IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MERRILL LYNCH, PIERCE, FENNER & SMITH INCORPORATED, **Applicant,** **v.** **JOHN MICHAEL PALOMBO,** **Respondent.**	**Civil Action No. 4:21-cv-04256**

RESPONDENT JOHN MICHAEL PALOMBO'S
MOTION TO VACATE ARBITRATION AWARD

Respondent John Michael Palombo ("John Palombo"), pursuant to Section 10 of the Federal Arbitration Act ("FAA"), 9 U.S.C. §1, *et seq.*, hereby moves to vacate the underlying arbitration award ("Award") in its entirety and order a rehearing before new arbitrators.

Dated: February 11, 2022

Respectfully submitted,

/s/ Jeremy M. Halpern

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I. INTRODUCTION

John Palombo wants to exercise his right to arbitrate his claims and prove that Merrill Lynch defrauded him into joining the Client Transition Program ("CTP"). Instead, the panel of arbitrators ("Panel") committed misconduct by refusing to hear any evidence from John Palombo for his claims for fraudulent inducement, and exceeded their authority by not postponing the final hearing. After the Panel dismissed John Palombo's claims without allowing him to submit evidence, John Palombo moved for reconsideration, and the Panel denied the request without explanation.

The Panel then destroyed John Palombo's chance at a fair hearing by refusing to reschedule or postpone the final hearing until John Palombo's counsel was available. In October 2021, the parties provided the arbitrators with four agreed dates to reschedule the final hearing for dates in 2022. The arbitrators ignored these dates, violating the forum rules, and set the hearing only six weeks out. Moreover, the Panel selected that date knowing that John Palombo's counsel was unavailable. Despite this showing of sufficient cause, the arbitrators did not move the final hearing. John Palombo then asked the director of FINRA Dispute Resolution for an emergency postponement, and his request was denied without explanation. John Palombo's counsel was eventually able to make herself available, but could only begin preparing less than three weeks before the hearing.

The Panel then cruelly exceeded its authority based upon the rulings within the Award. The Panel ordered John Palombo to claw back all non-salary compensation he received for the entire term of his CTP Agreement and give it to Merrill Lynch, thus creating a *de facto* rescission of the agreement. However, the Panel still chose to enforce

all of the terms of the CTP against John Palombo for which he received no compensation. This *de facto* rescission makes two elements of the award legally impossible. The Panel rescinded the contract and yet simultaneously upheld the release provision therein (used as the basis to dismiss John Palombo's claims). Likewise, by rescinding the contract, the Panel exceeded its authority by awarding attorney's fees pursuant to a Texas statute that requires an enforceable contract in place. These legal contradictions prove that the Panel ruled on issued not presented to it, and thus acted outside the scope of its authority.

Finally, the Award was in part the product of fraud by Merrill Lynch's counsel. The Panel's decision on the Motion to Dismiss clearly relied upon false representations by Merrill Lynch's counsel about the factual record, as no facts had been stipulated by the parties or evidence had been submitted in the record. These false statements were made with the intent for the Panel to rely upon them, which the Panel clearly did based upon the language of their orders, and thus the Award was procured by fraud.

II. FACTUAL AND PROCEDURAL BACKGROUND

a. John Palombo Joins Merrill Lynch

John Palombo is a registered representative through the Financial Industry Regulatory Authority ("FINRA"), with whom he carries multiple licenses that permit him to conduct securities trades and provide investment advice. John has been licensed through FINRA since 1995, and has worked at several major broker/dealers. John Palombo and his wife, Susan Palombo, are sophisticated individuals with one another's business and financial interests at heart. John has worked with Susan throughout his career. The two worked together prior to John entering the financial services industry. When John entered

the financial services industry, Susan separately earned her MBA. John joined the Minneapolis, MN branch of Merrill Lynch in 2008, Susan followed shortly thereafter. Susan obtained her industry licenses in 2012, and earned other designations such as CFP® and CIMA®. John and Susan relocated to Austin, TX in August 2014, where they remained employed with Merrill Lynch at a new branch. They continued their success in the Austin, TX branch until a change in local management eventually prompted the events that were covered in the underlying arbitration.

b. John Palombo Seeks an Exit

After a few years in Austin, TX, a change in local management resulted in numerous conflicts. John's disability created tensions when the building security failed to accommodate his transportation requirements, and Merrill Lynch seemingly looked for ways to pin John for any kind of blame. As outlined in the pleadings of the underlying arbitration, John Palombo was the recipient of discrimination by Merrill Lynch based upon his disabilities.

John Palombo did not want his conflicts with management to interfere with the success of the Palombos as a team. John and Susan worked together as part of a team generating over $1.7 million in annual revenue for Merrill Lynch, and received valuable compensation for their hard work. John and Susan had a continuing mutual interest of maximizing their joint compensation—the method of how Merrill Lynch divvied the compensation between them was largely irrelevant. The timing of this conflict was somewhat fortuitous, as the two had already planned on transitioning leadership of the business from John to Susan. The question was how the Palombos would effectuate this

transition. In August 2018, John and Susan Palombo began requesting information about the options available to transition the book of business from John to Susan.

c. The Palombos Evaluate Their Options

Merrill Lynch presented John and Susan with two main choices for how John could transition the book of business to Susan. The first choice was for John and Susan to use a modified team agreement. Under the "team option," all of the Palombo's revenue would be placed under a team number from which Susan would receive 99% of the compensation and John would receive 1%. The team option allowed John to continue operating as a registered representative while turning over active day-to-day responsibilities to Susan Palombo. John could exit the industry on his own terms. Most importantly, if the situation at Merrill Lynch became unpleasant, John and Susan could leave Merrill Lynch at any time and solicit their book of business in compliance with industry standards.

The second choice was for John and Susan to enter Merrill Lynch's CTP. The program was created as a way for a retiring advisor to pick a younger advisor to transfer his or her book, in exchange for compensation from the receiving advisor. From John's perspective as retiring advisor, his compensation drops significantly and immediately. His title changes to "Senior Consultant," and he is required to maintain his licenses to help transition customers to the receiving advisor, Susan, over the next two years. The retiring advisor is required to terminate his employment after those two years. The CTP then continues to pay John for three years after retirement. From Susan's perspective, although her attributed revenue goes up substantially, her commissions do not keep pace. The CTP

forces Susan to take a significant reduction in pay for five full years; the proceeds from this pay cut are used to pay John in retirement.

From Merrill Lynch's perspective, the total compensation paid to John and Susan under the CTP is somewhat similar—though appreciably higher—to what Merrill Lynch previously paid just to John. The CTP calculates total compensation based on revenue from John's book of business. However, the CTP allocates that compensation between both John and Susan. When operated as designed, the impact to Merrill Lynch of the CTP is essentially cost-neutral. To ensure things operate as designed, John and Susan would either sign releases, agree to various restraints of future conduct, or both.

d. Merrill Lynch Commits Fraud

Merrill Lynch presented John and Susan Palombo with information designed to induce them to enter into the CTP. According to Merrill Lynch's projections, John and Susan would make significantly more money as a couple by entering the CTP than by using the team option. Although Susan would make far less per year under the CTP, the reduction would be offset by increases to John's compensation.

John and Susan repeatedly exchanged correspondence with employees who administrated the CTP to ensure that the projections were accurate. Several errors were discovered in the initial drafts. Merrill Lynch's calculations were critical to the Palombos' decision—participating in the CTP meant agreeing to significant restraints on future conduct (including their ability to move to the competition) along with releasing Merrill Lynch of liability for its past bad conduct. By comparison, the "team option" would allow John and Susan to move freely throughout the industry and maintain any claims for

discrimination. After repeated assurances as to the accuracy of the calculations, John and Susan agreed to enter the CTP.

However, Merrill Lynch deliberately lied to John and Susan Palombo to induce them to join the CTP. Once John and Susan entered the program, they quickly discovered the ruse. Susan's compensation was not calculated using the same metrics provided during negotiations. Moreover, John's new role was revealed to be a demotion—with his new title of "Senior Consultant" he was no longer able to perform the same tasks under the CTP. John and Susan repeatedly complained to Merrill Lynch management about the errors in an effort to have their compensation and roles align with what was promised.

e. John Palombo Initiates Arbitration

After repeatedly arguing with management with no results, John Palombo retained counsel and filed a Statement of Claim in FINRA Arbitration after only 16 months of the 5-year term of the CTP.[1] In short, the bedrock allegation of the Statement of Claim was that Merrill Lynch fraudulently induced John Palombo to enter into the CTP Agreement. John Palombo's Statement of Claim sought two types of relief. First, John wanted to rescind the CTP Agreement on the basis that he was fraudulently induced into signing it, and sought to recover damages associated with the reduction of his compensation from entering into the CTP. Second, once the CTP was rescinded, John Palombo wanted to recover damages for the discrimination claims against Merrill Lynch that he had previously waived under the CTP Agreement.

[1] Exhibit 1 hereto is a Declaration of John Michael Palombo ("Declaration"). A copy of the Statement of Claim is attached to the Declaration as Exhibit A.

John and Susan Palombo were both active employees of Merrill Lynch at the time John initiated the arbitration.[2] After fighting with management for 16 months, John Palombo had exhausted all other resources to overturn the CTP Agreement. The arbitration was the final step in John Palombo's attempt to rescind the agreement, receive the compensation that was rightfully his, and pursue his claims for discrimination. In the alternative, John Palombo wanted to ensure that he and Susan Palombo were paid the full benefit of their bargain, allowing Susan to work at Merrill Lynch for years to come.

f. FINRA Arbitration – Discovery and the Motion to Dismiss

Discovery in FINRA Arbitration is different from courts or other arbitration forums. The FINRA Code of Arbitration Procedure ("FINRA Code") requires that all testimony take place during the final hearing itself, and does not permit interrogatories or depositions. The only pre-hearing discovery permitted under the FINRA Code is the production of documents and the identification of witnesses. Due to these limitations, adjudicating claims in FINRA before the final hearing is severely limited. Motions for Summary Judgment simply do not exist within the FINRA Code. The rules are designed so that parties are allowed to present their full case in chief at the final hearing.

Shortly after arbitration began, Merrill Lynch filed a Motion to Dismiss most of John Palombo's claims. The FINRA Code explicitly states that pre-hearing motions to dismiss are discouraged in arbitration.[3] Pre-hearing motions to dismiss may be granted in only four situations, one of which was cited by Merrill Lynch: if the non-moving party

[2] The BrokerCheck Reports for John and Susan Palombo are attached to the Declaration as Exhibit B.
[3] FINRA Code, Rule 13504(a)(1). (https://www.finra.org/rules-guidance/rulebooks/finra-rules/13504)

previously released the claim in dispute by a written release[4]. Merrill Lynch argued that the CTP Agreement included an enforceable release, and so John Palombo's claims should be dismissed.[5] John Palombo's response was that the release was in a contract that was procured by fraud, and thus the release cannot be enforced.[6] Merrill Lynch alleged in response John Palombo's conduct subsequently ratified any alleged fraud.[7] Accordingly, the questions before the Panel were ones of fact. Merrill Lynch had to either prove that it did not fraudulently induce John Palombo to enter into the CTP Agreement, or prove when John Palombo became aware of the fraud and prove that his conduct thereafter was sufficient to ratify the CTP Agreement.

Merrill Lynch did not provide the Panel with evidence in support of its position that the contract was not the product of fraud or that a fraudulent contract was ratified by John Palombo. No testimony was entered that would verify what John Palombo did with respect to any discovery of the alleged fraud or his possible conduct thereafter. The only documents submitted to the Panel were a handful of unverified contracts and emails.

John Palombo's briefs argued that the enforceability of the contract was a question of fact that could not be decided on the papers without testimony and documentary evidence from both sides. Of course, John Palombo was unable to submit evidence in support of his position, as Merrill Lynch possessed essentially every document that would be needed to prove his case. Accordingly, motion should be denied without prejudice until

[4] FINRA Code, Rule 13504(6) (*Id.*)
[5] Merrill Lynch's Motion to Dismiss is attached to the Declaration as Exhibit C.
[6] John Palombo's Response to the Motion to Dismiss is attached to the Declaration as Exhibit D.
[7] Merrill Lynch's Reply to the Motion to Dismiss is attached to the Declaration as Exhibit E.

after the final hearing when John Palombo had the chance to conduct discovery, introduce documents into evidence, and present witnesses for testimony and cross-examination.

g. The Hearing on the Motion to Dismiss

On December 15, 2020, the Panel conducted a hearing on the Motion to Dismiss. The FINRA Code states that the official record of the hearing is the audio recording. John Palombo independently paid to have the hearing transcribed.[8]

No evidence of any kind was presented to the Panel, as it was a non-evidentiary hearing. Neither party presented affidavits or deposition transcripts. Neither party produced admissions or interrogatory responses. John Palombo did not address the documents presented by Merrill Lynch, because he could not—there were no witnesses available to question or cross-examine concerning the content or veracity of the documents.

John Palombo's counsel repeatedly argued that the enforceability of the waiver, and thus the Motion to Dismiss based upon that waiver, was an issue of fact.

> "It's up to this panel, as a matter of fact, to determine if this was a valid contract or if we assert it was not […] but how can you decide that without a hearing on the merits? You cannot determine the validity of the waiver until Mr. Palombo's received full discovery and has been able to provide you the evidence that you'll require to make this decision" (Transcript, p. 19)

> "The waiver included in the CTP agreement cannot deem to be valid when the validity of the agreement itself is what is at issue in this arbitration; thus, the waiver cannot be deemed to be valid at this stage of the litigation and this motion must be denied." (*Id.*, p. 23)

John Palombo's position was unwavering—without a chance to present evidence, the Panel could not make a determination of fact as to whether the release was enforceable.

[8] A copy of the transcription ("Transcript") is attached to the Declaration as Exhibit F.

Moreover, a decision at this stage of the arbitration would completely deny him the chance to present the same evidence he would need to prove his allegations.

At hearing, Merrill Lynch argued that John Palombo ratified the release with his conduct. However, Merrill Lynch did not provide any evidence for its position. The only support was "testimony" from the attorney for Merrill Lynch:

> "[Palombo] collected more than $715,000 and performed his job as a CTP senior consultant for two full years after discovering what he now characterizes as either a mutual mistake or fraud" (Transcript, p. 12)
>
> "He acted in accordance with [the CTP] for two years." (*Id.*, p. 13)
>
> "The facts that we are relying on in our motion are entirely undisputed." (*Id.*, p. 27)

Again, no witnesses available to testify to the veracity of these statements, or for that matter, the veracity of any of the allegations by either party. Had this been an evidentiary hearing, John Palombo could have easily testified that he continually fought with management to overturn the contract up until the moment he filed his Statement of Claim. Nonetheless, John Palombo maintained his position that making a finding of fact without evidence was by its very nature premature.

h. <u>The Order of Dismissal and Subsequent Efforts to Overturn</u>

On December 16, 2020, the Panel issued its order dismissing John Palombo's claims of fraudulent inducement and for discrimination. Although the Panel had absolutely no evidence to evaluate when deliberating, the Panel nonetheless made two critical findings of fact: (1) "Claimant knowingly operated from that date under the CTP"; and (2) "[Claimant] accepted payments in accordance with [the CTP's] terms and conditions."

Based upon these so-called findings of fact, the Panel thus concluded that John Palombo ratified any fraud and thus became bound by the CTP Agreement and its provisions.

John Palombo filed a motion for reconsideration of the order dismissing his claims after a chance to conduct discovery. The motion for reconsideration was filed on August 25, 2021, and the parties fully briefed the issue.[9] On September 11, 2021, the Panel ruled on the motion. Without any explanation or justification, the motion was denied[10]:

With no other method of recourse, John Palombo filed a Motion to Vacate on October 7, 2021 in the District Court for Travis County, Texas. The basis of the motion was that the decision of the panel prevented John Palombo from presenting any evidence in support of his claims, and thus served as grounds to vacate the award. Although that motion is still pending, the present motion before this Court may render that motion moot. However, the impact of that motion would soon reveal itself in the underlying arbitration.

i. Rescheduling the Final Hearing

The final hearing for the underlying arbitration was postponed and rescheduled multiple times. To reschedule the final hearing, all parties and all members of the Panel submitted their availability to identify times when everyone could participate. The problem was finding the soonest dates when the parties, their attorneys, and all members of the Panel were simultaneously free for an entire week.

A scheduling poll revealed that the week of November 30 was available for all participants except for John Palombo. On September 15, John Palombo wrote to the Panel

[9] The briefs concerning the motion for reconsideration are attached to the Declaration as Exhibit G.
[10] The order denying the motion for reconsideration is attached to the Declaration as Exhibit H.

explaining that his attorney was occupied with a separate week-long arbitration during the week of November 30.[11] The parties conferred and offered two sets of agreed dates to postpone the final hearing. On October 7, 2021 the Panel rejected the dates because the Panel was unavailable.[12] On October 12, 2021, the parties submitted four additional sets of dates in January, February, and March 2022 for postponing the final hearing.[13] As of October 12, 2021, the final hearing had not been rescheduled for a specific date.

Later that day, after the parties had agreed to their availability for a postponed final hearing, John Palombo separately filed an emergency motion to postpone the final hearing indefinitely based upon the October 7 Motion to Vacate.[14] Merrill Lynch disputed the indefinite postponement, and reiterated its request for a postponement to one of the four jointly-agreed dates: "For all of the foregoing reasons, [Merrill Lynch] respectfully requests that the Panel deny [John Palombo's] Motion to Continue and move forward with scheduling the final hearing during the January – February 2022 dates jointly proposed by the parties."

The Panel seemingly took the motion to continue (and the motion to vacate referenced therein) as an attack on their authority. In response, the Panel vindictively denied the motion and ordered the final hearing to take place during the exact week that only John Palombo was not available—November 30 to December 4, 2021.[15] This week was not one of the four weeks agreed to by the parties for postponement of the final hearing.

[11] John Palombo's objection is attached to the Declaration as Exhibit I.
[12] Correspondence from the Panel is attached to the Declaration as Exhibit J.
[13] *See* Merrill Lynch's Objection to the Motion to Postpone, attached as Exhibit L.
[14] John Palombo's Motion to Postpone is attached as Exhibit K.
[15] The Panel's Order dated October 18, 2021 is attached to the Declaration as Exhibit M.

John Palombo immediately sent an emergency request to the director of FINRA Dispute Resolution, asking that he exercise his powers as director to postpone the final hearing and allow the parties to select dates that are available for all participants.[16] On November 2, 2021—merely 4 weeks before the hearing would start—the request was denied without explanation.[17]

> The Director of FINRA Dispute Resolution Services has reviewed the emergency request to postpone the evidentiary hearing scheduled for November 30–December 3, 2021 and all responses and replies thereto. The request is denied.

John Palombo was placed in an impossible position. Either he would have to retain new counsel with less than 4 weeks to prepare, or John Palombo's counsel would have to work a miracle to postpone the other arbitration without prejudicing her client. With only 20 days to spare, the other hearing was rescheduled. However, John Palombo's counsel was denied several additional weeks of preparation for this case due to the uncertainty of which case would take place on that date, whether she would continue representing John Palombo, and her ongoing preparations for the other case. Accordingly, John Palombo was materially prejudiced by the Panel's decision.

j. The Panel Was Financially Motivated to Deny John Palombo's Requests for Postponement

While at the final hearing, John Palombo inadvertently discovered that at least one member of the Panel was in need of quick cash, creating a direct personal financial incentive to schedule the final hearing as soon as possible. John Palombo documented his

[16] This correspondence dated October 22, 2021 is attached to the Declaration as Exhibit N.
[17] This correspondence dated November 2, 2021 is attached to the Declaration as Exhibit O.

discoveries in correspondence that was submitted to the arbitration case administrator immediately after the close of the final hearing (and before an award was entered).[18] On the first day of the hearing, John Palombo took his seat which was next to arbitrator Brian Tagtmeier. Arbitrator Tagtmeier was speaking with Chairperson Daniel Pagnano and mentioned that he had an upcoming trip to Belarus. John Palombo overheard Arbitrator Tagtmeier say he was anxious to get this hearing done so that he could use the arbitrator fees to purchase his ticket for the trip. Chairperson Pagnano laughed and stated, "yeah I hear you." Subsequent comments made by Arbitrator Tagtmeier were consistent with pushing the arbitration toward a quick conclusion, including questions about how much longer various witnesses and arguments would take. Mr. Tagtmeier also offered to conduct extra sessions in a given day to expedite the conclusion of the final hearing.

k. The Award

On December 16, 2021, the Panel issued its Award in favor of Merrill Lynch and against John Palombo.[19] The award contains multiple self-contradictions that appear to act as further unwarranted and unlawful punishment against John Palombo, and demonstrate that the arbitrators were exceeding their authority.

The Award begins by treating the CTP Agreement as an enforceable contract. The Award reiterates its position that the release was enforceable against John Palombo, and thus claims for conduct prior to December 1, 2018—the date John and Susan Palombo entered the CTP—were released. The Award references the CTP Agreement several times,

[18] This correspondence dated December 6, 2021 is attached to the Declaration as Exhibit P.
[19] The Award is attached to the Declaration as Exhibit Q.

and uses it as the foundation for its award of lost profits to Merrill Lynch, as well as attorney's fees to Merrill Lynch under Tex. Civ. Prac. & Rem. Code § 38.001.

However, the Award also appears to simultaneously rescind the CTP Agreement in its entirety. In his Statement of Claim, John Palombo requested that if the Panel does not find fraud, that the Panel award the full amounts due to him under the CTP. Instead, the Panel did the complete opposite, ordering John Palombo to repay to Merrill Lynch the entire amount of CTP compensation that he received for the entire two-year period he was operating under the program. The Panel ordered John Palombo to pay "the sum of $595,370.39 in non-salary compensation under the CTP Agreement, plus $32,541.48 in interest." This $595,000 figure was directly referenced in the December 15, 2020 hearing on the motion to dismiss, and represented all amounts that John Palombo received by virtue of his participation in the CTP. By forcing John Palombo to turn over every penny he received under the CTP, the Panel has *de facto* ordered rescission of the CTP Agreement.

In essence, the Panel exceeded the scope of its authority by going beyond the law in an effort to punish John Palombo. The Panel cannot lawfully strip John Palombo of all compensation received under an agreement while at the same time enforcing that agreement to the fullest extent possible against him. By forcing repayment of the proceeds earned thereunder, the Award makes the CTP Agreement a contract without consideration, and thus legally unenforceable.

III. LEGAL ANALYSIS

The Award in the underlying arbitration was improper and should be vacated based upon multiple violations of the Federal Arbitration Act. The legal analysis as described

below aligns with the common sense analysis from the facts above. If a party cannot present any evidence in their case, if the Panel deliberately sets a hearing at a time that the party cannot appear, if the Panel relies upon false statements about the factual record, and if the Panel awards relief that is not even legally cognizable, then it cannot be said that the party has had a meaningful opportunity to arbitrate its claims.

Under the Federal Arbitration Act, 9 U.S.C. § 1, *et seq.*, a district court may vacate an arbitration 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). These provisions are an important safety net for parties in a private arbitration. *Hoeft v. MVL Grp., Inc.*, 343 F.3d 57, 63 (2d. Cir. 2003) (overruled on other grounds); *Hall St. Assocs. v. Mattel, Inc.*, 522 U.S. 576 (2008). They protect parties from the injustice that would result if arbitrary decisions that violate the arbitration agreement or fundamental fairness were allowed to stand. See *id.*

Courts will not hesitate to vacate an award when the statutory elements are satisfied. In fact, a FINRA Arbitration Award was vacated just two weeks ago upon similar grounds. *Brian Leggett, Bryson Holdings, LLC v. Wells Fargo Clearing Services, LLC D/B/A Wells*

Fargo Advisors, LLC, Jay Pickett, III, 2019CV328949.[20] In *Leggett*, the court vacated the award based upon multiple grounds shared by this case: (i) the arbitrators refused to postpone the hearing and provided no basis for their decision; (ii) the arbitrators refused to allow two non-cumulative witnesses to testify in support of Leggett's main claims; (iii) the attorney for Wells Fargo deliberately made false statements about witness testimony in a successful effort to influence the final award; and (iv) the arbitrators awarded attorney's fees where not authorized by statute. Just as in the present matter, the arbitrators in *Leggett* appeared to treat the individual party with disdain—repeatedly denying the petitioner's reasonable requests for relief and providing no basis or explanation for the decision.

a. <u>The Arbitrators Committed Misconduct in Refusing to Hear Evidence Pertinent and Material to the Controversy</u>

The Panel committed misconduct by refusing to hear literally any evidence in support of John Palombo's claims for fraudulent inducement. Although arbitrators have a great deal of discretion to exclude evidence as redundant, or otherwise unnecessary to the decision-making process, arbitrators cannot completely bar a party's right to present evidence entirely. *See Weinberg v. Silber*, 140 F. Supp. 2d 712, 719 (N.D. Tex. 2001), aff'd, 57 F. App'x 211 (5th Cir. 2003)

Vacatur is appropriate when the exclusion of relevant evidence "so affects the rights of a party that it may be said that he was deprived of a fair hearing". *Newark Stereotypers' Union No. 18 v. Newark Morning Ledger Co.*, 397 F.2d 594, 599 (3rd Cir. 1968) The arbitrator is not bound to hear all of the evidence tendered by the parties; however, he must

[20] A copy of the *Leggett* order is attached as Exhibit 2.

give each of the parties to the dispute an adequate opportunity to present its evidence and arguments. *Hoteles Condado Beach, La Concha & Convention Ctr. v. Union De Tronquistas Loc. 901*, 763 F.2d 34, 39 (1st Cir. 1985). All parties in an arbitration proceeding are entitled to notice and an opportunity to be heard. *Citizens Bldg. of West Palm Beach, Inc. v. Western Union Tel. Co.*, 120 F.2d 982, 984 (5th Cir. 1941).

The case of *Gulf Coast Indus. Workers Union v. Exxon Co., USA*, 70 F.3d 847, 849 (5th Cir. 1995), provides clear direction from the Fifth Circuit that an award must be vacated when the arbitrators refused to hear pertinent evidence. In *Gulf Coast*, an employee was terminated for refusal to submit to drug testing. The employee's Collective Bargaining Agreement required drug testing if reasonable cause existed to suspect drug use. At arbitration, the employer (Exxon) attempted to admit a Substance Analysis Report demonstrating that drugs were found in the employee's car, thus providing reasonable cause to suspect drug use. The arbitrator denied the request, stating that Exxon did not have to establish this information because it was already in evidence. However, in the final Award, the arbitrator ruled against Exxon, holding that Exxon failed to establish reasonable cause of drug use due to lack of evidence. The District Court, and the Fifth Circuit thereafter, both found that the arbitrator prevented Exxon from entering the exact evidence that its case relied upon. Accordingly, the courts ruled that the award "fits squarely" into the FAA's statutory grounds requiring the award to be vacated.

Similarly, cases have found that failure to accept testimony for allegations of fraudulent inducement serve as grounds to vacate the award. *Tempo Shain Corp. v. Bertek, Inc.*, 120 F.3d 16 (2d Cir. 1997). In *Tempo Shain*, an affiliate of Tempo Shain Corporation

("Tempo Shain"), entered into an agreement with Bertek, Inc. ("Bertek") to purchase a license agreement. The parties ran into a disagreement and entered into arbitration. Both parties claimed fraudulent inducement and asked for breach of contract charges. Bertek intended to call Wayne Pollock, former President of Bertek's Laminated Products Division, as a witness to provide what Bertek considered to be crucial testimony concerning the negotiations and dealings between the parties; however, Pollock was unavailable to testify due to his wife's illness. The arbitrators refused to postpone the final hearing to hear Bertek's testimony, holding that the evidence would be cumulative of other evidence already presented at the hearing and later issued an award against Bertek. The Second Circuit held that "there was no reasonable basis for the arbitrators to conclude that Pollock's testimony would have been cumulative with respect to those issues" and ordered that the award be vacated. *Id.* at 21. Notably, the arbitrators' failure to postpone the hearing to allow for full participation served as separate grounds to vacate the award, which will be discussed later in this motion.

In the present matter, John Palombo was completely barred from presenting any evidence of any kind in support of multiple claims he filed. John Palombo filed claims of fraudulent inducement as well as claims for discrimination for conduct that took place prior to December 1, 2018. John Palombo has the statutory and contractual right to present evidence for these claims, as the parties to the arbitration have a dispute as to the facts at issue in the arbitration. However, the Panel dismissed these claims without giving John Palombo the opportunity to present evidence in support of his position.

The Panel's basis for preventing John Palombo from presenting evidence was fundamentally flawed and is misconduct as defined by the FAA. John Palombo clearly stated in his initial pleading, his response to the motion to dismiss, and orally at hearing, that Merrill Lynch fraudulently induced him into signing a contract that contained, *inter alia*, a release of liability. Merrill Lynch sought to enforce this release through a motion to dismiss, but John Palombo was denied the opportunity to present evidence which would support his position. Moreover, John Palombo was denied the opportunity to present evidence which would support his claim that he never ratified the contract. In fact, the sole basis for the Panel's decision was the representations of counsel, as no evidence was submitted by either party. Merrill Lynch's motion to dismiss simply could not have been granted in the absence of evidence, and thus the Panel's subsequent refusal to allow John Palombo to present evidence in support of these claims was misconduct by the Panel. Moreover, by refusing to hear evidence when the motion to dismiss was itself being evaluated, the Panel committed further misconduct under the definition of 9 U.S.C. § 10(a)(3).

The Panel refused to hear John Palombo's evidence in support of his claims. The FAA clearly defines such behavior as misconduct that supports vacating the arbitration award. On this basis alone, the Award should be vacated, and the parties should be remanded back to arbitration to proceed forward with a different set of arbitrators.

b. The Arbitrators Committed Misconduct in Refusing to Postpone the Hearing upon Sufficient Cause Shown

An arbitration award may be vacated where the arbitrators were "guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown." 9 U.S.C. § 10(a)(3). The arbitrary denial of a reasonable request for a postponement may serve as grounds for vacating an arbitration award. *Sheet Metal Workers Int'l Ass'n, Loc. No. 162 v. Jason Mfg., Inc.*, 900 F.2d 1392, 1398 (9th Cir. 1990.

The present facts align strongly with those of *Tube & Steel Corp. of Am. v. Chicago Carbon Steel Prod.*, 319 F. Supp. 1302, 1303 (S.D.N.Y. 1970), in which the court vacated the arbitration award. In that case, the parties communicated back and forth about a date for the arbitration hearing roughly two months in advance. The parties were told that the arbitrators were available for a hearing on the week of August 17, which the parties accepted. *Id.* at 1303. However, six weeks before the hearing, one party noticed the final hearing for August 10 instead. After receiving this notice, respondent replied that it was unavailable for that week due to scheduling and logistical issues. The arbitrators reviewed the correspondence between the parties and upheld the August 10 hearing date despite the sufficient cause stated by respondent. The court found that the refusal to postpone constituted misconduct by unduly prejudicing the party who could not attend.

In the present matter, John Palombo provided the Panel with sufficient cause to postpone the final hearing. First, John Palombo notified the Panel that his counsel was unavailable for the week of November 30 due to a separate week-long arbitration hearing. Second, John Palombo notified the Panel of an existing motion to vacate that had been filed

which, if ruled upon, would fundamentally change the scope of the arbitration final hearing. The Panel ignored this sufficient cause and simply set the hearing at a time convenient for them. A failure to postpone the hearing under these circumstances clearly rises to the level of misconduct under the Federal Arbitration Act, and as such the award should be vacated.

c. The Arbitrators Exceeded their Powers

The Panel clearly exceeded the authority given to it under the FINRA Code, thus requiring that the Award be vacated and the parties remanded to arbitration to proceed with a new panel. Arbitration is contractual and arbitrators derive their authority from the scope of the contractual agreement. *United Steelworkers of America v. Enterprise Wheel and Car Corp.*, 363 U.S. 593, 597, 80 S.Ct. 1358, 4 L.Ed.2d 1424 (1960). Accordingly, the award of an arbitration panel may be vacated where the arbitrators exceed their powers. 9 U.S.C. § 10(a)(4). *E.g., Retail Store Employees Union Local 782 v. Sav-on-Groceries*, 508 F.2d 500 (10th Cir. 1975).

First, the arbitrators exceeded their authority by failing to postpone the hearing upon the parties' agreement. Rule 13601(a)(1) of the FINRA Code states: "A hearing shall be postponed by agreement of the parties." (Emphasis added). This rule is mandatory, as it states the hearing "shall" be postponed when the conditions are met. On October 12, 2021, John Palombo and Merrill Lynch both agreed to a postponement of the final hearing, and provided proposed dates in January, February, and March 2022 to the panel. On the evening of October 18, 2021, the Panel explicitly ignored the parties' agreement and unilaterally scheduled the final hearing for dates not agreed to by the parties. Moreover, the Panel's order references that it reviewed Merrill Lynch's October 15, 2021 submission that clearly

indicated the agreement of the parties as to which dates were acceptable for the postponement. Rule 13601(a)(1) is a clear limitation on the Panel's authority for setting a final hearing, and the Panel's decision exceeded this authority. For that reason alone, the award must be vacated.

Second, through the onerous award against John Palombo, the Panel awarded relief that exceeded its authority. Arbitrators can exceed their authority by awarding damages not properly submitted to them. *See Totem Marine Tug & Barge, Inc. v. N. Am. Towing, Inc.*, 607 F.2d 649, 651 (5th Cir. 1979). The parties presented arguments in favor of, and in opposition to, the enforceability of the CTP Agreement. A fundamental legal principle regarding contract interpretation is that a contract is either enforceable or it is not. However, the Panel exceeded its authority and acted in a manner that denied John Palombo enforcement of the provisions of the contract—forcing him to return the compensation he was paid over two full years—while simultaneously enforcing other provisions of the contract against John Palombo—forcing him to abide by a release therein, and forcing him to pay damages based upon a breach of that same contract for which he would return all compensation. An award of this kind exceeds the authority of the Panel by granting relief not legally possible and not legally presented thereto. Accordingly, the Award should be vacated as it was entered in excess of the arbitrators' authority.

d. <u>The Arbitration Award was Procured by Fraud</u>

As a final matter, the Award was procured through the fraudulent misrepresentations of counsel for Merrill Lynch. Under Section 10(a)(1) of the FAA, an award may be vacated when the award was procured by corruption, fraud, or undue means.

Courts have held that perjury of a participant can serve as grounds for vacating an award on the basis of fraud. *See Newark Stereotypers' Union, supra* ("We may assume that the obtaining of an award by perjured testimony would constitute fraud under § 10(a).")

The *Leggett* case, *supra*, saw an award overturned in part due to an attorney's fraudulent testimony to the panel. In *Leggett*, the final hearing was postponed partway through a witness's testimony, and rescheduled to continue on a date several months later. When the witness resumed the stand after all those months, the testimony appeared to have changed considerably. Leggett objected to the change in testimony, but a lack of formal record prevented him from offering direct evidence at that time to the panel. In contrast, the attorney for Wells Fargo knowingly misrepresented the status of the testimony to the panel in an attempt to bolster the witness's credibility and confuse the panel as to what had been previously said. The panel relied upon the attorney's statements, and ultimately entered an award against Leggett. In the order vacating the Award, the court found that these material misrepresentations by the attorney as to the evidence in the case constituted fraud upon the panel, and thus established that the award was procured by fraud.

In the present matter, counsel for Merrill Lynch materially misrepresented the status of evidence and admissions by the parties. No evidence was formally submitted to the Panel, as no documents had even been verified by either party or witness. Moreover, Merrill Lynch misrepresented that various facts were undisputed, as counsel for John Palombo repeatedly suggested otherwise at the hearing. This deliberate misstatement was made for the purpose of having the Panel rely upon it, and the tactic worked—the December 16, 2020 order clearly identified that the Panel found evidence of ratification by

John Palombo when granting the motion to dismiss. The Award, based upon the representations of counsel for Merrill Lynch, as supported in the Order granted the Motion to Dismiss (which was subsequently repeated in the Award itself), clearly relied upon this fraudulent statement. For that reason, the Award should be vacated as the product of fraud.

IV. CONCLUSION

John Palombo wants to exercise his right to arbitrate his claims. The Panel's misconduct and acts in excess of authority meaningfully prevented John Palombo from doing so. The Award in the underlying arbitration should not act as the final word as to John Palombo's claims, because he never had a meaningful chance to argue them. This Court has the statutory authority to correct this egregious violation of rights and allow John Palombo to argue his case on the merits. Win or lose, every party in arbitration should have a chance to have their day in court. For that reason, John Palombo asks that the award be vacated and he have a fresh opportunity to argue his case before a panel of arbitrators that will adhere to the governing rules and statutes.

WHEREFORE, John Michael Palombo respectfully requests:

(1) That the Award be vacated;

(2) That all improper orders of the arbitration panel be struck, including the order of dismissal;

(3) That the parties be remanded to arbitration and that the parties select a new panel pursuant to the Rules of the FINRA Code; and

(4) That John Michael Palombo be awarded such other and further relief as the Court determines to be just and proper.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing has been served upon counsel for all parties via CM/ECF filing and electronic mail this 11th day of February, 2022.

/s/ Jeremy M. Halpern
Jeremy M. Halpern, Esq.