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December 29, 2021

Via Email (Secretarys-Office@sec.gov)
Ms. Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Petition for Rulemaking to Abrogate or Amend Financial Industry Regulatory Authority Rules 2268(d), 12200, and 12204(d)

Dear Ms. Countryman:

Pursuant to 15 U.S.C. § 78s(c) and Rule 192(a) of the Securities Exchange Commission Rules of Practice, Thrivent Financial for Lutherans and its subsidiary, Thrivent Investment Management Inc., through undersigned counsel, hereby submit the enclosed Petition for Rulemaking ("Petition"), respectfully requesting that the Commission abrogate or amend Financial Industry Regulatory Authority, Inc. ("FINRA") Rules 2268(d), 12200, and 12204(d). These FINRA Rules improperly prohibit customer arbitration agreements requiring individual arbitration of disputes arising between FINRA-member broker-dealers and their customers in a non-FINRA arbitration forum, notwithstanding that such agreements are valid and enforceable under federal law. For the reasons set forth in the Petition, these FINRA Rules are unlawful and invalid, and must be abrogated or amended by the Securities Exchange Commission to comply with federal law.

Thank you for your consideration of this matter.

Sincerely yours,

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Enclosure:
Thrivent Financial for Lutherans' and Thrivent Investment Management Inc.'s Petition for Rulemaking to Abrogate or Amend Financial Industry Regulatory Authority Rules 2268(d), 12200, and 12204(d), and Exhibits thereto.

Petition for Rulemaking to Abrogate or Amend Financial Industry Regulatory Authority Rules 2268(d), 12200, and 12204(d)

Respectfully Submitted by Thrivent Financial for Lutherans and Thrivent Investment Management Inc.
Date: December 29, 2021

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I. INTRODUCTION

1. Thrivent Financial for Lutherans ("Thrivent") and Thrivent Investment Management Inc. ("TIMI," and together with Thrivent, "Petitioners") respectfully submit this petition for rulemaking ("Petition") to the Securities and Exchange Commission ("Commission" or "SEC"), pursuant to 15 U.S.C. § 78s(c) and Rule 192(a) of the SEC Rules of Practice,[1] to request that the Commission abrogate or amend Financial Industry Regulatory Authority ("FINRA") Rules 2268(d), 12200, and 12204(d)[2] (the "Challenged FINRA Rules"), which prohibit FINRA members from: (1) marketing or selling securities products, the disputes related to which are governed by customer arbitration agreements that require individual arbitration in a non-FINRA forum, and/or (2) enforcing customer arbitration agreements that require individual arbitration in a non-FINRA forum.

2. Thrivent and its FINRA-member subsidiary TIMI have an interest in the subject of this Petition because Thrivent's Bylaws establish a Member Dispute Resolution Program ("MDRP") for disputes between Thrivent's customers, all of whom are members of Thrivent ("Members") on the one hand, and Thrivent (or those operating for Thrivent in an agency capacity, including TIMI) on the other. The MDRP requires individual arbitration under terms set forth in Thrivent's Bylaws, rather than those established by the Challenged FINRA Rules. However, for

[1] 15 U.S.C. § 78s(c) provides that "[t]he Commission, by rule, may abrogate, add to, and delete from . . . the rules of a self-regulatory organization (other than a registered clearing agency) as the Commission deems necessary or appropriate to insure the fair administration of the self-regulatory organization, to conform its rules to requirements of this chapter and the rules and regulations thereunder applicable to such organization, or otherwise in furtherance of the purpose of this chapter . . . ."

Rule 192(a) of the SEC Rules of Practice allows "[a]ny person desiring the issuance, amendment or repeal of a rule of general application" to petition the Commission. This provision is the vehicle by which persons may address with the Commission any concerns with its rules, or those of any self-regulatory organization (defined in paragraph 12 below), including FINRA, that the Commission has approved.

[2] The current text of FINRA Rules 2268(d), 12200, and 12204(d) is set forth below in Section IV.A. (paragraphs 29-43 below).

Thrivent variable annuities and variable life insurance products (collectively, "Variable Products") that incorporate and require application of the MDRP Bylaw, the Challenged FINRA Rules addressed in this Petition: (1) preclude TIMI from selling such Variable Products; (2) preclude the Variable Products from being sold by FINRA members, and therefore from being sold at all; and (3) prohibit enforcement of the otherwise valid MDRP to disputes with Thrivent Members, notwithstanding those Members' agreement to resolve their disputes through the MDRP in a non-FINRA forum.

3. FINRA asserts that its Rules carry the force of federal law, a proposition that FINRA has successfully argued in federal courts and administrative proceedings. FINRA Rules, accordingly, must be consistent with federal law. Further, broker-dealers selling retail securities products are required to be members of FINRA and abide by FINRA Rules. The Commission exercises substantial oversight over FINRA in accordance with federal securities laws and must review and approve FINRA Rules.

4. The Challenged FINRA Rules prohibit customer arbitration agreements, containing provisions similar to the MDRP, that require individual arbitration in a non-FINRA forum for disputes arising between FINRA-member broker-dealers and their customers. Further, FINRA Rule 2268(d) prohibits FINRA members from selling securities products where customer arbitration agreements that require individual arbitration in a non-FINRA forum govern the disputes with respect to such securities products. As discussed below in paragraphs 36 and 59, FINRA Rule 2268 also imposes additional requirements that exceed both the SEC and FINRA's authority under federal law with respect to customer arbitration agreements like the MDRP.

5. The Federal Arbitration Act, 9 U.S.C. § 1 *et seq.* ("FAA"), overrides the Challenged FINRA Rules, thus establishing the validity and *requiring* enforcement of arbitration agreements

like the MDRP. Specifically, the FAA requires that "[a] written provision" in "a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract," such as the MDRP, "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. Interpreting this provision, the United States Supreme Court has explained that the only circumstances under which agreements to arbitrate can be limited or prohibited are when Congress, through other legislation, has commanded as much with respect to agreements falling within the substantive scope of that specific federal legislation. Such a "congressional command" to limit the enforceability of agreements to arbitrate must be "deducible from [the statute's] text or legislative history," *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985), and any such "congressional command" overriding the FAA and limiting the enforceability of agreements to arbitrate specific types of disputes must be "clear and manifest." *Epic Systems Corp. v. Lewis*, 584 U.S. __, 138 S. Ct. 1612, 1617 (2018). Here, the federal securities laws did not provide the Commission or FINRA with such "clear and manifest" authority to promulgate or enforce the Challenged FINRA Rules, which impede or supersede FINRA members and their customers' agreements to arbitrate claims individually and/or outside the FINRA arbitration forum, and which preclude FINRA members and their customers from entering into such agreements.[3]

6. The FAA reflects a congressional determination that private arbitration agreements are a favored means of dispute resolution. Indeed, as the United States Supreme Court has repeatedly held, the FAA "is a congressional declaration of a liberal federal policy favoring

[3] As discussed further in paragraphs 49-50, below, under 15 U.S.C. § 78o(o), the Commission has authority to prohibit or otherwise impose conditions or limits on some arbitration agreements, but the Commission only can do so "by rule"—meaning by following rulemaking procedural requirements under the Administrative Procedure Act ("APA"), 5 U.S.C. § 551 *et seq.*—and the Commission has undertaken no such rulemaking.

arbitration agreements" like the MDRP. *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983); *see also AT&T Mobility LLC v. Concepcion*, 563 U.S. 333, 339 (2011) ("We have described [the FAA] as reflecting both a liberal federal policy favoring arbitration . . . and the fundamental principle that arbitration is a matter of contract." (internal citations and quotations omitted)); *Epic Systems*, 138 S. Ct. at 1621 ("The [FAA] . . . establishes 'a liberal federal policy favoring arbitration agreements'" and reflects "'the unmistakable clear congressional purpose that the arbitration procedure, when selected by the parties to a contract, be speedy and not subject to delay and obstruction in the courts.'" (quoting *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 (1967)).

7. As discussed in detail below in Section IV.B., the Supreme Court has made clear that the federal securities laws do not reflect congressional intent to empower FINRA, pursuant to Rules approved by the Commission, to preclude or limit parties' agreements to arbitrate. *See, e.g.*, *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987) (holding that the Securities Exchange Act of 1934, 15 U.S.C. § 78a *et seq.* ("Exchange Act"), includes no provisions that reflect congressional intent to override the FAA and limit the enforceability of parties' agreements to arbitrate Exchange Act claims). Therefore, the Challenged FINRA Rules are invalid insofar as they prevent FINRA members from entering into or enforcing arbitration agreements requiring individual arbitration in a non-FINRA forum or from marketing or selling securities products to which such arbitration agreements would apply.

8. For the foregoing reasons, which are discussed below in greater detail, the Challenged FINRA Rules are unlawful and therefore invalid. The Commission must exercise its authority under 15 U.S.C. § 78s(c) either to abrogate or amend these Rules so that they do not

exceed the statutory authority of the Commission and FINRA or otherwise conflict with the constraints imposed by the FAA.

II. BACKGROUND REGARDING THE PETITIONERS

A. Thrivent and the MDRP

9. Thrivent is a fraternal benefit society, which is a special type of non-profit organization that provides insurance and other benefits to its Members. As a fraternal benefit society, Thrivent is owned and governed by its Members who are united by a common bond. The common bond for Thrivent Members is Christianity. Thrivent sells insurance products, including variable annuities and variable life insurance products, only to persons who already are Thrivent Members or who become Members at the time they purchase a Variable Product. Thrivent Variable Products are securities registered with the Commission under the Securities Act of 1933, 15 U.S.C. § 77a *et seq.* ("Securities Act").

10. Thrivent's Articles of Incorporation and Bylaws, included herewith as Exhibit 1, govern its structure and relationship with its Members. The Articles of Incorporation and Bylaws establish the framework for all of Thrivent's programs, operations, and policies. All Thrivent Members agree to be bound by Thrivent's Articles of Incorporation and Bylaws, which are incorporated into each Thrivent insurance contract as mandated by state law.[4] As a member-governed organization, uniform application of the Bylaws is a core component of Thrivent's governance structure. The MDRP is set forth in Thrivent's Bylaws, and establishes the process for addressing disputes between Thrivent and its Members. Consistent with legal principles of agency,

[4] Wis. Stat. § 632.93. As a fraternal benefit society organized and operating pursuant to the Wisconsin Fraternal Code, Chapter 614 of the Wisconsin Statutes, Thrivent provides insurance for its members in accordance with the Wisconsin Fraternal Code and other applicable provisions of Wisconsin's insurance laws. Every state has adopted a fraternal code, and the states' fraternal codes are substantively very similar to one another because almost every state based its fraternal code on the same Model Fraternal Code.

the MDRP expressly extends its scope to include those acting on Thrivent's behalf in an employment or agency capacity, including TIMI and other broker-dealers (along with their registered representatives) who sell Thrivent's Variable Products.[5] The MDRP is a multi-step process to resolve disputes culminating in mandatory individual arbitration in a non-FINRA forum where necessary.

B. TIMI

11. TIMI is registered with the SEC as a broker-dealer under the Exchange Act and is a member of FINRA. TIMI is a wholly owned subsidiary of Thrivent. On Thrivent's behalf, TIMI, through its registered representatives, sells Thrivent's insurance products (including Thrivent Variable Products) only to Thrivent Members and individuals who become Thrivent Members upon the purchase of a Thrivent insurance product. Other broker-dealers, pursuant to selling agreements with Thrivent and TIMI (which is the principal underwriter for Thrivent Variable Products), also operate on Thrivent's behalf by selling Thrivent Variable Products to Thrivent Members; however, TIMI is responsible for nearly all sales of Thrivent Variable Products. TIMI and others acting on Thrivent's behalf to sell Variable Products are licensed insurance producers appointed by Thrivent, and accordingly they are agents of Thrivent within the ambit of the MDRP.

III. FINRA STRUCTURE AND COMMISSION OVERSIGHT RESPONSIBILITY

12. FINRA is a national securities association, a type of self-regulatory organization ("SRO") established by congressional authority pursuant to the requirements set forth in the

[5] Ex. 1 at 3-4 (Section 11 of Thrivent's Bylaws sets forth the MDRP, which applies to disputes arising between Thrivent Members or beneficiaries and Thrivent "or its directors, officers, agents, and employees.").

Exchange Act.[6] Specifically, 15 U.S.C. § 78o-3 sets forth the requirements for establishing national securities associations, which are subject to the Commission's oversight and operate under its authority. FINRA is the only existing national securities association registered under Section 78o-3. Under the Exchange Act, the Commission has substantial oversight obligations with respect to FINRA to ensure that FINRA's operations, and the rules FINRA promulgates, are consistent with federal law.

A. The Commission Must Review, Approve, and Amend FINRA Rules to Ensure Compliance with Federal Law

13. As an SRO, FINRA may promulgate rules applicable to its members, subject to Commission review, approval, and amendment in accordance with the provisions set forth in 15 U.S.C. § 78s. Specifically, FINRA is required to file any proposed rules or proposed rule changes with the Commission. 15 U.S.C. § 78s(b). The Commission then must perform its own review of the proposed FINRA Rules, publish notice of the proposed FINRA Rules or changes thereto, and conduct hearings if necessary and appropriate before approving FINRA Rules. *Id.* In reviewing and approving FINRA Rules, the Commission is responsible for ensuring that FINRA Rules comply with federal law, including an express mandate to ensure compliance with the federal securities laws. 15 U.S.C. § 78s(g).

14. The Commission may only approve FINRA Rules that comply with "the requirements of [the Exchange Act] and the rules and regulations issued" thereunder. 15 U.S.C. § 78s(b)(2)(C)(i). Thus, where FINRA Rules exceed the authority of the SEC or FINRA under federal law, or otherwise are unlawful, it is necessary and appropriate for the Commission, and the

[6] Under 15 U.S.C. § 78c(26), the term "self-regulatory organization" means "any national securities exchange, registered securities association, or registered clearing agency, or (solely for purposes of sections 78s(b), 78s(c), and 78w(b) of this title) the Municipal Securities Rulemaking Board established by section 78o–4 of this title."

Commission is obliged, to correct such unlawful rules. To satisfy this oversight obligation, the Commission has authority to "abrogate, add to, and delete from" FINRA Rules. 15 U.S.C. § 78s(c).

B. FINRA Rules Have the Force of Federal Law

1. FINRA Has Asserted, And Courts Have Agreed, That FINRA Rules Have the Force of Law

15. FINRA asserts that its Rules have the force of federal law, and federal courts have agreed. For example, in published regulatory guidance, FINRA asserts that its Rules "are approved by the [SEC], binding on FINRA member firms and associated persons, and have the force of federal law." FINRA Regulatory Notice 16-25 at *3.[7] Likewise, in enforcement proceedings FINRA has asserted this position. *See, e.g.*, *In the Matter of Dep't of Enforcement v. Charles Schwab & Co.*, 2014 WL 1665738, at *16-18 (FINRA Bd. Apr. 24, 2014) ("FINRA rules have the force and effect of a federal regulation for the purposes of resolving federal conflicts of law").

16. Several federal courts have agreed that FINRA Rules have the force of federal law because rules of SROs, including FINRA, are established in accordance with provisions of the Exchange Act and applied under delegated federal authority. *See, e.g.*, *McDaniel v. Wells Fargo Invs., LLC*, No. 10-4916, 2011 WL 2976784, at *2-3 (N.D. Cal. July 22, 2011) (Exchange Act created a system of self-regulation in which SROs are the primary regulators of securities broker-dealers and use delegated government power to promulgate Rules and enforce compliance); *Bloemendaal v. Morgan Stanley Smith Barney LLC*, No. 10-1455, 2011 WL 2161352, at *4 (C.D. Cal. May 23, 2011) (SROs have been delegated government power to enforce compliance with both the Exchange Act and ethical standards going beyond those requirements); *Empire Fin. Grp. v. FINRA*, No. 08-80534, 2009 WL 10644856, at *2 (S.D. Fla. Jan. 15, 2009) ("Once approved by

[7] FINRA Regulatory Notice 16-25, *Forum Selection Provisions, Involving Customers, Associated Persons and Member Firms*, 2016 WL 4060371 (July 22, 2016).

the SEC, FINRA rules have the status of federal law."). In the arbitration context, federal courts also have held that FINRA Rules have the force of law in preempting conflicting state law. *See, e.g.*, *Credit Suisse First Boston Corp. v. Grunwald*, 400 F.3d 1119, 1128-32 (9th Cir. 2005).[8]

2. Judicial and Regulatory Estoppel Preclude FINRA from Asserting that Compliance with FINRA Rules is Voluntary

17. Under the well-established doctrine of judicial estoppel, "'[w]here a party assumes a certain position in a legal proceeding, and succeeds in maintaining that position, he may not thereafter, simply because his interests have changed, assume a contrary position.'" *New Hampshire v. Maine*, 532 U.S. 742, 749 (2001) (quoting *Davis v. Wakelee,* 156 U.S. 680, 689 (1895)). The doctrine of judicial estoppel likewise applies to bind parties to positions taken in regulatory proceedings. *See, e.g.*, *Chaveriat v. Williams Pipe Line Co.*, 11 F.3d 1420, 1427 (7th Cir. 1993) ("Though called judicial estoppel, the doctrine has been applied, rightly in our view, to proceedings in which a party to an administrative proceeding obtains a favorable order that he seeks to repudiate in a subsequent judicial proceeding.").

18. The "'doctrine of judicial estoppel prevents a party from asserting a claim in a legal proceeding that is inconsistent with a claim taken by that party in a previous proceeding.'" *Maine*, 532 U.S. at 749 (quoting 18 Moore's Federal Practice § 134.30, p. 134–62 (3d ed. 2000)). The basis for the doctrine is that "'judicial acceptance of an inconsistent position in a later proceeding

[8] A few federal courts considering this issue in different contexts have rejected the notion that FINRA Rules—and rules of FINRA's predecessor, the National Association of Securities Dealers ("NASD")—carry the force of federal law. *See, e.g.*, *Ford v. Hamilton Invs., Inc.*, 29 F.3d 255, 259 (6th Cir.1994) (holding that NASD rules did not constitute federal securities laws or "rules and regulations adopted thereunder" to allow for jurisdiction over the claims presented.); *Kenosha Unified Sch. Dist. v. Stifel Nicolaus & Co.*, 607 F. Supp. 2d 967, 977-78 (E.D. Wis. 2009) (finding that FINRA rules are not "rules" or "regulations" for purposes of Section 27 of the Exchange Act, and stating "[a]lthough the Exchange Act expressly requires that a self-regulatory organization comply with its own rules and that dealers comply with the Exchange Act, *it does not expressly require NASD members to comply with NASD rules nor does it recognize a right of action against a dealer for NASD violations.*" (emphasis in original and citation omitted)); *Schouten v. Jakubiak* (*In re Jakubiak*), 591 B.R. 364, 376-77 (Bankr. E.D. Wis. 2018) (Rejecting the argument that FINRA rules are securities laws, or that "SEC oversight transforms all of FINRA's rules into regulations under the federal securities laws.").

. . . create[s] the perception that either the first or the second court was misled, thus posing a threat to judicial integrity." *Moses v. Howard Univ. Hosp.*, 606 F.3d 789, 792 (D.C. Cir. 2010) (internal citation omitted).

19. FINRA successfully has taken the position in federal court that its Rules have the force of federal law. For example, in FINRA's May 21, 2008 motion to dismiss filed with the United States District Court for the Southern District of Florida, FINRA asserted that "[o]nce approved by the SEC, FINRA Rules enjoy the status of federal law." Mot. to Dismiss, *Empire Fin. Grp. v. FINRA*, No. 08-cv-80534 (S.D. Fla. May 21, 2008), ECF No. 2. In granting FINRA's motion to dismiss, the court adopted FINRA's argument almost verbatim. *Empire Fin. Grp. v. FINRA*, 2009 WL 10644856, at *2 ("Once approved by the SEC, FINRA rules have the status of federal law."). The doctrine of judicial estoppel therefore precludes FINRA from asserting that its Rules do not carry the force of law or are otherwise not mandatory.

20. Numerous courts also have held that judicial estoppel applies to positions taken in administrative proceedings.[9] Because FINRA successfully has taken the position in administrative proceedings that its rules carry the force of federal law, FINRA is bound to this position. For example, in administrative proceedings against Charles Schwab & Company, Inc. ("Schwab"), discussed further below in paras. 37–40, the FINRA Board asserted, "FINRA rules have the force

[9] *See, e.g.*, *Chaveriat*, 11 F.3d at 1427; *Smith v. Pinner*, 891 F.2d 784, 787 n.4 (10th Cir.1989) (per curiam) ("We do not consider the initial administrative context of plaintiff's stipulation an impediment to invocation of this rule of judicial estoppel, since it is well-established in Colorado that the closely related principles of collateral estoppel and res judicata also apply to administrative decisions, so long as the tribunal in question possesses subject matter jurisdiction."); *Czajkowski v. City of Chicago*, 810 F. Supp. 1428, 1435–36 (N.D. Ill. 1992) (applying judicial estoppel doctrine to "quasi-judicial administrative proceedings based on such an application being consistent with the purposes of promoting truth and preventing parties from deliberately shifting positions to suit the exigencies of the moment") (internal quotation and citation omitted.); *Scott v. Land Span Motor, Inc.*, 781 F. Supp. 1115, 1119 (D.S.C. 1991) (holding that the judicial estoppel doctrine "is applicable regardless of whether the prior position was taken in a judicial or a quasi-judicial proceeding."); *Zapata Gulf Marine Corp. v. Puerto Rico Maritime Shipping Auth.*, 731 F. Supp. 747, 750 (E.D. La. 1990) (holding that the judicial estoppel doctrine "applies equally to positions taken in quasi-judicial administrative proceedings as it does in courts of law.").

and effect of a federal regulation" in support of its authority to take enforcement action against Schwab for its violation of FINRA rules. *In the Matter of Dep't of Enforcement v. Charles Schwab & Co.*, 2014 WL 1665738, at * 16 (FINRA Bd. Apr. 24, 2014). Notably, the substantive FINRA rules at issue in that proceeding are the same rules as the Challenged FINRA Rules that are the subject of this Petition.

21. The doctrine of judicial estoppel, including its application to regulatory proceedings, therefore precludes FINRA from asserting in connection with this Petition that its Rules do not have the force of federal law, and that compliance with its Rules is merely a voluntary undertaking by FINRA members. Indeed, if compliance with FINRA's Rules were voluntary, Thrivent and TIMI would be able to administer and enforce the MDRP for Member disputes without FINRA's objection.

C. Broker-Dealers Selling Variable Products Are *Required* to Join FINRA and Comply with FINRA Rules

22. For an additional reason, FINRA's Rules establish binding legal requirements for broker-dealers: Under federal law, broker-dealers have no choice other than to become FINRA members and subject themselves to FINRA Rules. According to the Exchange Act:

> It shall be unlawful for any registered broker or dealer to effect any transaction in, or induce or attempt to induce the purchase or sale of, any security (other than or commercial paper, bankers' acceptances, or commercial bills), unless such broker or dealer is a member of a securities association registered pursuant to section 78o–3 of this title or effects transactions in securities solely on a national securities exchange of which it is a member.

15 U.S.C. § 78o(b)(8).

23. Broker-dealers who sell securities products outside of a national securities exchange like the New York Stock Exchange are legally obligated to become "a member of a securities association registered pursuant to section 78o–3." And FINRA is the *only* national

securities association registered under 78o-3.[10] As the Seventh Circuit explained in *Aslin v. FINRA*, 704 F.3d 475, 476 (7th Cir. 2013):

> Firms that deal in securities must comply with FINRA rules because federal law requires them to do so. Federal securities law requires most securities firms to register with a national securities association and to follow the association's rules. 15 U.S.C. § 78o(b)(11). FINRA is currently the only national securities association, so all such brokerage firms must register with FINRA. In addition to firms, FINRA regulates individual securities brokers by requiring them to register and abide by FINRA's rules. FINRA Rule 1031. Employees required to register with FINRA must pass an examination and are referred to as "registered persons" in FINRA's rules.

Thus, by operation of law, broker-dealers like TIMI are required to become FINRA members and comply with FINRA Rules.

D. The Exchange Act Limits the Scope of the Commission's and FINRA's Regulatory Authority

24. Both the Commission and FINRA operate under authority conferred by the Exchange Act. Further, FINRA operates under the Commission's authority and is subject to the Commission's oversight, including with respect to ensuring that FINRA Rules comply with federal law and approving, amending, or rescinding FINRA Rules as appropriate and required by law. 15 U.S.C. § 78s. FINRA's exercise of regulatory authority derives from, and at most is coterminous with, the Commission's regulatory authority.[11]

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[10] Section 78o-3 also provides for the registration of "affiliated securities association[s]" but these associations must operate as affiliates of, and in accordance with the terms of, a national securities association. 15 U.S. C. § 78o-3(c), (d).

[11] The Exchange Act draws a distinction between: (1) FINRA regulatory rules for which FINRA's authority derives from the Commission's regulatory authority; and (2) more ministerial rules (*e.g.*, FINRA Rules addressing fees or other administrative matters). For changes to FINRA Rules by which FINRA regulates its members, the Exchange Act requires specifically delineated Commission oversight and an approval process that includes a public notice and comment period before the new Rule becomes effective. 15 U.S.C. §§ 77s(b)(1)-77s(b)(2). By contrast, changes to FINRA Rules addressing FINRA administrative matters and functions "take effect upon filing with" the Commission and do not require public notice and comment or SEC approval to become effective. 15 U.S.C. § 77s(b)(3). FINRA Rules precluding arbitration agreements containing provisions like the MDRP are plainly not ministerial, and therefore the authority for such Rules derives from the Commission's regulatory authority and is subject to Commission approval and oversight.

25. The Commission cannot, by its approval of FINRA Rules or otherwise, confer authority upon FINRA to take regulatory action that exceeds the scope of the Commission's own authority under the Exchange Act. Otherwise, the Commission could shirk legal constraints on its own regulatory authority by allowing or even requiring FINRA to impose Rules that the Commission could not impose on its own.

26. Further, because FINRA Rules carry the force of federal law and bind entities that are legally compelled to become FINRA members, FINRA Rules must themselves comply with and be consistent with federal law. Otherwise, FINRA could impose legal requirements that mandate extralegal activity. *See, e.g.*, *Ragsdale v. Wolverine World Wide, Inc.*, 535 U.S. 81, 91 (2002) (invalidating a challenged regulation that "worked an end run around important limitations" in Congress's statutory scheme, and holding that "'[r]egardless of how serious the problem an administrative agency seeks to address . . . it may not exercise its authority in a manner that is inconsistent with the administrative structure that Congress enacted into law.'") (quoting *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 125 (2000)); *New York Stock Exchange LLC v. Securities & Exchange Comm'n*, 962 F.3d 541, (D.C. Cir. 2020) (vacating a rule the Commission argued was "reasonably related to the purposes of the [SEC's] enabling legislation" because "[n]othing in the Commission's rulemaking authority authorize[d] it to promulgate" the challenged rule); *Aid Ass'n for Lutherans v. U.S. Postal Serv.*, 321 F.3d 1166, 1174 (D.C. Cir. 2003) ("An agency construction of a statute cannot survive judicial review if a contested regulation reflects an action that exceeds the agency's authority.").

E. This Petition Respectfully Requests that the Commission Redress SEC/FINRA Regulatory Overreach

27. The Challenged FINRA Rules exceed the Commission's and FINRA's authority under the Exchange Act. The Commission did not approve the Challenged FINRA Rules based

on language in the federal securities laws (or anywhere else) by which Congress expressed its intent to allow the SEC or FINRA to restrain the formation or enforcement of private arbitration agreements requiring individual arbitration. Therefore, the FAA overrides and invalidates these Rules, *see, e.g.*, *McMahon*, 482 U.S. at 226, and the Commission has an affirmative obligation to abrogate or amend them.

IV. FINRA RULES PRECLUDING PRIVATE PREDISPUTE CUSTOMER ARBITRATION AGREEMENTS ARE INVALID AND THE SEC MUST ABROGATE OR AMEND THESE RULES

28. As discussed below in paragraphs 29–43, the Challenged FINRA Rules preclude customer arbitration agreements, containing provisions like the MDRP, that mandate individual arbitration in a non-FINRA arbitration forum (and do not permit filing disputes in court), and further preclude broker-dealers and their registered representatives from selling securities products if customer arbitration agreements requiring individual arbitration in a non-FINRA forum apply. However, neither the Exchange Act nor any other federal securities law expressly provides FINRA with authority to impose such constraints on private customer arbitration agreements. The Rules are therefore invalid because they limit parties' ability to agree to arbitrate, in violation of the FAA, and the Commission must either abrogate or amend these FINRA Rules to comply with federal law. *Cf. Epic Systems*, 138 S. Ct. at 1624 (holding that the terms of an arbitration agreement were enforceable because the National Labor Relations Act ("NLRA") did not provide the National Labor Relations Board ("NLRB") with statutory authority to override the FAA).

A. The Challenged FINRA Rules Prohibit Enforcement of Private Arbitration Agreements Mandating Individual Customer Arbitration in a Non-FINRA Forum and the Sale of Securities Products that Include Such Agreements

29. FINRA Rule 12200 states, in full:

> Parties must arbitrate a dispute under the Code 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.[12]

30. Rule 12200 requires FINRA members to submit disputes to FINRA arbitration if "[r]equested by the customer," even if the customers have otherwise agreed to arbitrate or resolve disputes outside of FINRA arbitration. Indeed, as discussed further below in paragraphs 39 and 42, FINRA staff interprets Rule 12200 as requiring FINRA members to offer customers the option of arbitration under the FINRA customer code even if the customers previously agreed to arbitrate outside of FINRA arbitration.

31. FINRA Rule 12204(d) states, in full:

> A member or associated person may not enforce any arbitration agreement against a member of a certified or putative class action with respect to any claim that is the subject of the certified or putative class action until:
> - The class certification is denied;
> - The class is decertified;
> - The member of the certified or putative class is excluded from the class by the court; or

[12] The exception in Rule 12200 for "insurance business activities of a member that is also an insurance company" does not preclude application of FINRA Rules to disputes between TIMI (or others selling Variable Products on Thrivent's behalf) and Thrivent Members. Courts interpreting similar language under the code of FINRA's predecessor, the NASD, narrowly interpreted this exception to cover only "intrinsically insurance" claims. *In re Prudential Ins. Co. of Am. Sales Practice Litig.*, 133 F.3d 225, 234 (3d Cir. 1998); *see also IDS Life Ins. Co. v. Royal Alliance Assocs.*, 266 F.3d 645, 652 (7th Cir. 2001) (noting that "[t]he purposes of the exclusion are to keep arbitrators away from issues that are peculiar to insurance, such as reserves, reinsurance, actuarial calculations, rates, coverage, and mandatory terms, and to prevent [NASD] arbitrators from being swamped with insurance claims, which are apt to be more numerous than securities claims.").

> • The member of the certified or putative class elects not to participate in the class or withdraws from the class according to conditions set by the court, if any.
>
> This paragraph does not otherwise affect the enforceability of any rights under this Code or any other agreement.

32. Rule 12204(d) prohibits FINRA members from enforcing arbitration agreements that would require customers to resolve disputes individually in arbitration, rather than through pursuing a putative judicial class action with respect to claims against a FINRA member.

33. FINRA Rule 2268(d) states, in full:

> No predispute arbitration agreement shall include any condition that:
> (1) limits or contradicts the rules of any self-regulatory organization;
> (2) limits the ability of a party to file any claim in arbitration;
> (3) limits the ability of a party to file any claim in court permitted to be filed in court under the rules of the forums in which a claim may be filed under the agreement;
> (4) limits the ability of arbitrators to make any award.

34. By precluding predispute arbitration agreements that "limit[] the ability of a party to file any claim in court . . . under the rules of the forums in which a claim may be filed under the agreement," Rule 2268(d)(3) prohibits (1) enforcement of arbitration agreements that mandate individual arbitration in a non-FINRA forum (and otherwise do not permit bringing individual claims or class actions in court); and (2) the sale of securities products by FINRA members if arbitration agreements that mandate individual arbitration in a non-FINRA forum apply to disputes arising with respect to these securities products.

35. Further, the Rule 2268(d)(1) prohibition on any predispute arbitration agreement that "limits or contradicts the rules of any self-regulatory organization," reinforces the Rule 12200 prohibition against arbitration agreements that require arbitration outside of the FINRA arbitration forum, because such agreements would "limit or contradict" the Rule 12200 requirement entitling customers to FINRA arbitration upon request. FINRA Rule 2268(d)(1).

36. FINRA Rule 2268 also imposes special notice requirements with respect to predispute arbitration clauses included in FINRA members' customer agreements, including:

a. A requirement that "[a]ny predispute arbitration clause shall be highlighted." FINRA Rule 2268(a);

b. A requirement that any predispute arbitration clause "shall be immediately preceded" by specified language imposing specific procedural requirements for the arbitration process. FINRA Rules 2268(a)(1)-(a)(7); and

c. A requirement that "[i]n any agreement containing a predispute arbitration agreement, there shall be a highlighted statement immediately preceding any signature line or other place for indicating agreement that states that the agreement contains a predispute arbitration clause" and "indicate[s] at what page and paragraph the arbitration clause is located." FINRA Rule 2268(b)(1).

37. FINRA has taken enforcement action to affirm that its Rules prohibit enforcement of private arbitration agreements that mandate individual arbitration outside the FINRA forum. For example, FINRA undertook enforcement proceedings against Schwab, after Schwab included a class action waiver provision in its customer contract. *In the Matter of Dep't of Enforcement*, 2014 WL 1665738.

38. FINRA's Board of Governors concluded in *Schwab* that the class action waiver provision violated FINRA Rules, which were "approved by the SEC" and which require "that customer class actions will be litigated in court, while FINRA arbitration will be available for customers to make individual claims against FINRA firms." *Id.*, 2014 WL 1665738, at * 2. Specifically, the FINRA Board "determine[d] that Rule 12204 . . . was intended to preserve investor access to the courts to bring or participate in judicial class actions, and that through its

[class action waiver], Schwab violated FINRA Rules 2268(d)(1) and (d)(3), and Rule 12204." *Id.* at *11. The FINRA Board asserted, "FINRA rules have the force and effect of a federal regulation" in support of its authority to take enforcement action against Schwab for its violation of these Rules. *Id.* at *16.

39. FINRA also has published regulatory guidance asserting that its Rules prohibit enforcement of private arbitration agreements that mandate individual arbitration outside the FINRA forum. For example, in FINRA Regulatory Notice 16-25, FINRA rejected a series of federal court decisions that hold that predispute forum selection clauses in agreements between member firms and their customers and employees could require those customers and employees to give up their rights to FINRA arbitration. FINRA Regulatory Notice 16-25, 2016 WL 4060371, at *2-3 (July 22, 2016).[13] FINRA asserts that FINRA Rule 12200 "preserves a customer's ability to resolve disputes through FINRA arbitration, regardless of whether arbitration is required by a written agreement." *Id.* at *2. FINRA also asserts that Rule 2268(d) "prohibits any predispute arbitration agreement from including any condition that . . . limits or contradicts the rules of any self-regulatory organization," including Rule 12200, which requires that customers have the option to pursue arbitration in the FINRA arbitration forum. *Id.* at *2. In support of its authority to enforce these Rules, FINRA states that its Rules "are approved by the Securities and Exchange Commission (SEC), binding on FINRA member firms and associated persons, and have the force of federal law." *Id.* at *3.

[13] In FINRA Regulatory Notice 16-25, *supra* note 7, FINRA states that it "is aware of federal appellate court decisions that have held that forum selection clauses in agreements between member firms and customers supersede the requirements of FINRA Rule 12200, permitting member firms to require customers to arbitrate in a private arbitration forum or to litigate in state or federal court" but asserts that "the reasoning giving rise to these decisions is mixed and conflicts with FINRA's views regarding the application of its arbitration rules." *Id.* at *2. The federal appellate court decisions FINRA identifies are: *Goldman, Sachs & Co. v. Golden Empire Schs. Fin. Auth.*, 764 F.3d 210 (2d Cir. 2014); *Goldman, Sachs & Co. v. City of Reno*, 747 F.3d 733 (9th Cir. 2014); and *Applied Energetics, Inc. v. NewOak Capital Markets, LLC*, 645 F.3d 522 (2d Cir. 2011). Reg. Not. 16-25 at *2, n.7.

40. FINRA also recently issued Regulatory Notice 21-16 (April 21, 2021), included herewith as Exhibit 2, which reaffirms FINRA's position that agreements requiring individual resolution of disputes, and thus precluding resolution through a class action, are prohibited. Specifically, FINRA states "FINRA rules prohibit member firms from incorporating provisions that would prevent customers from bringing or participating in judicial class actions by adding waiver language into customer agreements (class action waivers) and prohibit member firms from enforcing arbitration agreements against members of a certified or putative class action." Ex. 2 at 1. Referring to its enforcement action against Schwab, FINRA further states:

> FINRA crafted Rule 12204 to prevent member firms from using an existing arbitration agreement to defeat class certification or participation. In approving FINRA Rules 12204 and 2268, the SEC stated that "in all cases, class actions are better handled by the courts and that investors should have access to the courts to resolve class actions efficiently." FINRA Rules 2268(d)(1) and (d)(3) prohibit member firms from incorporating class action waivers into their customer agreements.
>
> As stated above, member firms with provisions in customer agreements that do not comply with FINRA rules may be subject to disciplinary action. For example, in 2014, FINRA issued a decision finding that a firm violated FINRA rules when it inserted provisions in predispute arbitration agreements that prevented customers from bringing or participating in judicial class actions.

Ex. 2 at 4 (internal citations omitted).

41. In referring in Regulatory Notice 21-16 to the Commission's approval of FINRA Rules 12204 and 2268, FINRA cites to Exchange Act Release No. 31371 (Oct. 28, 1992) ("Release 31371"), in which the Commission approved an NASD proposed rule change relating to the exclusion of class actions from arbitration proceedings. Ex. 2 at 4, n.11. However, Release 31371 does not identify any statutory language reflecting congressional intent to allow the Commission to preclude parties from entering into or enforcing arbitration agreements that require arbitration on an individual basis. *See Approval of Proposed Rule Changes* (Exchange Act Release No.

31371), 57 Fed. Reg. 52,659, 52,660 (SEC Nov. 3, 1992) (Order Approving File No. SR-NASD-92-28). Further, Release No. 31371 pre-dates the Supreme Court's holdings in *American Express Co. v. Italian Colors Restaurant*, 570 U.S. 228, 233 (2013) and *Epic Systems*, 138 S. Ct. at 1624, which affirm that a class action waiver in an arbitration clause is enforceable under the FAA unless a statute provides a "contrary congressional command," that is a "clear and manifest" expression of congressional intent that agreements to arbitrate certain types of disputes can be limited or precluded.

42. Before filing this Petition, Thrivent and TIMI met informally with FINRA staff seeking an interpretation of FINRA Rules that would allow Thrivent and TIMI to enforce the MDRP. After these discussions, in a February 25, 2021 letter to TIMI, FINRA staff confirmed its position that under Rule 12200, "customers have a right to request arbitration at the FINRA forum at any time and do not forfeit that right under FINRA rules by signing any agreement with a forum selection provision specifying another dispute resolution process or an arbitration venue other than the FINRA arbitration forum." Exhibit 3, Letter from FINRA to TIMI (Feb. 25, 2021), at 1.

43. In further support of this position, FINRA staff also referred to Rule 2268, stating that it "make[s] clear that predispute arbitration agreements must preserve customers' rights under FINRA rules." *Id.* at 2. FINRA staff concluded that "[t]o comply with FINRA rules, any predispute arbitration agreement or any other agreement related to disputes between TIMI and Thrivent members should make clear that Thrivent members are not prohibited from requesting arbitration of a dispute in the FINRA arbitration forum as specified in FINRA rules." *Id.*

B. Neither the Commission nor FINRA have Authority under Federal Law to Use FINRA Rules to Prohibit Enforcement of the MDRP or the Sale of Securities Products that Include the MDRP

44. The FAA provides that arbitration provisions are valid, irrevocable, and enforceable, unless there is a non-arbitration-specific legal ground, applicable to contracts

generally (such as lack of mutual assent or unconscionability), to revoke the arbitration agreement.[14] The Supreme Court has explained many times that the FAA reflects a federal pro-arbitration policy. *See, e.g.*, *Moses H. Cone Mem'l Hosp.,* 460 U.S. at 24 (1983) (explaining that the FAA establishes "a liberal federal policy favoring arbitration agreements"); *Concepcion*, 563 U.S. at 339 (same); *CompuCredit Corp v. Greenwood*, 565 U.S. 95, 98 (2012) (same); *Epic Systems*, 138 S. Ct. at 1621 (same). As the Supreme Court has further explained, Congress established this federal policy favoring arbitration because private agreements to arbitrate can confer many benefits on the parties to a dispute:

> The point of affording parties discretion in designing arbitration processes is to allow for efficient, streamlined procedures tailored to the type of dispute. It can be specified, for example, that the decisionmaker be a specialist in the relevant field, or that proceedings be kept confidential to protect trade secrets. And the informality of arbitral proceedings is itself desirable, reducing the cost and increasing the speed of dispute resolution.

Concepcion, 563 U.S. at 344-45. *See also, Mitsubishi Motors Corp.*, 473 U.S. at 633 (stating that "adaptability and access to expertise are hallmarks of arbitration" and that "it is often a judgment that streamlined proceedings and expeditious results will best serve their needs that causes parties to agree to arbitrate their disputes; it is typically a desire to keep the effort and expense required to resolve a dispute within manageable bounds that prompts them mutually to forgo access to judicial remedies.").

45. To ensure adherence to the federal pro-arbitration policy Congress established in the FAA, the Supreme Court has repeatedly held that unless another statute clearly and expressly overrides the FAA, the FAA "requires courts to enforce agreements to arbitrate according to" the terms of the arbitration agreement, "even when the claims at issue are federal statutory claims."

[14] 9 U.S.C. § 2.

CompuCredit, 565 U.S. at 98 (quoting *McMahon*, 482 U.S. at 226). Further, regulators are precluded from imposing prohibitions against entering into or enforcing otherwise valid arbitration agreements unless a federal statute clearly and expressly provides the regulators with such authority. *See, e.g.*, *Epic Systems*, 138 S. Ct. at 1624 (holding that the terms of an arbitration agreement were enforceable, and that the NLRA did not provide the NLRB with statutory authority to override the FAA, because the NLRA "does not express approval or disapproval of arbitration . . . does not mention class or collective action procedures . . . [and] does not even hint at a [congressional] wish to displace the [FAA]—let alone accomplish that much clearly and manifestly, as our precedents demand.").[15]

46. Under the FAA, arbitration agreements must be enforced unless Congress, by statute, overrides the FAA in the particular area at issue. FINRA, which exercises regulatory authority only under the federal securities laws and with the Commission's imprimatur, cannot promulgate or enforce rules that the Commission could not itself adopt or enforce.

1. Neither the Commission nor FINRA had Authority under Federal Law to Adopt the Challenged FINRA Rules

47. The Commission derives its authority from the federal securities laws, including the Exchange Act and the Securities Act. These laws do not provide explicit authority for FINRA Rules prohibiting enforcement of private arbitration agreements that mandate individual arbitration outside the FINRA forum, which is the only way that FINRA Rules could supersede

[15] Although *Epic Systems* arises in the context of arbitration agreements addressing employment disputes, the *Epic Systems* holding and the Supreme Court precedent on which it relies, like the FAA itself, apply broadly to all "agreements to arbitrate." 9 U.S.C. § 2. The *Epic Systems* holding thus is not limited to arbitration provisions governing employment disputes. For example, in *Epic Systems* the Supreme Court relied on, *inter alia*, its prior holdings in: *Italian Colors*, 570 U.S. at 231 (addressing an arbitration agreement between a credit card company and merchants who accept the credit cards); *CompuCredit,* 565 U.S. at 96-97 (addressing an arbitration agreement between consumers and a credit card issuer and marketing company); *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 478 (1989) (addressing an arbitration agreement between a securities brokerage firm and its customers); and *McMahon*, 482 U.S. at 222 (addressing an arbitration agreement between a securities brokerage firm and its customers). *Epic Systems*, 138 S. Ct. at 1627-28.

the FAA and prohibit FINRA members and their customers from agreeing to arbitrate in a manner not prescribed by FINRA.

48. In *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 226 (1987), the Supreme Court held that the Exchange Act does not override the FAA. In *McMahon*, the Court addressed whether the McMahons, who were customers of registered brokerage firm Shearson/American Express Inc., were bound by an arbitration agreement with respect to claims alleging violations of the antifraud provisions in Section 10(b) of the Exchange Act. The Supreme Court explained that the FAA "may be overridden by a contrary congressional command," and that the burden is "on the party opposing arbitration" to show that Congress intended the FAA to be overridden with respect to the arbitration agreement at issue. *McMahon*, 482 U.S. at 226-27. Thus, the McMahons had to "demonstrate that Congress intended to make an exception to the [Federal] Arbitration Act for claims arising under . . . the Exchange Act, an intention discernible from the text, history, or purposes of the statute." The Supreme Court analyzed and rejected numerous arguments asserting that the Exchange Act overrides the FAA (*Id.* at 227-38), before concluding that "the McMahons' agreements to arbitrate Exchange Act claims [are] 'enforceable . . . in accord with the explicit provisions of the [Federal] Arbitration Act.'" *Id.* at 238 (quoting *Scherk v. Alberto-Culver Co.,* 417 U.S. 506, 520 (1974)).

49. Since *McMahon*, Congress in 2010 adopted the Dodd-Frank Act, which amended the Exchange Act by adding Section 78o(o), which states as follows:

> The Commission, by rule, may prohibit, or impose conditions or limitations on the use of, agreements that require customers or clients of any broker, dealer, or municipal securities dealer to arbitrate any future dispute between them arising under the Federal securities laws, the rules and regulations thereunder, or the rules of a self-regulatory organization if it finds that such

> prohibition, imposition of conditions, or limitations are in the public interest and for the protection of investors.[16]

50. While Section 78o(o) gives the Commission authority to prohibit or otherwise impose conditions or limits on some arbitration agreements, the Commission only can do so "by rule"—meaning by following rulemaking procedural requirements under the APA, 5 U.S.C. § 551 *et seq*. The Commission has not proposed a rule nor undertaken notice and comment rulemaking to establish its own authority to impose restrictions on arbitration agreements pursuant to Section 78o(o), much less to approve FINRA Rules that confer on FINRA the authority to override the FAA.[17]

51. Two years after *McMahon*, in *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), the Supreme Court similarly held that the Securities Act does not override the FAA. The Court in *Rodriguez* held that Section 14 of the Securities Act did not "prohibit[] agreements to arbitrate future disputes relating to the purchase of securities." Further, the Court did not find any other statutory basis in the Securities Act to justify prohibiting arbitration agreements with respect to Securities Act claims. *Rodriguez*, 490 U.S. at 480. In so holding, the Supreme Court expressly overruled its prior holding in *Wilko v. Swan*, 346 U.S. 427 (1953), putting to rest any lingering question as to whether federal securities laws empower the Commission—or FINRA—to prohibit or limit parties' ability to agree to resolve disputes in arbitration, notwithstanding the FAA.

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[16] 15 U.S.C. § 78o(o).

[17] The Commission provided notice and comment with respect to the Challenged FINRA Rules at the time they were adopted, nearly two decades prior to the Dodd Frank Act's addition of 15 U.S.C. § 78o(o), without citing any statutory authority reflecting congressional intent to allow the Commission or FINRA to impose the constraints on private arbitration agreements imposed by the Challenged FINRA Rules, and prior to Supreme Court holdings in *Italian Colors* and *Epic Systems* affirming that the FAA can only be overridden, both with respect to agreements to arbitrate and with respect to class action waiver provisions, where there is statutory authority clearly and manifestly reflecting congressional intent to supersede the FAA.

2. Federal Securities Laws Also Do Not Override the FAA's Protection of Arbitration Provisions Requiring *Individual* Claims

52. Supreme Court jurisprudence since *McMahon* and *Rodriguez* not only confirms the arbitrability of claims under the federal securities laws, but also confirms that agreements to resolve disputes individually in arbitration, and thus waive putative class actions, are enforceable to the same extent as other provisions specifying the form of arbitration to which the parties agree. Indeed, the Supreme Court has affirmed the strong policy basis for allowing parties to agree to a class action waiver as part of an arbitration agreement. In *AT&T Mobility LLC v. Concepcion*, the Court stated as follows:

> The point of affording parties discretion in designing arbitration processes is to allow for efficient, streamlined procedures tailored to the type of dispute. It can be specified, for example, that the decisionmaker be a specialist in the relevant field, or that proceedings be kept confidential to protect trade secrets. And the informality of arbitral proceedings is itself desirable, reducing the cost and increasing the speed of dispute resolution.
> …
> [T]he switch from bilateral to class arbitration sacrifices the principal advantage of arbitration—its informality—and makes the process slower, more costly, and more likely to generate procedural morass than final judgment.

Concepcion, 563 U.S. at 344-45.

53. Thus, in *Italian Colors,* 570 U.S. at 233, the Supreme Court affirmed that unless there is federal law that clearly overrides the FAA and allows a regulator to limit arbitration rights in that specific statutory context, an agreement to resolve claims individually in arbitration, and thus waive potential resolution through a class action, is enforceable under the FAA. Likewise, in *Epic Systems*, a case addressing an arbitration provision agreeing to resolve disputes individually and waiving class actions, the Supreme Court affirmed that congressional intent to override the FAA and prohibit a class action waiver provision must be "clear and manifest." *Epic Systems*, 138 S. Ct. at 1624.

54. In *Epic Systems*, the Supreme Court addressed whether the provision in Section 7 of the NLRA that guarantees workers "the right . . . to engage in other concerted activities for the purpose of collective bargaining or other mutual aid or protection" empowered the NLRB to override the FAA and preclude class action waivers in arbitration provisions included in employment agreements. The Supreme Court rejected the argument that this language in the NLRA regarding "concerted activities" reflected congressional intent to prohibit class action waivers in arbitration provisions. *Epic Systems*, 138 S. Ct. at 1625-29. The Court overturned the NLRB's interpretation that the NLRA's language prohibited class action waivers in agreements to arbitrate employment disputes.

55. *Epic Systems* stands for the proposition that federal agencies do not have the authority to override the FAA and limit arbitration rights, unless the agency's enabling statute(s) expressly confers such authority.[18] Also, the federal securities laws do not include any indication, much less the required "clear and manifest" indication, that Congress intended to override the FAA and allow FINRA to promulgate or enforce FINRA Rules precluding arbitration provisions that mandate individual arbitration of claims in a non-FINRA arbitration forum. Nor has the Commission undertaken rulemaking to address broker-dealer arbitration agreements with customers under the authority conferred in Section 78o(o) by the Dodd-Frank Act in 2010.

[18] The Supreme Court's holding in *Lamps Plus v. Varela*, 587 U.S. __, 139 S. Ct. 1407 (2019), further affirms that the FAA protects class action waiver provisions. In *Lamps Plus*, the Supreme Court cited *Epic Systems* for the proposition that "class arbitration fundamentally changes the nature of the 'traditional individualized arbitration' envisioned by the FAA," and further affirmed that "'a party may not be compelled under the FAA to submit to class arbitration unless there is a contractual basis for concluding that the party *agreed* to do so.'" *Lamps Plus*, 139 S. Ct. at 1412 (quoting *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662, 684 (2010)). In *Lamps Plus* the Supreme Court further concluded that the FAA bars an order requiring class-wide arbitration, rather than individual arbitration, when an agreement is ambiguous rather than silent as to whether claims can be addressed on a class-wide basis. *Id.* at 1419.

3. Neither the Commission nor FINRA have Authority under Federal Law to Prohibit the Sale of Securities Products, the Disputes of which are Governed by Private Arbitration Agreements

56. The FAA also protects the *formation* of otherwise valid and enforceable arbitration agreements, in addition to their enforceability. In *Kindred Nursing Centers Ltd. Partnership v. Clark*, the Supreme Court expressly rejected the notion that "the FAA has no application to contract formation issues," holding instead that the FAA "cares not only about the enforce[ment] of arbitration agreements, but also about their initial validity—that is, about what it takes to enter into them." *Kindred Nursing Ctrs. Ltd. P'ship v. Clark*, 581 U.S. __, 137 S. Ct. 1421, 1428 (2017) (internal quotations omitted).

57. But FINRA Rule 2268(d) expressly prohibits the formation of certain types of otherwise valid arbitration agreements, including those that "limit[] the ability of a party to file any claim in court permitted to be filed in court under the rules of the forums in which a claim may be filed under the agreement." FINRA Rule 2268(d)(3). Consequently, not only are FINRA members not allowed to enforce such agreements where they already exist, but also they are not allowed to enter into such agreements or sell securities products if customer disputes are covered by such agreements. Moreover, because broker-dealers legally are required to become FINRA members (see above paras. 22–23), the effect of this rule is to prohibit the sale of securities products with arbitration agreements that impose limitations disallowed by FINRA Rule 2268(d).

58. By prohibiting the sale of securities products with arbitration agreements disallowed by FINRA, Rule 2268(d) in effect prohibits parties from entering into certain types of otherwise valid arbitration agreements, thereby directly implicating the FAA as the Supreme Court held in *Kindred Nursing*. FINRA Rule 2268(d) thus precludes parties from agreeing to resolve disputes through individual arbitration—a form of dispute resolution that is favored by federal law. *McMahon* and *Rodriguez* confirm that the federal securities laws do not authorize the Commission

or FINRA to impose such a prohibition. Therefore, the FAA overrides and invalidates FINRA Rule 2268(d) as written.

59. Without any express statutory authority, FINRA Rule 2268 also imposes special notice requirements with respect to arbitration clauses included in customers' contracts that single out these arbitration clauses for special treatment that is not generally applicable to other contract terms. (See above para. 36.) These special notice requirements are contrary to the FAA and Supreme Court precedent interpreting the FAA, and thus they also are invalid. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996) (invalidating a Montana statute that conditioned enforceability of arbitration agreements on compliance with a special notice requirement—requiring that the arbitration clause be printed on the first page in underlined capital letters—that was not applicable to contracts generally and therefore preempted by the FAA). As the Supreme Court explained in *Doctor's Associates*, special notice requirements like those set forth in FINRA Rules 2268(a) and (b) "condition[] the enforceability of arbitration agreements on compliance with a special notice requirement not applicable to contracts generally." *Id.* at 687. Such special notice requirements thus are contrary to the "goals and policies" of the FAA, which is intended to preclude threshold limitations placed specifically and solely on arbitration provisions. *Id.* at 688.

C. The Commission Must Abrogate or Amend the Challenged FINRA Rules

60. As the foregoing authority illustrates, the federal securities laws do not allow FINRA to promulgate, or the Commission to approve, FINRA Rules that prohibit enforcement of private agreements mandating individual arbitration outside of the FINRA arbitration forum. Nor do they allow FINRA to promulgate, or the Commission to approve, FINRA rules that require special notice of arbitration agreements as compared to other types of agreements or contract provisions. Consistent with Supreme Court precedent, the Challenged FINRA Rules, and any other

FINRA Rules that impose such restrictions on private arbitration agreements, are beyond the scope of Commission/FINRA authority, contrary to federal law, and invalidated by the FAA.

61. The Exchange Act requires the Commission to oversee FINRA, ensure that FINRA operates in accordance with federal law, and approve only those FINRA Rules that comply with "the requirements of [the Exchange Act] and the rules and regulations issued under [the Exchange Act]." 15 U.S.C. § 78s(b)(2)(C)(i). The Exchange Act does not eclipse the FAA because it does not reflect congressional intent to supersede the FAA. *McMahon*, 482 U.S. at 226. Similarly, FINRA Rules approved by the Commission pursuant to the Exchange Act do not supersede the FAA. Thus, it is necessary and appropriate for the Commission to "abrogate, add to, and delete from" these Challenged FINRA Rules to bring them into compliance with federal law.

62. Further, the Securities Act and the Exchange Act both mandate that whenever "the Commission is engaged in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation." 15 U.S.C. § 77b(b); 15 U.S.C. § 78c(f). The FAA, which again is "a congressional declaration of a liberal policy favoring arbitration agreements" (*Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24), already speaks to the benefit to investors of allowing them to agree to resolve disputes through individual private arbitration. Amending or abrogating the Challenged FINRA Rules to comply with the FAA also will promote efficiency—by allowing parties to choose individual arbitration as an efficient means to resolve their disputes—as well as competition and capital formation. Amendment or abrogation would remove the impediments the Challenged FINRA Rules impose upon, and allow for further investment in, securities products subject to private agreements to arbitrate disputes individually.

63. Thrivent and TIMI do not suggest, by this Petition, that the SEC and FINRA have *no* authority to oversee and regulate the resolution of disputes between FINRA members and their customers in order to achieve their institutional goals of investor protection. But neither the SEC nor FINRA have statutory authorization to entirely disallow FINRA members and their customers from entering into private arbitration agreements mandating individual arbitration of their disputes as the Challenged FINRA Rules do. The Challenged FINRA Rules therefore are unlawful and invalid under the FAA and must be abrogated or amended to conform with federal law.

V. THE PETITIONERS' INTEREST IN ABROGATING OR AMENDING THE CHALLENGED FINRA RULES

64. As explained above in paragraphs 2 and 10, Thrivent's Bylaws establish the MDRP to address disputes between Thrivent Members on the one hand and Thrivent or those acting on Thrivent's behalf (including TIMI) on the other. The MDRP provides for mandatory individual arbitration under terms set forth in Thrivent's Bylaws, rather than those established by FINRA Rules.

65. Thrivent's MDRP is set forth in Section 11 of the Bylaws. Ex. 1 at 3-4. Thrivent Members adopted the MDRP over 20 years ago. The MDRP is intended to address any disputes that arise between Thrivent (or those acting on Thrivent's behalf) and Thrivent's Members. The MDRP includes a three-step process that concludes, when necessary, with mandatory and binding individual arbitration consistent with the FAA, the cost of which is borne by Thrivent. The MDRP is part of Thrivent's governing documents. Further, state law requires incorporation of Thrivent's Bylaws, which include the MDRP provision, into all of Thrivent's insurance products that Thrivent Members purchase. Wis. Stat. § 632.93. Thus, pursuant to state law, the Bylaws apply equally and uniformly to all Thrivent Members. The MDRP is enforceable under state law. Courts around the

country have addressed the MDRP in connection with disputes related to traditional insurance products, and unanimously have held that the MDRP is enforceable.[19]

66. In Thrivent's experience, the MDRP is highly beneficial to Thrivent Members for several reasons. *First*, it allows for efficient resolution of disputes, at Thrivent's expense. In this respect and others, Thrivent has designed its MDRP to ensure that its Members' concerns are heard and addressed, even if the dollar value of a particular dispute is small. *Second*, because Thrivent has its own dispute resolution process, with only individual claims, Thrivent Members can present their specific concerns directly to Thrivent, and Thrivent can hear and resolve those concerns in a manner that is specific to the Member; this process allows Thrivent to better maintain the fraternal relationship with and among its Members. *Third,* because Thrivent has no other stakeholders—it is a not-for-profit organization and owned by its Members—Thrivent's incentives are to resolve disputes fairly and in a manner conducive to its fraternal character.

67. As a member-governed organization, uniform application of the Bylaws, including the MDRP Bylaw, is a core component of Thrivent's governance structure. Further, the successful history of the MDRP in both resolving disputes with Thrivent Members and maintaining the fraternal relationship among the membership even when disputes arise makes ensuring uniform application of the MDRP of paramount importance to Thrivent. Inconsistent with Thrivent's Bylaws, however, the Challenged FINRA Rules require Thrivent to apply one set of dispute resolution requirements to disputes arising with respect to the purchase of Thrivent insurance

[19] *See, e.g.*, *Erickson v. Thrivent Ins. Agency, Inc., d/b/a Thrivent Financial for Lutherans*, 231 F. Supp. 3d 324 (D.S.D. 2017); *Agri-Turf Supplies, Inc. v. Thrivent Financial for Lutherans*, No. 12-4958, 2012 WL 12914723 (C.D. Cal. Sept. 18, 2012); *Lulloff v. Thrivent Financial for Lutherans f/k/a Lutheran Brotherhood*, No. 02-3887, 2003 WL 22717879 (Wis. Cir. Ct. Oct. 29, 2003); *Hawkins v. Aid Ass'n for Lutherans*, 338 F.3d 801, 809 (7th Cir. 2003) (addressing prior version of MDRP Bylaw adopted by Thrivent's predecessor), *aff'g* No. 00-C-1327, 2001 WL 34388865 (E.D. Wis. Oct. 31, 2001), *and aff'g Aid Ass'n for Lutherans v. Radmer*, No. 99-C-1205, 2001 WL 34388864 (E.D. Wis. Oct. 31, 2001), *cert. denied*, 540 U.S. 1149 (2004); *Thrivent Fin. for Lutherans v. Lakin*, 322 F. Supp. 2d 1017 (W.D. Mo. 2004).

products that are not securities (such as fixed annuities) and another set of requirements with respect to Thrivent products that are securities (such as Variable Products).

68. Nevertheless, as a voluntary accommodation to the Commission staff, Thrivent historically has treated the MDRP as optional with respect to Member disputes arising in connection with its Variable Products ("Voluntary Undertaking"). Under the Voluntary Undertaking, the MDRP also has been treated as optional with respect to Member disputes involving Variable Products that arise between Thrivent Members and Thrivent or the broker-dealers selling Variable Products on Thrivent's behalf. Consistent with this Voluntary Undertaking, when a dispute with respect to a Thrivent Variable Product arises, Thrivent and TIMI follow a specific procedure: 1) Members submit disputes to Thrivent's Member Relations Department; 2) if the dispute is not resolved by Thrivent's Member Relations Department, Thrivent provides Members with a brochure explaining the MDRP process, which expressly states that the MDRP is optional, not mandatory, with respect to a Variable Product dispute; and 3) the customer determines whether to continue under the MDRP process or under FINRA customer arbitration. The Commission staff has previously reviewed and agreed to the timing and content of Thrivent's brochure disclosure regarding the Voluntary Undertaking.[20] Currently, the Voluntary Undertaking results in disparate treatment among Thrivent's membership, depending on whether the Member purchases a Variable Product or a Thrivent insurance product that is not a security and thus not subject to the Voluntary Undertaking.

69. However, Thrivent has determined to discontinue the Voluntary Undertaking for purposes of consistent administration of its business and consistent treatment of Members. Thrivent Variable Products, like Thrivent non-variable insurance products, are only available to

[20] See Exhibit 4, May 13, 2008 letter from Thrivent to the SEC staff; Exhibit 5, May 21, 2008 letter from Thrivent to the SEC staff.

persons who already are, or become, Thrivent Members. Thus, all purchasers of the Variable Products *already* have agreed to abide by Thrivent's Bylaws, including the MDRP Bylaw. In addition, the insurance contract for all Thrivent Variable Products expressly incorporates Thrivent's Articles of Incorporation and Bylaws, including the MDRP Bylaw, which means the MDRP is legally part of the insurance contract. Thus, those who purchase Thrivent Variable Products have already agreed to application of the MDRP provisions. But notwithstanding this agreement, pursuant to the Voluntary Undertaking, Members are in a position of deciding *again*, at the time a dispute already exists, whether they will agree to the MDRP. In Thrivent's experience, this is not consistent with the MDRP's salutary goals of attempting to maintain Thrivent's relations with its Members, resolve disputes fairly and efficiently, and ensure uniformity of rights and obligations among Thrivent's membership. Stated simply: Thrivent believes that the MDRP is a better way for Thrivent to resolve disputes with its Members, as compared to the ways that the Challenged FINRA Rules require Thrivent to resolve disputes with its Members in connection with Variable Products. But the Challenged FINRA Rules will not allow Thrivent and its Members to agree in advance to resolve disputes through the MDRP, regardless of whether they otherwise would agree to do so and regardless of the fact that the MDRP is a core component of Thrivent's governance structure and Bylaws.

70. The proposal to abrogate or amend the Challenged FINRA Rules ensures that the MDRP will be applied to all Thrivent Members equally—purchasers of Thrivent Variable Products and non-variable insurance products alike. This furthers Thrivent's interest in uniform application of its Bylaws to its Members, which is a core component of Thrivent's governance structure. (See above paras. 10 and 67).

71. Thrivent, TIMI, and other broker-dealers selling Variable Products on Thrivent's behalf have a further compelling interest in the proposed abrogation of or amendment to the Challenged FINRA Rules: Thrivent is required by state law to incorporate its Bylaws, which include the MDRP provision, into all of Thrivent's insurance products; but absent the Voluntary Undertaking, Rule 2268(d) would have the effect of prohibiting the sale of Thrivent Variable Products because such Variable Products incorporate the MDRP's class action waiver provision.

72. For all of the foregoing reasons, Thrivent and TIMI submit that the Commission should grant this Petition to abrogate or amend the Challenged FINRA Rules, which neither the Commission nor FINRA have authority to promulgate or enforce, and which are invalidated by the FAA.

VI. PROPOSED AMENDMENTS TO FINRA RULES

73. To address and correct the Challenged FINRA Rules—which the FAA requires the Commission to do—the Commission could simply remove the Challenged FINRA Rules from FINRA's rule book. Alternatively, the Commission should amend the Challenged FINRA Rules, consistent with the FAA and Supreme Court precedent, to clarify that private agreements between FINRA members and their customers that require individual arbitration in a non-FINRA forum are valid and enforceable under FINRA Rules, and that FINRA's special notice requirements applicable to arbitration provisions are not enforceable. Indeed, several federal courts have already concluded, consistent with the FAA, that private arbitration agreements between customers and FINRA members override FINRA Rules.[21]

[21] *See, e.g.*, *City of Reno*, 747 F.3d at 741 (9th Cir. 2014) (holding that a forum selection clause in a customer contract "superseded Goldman's default obligation to arbitrate under the FINRA Rules."); *UBS Fin. Servs, Inc. v. Carilion Clinic*, 706 F.3d 319, 328 (4th Cir. 2013) (agreeing with the proposition that " the obligation to arbitrate under FINRA Rule 12200 can be superseded and displaced by a more specific agreement between the parties."); *American Express Co. v. Beland* (*In re Am. Express Fin. Advisors Sec. Litig.*), 672 F.3d 113, 132 (2d Cir. 2011) ("[D]ifferent or additional contractual arrangements for arbitration can supersede the rights conferred on a customer by virtue of a broker's membership in a self-regulating organization such as FINRA." (internal brackets omitted)).

74. To the extent the Commission or FINRA elect to amend the Challenged FINRA Rules, they retain institutional authority to impose some oversight with respect to the substance of private dispute resolution, consistent with the statutory authority conferred upon them under the federal securities laws. Under the Exchange Act, for example, the Commission has the authority and responsibility to ensure that FINRA Rules, *inter alia*, "are designed to prevent fraudulent and manipulative acts and practices . . . and, in general, to protect investors and the public interest." 15 U.S.C. § 78o-3(b)(6).[22] Thus, the Commission and FINRA have authority to craft rules to ensure that FINRA members' private arbitration agreements with their customers are not fraudulent or unconscionable. But what the Commission and FINRA cannot do under the FAA or the federal securities laws is promulgate FINRA Rules that entirely foreclose FINRA members from entering into any private arbitration agreements requiring individual arbitration in a non-

[22] 15 U.S.C. § 78o-3(b)(6) states, in full:

> An association of brokers and dealers shall not be registered as a national securities association unless the Commission determines that . . . [t]he rules of the association are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, to fix minimum profits, to impose any schedule or fix rates of commissions, allowances, discounts, or other fees to be charged by its members, or to regulate by virtue of any authority conferred by this chapter matters not related to the purposes of this chapter or the administration of the association.

Similarly, Article XI of FINRA's Bylaws states:

> To promote and enforce just and equitable principles of trade and business, to maintain high standards of commercial honor and integrity among members of the Corporation, to prevent fraudulent and manipulative acts and practices, to provide safeguards against unreasonable profits or unreasonable rates of commissions or other charges, to protect investors and the public interest, to collaborate with governmental and other agencies in the promotion of fair practices and the elimination of fraud, and in general to carry out the purposes of the Corporation and of the Act, the Board is hereby authorized to adopt such rules for the members and persons associated with members, and such amendments thereto as it may, from time to time, deem necessary or appropriate. If any such rules or amendments thereto are approved by the Commission as provided in the Act, they shall become effective Rules of the Corporation as of such date as the Board may prescribe. The Board is hereby authorized, subject to the provisions of the By-Laws and the Act, to administer, enforce, suspend, or cancel any Rules of the Corporation adopted hereunder.

FINRA forum. That is what the Challenged FINRA Rules do as presently constituted, and thus they are unlawful and invalid under the FAA.

VII. CONCLUSION

75. Based upon the foregoing, the Commission must take prompt action. The Challenged FINRA Rules violate the FAA because, without congressional authorization, these Rules prohibit Thrivent from applying the MDRP's otherwise enforceable mandate for individual arbitration as intended. Specifically, and as explained above in detail, if Thrivent Variable Products mandate application of the MDRP's arbitration provision as intended by Thrivent's Bylaws, the Challenged FINRA Rules: (1) preclude TIMI from selling such Variable Products; (2) preclude the Variable Products from being sold by FINRA members, and therefore from being sold at all; and (3) prohibit enforcement of the otherwise valid MDRP. Because the Challenged FINRA Rules violate federal law by exceeding the Commission's statutory authority and are invalidated by the FAA, the Commission must use its authority under 15 U.S.C. § 78s(c) to abrogate or amend these Rules.

76. Thrivent and TIMI respectfully request that the Commission act expeditiously to address the issues raised in this Petition. To the extent the Commission disagrees with the position set forth in this Petition, Thrivent and TIMI respectfully request that the Commission promptly issue a final decision setting forth the Commission's contrary position so that additional avenues of legal recourse can be pursued. This will avoid unnecessarily prolonging the time during which FINRA members are required to operate in accordance with the unlawful and invalid Challenged FINRA Rules.

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