

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-66109; File No. SR-FINRA-2011-075]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change To Amend the Code of Arbitration Procedure for Industry Disputes To Preclude Collective Action Claims From Being Arbitrated

January 5, 2012.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on December 22, 2011, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend Rule 13201 of the Code of Arbitration Procedure for Industry Disputes (“Industry Code”) to preclude collective action claims by employees of FINRA members under the Fair Labor Standards Act (FLSA), the Age Discrimination in Employment Act (ADEA), or the Equal Pay Act of 1963 (EPA) from being arbitrated under the Industry Code.

The text of the proposed rule change is available on FINRA’s Web site at <http://www.finra.org>, at the principal office of FINRA and at the Commission’s Public Reference Room.

#### II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

#### A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

##### 1. Purpose

Current Rules 12204 of the Code of Arbitration Procedure for Customer Disputes (Customer Code) and 13204 of the Industry Code (together, class action rules) provide that any claim that is based upon the same facts and law, and involves the same defendants as in a court-certified class action or a putative class action, shall not be arbitrated, unless the party bringing the claim files with FINRA one of the following: (1) A copy of a notice filed with the court in which the class action is pending that the party will not participate in the class action or in any recovery that may result from the class action, or has withdrawn from the class according to any conditions set by the court; or (2) a notice that the party will not participate in the class action or in any recovery that may result from the class action.

In 1999, FINRA issued an Interpretive Letter (FINRA Letter) stating that its class action rules should include collective action claims brought under the FLSA<sup>3</sup> and, therefore, has considered these claims ineligible for arbitration in its forum.<sup>4</sup> Nevertheless, in *Hugo Gomez et al. v. Brill Securities, Inc. et al.*, the United States District Court for the Southern District of New York found that an FLSA collective action is not a class action for purposes of Rule 13204 of the Industry Code and, thus, compelled arbitration of the claim in FINRA’s dispute resolution forum.<sup>5</sup>

As the court found that FINRA’s interpretation of its class action rules did not expressly exclude collective actions from being arbitrated in the forum, FINRA is proposing to amend its class action rule of the Industry Code to preclude collective action claims under the FLSA from being arbitrated in its forum. As a collective action claim also may be filed pursuant to the ADEA<sup>6</sup> or EPA,<sup>7</sup> FINRA is proposing to preclude

these claims from being arbitrated as well. The Customer Code would not be amended because, for the FLSA, ADEA or EPA to apply, there must be an employment relationship between an “employer” and “employee.”<sup>8</sup>

#### United States District Court Decision

In *Gomez*, the plaintiffs, registered representatives formerly employed by Brill Securities, Inc. (Brill), filed an FLSA collective action claim seeking unpaid overtime compensation on behalf of similarly situated former and current Brill stockbrokers. They relied on the FINRA Letter, which concludes that FLSA claims should be considered ineligible for arbitration in the NASD Regulation (now FINRA) forum.<sup>9</sup> The court found that the FINRA Letter did not, however, distinguish between collective and class actions and, therefore, did not expressly preclude collective actions from being eligible for arbitration at FINRA. The *Gomez* court was not persuaded by the FINRA Letter and concluded that the differences between a class action and an FLSA collective action undercut FINRA’s position that collective actions should be treated like class actions. Based on its analysis, the court found that an FLSA collective action is not a class action for purposes of Rule 13204, and compelled arbitration of the plaintiffs’ claims.<sup>10</sup>

#### Collective Actions Under the FLSA, ADEA, and EPA

As stated above, under the FLSA, ADEA, and EPA, courts are permitted to certify a collective action,<sup>11</sup> rather than a class action, under the Federal Rules

Commission. The relief provisions of the EPA also incorporate Section 16 of the FLSA.

<sup>8</sup> See U.S. Department of Labor, “What does the Fair Labor Standards Act require?,” elaws—Fair Labor Standards Act Advisor, available at <http://www.dol.gov/elaws/esa/flsa/screen5.asp> (last visited July 26, 2011).

<sup>9</sup> *Supra* note 4 at 2.

<sup>10</sup> *Supra* note 7. Several courts have agreed with this finding when they considered whether an FLSA collective action is arbitrable under FINRA rules. See, e.g., *Velez v. Ph.D. Capital Corp.*, No. 10 Civ. 3735, 2011 U.S. Dist. LEXIS 16678 (S.D.N.Y. Feb. 3, 2011); *Suschil v. Ameriprise Financial Servs., Inc.*, No. 07 Civ. 2655, 2008 U.S. Dist. LEXIS 27903 (N.D. Ohio Apr. 7, 2008); and *Chapman v. Lehman Bros., Inc.*, 279 F. Supp. 2d 1286 (S.D. Fla. 2003).

<sup>11</sup> See *Hyman v. First Union Corp.*, 982 F. Supp. 1, 26 (D.D.C. 1997) (approving two collective actions for (1) former bank employees and (2) persons seeking employment, alleging age discrimination under the ADEA). See also *Schwed v. General Electric Co.*, No. 94-CV-1308, 1997 U.S. Dist. LEXIS 5103 at \*10 (N.D.N.Y. April 11, 1997) (approving collective action for former employees of an industrial power plant alleging age discrimination); *Jarvaise et al. v. Rand Corporation*, Civil Action No. 96-2680, 212 F.R.D. 1 (D.D.C. 2002) (certifying class of all female Rand employees in exempt positions under EPA).

<sup>3</sup> See 29 U.S.C. 201 *et seq.*

<sup>4</sup> See, e.g., FINRA Interpretive Letter to Cliff Palefsky, Esq., dated Sept. 21, 1999. The letter is available at <http://www.finra.org/Industry/Regulation/Guidance/InterpretiveLetters/P002521> (last visited on June 7, 2011).

<sup>5</sup> *Hugo Gomez et al. v. Brill Securities, Inc. et al.*, No. 10 Civ. 3503, 2010 U.S. Dist. LEXIS 118162 (S.D.N.Y. Nov. 2, 2010).

<sup>6</sup> See 29 U.S.C. 621 *et seq.* The relief provisions of the ADEA incorporate Section 16 of the FLSA, which outlines the penalties for violations of the statute, and state that the ADEA shall be enforced by the “powers, remedies and procedures” of the FLSA. See 29 U.S.C. 626(b).

<sup>7</sup> See 29 U.S.C. 206(d). The EPA, which is part of FLSA as amended, is administered and enforced by the United States Equal Employment Opportunity

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

of Civil Procedure.<sup>12</sup> One difference between a collective action and a class action is that, under the collective action statutes, collective action members must affirmatively consent or “opt-in” to become a member of a collective action to benefit or be bound by the judgment. This means that a collective action member will not be bound by the case, unless the person affirmatively consents to become a member.<sup>13</sup> This requirement effectively protects the interests of absent class members, because a lack of consent to join a collective action would not preclude them from pursuing their claims in other forums.<sup>14</sup>

#### Proposed Amendments to Rule 13204

FINRA is proposing, therefore, to amend Rule 13204 of the Industry Code to preclude collective actions from being arbitrated in the forum.

The current rule would be separated into two sections: Subparagraph (a) for class actions, and subparagraph (b) for collective actions. Subparagraph (a) would be titled, “Class Actions,” and re-numbered. Subparagraph (b) would be titled, “Collective Actions,” and would contain four subparagraphs.

First, proposed Rule 13204(b)(1) would state that collective action claims under the FLSA, the ADEA, or the EPA may not be arbitrated under the Code. FINRA believes that, although collective actions are opt in actions, once a court grants approval for the collective action to proceed under a federal statute, the claims in dispute are administered like a class action, and, therefore, should be ineligible for arbitration in FINRA’s forum. Moreover, FINRA believes that collective actions, like class actions, should be handled by the judiciary system, which has extensive procedures to manage such claims.

Second, under proposed Rule 13204(b)(2), any claim that involves similarly-situated<sup>15</sup> plaintiffs against the same defendants, like a court-

certified collective action or a putative collective action,<sup>16</sup> would not be arbitrated in FINRA’s arbitration forum. Thus, if an associated person opts in to a collective action, that person could not arbitrate the same claims in FINRA’s arbitration forum. The proposed rule would not prevent an associated person from opting in to a collective action in court. However, an associated person would be required to choose the forum—either arbitration or court—that the person believes would address effectively the issues in dispute. Further, under proposed Rule 13204(b)(2), a case in which a court orders the plaintiffs to file as a collective action at a forum not sponsored by a self-regulatory organization would be ineligible for arbitration at FINRA.

Third, proposed Rule 13204(b)(3) would give arbitrators the authority to decide disputes about whether a claim is part of a collective action. This provision would be consistent with the proposed, renumbered class action rule, Rule 13204(a)(3), in that the panel decides the merits and disposition of an arbitration claim. Alternatively, under the proposed rule, parties may ask the court hearing the collective action to resolve the dispute concerning whether the claim is part of the collective action within 10 days of receiving notice that the Director has decided to refer the dispute to a panel.

Fourth, proposed Rule 13204(b)(4) would prohibit a member firm or associated person from enforcing any arbitration agreement against a member of a certified or putative collective action with respect to any claim that is the subject of the certified or putative collective action until either the collective certification is denied or the group is decertified. This proposed rule clarifies that the existence of a certified or putative collective action nullifies any pre-dispute arbitration agreements. If, however, a court denies a plaintiff’s request to certify a collective action or the court decertifies the collective action, the pre-dispute arbitration agreement would be enforceable, and FINRA would arbitrate the claims.

Finally, FINRA is proposing to amend grammatical references in the concluding paragraph of Rule 13204 to clarify that it applies to class actions as well as collective actions.

FINRA believes the proposed rule would facilitate the efficient resolution of collective actions, as the courts have established procedures to manage these types of representative actions.

Moreover, FINRA believes access to courts for class or collective action litigation should be preserved for associated persons, and the proposal accomplishes this goal.

#### 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>17</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes the proposal would facilitate the efficient resolution of collective actions, as courts have established procedures to manage these types of representative actions. Further, FINRA believes preserving access to courts for these types of claims for associated persons protects the public interest as it permits associated persons and the forum to allocate resources effectively.

#### B. Self-Regulatory Organization’s Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition or capital formation that is not necessary or appropriate in furtherance of the purposes of the Act, as amended. Further, FINRA believes that the proposal will promote efficiency in the arbitration forum as class and collective actions will be administered by the judicial system, which have established procedures to manage such cases.

#### C. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

Written comments were neither solicited nor received.

#### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve or disapprove such proposed rule change, or

<sup>12</sup> Fed. R. Civ. P. 23.

<sup>13</sup> *Cathy Ventrell-Monsees, Representative and Collective Actions Under the ADEA Class Actions in Employment Law: Class Action Basics*, Aug. 10, 1999, <http://www.bna.com/bnabooks/ababna/annual/99/adeaclas.pdf> at 1–3.

<sup>14</sup> See *Saincome v. Truly Nolen of America, Inc.*, No. 11–CV–825–JM, 2011 U.S. Dist. LEXIS 85880 (S.D.C.A. Aug. 3, 2011) (affirming that 29 U.S.C. 216(b) of FLSA permits class members to participate in a collective action on an opt-in basis only, thus preserving absent parties’ rights to proceed with the claim in arbitration).

<sup>15</sup> The FLSA uses the term “similarly-situated,” but does not define it. See 29 U.S.C. 216(b). However, its meaning can be understood by considering two criteria that a plaintiff must demonstrate under the FLSA: (1) That there are common questions of law or fact, and (2) that the claims or defenses are typical of those of the class of plaintiffs. See *supra* note 3.

<sup>16</sup> Before a collective action is certified, courts often refer to the case as a putative collective action.

<sup>17</sup> 15 U.S.C. 78o–3(b)(6).

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2011-075 on the subject line.

##### *Paper Comments*

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090.
- All submissions should refer to File Number SR-FINRA-2011-075. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-FINRA-2011-075 and should be submitted on or before February 1, 2012.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>18</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-66102; File No. SR-CME-2011-22]

### Self-Regulatory Organizations; Chicago Mercantile Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Establish Certain Fee Programs in Connection With Its OTC Interest Rate Swap Clearing Offering

January 5, 2012.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on December 22, 2011, Chicago Mercantile Exchange Inc. ("CME") filed with the Securities and Exchange Commission ("Commission") the proposed rule change described in Items I, II and III below, which items have been prepared primarily by CME. CME filed the proposed rule change pursuant to Section 19(b)(3)(A)<sup>3</sup> of the Act and Rule 19b-4(f)(2)<sup>4</sup> thereunder.

#### I. Self-Regulatory Organization's Statement of Terms of Substance of the Proposed Rule Change

CME is proposing to make certain fee-related changes that would apply to its OTC Interest Rate Swap clearing offering. The text of the proposed changes is as follows:<sup>5</sup>

##### *CME Incentive Program for Over-the-Counter Interest Rate Swaps*

##### *Program Purpose*

The purpose of the Program is to incentivize participants to increase the volume in CME over-the-counter ("OTC") interest rate swaps which will improve market liquidity. The resulting addition of liquidity for these Products (as defined below) benefits all participants in the market.

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(2).

<sup>5</sup> The text of the proposed changes does not appear in CME's rulebook but is available on CME's Web site at <http://www.cmegroup.com/market-regulation/rule-filings.html>. Telephone conference between Tim Elliot, Director and Associate General Counsel, CME, and Doyle Horn, Special Counsel, Securities and Exchange Commission Division of Trading and Markets on January 4, 2012.

#### *Product Scope*

CME OTC Interest Rate Swaps cleared by the Clearing House ("Products").

#### *Eligible Participants*

CME may designate up to five (5) participants in the Program based on their level of expertise and experience with the Products. Participants may be CME members and/or non-members.

CME will also take potential participants' experience in the Products and historical volume in the Products with the Clearing House when making its selections.

#### *Program Term*

##### *Non-Asset Managers*

Qualification Period: January 6, 2012 through December 31, 2012.

Earned Incentive Period: January 1, 2013 through December 31, 2016.

##### *Asset Managers*

Qualification Period: January 6, 2012 through December 31, 2012.

Earned Incentive Period: January 1, 2013 through December 31, 2021.

#### *Hours*

N/A.

#### *Obligations*

Participants must provide designated accounts to CME in order for the account to receive consideration for the incentives described below.

#### *Incentives*

1. Fee Discounts. Once accepted into the Program, participants will be eligible to receive predetermined discounts for transaction fees and maintenance fees in the Products during the Term.

2. Volume Discount Incentives. Additionally, once accepted into the Program, participants may qualify for predetermined fee discounts based on the overall fees charged for transactions in the Products submitted to the Clearing House during the Qualification Period.

#### *Monitoring and Termination of Status*

The Clearing House shall monitor participants' activity and performance and shall retain the right to revoke Program participant status if they conclude from review that a Program participant no longer meets the eligibility requirements of the Program.

\* \* \* \* \*

### Founding Member Over-the-Counter Interest Rate Swap Incentive Program

#### *Program Purpose*

The purpose of the Program is to provide more liquid markets in OTC

<sup>18</sup> 17 CFR 200.30-3(a)(12).