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## Arbitration and FINRA's Customer Code: A Tailored Approach to When a Forum Selection Clause May Supersede FINRA Rule 12200

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**ARBITRATION AND FINRA’S CUSTOMER CODE:  
A TAILORED APPROACH TO WHEN A FORUM  
SELECTION CLAUSE MAY SUPERSEDE FINRA  
RULE 12200**

*Peter Giovine\**

*This Note examines a circuit split concerning whether forum selection clauses supersede Financial Industry Regulatory Authority (FINRA) Rule 12200, which requires FINRA members to arbitrate customer disputes upon the customer’s request. The U.S. Courts of Appeals for the Second and Ninth Circuits have upheld a waiver of the right to arbitrate even when arbitration is not explicitly mentioned in a forum selection clause. The U.S. Courts of Appeals for the Third and Fourth Circuits, on the other hand, have held that a forum selection clause that does not explicitly mention arbitration does not supersede FINRA Rule 12200. This Note explores this circuit split and advocates for a middle ground between the two approaches, suggesting that such forum selection clauses should control over FINRA Rule 12200 only for institutional customers. In such cases, the parties are more likely to thoroughly negotiate a forum selection clause and intend for it to mean exactly what it says: that the forum selected in the contract should control.*

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## INTRODUCTION

On December 14, 2018, Adam Ausloos, an investment adviser and owner of Tax Deferral Trustee Services, LLC, initiated an arbitration before the Financial Industry Regulatory Authority (FINRA)<sup>1</sup> against Robert Binkele, a registered representative of a broker-dealer.<sup>2</sup> FINRA's rules govern broker-dealers and associated persons like Binkele.<sup>3</sup> FINRA rules state that a customer, which Ausloos claimed to be, is entitled to arbitration at FINRA's forum if the customer requests it.<sup>4</sup> However, here, the parties agreed to a forum selection clause which stated that "any dispute arising out of" their agreement would be settled elsewhere.<sup>5</sup> Binkele did not respond in an attempt to avoid "submitting to FINRA's jurisdiction."<sup>6</sup> When Binkele sought to enjoin arbitration in federal court, the district court was left with a choice: either follow the contract and enjoin FINRA arbitration or follow FINRA rules and allow FINRA arbitration, which would result in a \$125,000 default judgment.<sup>7</sup> The court chose the former, stating that Binkele would "suffer irreparable harm" if forced into FINRA arbitration.<sup>8</sup>

Courts have recently grappled with the question at the center of *Binkele v. Ausloos*<sup>9</sup>: when a broker-dealer's customer freely signs a contract waiving FINRA arbitration, should this contract supersede FINRA rules? A circuit split has emerged around this issue. The U.S. Courts of Appeals for the Second and Ninth Circuits uphold waiver for FINRA arbitration even when arbitration is not explicitly mentioned.<sup>10</sup> The U.S. Courts of Appeals for the Third and Fourth Circuits have found identical forum selection clauses to not

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1. FINRA is a government-authorized nonprofit organization tasked with protecting investors and safeguarding market interests. *See* 15 U.S.C. § 78o-3(b)(6); *Restated Certificate of Incorporation of Financial Industry Regulatory Authority, Inc.*, FINRA, <https://www.finra.org/rules-guidance/rulebooks/corporate-organization/restated-certificate-incorporation-financial> [<https://perma.cc/3F3H-M8Y5>] (last visited Nov. 7, 2022); *What We Do*, FINRA, <https://www.finra.org/about/what-we-do> [<https://perma.cc/3XYW-KK9W>] (last visited Nov. 7, 2022); *infra* Part I.A.1.

2. *See Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368, at \*2 (D. Nev. July 16, 2019); Complaint for Declaratory Judgment and Relief at 3, *Centaurus Fin., Inc. v. Ausloos*, No. 19-cv-243, 2019 U.S. Dist. LEXIS 77680 (E.D. Wis. May 8, 2019), ECF No. 1.

3. *See* FINRA RULE 12100 (FINRA 2022) (defining "associated person" to include a person registered under FINRA rules as well as a person "directly or indirectly" controlled by a FINRA member); *id.* 12200 (FINRA 2008); *What We Do*, *supra* note 1; *infra* text accompanying note 43.

4. *See Binkele*, 2019 U.S. Dist. LEXIS 225368, at \*4; FINRA RULE 12200.

5. *See Binkele*, 2019 U.S. Dist. LEXIS 225368, at \*2.

6. *See* Motion for Temporary Restraining Order & Preliminary Injunction at 2, *Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368 (D. Nev. July 15, 2019), ECF No. 5.

7. *See Binkele*, 2019 U.S. Dist. LEXIS 225368, at \*7.

8. *See id.* at \*7–8. The preliminary injunction was also granted on the grounds that Binkele was not acting as an associated person at the time of the contract's execution. *See id.* at \*4–5.

9. No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368 (D. Nev. July 16, 2019).

10. *See* *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 216 (2d Cir. 2014); *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 754 (9th Cir. 2014).

constitute waiver of a customer's arbitration right.<sup>11</sup> FINRA, the self-regulatory organization (SRO) designated by Congress to monitor the securities industry,<sup>12</sup> has weighed in on the side of the Third and Fourth Circuits through Regulatory Notice 16-25, which asserts that FINRA members might even face discipline for inserting forum selection clauses into their agreements with customers.<sup>13</sup> Nevertheless, the split persists, with district courts in the Second and Ninth Circuits following controlling precedent and allowing waiver.<sup>14</sup>

This Note advocates for courts to adopt an approach potentially beneficial to both broker-dealers and their customers by reading forum selection clauses to waive the customer's arbitration right only for institutional customers. This approach would allow broker-dealers to use the more extensive process provided by litigation in cases like *Binkele* in which the customer is not a retail customer, while preserving the right to arbitrate for customers whose hope for relief is FINRA arbitration.

This Note focuses on the circuit split, discussing the reasoning of the circuit courts and certain district courts, as well as FINRA's reaction to the split.<sup>15</sup> Part I describes FINRA arbitration and three lines of cases that set the stage for the circuit split. Part II utilizes circuit and district court decisions to discuss the central issues on both sides. Part III argues that courts should adopt a compromise approach, permitting waiver for institutional but not retail customers.

#### I. FINRA, ARBITRATION, AND FORUM SELECTION CLAUSES

This part details background information regarding FINRA, securities arbitration, and FINRA Rule 12200. Part I.A discusses the statutory and regulatory landscape of securities arbitration. Then, Part I.B describes three key issues central to the circuit split that affect whether a court allows waiver.

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11. *See Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87, 103 (3d Cir. 2018); *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 330 (4th Cir. 2013).

12. *About FINRA*, FINRA, <http://www.finra.org/AboutFINRA> [https://perma.cc/HT7Y-659Q] (last visited Nov. 7, 2022).

13. *See FINRA, REGULATORY NOTICE 16-25: FORUM SELECTION PROVISIONS INVOLVING CUSTOMERS, ASSOCIATED PERSONS AND MEMBER FIRMS 1* (2016), [https://www.finra.org/sites/default/files/notice\\_other\\_file\\_ref/Regulatory-Notice-16-25.pdf](https://www.finra.org/sites/default/files/notice_other_file_ref/Regulatory-Notice-16-25.pdf) [https://perma.cc/Y7HM-WDXM].

14. *See infra* Part II.C.

15. The Note focuses on customer disputes and, as a result, does not consider associated-persons disputes, which do not implicate FINRA Rule 12200, but rather FINRA Rule 13200 and the Code of Arbitration Procedures for Industry Disputes. *See, e.g.*, *Credit Suisse Sec. (USA) LLC v. Tracy*, 812 F.3d 249 (2d Cir. 2016); *Barclays Cap. Inc. v. Pair*, No. 16-CV-173 (N.D. Ga. Mar. 15, 2017). Additionally, although courts have indicated receptivity to explicit waiver, this Note is focused on the more contentious issue of implicit waiver that gave rise to the circuit split discussed forthwith. *See Reading Health Sys.*, 900 F.3d at 104 n.83 (disapproving of implicit waiver but indicating that an explicit waiver's validity is an open question); *Carilion Clinic*, 706 F.3d at 328 (noting sufficiently specific waiver is permissible); *infra* Part I.B.3 (describing line of cases permitting waiver of FINRA Rule 12200).

### A. Regulatory and Statutory Background

A broker is “any person engaged in the business of effecting transactions in securities for the account of others.”<sup>16</sup> A dealer is “any person engaged in the business of buying and selling securities . . . for such person’s own account through a broker or otherwise.”<sup>17</sup> Brokers and dealers typically are referred to collectively as “broker-dealers” or “brokerage firms.”<sup>18</sup>

The securities industry is regulated by a number of federal laws, including the Securities Exchange Act of 1934<sup>19</sup> (the “Exchange Act”). The Exchange Act created the U.S. Securities and Exchange Commission (SEC) and empowered it with broad authority over the securities industry, granting the power to register, regulate, and oversee brokerage firms and securities SROs,<sup>20</sup> including FINRA.<sup>21</sup> Under the SEC’s supervision, FINRA writes and enforces rules governing the activities of brokerage firms, including rules on dispute resolution.<sup>22</sup> FINRA also conducts dispute resolution between broker-dealers and their customers, governed by the FINRA Code of Arbitration Procedure for Customer Disputes (the “Customer Code”).<sup>23</sup> FINRA Rule 12200 in the Customer Code establishes the requirements for when a customer dispute must be arbitrated by FINRA.<sup>24</sup>

#### 1. FINRA and Its Arbitration Forum

In 2007, the National Association of Securities Dealers (NASD) and the member regulation, enforcement, and arbitration functions of the New York Stock Exchange consolidated.<sup>25</sup> The resulting organization, FINRA, regulates almost all broker-dealers.<sup>26</sup> FINRA is a government-authorized nonprofit organization tasked with protecting investors and safeguarding

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16. 15 U.S.C. § 78c(a)(4)(A).

17. *Id.* § 78(c)(a)(5)(A).

18. *See Broker-dealer*, BLACK’S LAW DICTIONARY (11th ed. 2019).

19. 15 U.S.C. §§ 78a–78qq.

20. *See Self-Regulatory Organization*, BLACK’S LAW DICTIONARY (11th ed. 2019) (defining an SRO as a “nongovernmental organization that is statutorily empowered to regulate its members by adopting and enforcing rules of conduct,” especially “those governing fair, ethical, and efficient practices”).

21. *See The Laws That Govern the Securities Industry*, INVESTOR.GOV, <https://www.investor.gov/introduction-investing/investing-basics/role-sec/laws-govern-securities-industry> [<https://perma.cc/AD54-446K>] (last visited Nov. 7, 2022). Proposed rules are submitted to the SEC via notice-and-comment rulemaking. *See id.*

22. *See* Paul McCurdy, Philip D. Robben & Genna S. Steinberg, *The Uncertain State of FINRA Arbitration*, PRACTICAL L.J. TRANSACTIONS & BUS., Feb. 2015, at 74, 75.

23. *See Code of Arbitration Procedure for Customer Disputes*, FINRA, <https://www.finra.org/arbitration-mediation/printable-code-arbitration-procedure-12000> [<https://perma.cc/834L-75J6>] (last visited Nov. 7, 2022).

24. *See* FINRA RULE 12200 (FINRA 2008).

25. *See* Nancy Condon & Herb Perone, *News Release, NASD and NYSE Member Regulation Combine to Form the Financial Industry Regulatory Authority—FINRA*, FINRA (July 30, 2007), <https://www.finra.org/media-center/news-releases/2007/nasd-and-nyse-member-regulation-combine-form-financial-industry> [<https://perma.cc/4KAD-33QG>].

26. *See Statistics*, FINRA, <https://www.finra.org/media-center/statistics> [<https://perma.cc/UL9D-B7TS>] (last visited Nov. 7, 2022).

market interests.<sup>27</sup> Brokerage firms and their employees must register with FINRA and, in registering, agree to abide by FINRA rules.<sup>28</sup> They are subject to examination and discipline by FINRA and the SEC.<sup>29</sup>

FINRA runs the largest securities dispute-resolution forum in the United States, assisting in the resolution of disputes involving customers, brokerage firms, and their employees.<sup>30</sup> Broker-dealers often contract to resolve disputes in FINRA's forum, as the lower expense and efficiency of the process may be beneficial to customers and broker-dealers alike.<sup>31</sup>

However, recently, broker-dealers have increasingly opted to settle their disputes in court<sup>32</sup> for several reasons. FINRA's forum lacks the broad discovery permitted in court.<sup>33</sup> FINRA may decide a case on the basis of equity or industry custom, which may disadvantage broker-dealers.<sup>34</sup> Additionally, there is limited opportunity to appeal even large awards.<sup>35</sup> With no written decision unless both parties request one,<sup>36</sup> parties may be left without much guidance about what to do differently in the future. Thus, while FINRA arbitration provides benefits to both broker-dealers and customers, there are cases in which resolution in court may be optimal.

However, resolution in court is often subject to a customer's assent. Under FINRA Rule 12200, customers have a right to request arbitration at FINRA's forum.<sup>37</sup> As discussed in greater detail below, FINRA takes the position that customers do not forfeit that right by signing any agreement with a forum selection provision specifying another dispute resolution process or arbitration venue.<sup>38</sup>

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27. See *supra* note 1.

28. See *Application for Membership*, FINRA, <https://www.finra.org/rules-guidance/rulebooks/corporate-organization/application-membership> [https://perma.cc/E9A5-4XE4] (last visited Nov. 7, 2022).

29. See FINRA RULE 9211 (FINRA 2018); Jill I. Gross, *The Customer's Nonwaivable Right to Choose Arbitration in the Securities Industry*, 10 BROOK. J. CORP. FIN. & COM. L. 383, 384 (2016).

30. See *Financial Industry Regulatory Authority*, SECLAW.COM (Jan. 1, 2016, 5:29 PM), <https://www.seclaw.com/glossary/financial-industry-regulatory-authority/> [https://perma.cc/7LZ4-BRQN].

31. See Jill I. Gross, *Arbitration Archetypes for Enhancing Access to Justice*, 88 FORDHAM L. REV. 2319, 2327–30 (2020) (detailing reasons why arbitration may be quicker and less costly).

32. See Kevin Neumar, *Arbitration Agreements or Forum Selection Clauses Involving FINRA Members: Circuit Split Creates Confusion, Increases Investor Skepticism*, 17 DUQ. BUS. L.J. 289, 300 (2015).

33. See FINRA RULE 12506 (FINRA 2017); *id.* 12507 (FINRA 2017).

34. See Barbara Black & Jill I. Gross, *Making It Up as They Go Along: The Role of Law in Securities Arbitration*, 23 CARDOZO L. REV. 991, 1035–40, 1047 (2002).

35. See *STMicroelectronics, N.V. v. Credit Suisse Sec. (USA) LLC*, 648 F.3d 68, 78 (2d Cir. 2011) (noting that courts “will not vacate an award because of ‘a simple error in law or a failure by the arbitrators to understand or apply it’ but only when a party clearly demonstrates ‘that the panel intentionally defied the law’” (quoting *Duferco Int'l Steel Trading v. T. Klaveness Shipping A/S*, 333 F.3d 383, 389, 393 (2d Cir. 2003))).

36. See FINRA RULE 12904 (FINRA 2018).

37. See *id.* 12200 (FINRA 2008).

38. See FINRA, *supra* note 13, at 1.

## 2. FINRA Does Not Condone Inserting an Exclusive Forum Selection Clause to Prevent Customer-Requested Arbitration

FINRA Rule 12200 of the Customer Code states that “[p]arties must arbitrate a dispute under the Code” if three conditions are met<sup>39</sup>: First, parties must submit to FINRA arbitration if it is either “[r]equired by a written agreement, or . . . [r]equested by the customer.”<sup>40</sup> Second, the dispute must be “between a customer and a member or associated person of a member.”<sup>41</sup> Third, the dispute must “arise[] in connection with the business activities of the member or associated person.”<sup>42</sup> As defined in the Customer Code, an “associated person” includes “a natural person engaged in the investment banking or securities business who is directly or indirectly controlling or controlled by a member.”<sup>43</sup> “Customer” has a broad definition and includes those who purchase goods or services from a FINRA member or hold an account with a FINRA member.<sup>44</sup>

Further, FINRA Rule 2268 governs predispute arbitration agreements.<sup>45</sup> FINRA Rule 2268(d) states that predispute arbitration agreements may not “limit[] the ability of a party to file any claim in arbitration” or “limit[] the rules of any self-regulatory organization.”<sup>46</sup>

FINRA Regulatory Notice 16-25 draws on these rules to state that, generally, arbitration must be an option for customers.<sup>47</sup> FINRA states that any denial or limitation of “a customer’s right to request FINRA arbitration, even if the customer seeks to exercise that right after having agreed to a forum selection clause specifying a venue other than a FINRA arbitration forum, would violate FINRA Rules 2268 and 12200.”<sup>48</sup> FINRA asserts that, while courts have held otherwise, FINRA rules control.<sup>49</sup>

While courts have found that FINRA rules are contractual,<sup>50</sup> FINRA, via Regulatory Notice 16-25, disagrees.<sup>51</sup> FINRA states that because the Exchange Act mandates that most broker-dealers become FINRA members, and FINRA rules are subject to SEC approval, FINRA rules are binding and have the force of federal law.<sup>52</sup> In support, FINRA relies on *Credit Suisse*

39. FINRA RULE 12200.

40. *Id.*

41. *Id.*

42. *Id.*

43. *See id.* 12100(w) (FINRA 2022).

44. *See Citigroup Glob. Mkts. Inc. v. Abbar*, 761 F.3d 268, 275–76 (2d Cir. 2014); *infra* note 128.

45. *See* FINRA RULE 2268 (FINRA 2011).

46. *Id.* 2268(d) (FINRA 2011).

47. *See* FINRA, *supra* note 13, at 2–3.

48. *Id.* at 5.

49. *See id.* at 3, 5, 9 n.11.

50. *See infra* Part I.B.3.

51. *See* FINRA, *supra* note 13, at 3.

52. *See id.*



*First Boston Corp. v. Grunwald*,<sup>53</sup> in which the Ninth Circuit held that SEC-approved NASD arbitration procedures preempted state law.<sup>54</sup>

Finally, FINRA notes that it views the refusal to grant a customer's request for arbitration after inserting a forum selection clause as a violation of FINRA Rule 2010, which sets forth the standards of commercial honor and principles of trade.<sup>55</sup> Further, FINRA IM-12000 of the Customer Code states that "fail[ure] to submit a dispute for arbitration under the Code as required by the Code" could be seen as contravention of the just and equitable principles of trade.<sup>56</sup>

A member firm that has an agreement, even if unenforced, that is not in compliance with FINRA Rule 12200 is in violation of FINRA rules and could be disciplined.<sup>57</sup> Sanctions for noncompliance include "expulsion, suspension, limitation of activities, functions, and operations, fine, censure, being suspended or barred from being associated with a member, or any other fitting sanction."<sup>58</sup> However, it is an "open issue" whether FINRA will actually discipline members for inserting forum selection clauses in their contracts.<sup>59</sup> A search of the FINRA disciplinary proceedings database turned up one action for violation of Rule 12200.<sup>60</sup> This is the same action referenced by FINRA in Regulatory Notice 16-25<sup>61</sup>: *Department of Enforcement v. Charles Schwab & Co.*<sup>62</sup>

Charles Schwab & Company, Inc. ("Schwab") amended more than 6.8 million agreements with customers to mandate that consumers waive FINRA arbitrators' ability to consolidate claims<sup>63</sup> despite the fact that the Customer Code permits such actions.<sup>64</sup> FINRA sought to discipline Schwab for violation of FINRA Rule 2268(d), which, as described above, states that predispute arbitration agreements cannot limit SRO rules (here, Rule 12200 was limited), and for violation of FINRA Rule 2010 regarding standards of

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53. 400 F.3d 1119 (9th Cir. 2005).

54. See FINRA, *supra* note 13, at 3 & 9, n.9 (citing *Credit Suisse First Bos. Corp. v. Grunwald*, 400 F.3d 1119, 1128 (9th Cir. 2005)).

55. See *id.* at 5; FINRA RULE 2010 (FINRA 2008) ("A member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade.").

56. See FINRA, *supra* note 13, at 5 (citing FINRA IM-12000 (FINRA 2008)).

57. See *id.* FINRA has also stated that firms should review past agreements to ensure compliance. See *id.*

58. See 15 U.S.C. § 78o-3(b)(7).

59. See McCurdy et al., *supra* note 22, at 75.

60. This search was conducted on November 6, 2021, using FINRA's disciplinary actions database. Terms searched (each in a separate search) included "Rule 12200," "arbitration under an arbitration agreement," and "forum selection." These searches pull from fields including case name and document text. See *FINRA Disciplinary Actions Online*, FINRA, <https://www.finra.org/rules-guidance/oversight-enforcement/finra-disciplinary-actions-online> [https://perma.cc/9K45-4EHA] (last visited Nov. 6, 2021).

61. See FINRA, *supra* note 13, at 10 n.17.

62. No. 2011029760201, 2014 FINRA Discip. LEXIS 5 (FINRA Bd. of Governors Apr. 24, 2014).

63. See *id.* at \*1.

64. See FINRA RULE 12312(b) (FINRA 2008).

“commercial honor.”<sup>65</sup> Schwab challenged FINRA’s enforcement in federal court in *Charles Schwab & Co. v. Financial Industry Regulatory Authority, Inc.*,<sup>66</sup> but the U.S. District Court for the Northern District of California stated that the administrative remedies were not exhausted and noted that it would defer to FINRA and the SEC’s expertise in establishing an underlying agency record.<sup>67</sup> Thereafter, the FINRA board of governors found that the agreements violated FINRA Rule 2268(d).<sup>68</sup> Ultimately, Schwab settled the matter, agreeing to pay \$500,000 and to notify customers of its withdrawal of the class action waiver.<sup>69</sup>

### *B. Three Lines of Cases Central to Circumventing FINRA Arbitration*

With the legal framework underlying securities arbitration established, Part I.B focuses on three lines of cases, which, while not themselves a part of the circuit split examined in this Note, establish the fundamental principles that allow waiver of FINRA arbitration. These principles have been challenged by those who argue waiver is impermissible,<sup>70</sup> so it is essential to describe each line of cases in detail.

#### 1. Waiver of Exchange Act Provisions

*Shearson/American Express Inc. v. McMahon*<sup>71</sup> and its progeny allowed waiver of Exchange Act (and thus SRO) provisions in certain circumstances.<sup>72</sup> FINRA Rule 12200 is an SRO provision, and, as a result, *McMahon* has been cited as support for permitting waiver of FINRA Rule 12200 under the Exchange Act.<sup>73</sup>

In *McMahon*, the U.S. Supreme Court stated that section 29(a) of the Exchange Act, which forbids waiver of Exchange Act provisions, “only prohibits waiver of the substantive obligations imposed by the Exchange Act.”<sup>74</sup> The Court further noted that, although the Exchange Act provides

65. See *Charles Schwab & Co. v. Fin. Indus. Regul. Auth. Inc.*, 861 F. Supp. 2d 1063 (N.D. Cal. 2012); *supra* text accompanying notes 45–46.

66. 861 F. Supp. 2d 1063 (N.D. Cal. 2012).

67. See *id.* at 1076. This did not constitute deference granted to FINRA Regulatory Notice 16-25, a guidance document which had not yet been promulgated. See FINRA, *supra* note 13, at 1 (noting document type as guidance). Courts defer to agency guidance documents under *Kisor v. Wilke*, which makes deference contingent on several questions, such as whether the interpretation creates unfair surprise, was made by the agency, etc. See 139 S. Ct. 2400, 2418 (2019). However, deference is irregularly applied to SROs, as they are nongovernmental in nature and lack direct accountability to the legislative and executive branches. See Emily Hammond, *Double Deference in Administrative Law*, 116 COLUM. L. REV. 1705, 1757 (2016).

68. See *Charles Schwab*, 2014 FINRA Discip. LEXIS 5, at \*8.

69. See FINRA LETTER OF ACCEPTANCE, WAIVER AND CONSENT, NO. 2011029760202, at 2 (2014), [https://www.finra.org/sites/default/files/fda\\_documents/2011029760202\\_FDA\\_D826113%20%282019-1562966372043%29.pdf](https://www.finra.org/sites/default/files/fda_documents/2011029760202_FDA_D826113%20%282019-1562966372043%29.pdf) [<https://perma.cc/X7UD-P3Y4>].

70. See *infra* Part III.B (considering these arguments).

71. 482 U.S. 220 (1987).

72. See *id.* at 228; *J.P. Morgan Sec. LLC v. Quinnipiac Univ.*, No. 14-Civ-429, 2015 U.S. Dist. LEXIS 67135, at \*12 (S.D.N.Y. May 22, 2015).

73. See *Quinnipiac Univ.*, 2015 U.S. Dist. LEXIS 67135, at \*12.

74. See *McMahon*, 482 U.S. at 228.

that disputes would be settled in district court, one does not usually lose substantive rights by agreeing to arbitrate.<sup>75</sup> The question was whether the agreement “weaken[s] [one’s] ability to recover under the [Exchange] Act.”<sup>76</sup> According to the Court, the SEC maintains authority over arbitration procedures via the ability to approve or deny SRO rules, including procedures that “ensure that arbitration procedures adequately protect statutory rights”; therefore, rights were not weakened in the present case.<sup>77</sup> Other cases that built on this substantive-procedural distinction followed.<sup>78</sup>

After *McMahon*, SRO arbitration increased significantly.<sup>79</sup> In 2010, under the Dodd-Frank Wall Street Reform and Consumer Protection Act<sup>80</sup> (the “Dodd-Frank Act”), Congress amended section 29(a) of the Exchange Act to apply to rules of a “self-regulatory organization.”<sup>81</sup> Thus, section 29(a) now states explicitly that one cannot waive an SRO rule.<sup>82</sup> However, courts have still found FINRA arbitration rules regarding forum to be not substantive and have thus permitted waiver.<sup>83</sup>

Even if the Exchange Act permits waiver of forum selection rules, the presumption of arbitrability—a presumption that a dispute may be resolved by arbitrators<sup>84</sup>—if applicable, would effectively mandate reading forum selection clauses narrowly to not include waiver of arbitration. The next section discusses when the presumption of arbitrability does not apply.

## 2. The Presumption of Arbitrability

*Granite Rock Co. v. International Board of Teamsters*<sup>85</sup> and its progeny established that the presumption of arbitrability does not apply when the

75. *See id.* at 229–30.

76. *Id.* at 230 (first and third alterations in original) (quoting *Wilko v. Swan*, 346 U.S. 427, 432 (1953)).

77. *Id.* at 234.

78. *See, e.g., Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477 (1989) (holding that the venue provisions of the Exchange Act are also procedural and not substantive); *Quinnipiac Univ.*, 2015 U.S. Dist. LEXIS 67135, at \*12–13.

79. *See Black & Gross, supra* note 34, at 998–1005.

80. Pub. L. No. 111-203, 124 Stat. 1376 (2010) (codified as amended in scattered sections of the U.S.C.).

81. *See id.* §§ 927, 929T, 124 Stat. at 1852, 1867.

82. *See id.*; *see also* 15 U.S.C. § 78cc(a).

83. *See, e.g., Quinnipiac Univ.*, 2015 U.S. Dist. LEXIS 67135, at \*10 (quoting section 29(a) as amended by the Dodd-Frank Act in finding that the antiwaiver provision does not apply to forum selection clauses waiving FINRA Rule 12200); *id.* at \*11 (noting that in *Golden Empire* as well, the court implicitly considered the Exchange Act in its decision, since the parties had raised it in their postargument letters); *Credit Suisse Sec. (USA) LLC v. Tracy*, No. 14 Civ. 8568, 2015 U.S. Dist. LEXIS 4428, at \*21 (S.D.N.Y. Jan. 8, 2015), *aff’d*, 812 F.3d 249 (2d Cir. 2016).

84. Arbitrability refers to “[t]he status, under applicable law, of a dispute’s being or not being resolvable by arbitrators because of the subject matter.” *See Arbitrability*, BLACK’S LAW DICTIONARY (11th ed. 2019). This includes whether a dispute is “within the scope of the arbitration agreement.” *See id.*

85. 561 U.S. 287 (2010).

existence of an arbitration agreement itself is in question.<sup>86</sup> Courts have cited this line of cases in finding that superseding forum selection clauses implicate such a question of existence and that, as a result, the presumption of arbitrability does not apply.<sup>87</sup>

The Supreme Court has read the Federal Arbitration Act<sup>88</sup> (FAA), the statute governing contracts in interstate commerce containing arbitration provisions, to articulate a “liberal federal policy favoring arbitration agreements.”<sup>89</sup> However, the policy in favor of arbitration “is merely an acknowledgment of the FAA’s commitment to ‘overrule the judiciary’s longstanding refusal to enforce agreements to arbitrate and to place such agreements upon the same footing as other contracts.’”<sup>90</sup> The “first principle that underscores all . . . arbitration decisions” is that “[a]rbitration is strictly ‘a matter of consent,’ and thus ‘is a way to resolve those disputes—but *only those disputes*—that the parties have agreed to submit to arbitration.”<sup>91</sup> The federal policy favoring arbitration does not “override” this principle.<sup>92</sup>

In determining whether parties intended to arbitrate, courts apply a presumption of arbitrability furthering the federal policy in favor of arbitration only if there is a “validly formed” and enforceable arbitration agreement that is ambiguous as to its scope.<sup>93</sup> If it is unclear whether an agreement to arbitrate exists to begin with, then the presumption of arbitrability does not apply.<sup>94</sup> Additionally, the presumption may be rebutted.<sup>95</sup> When the presumption of arbitrability does not apply, state-law contract-interpretation rules apply instead.<sup>96</sup>

In *Granite Rock*, a concrete-and-buildings company sued for strike-related damages, and the union sought arbitration regarding the date of ratification of the collective bargaining agreement between the parties.<sup>97</sup> Since the agreement might not have been in place when the unions acted, the enforceability of the agreement itself was in question.<sup>98</sup> Additionally, the agreement covered disputes that “arise under” it, and, as a result, the agreement’s scope did not extend to cover the question of the existence of

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86. *See id.* at 313–14; *Applied Energetics, Inc. v. NewOak Cap. Mkts., LLC*, 645 F.3d 522, 526 (2d Cir. 2011).

87. *See, e.g.*, *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 215 (2d Cir. 2014); *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 744 (9th Cir. 2014).

88. 9 U.S.C. §§ 1–15.

89. *See Moses H. Cone Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24–25 (1983).

90. *See Granite Rock Co.*, 561 U.S. at 302 (quoting *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 478 (1989)).

91. *Id.* at 299 (quoting *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989)).

92. *See id.* at 302.

93. *See id.* at 301; *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 215 (2d Cir. 2014).

94. *See Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 742 (9th Cir. 2014); *Applied Energetics, Inc. v. NewOak Cap. Mkts., LLC*, 645 F.3d 522, 526 (2d Cir. 2011).

95. *See Granite Rock Co.*, 561 U.S. at 301; *Golden Empire*, 764 F.3d at 215.

96. *See City of Reno*, 747 F.3d at 742–43.

97. *Granite Rock Co.*, 561 U.S. at 294–95.

98. *See id.* at 304.

the arbitration agreement.<sup>99</sup> Thus, the Court found that the presumption of arbitrability did not apply.<sup>100</sup>

The Second Circuit, in *Applied Energetics, Inc. v. NewOak Capital Markets, LLC*,<sup>101</sup> took *Granite Rock* a step further.<sup>102</sup> Applied Energetics, Inc. and a broker-dealer, NewOak Capital Markets, LLC, agreed to NASD arbitration in a preliminary letter agreement, but also noted that a subsequent, formal agreement would follow.<sup>103</sup> The formal agreement did not mention arbitration but contained a forum selection clause: “Any dispute arising out of this Agreement shall be adjudicated in the Supreme Court, New York County or in the federal district court for the Southern District of New York.”<sup>104</sup> The court cited *Granite Rock*, and noted that the presumption of arbitrability did not apply, as the question of whether the later agreement superseded the former was a question of “whether an agreement to arbitrate ha[d] been made.”<sup>105</sup> Other courts such as the U.S. Courts of Appeals for the Eleventh and Third Circuits have similarly found that the question of whether a later agreement supersedes an earlier one is not subject to the presumption of arbitrability.<sup>106</sup> If a court accepts that the presumption of arbitrability does not apply, the question, then, becomes whether FINRA rules can be superseded by contract.

### 3. Contracting Around the SRO Arbitration Right

The Fourth and Ninth Circuits cite the line of cases following *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Georgiadis*<sup>107</sup> in noting that FINRA arbitration rules can be superseded by contract.<sup>108</sup> Thus, this third line of cases underlying the circuit split is key in determining whether parties can contract around FINRA Rule 12200.

In *Georgiadis*, the American Stock Exchange (AMEX) constitution stated that arbitration should take place via the American Arbitration Association, but a contract between the parties provided for arbitration in other fora.<sup>109</sup> The Second Circuit held that the AMEX constitution could be superseded by a customer agreement that was more specific.<sup>110</sup> However, since arbitration

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99. *See id.* at 308.

100. *See id.* at 313–14.

101. 645 F.3d 522 (2d Cir. 2011).

102. *See id.* at 526.

103. *See id.* at 523.

104. *See id.*

105. *See id.* at 525.

106. *See, e.g.,* Jaludi v. Citigroup, 933 F.3d 246, 255 (3d Cir. 2019) (“[T]he question of whether a later agreement supersedes a prior arbitration agreement is tantamount to whether there is [still] an agreement to arbitrate.”); Dasher v. RBC Bank (USA), 745 F.3d 1111, 1121–22 (11th Cir. 2014) (finding that the presumption of arbitrability did not apply).

107. 903 F.2d 109 (2d Cir. 1990).

108. *See* Goldman, Sachs & Co. v. City of Reno, 747 F.3d 733, 739 (9th Cir. 2014); UBS Fin. Servs., Inc. v. Carilion Clinic, 706 F.3d 319, 328 (4th Cir. 2013); *see also* Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth., 764 F.3d 210, 216 (2d Cir. 2014) (relying on *City of Reno* and *Carilion Clinic* in determining that FINRA Rule 12200 can be superseded).

109. *See Georgiadis*, 903 F.2d at 111.

110. *See id.* at 113.

could proceed in a different forum, the *Georgiadis* court did not consider waiver of the right to arbitrate altogether.<sup>111</sup>

The Second Circuit expounded on *Georgiadis* in *Kidder, Peabody & Co. v. Zinsmeyer Trusts Partnership*.<sup>112</sup> There, the arbitration clause had been stricken, and the contract specified that NASD rules governed.<sup>113</sup> Section 12 of the NASD Code of Arbitration Procedure required members to arbitrate if customers so requested.<sup>114</sup> The court acknowledged that contracts for arbitration could supersede a customer's SRO arbitration rights.<sup>115</sup> However, it was unnecessary to determine whether complete waiver of the right to arbitrate was possible because the agreement simply struck the arbitration clause rather than specifying an alternative forum.<sup>116</sup>

In *Anderson v. Beland (In re American Express Financial Advisors Securities Litigation)*,<sup>117</sup> the court drew on the finding in *Kidder* that "different or additional contractual arrangements for arbitration can supersede the rights conferred on [a] customer by virtue of [a] broker's membership in a self-regulating organization such as [FINRA]" and the logic of *Stolt-Nielsen S.A. v. AnimalFeeds International Corp.*,<sup>118</sup> which noted that an arbitrator gains power from the parties' agreement.<sup>119</sup> Thus, the court held that when a party gives up the right to arbitration via settlement, that party waives the arbitration right under FINRA Rule 12200.<sup>120</sup> Complete waiver of the right to arbitrate was acceptable.<sup>121</sup>

These cases opened the door for the circuit split. Circuit courts, with some exceptions detailed below,<sup>122</sup> either agreed with these three lines of cases or remained silent on these issues.<sup>123</sup> Nonetheless, the circuit split arose. The next part details why this happened and describes this split further.

## II. CIRCUIT SPLIT: SAME CLAUSE, DIFFERENT READINGS

This circuit split centers around forum selection clauses in agreements between broker-dealers and customers that do not explicitly preclude arbitration, but rather say approximately that "all actions and proceedings"

111. *See generally id.*

112. 41 F.3d 861 (2d Cir. 1994).

113. *See id.* at 862.

114. *See id.* at 863.

115. *See id.* at 864.

116. *See id.*

117. 672 F.3d 113 (2d Cir. 2011).

118. 559 U.S. 662 (2010).

119. *See In re Am. Express Fin. Advisors Sec. Litig.*, 672 F.3d at 132–33 (alterations in original) (quoting *Kidder, Peabody & Co. v. Zinsmeyer Trs. P'ship*, 41 F.3d 861, 864 (2d Cir. 1994)).

120. *See id.* at 133.

121. *See id.*

122. *See infra* Part II.A.2 (describing the Third Circuit's suggestion in *Reading Health System* that explicit waiver of the customer's arbitration right may be impermissible under section 29(a) of the Exchange Act, and describing the Third Circuit's reliance on a case that based its holding on the federal policy favoring arbitration).

123. *See, e.g., supra* notes 83, 93–96, 108 and accompanying text.

related to the agreement “shall be brought” in a specified court.<sup>124</sup> Part II.A analyzes the reasoning behind the Third and Fourth Circuits’ findings against contractual waiver of FINRA arbitration requested by the customer. Part II.B examines the reasoning of the Second and Ninth Circuits’ findings that the forum selection clauses in customer agreements may function as a waiver of a customer’s right to FINRA arbitration. Part II.C discusses the state of the circuit split today, after the release of FINRA Regulatory Notice 16-25.

*A. The Third and Fourth Circuits: Forum Selection Clauses Do Not  
Constitute Waiver of FINRA Rule 12200*

The Third and Fourth Circuits have held that forum selection clauses covering “all actions and proceedings” are not sufficiently specific to waive the customer’s arbitration right under FINRA Rule 12200.<sup>125</sup> This section discusses these circuits’ reasonings.

1. The Fourth Circuit: “All Actions and Proceedings” Fails the  
“Sufficiently Specific” Test

The Fourth Circuit in *UBS Financial Services Inc. v. Carilion Clinic*<sup>126</sup> found that a forum selection clause was not sufficiently specific to waive arbitration.<sup>127</sup> Carilion, an entity that runs numerous Virginia hospitals, contracted with UBS and Citigroup to guide it in structuring bond issues.<sup>128</sup> UBS and Citi suggested utilizing auction-rate bonds, and Carilion issued \$234,225,000 worth of auction rate securities (ARS) with UBS and Citi as broker-dealers.<sup>129</sup> In 2008, UBS and Citi no longer issued support bids for the ARS, and this led bids to fail and interest rates to increase substantially, costing Carilion millions.<sup>130</sup> Carilion’s claims included negligent misrepresentation, in that it was never told about the custom of support bids, and Carilion sought FINRA arbitration.<sup>131</sup> When Carilion requested FINRA arbitration,<sup>132</sup> UBS and Citi sought an injunction in federal court,<sup>133</sup> arguing

124. See Gross, *supra* note 29, at 387 (describing how these clauses might be inserted as a choice-of-venue provision on the presupposition that issues would be resolved in court, and thus the clause would control choice of venue); McCurdy et al., *supra* note 22, at 77–79.

125. See Reading Health Sys. v. Bear Stearns & Co., 900 F.3d 87, 102–03 (3d Cir. 2018); UBS Fin. Servs., Inc. v. Carilion Clinic, 706 F.3d 319, 330 (4th Cir. 2013).

126. 706 F.3d 319 (4th Cir. 2013).

127. See *id.* at 328–29. *Carilion Clinic* also considered whether an issuer is a customer in this context. See *id.* at 323–24. Courts define “customer” broadly, and, as a result, issuers have consistently been found to be customers. See, e.g., Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth., 764 F.3d 210, 214 (2d Cir. 2014); Goldman, Sachs & Co. v. City of Reno, 747 F.3d 733, 735–36 (9th Cir. 2014).

128. See *Carilion Clinic*, 706 F.3d at 321.

129. See *id.* at 321–22. ARS have interest rates that reset at auctions where investors bid, and the lowest-interest-rate bidder prevails. *Id.* If the bids do not fully cover the bonds sold, then the auction fails, and the new interest rate is pegged to the contractual maximum rate. See *City of Reno*, 747 F.3d at 736.

130. See *Carilion Clinic*, 706 F.3d at 322.

131. See *id.*

132. See *id.* at 328.

133. See *id.* at 322.

that the forum selection clause in their broker-dealer agreements<sup>134</sup> precluded arbitration.<sup>135</sup> They argued that the forum selection clause superseded FINRA Rule 12200.<sup>136</sup> The clause stated that “all actions and proceedings arising out of this Agreement . . . shall be brought in the United States District Court the County of New York.”<sup>137</sup>

The court described the “sufficiently specific” test—to bypass arbitration, an agreement must be “sufficiently specific to impute to the contracting parties the reasonable expectation” that they are superseding or waiving FINRA Rule 12200’s arbitration right.<sup>138</sup> The court found that the agreement was not specific enough to supersede FINRA Rule 12200.<sup>139</sup>

In so holding, the court made three main points. First, the court considered that the agreement stated that “all actions and proceedings arising out of [the agreement] shall be brought in the United States District Court in the County of New York.”<sup>140</sup> The court noted that if “actions and proceedings” encompassed arbitration, then this would mean that “arbitration” shall “be brought” in district court.<sup>141</sup> Although it could not be brought in the court itself, the court would play a part in the arbitration and award.<sup>142</sup> Thus, the phrase could mean that the arbitration would proceed, but the district court would play a role in these proceedings.<sup>143</sup> Second, the court noted that arbitration was not explicitly mentioned, and if it indeed was so central to the parties’ desires, one would presume that it would have been explicitly mentioned.<sup>144</sup> Lastly, the court noted that a broad reading of “actions and proceedings” to include arbitration would make little sense in light of the

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134. In *Carilion Clinic, City of Reno*, and *Golden Empire*, each issuance was accompanied by broker-dealer agreements that contained the forum selection provision and underwriter agreements. See *Carilion Clinic*, 706 F.3d at 329; *City of Reno*, 747 F.3d at 736; *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 212 (2d Cir. 2014). Additionally, a merger clause stating that the agreement supersedes all prior understandings strengthened the case for superseding FINRA Rule 12200. See *id.* at 212–13; *City of Reno*, 747 F.3d at 750. A merger clause may be helpful, and perhaps necessary, when there is both an underwriter agreement and broker-dealer agreement, only one of which has a forum selection clause.

135. See *Carilion Clinic*, 706 F.3d at 328.

136. See *id.* at 321.

137. See *id.* at 328. The clauses at issue in this circuit split all stated that “all actions and proceedings arising out of [the agreement] shall be brought” in a specified court. See *Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87, 91 (3d Cir. 2018); *Golden Empire*, 764 F.3d at 212; *City of Reno*, 747 F.3d at 736–37; *Carilion Clinic*, 706 F.3d at 329. As asserted below, minor differences in wording between such clauses should be immaterial. See *infra* Parts III.C.1–2.

138. See *Carilion Clinic*, 706 F.3d at 328 (first citing *Anderson v. Beland (In re Am. Express Fin. Advisors Sec. Litig.)*, 672 F.3d 113, 132 (2d Cir. 2011); and then *Smith Barney, Inc. v. Critical Health Sys. of N.C., Inc.*, 212 F.3d 858, 862 (4th Cir. 2000)).

139. See *Carilion Clinic*, 706 F.3d at 329–30.

140. See *id.* (emphasis omitted).

141. See *id.* (“In whatever way that sentence could be read, it could not be read to *preclude* arbitration; to the contrary, it presumes its availability but localizes it, albeit to a forum where it could not be pursued.”).

142. See *id.*

143. See *id.*

144. See *id.*



waiver of right to trial by jury.<sup>145</sup> The phrase, when used with mention of “courts” and “jury,” often indicates judicial resolution.<sup>146</sup> This, the court reasoned, was the “natural reading.”<sup>147</sup>

## 2. The Third Circuit: Explicit Waiver May Not Be Enforceable

In *Reading Health System v. Bear Stearns & Co.*,<sup>148</sup> the Third Circuit heard a case similar to *Carilion Clinic* in which Bear Stearns & Co. (later J.P. Morgan) served as broker-dealer for Reading Health System’s ARS issuance of more than \$500 million.<sup>149</sup> Like in *Carilion Clinic*, the customer sought FINRA arbitration and brought claims including negligent misrepresentation when the broker-dealer stopped issuing support bids in 2008.<sup>150</sup> Reading Health System brought an action for a declaratory judgment to compel J.P. Morgan to submit to FINRA arbitration.<sup>151</sup>

The Third Circuit agreed with the Fourth Circuit and found that a forum selection clause that covered “actions and proceedings arising out of” broker-dealer agreements did not cover arbitration.<sup>152</sup> The court referenced the reasoning in *Patten Securities Corp. v. Diamond Greyhound & Genetics, Inc.*,<sup>153</sup> a 1987 Third Circuit case that read a forum selection clause with more permissive language to not waive NASD arbitration rules.<sup>154</sup> The court noted that *Patten Securities Corp.* was decided based on the FAA’s policy in favor of arbitration and the principle that a party must know the rights it is waiving.<sup>155</sup> In *Reading Health System*, the court stated that the forum selection clause did not explicitly mention arbitration, and thus, it “lack[ed] the specificity required to advise Reading that it was waiving its affirmative right to arbitrate.”<sup>156</sup> In other words, a forum selection clause referencing “all actions and proceedings” was not sufficiently specific.

The court also claimed that finding waiver would “deny investors the benefits of FINRA’s arbitration program.”<sup>157</sup> Additionally, the court noted that it was hesitant to find implied waiver because FINRA Rule 12200 is “binding” and has been approved by the SEC.<sup>158</sup> The Third Circuit went a step further than the Fourth Circuit did in suggesting that explicit waiver

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145. *See id.*

146. *See id.* at 330.

147. *See id.* The U.S. District Court for the District of Minnesota also has held that a forum selection clause covering “all actions and proceedings” should not supersede FINRA Rule 12200, citing *Carilion Clinic* and employing similar reasoning. *See UBS Sec. LLC v. Allina Health Sys.*, No. 12-2090, 2013 U.S. Dist. LEXIS 17799, at \*17–18 (D. Minn. Feb. 11, 2013).

148. 900 F.3d 87 (3d Cir. 2018).

149. *See id.* at 90.

150. *See id.* at 91 & n.8; *Carilion Clinic*, 706 F.3d at 322.

151. *See Reading Health Sys.*, 900 F.3d at 90.

152. *See id.*

153. *See* 819 F.2d 400 (3d Cir. 1987).

154. *See Reading Health Sys.*, 900 F.3d at 103.

155. *See id.*

156. *Id.*

157. *Id.* at 103–04, 104 n.82.

158. *See id.* at 93–94, 103.

might not be enforceable, either.<sup>159</sup> The court explained that section 29(a) of the Exchange Act may prevent waiver because the statute states that waiver of “any rule of a self-regulatory organization shall be void,” and cited Professor Jill I. Gross’s *The Customer’s Nonwaivable Right to Choose Arbitration in the Securities Industry* as support.<sup>160</sup>

### 3. Professor Jill Gross’s Scholarly Support

Professor Gross, a prolific and accomplished securities scholar and FINRA arbitrator,<sup>161</sup> asserts that, under the statutory framework discussed above, customer-requested arbitration is indeed mandatory and should not be subject to waiver.<sup>162</sup> In *The Customer’s Nonwaivable Right to Choose Arbitration in the Securities Industry*, Professor Gross argues that section 29(a) of the Exchange Act, the so-called “anti-waiver provision,” applies to FINRA Rule 12200.<sup>163</sup> Professor Gross notes that the Dodd-Frank Act altered section 29(a) to apply to SROs.<sup>164</sup> As a result, she asserts that “section 29(a) now explicitly invalidates provisions in brokerage agreements that require customers to waive compliance with FINRA rules, whereas before Dodd-Frank, the express language of the statute appeared to apply to waivers of rules of only securities exchanges.”<sup>165</sup>

Professor Gross acknowledges that *McMahon* found that section 29(a) governs only substantive rights and that the language of the case “suggest[s]” that forum selection is procedural and not a substantive right.<sup>166</sup> However, Professor Gross reads *McMahon* narrowly, noting that the case only says that broker-dealers can compel customers to waive litigation rights under section 29(a) and should not be read broadly to permit broker-dealers to waive arbitration rights as well.<sup>167</sup> In *McMahon*, the Supreme Court did not address waiver of arbitration rights and whether it would violate section 29(a).<sup>168</sup> Professor Gross asserts that the distinction between procedural and substantive rights is “not talismanic” and, thus, the right to arbitration should

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159. *See id.* at 104 n.83. The court did not make a finding on the issue and noted that it “need not address whether an explicit waiver of the right to arbitrate would be invalid and unenforceable under Section 29(a) of the Exchange Act.” *Id.* The court’s caveat in itself is significant in light of the absence of such discussion from other circuits. *See supra* Part II.A.1; *infra* Part II.B.

160. *Reading Health Sys.*, 900 F.3d at 104 n.83 (emphasis omitted) (first quoting 15 U.S.C. § 78cc(a); and then citing Gross, *supra* note 29, at 388).

161. *See Jill Gross*, PACE UNIV., <https://law.pace.edu/faculty/jill-gross> [<https://perma.cc/3Y9R-5849>] (last visited Nov. 7, 2022).

162. *See* Gross, *supra* note 29, at 388.

163. *See generally id.*

164. *See id.* at 390.

165. *See id.*; *see also* Luke Colle, *An Investor’s FINRA Rule 12200*, 28 PIABA BAR J. 215, 229 & n. 91 (2021) (suggesting that because the Senate report refers to “enforcement issues,” Congress’s goal was to prevent circumvention of FINRA Rule 12200).

166. *See* Gross, *supra* note 29, at 391–92.

167. *See id.* at 403.

168. *See id.*

not be considered a procedural right under *McMahon*'s exception to section 29(a).<sup>169</sup>

Professor Gross also notes that according to FINRA arbitration rules, a member must “execute and file a submission agreement” when filing its answer to a customer claim.<sup>170</sup> These “agreements,” Professor Gross asserts, are written agreements to arbitrate (i.e., FINRA Rule 12200 cannot be treated as the written agreement to arbitrate).<sup>171</sup> As a result, a forum selection clause would be the earlier agreement and could not supersede the later agreement to arbitrate.<sup>172</sup>

*B. The Second and Ninth Circuits: Forum Selection Clauses Constitute Waiver of FINRA Rule 12200*

In contrast, the Second and Ninth Circuits have diverged from the Third and Fourth Circuits, finding forum selection clauses covering “all actions and proceedings” to be sufficiently specific.<sup>173</sup> However, there is some agreement between courts on both sides of the circuit split as to the use of the “sufficiently specific” test and the meaning of “customer.”<sup>174</sup> This section will discuss such issues in detail.

1. The Ninth Circuit: “All Actions and Proceedings” Passes the “Sufficiently Specific” Test

The Ninth Circuit considered whether a forum selection clause was sufficiently specific in *Goldman, Sachs & Co. v. City of Reno*.<sup>175</sup> In 2005 and 2006, Goldman served as underwriter and broker-dealer for \$211 million in ARS for the city of Reno.<sup>176</sup> The facts were substantially similar to those in the Third and Fourth Circuit cases.<sup>177</sup> Reno sought FINRA arbitration, claiming negligent misrepresentation due to Goldman's failure to notify Reno that it was placing ARS support bids.<sup>178</sup> Goldman responded by suing for a declaratory judgment that FINRA did not have jurisdiction and sought an injunction.<sup>179</sup> Goldman based its argument on the agreements between the parties, which contained a forum selection clause covering “all actions and proceedings.”<sup>180</sup>

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169. *See id.*

170. *See id.* at 401.

171. *See id.* at 400–01.

172. *See id.* at 401.

173. *See* *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 216 (2d Cir. 2014); *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 753 (9th Cir. 2014).

174. *See infra* Part II.B.2.

175. 747 F.3d 733 (9th Cir. 2014).

176. *See id.* at 735.

177. *See supra* Parts II.A.1–2.

178. *See City of Reno*, 747 F.3d at 737.

179. *See id.* at 735–37.

180. *See id.* at 737.

The court held that the forum selection clause waived Reno's arbitration right.<sup>181</sup> In its analysis, the court found that the presumption in favor of arbitrability did not apply.<sup>182</sup> Instead, because the forum selection clause, like those previously discussed, concerned FINRA rules, the existence of an arbitration agreement itself was at issue and, thus, the presumption in favor of arbitrability was inapplicable.<sup>183</sup>

In interpreting the forum selection clause itself, the court, like the *Carilion Clinic* court, employed the "sufficiently specific" test.<sup>184</sup> However, unlike the *Carilion Clinic* court, which found that the forum selection clause was not sufficiently specific,<sup>185</sup> the *City of Reno* court found that this almost identical forum selection clause was specific enough.<sup>186</sup> Although the New York Civil Practice Law and Rules (CPLR) do not consider arbitrations to be "actions" or "proceedings," the court noted that the CPLR were not referenced in the contract and, as a result, the CPLR's definition should not control.<sup>187</sup> Rather, the Ninth Circuit noted that the Supreme Court, state courts, and FINRA rules themselves refer to arbitrations as "actions" or "proceedings."<sup>188</sup> This, in the court's view, outweighed the CPLR's reference to "proceedings."<sup>189</sup> The parties did not need to include "any dispute" to cover arbitration, as "actions and proceedings" could be read just as broadly.<sup>190</sup>

The court responded to the *Carilion Clinic* court's argument that such a clause could be read to simply "localize[]" arbitration "to a forum where it could not be pursued" by stating that, although a federal court may enforce an arbitration, an arbitration by its very nature takes place outside of court.<sup>191</sup> The court also responded to the *Carilion Clinic* court's finding that reference to "jury trial" meant that the phrase "actions and proceedings" excludes arbitration, where by definition a jury is lacking.<sup>192</sup> The circuit court noted

181. *See id.* at 747.

182. *See id.* at 743.

183. *See id.*; *see also supra* Part I.B.2 (describing the presumption in favor of arbitrability). The Second Circuit later found the same, employing similar reasoning. *See Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 215 (2d Cir. 2014).

184. *See City of Reno*, 747 F.3d at 744 ("[F]orum selection clauses need only be sufficiently specific to impute to the contracting parties the reasonable expectation that they would litigate any disputes in federal court . . ."); *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 328 (4th Cir. 2013).

185. *Carilion Clinic*, 706 F.3d at 328.

186. *See City of Reno*, 747 F.3d at 744.

187. *See id.* (citing N.Y. C.P.L.R. §§ 103, 304 (McKinney 2014)).

188. *See id.* (first citing 14 Penn Plaza LLC v. Pyett, 556 U.S. 247, 269 (2009); then *Sacks v. Dietrich*, 663 F.3d 1065, 1066–67 (9th Cir. 2011); and then *City of New York v. Uniformed Fire Officers Ass'n, Local 699*, 263 A.D.2d 3, 7 (N.Y. App. Div. 1999)). *But see* FED. R. CIV. P. 1 (referring to judicial proceedings as "actions or proceedings").

189. *See City of Reno*, 747 F.3d at 745.

190. *See id.* at 745 n.4.

191. *See id.* at 745–46 (quoting *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 329 (4th Cir. 2013)).

192. *See id.* at 746.

that there would be a jury in some “actions and proceedings” but not in others.<sup>193</sup>

Judge Anthony J. Battaglia, dissenting, raised the possibility of reconciling FINRA rules with the forum selection clause by permitting arbitration and later allowing a party to challenge the award in a forum dictated by the clause.<sup>194</sup> However, the court explained that although this “alternative reading” was possible, the goal of the court is to “effectuate the intent of the parties,” not presume arbitrability.<sup>195</sup>

## 2. The Second Circuit: Furthering the “Plain Meaning” Rationale

Within months of the Ninth Circuit’s holding, the Second Circuit held that a similar forum selection clause superseded FINRA arbitration rules in *Goldman, Sachs & Co. v. Golden Empire School Financing Authority*.<sup>196</sup> Goldman Sachs served as underwriter and broker-dealer over three years for an approximately \$125 million issuance of ARS by the Golden Empire Schools Financing Authority and Kern High School District (collectively, “Golden Empire”).<sup>197</sup> Golden Empire commenced FINRA arbitration, alleging that it was fraudulently induced to offer ARS, and Goldman sought to enjoin the arbitration in federal court.<sup>198</sup> *Citigroup Global Markets Inc. v. North Carolina Eastern Municipal Power Agency*<sup>199</sup> centered around similar issues. North Carolina Eastern Municipal Power Agency (NCEMPA) used Citigroup to underwrite around \$223 million in ARS.<sup>200</sup> In 2012, NCEMPA attempted to subject Citigroup to FINRA arbitration and, in response, Citigroup brought an action for declaratory relief and injunction.<sup>201</sup> In both cases, the broker-dealer agreements included forum selection clauses encompassing “all actions and proceedings.”<sup>202</sup> The Second Circuit decided both *NCEMPA* and *Golden Empire* in one opinion.<sup>203</sup>

The Second Circuit agreed with the Ninth Circuit regarding the “sufficiently specific” test.<sup>204</sup> There was no need for a specific reference to arbitration, and rather, “all actions and proceedings” was sufficiently specific to allow the agreement to supersede FINRA Rule 12200.<sup>205</sup> The court found that the plain meaning of “actions and proceedings” included arbitrations as a type of proceeding.<sup>206</sup> FINRA rules themselves refer to arbitrations as

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193. *See id.*

194. *See id.* at 750 (Battaglia, J., dissenting).

195. *See id.* at 746 (majority opinion).

196. 764 F.3d 210 (2d Cir. 2014).

197. *See id.* at 212.

198. *See id.*

199. No. 13-CV-1703, 2013 U.S. Dist. LEXIS 188771 (S.D.N.Y. May 10, 2013).

200. *See Golden Empire*, 764 F.3d at 213.

201. *See id.*

202. *See id.* at 212–13.

203. *See id.* at 212.

204. *See id.* at 216.

205. *See id.* at 215 (citing *Applied Energetics, Inc. v. NewOak Cap. Mkts., LLC*, 645 F.3d 522, 525 (2d Cir. 2011)).

206. *See id.* at 216–17.

proceedings.<sup>207</sup> The court pointed to a number of opinions and the parties' own filings stating the same.<sup>208</sup>

The court referred to the Fourth Circuit's assertion that if "action" covers arbitration, then arbitration would have to be brought in district court as the result of a "linguistic trick."<sup>209</sup> The Second Circuit also noted that state proceedings could not be brought in federal court but fall under "all actions and proceedings."<sup>210</sup>

### 3. The Southern District of New York's Rebuttal of Professor Gross's Exchange Act Argument: Forum Selection Clauses Are Not Substantive Provisions

Within a year of *Golden Empire*, the U.S. District Court for the Southern District of New York applied binding precedent from the Second Circuit in *J.P. Morgan Securities LLC v. Quinnipiac University*.<sup>211</sup> There, J.P. Morgan served as underwriter for Quinnipiac's ARS issuance.<sup>212</sup> There was a forum selection clause covering "all actions and proceedings arising out of this Broker-Dealer Agreement."<sup>213</sup> J.P. Morgan, like the broker-dealers previously described, ceased support bids, and Quinnipiac sued for damages of more than \$20 million.<sup>214</sup> Quinnipiac raised section 29(a) of the Exchange Act, noting that it voids any provision waiving compliance with SRO rules.<sup>215</sup> The Southern District noted that the Second Circuit in *Golden Empire* had implicitly considered section 29(a) because it was raised by the parties in that case.<sup>216</sup> Even *Golden Empire* itself had acknowledged that one could contract around FINRA Rule 12200.<sup>217</sup> Additionally, the court reviewed the issue de novo and found that the Supreme Court in *McMahon* noted that section 29(a) "only prohibits waiver of the substantive obligations imposed by the Exchange Act."<sup>218</sup> This was meant to cover an agreement

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207. *See id.* at 217 (citing FINRA RULE 12405 (FINRA 2011)).

208. *See id.* at 216–17 (first quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 634 (1985) (referring to "arbitral body conducting a proceeding"); then citing *Citigroup Glob. Mkts., Inc. v. VCG Special Opportunities Master Fund Ltd.*, 598 F.3d 30, 32 (2d Cir. 2010) (referring to "arbitration proceedings"); then *City of New York v. Uniformed Fire Officers Ass'n, Local 854*, 263 A.D.2d 3, 7 (N.Y. App. Div. 1999) (calling arbitration "the proceeding"); and then N.Y. C.P.L.R. § 7505 (McKinney 2014) (referring to an "arbitration proceeding")).

209. *See id.* at 217 (quoting *Citigroup v. AllChildren's Hosp. Inc.*, 5 F. Supp. 3d 537, 541 (S.D.N.Y. 2014)).

210. *See id.*

211. No. 14-Civ-429, 2015 U.S. Dist. LEXIS 67135 (S.D.N.Y. May 22, 2015).

212. *See id.* at \*2.

213. *See id.* at \*2–3.

214. *See id.* at \*4.

215. *See id.* at \*10.

216. *See id.* at \*11.

217. *See id.*

218. *See id.* at \*12 (quoting *Dep't of Enf't v. Charles Schwab & Co.*, No. 2011029760201, 2014 FINRA Discip. LEXIS 5, at \*63 (FINRA Bd. of Governors Apr. 24, 2014)).

that “weaken[s] [a party’s] ability to recover under the [Exchange] Act.”<sup>219</sup> Since a rule determining forum is not substantive, the court found that section 29(a) would not preclude the forum selection clause from superseding FINRA Rule 12200.<sup>220</sup> Thus, the court granted a permanent injunction<sup>221</sup> and offered a rebuttal to the section 29(a) argument raised by Professor Gross.<sup>222</sup>

### C. *The State of the Circuit Split Today*

This circuit split persists, despite FINRA’s 2016 Regulatory Notice 16-25, which claimed that the Second and Ninth Circuits were incorrect in their application of the law.<sup>223</sup> In the 2019 case, *Binkele*, the U.S. District Court for the District of Nevada rejected FINRA Regulatory Notice 16-25, which had been released several years prior and explicitly denied forum selection clauses the power to override FINRA Rule 12200.<sup>224</sup> The court found that the Ninth Circuit’s holding in *City of Reno* was controlling over Regulatory Notice 16-25 and that the contract superseded FINRA Rule 12200.<sup>225</sup> The court stated that the Ninth Circuit precedent is binding, and “FINRA has no authority over federal courts in this regard.”<sup>226</sup> The court also considered the importance of freedom of contract.<sup>227</sup>

In 2020, in *New York Bay Capital, LLC v. Cobalt Holdings, Inc.*,<sup>228</sup> the Southern District of New York, like the *Binkele* court, explicitly rejected FINRA Regulatory Notice 16-25.<sup>229</sup> The clause at issue stated that “any action, suit or proceeding” would be settled in the district court.<sup>230</sup> The court noted that the statement in FINRA Regulatory Notice 16-25 that FINRA rules are mandatory does not hold water and noted that, in the Second Circuit, “a forum selection clause requiring ‘all actions and proceedings’ to be brought in federal court supersedes an earlier agreement to arbitrate.”<sup>231</sup> The court stated that “[t]he arbitration rules of an industry self-regulatory organization such as FINRA are interpreted like contract terms.”<sup>232</sup> Thus, the court granted the motion to enjoin FINRA arbitration.<sup>233</sup>

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219. *See id.* at \*12–13 (alterations in original) (quoting *Shearson/Am. Express Inc. v. McMahon*, 482 U.S. 220, 230 (1987)).

220. *See id.* at \*13.

221. *See id.* at \*15.

222. *See supra* Part II.A.3.

223. *See supra* Part I.A.2.

224. *See Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368, at \*5 n.1 (D. Nev. July 16, 2019); *see also supra* text accompanying notes 2–9.

225. *See Binkele*, 2019 U.S. Dist. LEXIS 225368, at \*5 n.1.

226. *Id.*

227. *See id.* at \*7.

228. 456 F. Supp. 3d 564 (S.D.N.Y. 2020).

229. *See id.* at 573.

230. *See id.* at 568.

231. *Id.* at 572 (quoting *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 215 (2d Cir. 2014)).

232. *Id.* at 569 (quoting *Citigroup Glob. Mkts. Inc. v. Abbar*, 761 F.3d 268, 274 (2d Cir. 2014)).

233. *See id.* at 574–75.

Later in 2020, in *Goldberg v. Bruderman Bros.*,<sup>234</sup> a New York supreme court addressed the preemption argument presented by FINRA Regulatory Notice 16-25, stating that “FINRA is, itself, a creature of federal legislation” and, as a result, federal courts deserve “substantial deference” when deciding such matters.<sup>235</sup> Thus, the regulatory notice did not control.<sup>236</sup>

As the split has persisted despite FINRA Regulatory Notice 16-25, a modified approach reconciling both sides of this circuit split is necessary. Part III will describe such an approach and consider its potential benefits.

### III. A MODIFIED APPROACH IS NECESSARY: DECIDE BASED ON THE CUSTOMER

Courts should adopt an approach beneficial to both broker-dealers and their customers by reading forum selection clauses to waive the customer’s arbitration right only when the customer is an institutional customer. Part III.A describes the proposed approach. Part III.B explores why this approach is permissible within the current legal framework. Finally, Part III.C discusses why this approach accommodates the needs of both broker-dealers and customers.

#### A. *The Proposal: Read Forum Selection Clauses to Waive the Arbitration Right Only When the Customer Is an Institutional Customer*

In cases in which there is a forum selection clause covering “all actions and proceedings” (or the like) without explicitly mentioning arbitration, the question is whether the forum selection clause should supersede FINRA Rule 12200. When the dispute involves an institutional customer, then the forum selection clause should be interpreted as warranting litigation in accordance with the Second and Ninth Circuits’ holdings.<sup>237</sup> However, when the dispute involves a retail customer, then the forum selection clause should not be interpreted to encompass arbitration in accordance with the Third and Fourth Circuits’ holdings.<sup>238</sup>

234. No. 159280/2019, 2020 NYLJ LEXIS 1654 (N.Y. Sup. Ct. Oct. 20, 2020).

235. *See id.* at \*10 n.7.

236. *See id.* at \*10. *Bruderman Bros.* and *Binkele*, unlike *New York Bay Capital, LLC* and the circuit court cases discussed above, concerned resolution in another arbitral forum rather than resolution in court. *See Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368, at \*2 (D. Nev. July 16, 2019); *Bruderman Bros.*, 2020 NYLJ LEXIS 1654, at \*2. However, *Binkele* claimed that this side of the circuit split was controlling precedent. *See Binkele*, 2019 U.S. Dist. LEXIS 225368, at \*5 n.1. Both cases concern forum selection clauses that are not explicit and are especially relevant in their responses to FINRA Regulatory Notice 16-25. *See id.* at \*5–6; *Bruderman Bros.*, 2020 NYLJ LEXIS 1654, at \*10.

237. *See Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210 (2d Cir. 2014); *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733 (9th Cir. 2014); *supra* Parts II.B.1–2.

238. *See Reading Health Sys. v. Bear Sterns & Co.*, 900 F.3d 87 (3d Cir. 2018); *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319 (4th Cir. 2013); *supra* Parts II.A.1–2.



Institutional customers should be defined based on FINRA's own definition in FINRA Rule 4512(c).<sup>239</sup> This definition is referenced throughout the FINRA rules to define institutional and retail customers.<sup>240</sup> In short, an institutional customer is determined based on a fifty-million-dollar threshold.<sup>241</sup> If an entity or person, "whether a natural person, corporation, partnership, trust or otherwise," has total assets of at least fifty million dollars, then such an entity or person would qualify as an institutional customer.<sup>242</sup> Additionally, regardless of wealth, institutional customers should include registered investment advisers, banks, savings and loan associations, insurance companies, and registered investment companies in accordance with FINRA rules.<sup>243</sup> Retail customers, under such a definition, are any customers that are not institutional customers.<sup>244</sup>

FINRA's fifty-million-dollar threshold is high enough to implicate those with substantial resources and, thus, those with substantial bargaining power when compared to broker-dealers.<sup>245</sup> These are parties less likely to enter into adhesion contracts and more likely to freely negotiate, as discussed below.<sup>246</sup> Parties with such wealth are also able to afford going to court.<sup>247</sup> FINRA has considered the fifty-million-dollar figure carefully and, for these reasons, has determined that other monetary benchmarks would not be as effective.<sup>248</sup>

FINRA's definition is also broad enough to include members that can protect themselves. The "institutional customer" definition encompasses natural persons and, as a result, very wealthy individuals who likely agreed to a contract containing a forum selection clause on advice of legal counsel could not avoid the result of such a clause.<sup>249</sup> The definition also includes parties that may freely negotiate contracts with broker-dealers, such as banks

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239. See FINRA RULE 4512(c) (FINRA 2019); see also *id.* 2111(b) (FINRA 2020). This approach simply adopts the standard from FINRA Rule 4512(c), which describes institutional customers' accounts, and thus should not be limited to those who have accounts with FINRA members but expanded to those who purchase a "good or service" from FINRA members. See *Citigroup Glob. Mkts. Inc. v. Abbar*, 761 F.3d 268, 275 (2d Cir. 2014) (noting that both groups are classified as customers under FINRA Rule 12200); FINRA RULE 2210(a)(4) (FINRA 2019) (utilizing the standard from FINRA Rule 4512(c) for institutional investors without requiring an account).

240. See, e.g., FINRA RULE 2111 (FINRA 2020); *id.* 2210 (FINRA 2019); *id.* 2330 (FINRA 2014); *id.* 2360 (FINRA 2022); *id.* 4512(c).

241. See *id.* 4512(c).

242. See *id.*

243. See *id.*

244. See *id.* 2210(a)(6) (FINRA 2019).

245. See Gross, *supra* note 29, at 388 (describing retail investors' lack of bargaining power as compared to broker-dealers).

246. See *infra* Part III.C.2.

247. See FINRA, *supra* note 13, at 1.

248. See Letter from Joseph P. Savage, Vice President & Couns., Inv. Cos. Regul., FINRA, to Elizabeth M. Murphy, Secretary, Sec. & Exchange Comm'n, at 7 (Dec. 22, 2011), <https://www.sec.gov/comments/sr-finra-2011-035/finra2011035-19.pdf> [<https://perma.cc/EAB3-MDHY>] (stating that setting the bar higher or lower than fifty million dollars would be arbitrary).

249. See FINRA RULE 4512(c) (FINRA 2019).

and many issuers.<sup>250</sup> These parties are industry professionals, tend to be sophisticated and, therefore, are less in need of protections than are retail customers.<sup>251</sup>

This approach accords with the general approach advocated by certain members of the FINRA Dispute Resolution Task Force, which includes professionals representing both public and private interests.<sup>252</sup> In a report, these members suggested interpreting a forum selection clause to constitute waiver for sophisticated customers, but not for retail customers.<sup>253</sup> The report did not further clarify what benchmark should be used to distinguish retail customers from sophisticated customers.<sup>254</sup> Sophistication itself can be an elusive term.<sup>255</sup> Wealth has historically served as a rough proxy for sophistication throughout securities laws.<sup>256</sup> Thus, sophisticated and institutional customers are often referred to synonymously.<sup>257</sup> Since there may be sophisticated retail customers, the task force approximated this

250. *See id. Compare* Goldman, Sachs & Co. v. City of Reno, 747 F.3d 733, 741 (9th Cir. 2014) (describing negotiations between issuer and broker-dealer), with Dep't of Enf't v. Charles Schwab & Co., No. 2011029760201, 2014 FINRA Discip. LEXIS 5, at \*1–2 (FINRA Bd. of Governors Apr. 24, 2014) (noting that Schwab amended customer account agreements for almost seven million customers in their account statements at the end of the month).

251. *Harsco Corp. v. Segui*, 91 F.3d 337, 343 (2d Cir. 1996) (noting that since parties were sophisticated, there was no reliance).

252. *See* FINRA, FINAL REPORT AND RECOMMENDATIONS OF THE FINRA DISPUTE RESOLUTION TASK FORCE 1 (2015), <https://www.finra.org/sites/default/files/Final-DR-task-force-report.pdf> [<https://perma.cc/RPV5-5WDE>]. In *UBS Financial Services v. West Virginia University Hospitals, Inc.*, the Second Circuit rejected an argument that FINRA arbitration rules do not consider arbitration for sophisticated customers. *See* 660 F.3d 643, 651–52 (2d Cir. 2011). However, this Note does not contend that FINRA arbitration rules are not meant to apply to sophisticated customers. Rather, it asserts that an institutional customer, while remaining a customer for FINRA purposes, should expect that an agreed-upon forum selection clause may waive its arbitration right. *See infra* Part III.C. Thus, FINRA Rule 12200 would function unchanged, granting institutional and retail customers alike the right to request arbitration and would only demarcate when it comes to sufficiently specific contractual waiver such as a forum selection clause.

253. *See* FINRA, *supra* note 252, at 49.

254. *See id.* It is possible that members would approve of the fifty-million-dollar threshold as, at the time of the report, Regulation BI had yet to be adopted, and, thus, “retail customer” often referred to those who had not met the fifty-million-dollar threshold. *See* Dana G. Fleischman, Stephen P. Wink, Laura N. Ferrell & Deric M. Behar, *What Institutional Broker-Dealers Need to Know About Regulation BI*, LATHAM & WATKINS (July 8, 2019), <https://www.jdsupra.com/legalnews/what-institutional-broker-dealers-need-86581/> [<https://perma.cc/PJ3G-EAR4>].

255. *See Accredited Investor vs. Sophisticated Investor—Deceptively Similar Terms with a Huge Difference in Definition*, VERIFYINVESTOR.COM (Jan. 29, 2021), <https://blog.verifyinvestor.com/blog/2021/1/29/accredited-investor-vs-sophisticated-investor-deceptively-similar-terms-with-a-huge-difference-in-definition> [<https://perma.cc/4J96-SPRE>].

256. *See* NATALIE N. WILSON & MICHAEL J. GORBACK, HANSONBRIDGETT, ACCREDITED INVESTORS: WEALTH IS NO LONGER THE SOLE PROXY FOR FINANCIAL SOPHISTICATION (2020), <https://www.hansonbridgett.com/Publications/articles/2020-08-27-accredited-investors-alert?pdf=1> [<https://perma.cc/E8WW-KCD5>].

257. *See, e.g.,* Gross, *supra* note 29, at 383; Jerry Markham, *Protecting the Institutional Investor—Jungle Predator or Shorn Lamb?*, 12 YALE J. ON REG. 345, 345 (1995) (“Institutions . . . are often believed to be experienced and ‘sophisticated’ investors.”).

distinction, too.<sup>258</sup> It is possible that the task force referred to retail customers and institutional customers as defined by the FINRA Customer Code.<sup>259</sup> This Note advocates precisely defining the standard based on the distinction between institutional and retail customers to avoid potential confusion.

Using the fifty-million-dollar threshold as a proxy for sophistication is both over- and under-inclusive, as a wealthy investor may lack sophistication, and a less wealthy investor may be more sophisticated.<sup>260</sup> Additionally, there may not be a major difference between investors with \$49,999,999 and those with \$50 million. However, for consistency's sake, FINRA draws the line at fifty million dollars.<sup>261</sup> Since the fifty-million-dollar benchmark is widespread and is used to define institutional customers throughout FINRA rules, investors and regulators alike will recognize this demarcation.<sup>262</sup> Broker-dealers could ensure compliance without extra cost, as they already monitor which clients meet the FINRA Rule 4512(c) test in complying with suitability and advertising rules.<sup>263</sup> Additionally, the FINRA Rule 4512(c) test, unlike a test for sophistication, is relatively clear-cut. It does not require looking into fact-specific circumstances, but rather calls for analyzing the objective measures of total assets and status.<sup>264</sup> This bright-line approach therefore makes sense.

Status as a retail customer is likely a stronger benchmark than others. One could, for example, waive arbitration whenever the amount of the claim met FINRA Rule 12401's one-hundred-thousand-dollar requirement, which is usually used to determine the number of arbitrators.<sup>265</sup> "If the amount of a claim is more than \$100,000, exclusive of interest and expenses,"<sup>266</sup> the forum selection clause would supersede FINRA Rule 12200 even if it does not explicitly mention superseding arbitration. However, the one-hundred-thousand-dollar benchmark is quite low and would run the risk of flooding the courts. Even if the amount was set higher, this approach is

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258. See FINRA, *supra* note 252, at 49.

259. See *id.*

260. As noted above, the fifty-million-dollar figure is based on parity of bargaining power between customers and broker-dealers. See *supra* text accompanying notes 242–43.

261. See FINRA, REGULATORY NOTICE 09-25: PROPOSED CONSOLIDATED FINRA RULES GOVERNING SUITABILITY AND KNOW-YOUR-CUSTOMER OBLIGATIONS 5 n.8 (2009), <https://www.finra.org/sites/default/files/NoticeDocument/p118709.pdf> [https://perma.cc/WA2D-BFBB].

262. See, e.g., FINRA RULE 2111 (FINRA 2020); *id.* 2210 (FINRA 2019); *id.* 2330 (FINRA 2014); *id.* 2360 (FINRA 2022); *id.* 4512(c) (FINRA 2019). Additionally, the metric of total assets is commonly used throughout securities law to categorize parties and determine what rights they are owed. For instance, certain disclosure exemptions to section 5 of the Exchange Act apply with regard to "accredited investors," a designation retained based in part on total assets. See 17 C.F.R. §§ 230.501, 230.506; see also 15 U.S.C. § 80a-2(a)(51) (defining the designation of qualified purchaser based in part on the amount owned in investments).

263. See FINRA RULE 2111 (FINRA 2020); *id.* 2210 (FINRA 2019).

264. See *id.* 4512(c) (FINRA 2019).

265. See *id.* 12401(c) (FINRA 2012).

266. See *id.*

difficult, as there may be a small claim brought by an institutional customer. Thus, under this approach, an issuer with in-house counsel could simply evade enforcement of a forum selection clause by claiming less in damages.

Basing a threshold on the transaction amount in a contract could be complicated as well. Oftentimes, these transactions span many contracts,<sup>267</sup> and thus there would be a question of how to value the transaction. Additionally, it is possible that a wealthy investor signed a contract with a broker-dealer for a small amount, fully understanding that the investor would be subject to litigation rather than arbitration. Thus, the stronger alternative is to distinguish based on status as a retail customer.

Courts should apply this proposed standard to the cases that come before them. Additionally, FINRA may find it useful to issue a regulatory notice adopting such an approach, as this framework would accomplish FINRA's goals. With the proposed standard explained, this Note will now discuss the permissibility of such an approach, and then discuss its potential benefits and drawbacks.

#### *B. This Approach Is Permissible Within the Current Legal Framework*

Essential to the approach advocated in this Note is the ability to supersede FINRA Rule 12200. Thus, this section will assert that forum selection clauses can supersede FINRA Rule 12200. In so arguing, this section will consider the three lines of cases discussed above, describing why waiver of FINRA Rule 12200 through a forum selection clause falls under such precedent, and it will also consider some of the major arguments raised by those who state that forum selection clauses may not supersede FINRA Rule 12200.

##### 1. Waiver of FINRA Rule 12200's Arbitration Right Is Permissible Under the Exchange Act

The Exchange Act permits waiver of FINRA Rule 12200. As described above, the Supreme Court in *McMahon* held that because Exchange Act section 29(a) only prohibits waiver of substantive Exchange Act provisions, and because arbitration agreements do not waive substantive provisions, such agreements are permissible.<sup>268</sup> Like an agreement to arbitrate, an agreement to waive FINRA Rule 12200 concerns where disputes are to be heard and, as a result, is procedural and not substantive.<sup>269</sup> Forum selection clauses should not be subject to the antiwaiver rule. Courts have extended *McMahon* to forum selection clauses and FINRA Rule 12200 specifically.<sup>270</sup>

Professor Gross's scholarship regarding section 29(a)<sup>271</sup> is not dispositive. The Dodd-Frank Act's application of section 29(a) to SRO rules does not

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267. See, e.g., *supra* note 134 (detailing multiple agreements at issue).

268. See *supra* text accompanying note 82.

269. See *supra* note 83 and accompanying text.

270. See *supra* note 83 and accompanying text.

271. See *supra* Part II.A.3.

indicate legislative intent to prevent waiver of FINRA Rule 12200.<sup>272</sup> As Professor Gross herself acknowledges, the “animating purpose” of the amendment to section 29(a) is “mysterious.”<sup>273</sup> The *Quinnipiac University* court explicitly quoted section 29(a) as amended by Dodd-Frank in finding that the antiwaiver provision does not apply to forum selection clauses waiving FINRA Rule 12200.<sup>274</sup> Additionally, the Dodd-Frank Act does not change the holding in *McMahon* permitting waiver of nonsubstantive provisions.<sup>275</sup>

Professor Gross’s narrow reading of *McMahon* as suggesting that an agreement can “waive the right to litigate” but not necessarily the right to arbitrate<sup>276</sup> should not control. While the *McMahon* Court did directly consider the waiver of the right to litigate, it also allowed waiver of obligations that are not substantive in nature.<sup>277</sup> Professor Gross’s response on this point, asserting that the substantive-procedural distinction is not “talismanic” and that courts should instead look to when agreements waive compliance,<sup>278</sup> is too far from the language of *McMahon*, which states that “§ 29(a) only prohibits waiver of the substantive obligations imposed by the Exchange Act.”<sup>279</sup> This language effectively construes section 29(a)’s compliance obligation as not waiving any substantive obligation. Additionally, the Court was not focused on formalistic or arbitrary distinctions between procedural and substantive but rather centered its inquiry on whether the agreement “weaken[s] [the] ability to recover under the [Exchange] Act.”<sup>280</sup> It is unlikely that litigation, especially in the case of institutional customers (for whom this Note suggests waiver), would weaken the ability to recover.<sup>281</sup> Courts have read *McMahon* to allow waiver of

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272. See Gross, *supra* note 29, at 390.

273. See *id.* Luke Colle, a 2021 J.D. candidate, suggested that because the Senate report refers to “enforcement issues,” Congress’s goal was to prevent circumvention of FINRA regulations, see *supra* note 165, but one cannot extrapolate from such general statements that a lawful contract would constitute an enforcement issue.

274. See *supra* note 83 and accompanying text.

275. See *supra* text accompanying note 82.

276. See *supra* text accompanying note 167.

277. See *Shearson/Am. Express Inc. v. McMahon*, 482 U.S. 220, 228 (1987). As the Southern District of New York noted in finding that *McMahon* did not preclude waiver of FINRA Rule 12200, forum selection is a procedural issue. See *supra* text accompanying note 220.

278. See Gross, *supra* note 29, at 403 (quoting *Guaranty Tr. Co. v. York*, 326 U.S. 99, 115 (1945) (Rutledge, J., dissenting)).

279. *McMahon*, 482 U.S. at 228.

280. See *id.* at 230 (first and third alterations in original) (quoting *Wilko v. Swan*, 346 U.S. 427, 432 (1953)).

281. See *J.P. Morgan Sec. LLC v. Quinnipiac Univ.*, No. 14-Civ-429, 2015 U.S. Dist. LEXIS 67135, at \*13 (S.D.N.Y. May 22, 2015); *infra* Part III.C.2. The Court in *McMahon* addressed “suspicion” toward arbitration, see *McMahon*, 482 U.S. at 226 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626–27 (1985)), and, thus, it is a stretch to read *McMahon* as permitting agreements that waive Exchange Act provisions to allow arbitration yet not to allow agreements that waive FINRA provisions to allow litigation.

FINRA Rule 12200,<sup>282</sup> and no court has agreed with Professor Gross's argument concerning *McMahon*.<sup>283</sup>

Professor Gross argues that based on the policy in favor of arbitration, waiver should not be allowed.<sup>284</sup> However, as explained below, the presumption of arbitrability is inapplicable in these cases.

## 2. The Presumption of Arbitrability Does Not Attach

The presumption of arbitrability does not attach to waiver of FINRA Rule 12200. The proposition stated by the Supreme Court in *Granite Rock*—that the presumption of arbitrability does not apply when the existence of the agreement to arbitrate itself is in question—has been applied beyond the immediate context of labor law; *Granite Rock* has been applied to securities arbitration and FINRA Rule 12200 specifically.<sup>285</sup>

FINRA Rule 12200 constitutes an agreement to arbitrate, but when modified by a forum selection clause, there is a clear question of whether there is an agreement to arbitrate in the first place.<sup>286</sup> On the one hand, the forum selection clause could be read to supersede FINRA Rule 12200 and thus, there would be no agreement to arbitrate. On the other hand, a forum selection clause (perhaps stating that any litigation goes to a specific forum) could be read to complement FINRA Rule 12200, and thus, a valid agreement to arbitrate would exist.<sup>287</sup> Since there is a question of the existence of the agreement to arbitrate, the presumption of arbitrability does not attach.<sup>288</sup>

The only circuit court that favorably mentioned the presumption of arbitrability in the context of this circuit split was the Third Circuit in *Reading Health System*.<sup>289</sup> The Third Circuit referenced the presumption in the context of *Patten Securities Corp.*, a Third Circuit case decided before *Granite Rock*, without specifically applying the presumption to the case before it and thus did not consider the point in detail.<sup>290</sup>

282. See *supra* note 83 and accompanying text.

283. But see *supra* notes 159–60 and accompanying text (stating that the Third Circuit has considered this argument but not taken it up).

284. See Gross, *supra* note 29, at 385, 403–04.

285. See *supra* Part I.B.2.

286. See *supra* note 183 and accompanying text.

287. See *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 742 (9th Cir. 2013).

288. See *supra* Part I.B.2. When the presumption of arbitrability does not attach, courts employ general state-law contract principles and consider the intent of the parties. See *City of Reno*, 747 F.3d at 746.

289. See *Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87, 103 (3d Cir. 2018); see also *UBS Sec. LLC v. Allina Health Sys.*, No. 12-2090, 2013 U.S. Dist. LEXIS 17799, at \*17, \*19 (D. Minn. Feb. 11, 2013).

290. See *Reading Health Sys.*, 900 F.3d at 103 (citing *Patten Sec. Corp. v. Diamond Greyhound & Genetics, Inc.*, 819 F.2d 400, 407 (3d Cir. 1987)); text accompanying *supra* notes 153–55. Additionally, Suleman Malik, in his student note covering this circuit split, references Supreme Court precedent stating that the presumption of arbitrability would apply “whether the problem at hand [was] the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability.” See Suleman Malik, Note, *Where Do We Fight?: A Way To Resolve the Conflict Between a Forum Selection Clause and FINRA Arbitration Rule 12200*, 17 *CARDOZO J. CONFLICT RESOL.* 215, 226 & n.100 (2015) (alteration

### 3. Parties Can Contract Around FINRA Rule 12200

A contract can supersede FINRA Rule 12200's arbitration right. As described above, the *Georgiadis* line of cases established that parties can contract around the right to FINRA arbitration.<sup>291</sup> Further, under *In re American Express*, complete waiver of FINRA Rule 12200 itself was acceptable.<sup>292</sup> The court noted that a settlement agreement is a contract,<sup>293</sup> and, thus, waiver of FINRA Rule 12200's arbitration obligation is permitted via contract. However, FINRA, via Regulatory Notice 16-25, states that its provisions are not contractual but rather have the binding force of federal law.<sup>294</sup>

FINRA's argument is not controlling on this issue. FINRA Regulatory Notice 16-25 states that "courts that have upheld forum selection clauses have relied on authority that traces back to two appellate decisions in the 1990s that never actually decided whether a member firm may obtain and enforce a waiver of its obligation to arbitrate as set forth in FINRA Rule[] 12200."<sup>295</sup> While it is true that the Second Circuit, in the two cases referenced by FINRA, *Georgiadis* and *Kidder*, did not consider complete waiver under FINRA Rule 12200,<sup>296</sup> *In re American Express* did consider complete waiver in determining that a settlement agreement could waive arbitration rights and arrived at this conclusion not solely through reliance on *Kidder*.<sup>297</sup> The court relied on *Kidder* for the general principle that "different or additional contractual arrangements for arbitration can supersede the rights conferred on [a] customer by [FINRA]."<sup>298</sup> The court did not presume that *Kidder* stood for the proposition that the arbitration right itself could be waived. Rather, the court additionally cited the holding in *Stolt-Nielsen* that an arbitrator's power comes from agreement and stated that "it follows" that FINRA arbitration can be superseded in settlement cases.<sup>299</sup> The court consciously chose to expand on the *Kidder* holding in applying it to waiver of FINRA Rule 12200's arbitration right.<sup>300</sup> As a result, when the *Carilion Clinic* court referred to *In re American Express* to state that FINRA Rule

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in original) (quoting *Moses H. Cone Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24–25 (1983)). However, this case considered such matters to be questions of scope. *See Moses H. Cone Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24–25 (1983). *Granite Rock* has made it clear that an agreement must be validly formed and enforceable before the presumption of arbitrability can apply to such questions of scope. *See Granite Rock Co. v. Int'l Bd. of Teamsters*, 561 U.S. 287, 301 (2010).

291. *See supra* Part I.B.3.

292. *See Anderson v. Beland (In re Am. Express Fin. Advisors Sec. Litig.)*, 672 F.3d 113, 132–33 (2d Cir. 2011).

293. *See id.*

294. *See FINRA, supra* note 13, at 3.

295. *See id.* at 4, 9 nn.10–11.

296. *See supra* Part I.B.3.

297. *See In re Am. Express Fin. Advisors Sec. Litig.*, 672 F.3d at 132–33.

298. *See id.* at 132 (first alteration in original) (quoting *Kidder, Peabody & Co. v. Zinsmeyer Trs. P'ship*, 41 F.3d 861, 864 (2d Cir. 1994)).

299. *See id.* at 132–33.

300. *See id.*

12200 could be superseded, it was on solid ground.<sup>301</sup> Therefore, FINRA's assertion that the court assumed that the issue was settled<sup>302</sup> appears to be unwarranted.

Given that this argument regarding the *Georgiadis* line of cases is flawed, FINRA's assertion that a forum selection clause violates the standards of commercial honor and principles of trade<sup>303</sup> should similarly not prevail. FINRA IM-12000 of the Customer Code states that failure to arbitrate as "required by the Code" constitutes a violation of the standards of commercial honor.<sup>304</sup> However, if courts hold that the code allows for waiver and does not require arbitration under these circumstances, then there is a weak case for finding such a violation.<sup>305</sup>

A similar provision cited by FINRA, FINRA Rule 2268(d), which states that "[n]o pre-dispute arbitration agreement shall include any condition that . . . limits or contradicts the rules of any self-regulatory organization,"<sup>306</sup> is not controlling either. FINRA Rule 2268 only governs predispute arbitration agreements, which concern resolution via arbitration, and not forum selection clauses, which concern resolution in court.<sup>307</sup> As a result, FINRA Rule 2268(d) does not control. FINRA Rule 2268(d) originated in the 1980s with NASD Rule 3110.<sup>308</sup> The rule took its current form in 1998.<sup>309</sup> Thus, *In re American Express* and the cases that drew on it allowing waiver of the arbitration right were decided despite the alleged constraints of this rule.<sup>310</sup>

Further, Professor Gross's argument that a submission agreement executed and filed as required by FINRA arbitration rules, and not FINRA Rule 12200, constitutes the agreement to arbitrate<sup>311</sup> is contrary to the weight of authority,

301. See *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 328 (4th Cir. 2013).

302. See FINRA, *supra* note 13, at 4 & 9 nn.10–11.

303. See *supra* notes 55–56 and accompanying text.

304. See FINRA IM-12000 (FINRA 2008).

305. See *id.*; *Citigroup Glob. Mkts., Inc. v. Mun. Elec. Auth.*, No. 14 Civ. 2903, 2014 U.S. Dist. LEXIS 110511, at \*9 (S.D.N.Y. June 19, 2014) (finding forum selection clause superseded FINRA Rule 12200 and noting IM-12000 does not in itself "preclude[] members from entering into specific agreements with customers which waive arbitration under the Code" and that "the only effect of this language is to provide that *if* the Code requires arbitration, a failure to arbitrate would be unjust").

306. See FINRA RULE 2268(d) (FINRA 2011); *supra* text accompanying note 46.

307. See *INTL FCStone Fin. Inc. v. Jacobson*, 950 F.3d 491, 503 n.8 (7th Cir. 2020); Reply Brief for Defendant-Appellant at 17, *Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87 (3d Cir. 2018) (No. 16-4234), 2017 U.S. 3RD CIR. BRIEFS LEXIS 760, at \*19. Further, it has been asserted that predispute arbitration agreements govern agreements requiring arbitration, not those that prohibit it. See *id.* at 19, 2017 U.S. 3RD CIR. BRIEFS LEXIS 760, at \*22.

308. See FINRA RULE 2268(d); SEC Release No. 34-26805, 54 Fed. Reg. 21144, 21144 (May 16, 1989).

309. See Amendments to Rule 3110(f) Governing Predispute Arbitration Agreements with Customers, 64 Fed. Reg. 66681 (Nov. 29, 1999).

310. See *Anderson v. Beland (In re Am. Express Fin. Advisors Sec. Litig.)*, 672 F.3d 113, 113 (2d Cir. 2011) (dating from 2011); see also *Singh v. Interactive Brokers LLC*, 219 F. Supp. 3d 549, 560 (E.D. Va. 2016) (finding arbitration agreement valid despite violation of FINRA Rule 2268).

311. See *supra* text accompanying notes 170–71.



as courts on both sides of the circuit split find that FINRA Rule 12200 constitutes an agreement to arbitrate.<sup>312</sup> Even assuming that this document constituted an agreement to arbitrate, a party to a requested arbitration might refuse to return an executed document (or simply might not answer) and instead immediately sue in court for a declaratory judgment.<sup>313</sup>

Although FINRA claims that it may discipline firms for contracting around FINRA Rule 12200, it is unclear whether firms will actually be disciplined. FINRA has only chosen to discipline the broker-dealer in one case out of many concerning forum selection clauses—*Charles Schwab*.<sup>314</sup> The holding in *Charles Schwab* was narrow: FINRA may “enforce its existing rules . . . even when there is a valid predispute arbitration agreement between a firm and its customers.”<sup>315</sup> FINRA’s disciplinary actions are reviewable by the SEC and the U.S. courts of appeals.<sup>316</sup>

FINRA’s disciplinary actions themselves likely do not warrant deference. Courts often defer to agencies based on accountability to the legislative or executive branches, but SROs are nongovernmental in nature and lack the same accountability.<sup>317</sup> This undermines the rationale for deference, and, thus, courts often do not defer to SROs.<sup>318</sup> The court in *Charles Schwab* deferred so that FINRA could make a record, as administrative remedies had not yet been exhausted.<sup>319</sup> As part of this exhaustion process, the case could be appealed to the SEC, which would then lend its own expertise (or refuse to hear the appeal, essentially underwriting FINRA’s decision).<sup>320</sup> Blurring the line between the SEC and FINRA only appears rational if the enforcement proceeding has had a chance to go to the SEC. The *Charles Schwab* disciplinary action was not appealed as the company agreed to notify

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312. See, e.g., *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 739 n.1 (9th Cir. 2014) (“FINRA Rule 12200 constitutes an ‘agreement in writing’ under the FAA . . . .”); *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 328 (4th Cir. 2013).

313. See, e.g., *City of Reno*, 747 F.3d at 737 (“In response to Reno’s Statement of Claim, Goldman filed this action in the United States District Court for the District of Nevada, seeking a declaratory judgment that FINRA lacks jurisdiction over the dispute.”).

314. See *Dep’t of Enf’t v. Charles Schwab & Co.*, No. 2011029760201, 2014 FINRA Discip. LEXIS 5 (FINRA Bd. of Governors Apr. 24, 2014); *supra* text accompanying notes 60–69. This case was particularly notable because the broker-dealer amended millions of agreements. See *supra* text accompanying note 63.

315. See *Charles Schwab*, 2014 FINRA Discip. LEXIS 5, at \*73 (emphasis added).

316. See 15 U.S.C. § 78s(d).

317. See Hammond, *supra* note 67, at 1709.

318. See, e.g., *N.Y. Bay Cap., LLC v. Cobalt Holdings, Inc.*, 456 F. Supp. 3d 564, 573–74 (S.D.N.Y. 2020); *Morgan Keegan & Co. v. Drzayick*, No. 11-CV-00126, 2011 U.S. Dist. LEXIS 129366, at \*5 n.1 (D. Idaho Nov. 8, 2011) (explicitly refraining from applying deference to FINRA director’s previous decisions). While a number of other courts have granted deference to SROs, such deference is often not dispositive. See, e.g., *Heath v. SEC*, 586 F.3d 122, 138–39 (2d Cir. 2009) (noting that “dispositive deference” was not given to NYSE’s regulation arm or the SEC); *Moses v. Burgin*, 445 F.2d 369, 382 (1st Cir. 1971) (noting that federal courts have leeway to overrule exchange interpretations).

319. See *supra* text accompanying note 67.

320. See *Charles Schwab v. Fin. Indus. Regul. Auth. Inc.*, 861 F. Supp. 2d 1063, 1066 (N.D. Cal. 2012).

its customers and pay a fine.<sup>321</sup> Thus, it is difficult to tell whether a disciplinary action from FINRA appealed to the SEC would hold up.<sup>322</sup>

For similar reasons, FINRA Regulatory Notice 16-25 itself should not be accorded deference. The court in *Charles Schwab* considered FINRA's formal adjudication, not a guidance document (in fact, the guidance document was promulgated years later).<sup>323</sup> FINRA Regulatory Notice 16-25 was not subject to review by the SEC but took effect upon filing,<sup>324</sup> thus similarly undermining the argument for deference, as there is a lack of accountability to the legislature or executive. It is notable that, although one of the parties in *Reading Health System* cited this case to argue for deference, the Third Circuit did not similarly defer.<sup>325</sup> In fact, no court that has considered Regulatory Notice 16-25 has given FINRA's interpretation deference.<sup>326</sup> As described above, courts have repeatedly chosen not to let Regulatory Notice 16-25 upend binding circuit court precedent.<sup>327</sup>

Assuming *arguendo* that FINRA was treated like the SEC and accorded deference, the document at issue is a guidance document, and, recently, the Supreme Court narrowed deference for guidance documents in *Kisor v. Wilke*.<sup>328</sup> For instance, to receive deference under *Kisor*, the interpretation

321. See FINRA LETTER OF ACCEPTANCE, WAIVER AND CONSENT, *supra* note 69, at 2; *supra* text accompanying note 69.

322. See *Singh v. Interactive Brokers LLC*, 219 F. Supp. 3d 549, 559 (E.D. Va. 2016) (criticizing the decision in *Charles Schwab* and noting the lack of appeal).

323. See *Charles Schwab*, 861 F. Supp. at 1065; see also 15 U.S.C. § 78s(d) (describing review process for FINRA's disciplinary actions).

324. See 15 U.S.C. § 78s(b)(3)(A); FINRA, *supra* note 13, at 1 (designating notice type as guidance); Reply Brief for Defendant-Appellant, *supra* note 307, at 21, 2017 U.S. 3RD CIR. BRIEFS LEXIS 760, at \*24 (stating that there is "no contention that Regulatory Notice 16-25 bears an agency's imprimatur"). Although the *Reading Health System* court noted that FINRA Rule 12200 was approved by the SEC, see *supra* text accompanying note 158, the SEC's lack of approval for FINRA Regulatory Notice 16-25 is the more relevant consideration because FINRA Rule 12200 alone could be read to permit waiver, see *supra* Part III.B.

325. See Brief of Plaintiff-Appellee at 15 n.7, *Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87 (3d Cir. 2018) (No. 16-4234), 2017 U.S. 3RD CIR. BRIEFS LEXIS 474, at \*55 n.7.

326. See, e.g., *Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87, 102 n.73 (3d Cir. 2018) (citing Regulatory Notice 16-25 but declining to accord any special deference to it); *N.Y. Bay Cap., LLC v. Cobalt Holdings, Inc.*, 456 F. Supp. 3d 564, 572-75 (S.D.N.Y. 2020); *Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368, at \*5 n.1 (D. Nev. July 16, 2019); *Goldberg v. Bruderman Bros.*, No. 159280/2019, 2020 NYLJ LEXIS 1654, at \*10 n.7 (N.Y. Sup. Ct. Oct. 20, 2020).

327. See *supra* Part II.C. Although *National Cable & Telecommunications Ass'n v. Brand X Internet Services* allowed granting agency deference in the face of conflicting court opinions if a court notes that a statute is ambiguous, this case is inapplicable, as Regulatory Notice 16-25 is a guidance document promulgated by an SRO, not a regulation promulgated by an agency. See 545 U.S. 967, 980, 996 (2005). Thus, courts were on solid ground when they followed binding circuit precedent instead of following Regulatory Notice 16-25. See, e.g., *supra* text accompanying note 226.

328. See 139 S. Ct. 2400, 2449 (2019); *supra* note 67. Some have suggested that *Kisor* deference (or, before that regime was articulated, its forebearer, deference under *Auer v. Robbins*, 519 U.S. 452 (1997)) might apply to FINRA Regulatory Notice 16-25. See, e.g., Brief of Plaintiff-Appellee, *supra* note 325, at 16, 2017 U.S. 3RD CIR. BRIEFS LEXIS 474, at \*16-17; Colle, *supra* note 165, at 234. However, courts have not taken up these arguments and have refrained from granting deference. See *supra* note 326.

may not (among other criteria) create “unfair surprise” by changing established industry practice.<sup>329</sup> Here, the guidance document demands that parties review all past agreements and purge them of any offending clauses,<sup>330</sup> thereby upending established practices. Additionally, an interpretation must be “actually made by the agency,”<sup>331</sup> and an interpretation by FINRA is not an interpretation by the SEC, the “agency” in this situation.<sup>332</sup> Application of *Kisor* is especially tenuous because deference is often not given in many deference-eligible cases.<sup>333</sup>

FINRA similarly notes that FINRA rules have the force of federal law, citing *Grunwald* in support of this proposition.<sup>334</sup> The court in *Grunwald* held that the Exchange Act preempts California’s ethics standards and that SEC-approved NASD arbitration procedures controlled.<sup>335</sup> However, since FINRA Rule 12200 is ambiguous, the provision prohibiting waiver is FINRA Regulatory Notice 16-25, which is a guidance document that took effect on filing and, unlike the procedures in *Grunwald*, was not subject to searching SEC review.<sup>336</sup> This undermines the potential preemptive effect of Regulatory Notice 16-25. Additionally, FINRA extrapolates that, as a result of their binding nature, FINRA rules are not contracts.<sup>337</sup> However, in no way did *Grunwald* prohibit contractual waiver or state that FINRA arbitration rules could not be contractual in nature.<sup>338</sup> *Grunwald* was a Ninth Circuit case, and the Ninth Circuit itself after *Grunwald* has held that FINRA arbitration rules were contractual and could be waived.<sup>339</sup> As a result, *Grunwald* is not controlling in this situation.<sup>340</sup>

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329. See *Kisor*, 139 S. Ct. at 2418 (quoting *Long Island Care at Home, Ltd. v. Coke*, 551 U.S. 158, 170 (2007)).

330. See FINRA, *supra* note 13, at 5.

331. See *Kisor*, 139 S. Ct. at 2416.

332. See *supra* note 67.

333. See Connor N. Raso & William N. Eskridge, Jr., *Chevron as a Canon, Not a Precedent: An Empirical Study of What Motivates Justices in Agency Deference Cases*, 110 COLUM. L. REV. 1727, 1740 (2010) (asserting that deference regimes are applied like canons rather than as precedent).

334. See FINRA, *supra* note 13, at 3 & 9 n.9 (citing *Credit Suisse First Bos. Corp. v. Grunwald*, 400 F.3d 1119, 1128 (9th Cir. 2005)).

335. See *Credit Suisse First Bos. Corp. v. Grunwald*, 400 F.3d 1119, 1128 (9th Cir. 2005).

336. See *supra* note 324 and accompanying text. Additionally, any preemptive effect on state law would not foreclose the ability of courts to interpret FINRA provisions. See *Goldberg v. Bruderman Bros.*, 159280/2019, 2020 NYLJ LEXIS 1654, at \*10 n.7 (N.Y. Sup. Ct. Oct. 20, 2020) (emphasizing that federal courts are “especially deserving of substantial deference” concerning waiver of FINRA Rule 12200 because “FINRA is, itself, a creature of federal legislation”).

337. See FINRA, *supra* note 13, at 3 & 9 n.9.

338. See generally *Grunwald*, 400 F.3d 1119.

339. See *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 739 n.1, 741 (9th Cir. 2014).

340. Cf. Brief for Plaintiff-Appellee at 38, *Credit Suisse Sec. (USA) LLC v. Tracy*, 812 F.3d 249 (2d Cir. 2016) (No. 15-0345-cv), ECF No. 89 (“[N]othing in *Grunwald* has anything to do with . . . any private arbitration agreement of any kind, nor does the case hold that NASD (now FINRA) rules constitute congressional action . . .”).

All circuits that have thus far ruled on this issue agree that FINRA Rule 12200 can be waived if indeed there is a sufficiently specific agreement.<sup>341</sup> Such consensus among the courts, including courts on both sides of the circuit split,<sup>342</sup> lends perhaps the strongest support for this Note's contention that FINRA Rule 12200 may be read as a contractual provision.

*C. This Approach Sensibly Accommodates Both Sides' Needs*

In determining whether a forum selection clause is viable, courts look to "effectuate the intent of the parties."<sup>343</sup> The forum selection clauses in cases in which the customer is institutional are sufficiently specific. One must be able "to impute to the contracting parties the reasonable expectation that they are superseding, displacing, or waiving the arbitration obligation created by FINRA Rule 12200."<sup>344</sup> It is far easier to impute such an expectation to an institutional customer, which is more likely to hire outside or in-house counsel.<sup>345</sup> An institutional customer may be more likely to view a provision as all-inclusive and mandatory, the hallmarks of a sufficiently specific provision.<sup>346</sup> Thus, the same forum selection clause may be sufficiently specific for institutional customers but not sufficiently specific for retail customers.

1. A Forum Selection Clause May Not Be Sufficiently Specific for Retail Customers

Forum selection clauses that do not explicitly mention arbitration and involve a retail customer should be found not to be sufficiently specific. This is sensible because retail customers generally might not consider the implications of leaving out important terms. Even a retail customer with

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341. See *INTL FCStone Fin. Inc. v. Jacobson*, 950 F.3d 491, 503 (7th Cir. 2020) ("Although we express no opinion on the merits of this issue, among the circuits that have, the obligation to arbitrate under FINRA Rule 12200 can be superseded or waived by specific agreement of the parties.").

342. See, e.g., *Reading Health Sys. v. Bear Stearns & Co.*, 900 F.3d 87, 90, 102–03 (3d Cir. 2018); *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733, 741 (9th Cir. 2014); *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 328 (4th Cir. 2013); *Anderson v. Beland (In re Am. Express Fin. Advisors Sec. Litig.)*, 672 F.3d 113, 132 (2d Cir. 2011).

343. See *City of Reno*, 747 F.3d at 746.

344. *Carilion Clinic*, 706 F.3d at 328.

345. See Teri J. Dobbins, *The Hidden Costs of Contracting: Barriers to Justice in the Law of Contracts*, 7 J.L. SOC'Y 116, 116 (2005) (describing how access to counsel is unequal and that this can have a "particular significance in the law of contracts").

346. See *Carilion Clinic*, 706 F.3d at 328; *Applied Energetics Inc. v. NewOak Cap. Mkts., LLC*, 645 F.3d 522, 525 (2d Cir. 2011). This approach is in line with the modified objective approach to contract interpretation, the majority approach employed by courts and advocated for by the Restatement (Second) of Contracts, which dictates that when both parties attach different meanings to a term and one party knew or had reason to know of the meaning of another, that latter party's construction prevails. See *RESTATEMENT (SECOND) OF CONTRACTS* § 201 (AM. L. INST. 1981); 5 *CORBIN ON CONTRACTS* § 24.5 (2021); Randy E. Barnett, *Consenting to Form Contracts*, 71 *FORDHAM L. REV.* 627, 629 (2002).

some sophistication might not have the resources or awareness to hire counsel knowledgeable in relevant matters.<sup>347</sup>

Retail customers may read the term “actions and proceedings” in different ways. For instance, the CPLR do not consider arbitration as an action or proceeding.<sup>348</sup> Retail customers might also be thrown by mention of terms like “judge” and “jury,” which the Fourth Circuit noted were terms indicative of litigation and thus, not preclusive of arbitrability.<sup>349</sup> Forum selection clauses may contain such language concerning judicial proceedings, and this is especially likely to evoke litigation, rather than arbitration, in a retail customer’s mind. As a result, the specific may, in these cases, limit the general.<sup>350</sup> It is unlikely that retail customers would be able to determine the meaning of such clauses when courts themselves are split, or that retail customers would research whether such a split exists.

Additionally, in these cases, the broker-dealer is almost invariably the drafter of the agreement.<sup>351</sup> A retail customer will not be drafting these agreements and, based on the contractual principle of construction against the drafter, the construction should be in favor of the retail customer.<sup>352</sup> Construction against the drafter dictates that the forum selection clause in covering “all actions and proceedings” does not waive the right to arbitration. As a result, it is sensible to presume that when a party is a retail customer, it does not have reason to know that “all actions and proceedings” could include arbitration, and thus it could not waive its arbitration right.

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347. Additionally, in practice, retail customers are often not negotiating contracts. *See, e.g.*, *Webb v. First Tenn. Brokerage*, No. E2012-00934-COA-R3-CV, 2013 Tenn. App. LEXIS 396, at \*18 (Ct. App. June 18, 2013) (noting retail customer had contract presented on “take-it-or-leave-it basis”); *Dep’t of Enf’t v. Charles Schwab & Co.*, No. 2011029760201, 2014 FINRA Discip. LEXIS 5, at \*69 (FINRA Bd. of Governors Apr. 24, 2014) (noting that Schwab amended customer agreements for almost seven million customers in their account statements at the end of the month, abridging arbitrators’ ability to consolidate claims and thus, the ability to arbitrate “under the Code” provided by FINRA Rule 12200). However, even if a retail customer has the ability to negotiate, retail customers are still due protection as a group because of their reasonable expectations.

348. *See* N.Y. C.P.L.R. §§ 103, 304 (McKinney 2022).

349. *See Carilion Clinic*, 706 F.3d at 329–30. While this Note does not assert that terms like “judge” and “jury” must be present in a forum selection clause to trigger FINRA Rule 12200’s protections for retail customers, their use serves as an example of language that may confuse retail customers.

350. *See id.*

351. *See, e.g.*, *Patten Sec. Corp. v. Diamond Greyhound & Genetics, Inc.*, 819 F.2d 400, 407 (3d Cir. 1987); *Defendant’s Cross-Motion to Enjoin the Arbitration at 20*, *Reading Health Sys. v. Bear Stearns & Co.*, No. 15-cv-01412 (E.D. Pa. Feb. 18, 2016), ECF No. 19 (arguing that defendant broker-dealer drafted and inserted the forum selection clause, and thus construction against the drafter should apply).

352. To the extent that such terms are boilerplate, this furthers the argument for use of construction against the drafter. *See* RESTATEMENT (SECOND) OF CONTRACTS § 206 cmt. a (AM. L. INST. 1981) (noting that construction against the drafter is often applied to standardized contracts and in cases where there is a disparity in bargaining power).

## 2. A Forum Selection Clause May Be Sufficiently Specific for Institutional Customers

Since an institutional customer has reason to know (or a reasonable expectation) that the meaning of a forum selection clause encompassing “all actions and proceedings” could include arbitration, it is sensible to interpret that clause as including arbitration. An institutional customer likely was advised by counsel well-informed about securities regulations and the customer’s arbitration right.<sup>353</sup>

First, an institutional customer, via counsel, has the ability to weigh the significance of the many sources that use the term “actions or proceedings”<sup>354</sup> to refer to arbitration. As noted in *City of Reno*, the Supreme Court “routinely refer[s] to arbitrations as ‘actions’ or ‘proceedings.’”<sup>355</sup> Those familiar with securities law would be more likely to know that the FINRA rules themselves refer to arbitrations as “actions” or “proceedings.”<sup>356</sup> And, of course, if such a bright-line rule were adopted, going forward, such parties would be aware of the rule.

Looking to context, if words such as “jury” are used, an institutional customer or its counsel is more likely to read with nuance. As the Ninth Circuit noted in response to the use of words such as “jury,” there would be a jury in some actions but not in others.<sup>357</sup> An institutional customer’s counsel reviewing a forum selection clause might notice that “all actions and proceedings” includes those that do not involve a jury (as not even all litigation does).

Further, *City of Reno* effectively counters *Carilion Clinic*’s finding that if “all actions and proceedings” is read to include arbitrations, then it effectively means arbitration shall be brought in court and therefore is illogical.<sup>358</sup> Arbitration falls under the “broad umbrella” of “actions and proceedings.”<sup>359</sup> Thus, the dispute, as an action or proceeding, must be brought in district court, but not as an arbitration.<sup>360</sup> Nothing in a forum selection clause says that the dispute must keep its form. Rather, the dispute would be brought in district court as a judicial action.<sup>361</sup> Additionally, as the *Golden Empire* court noted, some cases in state court, much like arbitrations,

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353. See Dobbins, *supra* note 345, at 116. Luke Colle argues that customers have a reasonable expectation of arbitration under FINRA Rule 12200, due in large part to how routine arbitration has become. See Colle, *supra* note 165, at 243–44. However, institutional customers that have agreed to settle “all actions and proceedings” in court likely do not have such an expectation, as they know that they have agreed to something other than what is routine. Cf. Dobbins, *supra* note 345, at 116.

354. See *supra* notes 187–89 and accompanying text.

355. See Goldman, Sachs & Co. v. City of Reno, 747 F.3d 733, 744 (9th Cir. 2014).

356. See *id.* at 744–45.

357. See *id.* at 746.

358. See *id.* at 745.

359. See *id.* at 746.

360. See *id.* at 745–46, 745 n.6.

361. See *id.* at 746.

cannot be “brought” in federal court.<sup>362</sup> Yet, it is well known that such forum selection clauses mandate bringing such disputes in federal court.<sup>363</sup> Therefore, in context, it is logical for “actions and proceedings” to be read to include arbitration.

One could, as the dissent in *City of Reno* suggested, reconcile forum selection clauses and FINRA rules by permitting arbitration and then allowing a party to challenge the award in a forum dictated by the clause.<sup>364</sup> However, awards are only vacated for intentional defiance of the law,<sup>365</sup> and, thus, under the dissent’s approach, the forum selection clause would have little, if any, practical effect. It is unlikely that parties would intend such an absence of effect. As the majority in *City of Reno* noted, state contract law governs, and the goal is to effectuate the reasonable expectation of the parties and not to presume arbitration.<sup>366</sup>

In cases in which the customer is an institutional customer, construction against the drafter is not applicable.<sup>367</sup> The broker-dealer and customer are close in bargaining power, and both agreed via contract to supersede their default obligation to arbitrate under FINRA Rule 12200. This approach thus avoids forcing arbitration when there is a superseding agreement removing consent.

### 3. Policy Implications

This approach would serve as a middle ground of sorts between the two sides of the circuit split. As such, it would accomplish investor-protection goals inherent in the Third and Fourth Circuits’ approach,<sup>368</sup> while simultaneously accomplishing freedom-of-contract goals inherent in the Second and Ninth Circuits’ approach.<sup>369</sup>

FINRA notes two policy reasons behind providing arbitration as an option, regardless of forum selection clauses: investor protection and market integrity.<sup>370</sup> In terms of investor protection, this approach will protect those who need it most. As described above, a retail customer may be less likely to read an implicit provision covering all “actions and proceedings” to include arbitration.<sup>371</sup> Additionally, FINRA has noted that without access to

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362. See *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 217 (2d Cir. 2014).

363. See *id.*

364. See *City of Reno*, 747 F.3d at 750 (Battaglia, J., dissenting).

365. See *supra* note 35 and accompanying text.

366. See *City of Reno*, 747 F.3d at 743–44, 746.

367. See *Joyner v. Adams*, 361 S.E.2d 902, 905–06 (N.C. Ct. App. 1987) (stating that construction against the drafter does not apply when the parties are equally sophisticated).

368. See FINRA, *supra* note 13, at 4.

369. See *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210, 216 (2d Cir. 2014); *City of Reno*, 747 F.3d at 746 (discussing the importance of giving the parties the contract they bargained for); see also *Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368, at \*7 (D. Nev. July 16, 2019) (discussing freedom-of-contract concerns to justify allowing contract to supersede FINRA Rule 12200).

370. See FINRA, *supra* note 13, at 2.

371. See *supra* Part III.C.1.

FINRA's forum, customers may be unable "as a practical matter" to bring claims at all, "particularly small claims," due to expense and the complicated nature of the proceedings.<sup>372</sup> This approach will protect such retail customers by preserving their right to pursue FINRA arbitration despite alleged contractual waiver.

At the same time, this approach will preserve market integrity by sending institutional customers to litigation. Parties in court are granted more opportunity for discovery,<sup>373</sup> and, while avoiding flooding courts with small claims, this approach would allow for greater discovery in transactions like those in *Carilion Clinic*.<sup>374</sup> Institutional customers should be subject to such discovery if the broker-dealer so wishes, as they are more likely to have a vast trove of relevant materials.<sup>375</sup> These materials may vindicate the broker-dealer. Conversely, expanded discovery may reveal a broker-dealer's mismanagement, benefitting the institutional customer. As a result, overall, expanded discovery will allow devotion of time and resources to large matters, allowing only meritorious claims to proceed. The use of extra resources is warranted, as these claims are often high stakes and may have a large economic effect. Ability to appeal such awards would serve as another check on the process.<sup>376</sup> Avoidance of decisions in equity would lead to more predictable findings.<sup>377</sup>

This approach will also protect freedom of contract. If an institutional customer truly wishes to contract away its right to demand arbitration, it can. Ability to negotiate a forum selection clause may be a more serious concern in a large transaction involving an institutional customer.<sup>378</sup> Liabilities from such a transaction are likely greater, and thus a party may wish to ensure access to courts. By disallowing the ability to contract away one's right to request arbitration entirely, the institutional customer is hurt because it loses a powerful bargaining chip. Parties may possibly forgo certain transactions altogether.<sup>379</sup>

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372. See FINRA, *supra* note 13, at 4.

373. See McCurdy et al., *supra* note 22, at 77.

374. See UBS Fin. Servs., Inc. v. Carilion Clinic, 706 F.3d 319, 322, 328 (4th Cir. 2013) (describing transaction for \$234 million in auction-rate bonds and millions of dollars in losses).

375. See, e.g., Rangarajan v. Johns Hopkins Univ., 917 F.3d 218, 222 (4th Cir. 2019) (noting tens of thousands of emails provided by large organization during discovery); Citigroup Glob. Mkts., Inc. v. Bock, No. 10-24157-MC, 2013 U.S. Dist. LEXIS 7455, at \*6 (S.D. Fla. Jan. 17, 2013) (noting thousands of emails to be released by Citigroup during discovery).

376. See *supra* note 35 and accompanying text.

377. See Black & Gross, *supra* note 34, at 1047.

378. See *supra* note 250 and accompanying text (describing how institutional customers are more likely than retail customers to negotiate such contracts).

379. See Atl. Marine Constr. Co. v. U.S. Dist. Ct., 571 U.S. 49, 66 (2013) (noting that a forum selection clause may "have been a critical factor in [the parties'] agreement to do business together in the first place"); Brief for Defendant-Appellant and Joint Appendix: Volume I of II at 22, Reading Health Sys. v. Bear Stearns & Co., 900 F.3d 87 (3d Cir. 2018) (No. 16-4234), 2017 U.S. 3RD CIR. BRIEFS LEXIS 284, at \*27.



Thus, such an approach would allay fears of reduced confidence in the SRO arbitration system.<sup>380</sup> It would build trust in the system by allowing it to function efficiently and meaningfully serve those who need it most.

#### CONCLUSION

In *Binkele*, Ausloos, the claimant, was a sophisticated investment adviser.<sup>381</sup> Both Ausloos and Binkele maintained significant businesses and contracted to waive FINRA arbitration.<sup>382</sup> The approach described herein would prevent situations in which those like Binkele, who contract with a sophisticated party, invoke an agreed-upon forum selection clause to no avail and incur a sizable default judgment by relying on that contract.

Courts should read forum selection clauses that cover “all actions and proceedings” or contain similar language to waive the customer’s arbitration right only when the customer is an institutional customer. This approach is consistent with underlying case law. Under *McMahon*, FINRA Rule 12200 should be read to implicate procedural rather than substantive rights and, as a result, this approach does not contravene the Exchange Act’s mandate that one cannot waive an SRO rule.<sup>383</sup> Additionally, under *Granite Rock*, since the existence of an agreement to arbitrate itself is in question in these situations, the presumption of arbitrability does not apply, and thus, state-law contract rules, which emphasize giving the parties the bargain they intended to strike, predominate.<sup>384</sup> Finally, under *In re American Express* and its progeny, contracts can supersede FINRA Rule 12200.<sup>385</sup> Institutional customers likely intended to bargain to settle their disputes in court, while retail customers may not have reviewed such a clause with an awareness of its consequences.

This approach is a middle ground between the divergent circuits: it protects retail customers while at the same time maintaining freedom of contract for institutional customers. Such an approach would protect broker-dealers from large awards that are unappealable and decided on the basis of equity, potentially ensuring the survival of the broker-dealer’s business. Additionally, preserving retail customers’ arbitration right may protect them from losing their life savings and ensure affordable access to a tribunal. This Note urges action from the courts in accordance with the proposal set forth herein to protect broker-dealers and the customers they serve.

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380. See Gross, *supra* note 29, at 402.

381. See *Binkele v. Ausloos*, No. 19-cv-01079, 2019 U.S. Dist. LEXIS 225368, at \*2 (D. Nev. July 16, 2019); Complaint for Declaratory Judgment and Relief at 3, *Centaurus Fin., Inc. v. Ausloos*, No. 19-cv-243, 2019 U.S. Dist. LEXIS 77680 (E.D. Wis. May 8, 2019), ECF No. 1.

382. See *Binkele*, 2019 U.S. Dist. LEXIS 225368, at \*2.

383. See *supra* Part III.B.1.

384. See RESTATEMENT (SECOND) OF CONTRACTS § 201 (AM. L. INST. 1981); *supra* Part III.B.2.

385. See *supra* Part III.B.3.