Center for Justice & Democracy's
Public Policy Clinic
New York Law School
185 West Broadway
New York, NY 10013

March 22, 2021

Acting Chair Allison Herren Lee
Securities and Exchange Commission
100 F St NE
Washington, DC 20549

Dear Acting Chair Lee:

Re: Support for Maintaining SEC's Position Against Mandatory Arbitration

My name is Daniel Beloosesky and I am a student intern at the Center for Justice & Democracy. I am writing to strongly urge the SEC to issue a strong statement reaffirming the SEC's longstanding policy against mandatory arbitration to resolve defrauded investors' disputes. While to date shareholders have rejected attempts to place forced arbitration clauses and class action bans into company governing documents, the issue has arisen several times in the last few years. That is why we believe it is important that the SEC take preemptive action today with a strong statement against such clauses.

Recent Actions by Activist Shareholders

In recent years, activist investors favoring mandatory arbitration and class action bans have introduced corporate bylaw proposals that would require arbitration of securities fraud claims and ban class actions, to the detriment of defrauded investors. Last year, an activist shareholder introduced a mandatory arbitration proposal at an Intuit board meeting, after introducing a similar proposal at Johnson & Johnson the year before. Unlike Johnson & Johnson's board, which asked the SEC to stop the vote, Intuit's board allowed the vote to occur.[1] And while Intuit's shareholders "overwhelmingly" rejected the proposal,[2] there is no reason to believe the issue will not arise again at another company. That is why it is critical that the SEC act on this now.

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[1] Frankel, Alison. "New Battleground in the Fight over Mandatory Shareholder Arbitration: Intuit's Annual Meeting." *Reuters U.S.*, Jan. 16, 2020, www.reuters.com/article/us-otc-arbitration/new-battleground-in-the-fight-over-mandatory-shareholder-arbitration-intuits-annual-meeting-idUSKBN1ZF2VQ.

[2] Secure our Savings, "Intuit Shareholders Overwhelmingly Repudiate Forced Arbitration Proposal," Jan. 28, 2020, https://secureoursavings.com/wp-content/uploads/2020/01/1.28.20-Intuit-Forced-Arbitration.pdf.

Access to the Courts Helps the SEC Deter Fraud While Providing Compensation to Defrauded Investors

The SEC plays a crucial role in overseeing markets and obtaining restitution for defrauded investors as part of fulfilling its mission to "protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation."[3] Court actions brought by defrauded investors have helped the SEC fulfill its mission by holding companies accountable as well as providing restitution to defrauded shareholders. The AFL-CIO found that while SEC enforcement actions for financial fraud by companies like Enron, WorldCom, and Tyco obtained investors "$1.75 billion in penalties and fees, … private lawsuits [obtained investors] more than $19.4 billion…."[4]

Moreover, securities fraud cases are extremely expensive to bring, and can only realistically be brought if shareholders are able to join together in a class action.[5] For example, a comparison of 16 securities class action lawsuits revealed "expenses ranging from a low of $1.2 million in the Madoff case to a high of $34.3 million and $28.9 million respectively in the Household International and Tyco International cases."[6] While some "institutional investors" could potentially afford such high arbitration costs, most individual investors, unable to join as a class, would be locked out of arbitration.[7] This means that individual investors' recoveries would only include that obtained through limited SEC enforcement. The under-resourced SEC is further limited by a five-year statute of limitations for bringing disgorgement actions, further limiting its ability to police misconduct.[8]

Court Cases and Written Decisions Help Deter Abuse and Fraud

Individual arbitration harms the SEC's mission of deterring corporate abuse and fraud because arbitration is a private process that results in no written decisions. This lack of "precedential value" hampers case law development that could protect investors against future abusive corporate behavior.[9] According to the Consumer Federation of America, "the publication of legal opinions resulting from litigation in court …. deters future misconduct by providing public notice of permissible and impermissible behavior."[10] In addition, public trials help alert the wider public to corporate fraud. Without this knowledge, consumers might make riskier investments, with resulting losses increasing their wariness to invest in the future. As a result, the

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[3] "SEC.Gov | What We Do." *SEC.Gov*, Feb. 19, 2020, http://www.sec.gov/about/what-we-do.
[4] Antilla, Susan. "Will Shareholders Lose the Right to Sue Over Corporate Fraud?" *The Intercept*, Aug. 22, 2018, https://theintercept.com/2018/08/21/sec-mandatory-arbitration-shareholders/.
[5] Hauptman, Micah and Roper, Barbara. "A settled Matter: Mandatory Shareholder Arbitration Is Against the Law and the Public Interest," *Consumer Federation of America* 31 (Aug. 2, 2018), https://consumerfed.org/wp-content/uploads/2018/08/cfa-mandatory-shareholder-arbitration-white-paper.pdf.
[6] Id at 29.
[7] Id at 31.
[8] Jackson, Robert J. "Keeping Shareholders on the Beat: A Call for a Considered Conversation About Mandatory Arbitration." SEC.Gov, Feb. 26, 2018, https://www.sec.gov/news/speech/jackson-shareholders-conversation-about-mandatory-arbitration-022618 (noting the impact of *Kokesh v. SEC,* 137 S. Ct. 1635, 1639 (2017).)
[9] Hauptman and Roper. "A settled Matter: Mandatory Shareholder Arbitration Is Against the Law and the Public Interest," 33.
[10] Ibid.

market could suffer harm, while a likely increase in abuse and fraud would increase the SEC's enforcement workload.

Also, the absence of a public record in cases involving repeated corporate fraud forces investors and their counsel to build their cases from scratch, greatly increasing costs for no reason. The disadvantages to plaintiffs are only compounded by other advantages that companies enjoy in arbitration like latitude in "selecting an arbitrator," inapplicability of federal "rules of evidence," and decisions being "nearly impossible to appeal."[11] Considering these disadvantages, plaintiffs who can afford arbitration, may nevertheless feel that it is not worthwhile to arbitrate their claims, leaving SEC enforcement as the only tool for them to be made whole.

In sum, we urge the SEC to preemptively issue a strong statement that it will not change its policy prohibiting mandatory shareholder arbitration and class action bans. At a minimum, if presented with a corporate bylaw approving the use of forced arbitration, we urge the agency to not consider changing its policy without full notice and comment rulemaking. Blocking access to the courts will lead to worse corporate behavior, increasing the SEC's workload, and cultivating greater market wariness by potential investors. We hope the agency takes this important action.

Thank you for your time and consideration.

Sincerely,

/s/

Daniel Beloosesky

[11] Silver-Greenberg, Jessica and Corkery, Michael. "In Arbitration, a 'Privatization of the Justice System.'" *The New York Times*, 24 Oct. 2017, https://www.nytimes.com/2015/11/02/business/dealbook/in-arbitration-a-privatization-of-the-justice-system.html.

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