

Given the pro-claimant shift that FINRA arbitration rules have taken in recent years, if left undisturbed, the Second Circuit's decision in *Golden Empire* has the potential to remove from FINRA's purview *any* dispute where the parties agreed to a forum selection clause like the one in *Golden Empire*. It remains to be seen whether firms will now elect to attempt to expand this apparent carve-out from mandatory arbitration to a larger group of potential disputes with customers.

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