UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

ADAM S. KAPLAN and DANIEL E. KAPLAN, Petitioners, v. MERRILL LYNCH, PIERCE, FENNER & SMITH INC., Respondent.	Case No. 1:22-CV-1333 **PETITION TO VACATE ARBITRATION AWARD**

Petitioners Adam Scott Kaplan and Daniel Evan Kaplan (together, "Petitioners" or the "Kaplans"), by and through their attorneys, ChaudhryLaw PLLC and the Law Office of Daniel F. Wachtell, allege as follows:

NATURE OF PROCEEDING AND RELIEF SOUGHT

1. The Kaplans commence this proceeding pursuant to the Federal Arbitration Act, 9 U.S.C. § 10 (the "FAA"), to vacate an arbitration award rendered by the Financial Industry Regulatory Authority ("FINRA"), to the extent that it was entered against them and in favor of Respondent Merrill Lynch, Pierce, Fenner & Smith Inc. ("Merrill Lynch" or "Merrill"), in the FINRA Dispute Resolution Services matter captioned *Adam Scott Kaplan & Daniel Evan Kaplan v. Merrill Lynch, Pierce, Fenner & Smith Inc.*, Case Number 19-00803.

2. Petitioners served a Statement of Claim on or about March 25, 2019, Ex. 1, and an Amended Statement of Claim on or about June 20, 2019, Ex. 2, seeking expungement of retaliatory, defamatory, and false statements made by Merrill about the Kaplans on identical Form U5 Uniform Termination Notices ("Form U5s" or "U5s") for the Kaplans, filed by Merrill with FINRA on or about April 5, 2018. Ex. 3.

3. Following a two-day hearing held on October 27 and 28, 2021, a three-person panel of FINRA Dispute Resolution Services arbitrators (the "Panel") rendered an award in favor of Merrill, and against the Kaplans, which was served upon the Kaplans on November 16, 2021 (the "Award"). Ex. 4.

4. Following the Award, Petitioners discovered that the Chairman of the Panel, Andrew Schmertz, had previously been employed by Merrill. Both Schmertz and Merrill failed to disclose this at any time.

5. The FAA provides four statutory bases for vacating an arbitration award. Here, vacatur of the Award is required because, among other reasons: the Chairman of the Panel failed to disclose a material conflict that rendered him "evidently partial" in favor of Merrill; the Award was "fundamentally unfair" because the Panel improperly admitted evidence offered by Respondent in contravention of the parties' stipulation to the contrary; and the Panel, together with those two factors, "manifestly disregarded" the existence (or non-existence) of relevant rules and regulations in rendering its decision.

INTRODUCTION

6. This case involves an unextraordinary circumstance: two individuals, employed as financial advisors, who were terminated by Merrill Lynch not long into their at-will employment. The individuals – the Petitioners, who are identical twin brothers – came to Merrill with a complicated history and were embroiled in difficulty from the moment they arrived due to unresolved issues with their prior employer, Morgan Stanley (issues which subsequently were resolved entirely in the Kaplans' favor). Merrill was entirely within its rights to decide that having the Kaplans on board was not worth the increased cost and burden of closely monitoring

them and dealing with the bumpy transition away from Morgan Stanley, and thus within its rights to terminate their at-will employment at any point.

7. An uncomplicated parting of ways should have been the end of the story. However, it was not: after terminating the Kaplans for the reason stated above, Merrill decided to take the additional baseless and prejudicial step of falsely indicating, on the U5s that described the end of Petitioners' employment, that (1) the Kaplans were each discharged for "conduct involving client logon credentials to access client accounts"; and (2) the Kaplans were discharged for "violating investment-related statutes, regulations, rules or industry standards of conduct." *See* Ex. 3, pgs.

8. There was no basis for these actions by Merrill, and Petitioners pursued a FINRA arbitration to seek expungement of the U5s, which was unsuccessful. That arbitration proceeding is at issue in this Petition to Vacate.

9. Although the Kaplans did not know it at the time, the arbitration was infected from the outset by the prejudice of the Chairman of the Panel, Andrew Schmertz, who failed to disclose that he had previously been employed by Merrill Lynch, the Respondent in the arbitration. Not only did Chairman Schmertz fail to disclose this to the parties at any point pre-hearing, he expressly represented at the beginning of the hearing, *sua sponte*, that he had no conflicts of interest at all.

10. Standing alone, this intentionally undisclosed conflict is sufficient under the FAA to call into question the legitimacy of the arbitration award rendered in favor of Merrill. Indeed, such a blatant conflict of interest is precisely why the FAA requires conflict disclosures before arbitrators are empaneled.

11. Two additional provisions of the FAA are implicated here in similarly substantive and prejudicial ways, and taken together with Chairman Schmertz's evident partiality, they leave no doubt that the Award must be vacated.

12. First, in accepting Merrill's determination that the Kaplans were terminated for "violating investment-related statutes, regulations, rules or industry standards of conduct," the Panel exceeded its powers by manifestly disregarding the fact that – even assuming *arguendo* that the Kaplans did use client logon credentials to access client accounts – their conduct did not violate any investment-related statutes, regulations, rules, or industry standards of conduct.[1] Indeed, after terminating the Kaplans, Merrill subsequently changed its internal rules to prohibit what the Kaplans were alleged to have done, making clear that no such rule existed at the relevant time. Simply, it was not within the Panel's power to determine that the Kaplans violated a rule that did not exist at the time. Moreover, the Panel disregarded the fact that the supposed "evidence" of the Kaplans' misconduct was not discovered until after they had been terminated, giving lie to Merrill's claim that the conduct formed the basis for the terminations.

13. Second, the Panel prejudiced the Kaplans' rights, and rendered the arbitration proceeding fundamentally unfair, by allowing Merrill to present evidence that contravened the parties' stipulation regarding what evidence would be admissible. Specifically, even though the parties had stipulated that all evidence and demonstrative exhibits had to be produced at least twenty days prior to the arbitration hearing, the Panel (over the Kaplans' objection) allowed Merrill to present demonstrative exhibits and so-called expert testimony about the same, even though those demonstratives and the voluminous data underlying them were produced less than

[1] The Kaplans maintain that they did not use client logon credentials to access client accounts.

24 hours before the hearing, long after the applicable deadline.[2] This last-minute demonstrative also introduced entirely new topics into the proceeding that had not been raised during the previous three-and-a-half years.[3] This stripped the Kaplans of their ability to properly prepare their case, leaving them without any opportunity to confront the evidence or present competing testimony about the import of the data, and effectively ensuring that the Panel would only have Merrill's one-sided presentation to consider.

14. Petitioners are well aware that the FAA instructs that arbitration awards be overturned only in limited circumstances. Petitioners are also aware that the law of this Circuit requires that a panelist's conflict of interest rise to the level of "evident partiality" to mandate vacatur, at least standing alone. This, though, is one of those limited circumstances. The undisclosed conflict of the Panel's Chairman, taken together with the Panel's manifest disregard for the applicable law and the fundamental unfairness of the way it conducted the hearing, rendered the hearing unfair and the Award unreliable. It is inexplicable that the Panel could have allowed Merrill to present the evidence that it did in the manner that it did, and equally inexplicable that it could have credited the argument that the Kaplans violated rules that did not even exist. Inexplicable, at least, without the clear explanation that the award was influenced by the Chairman's prejudice. The arbitration award denying the Kaplans' claim to have their U5s expunged should be vacated, and this Court can and should correct this injustice by directing a rehearing before a newly constituted, impartial panel of arbitrators.

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[2] The demonstrative exhibit also failed to specifically refer to Bates numbers in Merrill's production, compounding the prejudice to the Kaplans, who were thus unable to identify or locate the underlying data.

[3] The Panel permitted this evidence to be introduced over objections from counsel for the Kaplans.

THE PARTIES

15. Petitioner Adam Scott Kaplan ("Adam Kaplan" or "Adam") is a natural person and resident of the State of Florida.

16. Petitioner Daniel Evan Kaplan ("Daniel Kaplan" or "Daniel") is a natural person and resident of the State of Florida.

17. Respondent Merrill Lynch is a broker-dealer incorporated in the State of Delaware with its principal place of business at One Bryant Park, New York, New York 10036.

JURISDICTION AND VENUE

18. This Court has subject matter jurisdiction, pursuant to 28 U.S.C. §1331, because this action to vacate an arbitration award under the FAA is a civil action "arising under the Constitution, laws, or treaties of the United States."

19. This Court has general personal jurisdiction over Merrill because Merrill regularly transacts business in this State through its headquarters, located at One Bryant Park, New York, New York 10036. Moreover, this Court has specific personal jurisdiction over Merrill because the facts underlying the Petition arise out of Merrill's conduct in and directed at this State, and because Merrill consented to and participated in the arbitration hearing in this State. *See Doctor's Assocs. v. Stuart*, 85 F.3d 975, 983 (2d Cir. 1996) ("A party who agrees to arbitrate in a particular jurisdiction consents not only to personal jurisdiction but also to venue of the courts within that jurisdiction.").

20. Venue is proper, pursuant to 28 U.S.C. § 1391, as the arbitration took place in, and the Award was issued from within this judicial district.

FACTUAL BACKGROUND

A. The Kaplans Leave Morgan Stanley for Merrill Lynch

21. Adam and Daniel Kaplan, who are identical twin brothers, were employed at Morgan Stanley as registered representatives beginning in or about March 2016.

22. The Kaplans' tenure at Morgan Stanley is relevant to this matter inasmuch as it was fraught from the outset, with the Kaplans' supervisor – Golan Yehuda – engaging in repeated and various improper conduct, including but not limited to aggressively soliciting investments and other purchases from the Kaplans' parents.

23. As a result of Mr. Yehuda's conduct, the details of which are not specifically relevant to this Petition, the Kaplans filed an internal complaint against him with Morgan Stanley on or about April 7, 2017.

24. Immediately following the filing of that complaint, the Kaplans were stripped by Morgan Stanley of their email and telephone access, their ability to use their physical offices, and their ability to contact their client base.

25. Consequently, on or about May 18, 2017, the Kaplans tendered a combined resignation letter to Morgan Stanley, effective immediately, and began their employment at Merrill Lynch the very next day, May 19, 2017.

B. The Kaplans' Employment at (and Termination from) Merrill Lynch

26. Unfortunately, the contentious circumstances surrounding the Kaplans' employment at Morgan Stanley followed them to Merrill.

27. When the Kaplans left Morgan Stanley, nearly one hundred percent of their client base left with them, transferring some or all of their account assets to Merrill.

28. As the Kaplans described in the Amended Statement of Claim filed in connection with the Arbitration, Morgan Stanley was – both because of the complaint against Yehuda and the lost clientele – "hellbent on imperiling" the Kaplans' new employment with Merrill and precluding them from landing softly in their new roles. *See* Ex. 2. To wit, on the very first day of the Kaplans' employment at Merrill on May 19, 2017, a registered representative of Morgan Stanley, Anne Tamayo, called and emailed a manager at Merrill, Anthony Falconieri, to besmirch the Kaplans' character.

29. Moreover, within a month, Morgan Stanley had filed U5s in connection with the Kaplans' departures that included false and defamatory statements regarding the Kaplans. These Morgan Stanley U5 filings forced the Kaplans to commence a separate FINRA arbitration (not directly at issue in this Petition) in order to clear their names (the "Morgan Stanley Arbitration"). The Morgan Stanley Arbitration ultimately resulted in an arbitral finding, in 2019, that was entirely in the Kaplans' favor, and ended with Morgan Stanley's improper U5 statements being expunged.

30. However, the specter of that arbitration loomed large over the Kaplans' tenure at Merrill where they were subject to additional oversight and monitoring. As Michael Gonzalez, a Market Supervision Manager at Merrill who was responsible for supervising the Kaplans, testified at the arbitration that is the subject of this Petition: "It's effectively enhanced monitoring where we would, you know, take a deeper dive. There are custom plans that are created given the facts and circumstances of what occurred. But, generally speaking, we would review trades that were done on a daily basis. We would do a deeper dive into electronic communications. Any incoming and outgoing correspondence. There is a client contact component in which you would reach out to clients." Ex. 5, 178:4-179:23. During the time the Kaplans were at Merrill Lynch,

Merrill received reports of irregularities involving four of the clients (or families of clients) who had followed the Kaplans from Morgan Stanley. Each of these four circumstances had a reasonable explanation, and – upon information and belief – each of the four reports was instigated, in one way or another, by Morgan Stanley as part of its campaign of retaliation against the Kaplans for (a) complaining about Yehuda and (b) leaving for Merrill with their book of business. In connection with the Arbitration, however, Merrill stipulated that neither the heightened supervision, nor any of the client issues referenced in the foregoing paragraphs, had anything to do with the unauthorized access to client accounts that supposedly formed the basis for the Kaplans' termination.

31. Upon information and belief, the difficulty and aggravation of supervising the Kaplans, from the outset of their employment, formed the basis for Merrill's decision to terminate the Kaplans' at-will employment on March 8, 2018, which was entirely appropriate and within Merrill's discretion to do.

32. Indeed, this is the only reasonable explanation for Merrill's decision to end the Kaplan's employment at the time that decision was taken. As described further below, while Merrill had received one suggestion that the Kaplans improperly accessed a client's account information prior to their termination, that allegation was (a) unsubstantiated at the time and (b) had been made by a customer with a history of erratic behavior,[4] and thus could not properly have formed the basis for the Kaplans' termination.

[4] Importantly, this customer, Mengfei Song, has since followed the Kaplans to their new firm after their termination by Merrill.

C. The Subsequent, Pretextual Merrill Investigation and Improper U5 Filings

33. As noted previously, this should have been the end of the story between the Kaplans and Merrill. It was not.

34. Following the Kaplans' termination, Merrill was obliged to file U5 forms within 30 days, during which time Merrill hastily convened an "investigation" into the Kaplans' conduct. From the outset, the investigation was intended to establish a pretext for marking the U5s in an inaccurate manner that would be detrimental to the Kaplans, rather than in a manner that fairly and accurately reflected the reason for their departure from Merrill.

35. Based on a single reported instance of one of the Kaplans logging into a client's "MyMerrill" account from their own electronic device – an allegation made by a source with dubious credibility,[5] and with no allegation that the Kaplans had done anything more than look at the account – Merrill investigated and supposedly found evidence of the Kaplans engaging repeatedly in the same conduct.

36. Instead of correctly noting on the Kaplans' U5s that the Kaplans were terminated for the non-pejorative, reputationally-neutral reason that it was an overwhelming burden and distraction to engage in heightened supervision of them due to the fallout from their prior employment at Morgan Stanley, Merrill chose a different course.

37. In two places on the U5s, Merrill gave explanations for the Kaplans' termination that were false, defamatory, and illogical.

38. First, relying on the supposed results of the aforementioned investigation, Merrill wrote in response to Question 3 on the Form U5s (which includes a space to provide a narrative

[5] This is the same client referenced in Paragraph 32 above, Mengfei Song.

explanation of the Reason for Termination) that the Kaplans were terminated for "conduct involving client logon credentials to access client accounts." *See* Ex. 3.

39. This could not have been true; the evidence of such conduct – even assuming *arguendo* that it exists[6] – was not known to Merrill until after the Kaplans were terminated and the firm subsequently conducted an investigation.

40. Even if Merrill had relied in part on the single pre-termination allegation of improperly accessing a client account, there is a significant difference between such an allegation forming a small fraction of the basis for a termination decision and it being reported as the sole basis for termination on the Kaplans' U5s.

41. Second, relying on the same supposed findings, Merrill indicated (by checking the "Yes" option for Question 7F(1)) that the Kaplans were discharged for "violating investment-related statutes, regulations, rules or industry standards of conduct."

42. This too was blatantly false: not only was the conduct that the Kaplans were accused of – accessing and reviewing client accounts without authorization, but without ever intending to make, attempting to make, or actually making any investment or investment-related decision – patently not "investment-related," it did not violate any statute, regulation, rule, or industry standard of conduct.

D. <u>The Flawed FINRA Arbitration</u>

43. The Kaplans, naturally, were appalled to discover that Merrill had put these quite literal black marks on their reputation by choosing to complete the U5s in such a dishonest and

[6] As noted in Paragraphs 79-81 and 109, below, Petitioners have yet to have a fair chance to assess or confront the evidence allegedly gleaned from Merrill's investigation, and one of the bases for this Petition for vacatur is that summaries of such evidence, and testimony regarding the same, were improperly introduced at the hearing in a manner that was grossly prejudicial to the Kaplans.

prejudicial manner. Consequently, they promptly filed a Statement of Claim with FINRA on or about March 25, 2019, and an Amended Statement of Claim, together with numerous exhibits, on or about June 20, 2019. *See* Exs. 1, 2.

44. Like all FINRA arbitrations, this one began with a mundane arbitration selection process in which candidates submitted Arbitrator Disclosure Reports ("ADR") to the parties; the parties, armed with this information about the potential arbitrators, had the opportunity to accept or reject arbitrator candidates.

45. Critical to these disclosures—and typical for ADRs—is the potential arbitrator's reporting of their relevant work history, any connection they may have to either party and any potential conflict they may have.

46. From the pool, the parties initially selected three candidates: Ann Gellis, Steven A. Certilman, and Robert Harrison. But then, at the last minute, there was a change.

47. Right before the arbitration was set to begin, the intended Chair of the arbitration, Robert Harrison, backed out. In short order, Andrew Schmertz presented himself as a potential replacement. Schmertz submitted an innocuous ADR betraying neither affiliations nor ties with either the Kaplans or Merrill. Ex. 6. The Kaplans—relying on the accuracy of Schmertz's ADR and ready to begin the proceeding that would clear their reputations—accepted Schmertz as the new Chair.[7]

48. Prior to the Arbitration, the parties conducted four pre-hearing sessions with the three-member Panel in August 2019; September 2020; August 2021; and October 2021. Two of

[7] Another change was made to the Panel on June 9, 2021, when Steven A. Certilman withdrew from the arbitration and was replaced by Rick Rutman.

the four pre-hearing sessions were conducted after Schmertz was appointed as Chairman of the Panel in May 2021.

49. In addition to selecting arbitrators and engaging in pre-hearing conferences, the parties exchanged voluminous discovery. In anticipation of the hearing, the parties also entered into a stipulation, dated June 30, 2021, which was intended to streamline the hearing and ensure fairness. Ex. 7. Among other things, the stipulation – which was delivered to the Panel on or about October 4, 2021, well in advance of the hearing – provided:

> The **only** documents that shall be introduced at the hearing shall be limited to documents and demonstrative exhibits pertaining to MyMerrill account activity for accounts associated with clients of the Kaplans. Any such documents and demonstrative exhibits shall also be identified in accordance with the FINRA Rules twenty (20) days before the scheduled hearing date.

Ex. 7, pg. 3[8] (emphasis in original).

50. The Arbitration hearing itself was conducted in New York on October 27, 2021, (for an entire day) and October 28, 2021 (for a partial day). The Panel heard from just four witnesses: Adam Kaplan, whose testimony was offered initially by Petitioners; Michael

[8] While the Stipulation, which was wildly violated by Merrill, appears to proscribe either party from seeking to vacate the Award, the law of this Circuit is clear: this Court maintains the power to review and vacate any award which can be presented for confirmation. "Arbitration awards are not self-enforcing . . . thus, while we have spoken in broad terms of deference to private agreements to arbitrate, we have always done so with an awareness of the confirmations-and-vacatur safety net that hangs below." *Hoeft v. MVL Group, Inc.* 343 F.3d 57, 63. (2d Cir. 2003) "An agreement that contemplates confirmation but bars all judicial review presents serious concerns...the integrity of the arbitration process could be compromised, if parties could require that awards, flawed for any of these reasons [in FAA], must nevertheless be blessed by federal courts. Since federal courts are not rubber stamps, parties may not, by private agreement, relieve them of their obligation to review arbitration awards for compliance with Section 10(a)." *Id* at 64. "Parties may not interfere with the judicial process by dictating how the federal courts operate." *Id*. at 65.

Gonzalez and Jennifer Melton, who were Respondent's witnesses; and Daniel Kaplan, who was called as a rebuttal witness by Petitioners.

51. On November 16, 2021, the Panel rendered the Award, which in sum and substance denied the Kaplans' requests for expungement of their Form U5s. *See* Ex. 4.

52. The Award provides no explanation or reasoning whatsoever for its conclusion. The entirety of the subsection captioned "Award" provides as follows:

> After considering the pleadings, the testimony and evidence presented at the hearing, and any post-hearing submissions,[9] the Panel has decided in full and final resolution of the issues submitted for determination as follows: (1) Adam Scott Kaplan's request for expungement of the Form U5 from registration records maintained by the CRD is denied. (2) Daniel Even (sic) Kaplan's request for expungement of the Form U5 from registration records maintained by the CRD is denied.

Ex. 4, pg.2.

53. Notwithstanding the short duration of the hearing, the proceedings were nevertheless infected with prejudice, unfairness, and misconduct that compel vacatur of the Award. As described hereinbelow, some of these factors were apparent at the time of the Arbitration. Unfortunately, others were not discovered until after the hearing was complete and the damage to Petitioners' interests was done.[10]

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[9] There were no post-hearing submissions filed by either side.

[10] Petitioners intend to presently file a letter requesting limited discovery in connection with this proceeding, pursuant to Rules 26 and 45 of the Federal Rules of Civil Procedure (which are applicable to proceedings to confirm and/or vacate awards under the FAA, *see* Fed. R. Civ. P. 81(a)(6)(B)), in order to further assess the scope of Chairman Schmertz's conflict of interest and his failure to disclose the same, as well as Merrill's knowledge of and/or failure to disclose the conflict. It would not have been possible for Petitioners to fully investigate this issue prior to filing, given the statutory time limitation requiring them to do so within 3 months of service of the award on November 16, 2021. Courts regularly authorize limited discovery in such circumstances, where the information sought is "relevant and necessary" to the showing of an arbitrator's conflict or bias. *See, e.g.*, *Frere v. Orthofix, Inc.*, 2000 WL 1789641 (S.D.N.Y. 2000); *Lyeth v. Chrysler Corp.*, 929 F.2d 891, 898-99 (2d Cir. 1991); *Sanko Steamship Co. v. Cook Industries*, 495 F.2d 1260, 1264-65 (2d Cir. 1973); *National Hockey League Players' Assn'n v. Bettman*, No. 93-CV-5769 (KMW), 1994 WL 38130 (S.D.N.Y. Feb. 4, 1994) (citing

ARGUMENT

A. The FINRA Arbitration Was Fatally Flawed and Must Be Vacated

54. While vacatur should not be granted haphazardly, "deference to arbitrators is not without its limits." *Jock v. Sterling Jewelers, Inc.*, 143 F. Supp. 3d 127, 133-34 (S.D.N.Y. 2015) (Rakoff, J.), *vacated on other grounds*, 2017 WL 3127243, at *2 (2d Cir. Jul. 24, 2017). "[A] ruling lacking 'barely colorable justification' in black-letter law or common sense" need not be "upheld purely because it issued from an arbitrator's pen." *Id*. (internal citation omitted); *see Porzig v. Dresdner, Kleinwort, Benson, N. Am. LLC*, 497 F.3d 133, 139 (2d Cir. 2007) ("A decision of an arbitrator . . . is not totally impervious to judicial review").

55. The district court "may make an order vacating the award . . . (1) where the award was procured by corruption, fraud, or undue means; (2) where there was evident partiality or corruption in the arbitrators, or either of them; (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made." 9 U.S.C. § 10(a).

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cases); *Pollak & Co. v. Shelgem Ltd.*, No. 90-CV-4532 (JFK), 1993 WL 248804 (S.D.N.Y. June 30. 1993); *I.A.M. Nat'l Pension Fund Benefit Plan A v. Allied Corp.*, 97 F.R.D. 34, 36 (D.D.C. 1983); *Andros Compania Maritima, S.A. v. Marc Rich & Co., A.G.*, 579 F.2d 691, 702 (2d Cir. 1978). Furthermore, as the Court is likely aware, Merrill merged in recent years with Bank of America, and thus the scope of Schmertz's conflict – which Petitioners have not yet had the opportunity to investigate – may also extend to involvement on the part of Bank of America, which would be imputed to Merrill as well. Upon information and belief, Bank of America may be involved in marketing efforts relating to Hopscotch Air, a business in which Schmertz has a disclosed ownership interest.

56. Under the law of this Circuit, § 10(a)(4) is implicated where the Award is fundamentally unfair because a law is manifestly disregarded.

57. Even if no one factor demanded vacatur, an accumulation of factors under 9 U.S.C. § 10(a) can together surpass the threshold needed to vacate due to the fundamental unfairness of the award, as set forth further below. *See, e.g., Porzig*, 497 F.3d at 140.

58. Here, Petitioners do not contend that the Award was procured by corruption, fraud, or undue means. However, as set forth below, Petitioners have a strong basis for believing: (a) that there was evident partiality in Andrew Schmertz, the Panel Chairman; (b) the Panel's decision to admit evidence that should not have been considered was fundamentally unfair and prejudiced the Petitioners' rights to a fair hearing; and (c) the Panel's Award in favor of Merrill was fundamentally unfair because it manifestly disregarded relevant rules and regulations – to wit, the absence of any rule or regulation prohibiting the conduct for which the Petitioners were terminated, as well as the lack of any nexus that could credibly make Petitioners' conduct "investment-related."

a. The Chairman of the Arbitration Panel Was "Evidently Partial" to Petitioners' Detriment

59. First and foremost, the Arbitration was unfair, and the Award must be vacated, because Panel Chairman Andrew Schmertz failed to disclose a material, direct conflict – described in detail below – that would and should have resulted in his exclusion from consideration for the Panel. Not only did Chairman Schmertz fail to disclose this conflict at any time prior to the hearing – including in connection with any of the two pre-hearing meetings that the Panel and the parties conducted during the months after Schmertz was empaneled – he confirmed at the outset of the hearing both that the parties knew of no conflicts and that the panelists themselves were neutral. Ex. 5, 3:2-3; 6:5-18.

60. In his ADR, Schmertz listed his employment history from June 1991 through the date of the ADR affirmation - *i.e.*, March 25, 2021. *See* Ex. 6. Schmertz included twenty-one entries under "disclosure/conflict information," including such banal disclosures as his Twitter handle, but never once made mention of Merrill. *Id*. Petitioners thus had absolutely no reason to believe that the Chairman had any form of conflict.

61. The fact that Schmertz omitted all information about his history and ties with Merrill strongly suggests that Schmertz knew that his relationship to Merrill would be material to the Kaplans.

62. During the hearing, Petitioners were naturally disappointed by the rulings on the admissibility of certain documentary evidence and testimony proffered by Merrill. At the close of the proceedings, however, Petitioners were heartened that at least one member of the Panel, panelist Rutman, seemed to have appreciated the gravamen of their substantive argument that Merrill's disclosures could not be appropriate because Petitioners' alleged conduct did not violate any extant rule or regulation.

63. That disappointment then turned to shock when the Award was rendered on November 16, as the Panel had evidently ignored the fact that there was no relevant rule violated, and by implication had credited the evidence that Merrill improperly presented.[11]

64. Petitioners, who had previously relied upon the panelists' ADRs as a guarantee of their impartiality, began to investigate independently.

[11] Because the Panel failed to explain its decision in any way, Ex. 4, Petitioners can ask this Court to draw reasonable inferences from the mere fact of the decision in Respondent's favor, including that the Panel must have credited the evidence presented by Merrill.

65. This investigation revealed for the first time Chairman Schmertz's conflict, as Petitioners discovered a number of documents and contexts in which Schmertz had identified himself as a past employee of Merrill Lynch.

66. Specifically, Schmertz – who has a varied professional background, including as a video producer and as the owner of a private jet company, Hopscotch Air, Inc. – identified himself in a 2020 filing with the United States Department of Transportation ("USDOT"), on behalf of Hopscotch Air, which was made under penalty of perjury, as having been employed as a "Producer with Merrill Lynch Corporate Video Services." Ex. 8.

67. Similarly, in a 2006 news article regarding individuals and entities who received loans to help with recovery from the September 11 attacks, Schmertz identified himself as having been employed producing webcasts for Merrill and stated that he had obtained a loan to replace damaged equipment that was in Merrill's offices at One World Financial Center at the time. Ex. 9.

68. Multiple documents filed by Schmertz and others further reveal that Schmertz had produced videos for various entities that were sponsored by Merrill Lynch. For instance, a annual "Report to the Community" released by WNET PBS Thirteen for 2008-2009, identified Schmertz as a content producer, with funds provided in part by contributions made by Merrill Lynch and Bank of America. Ex. 10, pgs. 23, 44. According to WNET's Report to the Community, *at the time* that Schmertz was Creative News Group LLC's, Managing Director, Merrill is listed as having donated greater than $1 million to WNET PBS Thirteen, in addition to its other gifting to the organization. Ex. 10, pg. 23, 44, 53. And, similarly, Schmertz's own professional biography – as it appeared in October 2008 on the website for Creative News Group LLC (of which Schmertz was, at the time, a Managing Director), and which is maintained

presently in the Center for Media and Democracy's "SourceWatch" database – identifies him as having co-produced and hosted inflight business news programming for British Airways which were sponsored by Merrill Lynch. Ex. 11.

69. While Chairman Schmertz's ADR listed his affiliations with Creative News Group, LLC and Hopscotch Air, Inc., it made no mention of any affiliation with Merrill Lynch – even though, as evinced by the 2020 USDOT filing referenced above, Chairman Schmertz was aware of the connection as recently as 2020. *See* Ex. 8.

70. Had Petitioners been even the slightest bit aware of Chairman Schmertz's prior employment and association with Merrill, they never would have consented to proceed with an arbitration with him as one of the panelists, much less as the Chairman. But more to the point: Chairman Schmertz had every opportunity to disclose this obvious, known conflict, and never did so despite being otherwise comprehensive in his ADR.[12]

71. This clear conflict, combined with Schmertz's failure to disclose it, is independently adequate, under precedent in this district and circuit, to amount to "evident partiality" and to warrant vacatur. *See Applied Indus. Materials Corp. v. Ovalar Makine Ticaret Ve Sanayi, A.S.*, 492 F.3d 132, 137 (2d Cir. 2007) (where "[a]n arbitrator ... knows of a material relationship with a party" but fails to disclose it, "[a] reasonable person would have to conclude that [the] arbitrator who failed to disclose under such circumstances was partial to one side.");

[12] Moreover, Merrill itself would have been in the best position of anyone to have known of its own prior employment of Schmertz, and thus had actual (or at least constructive) knowledge of Schmertz's conflict. Petitioners, as noted above, will seek discovery in connection with this conflict, including both Schmertz's knowledge and Merrill's. Petitioners note that another financial institution, Wells Fargo, was recently caught by a court in Georgia executing a scheme to secretly cull the pool of arbitrators in order to reduce the number of neutral arbitrators available to its opponents and ensure favorable panels. *Bryan Leggett and Bryson Holdings, LLC v. Wells Fargo, et al.*, Case No. 2019-cv-328949 (Fulton Cty. Super. Ct. Jan. 25, 2022).

see also Scandinavian Reins. Co. v. Saint Paul Fire & Marine Ins. Co., 668 F.3d 60, 72 (2d Cir. 2012) ("Among the circumstances under which the evident-partiality standard is likely to be met are those in which an arbitrator fails to disclose a relationship or interest that is strongly suggestive of bias in favor of one of the parties.").

72. Upon information and belief, as it is standard practice for parties to an arbitration to run comprehensive conflict checks of all potential arbitrators through their firm, company or personal databases, Merrill likely ran such a conflict check for Schmertz (and the other potential panel members) before agreeing to their appointment. Upon information and belief, such a conflict search would or should have revealed a conflict between Merrill and Schmertz.[13]

73. Moreover, Chairman Schmertz's failure to disclose the conflict amounts to "misbehavior" within the meaning of 9 U.S.C. 10(a)(3). *Avis Rent A Car Sys., Inc.* v. *Garage Employees Union*, 791 F.2d 22, 25 (2d Cir. 1986) (vacatur proper for "awards entered by arbitrators whose qualifications or method of appointment fail to conform to arbitration clauses"); *Move, Inc.* v. *Citigroup Global Markets, Inc.*, 840 F.3d 1152, 1159 (9th Cir. 2016) (party was "prejudiced by the inclusion of an arbitrator" who "should have been disqualified from arbitrating the dispute in the first place.").

74. Further, the information herein concerning Schmertz's undisclosed relationship with Merrill is merely what was gleaned from Petitioners' preliminary investigation. This uncovered information is just the tip of the iceberg and indicates that there are other undisclosed facts Petitioners have yet to discover.

[13] Yet, Merrill affirmed at the outset of the arbitration hearing that it knows of no conflict in any of the arbitrators. Ex. 5, 6:5-18.

75. Alternatively, even if Chairman Schmertz's conflict, standing alone, were not sufficient to warrant vacatur, an accumulation of factors under 9 U.S.C. 10(a) can together surpass the threshold needed to vacate, as set forth further below. *See, e.g., Porzig*, 497 F.3d 133.

b. The Arbitration Was Fundamentally Unfair Because the Panel Improperly Admitted Respondent's Evidence That Should Not Have Been Admitted

76. Second, the Award must be vacated because the Panel allowed evidence to be presented in a manner that was grossly unfair and prejudicial to Petitioners.

77. Specifically, during the course of the Arbitration, Merrill sought to introduce – and was allowed to introduce through the testimony of its witness, Jennifer Melton – a demonstrative exhibit purporting to show the Kaplans' repeated access to clients' MyMerrill accounts, using the Kaplans' own electronic devices.

78. The demonstrative exhibit, and Ms. Melton's testimony, summarized evidence involving so-called "e-signatures" that allegedly would have indicated when, and from what device, the account logins had occurred.

79. However, as noted by Petitioners' counsel during the hearing, Ex. 5, 53:10-54:6, the evidence to which Ms. Melton testified was sprung upon Petitioners at the last moment – scarcely 24 hours before the hearing, even though formal and informal discovery had been going on for over three years since the Kaplans were terminated in March 2018. That is, the "e-signature" topic had never been mentioned before in the proceedings or discovery. Moreover, as noted above, the demonstrative itself did not reference the Bates numbers of the documents upon which Merrill relied in creating the demonstrative, which was further to the Kaplans' detriment and prejudice.

80. Furthermore, Ms. Melton was allowed to testify as a pseudo-"expert" in analyzing and assessing the sort of data that was gathered and presented in the summary demonstrative,[14] whereas the Kaplans were given no opportunity – because the evidence, again, had been presented to them at the eleventh hour – to counter her testimony with a so-called "expert" of their own.

81. The Panel's decision to allow this evidence was unjust given the manifest unfairness to Petitioners and the favoritism it exhibited towards Merrill. In this case, the injustice is even worse: the parties had expressly stipulated that in order for evidence to be admissible at the hearing, it had to be exchanged twenty days before the hearing date – including any evidence underlying demonstrative exhibits, which themselves had to be provided in advance of the hearing. *See* ¶ 52, *supra*, and Ex. 7.

82. The Parties further had stipulated that "neither Party shall offer expert testimony or seek to qualify any witness as an expert," yet Merrill did precisely that with the testimony of Ms. Melton. *See generally* Ex. 5, 300:4-314:17.

83. Although the Award includes little explanation of the Arbitrators' basis for their findings, it is legitimate to assume that the Panel concluded that the Kaplans were in fact terminated for the reason that Merrill stated on their U5s, and moreover that the stated reason was a valid one.

84. While the latter conclusion, as argued below, does not have merit in any case, the former conclusion could have been reached only if the Panel credited the evidence introduced through the demonstrative and through Ms. Melton's testimony. As this evidence should not

[14] Two panelists, Schmertz and Gellis, refer to Ms. Melton as an "expert" in the hearing. Ex. 5, 303:5-11; 312:11-313:12. Further, counsel for Merrill referred to Ms. Melton as an "expert" in his closing argument. Ex. 5, 486:14-16.

have been considered, it was fundamentally unfair for the Panel to allow it, and to render an Award against Petitioners that was evidently based upon it.

85. This alone would be enough to warrant vacatur – which, although not common, is granted where the Panel has unfairly stripped one party of the opportunity to adequately present or defend his case. *Tempo Shain Corp. v. Bertek, Inc.*, 120 F.3d 16, 21 (2d Cir. 1997) (vacating the award due to fundamental unfairness because "although [he] is not required to hear all the evidence proffered by a party, an arbitrator must give each of the parties to a dispute an adequate opportunity to present its evidence and argument").

86. Together with the evident partiality of Chairman Schmertz, as detailed in Paragraphs 59 to 72, *supra*, there are abundantly sufficient grounds to vacate the Award. *See Porzig*, 497 F.3d 133.

c. The Panel Manifestly Disregarded Relevant Rules and Regulations in Allowing Merrill's U5 Designations to Stand When the Kaplans Did Not Violate Any Existing Rules or Laws

87. Third, the Panel's decision, in its manifest disregard for applicable law, amounts under this Circuit's precedent to the Panel having "exceeded their powers," and thus is an additional, independent ground for vacatur.

88. Because Merrill's selection of "Yes" in response to Question 7F (1) on the Kaplans' Form U5s – which asks whether they were terminated for "investment-related" violations of laws, rules or regulations – was apparently false and dishonest, the Panel, in confirming Merrill's conduct via the Award, necessarily disregarded applicable law.

89. To wit, there was *no evidence* offered at the hearing that Merrill terminated the Kaplans, on March 8, 2018, for "investment-related" reasons.

90. Moreover, there was *no evidence* offered at the hearing that the conduct Merrill *did* terminate the Kaplans for – allegedly accessing client accounts through the MyMerrill portal on numerous occasions – was a violation of any internal Merrill rule or regulation, or of any FINRA rule or regulation. Ex. 5, 231:20-236:5.

91. Merrill further admitted that it changed its internal rules to prohibit its advisors from accessing clients' MyMerrill accounts through the advisors' own devices *after* the Kaplans were terminated. Ex. 5, 235:14-236:5. Upon information and belief, no FINRA rule prohibits the conduct that the Kaplans allegedly engaged in.

92. As explained above, Petitioners believe that the essential reason they were terminated by Merrill was that the acrimonious circumstances of their departure from Morgan Stanley, their prior employer, had clouded their employment at Merrill from day one. Customer complaints – which the Kaplans argued at the hearing were likely instigated by Morgan Stanley in retaliation for leaving the firm with their clients – and a pending FINRA arbitration concerning their departure from Morgan Stanley – which the Kaplans won – caused Merrill to have to supervise them closely, which was an undesirable burden for Merrill.

93. In other words, the reason given by Merrill (in response to Question 3 on the Form U5s) for the Kaplans' termination was pretextual – the supposed "evidence" of their having improperly accessed client accounts by logging on to MyMerrill did not exist (or was not known to Merrill) at the time the Kaplans were terminated[15] – but moreover, even taken at face value, it is neither "investment-related" nor a violation of any applicable rule or regulation.

[15] At the time that Merrill terminated the Kaplans, there had been only one customer who had reportedly suggested that the Kaplans had logged into her MyMerrill account. There exists good reason, however, to cast doubt on the credibility of that customer, which reason Merrill was aware of at the time. The customer, Mengfei Song, had used multiple different aliases, and had engaged in erratic behavior, such as displaying photographs of herself with handguns on social

94. Merrill merely alleged that the Kaplans logged in, looked around at accounts and did not make any trades or take any other action that could be perceived as or understood to be investment-related. Indeed, testimony at the hearing confirmed that the Kaplans *could not have* made any trades or investment decisions with the access they allegedly obtained through the MyMerrill logins; moreover, the Kaplans could have obtained the same level of access to client accounts – that is, the ability to view them, but not take any actions – by logging in to their own accounts as financial advisors. Ex. 5, 103:13-105:22, 106:9-107:8.

95. This notwithstanding, the Panel nevertheless rendered an Award that effectively *sub silentio* legitimized Merrill's U5 filings, which stated that the Kaplans were terminated for investment-related reasons, and that those investment-related reasons were the improper access to the MyMerrill accounts of their clients using the Kaplans' own electronic devices.

96. There is simply no logical explanation for this – certainly, the Award itself does not provide one. It defies common sense: conduct cannot be "investment-related" if there *was no relation to an investment*, and conduct cannot violate a rule or regulation if that rule or regulation *does not exist*.

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media. Eventually—for reasons entirely unrelated to the Kaplans—Merrill investigated Ms. Song for fraud. Nevertheless, this customer provided Merrill with a letter after the Kaplans had been terminated – as did many other of the Kaplans' clients – avowing that the Kaplans had never accessed her account without her permission, and that if they had ever used her login information from their own electronic devices, it was in her presence and with her full authority. This information was presented to the hearing Panel; thus, a reasonable factfinder could not have found credible Merrill's claim that they terminated the Kaplans for "investment-related" reasons (namely, accessing the MyMerrill platform) based solely on this isolated claim, which was the only one that involved the improper use of customer login information. *See, e.g.*, *Duferco Int'l Steel Trading* v. *T. Klaveness Shipping A/S*, 333 F.3d 383, 390 (2d Cir. 2003) (the court "will *infer* knowledge and intentionality on the part of the arbitrator" where the court identifies "an error that is so obvious that it would be instantly perceived as such by the average person qualified to serve as an arbitrator." (emphasis added); *see also Capo* v. *Bowers*, 2001 WL 36193449, at *4 (S.D.N.Y. Mar. 12, 2001) (vacating award).

97. In order to vacate an award on the ground of "manifest disregard," a court should find both that: (i) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether; and (ii) the law ignored by the arbitrators was well-defined, explicit and clearly applicable to the case. *DiRussa v. Dean Witter Reynolds Inc.*, 121 F.3d 818, 821 (2d Cir. 1997).

98. Petitioners submit that this principle is no less applicable when the arbitrators knew of the *absence* of a governing legal principle and ignored the fact of that absence. Petitioners' contention, at the hearing, that Merrill had no rule or regulation precluding the conduct they allegedly engaged in[16] was uncontested. Ex. 5, 109: 2-22.

99. Thus, the arbitrators "knew of the rule"; the rule was "clearly applicable to the case"; and, evidently, the arbitrators "refused to apply it or ignored it altogether."

100. The fact that Petitioners cannot determine whether the arbitrators "refused to apply it" or "ignored it altogether," given the absence of any reasoning contained in the arbitral Award, is of no moment. In fact, this counsels *against* giving deference to the Award, and in favor of vacatur. *See Halligan* v. *Piper Jaffray, Inc.*, 148 F.3d 197, 204 (2d Cir. 1998) ("[W]here a reviewing court is inclined to find that arbitrators manifestly disregarded the law or the evidence and that an explanation, if given, would have strained credulity, *the absence of explanation may reinforce* the reviewing court's confidence that the arbitrators engaged in manifest disregard.") (emphasis added).

101. Moreover, Petitioners submit that deference is particularly inapt here given the overarching tarnish left on the Panel's credibility by the Chairman's undisclosed conflict. To the extent that one should search for a reasonable explanation for the Panel's unreasonable disregard

[16] To reiterate, Petitioners deny Merrill's allegations regarding the Kaplans' conduct.

for its obligations, Petitioners have presented this Court with such an explanation in the form of Chairman Schmertz's "evident partiality."

FIRST CLAIM FOR RELIEF
(Vacatur of Award pursuant to 9 U.S.C. 10(a))

102. Petitioners repeat Paragraphs 1 through 101 as though fully set forth herein.

103. The Federal Arbitration Act describes four statutory bases for vacating an arbitration award. Three of the four are implicated here, both independently and collectively.

104. First, a court may enter "an order vacating the award upon the application of any party to the arbitration . . . where there was evident partiality or corruption in the arbitrators." 9 U.S.C. § 10(a)(2).

105. In the instant case, this stands alone as an independent ground for vacatur, given that the Chairman of the Panel failed to disclose a clear conflict.

106. To wit, Chairman Schmertz had previously represented in various ways that he was employed by Respondent, but failed to disclose this conflict to Petitioners.

107. In this light, the further grounds provided in the FAA are brought into sharper relief, and themselves – or together with the Chairman's evident partiality – constitute sufficient bases for vacatur.

108. Specifically, the "arbitrators were guilty of . . . refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced." 9 U.S.C. § 10(a)(3).

109. To wit, the Panel improperly allowed testimony at the hearing that violated the parties' stipulation regarding the same and thus unfairly surprised Petitioners, who did not have a chance to prepare to confront the evidence or offer countermanding evidence, including expert testimony of their own.

110. And, finally, the arbitrators "exceeded their powers," within the meaning of 9 U.S.C. § 10(a)(4), in that they showed "manifest disregard" for applicable rules and regulations by countenancing Respondent's statement that Petitioners were terminated for violating standards that did not even exist; and on the basis of evidence that did not exist at the time of their termination; and that the supposed violations were "investment-related" when they plainly were not.

111. To wit, at the time Petitioners were terminated, there was no rule or regulation that would have prevented them from accessing client accounts using client login credentials from Petitioners' own electronic devices, yet the Panel found that Merrill was justified in stating on Petitioners' U5s that they were terminated for violating investment-related laws, rules, or regulations.

PRAYER FOR RELIEF

WHEREFORE, Petitioners Adam and Daniel Kaplan respectfully pray that this Court:

(i) Vacate the Award in its entirety; and

(ii) Award such other and further relief as this Court deems just and proper.

Dated: New York, New York

February 16, 2022

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