

## Dispute Between Securities' Brokers Not Subject to FINRA Arbitration

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[Valentine Capital Asset Management, Inc. v. Agahi](#), \_\_ Cal. App. 4th \_\_, 2009 WL 1496819 (June 1, 2009).

Several of our insurer clients who act as broker-dealers in connection with the sale of “securities” find themselves litigating in Financial Industry Regulatory Authority (“FINRA”) (formerly NASD) arbitrations when disputes arise. Sometimes, our insurer clients prefer not to litigate in a FINRA forum under its rules. A very recent California Court of Appeals case discussed the types of disputes that are not subject to FINRA arbitration.

In [Valentine Capital Asset Management, Inc. v. Agahi](#), \_\_ Cal. App. 4th \_\_, 2009 WL 1496819 (June 1, 2009), the court held that a dispute between securities’ brokers was not subject to arbitration pursuant to FINRA rules because the dispute did not relate to the brokers’ activities as members of FINRA-associated firms.

Valentine was the founder and president of Valentine Capital Asset Management, Inc. (“VCAM”) and Valentine Wealth Management, Inc. (“VWM”), neither of which was a member of FINRA.

Agahi, Luippold and Ortale worked for VCAM and VWM. When they left, Agahi formed a competing firm. Luippold and Ortale joined him at that firm and they allegedly took with them the VCAM and VWM client databases. Valentine sued Agahi, Luippold and Ortale (“defendants”) for misappropriation of trade secrets and other causes of action. Defendants moved to compel arbitration, arguing that because they were all members of FINRA, their dispute was subject to mandatory arbitration under FINRA’s arbitration clause. Valentine opposed the defendants’ motion, contending essentially that the defendants had waived their right to arbitrate and that the disputes in the litigation were not subject to FINRA arbitration.

The trial court denied the motion to compel arbitration, finding that FINRA was inapplicable because the parties’ dispute did not arise out of their business activities as FINRA members. The Court of Appeal affirmed.

The Court first explained that written arbitration provisions in interstate commercial transactions are enforceable under the FAA and that the FAA therefore applied to determine the scope of arbitration provisions in contracts with FINRA-member firms. Before engaging in activities as a registered representative for a FINRA-member firm, all registered representatives of broker-dealers, investment advisors, and securities issuers must sign a “Uniform Application for Securities Industry Registration or Transfer,” commonly referred to as Form U-4. *See McManus v. CIBC World Markets Corp.*, 109 Cal. App. 4th 76, 88 fn. 3 (2003). Form U-4 contains an arbitration provision. By signing this form, Valentine and the defendants agreed to arbitrate every dispute required to be arbitrated under FINRA rules.

Noting that arbitration of a dispute between associated persons is required under FINRA Rule 13200 only “if the dispute arises out of the business activities of a member or an associated person . . .,” the court stated:

[T]he phrase ‘business activities of ... an associated person’ must have some limitation and cannot include the activities of every possible business enterprise in which an individual, who happens to be an ‘associated person,’ might be engaged. The mandate to arbitrate disputes arising out of ‘business activities of ... an associated person,’ reasonably read, must require arbitration of disputes only if they arise out of the business activities of an individual as an associated person of a FINRA member.

The court held that there was no allegation that any of the parties were acting for any FINRA-member firm or as an associated person and no relation was alleged between any FINRA-member firm and the work performed for Valentine. Further, the Court determined that none of the purported wrongdoing was alleged to have occurred in the course of the parties’ duties as associated persons with a FINRA-member firm. Instead, it allegedly occurred in connection with investment advisory firms which were not members of FINRA. The disputes thus related to Valentine and defendants, but not to their business activities as associated persons of a FINRA member.