08-4630-cv

United States Court of Appeals

for the

Second Circuit

HIGHLAND CAPITAL MANAGEMENT LP,

Plaintiff-Appellee,

RBC DOMINION SECURITIES CORP.,

Third-Party Defendant-Counter-Claimant-Appellee,

– v. –

LEONARD SCHNEIDER, LESLIE SCHNEIDER, SCOTT SCHNEIDER, SUSAN SCHNEIDER,

Defendants-Third-Party-Plaintiffs-Counter-Defendants-Appellants,

JENKENS & GILCHRIST PARKER CHAPIN LLP,

Defendant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF AMICUS CURIAE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF APPELLEES' PETITIONS FOR PANEL REHEARING AND REHEARING *EN BANC*

Kevin M. Carroll
SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
1110 New York Avenue, NW
Washington, DC 20005
(202) 962-7382

Sean M. Murphy
MILBANK, TWEED, HADLEY & MCCLOY LLP
One Chase Manhattan Plaza
New York, NY 10005
(212) 530-5000
Counsel for Amicus Curiae

RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Amicus curiae Securities Industry and Financial Markets Association ("SIFMA") is a non-profit corporation. It has no parent corporation, and no publicly-held corporation owns 10% or more of its stock.

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STATEMENT OF IDENTITY AND INTEREST[1]

The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation, and economic growth, while building trust and confidence in the financial markets. Fundamental to achieving this mission is earning, inspiring, and upholding the public's trust in the industry and the markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association.

SIFMA has an interest in this case in that the panel's June 11, 2010 Opinion (as corrected June 22, 2010) (the "Opinion") appears to require participants in the capital markets, including SIFMA members, to make an inquiry into the scope of their counterparties' authority to engage in a particular trade when dealing with a broker.[2]

From the day the capital markets as we know them were established, securities have been traded daily on the basis of oral agreements. Today, billions of dollars of securities are traded every day on the capital markets by SIFMA member firms pursuant to oral agreements. This is particularly true in those

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1 All parties to this appeal have consented to the filing of this brief.

2 Pursuant to Rule 29.1 of the Local Rules of the United States Court of Appeals for the Second Circuit, counsel for appellee RBC Capital Markets Corporation ("RBC") authored this brief in part at RBC's expense.

market sectors in which sales of securities are conducted via auctions, as well as those sectors, such as institutional options and debt trading as well as credit default swap trading, where a salesperson or trader picking up the telephone and making calls to clients or other potential counterparties remains a significant origin for the trades that take place on the market. Many of these transactions are conducted telephonically by traders on trading desks acting either in a principal capacity on behalf of themselves or their employers or as broker agents on behalf of a customer or third party. In these cases, the traders reach oral agreement as to "size" and "price" on behalf of themselves or other third party principals on the telephone call, and they confirm their oral agreement by a subsequent written confirmation.

Without the certainty attaching to oral agreements for the sale of securities, market participants would be unable to assess properly their financial condition and the effect of a trade, or to plan any future trades that are contingent upon the consummation of any trade that is made pursuant to an oral agreement. Instead, such participants would be required to wait for a written confirmation to be sent. In an ever-changing securities market, market participants must be able to react quickly and decisively to market conditions and opportunities.

In the instant case, however, the panel appears to have found that, even assuming that appellants' broker had authority to convey appellants' assent to a sale of certain securities, evidence that the broker agreed to the size and price of

the securities to be sold was insufficient to support the jury's finding that appellants had entered into a binding oral agreement to sell the securities on those terms. To the extent the panel adds a new, unprecedented condition to the enforceability of market participant's oral agreements for the sale of a security, the decision undermines the finality of the oral agreements under New York law that are entered into daily, and SIFMA requests that the panel revisit the Opinion or the full Court grant rehearing *en banc*.

ARGUMENT

New York law codifies the securities industry custom and practice in Section 8-113(a) of the New York Uniform Commercial Code ("UCC"), which exempts the sale of most securities from the Statute of Frauds that would otherwise require such agreements to be in writing to be enforceable. *See* NY UCC § 8-113(a).[3] Indeed, the UCC reflects the New York legislature's efforts to conform the law of New York with the real-world mechanics by which securities are actually traded on the capital markets. *See Tradewinds Fin. Corp. v. Repco Secs., Inc.*, 5 A.D.3d 229, 229-230 (1st Dep't 2004); *see also Highland Capital Mgmt., L.P. v. Schneider*, 8 N.Y.3d 406, 866 N.E.2d 1020 (2007); *Highland Capital*

[3] Section 8-113 provides that "[e]xcept as provided in subsection (b), a contract or modification of a contract for the sale or purchase of a security is enforceable *whether or not* there is a writing signed or record authenticated by a party against whom enforcement is sought, even if the contract or modification is not capable of performance within one year of its making." NY UCC § 8-113(a) (emphasis added).

Mgmt., L.P. v. Schneider, 485 F.3d 690, 692-693 (2d Cir. 2007). This codification of industry custom and practice – the enforceability of oral agreements as to "size" and "price" of securities – helps ensure the seamless functioning of the capital markets.

The panel's apparent limitation on the scope of authority on which a counterparty is entitled to rely threatens to add an impractical layer of complexity to oral dealings. In the securities industry, many transactions are conducted by agent brokers on behalf of their principals. In the majority of instances when dealing with a broker, market participants rely on the fact that such broker has the actual authority of its principal to engage in a transaction. That is, the agent broker has received a direct manifestation of authority – whether in writing, verbally or by other means – from its principal that it has the authority to take certain action on behalf of the principal. *Peltz v. SHB Commodities, Inc.*, 115 F.3d 1082, 1088 (2nd Cir. 1997) (quoting *Demarco v. Edens*, 390 F.2d 836, 844 (2d Cir. 1968)).[4]

Where such actual authority is lacking, under New York law, a trade may be enforceable if the broker agent had apparent authority to enter into a trade. The ability of third parties to rely on apparent authority reduces the risk that a principal and agent simply deny the existence of authority if a trade is unsuccessful or otherwise unprofitable to the principal. As the panel recognized, apparent

[4] SIFMA makes no comment with regard to the panel's discussion of actual authority.

authority exists "when a principal, either intentionally or by lack of ordinary care, induces [a third party] to believe that an individual has been authorized to act on its behalf." Op. at 11 (citing *Peltz v, SHB Commodities, Inc.*, 115 F.3d 1082, 1088 (2nd Cir. 1997)); *see also Herbert Constr. Co. v. Continental Ins. Co.*, 931 F.2d 989, 993 (2d Cir. 1991). Further, under New York law, it is well-established that a third party is not required to inquire into the scope of an agent's apparent authority unless "the facts and circumstances are such as to put him on inquiry, the transaction is extraordinary, or the novelty of the transaction alerts the third party to the danger of fraud." *Herbert*, 931 F.2d at 996 (internal quotations and citations omitted).

In the Opinion, however, the panel appears to create an abstract affirmative duty in the context of dealing orally with brokers in the securities industry. Specifically, the panel found that, as a matter of law, the broker agent lacked apparent authority to enter into a sale of a security, even "assum[ing] arguendo that by authorizing [the agent] to negotiate with [the third party] on their behalf, the [principals] gave [the agent] apparent authority to communicate their assent either expressly or by implication (even if they had not in fact assented)," because there was insufficient evidence that the third party reasonably believed that the agent had actually received authorization from the principal to sell the securities at a particular price. Op. at 12. Yet the scope of authority which the

panel expressly assumes – *i.e.*, authority to communicate a principal's assent – is the very authority on which the markets rely.[5] Broker agents are hired for the very purpose of removing principals from the process of negotiating trades, making confirmation of specific authority from the principal difficult – if not impossible – to obtain (particularly in those cases where the principal subsequently seeks to back away from a trade).

To the extent the panel suggests that such duty exists to corroborate the scope of a broker's authority for every transaction, the panel creates an unnecessary and cumbersome hurdle to the functioning of the capital markets. Indeed, the Opinion offers little comfort to those parties who, having taken steps to ensure that a broker agent is authorized to communicate a principal's agreement to a trade and having relied on such authority, are thereafter informed by the broker agent that such authority did not exist with respect to specific details of a trade. Requiring the parties to confirm the scope of authority at each step of the negotiation process would hinder the smooth functioning of the capital markets, and is inconsistent with both the law and industry custom and practice.

Thus, to the extent the panel departs from the well-established law and practice governing the sale of securities and creates a new duty of inquiry with

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[5] *See, e.g.*, FINRA Rule 5220 ("No member shall make an offer to buy from or sell to any person any security at a stated price unless such member is prepared to purchase or sell, as the case may be, at such price and under such conditions as are stated at the time of such offer to buy or sell.")

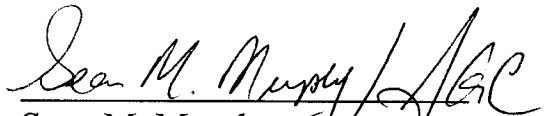
regard to the scope of a broker's authority, we respectfully submit that rehearing *en banc* is appropriate to review the Opinion in light of the significant impact it may have on the oral agreements transacted daily on the capital markets.

CONCLUSION

For all of the foregoing reasons, the panel should revisit the Opinion, or the full Court should grant rehearing *en banc*.

Dated: July 2, 2010

Respectfully submitted,



Sean M. Murphy
MILBANK, TWEED, HADLEY & McCLOY LLP
One Chase Manhattan Plaza
New York, NY 10005
(212) 530-5000

Counsel for Amicus Curiae Securities Industry and Financial Markets Association

Kevin M. Carroll
SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
1110 New York Avenue, NW
Washington, DC 20005
(202) 962-7382

NOTICE OF APPEARANCE FOR SUBSTITUTE, ADDITIONAL, OR AMICUS COUNSEL

Short Title: Highland Capital v. Schneider Docket No.: 08-4630

Counsel of Record (name/firm): N/A

Appearance for (party/designation): Amicus Curiae Securities Industry and Financial Markets Association

Select One:

☐ Substitute Counsel (replacing name/firm: _____)

☐ Additional Counsel (co-counsel with name/firm: _____)

OR

☑ Amicus (in support of (party/designation): in support of Appellees' Petitions for Rehearing)

DOCKET SHEET AMENDMENTS

Substitute, Additional, or Amicus Counsel's Contact Information is as follows:

Name: Sean M. Murphy
Firm: Milbank, Tweed, Hadley & McCloy LLP
Address: One Chase Manhattan Plaza, New York, NY 10005
Telephone: (212) 530-5000 Fax: (212) 530-5219
Email: smurphy@milbank.com

CERTIFICATION

I certify that:

☑ I am admitted to practice in this Court and, if required by Local Rule 46.1(a)(2), have renewed my admission on _____ OR

☐ I applied for admission on _____.

Signature of Counsel: Sean M. Murphy

Type or Print Name: Sean M. Murphy

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

AFFIDAVIT OF SERVICE BY OVERNIGHT MAIL

MARY M. NIELSEN, being duly sworn, deposes and says:

1. I am not a party to this action, am over 18 years of age and reside in Staten Island, New York.

2. On July 2, 2010, I completed the service of the Notice of Appearance and Brief of Amicus Curiae of Securities Industry and Financial Markets Association in Support of Appellees' Petitions for Panel Rehearing and Rehearing En Banc, upon:

Troutman Sanders LLP
Alvin M. Stein
Katherine C. Ash
405 Lexington Avenue
New York, New York 10174
(212) 704-6000
alvin.stein@troutmansanders.com; katherine.ash@troutmansanders.com

Debevoise & Plimpton LLP
Edwin G. Schallert
Steven Klugman
919 Third Avenue
New York, New York 10022
(212) 909-6000
egschallert@debevoise.com; sklugman@debevoise.com

Seward & Kissel LLP
Michael J. McNamara
Jack Yoskowitz
One Battery Park Plaza
New York, NY 10004
(212) 574-1200
mcnamara@sewkis.com; yoskowitz@sewkis.com

Lackey Hershman, LLP
Paul Lackey
Jamie Welton
3102 Oak Lawn Avenue, Suite 777
Dallas, Texas 75219
(214) 560-2201
pbl@lhlaw.net; jrw@lhlaw.net

the addresses designated by said attorneys for that purpose by depositing 2 true copies of same, enclosed in a postpaid properly addressed Federal Express Overnight Mail envelope in a Federal Express Depository and served electronically, via e-mail.

Mary M. Nielsen
MARY M. NIELSEN

Sworn to before me this
2d day of July 2010

Cheryl A. Witkowski
Notary Public

CHERYL A. WITKOWSKI
Notary Public, State of New York
No. 43-4779170
Qualified in Richmond County
Commission Expires April 30, 20 11