THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM GREENVILLE COUNTY
Court of Common Pleas

D. Garrison Hill, Circuit Court Judge

Opinion No. 2013-UP-014 (S.C. Ct. App. Filed Jan. 9, 2013)

DAVID W. KELLER, Respondent,

v.

ING FINANCIAL PARTNERS, INC., WILLIAM C. JOHNSON, DIVERSIFIED BUSINESS CONCEPTS, INC. and JACKSON NATIONAL LIFE INSURANCE COMPANY Defendants,

Of Whom ING FINANCIAL PARTNERS, INC., WILLIAM C. JOHNSON, and DIVERSIFIED BUSINESS CONCEPTS, INC., are, Petitioners.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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INTRODUCTION

On June 7, 2013, Petitioners petitioned this Court to grant certiorari to review an opinion of the South Carolina Court of Appeals, which upheld the denial of Petitioners' motion to compel arbitration of a dispute between an investor and his financial advisor and securities broker-dealer arising from the purchase of an investment product. This type of dispute is routinely arbitrated before the Financial Industry Regulatory Authority ("FINRA"). However, the lower courts in this case have closed FINRA's doors to Petitioners simply because the arbitration agreement in this case refers to arbitration under the rules of FINRA's predecessor—the NASD. In doing so, the lower court departed from every other court that has considered this issue.

In his Return, Respondent fails to address or distinguish the numerous authorities that have considered this exact issue and reached the opposite result, other than to call those opinions "conclusory in their reasoning." Instead, Respondent continues to rely on an opinion from this Court that is not only distinguishable from the case at bar but that actually supports the Petition. Respondent also spends much of the Return trying to bolster the Court of Appeals' opinion with a theory that was not addressed by the lower court. As discussed below, however, this theory cannot uphold the lower court opinions. Respondent also attempts to downplay the significant impact that the Court of Appeals' opinion will have on what are likely thousands of similar arbitration agreements in this State. The Court of Appeals' opinion will undoubtedly inspire potential plaintiffs who are looking for ways to escape their arbitration agreements and it will guide the circuit judges of this State away from the strong pro-arbitration policy of this State.

REPLY ARGUMENT

I. Respondent Fails to Address And Cannot Distinguish The Numerous Decisions That Have Enforced Arbitration Before FINRA Where The Arbitration Agreement References only The NASD.

Respondent does not dispute the fact that the lower court decisions in this case are the only opinions from any court in the country to strike down an entire arbitration agreement simply because the agreement refers to arbitration under the NASD's rules since the NASD has been renamed FINRA. Respondent does not and cannot distinguish the numerous cases cited in the Petition, except to say that "most of these cases are conclusory in their reasoning, and the issue of FINRA's relationship to the NASD is not contested in most of these cases." (Resp't's Return at 9.) The fact that FINRA arbitration is not contested in so many cases where the agreement refers to NASD reinforces the fact that FINRA and NASD are one in the same for purposes of arbitration.

While most parties have not even attempted to argue (as Respondent does) that FINRA arbitration is materially different from NASD arbitration, some parties have, and, except for Respondent, <u>all</u> of those parties have had their arguments rejected by the courts. In fact, the plaintiff in *Bauscher v. Brookstone Securities, Inc.*, made the exact same argument as Respondent in his Return—that performance of the arbitration agreement is impossible because the NASD no longer exists. The *Bauscher* court rejected this argument: "Given that FINRA is the successor entity to NASD and serves the same function, the fact that the arbitration agreement refers to NASD does not render the contract illusory or performance impossible." *Bauscher*, 2012 U.S. Dist. LEXIS 107375 at *14-15 (D. Idaho July 30, 2012). Earlier this year another district court in the Fourth Circuit rejected Respondent's argument. *See Quality Air Servs., LLC v. Dipippo*,

Case No. 12-338-JFM, 2013 U.S. Dist. LEXIS 26443 at *7 (D. Md. Feb. 25, 2013) ("Plaintiff also contends that the NYLIFE Securities agreement calls for arbitration before the National Association of Securities Dealers, Inc., and the NASD no longer exists. Plaintiff's argument fails because the NASD did not simply cease to exist, but was assumed into the Financial Industrial Regulatory Authority ('FINRA'), which inherited NASD's existing rules and regulations."). At least two other courts have done the same. *See Branch v. Sickert*, No. 2:10-128, 2011 U.S. Dist. LEXIS 19392 (N.D. Ga. Feb. 28, 2011) (compelling arbitration before FINRA where agreement references rules of NASD and where plaintiff argued, like Respondent, that selection of rules is the same as exclusive selection of the forum); *Lewis v. UBS Fin. Servs.*, 818 F. Supp. 2d 1161, 1165-66 (N.D. Cal. 2011) ("[T]he fact that the other arbitration clauses do not specify FINRA is of little moment. . . . Given that FINRA is merely the successor entity to NASD, courts have compelled arbitration before FINRA where, as in this case, the arbitration agreement specifies that arbitration will occur under the rules of NASD.").[1] Respondent does not even attempt to distinguish these cases because they are indistinguishable from this case. Because the lower court's opinion is an outlier in an otherwise uniform body of case law on this issue, the Court should grant the Petition and review the lower court's decision.

II. The *Grant* Opinion Does Not Support The Court of Appeals' Refusal to Enforce The Parties' Arbitration Agreement.

Both lower courts and Respondent continue to mistakenly rely heavily on this

[1] These authorities are in addition to the dozens of cases, many of which are cited in the Petition, that did not involve direct challenges such as the one Respondent is making, but that did enforce compel FINRA arbitration where an arbitration agreement referred to the NASD. (Petition at 8-11.)

Court's opinion in *Grant v. Magnolia Manor-Greenwood, Inc.*, to support the denial of arbitration in this case. The parties in *Grant* had executed an arbitration agreement that contained a forum selection clause expressly providing for arbitration administered by the National Health Lawyers Association. *Id.* at 128. After entering into the agreement, the NHLA changed its rules such that it no longer arbitrated the type of dispute at issue between the parties. *Id.* One of the parties sought to appoint a substitute arbitrator, but the trial court refused, and instead found the entire arbitration agreement void. *Id.* at 132. In affirming the trial court's decision, the Court concluded that the arbitration agreement was unenforceable because the forum selection clause was integral to the agreement to arbitrate because the particular forum had its own specific rules. *Id.* at 131-132.

Grant does not support arbitration in this case. Unlike here where the Parties' arbitration agreement refers to multiple "arbitration forums" and to arbitration under the then-applicable rules of the NASD (R. at 64), the arbitration agreement in *Grant* contained an express forum selection clause, requiring that arbitration occur before the NHLA. *Id.* at 128. In addition, the *Grant* Court concluded that the parties had specific reasons for wanting to arbitrate before the NHLA that would be upset through the use of a different arbitrator. *Id.* at 131. In particular, the NHLA had specific rules regarding "communications, service, counting of days, publication and form of the award, release of documents, or administration." *Id.* In his Return, Respondent contends that the NASD has rules on these same issues, which "have implications substantively affecting the substantive outcome of the claim." (Resp't's Return at 6.) Respondent's argument only reinforces the error in the Court of Appeals' opinion, however, because, as explained in

detail in the Petition, the NASD Rules are now the FINRA rules. (Petition at 8-9.)[2] All of the NASD rules cited by Respondent in the Return were incorporated verbatim into FINRA's arbitration manual. *See* FINRA, FINRA Rules and Regulations, FINRA Manual Online, available at http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4033 (last visited August 13, 2013). In addition to being part of the FINRA Manual, the language from the NASD rules was incorporated almost verbatim into the new FINRA Code of Arbitration Procedure for Customer Disputes, which would govern arbitration in this case. *See id.* For example, of the rules that Respondent contends were so critical to his decision to arbitrate before NASD, NASD Rule 10100 is the exact same as FINRA Rule 12000; NASD Rule 10334 is the same as FINRA Rule 12211; NASD Rule 10314(b)(1) is substantially the same as FINRA Rule 12303; NASD Rule 1335(a)(4) is substantially the same as FINRA Rule 12100(j); and NASD Rule 10308, which is lengthy, is now a part of FINRA Rules 12100, 12401, 12402, 12403, 12407, and 12408.[3] Neither Respondent nor the lower courts have been able to point to a single FINRA rule that is materially different from the NASD rules. (R. at 124, Transcript p. 20 ("I cannot name a single change in the rules as they were and the FINRA rules as they exist today.".) Thus, when the Parties agreed to arbitrate under the "then applicable provisions of the Code of Arbitration Procedure of NASD," they agreed to arbitrate under the same rules applied by FINRA. Therefore, the intention of the Parties to arbitrate under the

[2] Respondent himself admitted in the Return that "FINRA is now the self-regulatory organization used to arbitrate disputes arising in the financial services industry." (Resp't's Return at 4.)

[3] The Parties' Agreement contemplated changes to the language and numbering of the rules by agreeing to arbitrate under the "then applicable" NASD rules. (R. at 64.)

"then applicable" rules of the NASD would be frustrated if the lower court's ruling is allowed to stand. In short, the reasons that the *Grant* found the forum selection clause in that case to be integral to the arbitration agreement are absent from this case.

The *Grant* opinion also supports arbitration in another critical way. As noted above, the arbitration agreement in *Grant* selected the National Health Lawyers Association as the arbitration forum. *Grant*, 383 S.C. at 128. At the time the parties sought to arbitrate, the NHLA no longer existed, but was instead known as the American Health Lawyers Association.[4] *Id.* Rather than strike down the entire arbitration agreement on that basis (as the Court of Appeals did here), the *Grant* Court simply noted, "The NHLA has since become the American Health Lawyers Association (the "AHLA") and hereinafter will be referred to by that name." *Id.* at 128 n.1. This case could be resolved with a similar footnote, "The NASD has since become FINRA, and, thus, the Parties' agreement to arbitrate before the NASD requires arbitration before FINRA." Had the AHLA provided an arbitral forum to the parties in *Grant*, Petitioner submits the outcome would have been different, as it should be in the instant action.

III. Respondent's Reliance on the Common Law Doctrine of Impossibility of Performance Is Misplaced.

Respondent devotes much of his Return to arguing that it is appropriate to strike down the entire arbitration agreement under the doctrine of impossibility of performance because the Parties chose to arbitrate under the then applicable rules of the NASD where

[4] Respondent tries to distinguish *Grant* by arguing that the NASD conversion to FINRA was more than a "mere name change." (Return at 12.) If true, then then the NHLA conversion to the AHLA was likewise more than a "mere name change" as the AHLA was created from the merger of two separate and distinct groups of healthcare lawyers. *See* American Health Lawyers Association, About AHLA, available at http://www.healthlawyers.org/about/Pages/default.aspx (last visited August 15, 2013).

the NASD no longer exists. That argument fails for at least three reasons: (1) the Court of Appeals' opinion did not address the doctrine of impossibility of performance; (2) performance is still possible through FINRA; and (3) the doctrine of impossibility of performance has not been applied to strike down an arbitration agreement in either Iowa or South Carolina.

Contrary to Respondent's assertion (Return at 10), the Court of Appeals' opinion did not discuss the doctrine of impossibility of performance but instead refused in conclusory fashion to compel arbitration before FINRA because the arbitration agreement refers to the rules of the NASD. Though Respondent may present additional sustaining grounds to support the lower court's ruling, the fact that Respondent focuses so much of his Return on a theory of law that the Court of Appeals failed to rely on raises significant questions about the validity of the lower court's decision to deny Petitioners' motion to compel arbitration and, thus, supports review of the lower court's opinion.

More importantly, Respondent's reliance on the doctrine of impossibility of performance fails because performance in this case is possible. The Parties' arbitration agreement provides for arbitration under the "then applicable provisions of the Code of Arbitration Procedure of NASD." (R. at 64.) As explained in the Petition, these rules are now the FINRA rules.[5] (Petition at 8-9.) Thus, performance of the terms of the arbitration agreement is most certainly possible.

Finally, none of the impossibility of performance cases cited by Respondent involved arbitration agreements. (Resp't's Return at 13.) Petitioner is unaware of any

[5] Respondent's argument that the trial court made a factual finding that FINRA and NASD are inherently different entities for purposes of arbitration that is entitled to deference is without merit. The lower court took no evidence on this issue and simply adopted the proposed order drafted by Respondent.

South Carolina or Iowa court that has struck down an arbitration agreement based on the doctrine of impossibility of performance. In fact, to do so simply because a chosen arbitrator is unavailable would conflict with § 5 of the Federal Arbitration Act, which allows for courts to appoint a substitute arbitrator. *See* 9 U.S.C. § 5. Moreover, the *Grant* opinion on which Respondent so heavily relies, never considered the doctrine of impossibility of performance as a means to strike down an arbitration agreement, even though the parties' chosen arbitration forum was unavailable. *See Grant,* 383 S.C. 125, 678 S.E.2d 435 (S.C. 2009). Thus, Respondent's contention that the arbitration agreement is invalid because performance of one of its terms (arbitration under the then-existing rules of the NASD) is impossible fails.

IV. The Importance of The Issues Warrants Review in This Case.

Respondent attempts to downplay the impact of the lower court's ruling, but its impact cannot be overstated. By Respondent's own reading of the lower court's opinion any arbitration agreement that refers to the NASD (either its rules or its forum) is prima facie invalid because the NASD no longer exists. (Resp't's Return at 13.) This would undoubtedly impact thousands of agreements in this State between investors and their financial advisors and hundreds of agreements between employees and their employers. One need only look at the volume of reported cases that already exist (only a portion of which were cited in the Petition) to see that the issues in this case will continue to arise in future cases. This is especially true if the Court of Appeals' decision is allowed to stand, as many parties that would otherwise have never even considered challenging a NASD clause will be able to take their dispute to court.

South Carolina Appellate Court Rule 242(b) provides that review of a decision should be granted only where there are "special and important reasons." As explained above and in the Petition, there are special and important reasons to grant review here because the lower court decisions are the only decisions from any court that have refused to enforce arbitration before FINRA simply because the arbitration agreement refers to NASD. As such, this raises a novel question of law, which calls for guidance from the Court regarding the enforceability of NASD arbitration agreements through FINRA. *See* Rule 242(b)(1), SCACR.

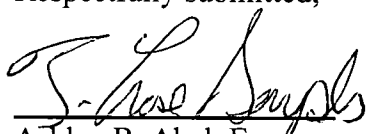
Review is also warranted under Rules 242(b)(3) and (b)(5) because the Court of Appeals' decision conflicts with the clear policies supporting arbitration announced by both this Court and the United States Supreme Court. This Court has repeatedly emphasized that arbitration serves important public policy interests that should be a "driving force" behind judicial review of a motion to compel arbitration. *See Landers v. FDIC*, 739 S.E.2d 209, 217 (S.C. 2013). "Unless a court can say with positive assurance that the arbitration clause is not susceptible to any interpretation that covers the dispute, arbitration should generally be ordered." *Partain v. Upstate Automotive Group*, 386 S.C. 488, 491, 689 S.E.2d 602, 603-04 (S.C. 2010). *See also Zabinski v. Bright Acres Assocs.*, 346 S.C. 580, 596, 553 S.E.2d 110, 118 (S.C. 2001) ("The policy of the United States and South Carolina is to favor arbitration of disputes."). Stated simply, the Court of Appeals' ruling conflicts with the pro-arbitration policies of this Court, the State of South Carolina, and of the United States Supreme Court, and it reflects a judicial hostility toward arbitration that the FAA was created to guard against. *See AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1745, 179 L. Ed. 2d 742, 751 (2011) (recognizing "liberal

federal policy favoring arbitration"). The ruling represents a significant step back in what otherwise has been a consistent trend in favor of arbitration. If left unchecked, the ruling will undoubtedly frustrate the State's pro-arbitration policy, not only with respect to agreements referring to the NASD, but also all other arbitration agreements.

CONCLUSION

The Petition for a Writ of Certiorari should be granted.

Respectfully submitted,



August 16, 2013

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Petitioners.

CERTIFICATE OF SERVICE

I certify that I have served the Reply In Support of Petition for Writ of Certiorari this 16th day of August 2013, on counsel for Keller and counsel for Defendant/Cross-Claimant Jackson National Life Insurance Company in the underlying action by depositing the same in the United States Mail, first class postage prepaid, as follows:

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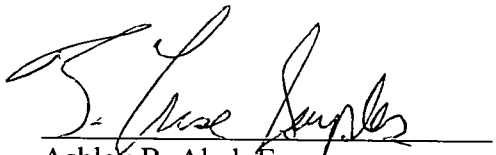

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Dated this 16th day of August 2013.