09-1556-cv(L), 09-1863-cv(XAP)

United States Court of Appeals

for the

Second Circuit

JOHN J. FIERO and FIERO BROTHERS, INC.,

Plaintiffs-Counter-Defendants-Appellants-Cross-Appellees,

– v. –

FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.,

Defendant-Counterclaimant-Appellee-Cross-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR DEFENDANT-COUNTERCLAIMANT-APPELLEE-CROSS-APPELLANT

TERRI L. REICHER, ESQ.
ASSOCIATE GENERAL COUNSEL
FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.
Attorneys for Defendant-Counterclaimant-Appellee-Cross-Appellant
1735 K Street, N.W.
Washington, D.C. 20006
(202) 728-8967

09-1556-cv(L), 09-1863-cv(XAP)

United States Court of Appeals

for the

Second Circuit

JOHN J. FIERO and FIERO BROTHERS, INC.,

Plaintiffs-Counter-Defendants-Appellants-Cross-Appellees,

– v. –

FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.,

Defendant-Counterclaimant-Appellee-Cross-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR DEFENDANT-COUNTERCLAIMANT-APPELLEE-CROSS-APPELLANT

TERRI L. REICHER, ESQ.
ASSOCIATE GENERAL COUNSEL
FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.
Attorneys for Defendant-Counterclaimant-Appellee-Cross-Appellant
1735 K Street, N.W.
Washington, D.C. 20006
(202) 728-8967

RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, Defendant-Appellee Financial Industry Regulatory Authority, Inc. discloses that it is not a publicly held corporation, has no parent corporation, and no publicly held corporation owns 10% or more of its stock.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page No.

Cases

Federal Statutes

State Statutes

Rules

Other Authorities

PRELIMINARY STATEMENT

This is an appeal and a cross-appeal from a judgment dated July 24, 2009 in favor of FINRA, and against Fiero Brothers, Inc. and John Fiero (collectively, "Fieros"). Fiero Brothers, Inc. was a FINRA member firm and a broker-dealer registered with the SEC. John J. Fiero was the sole registered representative of Fiero Brothers, Inc. *See* Special Appendix ("SPA") at pp. 45-49 (638 F. Supp. 2d 372 (S.D.N.Y. 2009)). The judgment was in the amount of $1,010,809.25, for the collection of a securities industry disciplinary fine imposed by FINRA on the Fieros in 2002. The judgment, issued by United States District Court Judge Victor Marrero, was correctly decided, and should be affirmed.

FINRA cross-appeals the district court's holding in its April 2, 2009 Memorandum Decision (incorporated by reference into the judgment under appeal) that there is no federal question jurisdiction over an action to enforce a disciplinary fine imposed by FINRA pursuant to regulatory authority delegated to FINRA by the Securities and Exchange Act of 1934 ("Exchange Act").

JURISDICTIONAL STATEMENT

The district court correctly exercised diversity jurisdiction pursuant to 28 U.S.C. § 1332. Diversity jurisdiction exists because FINRA is a Delaware corporation with its principal place of business in Washington, D.C., John Fiero is a citizen of Florida, and Fiero Brothers, Inc. is incorporated in New York. The district court also had federal-question jurisdiction under 28 U.S.C. § 1331 and 15 U.S.C. § 78aa, which provides that "[t]he district courts of the United States . . . shall have exclusive jurisdiction of violations of [the Exchange Act] or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by [the Exchange Act] or rules and regulations thereunder." Although the district court disagreed, and FINRA filed a protective notice of cross-appeal on that jurisdictional point, this Court can affirm without resolving the cross-appeal because the district court had diversity jurisdiction in any event.

Both the appeal and cross-appeal are of a final judgment of the court, specifically, the July 24, 2009 judgment that resolved all issues between the parties. Appellate jurisdiction therefore exists under 28 U.S.C. § 1291.

Both the appeal and cross-appeal were filed timely. The original judgment was issued on March 30, 2009. SPA-53. The Fieros' appeal was filed on April 14, 2009, and FINRA's cross-appeal on April 29, 2009. A-535, A-536. Following the

initial appeal, this Court remanded the case to permit the district court to correct the March 30, 2009 judgment, which inadvertently omitted the money amount awarded to FINRA. SPA-44. The mandate issued on July 15, 2009, and on July 24, 2009, the district court issued a corrected judgment. SPA-53. Both parties made timely requests by letter to reinstate the appeals, which this Court did by Order dated August 12, 2009. SPA-51.

COUNTER-STATEMENT OF THE ISSUES

1. Whether FINRA, a securities self-regulatory organization approved by the Securities and Exchange Commission ("SEC") pursuant to Section 15A of the Exchange Act, may judicially enforce a disciplinary fine imposed by FINRA upon a member firm and its registered representative, pursuant to FINRA rules and the Exchange Act?

2. Whether the district court's judgment was in compliance with the Full Faith and Credit Act, and the *Rooker-Feldman* Doctrine, where the New York Court of Appeals dismissed the prior litigation between the parties on the grounds of subject matter jurisdiction, and did not reach the merits of FINRA's claim against the Fieros, or the Fieros' claims against FINRA?

3. Whether the district court correctly concluded that a securities industry disciplinary proceeding brought under the Exchange Act and subject to SEC review is not an "arbitration award"?

4. Whether the district court correctly concluded that FINRA timely asserted its counterclaim?

5. Whether the district court correctly granted final judgment against the Fieros where the Fieros admitted all of the relevant facts, and where the court decided the case's only legal issue—FINRA's right to judicially enforce the fine in district court?

6. Whether the district court erroneously held that no federal question jurisdiction exists over an action to enforce a securities industry regulatory fine, where the underlying proceeding (which includes violations of Section 10b and Exchange Act Rule 10b-5) was brought pursuant authority delegated to FINRA by the SEC under the Exchange Act, the Fieros' obligation to pay fines arises from FINRA's SEC-approved By-Laws and rules, and where the SEC specifically approved FINRA's policy of judicially enforcing disciplinary fines?

COUNTER-STATEMENT OF THE CASE

A. Nature of the Case

1. History of the Dispute

This action arises from the Fieros' determined efforts to avoid payment of a securities industry disciplinary sanction originally imposed by FINRA in 2000, and affirmed in 2002 by the National Adjudicatory Council ("NAC"), FINRA's regulatory review board. The Fieros were the subject of a 1998 FINRA disciplinary action alleging significant violations of federal securities laws and FINRA rules. For their misconduct, FINRA fined the Fieros $1 million plus costs, and expelled them from the securities industry. The NAC decision became final on December 2, 2002, when the Fieros chose not to exhaust their administrative remedies by appealing the adverse decision to the SEC.

FINRA commenced enforcement of the fine in a lawsuit filed on or about February 23, 2004 in the Supreme Court for the State of New York, County of New York, Index No. 102755/04, originally captioned "NASD, Inc. [1] v. John J. Fiero and Fiero Brothers, Inc." On May 11, 2006, the state trial court granted summary judgment for FINRA in the total amount of $1,329,724.54, which

[1] NASD is short for FINRA's prior corporate name "National Association of Securities Dealers, Inc." On July 30, 2007, FINRA adopted its present corporate name, Financial Industry Regulatory Authority, Inc. For purposes of this case, defendant will be identified as "FINRA," except where the NASD name appears in a title, a case caption, or a quotation.

judgment was entered on June 1, 2006. A-174. The judgment was affirmed by the Appellate Division, First Department, on October 26, 2006. *Nat'l. Ass'n of Secs. Dealers, Inc. v. Fiero*, 33 A.D. 2d 547, 827 N.Y.S. 2d 4 (1st Dep't 2006). A-188. The New York Court of Appeals granted leave to appeal, and on February 7, 2008, reversed and dismissed the complaint for lack of state court subject matter jurisdiction. *Finan. Indus. Reg. Auth., Inc. v. Fiero*, 10 N.Y. 3d 12, 853 N.Y.S. 2d 267 (2008). The court determined that the FINRA complaint constituted an action to enforce a liability or duty created under the Securities Exchange Act of 1934 (15 U.S.C. § 78a, *et seq.*) ("Exchange Act"), and therefore fell within the exclusive jurisdiction of the federal courts pursuant to 15 U.S.C. § 78aa. The state court did not reach the merits of FINRA's claim, or the defenses asserted by the Fieros. 10 N.Y. 3d at 17.

2. Proceedings in the District Court

This is the Fieros' second federal case asserting these identical claims. The Fieros filed their initial complaint as Case No. 07-CIV-7679 (RJS), *John J. Fiero and Fiero Brothers, Inc. v. National Association of Securities Dealers, Inc.* on August 29, 2007, and served on FINRA on December 14, 2007. On February 8, 2008, the day after the New York Court of Appeals issued its decision, the Fieros voluntarily dismissed their complaint without prejudice, pursuant to Fed. R. Civ. P. 41(a), and immediately filed the instant case seeking declaratory judgment that

they were not liable to FINRA for the fine. On August 4, 2008, FINRA filed a counterclaim for the fine. A-90. FINRA and the Fieros moved to dismiss the complaint and counterclaim, respectively. A-12, A-99. On March 30, 2009, the district court issued an Order granting FINRA's Motion to Dismiss the Complaint, and denying Fieros' Motion to Dismiss the Counterclaim. SPA-1. The Order also instructed the clerk to enter judgment in favor of FINRA, but did not specify the amount of the judgment. SPA-1, 3. The district court issued a detailed Decision and Order on April 2, 2009. SPA-4. The Fieros noted their appeal on April 14, 2009, and FINRA noted its cross-appeal on April 29, 2009. A-535, 536.

On April 17, 2009, district court requested a "limited remand of this case for the purposes of enabling it to correct the inadvertent omission" of the monetary amount awarded to FINRA on the counterclaim. SPA-41. Over the Fieros' opposition, this Court granted the district court's request, and remanded the case by order dated July 15, 2009, noting that following the district court's issuance of a corrected order, the parties could reinstate the appeal by sending a letter request to the clerk of court. SPA-44.

On remand, the Fieros submitted a letter to the court asserting that any corrected judgment would violate the Full Faith and Credit Act, and the *Rooker-Feldman* Doctrine. A-538. On July 24, 2009, the district court issued an amended Judgment, as well as an additional Memorandum Decision characterizing the

Fieros' argument as "wholly without merit," but sufficiently serious to rebut, which the court proceeded to do. Both parties timely filed letter requests to reinstate their respective appeals, which this Court did by Order dated August 12, 2009. SPA-54.

B. Facts

1. FINRA and Its Role in Securities Regulation

FINRA is a private not-for-profit Delaware corporation and a self-regulatory organization ("SRO") registered with the Securities and Exchange Commission ("SEC") as a national securities association pursuant to the Maloney Act of 1938, 15 U.S.C. § 78o-3, *et seq*., amending the Exchange Act, 15 U.S.C. § 78a, *et seq*. *See Desiderio v. Nat'l Ass'n of Secs. Dealers, Inc.*, 191 F.3d 198, 201 (2d Cir. 1999), *cert denied,* 531 U.S. 1069 (2001); *Matter of Application of National Association of Securities Dealers, Inc.*, Rel. 34-2211, 5 S.E.C. 627 (Aug. 7, 1939). As a self-regulatory organization, FINRA is part of the Exchange Act's highly interrelated and comprehensive mechanism for regulating the securities markets. *See Desiderio*, 191 F.3d at 201. In this regard, FINRA acts under the plenary oversight of the SEC. *See McLaughlin, Piven, Vogel, Inc. v. Nat'l Ass'n of Secs. Dealers, Inc.*, 733 F. Supp. 694, 696-97 (S.D.N.Y. 1990).

Specifically, FINRA is charged with "conducting investigations and commencing disciplinary proceedings against FINRA member firms and their

associated member representatives relating to compliance with the federal securities laws and regulations." *D.L. Cromwell Inv., Inc. v. NASD Regulation, Inc.*, 279 F.3d 155, 157 (2d Cir.), *cert denied*, 537 U.S. 1028 (2002); *Datek Secs. Corp. v. Nat'l Ass'n of Secs. Dealers, Inc.*, 875 F. Supp. 230, 232 (S.D.N.Y. 1995). The FINRA Code of Procedure, which has been approved by the SEC, governs FINRA disciplinary proceedings against securities firms and their representatives. *Notice of Filing and Order Granting Temporary Accelerated Approval*, SEC Rel. No. 34-38908, 62 Fed. Reg. 43571 (Aug. 14, 1997). The entire Code is contained in the FINRA Manual, a CCH publication, available at http://finra.complinet.com.

Disciplinary hearings are conducted by hearing panels pursuant to the FINRA Code of Procedure, found in the FINRA Manual beginning with Rule 9000. The Exchange Act provides for a "three-tiered process of both administrative and judicial review of NASD disciplinary proceedings." *Swirsky v. Nat'l Ass'n of Secs. Dealers, Inc.,* 124 F.3d 59, 61 (1st Cir. 1997). An aggrieved party may appeal a hearing panel decision to the FINRA National Adjudicatory Council ("NAC"), which can affirm, modify or reverse the hearing panel's decision. FINRA Rule 9349(a). NAC decisions may be appealed to the SEC pursuant to 15 U.S.C. § 78s(d), and from the SEC to the United States Court of Appeals pursuant to 15 U.S.C. § 78y. Pursuant to Section 21(e) of the Exchange

Act (15 U.S.C. § 78u(e)), the SEC may institute actions to enforce disciplinary sanctions in actions affirmed by SEC on appeal.

2. FINRA's Disciplinary Case Against the Fieros

Fiero Brothers, Inc. was a FINRA member firm and a broker-dealer registered with the SEC. John J. Fiero was a registered representative and sole registered representative of Fiero Brothers, Inc. Fiero Brothers was initially registered as a broker-dealer in August 1990, and John Fiero had been registered in the securities industry since 1984. A-39, Form U4 Uniform Application for Securities Industry Registration or Transfer for John J. Fiero, dated August 15, 1990; A-42, Form BD Uniform Application for Broker Dealer Registration of Fiero Securities, Inc. (later, Fiero Brothers, Inc.), dated August 15, 1990. *See also*, A-11, Complaint at ¶¶ 13-14.

On February 6, 1998, FINRA's Department of Enforcement initiated Case No. CAF980002 against the Fieros, alleging that the Fieros carried out a "bear raid" of short selling to manipulate the prices of ten securities traded by another firm, Hanover Sterling. A-11, Complaint at ¶ 15; A-49, *DOE v. John Fiero and Fiero Brothers, Inc.*, Complaint No. CAF980002, 2002 NASD Discip. LEXIS 16 at 2[2] (NAC 2002). Hanover Sterling eventually collapsed under waves of short

[2] This document contains several sets of pagination, due to its being reprinted from LEXIS, and then electronically filed in the district court. For clarity, this brief will refer to the Joint Appendix pagination at the top center of each page.

selling by the Fieros and others working with them. *Id*. On December 6, 2000, the FINRA hearing panel issued a decision finding that the Fieros had violated Section 10(b) of the Exchange Act, Exchange Act Rule 10b-5, and various FINRA conduct rules. *Id*. at A-49. The hearing panel found that the Fieros' "bear raid" led to the demise of the securities' underwriter, and the underwriter's clearing firm, while generating significant profits for the Fieros. *Id.* at A-50.

The Fieros appealed the Hearing Panel Decision to the NAC, which in a carefully detailed decision dated October 28, 2002, affirmed the Hearing Panel, barred John Fiero from associating with any FINRA member firm in any capacity, and expelled Fiero Brothers, Inc. from FINRA membership. *Id.* at A-83; A-11, Complaint at ¶ 17. The NAC also affirmed the fines and costs assessed against the Fieros of $1,000,000 and $10,809.25, respectively. The decision became final on December 2, 2002 when the Fieros did not appeal it to the SEC within the prescribed time period. 15 U.S.C. § 78s(d)(2); FINRA Rule 9360, 9370; A-12, Complaint at -20-21.

3. Obligation to Pay Disciplinary Fines and FINRA Collection

a. Registration Forms

When the Fieros originally registered to do a securities business, they executed two registration forms: the Form U4 (Uniform Application for Securities

Industry Registration or Transfer) and the Form BD (Uniform Application for Broker Dealer Registration). A-9, Complaint at ¶¶ 13-14.

The Form U4 (A-39) contains a Certifications Page in which the applicant, in this case, John Fiero, agreed to the following provision, preceded by the following legend:

> **THE APPLICANT MUST READ THE FOLLOWING VERY CAREFULLY**
>
> 2. I apply for registration with the jurisdictions and organizations indicated in Item 10 as may be amended from time to time, and in consideration of the jurisdictions and organizations receiving and considering my application, I submit to the authority of the jurisdictions and organizations and agree to comply with all provisions, conditions, and covenants of the statutes, constitutions, certificates of incorporation, bylaws, and rules and regulations of the jurisdictions and organizations as they are or may be adopted, or amended from time to time. I further agree to submit to and comply with all requirements, rulings, orders, directives, and decisions of, and penalties, prohibitions, and limitations imposed by the jurisdictions and organizations, subject to right of appeal or review as provided by law. (Emphasis added).

A-41. The other form executed by the Fieros is the Form BD (A-42), an SEC-approved form that states at page 2 that the firm seeks registration with FINRA, thereby subjecting Fiero Brothers to FINRA rules, regulations and policies, including the rules relating to sanctions, fines and the obligation to pay them. *Kidder, Peabody & Co., Inc. v. Zinsmeyer Trusts P'ship*, 41 F.3d 861, 863 (2d Cir. 1994) (collecting cases) ("As a member of the NASD, Kidder is bound to adhere to the organization's rules and regulations.")

b. FINRA Rules

The Exchange Act requires registered securities associations to have rules, subject to SEC approval, to "provide a fair procedure for the disciplining of members and persons associated with members . . . " 15 U.S.C. § 78o-3(b)(8). In fact, the SEC cannot approve FINRA's rules without a specific finding that such rules are consistent with the Exchange Act. 15 U.S.C. § 78o-3(b). Section 15A(b)(7) requires the rules of a registered securities association to provide for members to "be appropriately disciplined for violation of any provision of this title . . . or the rules of the association, by 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." 15 U.S.C. § 78o-3(b)(7). Section 15A(h)(1) of the Exchange Act, 15 U.S.C. § 78o-3(h)(1) provides for registered securities associations to "impose a disciplinary sanction" upon a member or person associated with a member, and sets forth specific requirements for the initiation of disciplinary proceedings and for the imposition of sanctions. 15 U.S.C. § 78o-3(h)(1)(A-C).

Pursuant to this authority under the Exchange Act, and upon submission, review and approval by the SEC, FINRA has enacted numerous rules relating to the imposition of disciplinary fines and the collection thereof.

Article XIII of the FINRA By-Laws specifically authorizes the FINRA Board of Governors "to impose appropriate sanctions applicable to members, including censure, fine, suspension, or expulsion from membership, . . . and to impose appropriate sanctions applicable to persons associated with members, including censure, fine, suspension or barring a person associated with a member from being associated with all members . . ." (Emphasis added). A-304.[3]

FINRA Rule 8310(a) authorizes FINRA, following a disciplinary proceeding, to "impose one or more of the following sanctions on a member or person associated with a member . . .(2) impose a fine upon a member or person associated with a member. . . ." (Emphasis added). Rule 8310(b) provides that "each party to a proceeding resulting in a sanction shall be deemed to have assented to the imposition of the sanction unless such party files a written application for appeal, review or relief . . . ." A-305.

Rule 8330 provides that "a member or person associated with a member disciplined pursuant to Rule 8310 shall bear such costs of the proceeding as the Adjudicator deems fair and appropriate under the circumstances." (Emphasis added). A-307. FINRA Rule 8320(a) provides that "all fines and monetary

[3] The rules and by-laws reproduced in the Joint Appendix were the NASD rules and by-laws in effect in 2006. Following the regulatory consolidation with NYSE Regulation in 2007, and the attendant name change from NASD to FINRA, all by-laws and rules were reissued under the FINRA name, and in some cases, amended. However, each of the by-laws and rules cited herein is identical or nearly identical to the currently effective FINRA by-law or rule.

_____ shall be paid to the Treasurer of the Association and shall be used for general corporate purposes." (Emphasis added). A-306.

In 1990, FINRA filed with the SEC a notification that that it would pursue collection of fines, even if the respondent was also barred or expelled from the securities industry. *Notice of Filing and Immediate Effectiveness of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to the Collection of Fines and Costs in Disciplinary Proceedings*, SEC Rel. No. 34-28227, 55 Fed.Reg. 33036 (July 25, 1990). In that filing, FINRA notified the SEC that it "intends to take whatever steps it deems appropriate to collect fines and costs which are assessed in NASD disciplinary proceedings." These steps include referring matters "to external collection agencies and in appropriate situations, the NASD will seek to reduce such fines to a judgment." *Id*. at n 2. On July 18, 1990, the SEC issued its Release, and stated that the "foregoing rule change has become effective pursuant to 19(b)(3)(A)(1) of the Act and subparagraph (e) of Rule 19b-4 thereunder in that it constitutes a stated policy or practice with respect to the NASD's authority to impose sanctions in its disciplinary proceedings."

FINRA notified its members of the policy change in Notice to Members 90-21 entitled "Collection of Fines and Costs in Disciplinary Proceedings," issued in April 1990, FINRA advised its members and their associated persons that for cases concluded on or after July 1, 1990, FINRA would:

> in addition to the procedures relating to the payment of monetary sanctions and suspensions or revocation of membership or registration for failure to make such payment . . . the NASD intends to pursue other available means for collection of fines and costs . . .Thus, the NASD will pursue collection of a fine imposed pursuant to a District Committee, the Market Surveillance Committee, or Board of Governors decision issued on or after July 1, 1990, once such decision becomes final.

(Emphasis added). A-85, Notice to Members 90-21.

In October 1999, FINRA again advised members of its fine collection policies in Notice to Members 99-86 entitled "Imposition and Collection of Monetary Sanctions." In the Notice to Members, FINRA advised that it would "pursue the collection of any fine in sales practice cases, even if the individual is barred, if there has been widespread, significant, and identifiable customer harm; or the respondent has retained substantial ill-gotten gains." A-87, Notice to Members 99-86. (Emphasis added).

c. Fieros' Failure to Pay Fine

The above facts are not disputed—indeed, many of them appear in the Fieros' own complaint. *See, e.g.*, Complaint ¶¶ 13-14, A-11 (acknowledging that Fieros were subject to NASD rules pursuant to their execution of the Form U-4 and Form BD); ¶¶15-21, A-11-12 (describing disciplinary proceeding, appeal and admitting that they did not further appeal). Likewise, the entire aim of the Fieros' complaint is to obtain a judicial determination that they have no obligation to pay the fine, thereby acknowledging that they have not done so. A-13, Complaint at ¶¶

28-29. Each of the elements of FINRA's claim for recovery—the obligation to pay fines, the existence of a disciplinary fine and the Fieros' failure to pay it—are undisputed, and indeed admitted by the Fieros. The Fieros dispute only whether they have a legal obligation to pay the fine. Thus, the district court's determination that the Fieros are so obligated disposed of all issues in the case, leaving no issues requiring further proceedings.

STANDARD OF REVIEW

FINRA agrees that the applicable standard of review is *de novo* because all of the issues presented for review are matters of law.

SUMMARY OF THE ARGUMENT

This case is about judicial enforcement of a final disciplinary fine imposed by FINRA, a securities self-regulatory organization approved by the SEC to enforce federal securities laws and rules, and FINRA rules, upon entities and persons found to have violated Federal securities laws and FINRA rules. FINRA's right to impose and enforce disciplinary sanctions derives from the Exchange Act, which specifically authorizes SROs to impose disciplinary fines, and from FINRA's SEC-approved By-Laws and rules, which authorize the imposition of disciplinary fines, and obligate its members and registered representatives to pay such fines.

Ironically, it was the Fieros who initiated this federal lawsuit, seeking declaratory judgment that, having subjected themselves to FINRA's rules and the federal securities laws, they were not obligated to comply with FINRA rules regarding sanctions and the payment of fines, and that they had no legal obligation to pay the $1,000,000 fine imposed upon them in this case. FINRA counterclaimed for the fine, and the district court awarded judgment to FINRA and against the Fieros.

The Fieros' arguments on appeal run the gamut, from arguing that only the SEC may judicially enforce FINRA disciplinary decisions; to arguing that FINRA disciplinary decisions are not disciplinary decisions at all, they are arbitration

awards subject to the one-year limitation judicial confirmation; to arguing that prior state court litigation between the parties that was ultimately dismissed on jurisdictional grounds, but did not reach the merits, bars FINRA from asserting its counterclaim in this litigation.

The district court's judgment should be affirmed because FINRA does have a legal right to judicially enforce disciplinary fines it imposes upon firms and brokers that it regulates, and who agree to comply with all FINRA rules, including those pertaining to fines. This right is grounded in the Exchange Act, which specifically authorizes self-regulatory organizations to impose fines (*see* 15 U.S.C. § 78o-3(b)(7), (8)), requires the SEC to approve all FINRA disciplinary rules (15 U.S.C. §78s(b)(4)), and requires all persons and entities seeking to be registered in the securities industry through FINRA to submit to all FINRA rules. FINRA's fine collection policy was approved by the SEC, and was communicated to FINRA members twice during time the Fieros held securities licenses. Moreover, the Fieros executed registration forms in which they agreed to comply with FINRA rules, including those relating to fines. As a corporation, FINRA has the inherent right to judicially enforce debts owed to it. This is the core of the appeal in this matter, and the district court held, correctly, that FINRA has the legal right to judicially enforce its fines.

The other arguments raised by the Fieros in opposition to the district court's judgment find absolutely no support in the law. There was no violation of the Full Faith and Credit Act, or of the very narrow *Rooker-Feldman* doctrine. The prior state court decision, which was based solely on jurisdiction and did not reach the merits did not preclude FINRA from asserting its merits counterclaim in this litigation. Indeed, the state court's jurisdictional decision was based entirely upon its construction of Section 27 of the Exchange Act, which grants exclusive federal jurisdiction for actions to enforce liabilities or duties created under the Exchange Act. FINRA's counterclaim in this court does not seek to reverse the state court's decision—it is entirely consistent with it.

Likewise, no court, state or federal, has ever determined securities industry disciplinary proceedings to be "arbitration awards" subject to state and federal arbitration statutes. The district court's rejection of the Fieros' arbitration argument was nothing more than a recognition of the fundamental differences between FINRA disciplinary proceedings and arbitration. Likewise, FINRA's counterclaim was asserted well-within the applicable statute of limitations period, be it for state law breach of contract or a federal action to enforce a disciplinary fine.

The Fieros also dispute the district court's grant of judgment to FINRA at the motion to dismiss stage, but ignore their own tactical decision to admit the facts

in the complaint, and ask the court to decide a single legal issue—FINRA's right to judicially enforce its disciplinary fines. The Fieros framed their case so that an adverse decision necessarily established FINRA's right to enforce the fine. The district court's decision on this matter resolved all of the issues in the case, and judgment was therefore appropriate.

Finally, the district court properly found that subject matter jurisdiction exists in this case, albeit the district court disagreed with the New York Court of Appeals that exclusive federal jurisdiction applies to actions to enforce disciplinary fines. FINRA filed a protective appeal on this point, but this Court can resolve the principal issues without reaching this cross-appeal because subject matter jurisdiction exists.

ARGUMENT

I. FINRA HAS THE LEGAL RIGHT TO COLLECT FINES IMPOSED IN DISCIPLINARY MATTERS

FINRA's right to impose sanctions for regulatory violations is set forth in Sections 15A(b)(7) and 15A(h)(1) of the Exchange Act (15 U.S.C. § 78o-3(b)(7) and (h)(1)). FINRA's right to collect disciplinary fines imposed on its members springs from its SEC-approved By-Laws and rules, and from the Fieros' agreements (in the Forms BD and U4) to comply therewith.

The SEC has authorized FINRA's By-Laws and rules permitting FINRA to impose fines—a grant of authority that would be hollow if FINRA could not then collect those fines.

A. The SEC Has Approved FINRA's Right to Judicially Enforce Disciplinary Finds

FINRA's fine collection policy was filed with and approved by the SEC on July 18, 1990. *Notice of Filing and Immediate Effectiveness of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to the Collection of Fines and Costs in Disciplinary Proceedings*, SEC Rel. No. 34-28227, 55 Fed.Reg. 33036 (July 25, 1990). In that filing, FINRA notified the SEC that it "intends to take whatever steps it deems appropriate to collect fines and costs which are assessed in NASD disciplinary proceedings." These steps include referring matters "to external collection agencies and in appropriate situations, the

NASD will seek to reduce such fines to a judgment." *Id*. at n 2. FINRA's ability to assess fines against its members and associated persons "makes its imprimatur meaningful and commercially valuable to its membership." *Markowski v. SEC*, 34 F.3d 99, 105 (2d Cir. 1994).

B. The Fieros Agreed to Pay Fines as a Condition of their Securities Industry Registration

It is undisputed, and the district court recognizes, that the registration forms executed by the Fieros—the Form U4 and the Form BD (A-39. 42)—obligated the Fieros to comply with FINRA rules, to pay all monies assessed by FINRA, and to abide by any sanctions imposed by FINRA in a final disciplinary action. Article XIII of the FINRA By-Laws, FINRA Rules 8310, 8320 and 8330 discussed in Sec. B(3)(a) of the Facts above, all authorize FINRA to impose fines on its members and associated persons, and obligated the payment thereof in cases that are final.

This obligation is enforceable both as a matter of federal law, as discussed in the prior section, or as recognized by the district court, as a function of FINRA's corporate status. New York courts specifically recognize the inherent right of private organizations to impose and collect fines against members. *Sigma Phi Soc., Inc. (Alpha of New York) v. Renssalaer Fraternity Managers Ass'n, Inc.*, 114

A.D.2d 711 (3d Dep't 1985); *Colodney v. New York Coffee and Sugar Exch., Inc*. 4 A.D.2d 137 (1st Dep't 1957), *aff'd*, 4 N.Y.2d 698 (1958).[4]

As a Delaware corporation registered to do business in New York, FINRA already has the right under sections 202(a)(2) of both the New York Business Corporations Law and the Not-for-Profit Corporations Law "[t]o sue and be sued in all courts . . ." N.Y. Bus. Corp. Law § 202(a)(2); N.Y. Not-For-Prof. Corp. Law § 202(a)(2). Delaware, FINRA's state of incorporation, has similar provisions in its General Corporations Law. *See* 8 Del. Code Ann. § 122(2). Nothing in the laws of either state requires a corporation's by-laws to specifically authorize the filing of lawsuits to enforce obligations owed to the corporation.

C. The Fieros Were On Notice of FINRA's Fine Collection Policy

The Fieros' next argument—that FINRA never notified the Fieros that it expected them to pay that were imposed—is equally invalid. Similar versions of the FINRA By-Laws and rules cited in this brief were in effect when the Fieros became registered. FINRA has notified its members since at least 1990 that it

[4] The Fieros' citation of *Merchants Ladies Garment Association, Inc. v. Coat House of William M. Schwartz, Inc.*, 152 Misc. 130; 273 N.Y.S. 317 (Mun. Ct. Manhattan 1934) is inapposite to this case. In *Schwartz*, the by-laws of the membership association did not include fines as possible penalties for rule violations, unlike FINRA's By-Laws and rules. FINRA respectfully submits that the court's holding has effectively been overruled by subsequent enactment of § 507 of the Not-for-Profit Corporations Law (N.Y. Not-For-Prof. Corp. Law § 507), which specifically permits not-for-profit corporations such as FINRA to impose fines and penalties against its members.

would seek to collect disciplinary fines in appropriate cases when it issued Notice to Members 90-21. That notice (issued along with FINRA's SEC rule filing[5]) advised FINRA membership that for disciplinary decisions issued on or after July 1, 1990, "the NASD will pursue collection of a fine imposed pursuant to a District Committee, the Market Surveillance Committee, or Board of Governors . . . once such decision becomes final." Notice to Members 90-21. FINRA advised its membership that fine collection was in addition to other possible sanctions, such as suspending or revoking membership for failure to pay a fine.

The Notice to Members 90-21 was published in April 1990, and became effective July 1, 1990. The SEC approved the policy on July 18, 1990. The Fieros became registered with FINRA on or about August 15, 1990. Thus, at the time the Fieros registered with FINRA, they were on notice that FINRA had a policy of collecting disciplinary fines. This policy was part of the "statutes, constitutions, certificates of incorporation, by-laws and rules and regulations" that John Fiero agreed to comply with when he executed the Form U4 to become registered in the securities industry, and that Fiero Brothers agreed to comply with when it executed the Form BD.

---

[5] The 1990 rule filing anticipated the Fieros' argument—FINRA determined not to apply the policy to decisions that concluded before July 1, 1990, "in light of the fact that respondents might have entered into settlements or elected not to pursue appellate remedies believing that direct efforts would not be made to collect fines in their cases." SEC Rel. No. 34-28227.

The Fieros received further notice of FINRA's collection policy after FINRA commenced disciplinary proceedings against them. Notice to Members 99-86 confirmed long-standing FINRA policy on fine collection, and confirmed that FINRA could and would in appropriate cases pursue collection of monetary sanctions against firms and individuals, even in cases where such firms and individuals were also expelled and barred from the securities industry. The Notice explicitly applied to "all NAC, Hearing Panel decisions, and default decisions issued on or after November 1, 1999." The Fiero hearing panel decision was issued on December 6, 2000, and the NAC decision was issued on October 28, 2002. A-83. Thus, the Fieros were on notice during the entire time of the firm's membership, that they were obligated to pay disciplinary fines, even if they were barred or expelled.

The Fieros also rely upon an out-of context excerpt from the paperback April 2000 edition of the NASD Manual to argue that FINRA does not collect fines. The excerpt states: "NASD disciplinary procedures are not designed to recover damages or to obtain relief for any party." The next sentence in the section, omitted from the Fieros' brief, clarifies the context: "Instead, they are used to promote membership compliance with high standards of commercial honor and just and equitable principles of trade by appropriately penalizing those who fail to comply." NASD Manual, April 2000, "Profile of the NASD." (Emphasis

added). The cited section ends with the following sentence: "Depending on the nature of the violations that have occurred, NASDR may sanction a member or an associated person by imposing any one or more of the following penalties: censure, fine, suspension or expulsion of a firm from membership in the NASD or revocation of a person's license to sell securities." (Emphasis added.)

First, the sentence cited by the Fieros is not a FINRA By-Law, rule or regulation, but is taken from a narrative description of NASD's regulatory authority, and has no legal force or effect. *Second*, the sentence refers to the well-known doctrine that FINRA disciplinary proceedings are not intended to provide private recoveries for individual investors against firms or brokers. The sentence to bar FINRA from imposing sanctions on its members in its own disciplinary proceedings. The inanity of the Fieros' argument is demonstrated by taking the sentence literally: if FINRA disciplinary proceedings were truly not intended to "obtain relief for any party" to those proceedings, then FINRA itself would have no authority to impose any kind of sanction on its members for violations of the securities laws. Even the Fieros concede that FINRA has this authority.

D. Section 21(e) of the Exchange Act Does Not Bar FINRA from Judicially Enforcing Disciplinary Fines

The SEC's approval of FINRA's collection policy in 1990 is inconsistent with the Fiero's argument that the SEC has the exclusive right to pursue SRO collections. *See* SEC Rel. No. 34-28277, *supra*. At any rate, Section 21(e) of the

Exchange Act (15 U.S.C. § 78u(e)) of the Exchange Act is does not apply to this action.

Section 21(e) confers upon the SEC the authority to enforce final SEC orders, including those affirming FINRA disciplinary decisions. *SEC v. Pinchas*, 421 F. Supp. 2d 781, 783 (S.D.N.Y. 2006) (holding that SEC had power to enforce order affirming FINRA sanction). *See also SEC v. Vittor* 323 F.3d 930 (11th Cir. 2003); *SEC v. Mohn***,** 465 F.3d 647, 651-652 (6th Cir. 2006), *citing Vittor* (**"**courts have held that the SEC may use § 21(e) for applications to enforce orders originally issued pursuant to the SEC's appellate authority under § 19"). (Emphasis added).

The Fieros never appealed the FINRA disciplinary action to the SEC, and therefore, there was no "order" over which the SEC could exercise its enforcement authority under § 21(e). If the Fieros' interpretation of the Exchange Act were adopted, regulated individuals could avoid a significant regulatory sanction—fines—by not appealing their case to the SEC. This would subvert the regulatory intent of the Exchange Act, and finds no support in the law.

In sum, FINRA has the authority to impose and collect fines, and it placed its members on notice of this authority and intent during the entire time of the

Fieros' membership. The Fieros' studied refusal to acknowledge these and other FINRA rules does not undermine the validity of the rules or of their obligation.[6]

II. THE DISTRICT COURT'S JUDGMENT DOES NOT VIOLATE THE FULL FAITH AND CREDIT ACT OR THE *ROOKER-FELDMAN* DOCTRINE

A. The District Court Did Not Violate Full Faith and Credit Because the New York Court of Appeals Did Not Adjudicate on the Merits

The Fieros argue that the district court violated the Full Faith and Credit Act, 28 U.S.C. § 1738, because it granted FINRA judgment on its claim after the state court dismissed it. Since the New York Court of Appeals ruled only on subject matter jurisdiction, and did not reach the merits of the case, *Fiero*, 10 N.Y.3d at 17, this argument is unavailing.

New York state preclusion law determines whether a federal court can review a case previously brought in state court without violating the Full Faith and Credit Act. *See Marresse v. American Academy of Orthopaedic Surgeons,* 470 U.S. 373, 382 (1985); *Vasquez v. Lindt*, 724 F.2d 321, 325 (2d Cir. 1983). But both *res judicata* and collateral estoppel require a valid and final judgment on the merits to preclude a subsequent action. *Leather v. Eyck*, 180 F.3d 420, 424 (2d Cir. 1998);

---

[6] The Fieros also argue that FINRA has never judicially enforced disciplinary fines, and therefore may not do so now. Their argument is undercut by their own citation to a FINRA collection action, *NASD Inc. v. Rafael Pinchas*, Index No. 602057/04, (Sup. Ct. N.Y. Cty.). A-311-357, Complaint and Transcript of February 8, 2005 hearing.

St. Pierre v. Dyer, 208 F.3d 394, 400 (2d Cir. 2000); *Bracey v. Safir*, 1999 U.S. Dist. LEXIS 13060, * 9-11 (S.D.N.Y. Aug. 24, 1999) (*quoting McQuire v. City of New York,* 1985 U.S. Dist. LEXIS 15198, *8 (S.D.N.Y. Oct. 7, 1985). Jurisdictional matters are not considered preclusive. *Exxon Mobil Corp. v. Saudi Basic Indus. Corp.*, 544 U.S. 280, 293 (2005); *Central Hudson Gas & Electric Corp. v. Empresa Naviera Santa S.A.*, 56 F.3d 359, 368 (2d Cir. 1995); *Colon v. Coughlin*, 58 F.3d 865, 869 (2d Cir. 1995); *Bracey*, 1999 U.S. Dist LEXIS at *13-14.[7] Since the New York Court of Appeals did not reach the merits of FINRA's claim, the district court was not precluded from resolving it, and the Full Faith and Credit Act was not violated.

B. The District Court Correctly Held that the *Rooker-Feldman* Doctrine Does Not Bar FINRA's Claim

Following this Court's limited remand to the district court, the Fieros argued that the *Rooker-Feldman* doctrine bars the district court's consideration of

[7] Although the Fieros claim that the New York Court of Appeals dismissed FINRA's claims as preempted by federal law, this is inaccurate. The New York Court of Appeals instead concluded that the claims fell within the exclusive jurisdiction of the federal courts -- a non-merits jurisdictional decision that does not implicate the Full Faith and Credit Act. Moreover, the district court was not bound to accord any deference to a state court's interpretation of a federal statute, let alone a jurisdictional statute. *See Ex Parte Worcester Cty. Nat. Bank*, 279 U.S. 347, 359 (1929); *Bankr. Serv. v. Ernst & Young* (*In re CBI Holding Co.*), 529 F.3d 432, 454 (2d Cir. 2008); *Wojchowski v. Daines*, 498 F.3d 99, 110 n 9 (2d Cir. 2007)

FINRA's counterclaim. The district court correctly rejected this argument, and this Court should follow suit.

"The *Rooker-Feldman* doctrine is confined to cases of the kind from which it acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments." *Exxon*, 544 U.S. at 284. *Exxon*, which is the Supreme Court's most recent holding on *Rooker-Feldman*, but which was not cited in the Brief for Appellants, holds that *Rooker-Feldman* is an extremely narrow doctrine and "there are only limited circumstances in which federal courts are precluded from exercising subject matter jurisdiction in an action it would otherwise be empowered to adjudicate under a congressional grant of authority." *Id*. at 283; *see also McKithen v. Brown*, 480 F.3d 89, 96 (2d Cir. 2007); *Hoblock v. Albany County Bd. of Elect*, 422 F.3d 77, 85 (2d Cir. 2005).

Rooker-Feldman is only applicable if a federal plaintiff lost in state court and invites the district court to review and remedy injuries caused by that state-court judgment. *McKithen,* 480 F.3d at 97. *See Ashby v. Polinsky* 328 Fed. Appx. 21, 21 (2d Cir. 2009). Additionally, *Rooker-Feldman* does not apply to federal court cases that were filed before the state-court judgment issued. *McKithen,* 480 F.3d at 97 (*quoting Exxon*, 544 U.S. at 292)).

Rooker-Feldman does not apply to this case for the following reasons: *First*, FINRA is not claiming an injury caused by the New York Court of Appeals. FINRA's injury springs from the Fieros' failure to pay the disciplinary fine, which preceded the onset of the state court case, therefore it was not an injury caused by the state court judgment. *Second*, the Fieros, who prevailed in state court on a jurisdictional issue, not FINRA, initiated this litigation, seeking a declaratory judgment that they are not liable to FINRA on the disciplinary fine. *Third*, FINRA is not seeking to overturn the decision of the New York Court of Appeals. To the contrary, FINRA counterclaim is entirely consistent with the state court's jurisdiction ruling that FINRA's claim could be brought only in federal court.

Lastly, *Rooker-Feldman* is inapplicable because the Fieros initiated a federal declaratory judgment action against FINRA on this issue before the New York Court of Appeals issued its judgment. Case No. 07-CIV-7679 (JMM), *John J. Fiero and Fiero Brothers, Inc. v. National Association of Securities Dealers, Inc*, was filed in the Southern District of New York on August 29, 2007, and dismissed on February 8, 2008. "Where there is parallel state and federal litigation, *Rooker-Feldman* is not triggered simply by the entry of judgment in state court." *Exxon*, 544 U.S. at 292. The instant lawsuit was filed on February 8, 2008, the same day that the first lawsuit was dismissed, with identical parties and claims. Even if

Rooker-Feldman were otherwise applicable, the Fieros' initiation of the first federal lawsuit would bar the doctrine's application to this case.

III. THE DISTRICT COURT CORRECTLY FOUND THAT FINRA DISCIPLINARY PROCEEDINGS ARE NOT "ARBITRATION"

The Fieros devote almost half of their brief to the proposition that FINRA's collection action violated the one-year limitations period applicable to confirmation of arbitration awards under the Federal Arbitration Act, 9 U.S.C. § 9. The argument assumes that FINRA disciplinary proceedings are "arbitration."

The FINRA disciplinary proceeding was brought against the Fieros pursuant to FINRA's regulatory mandate under Section 15A of the Exchange Act, not the Federal Arbitration Act. *See, e.g. Maschler v. Nat'l Ass'n of Secs. Dealers, Inc.*, 827 F. Supp. 131 (E.D.N.Y. 1993). In this regulatory scheme, FINRA is the regulator, and the Fieros are regulated entities. This is not the same relationship that gives rise to arbitration, and bears none of the indicia of arbitration.

A. No Arbitration Agreement

Arbitration requires a "clear, explicit and unequivocal" agreement between parties to arbitrate disputes. *Waldron v. Goddess*, 61 N.Y.2d 181, 183-184; 461 N.E.2d 273 (1984). The existence of an obligation to arbitrate depends upon "an agreement to arbitrate . . . voluntarily made . . . ." *Sarhank Corp. v. Oracle Corp.*, 404 F. 3d 657, 661 (2d Cir. 2005). No such agreement exists between FINRA and

the Fieros regarding the Fieros' compliance with federal securities statutes and rules, and FINRA rules. The document governing a registered person's relationship with FINRA is the Form U4, which obligates the registrant, in this case John Fiero, to "submit to and comply" with all FINRA rules and orders, and to "submit to the authority" of FINRA. A-41. This describes a relationship between a regulator and a regulated entity.[8]

B. FINRA's Disciplinary Procedures Derive from the Exchange Act

The disciplinary proceeding is the exclusive method by which FINRA disciplines firms and brokers who violate FINRA rules and federal securities laws. The disciplinary process is not mutual. The Exchange Act authorizes FINRA to bring disciplinary proceedings and to impose sanctions for violation of its rules against the Fieros. 15 U.S.C. § 78o-3(b)(7).

Also, unlike arbitration, the Fieros had no right in their FINRA disciplinary proceeding to "choose" the decision makers. FINRA disciplinary proceedings are governed by the Code of Procedure, and heard by hearing panels composed of a hearing officer (a FINRA employee) and two members of a FINRA District

[8] The Form U4 does contain a separate arbitration agreement on the same page as the provision obligating John Fiero to submit to FINRA rules. A-41. The agreement binds the registrant to arbitrate disputes with customers and/or the registrant's employer under the FINRA arbitration rules—it contains no reference to disputes with FINRA or to disciplinary proceedings. The existence of a separate and explicit arbitration provision for disputes between brokers, or between customers and brokers rebuts any argument that disciplinary proceedings are also "arbitration".

Committee. Rule 9231(b). The requirement that adjudicators be impartial, which is argued by the Fieros to be evidence of "arbitration," is in fact a requirement of Section 15A of the Exchange Act, which requires SRO rules to provide "a fair procedure for the disciplining of members and persons associated with members . . . ." 15 U.S.C. § 78o-3(b)(8).

C. Different Standard of Review

Unlike arbitration awards, FINRA disciplinary decisions are not reviewable by a state court, or even directly reviewable by a federal district court, but exclusively by the SEC and thereafter by the United States Court of Appeals. *Maschler, id.* The standard of SEC review of FINRA disciplinary decisions (*de novo*) is fundamentally different from the narrow statutory bases for review of an arbitration award, which are set forth in § 10 of the Federal Arbitration Act, 9 U.S.C. § 10.

In this case, and in the four years of litigation preceding this case, the Fieros did not cite a single legal authority holding FINRA disciplinary proceedings to be arbitration.[9]

[9] In the complete absence of any legal authority, the Fieros "cite" to a stray reference in a transcript from an unrelated collection proceeding, in which a state court judge referred to a disciplinary decision as "award.". A-310-357, *NASD, Inc.d v. Rafael Pinchas*, Index No. 602057/04 (Sup. Ct. .N.Y. Cty). The disciplinary decision in that case was issued in 1998, but the court did not dismiss the case as an untimely attempt to confirm an arbitration award.

IV. FINRA'S COUNTERCLAIM FALLS WITHIN THE STATUTE OF LIMITATIONS

A. To the Extent FINRA's Claim Sounds in State Law, New York's Six-Year Statute of Limitations Applies

The date upon which the statute of limitations on FINRA's claim started to run is December 2, 2002 – the date when the FINRA disciplinary decision became final. *See* FINRA Rule 9360. New York has a six year statute of limitations for breach of contract. N.Y. C.P.L.R. § 213(2). Because FINRA brought its state court claim in February 2004[10] and its federal counterclaim on August 4, 2008, it is well within the six-year statute of limitations set forth in N.Y. C.P.L.R § 213(2).

In response, the Fieros assert that three other statutes of limitation apply to bar FINRA's counterclaim.

B. Arbitration

Because FINRA disciplinary proceedings are not arbitrations (See Section III above), an action to collect a resulting fine is not a proceeding to confirm an award subject to the Federal Arbitration Act or its one-year statute of limitations provision.

[10] The district court decision states that the FINRA state court lawsuit was brought in December 2003. That date, however, is the date the complaint was signed, not the date it was filed. The complaint was filed on February 23, 2004, and was pursuant to court practice assigned a case number ending in "04."

C. 28 U.S.C. § 2462

The Fieros argue that FINRA's counterclaim, brought in 2008, is barred by the five year limitations period in 28 U.S.C. § 2462, the statute that applies to the enforcement of federally imposed fines.

Even if the Court applies the five-year statute of limitations provision in 28 U.S.C. § 2462, FINRA's claim is not barred. Under Federal law, "[t]he doctrine of equitable tolling 'is read into every federal statute of limitation.'" *Fajardo v. INS*, 300 F.3d 1018, 1020 n.3 (9th Cir. 2002) (citations omitted); *Bowen v. Rubin*, 385 F. Supp. 2d 168, 179 (E.D.N.Y. 2005) ("Generally, federal equitable tolling doctrines apply so long as tolling is not inconsistent with the legislative purpose").

The doctrine of equitable tolling is applied on a case-by-case basis, *Catala v. Bennett*, 273 F. Supp. 2d 468, 472 (S.D.N.Y. 2003), and is ordinarily applied where:

> plaintiff actively pursued judicial remedies but filed a defective pleading during the specified time period,…plaintiff was unaware of his or her cause of action due to misleading conduct of the defendant,…or where a plaintiff's medical condition or mental impairment prevented her from proceeding in a timely fashion….

Zerilli-Edelglass v. N.Y. City Transit Auth., 333 F.3d 74, 80 (2d Cir. 2003) (citations omitted); *see also Polanco v. U.S. Drug Enforcement Admin.*, 158 F.3d 647, 655 (2d Cir. 1998) (the doctrine of equitable tolling "allows a district court to

toll the statute of limitations where, *inter alia*, a plaintiff initially 'asserted his rights in the wrong forum'"). When determining applicability of the equitable tolling doctrine, the court should consider whether the plaintiff "(1) has 'acted with reasonable diligence during the time period she seeks to have tolled,' and (2) has proved that the circumstances are so extraordinary that the doctrine should apply." *Zerilli-Edelglass*, 333 F.3d at 80-81 (citation omitted).

Where a plaintiff "has actively pursued his judicial remedies" but filed a defective pleading, equitable tolling of the statute of limitations is appropriate. *Hyatt v. U.S.*, 968 F. Supp. 96, 101-102 (E.D.N.Y. 1997). While statutes of limitation are designed to bar "plaintiffs who sleep on their rights," when that is not a concern, the doctrine of equitable tolling should act to preserve a plaintiff's claim. *See, e.g., Maxwell v. Swain*, 833 F.2d 1177, 1178 (5th Cir. 1987) (applying the doctrine of equitable estoppel to permit a claim filed outside the limitations period because the plaintiff asserted his claim during the applicable limitations period in state court, even though the state court action was subsequently dismissed for improper venue).

FINRA acted with reasonable diligence both before and during the time the state court action was pending. FINRA sought to collect the disciplinary fine from the Fieros, and after the Fieros refused to pay, timely filed the state court action to collect. During the time that the state court action was pending, there was no

reason for FINRA to believe that it had proceeded in the wrong forum to collect the fine or that the state court lacked subject matter jurisdiction to decide the dispute. In fact, both the Supreme Court of New York and the Appellate Division reviewed this matter and neither court concluded that they lacked jurisdiction to decide FINRA's claim. Nor was the legal issue of lack of subject matter jurisdiction raised by Fiero at any level in the state court action until the Court of Appeals considered the case. The Fieros were not prejudiced by the delay in filing the claim in federal court (as determined by the New York Court of Appeals to be the proper venue), nor have the Fieros provided any other reason why the statute of limitations should not be tolled.

D. 28 U.S.C. § 1658(b) is Inapplicable to this Case

The Fieros' final limitations argument is that FINRA's action to enforce its disciplinary fine is an action for securities fraud, and is subject to the limitations periods set forth in 28 U.S.C. § 1658(b). This argument is flawed for two reasons.

First, the Fieros never raised this argument below. "The law is well established that a federal appellate court will generally not consider an issue or argument not raised [in the district court]." *Midland Cogeneration Venture L.P. v. Enron Corp. (In re Enron Corp.),* 419 F.3d 115, 126 (2d Cir. 2005), *quoting, Kamagate v. Ashcroft*, 385 F.3d 144, 151 (2d Cir. 2004).

Second, 28 U.S.C. § 1658(b) by its own terms applies to "a private right of action," meaning, "private securities fraud cases." *In re Enterprise Mortgage Acceptance Co., LLC, Securities Litigation*, 391 F.3d 401, 403 (2d Cir. 2004). Nothing in the history of Sarbanes-Oxley suggests that this provision was intended to apply to disciplinary actions brought pursuant to or to enforce sanctions imposed under Section 15A of the Exchange Act. Imposing a limitations period based on "date of discovery" or "date of occurrence" upon an action to enforce a disciplinary sanction makes no sense. That FINRA's underlying disciplinary claim asserted fraud is irrelevant to the analysis—this action is to enforce an already-imposed disciplinary fine, and to obtain compliance with the Fieros' signed agreements to pay such fines.

In sum, FINRA's counterclaim falls within every *applicable* statute of limitations.

V. THE DISTRICT COURT PROPERLY ENTERED JUDGMENT WHERE THE FACTS WERE NOT IN DISPUTE, AND THE COURT RESOLVED ALL LEGAL ISSUES

The district court recognized that where the facts were not in dispute, and where the court resolved the only legal issue in the case, it was appropriate to enter final judgment. Fiero's complaint and FINRA's counterclaim presented opposite sides of the same coin: the Fieros sought declaratory judgment that they were not obligated to pay the FINRA disciplinary fine. FINRA sought to enforce that fine.

While the Fieros did not file an answer to the FINRA counterclaim, they admitted each of the necessary elements in their complaint, namely, that they were subject to FINRA rules by virtue of their securities industry registration (A-11, Complaint at ¶¶ 12-14); that FINRA filed a disciplinary complaint against them, and that they were fined $1,000,000, plus costs, as a result (Complaint at ¶¶ 15-16); that the Fieros exercised their right of appeal to the NAC, but did not appeal to the SEC, thereby rendering the decision final (Complaint at ¶¶ 17-18, A-12, Complaint at ¶ 21); and that they did not pay the fine (A-12, Complaint at ¶¶ 22-28, describing Fieros' legal battles to avoid paying the fine).

The Fieros staked their entire case upon their legal claim that FINRA does not have the authority to judicially enforce disciplinary fines it imposes, knowing that an adverse decision meant that FINRA does have the right to enforce its fines. When the district court resolved that issue, it resolved the entire case, and entry of final judgment was entirely appropriate.[11]

[11] The Fieros argue that judgment was improper because FINRA's damages were not liquidated, and that the Fieros were entitled to discovery on this issue. Under FINRA Rule 8310(b), however, the Fieros assented to the sanction when they did not appeal the NAC decision.

VI. FEDERAL JURISDICTION IS PROPER FOR CLAIMS THAT ARISE FROM FINRA'S FEDERALLY MANDATED REGULATORY DUTIES AND THEREFORE ARISE UNDER FEDERAL LAW

This Court can affirm the district court's grant of judgment to FINRA based upon the district court's correct finding of diversity jurisdiction. However, there is also federal question jurisdiction, as the New York Court of Appeals held. Section 27 of the Exchange Act, 15 U.S.C. § 78aa provides:

> The district courts of the United States and the United States courts of any territory or other place subject to the jurisdiction of the United States shall have excusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder:

The district court erred in analyzing federal question jurisdiction solely under 28 U.S.C. § 1331, without considering the independent grant of federal jurisdiction provided by Section 27 of the Exchange Act (which was the basis of the New York Court of Appeals decision). The district court relied upon *Merrell Dow Pharmaceuticals v. Thompson*, 478 U.S. 804 (1986), a § 1331 case, to find that there was no federal question jurisdiction. The *Merrell* line of cases was distinguished by the Ninth Circuit in *Sparta Surgical Corp. v. Nat'l Ass'n of Secs. Dealers, Inc.*, 159 F.3d 1209, 1212-13 (9th Cir. 1998): "[T]he rule that state law claims cannot be alchemized into federal causes of action by incidental reference has no application when relief is partially predicated on a subject matter committed exclusively to federal jurisdiction." *Sparta*, 159 F.3d at 1212–13 (citation

omitted) (holding that 15 U.S.C. § 78aa is basis for subject matter jurisdiction over state law claims arising from breach of FINRA rules).

The Exchange Act authorizes FINRA to enforce federal securities laws and rules, along with FINRA's own rules. FINRA's authority to impose sanctions on its members firms and their brokers derives from Section 15A(b)(7) of the Exchange Act:

> The rules of the Association [must] provide that . . . its members and persons associated with members shall be appropriately disciplined for any violation of any provision of this title, the rules or regulations thereunder . . . by expulsion, suspension, limitation of activities, functions, and operations, fine, censure, being suspended or barred from being associated with any member, or any other fitting sanction.

15 U.S.C. § 78o-3(b)(7). (Emphasis added).

Section 15A(h)(1) of the Exchange Act (15 U.S.C. § 78o-3(h)(1)), contemplates that SROs will impose "disciplinary sanctions" and sets forth requirements in order for registered securities associations to levy such sanctions. 15 U.S.C. § 78o-3(h)(1)(A-C). FINRA's disciplinary action against the Fieros found both violations of FINRA rules, and violations of Section 10(b) of the Exchange Act, and SEC Rule 10b-5. The SEC has approved FINRA's policy of judicially enforcing disciplinary fines. *See Notice of Filing and Immediate Effectiveness of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to the Collection of Fines and Costs in Disciplinary Proceedings*, Rel. No. 34-28227, 55 F.R. 30336 (Jul. 25, 1990).

The complaint and counterclaim in this action require judicial consideration of the Exchange Act, and of FINRA's SEC-approved rules and policies. The complaint in this case alleges that FINRA has no authority under the federal securities laws judicially enforce a disciplinary sanction. A-13, Complaint at ¶¶ 28, 30. The Fieros further argue that only the SEC has the right to collect FINRA fines in court (Brief of Appellants at 62-65); and that no FINRA rules, by-laws or other procedures permit the collection of disciplinary fines. (Brief of Appellants at 65-68). FINRA's counterclaim seeks judicial enforcement of the disciplinary proceeding that the Fieros dispute, pursuant to a policy communicated to the members and approved by the SEC.

The district court's characterization of FINRA disciplinary proceedings as "private" (*Fiero v. Finan. Indus. Reg. Auth., Inc*. 606 F. Supp. 2d 500, 507 (S.D.N.Y. 2009)) is fundamentally at odds with prevailing case law. Courts have recognized the essential federal nature of FINRA's activity in the analogous area of motions to remand, where courts have consistently found federal question jurisdiction. *See, e.g*., *Coleman v. National Association of Securities Dealers, Inc.*, No. 99 Civ. 248 (BSJ), 1999 U.S. Dist. LEXIS 7172 at * 3 (S.D.N.Y. May 14, 1999) (denying motion to remand because complaint that NASD violated "its internal rules" in plaintiff's disciplinary proceeding states federal question); *Christian, Klein & Cogburn v. Nat'l Ass'n of Secs. Dealers, Inc.*, 970 F. Supp. 276,

277 (S.D.N.Y. 1997) (denying remand of action for pre-complaint discovery where contemplated complaint included breach of contract claim). *See also Sparta, supra*; *Hawkins v. Nat'l Ass'n of Secs. Dealers, Inc*., 149 F.3d 330, 332 (5th Cir. 1998); *Empire Financial Group, Inc. v. FINRA, Inc., et al.*, No. 08-80534, Dkt. Entry 12 (S.D. Fla. Jan. 15, 2009); *Whitehall Wellington Invs., Inc. v. Nat'l Ass'n of Secs. Dealers, Inc.*, No. 00-3899-CIV-MIDDLEBROOKS, 2000 U.S. Dist. LEXIS 18607 at * 7 (S.D. Fla. Dec. 7, 2000); *Lowe v. NASD Regulation, Inc.*, No. 99-1751 (TFH), 1999 U.S. Dist. LEXIS 19489 (D.C. Dec. 14, 1999) (denying remand of state law claim for breach of contract); *Hibbard Brown & Co., Inc. v. Nat'l Ass'n of Secs. Dealers, Inc.*, No. 94-285-SLR, 1994 U.S. Dist. LEXIS 20527 at * 5 (D.Del. Oct. 6, 1994).

These cases do not contradict this Court's decision in *Barbara v. New York Stock Exchange, Inc.*, 99 F.3d 49 (2d Cir. 1995). In *Barbara*, the Court considered the removal of a state court action alleging violations of NYSE internal rules, concluding that removal was improper, but ultimately deciding that plaintiff's claims against the New York Stock Exchange were properly dismissed. 99 F.3d at 49.

Barbara does not stand for the proposition that all SRO claims implicating state law do not also pose a federal question. In *D'Alessio v. New York Stock Exchange, Inc.*, 258 F.3d 93 (2d Cir. 2001), this Court reached the opposite

conclusion in a case alleging numerous state law claims against the New York Stock Exchange. 258 F.3d at 97-98. In *D'Alessio*, this Court concluded that although the complaint made state law claims, "the federal interest is more substantial" because "D'Alessio's suit is rooted in violations of federal law, which favors a finding that federal jurisdiction exists." 258 F.3d at 101. *See also Frayler v. New York Stock Exchange, Inc.*, 118 F. Supp. 2d 448 (S.D.N.Y. 2000).

CONCLUSION

For the foregoing reasons, FINRA requests this Court to affirm the district court's judgment in all respects, except for the district court's finding on federal question jurisdiction, which should be reversed.

Respectfully submitted,

Dated: November 18, 2009
Washington, DC

FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.

/s/_____

Terri L. Reicher
Associate General Counsel
Financial Industry
Regulatory Authority, Inc.
1735 K Street, N.W.
Washington, DC 20006
Telephone (202) 728-8967
FAX (202) 728-8894
Terri.Reicher@finra.org

CERTIFICATE OF COMPLIANCE

Pursuant to Fed. R. App. P. 32(a)(7)(C), I hereby certify that this brief was produced in Times New Roman (a proportionally-spaced typeface), in 14-point type (inclusive of footnotes), and contains 9,728 words (based on the Microsoft Word word count function).

Dated: Washington, D.C.
November 18, 2009

/s/_____
Terri L. Reicher

STATE OF NEW YORK)
) ss.: **AFFIDAVIT OF**
COUNTY OF NEW YORK) **PERSONAL SERVICE**

I, , being duly sworn, depose and say that deponent is not a party to the action, is over 18 years of age and resides at the address shown above or at

On November 18, 2009

deponent served the within: **Brief for Defendant-Counterclaimant-Appellee-Cross-Appellant**

upon:

BRIAN GRAIFMAN
GUSRAE, KAPLAN, BRUNO & NUSBAUM PLLC
Attorneys for Plaintiffs-Counter-Defendants-Appellants-Cross-Appellees
120 Wall Street
New York, NY 10005
(212) 269-1400
BGraifman@gkblaw.com

the attorney(s) in this action by delivering **2** true copy(ies) thereof to said individual personally. Deponent knew the person so served to be the person mentioned and described in said papers as the Attorney(s) herein and electronically by email.

Sworn to before me on November 18, 2009

LUISA M. WALKER
Notary Public State of New York
No. 01WA6050280
Qualified in New York County
Commission Expires Oct 30, 2010

Job # **226029**

ANTI-VIRUS CERTIFICATION FORM
Pursuant to Second Circuit Local Rule 32(a)(1)(E)

CASE NAME: Fiero v. Financial Industry Regulatory Authority, Inc.

DOCKET NUMBER: 09-1556-cv (L); 09-1863-cv (XAP)

I, Luisa M. Walker, certify that I have scanned for viruses the PDF version of the:

_____ Appellant's Brief

__X_____ Appellee's Brief

_____ Reply Brief

_____ Amicus Brief

_____ _____

that was submitted in this case as an email attachment to <civilcases@ca2.uscourts.gov> and that no viruses were detected.

Please print the **name** and the **version** of the anti-virus detector that you used:

Vipre Enterprise Version 3.1 was used.

_____
Luisa M. Walker

Date: November 18, 2009