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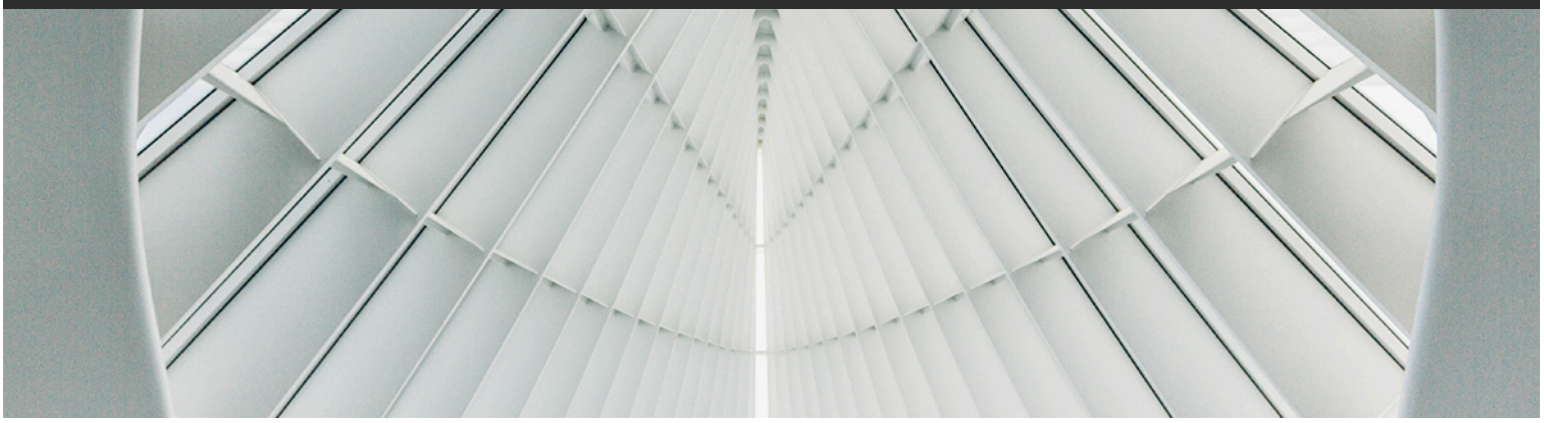

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The Eleventh Circuit Court of Appeals Answers When Would-Be 'Customers' May Bring a FINRA Arbitration Against FINRA Members and Associated Persons

Last week, the Eleventh Circuit U.S. Court of Appeals affirmed a Florida district court's order permanently enjoining two offshore trusts from pursuing a FINRA arbitration against a FINRA member and its associated person owners, *Pictet Overseas, Inc. v. Helvetia Trust*, --- F.3d ---, 2018 WL 4560685 (11th Cir. Sept. 24, 2018).

In *Pictet,* two offshore trusts, Helvetia Trust and AAA Group International Trust, held custodial accounts at a Swiss bank, Banque Pictet, and alleged that they were defrauded into investing in a Ponzi scheme by an unrelated investment advisor. Instead of suing Banque Pictet in Switzerland per the parties' custodial account agreement, the Trusts brought a FINRA arbitration against FINRA member and Banque Pictet affiliate, Pictet Overseas, and its indirect individual owners. Pictet Overseas and its owners had never agreed to arbitrate with the Trusts before FINRA, so they filed a lawsuit in federal court seeking to enjoin the putative arbitration. Indeed, the Trusts were not customers of nor had they ever done business with Pictet Overseas or its owners. After an evidentiary bench trial, the Honorable Kenneth A. Marra of the United States District Court for the Southern District of Florida agreed with Pictet Overseas and enjoined the FINRA arbitration, concluding that the Trusts' claims were not arbitrable. The Trusts appealed to the Eleventh Circuit Court of Appeals.

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Recognizing that the Trusts had no written pre-dispute arbitration agreement with Pictet Overseas or the owners, on appeal, the Trusts relied on FINRA Rule 12200, which requires members and associated persons to arbitrate disputes with its customers. It was clear that the Trusts had no basis to bring a FINRA arbitration against Pictet Overseas, since they had no accounts with the firm. The Trusts argued, however, that the owners should be compelled to arbitrate the underlying disputes so long as they could establish a relationship with the business activities of the owners. In other words, according to the Trusts, once an individual became an associated person, "customer" status was achieved if they connected the dots to the associated person's business activities. Arguably, under this sort of logic, if an associated person had a lemonade stand side business, any buyer of a glass of lemonade could sue in FINRA arbitration. In contrast, Pictet Overseas and the owners argued that to compel FINRA arbitration, the would-be claimants in a FINRA arbitration must demonstrate more than a connection to business activities of the associated person; they must show a connection to the business activities to the associated person in which the *associated person was acting in the capacity as an associated person*.

In analyzing Rule 12200 and FINRA's intent, the Eleventh Circuit applied basic statutory construction techniques to ascertain FINRA's intent under Rule 12200. The court started with the four corners of the Rule, but then also considered other FINRA rules to evaluate Rule 12200 in context. The court concluded that "we see nothing in the text of FINRA's Arbitration Code to indicate that Rule 12200 was intended to require arbitration before FINRA – an organization that was established to regulate stock brokerage firms – of disputes that are entirely unrelated to the business activities of a FINRA member or the associated person's activities undertaken in his or her capacity as an associated person." The court stressed that "[a]t best, the Trusts' claims arise out of the [owners'] business activities undertaken as general partners of Banque Pictet," but those claims had no connection to the business activities of Pictet Overseas "or of the [owners] undertaken in their capacity as associated persons of Pictet Overseas." The court concluded that the claims were not arbitrable under Rule 12200.

The *Pictet Overseas* case is the first time the Eleventh Circuit has interpreted FINRA Rule 12200 and clarified when investors may and may not claim to be "customers" and bring a FINRA member into arbitration. As Judge Pryor makes clear in his concurring opinion, "[t]he correct interpretation of Rule 12200 is that arbitration is required when the dispute arises in connection with the business activities of an associated person, *as an associated person*." (Emphasis in original). While not needed to resolve the *Pictet Overseas* case, the Eleventh Circuit left an important question unanswered; namely, when is the activity with the would-be customer one that is within the ambit of being "stock brokerage" related or adequately connected to those of the associated person "as an associated person"? To be continued to another day no doubt.

Authors

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