First Allied Sec., Inc. v. Carrier

United States District Court for the Southern District of Texas, Houston Division

November 19, 2020, Decided; November 19, 2020, Filed, Entered

CASE NO. 4:20-CV-3456

Reporter
2020 U.S. Dist. LEXIS 243758 *; 2020 WL 7658067

FIRST ALLIED SECURITIES, INC., Plaintiff, v. BRIAN CARRIER, et al., Defendants.

Counsel: [*1] For Ajay Patel, Craig Thiessen, Sadiq Sohani, Salim Gopalani, Stacia Dyess-Hammond, Allison Carrier, Jyotsna Bhakta, RRMI MD Professional Association, James Hammond, Mark Thiessen, RLT Partnership Ltd., Sai Gundlappali, Brian Carrier, Jignesh Patel, Roy Kumar, Defendants: Marc Fitapelli, LEAD ATTORNEY, Fitapelli Kurta, New York, NY.

For Craig Thiessen, Ajay Patel, Jignesh Patel, RLT Partnership Ltd., Jyotsna Bhakta, Mark Thiessen, Sai Gundlappali, Stacia Dyess-Hammond, Allison Carrier, Salim Gopalani, Brian Carrier, RRMI MD Professional Association, Sadiq Sohani, Roy Kumar, James Hammond, Defendants: Jonathan Kurta, LEAD ATTORNEY, Fitapelli Kurta, New York, NY.

For First Allied Securities Inc., Plaintiff: Martin Samuel Schexnayder, ATTORNEY TO BE NOTICED, Winget Spadafora & Schwartzberg LLP, Houston, TX.

Judges: VANESSA D. GILMORE, UNITED STATES DISTRICT JUDGE.

Opinion by: VANESSA D. GILMORE

Opinion

ORDER

Pending before the Court is Defendant's Motion for Summary Judgment, **(Instrument No. 13)**, and Plaintiff's Motion for Summary Judgment, **(Instrument No. 14)**.

I.

A.

This dispute arises from an arbitration action before the Financial Industry Regulatory Authority ("FINRA"). (Instrument No. 13 at 1). Plaintiff First Allied **[*2]** Securities, Inc. ("Plaintiff" or "First Allied") brings this suit seeking injunctive and declaratory relief against thirteen individuals and two entities to prevent them from continuing with the arbitration action against Plaintiff. (Instrument No. 1). Plaintiff is a registered broker-dealer and member of FINRA. (Instruments No. 13 at 3). Defendants are Brian Carrier, Allison Carrier, Salim Gopalani, James Hammon, Roy Kumar, RRM1 MD Professional Association, Sadiq Sohani, Mark Thiessen, RLT Partnership Ltd, Stacia Dyess-Hammond, Jignesh Patel, Sai Gundlapalli, Ajay Patel, and Jyotsna Bhakta (collectively, "Defendants"). *Id.*

Defendants are a group of investors who were clients of Masood Azad ("Azad"). (Instrument No. 1-1 at 3). Azad was a licensed attorney in Texas and a former broker registered with Plaintiff. (Instrument No. 1 at 6). Azad operated his law practice out of the same privately-leased office he used to conduct his brokerage services for Plaintiff. (Instrument No. 3 at 8). Plaintiff alleges that Azad was only Defendants' attorney and that Azad used his own servers and data accounts while representing Defendants. *Id.*

Beginning around 2015, Defendants allege that Azad unlawfully **[*3]** solicited Defendants to invest millions of dollars in his son-in-law's company, Corax Cyber Security ("Corax"). (Instrument No. 1-1 at 3). Defendants allege that this fundraising initiative was conducted out of Azad's First Allied office. *Id.* at 5. Based on the recommendations of Azad, Defendants allege losses ranging from $ 100,000 to $ 840,000. (Instrument No. 3 at 7). Defendants contend that Azad's efforts to fundraise for Corax was known to all employees at First Allied. (Instrument No. 1-1 at 5).

In 2017, First Allied fired Azad for engaging in outside unapproved securities transactions. (Instrument No. 1-1 at 7). Aside from the investments with Azad, Defendants never held any investment or brokerage accounts with

Plaintiff. (Instrument No. 14 at 13-14).

On or about August 18, 2020, Defendants filed a FINRA arbitration action ("FINRA Arbitration") against First Allied under Rule 12200 of the FINRA Code of Arbitration Procedure. (Instruments No. 1-1 at 2; No. 3 at 5). Defendants filed the action pursuant to a customer agreement requiring arbitration of the dispute. (Instrument No. 1-1 at 2). Currently, the FINRA Arbitration has not advanced beyond the initial pleading state. (Instrument No. 13 at **[*4]** 3).

B.

On October 7, 2020, Plaintiff filed its Complaint in federal court. (Instrument No. 1). Plaintiff seeks a declaratory judgment and permanent injunction against Defendants. (Instruments No. 1; No. 14 at 2). On October 7, 2020, Plaintiff filed a Motion for Temporary Restraining Order and Preliminary Injunction, seeking to temporarily enjoin the Defendants from pursuing the FINRA Arbitration. (Instruments No. 2; No. 3). On October 9, 2020, Defendants filed their Response in opposition to Plaintiff's Motion. (Instrument No. 5).

On October 9, 2020, the Court held a motion hearing and denied Plaintiff's Motion for Temporary Restraining Order. The Court ordered the filing of motions for summary judgment by both parties. On October 19, 2020, both parties filed their Motions for Summary Judgment. (Instruments No. 13; No. 14).

II.

Summary judgment is appropriate "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *Celotex Corp. v. Catrett*, 477 U.S. 317, 322, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986); *Warfield v. Byron*, 436 F.3d 551, 557 (5th Cir. 2006); *see also* Fed. R. Civ. P. 56(a).

The "movant bears the burden of identifying those portions of the **[*5]** record it believes demonstrate the absence of a genuine issue of material fact." *Triple Tee Golf, Inc. v. Nike, Inc.*, 485 F.3d 253, 261 (5th Cir. 2007) (citing *Celotex*, 477 U.S. at 322-25). "A genuine issue of material fact exists when the evidence is such that a reasonable jury could return a verdict for the non-moving party." *Fisk Elec. Co. v. DQSI, L.L.C.*, 894 F.3d 645, 650 (5th Cir. 2018) (internal quotations omitted); *see also Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986).

If the burden of proof at trial lies with the nonmoving party, the movant may satisfy its initial burden by "showing — that is, pointing out to the district court — that there is an absence of evidence to support the nonmoving party's case." *Celotex*, 477 U.S. at 325. While the party moving for summary judgment must demonstrate the absence of a genuine issue of material fact, it does not need to negate the elements of the nonmovant's case. *Boudreaux v. Swift Transp. Co.*, 402 F.3d 536, 540 (5th Cir. 2005) (citation omitted). "If the moving party fails to meet [its] initial burden, the motion [for summary judgment] must be denied, regardless of the nonmovant's response." *United States v. $ 92,203.00 in U.S. Currency*, 537 F.3d 504, 507 (5th Cir. 2008) (quoting *Little v. Liquid Air Corp.*, 37 F.3d 1069, 1075 (5th Cir. 1994) (en banc)).

After the moving party has met its burden, in order to "avoid a summary judgment, the nonmoving party must adduce admissible evidence which creates a fact issue concerning the existence of every essential component of that party's case." *Thomas v. Price*, 975 F.2d 231, 235 (5th Cir. 1992). The party opposing summary judgment cannot merely rely on the contentions contained **[*6]** in the pleadings. *Little*, 37 F.3d at 1075. Rather, the "party opposing summary judgment is required to identify specific evidence in the record and to articulate the precise manner in which that evidence supports his or her claim." *Ragas v. Tenn. Gas Pipeline Co.*, 136 F.3d 455, 458 (5th Cir. 1998); *see also Baranowski v. Hart*, 486 F.3d 112, 119 (5th Cir. 2007). Although the court draws all reasonable inferences in the light most favorable to the nonmoving party, *Connors v. Graves*, 538 F.3d 373, 376 (5th Cir. 2008), the nonmovant's "burden will not be satisfied by some metaphysical doubt as to the material facts, by conclusory allegations, by unsubstantiated assertions, or by only a scintilla of evidence." *Boudreaux*, 402 F.3d at 540 (quoting *Little*, 37 F.3d at 1075). Similarly, "unsupported allegations or affidavit or deposition testimony setting forth ultimate or conclusory facts and conclusions of law are insufficient to defeat a motion for summary judgment." *Clark v. Am.'s Favorite Chicken*, 110 F.3d 295, 297 (5th Cir. 1997).

In deciding a summary judgment motion, the district court does not make credibility determinations or weigh evidence. *E.E.O.C. v. Chevron Phillips Chem. Co., LP*, 570 F.3d 606, 612 n.3 (5th Cir. 2009). Nor does the

court "sift through the record in search of evidence to support a party's opposition to summary judgment." *Jackson v. Cal-Western Packaging Corp.*, 602 F.3d 374, 379-80 (5th Cir. 2010); *Malacara v. Garber*, 353 F.3d 393, 405 (5th Cir. 2003); *Ragas*, 136 F.3d at 458; *Nissho-Iwai Am. Corp. v. Kline*, 845 F.2d 1300, 1307 (5th Cir.1988) (it is not necessary "that the entire record in the case ... be searched and found bereft of a genuine issue of material fact before summary judgment may be properly entered"). Therefore, "[w]hen evidence exists in the summary **[*7]** judgment record but the nonmovant fails even to refer to it in the response to the motion for summary judgment, that evidence is not properly before the district court." *Malacara*, 353 F.3d at 405.

III.

Plaintiff argues that Defendants are not able to compel arbitration because they are not customers of Plaintiff or Azad. (Instruments No. 3 at 10; No. 5 at 2). Defendants argue, first, that they satisfy the requirements of FINRA Rule 12200 to arbitrate a dispute with Plaintiff. (Instrument No. 13 at 1-2). Second, Defendants argue that Plaintiff should be compelled to arbitrate because Plaintiff filed an answer in the FINRA Arbitration and submitted an agreement in writing to arbitrate. (Instrument No. 13 at 2).

Under the Federal Arbitration Act, the issue of arbitrability should generally be resolved by the courts, "[u]nless the parties clearly and unmistakably provide otherwise." *AT&T Techs., Inc. v. Commc'ns Workers of Am.*, 475 U.S. 643, 649, 106 S. Ct. 1415, 89 L. Ed. 2d 648 (1986). "[A]rbitration is a matter of contract and a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit." *United Steelworkers of Am. v. Warrior & Gulf Nav. Co.*, 363 U.S. 574, 582, 80 S. Ct. 1347, 4 L. Ed. 2d 1409, (1960); *see Pershing, L.L.C. v. Bevis*, 606 F. App'x 754, 756 (5th Cir. 2015) (noting that a party cannot force a FINRA member to arbitrate without an agreement). To determine if a party can be compelled to arbitrate, courts must first ask if the party has agreed to arbitrate **[*8]** the dispute. *Janvey v. Alguire*, 847 F.3d 231, 240 (5th Cir. 2017). "While there is a strong federal policy favoring arbitration, the policy does not apply to the initial determination whether there is a valid agreement to arbitrate." *Banc One Acceptance Corp. v. Hill*, 367 F.3d 426, 429 (5th Cir. 2004). "[A]ny doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration." *John Hancock Life Ins. Co. v. Wilson*, 254 F.3d 48, 58 (2d Cir. 2001) (internal quotation marks and citations omitted).

In 2007, the National Association of Securities Dealers, Inc. ("NASD") and the regulatory arm of the New York Stock Exchange created FINRA. *See Morgan Keegan & Co. v. Garrett*, 495 F. App'x 443, 448 (5th Cir. 2012). FINRA is a self-regulatory organization registered under the Securities Exchange Act of 1934 and has the authority to create and enforce rules for its members. *See* Securities and Exchange Commission Release No. 34-56145, 72 Fed. Reg. 42169, 42170 (Aug. 1, 2007); *Wachovia Bank, Nat. Ass'n v. VCG Special Opportunities Master Fund, Ltd.*, 661 F.3d 164, 172 (2d Cir. 2011). NASD Rule 10301, the precedent to FINRA Rule 12200, was substantively identical to Rule 12200 and cases interpreting the former rule have been applicable to interpretations of the FINRA Rules. *See Kashner Davidson Secs. Corp. v. Mscisz*, 601 F.3d 19, 21 (1st Cir. 2010); *Gonchar v. S.E.C.*, 409 F. App'x 396, 398 n.1 (2d Cir. 2010). Here, the parties concede that cases interpreting the NASD Code are applicable to interpretations of FINRA Rules. *See* (Instruments No. 13 at 8-9; No. 14 at 10). Consequently, the Court will look at case law interpreting the NASD Code to analyze the application of FINRA Rule 12200 to this case.

Under FINRA Rule 12200, arbitration clauses are included in contracts between FINRA members and customers. **[*9]** *See Pershing, L.L.C. v. Bevis*, 606 F. App'x 754, 757 (5th Cir. 2015).

Rule 12200 states that parties must arbitrate a dispute if:

- Arbitration under the Code is either:
  - (1) Required by a written agreement, or
  - (2) Requested by the customer;
- The dispute is between a customer and a member or associated person of a member; and
- The dispute arises in connection with the business activities of the member or the associated person, except disputes involving the insurance business activities of a member that is also an insurance company.

FINRA Rule 12200.

Plaintiff argues that Defendants are unable to establish privity between an investor and a FINRA member through interactions with an associated person, citing to two district court cases for support. (Instrument No. 14 at 9-10). However, the plain language of FINRA Rule 12200 runs contrary to this conclusion. Rule 12200 makes clear that a FINRA member must arbitrate a

dispute that arises between a customer and associated person of a member. *See* FINRA Rule 12200. Courts have also held the same. *See Citigroup Global Markets Inc. v. Abbar.*, 761 F.3d 268, 274 (2d Cir. 2014); *California Fina Group, Inc. v. Herrin*, 379 F.3d 311 (5th Cir. 2004) (holding the same under the NASD Code); *Mony Sec. Corp. v. Bornstein*, 390 F.3d 1340, 1344 (11th Cir. 2004) (same); *Vestax Securities Corp. v. McWood*, 280 F.3d 1078, 1082 (6th Cir. 2002) (same). The parties do not dispute that Azad is an "associated person" under Rule 12200. (Instruments No. 13 at 7; No. 14 at 8). Therefore, Defendants can compel Plaintiff to arbitrate a dispute if (1) Defendants are "customers" **[*10]** of Azad and (2) the dispute arose in connection with the business activities of Azad. *See* FINRA Rule 12200; *California Fina Grp., Inc. v. Herrin*, 379 F.3d 311, 316 (5th Cir. 2004).

A.

Plaintiff argues that Defendants are not customers of Azad. (Instruments No. 3 at 10-11; No. 14 at 3, 11-12). Because of this, Plaintiff contends, Defendants may not properly compel arbitration under FINRA Rule 12200. (Instrument No. 3 at 10-11).

FINRA has not specifically defined the term "customer." In its definitions section, the FINRA Code of Arbitration Procedure for Customer Disputes only states that a "customer" is not a broker or a dealer. *See* FINRA Rule 12100(k). Courts have defined "customer" as "one, not a broker or dealer, who purchases commodities or services from a FINRA member in the course of the member's business activities insofar as those activities are covered by FINRA's regulation, namely the activities of investment banking and the securities business." *UBS Fin. Servs., Inc. v. Carilion Clinic*, 706 F.3d 319, 325 (4th Cir. 2013); *Pershing LLC v. Bevis*, 2014 U.S. Dist. LEXIS 62847, 2014 WL 1818098, at *2 (M.D. La. May 7, 2014) (quoting the same), *aff'd*, 606 F. App'x 754 (5th Cir. 2015).

While the Fifth Circuit has not defined "customer" under FINRA, the Court has interpreted "customer" under NASD Rule 10301. The Fifth Circuit held that "customer" under NASD Rule 10301 was "plainly broad enough to include persons who purchased securities from a registered representative of a [member] firm, a.k.a. an 'associated **[*11]** person,' and who are not themselves brokers or dealers." *Herrin*, 379 F.3d at 318. In *Herrin*, investors who purchased fraudulent investments from a brokerage firm's associated person were determined to be "customers" of the firm even though the firm never sold the investments at issue and the associated person was neither a broker nor dealer. *See Herrin*, 379 F.3d at 318. Plaintiff argues that *Herrin* is distinguishable from the current issue because Defendants did not purchase any investments from an associated person, but Plaintiff fails to provide any evidence of this assertion. (Instrument No. 14 at 10, 12). During the Court's motion hearing for a temporary restraining order, Plaintiff even conceded that Defendants purchased securities from Azad. (Instrument No. 11 at 15-17). Therefore, Plaintiff fails to demonstrate that *Herrin*'s holding is inapplicable to the present situation.

Plaintiff contends that the Court should apply the definition of "customer," under FINRA Notice 12-55. (Instrument No. 14 at 12). FINRA Notice 12-55 states that a

> customer includes a person who is not a broker or dealer who opens a brokerage account at a broker-dealer or purchases a security for which the broker-dealer receives or will receive, directly or indirectly, compensation **[*12]** even though the security is held at an issuer, the issuer's affiliate or custodial agent . . . or using another similar arrangement.

FINRA Regulatory Notice 12-55, https://www.finra.org/rules-guidance/notices/12-55 (last visited Oct. 26, 2020). Because Defendants do not allege that Azad received fees in exchange for Defendants' investments, Plaintiff argues that Defendants are not "customers." (Instrument No. 14 at 12).

However, FINRA Notice 12-55 is a guidance document that specifically advises on FINRA's Suitability Rule, not on FINRA's Code of Arbitration Procedure for Customer Disputes. *See* FINRA Regulatory Notice 12-55, https://www.finra.org/rules-guidance/notices/12-55 (last visited Oct. 26, 2020) (noting that FINRA Notice 12-55 provides guidance on FINRA Rule 2111). Furthermore, Plaintiff proffers no authority stating that FINRA's guidance documents bind courts as they interpret FINRA arbitration agreements. Thus, the Court declines to apply this understanding of "customer" to the present case.

The present situation falls more squarely within the scope of Rule 12200 than the circumstance in *Herrin*. Here, Azad was a registered broker with Plaintiff unlike the associated person in *Herrin* who was neither a broker nor dealer. *See* (Instrument No. 13 **[*13]** at 3); *Herrin*, 379 F.3d at 312-13. Plaintiff concedes that

Defendants worked with Azad and purchased securities in Corax through this relationship. (Instruments No. 11 at 15-17; No. 14 at 3). Because Defendants purchased securities from a registered representative of Plaintiff, they are "customers" under FINRA Rule 12200.

B.

Plaintiff argues that Defendants' investments were not in connection with the business activities of Plaintiff or Azad. (Instrument No. 14 at 11). Plaintiff contends that Defendants were only the legal clients of Azad, not brokerage clients. *Id.* Because of this, Plaintiff asserts that Defendants' investments were unrelated to Plaintiff or Azad's business activities. *Id.* Defendants argue that the dispute arises in direct connection with both Plaintiff and Azad's business activities. (Instrument No. 13 at 10).

Even if a dispute existed as to whether Azad was operating in his capacity as a lawyer or broker when engaging with Defendants, Plaintiff fails to show that this is a material fact issue. "A dispute that arises from a firm's lack of supervision over its brokers arises in connection with its business." *John Hancock*, 254 F.3d at 58-59; *see also Vestax Sec. Corp. v. McWood*, 280 F.3d 1078, 1082 (6th Cir. 2002) (quoting the same). This is so even if the associated person was not operating as a **[*14]** broker or dealer. *See Herrin*, 379 F.3d at 318 (holding that the second requirement was met when the associated person, who is neither a broker nor dealer, sold fraudulent investments to appellees). Regardless of whether the dispute arises from Plaintiff's business, Rule 12200 makes clear that the dispute arose from Azad's business activities. It is undisputed that Azad is an "associated person" of Plaintiff. (Instruments No. 13 at 7; No. 14 at 8). Defendants' dispute arose from Azad's advice to purchase securities in Corax, which is connected to Azad's business activities. (Instrument No. 11 at 15-17). Therefore, the second element is met here.

Because the dispute is connected with an associated person's business activities, Defendants can properly compel arbitration. Accordingly, Defendants' Motion for Summary Judgment is **GRANTED** and Plaintiff's Motion for Summary Judgment is **DENIED**.

IV.

For the foregoing reasons, **IT IS HEREBY ORDERED** that Defendants' Motion for Summary Judgment is **GRANTED, (Instrument No. 13)**, and Plaintiff's Motion for Summary Judgment is **DENIED, (Instrument No. 14)**.

The Clerk shall enter this Order and provide a copy to all parties.

SIGNED on this the 19th day of November, 2020, at Houston, Texas.

[*15] /s/ Vanessa D. Gilmore

VANESSA D. GILMORE

UNITED STATES DISTRICT JUDGE

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