

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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STANDARD INVESTMENT CHARTERED, INC., :

Plaintiff, :

-v- :

07 Civ. 2014 (JSR)

NATIONAL ASSOCIATION OF SECURITIES
DEALERS, INC. et al., :

Defendants. :

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BENCHMARK FINANCIAL SERVICES, INC., :

Plaintiff, :

-v- :

08 Civ. 11193 (JSR)

FINANCIAL INDUSTRY REGULATORY
AUTHORITY, INC. et al., :

Defendants. :

MEMORANDUM ORDER

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JED S. RAKOFF, U.S.D.J.

These two related cases arise out of the regulatory consolidation, in 2007, of two self-regulatory organizations ("SROs") -- the National Association of Securities Dealers, Inc. ("NASD") and the regulatory arm of the New York Stock Exchange ("NYSE") -- to form the Financial Industry Regulatory Authority, Inc. ("FINRA"), the sole private regulator of member firms. Plaintiffs, who were members of NASD at the time of the consolidation, allege that material misrepresentations were made in the proxy statement that solicited NASD shareholder votes in favor of certain by-law amendments that were a necessary prerequisite to the consolidation. Most particularly,

plaintiffs allege that the proxy statement falsely asserted that \$35,000 was the maximum amount that NASD, a not-for-profit entity, was authorized by the Internal Revenue Service to pay members in connection with the merger.

While these cases were still pending before the late Honorable Shirley Wohl Kram, to whom they were originally assigned, defendants filed a motion to dismiss in the Benchmark action. Subsequent to the reassignment, the defendants in the Standard action filed motions to dismiss, and this Court received full briefing on all the motions and then heard oral argument on December 16, 2009. Among many reasons argued by defendants for dismissing the claims, one looms particularly large: defendants claim that they are entitled to absolute immunity. See Barbara v. New York Stock Exchange, Inc., 99 F.3d 49, 59 (2d Cir. 1996). Because the Court agrees, and on this ground dismisses the complaints, the Court does not reach the defendants' other arguments.

Pursuant to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78oo, the United States Securities and Exchange Commission is authorized to delegate certain regulatory functions to SROs, which are therefore considered "quasi-governmental" bodies. DL Capital Group, LLC v. Nasdaq Stock Market, Inc., 409 F.3d 93, 95 (2d Cir. 2005). As a result, SROs and their officers are absolutely immune from private damages suits challenging official conduct performed within the scope of their regulatory functions. See, e.g., DL Capital Group, 409 F.3d at 94-97. This immunity, being absolute, turns "on whether specific

acts and forbearances were incident to the exercise of regulatory power, and not on the propriety of those actions or inactions." In re NYSE Specialists S.E.C. Litig., 503 F.3d 89, 98 (2d Cir. 2007).

It is patent that the consolidation that transferred NASD's and NYSE's regulatory powers to the resulting FINRA is, on its face, an exercise of the SROs' delegated regulatory functions and thus entitled to absolute immunity. However, plaintiffs contend that the actions they are challenging -- that is, the making of the alleged misstatements in the proxy statement -- pertain solely to the proprietary functions of the SROs, to which absolute immunity does not apply. In particular, they argue that the alleged misstatement about the \$35,000 limit on payment related to defendants' finances, not their regulatory functions. But this attempt to parse the proxy in order to separate "financially-related" statements from "regulatory-related" statements is artificial and unconvincing. Although the shareholder vote for which the proxy statement was issued did not constitute a vote on the regulatory consolidation itself, the approval of the by-law amendments was not only a necessary prerequisite to the completion of that consolidation, but also was promoted as such in the proxy itself. See, e.g., Proxy Statement at 8 (Dec. 14, 2006) ("The Board of Governors has the authority to approve the Transaction and members are being asked only to approve the amendments to the NASD By-Laws. However, one of the conditions to the closing of the Transaction is member approval of the amendments to the By-Laws.").

Moreover, amendment of the by-laws itself falls within the parameters of NASD's statutory rulemaking authority. See 15 U.S.C. § 78s(b); id. § 78c(a)(27). To focus on the fact that amendment to the by-laws also encompassed a financial component would be to miss the entire purpose of the reorganization -- a regulatory purpose to which immunity applies. See, e.g., D'Alessio v. New York Stock Exchange, Inc., 258 F.3d 93, 98, 105-06 (2d Cir. 2001); Dexter v. Depository Trust & Clearing Corp., 406 F. Supp. 2d 260, 263-64 (S.D.N.Y. 2005), aff'd, 219 F. App'x 91 (2d Cir. 2007).

Accordingly, because all the defendants are entitled to absolute immunity, the Court hereby grants the defendants' motions to dismiss and dismisses both actions with prejudice.

SO ORDERED.



JED S. RAKOFF, U.S.D.J.

Dated: New York, New York
March 1, 2010