No. 11-1521

IN THE
Supreme Court of the United States

KPMG LLP,

Petitioner,

v.

ROBERT COCCHI, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the Fourth District Court of Appeal of the State of Florida

REPLY BRIEF OF PETITIONER

JOHN K. VILLA
DAVID A. FORKNER
WILLIAMS & CONNOLLY LLP
725 Twelfth Street, NW
Washington, DC 20005
(202) 434-5117

EDWARD A. MAROD
GUNSTER
777 S. Flagler Drive
Suite 500 East
W. Palm Beach, FL 33401
(561) 655-1980

CARTER G. PHILLIPS*
PAUL J. ZIDLICKY
ERIC D. MCARTHUR
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000
cphillips@sidley.com

GARY F. BENDINGER
GREGORY G. BALLARD
SIDLEY AUSTIN LLP
787 Seventh Avenue
New York, NY 10019
(212) 839-5300

Counsel for Petitioner

* Counsel of Record

September 27, 2011

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES Page

STATUTE

SCHOLARLY AUTHORITY

INTRODUCTION

Petitioner KPMG LLP previously demonstrated that the Florida court of appeal's refusal to compel arbitration of respondents' claims under the Federal Arbitration Act ("FAA") conflicts with this Court's decisions holding that (1) a court must compel arbitration of individual claims that are subject to arbitration even if other claims are not, Pet. 3–4, 13–14, 16–19; and (2) courts may not disregard generally applicable state law that "'permit[s] arbitration by or against nonparties to the written arbitration agreement,'" *id.* at 4, 14–15, 19–23. Respondents do not challenge these controlling legal principles, but instead argue that review should be denied because the Court "may lack jurisdiction," Opp. 12; the decision below is interlocutory, *id.* at 12–13; and the court below did not violate this Court's decisions under the FAA, *id.* at 8–12.

These arguments have no merit. *First*, this Court has jurisdiction over the decision below because the court of appeal denied KPMG's request to compel arbitration under the FAA. The FAA renders agreements to arbitrate enforceable as a matter of federal law. 9 U.S.C. § 2; *Arthur Andersen LLP* v. *Carlisle*, 129 S. Ct. 1896, 1901 (2009) (FAA creates "substantive federal law regarding the enforceability of arbitration agreements"). The court of appeal's refusal to compel arbitration under the FAA is a federal determination within this Court's jurisdiction. See *Michigan* v. *Long*, 463 U.S. 1032, 1040–41 (1983).

Second, the interlocutory nature of the decision below highlights the need for immediate review. Respondents cite inapposite cases and ignore this Court's holding that "to delay review of a state judicial decision denying enforcement of the contract

to arbitrate until the state-court litigation has run its course would defeat the core purpose of the contract to arbitrate" under the FAA. *Southland* v. *Keating*, 465 U.S. 1, 7–8 (1984). That ruling applies directly in this case.

Finally, the decision below should be set aside because it flouts this Court's command that courts must rigorously enforce arbitration agreements even if the result is piecemeal litigation. See *Dean Witter Reynolds Inc.* v. *Byrd*, 470 U.S. 213, 221 (1985). Respondents now argue that there is no conflict because the court of appeal held all their claims "to be direct," Opp. 8, but the decision below provides no support for that conclusion, as respondents acknowledged below, see Pet. 12. The court's refusal to follow controlling law under the FAA should be reversed and the case remanded for proceedings not inconsistent with the Court's judgment. Alternatively, the Court should grant plenary review.

I. THE COURT SHOULD EXERCISE JURISDICTION OVER THE COURT OF APPEAL'S REFUSAL TO COMPEL ARBITRATION UNDER THE FAA.

Respondents challenge the Court's jurisdiction and argue that it should deny review because the decision below is interlocutory. Opp. 3, 12–13. These arguments are addressed in turn.

1. Respondents argue, quoting *Lynch* v. *New York ex rel. Pierson*, 293 U.S. 52, 54–55 (1934), that the "Court may lack jurisdiction" because "'if it does not appear upon which of two grounds the judgment was based, and the ground independent of a federal question is sufficient in itself to sustain [the judgment], this Court will not take jurisdiction.'" Opp. 12. Respondents assert that, at best, the court

below "*may* have decided the case on a federal ground" and that is not enough. *Id.* Respondents are seeking to revive a legal standard this Court abandoned more than 25 years ago, and their substantive argument reflects a fundamental misunderstanding of the FAA's requirements.

First, *Lynch* does not set forth the legal standard for assessing whether a state-court ruling rests on an adequate and independent state-law ground. In *Michigan* v. *Long*, 463 U.S. 1032 (1983), this Court, citing *Lynch* and other precedents, "openly admit[ted] that we have thus far not developed a satisfying and consistent approach for resolving this vexing issue." *Id*. at 1038. The Court abandoned *Lynch* and other cases because they were "unsatisfactory," *id*. at 1039–40, and instead held that when a state-court decision "fairly appears" to be "interwoven with the federal law," and "when the adequacy and independence of any possible state law ground is not clear from the face of the opinion," the Court "will accept as the most reasonable explanation that the state court decided the case the way it did because it believed that federal law required it to do so," *id*. at 1040–41.

Second, Section 2 of the FAA makes arbitration agreements "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. The FAA thus "creates substantive federal law regarding the enforceability of arbitration agreements, requiring courts to place such agreements on the same footing as other contracts." *Arthur Andersen*, 129 S. Ct. at 1901 (internal quotation marks omitted). In the courts below, KPMG sought to compel arbitration under the FAA because it had broad arbitration agreements with the Rye Funds that encompassed respondents' claims and that were binding on

respondents because their claims were derivative of the Rye Funds' rights. Pet. 10–11.

This Court has jurisdiction because there is no adequate and independent state-law ground supporting the decision below. The court of appeal's refusal to compel arbitration under Section 2 of the FAA is governed by federal law and thus inherently is a determination "interwoven with the federal law." As a result, this Court has jurisdiction to review the state court's refusal to compel arbitration under the FAA. See *Long*, 463 U.S. at 1040–41.

2. Respondents likewise argue that review should be denied because the decision is interlocutory and the Court thus should grant review only if there is a showing of "'extraordinary inconvenience.'" Opp. 12–13 (emphasis omitted) (quoting *Am. Constr. Co.* v. *Jacksonville, Tampa & Key W. Ry.*, 148 U.S. 372, 384 (1893)). Here too, respondents' argument relies on inapposite cases and ignores the controlling law.

The decisions identified by respondents, *id.* at 13, arise out of federal court litigation in a variety of contexts having nothing to do with the FAA. This Court, however, applies a different standard for "interlocutory" decisions from state courts. *Cox Broad. Corp.* v. *Cohn*, 420 U.S. 469, 482–83 (1975). Applying the *Cox* standard, this Court has held that an order by a state court refusing to compel arbitration under the FAA should be reviewed immediately. See *Southland*, 465 U.S. at 6. In *Southland*, the Court explained that "failure to accord immediate review" of a decision denying arbitration under the FAA "might 'seriously erode federal policy.'" *Id.* at 7. The Court ruled that "to delay review of a state judicial decision denying enforcement of the contract to arbitrate until the state-court litigation has run its course would defeat

the core purpose of a contract to arbitrate" under the FAA. *Id.* at 7–8; accord *Perry* v. *Thomas*, 482 U.S. 483, 489 n.7 (1987) (following *Southland*).

Here, too, review of the court of appeal's refusal to compel arbitration is necessary to ensure that KPMG's federal right to arbitrate is not "defeat[ed]." *Southland*, 460 U.S. at 7. If KPMG is denied its right to arbitrate now and prevails on the merits in the state-court proceedings, then its federal right to arbitrate will have been rendered meaningless. See *id.* Moreover, reversal of the Florida court of appeal's decision would preclude further litigation of the causes of action for which KPMG has a right to compel arbitration. See *id.* at 6. As in *Southland*, denial of immediate review would "'seriously erode federal policy'" under the FAA. *Id.*

II. THE DECISION BELOW SHOULD BE SUMMARILY REVERSED BECAUSE IT CONFLICTS WITH THIS COURT'S PRECEDENTS UNDER THE FAA.

The decision below should be summarily reversed because it conflicts with this Court's decisions in *Dean Witter* and *Arthur Andersen* and thus undermines the uniform application of the FAA in a high-profile proceeding involving claims that federal courts have sent to arbitration under the FAA.

1. Respondents confirm that there is no dispute about the controlling legal standard for compelling arbitration under the FAA: "If respondents' claims are derivative under Delaware law, they are subject to arbitration." Opp. 1. The court of appeal denied arbitration of all claims without addressing whether respondents' claims for malpractice and aiding and abetting a breach of fiduciary duty were derivative and thus subject to arbitration under the FAA. By

doing so, the court of appeal necessarily held that the FAA does not compel arbitration of these claims even if they are derivative. At a minimum, the court's ruling does violence to the bedrock principle that, under the FAA, "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability." *Moses H. Cone Mem'l Hosp.* v. *Mercury Constr. Corp.*, 460 U.S. 1, 24–25 (1983).

The court of appeal's decision directly conflicts with (1) *Dean Witter*'s holding that a court must compel arbitration of claims subject to a binding arbitration agreement even if other claims before the court are deemed nonarbitrable, 470 U.S. at 218–21; and (2) *Arthur Andersen*'s holding that a court may not disregard state law mandating the enforcement of arbitration agreements against nonparties, 129 S. Ct. at 1902 & n.5.

2. Respondents contend that there is no conflict with this Court's precedent because the court of appeal "found all of respondents' claims to be direct," Opp. 8, even though it did not "expressly discuss" respondents' malpractice and aiding-and-abetting claims, *id.* at 1. Nothing in the court of appeal's opinion or the record supports that assertion.

The court of appeal recognized that respondents advanced four distinct claims. Pet. App. 25a. The court also ruled that the arbitration agreement "would not apply to the direct claims made by the individual plaintiffs," *id.*, but nowhere concluded that that the malpractice and aiding-and-abetting claims were direct. In contrast, applying *Tooley* v. *Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031 (Del. 2004), the court held that respondents' negligent-

misrepresentation and FDUTPA claims were direct because they "allege individual harm to the plaintiffs and involve torts directed at the individual limited partners." Pet. App. 26a. Having concluded that these two claims were direct and thus nonarbitrable, the court "affirm[ed] the trial court's denial of the motion to compel arbitration," *id.* at 27a, without ever addressing the malpractice and aiding-and-abetting claims.

Further, at oral argument, the court of appeal acknowledged that some claims might be deemed "direct" and others "derivative." Tr. Oral Ar. 20–21. The analysis in its ruling, however, was limited to "the claims of negligent misrepresentation and violation of FDUTPA." Pet. App. 26a. The court approvingly cited case law for the proposition that "the same set of facts may result in both direct and derivative claims," *id.* at 27a—a proposition that would have been irrelevant had the court concluded that all of respondents' claims were direct. Taken together, the court of appeal concluded either (1) that it was unnecessary to decide whether respondents' malpractice and aiding-and-abetting claims were direct, or (2) that these claims were derivative.

In fact, both claims are plainly derivative. Cf. Pet. 18 n.4. The malpractice claim depends on a showing that KPMG violated its duty to the Rye Funds to comply with professional standards in auditing their financial statements. Compl. ¶¶ 158–162. Likewise, the aiding-and-abetting claim depends on a showing that KPMG "knowingly perform[ed] an inadequate audit" of the Rye Funds' financial statements. *Id.* ¶ 186. For both claims, any injury to respondents is derivative of the injury to the Rye Funds. Indeed, one case cited by the court of appeal as support for its holding that negligent misrepresentation is a "direct"

claim ruled that a claim for aiding and abetting a fiduciary breach based on allegations similar to respondents' was "'a paradigmatic derivative claim.'" *Stephenson* v. *Citgo Grp. Ltd.*, 700 F. Supp. 2d 599, 610–11 (S.D.N.Y. 2010) (applying Delaware law).

3. To avoid these conclusions, respondents advance an argument that is contrary to the position they took below. In their response to KPMG's petition for rehearing, respondents stated that the court of appeal "held that at least two of Plaintiffs' claims are direct (and not arbitrable) and *was silent about whether any other claims are derivative*." Plaintiffs' Response to KPMG's Motion for Rehearing at 3 (emphasis added). Further, below, respondents defended the court's decision by arguing only that "th[e] Court correctly held that Plaintiffs' negligent misrepresentation and FDUTPA claims against KPMG are direct." *Id.* at 10. Nowhere did respondents suggest that the court of appeal had held that their malpractice and aiding-and-abetting claims were direct claims.

Respondents now assert that it is "unlikely" that the court disregarded this Court's precedents because respondents "at no point argued that the court of appeal should refuse to compel arbitration of their claims, even if they were derivative." Opp. 9, 10. That is not so. At oral argument, in response to a question whether there could be "some claims being heard in arbitration and some being heard in circuit court," respondents told the court that "as a practical matter if a claim is determined in our case to be derivative, it's never going to be pursued and there will be no arbitration." Tr. Oral Arg. 21–22.

Contrary to that representation, respondents have continued to force KPMG to litigate claims that the trial court previously had determined to be "deriva-

tive." Pet. 13. Moreover, the trial court has refused to compel arbitration of those claims because its prior order denying arbitration "'was affirmed'" by the court of appeal in the decision challenged here and KPMG's arguments under the FAA are "'nearly identical'" to those presented to the court of appeal. *Id.* As a result, KPMG has been forced to litigate claims that the trial court previously held were "derivative" even though respondents admit that any "derivative" claims "are subject to arbitration" under the FAA. Opp. 1.[1]

4. Contrary to respondents' contention, therefore, the issue here is not simply that the court of appeal did not "expressly discuss" respondents' malpractice and aiding-and-abetting claims—it treated them as irrelevant when it affirmed the trial court's order denying arbitration of those claims. That decision is irreconcilable with this Court's precedents.

As respondents acknowledge, *Dean Witter* and *Arthur Andersen* make clear that the claims must be sent to arbitration if they are derivative. *Id.* *Dean Witter* requires a court to determine whether *each* claim is nonarbitrable before denying arbitration as to that claim, because the FAA "mandates that district courts *shall* direct the parties to proceed to arbitration on issues as to which an arbitration agreement has been signed," even if other claims before the court are nonarbitrable. 470 U.S. at 218. The court of appeal was therefore obligated to decide whether respondents' malpractice and aiding-and-

[1] None of the six decisions respondents cite to argue that the Florida court of appeal "'rigorously enforce[s]'" arbitration agreements, Opp. 10–11, actually compelled arbitration under the FAA. *Cf. Buckeye Check Cashing, Inc.* v. *Cardegna*, 546 U.S. 440, 449 (2006) (reversing Florida Supreme Court decision that refused to compel arbitration under the FAA).

abetting claims were derivative before it could deny arbitration of those claims.

Accordingly, KPMG's petition does not depend on "speculation about what the Florida court of appeal might have done," Opp. 2, but rather on what the court of appeal undeniably did—denied arbitration as to all claims without addressing whether two of the claims were derivative and thus subject to binding arbitration under the FAA. In doing so, the court denied KPMG its core right under the FAA to receive a determination as to whether respondents' malpractice and aiding-and-abetting claims are derivative and, if so, to be granted an order compelling arbitration of those claims. That was clear error. See *Howlett ex. rel. Howlett* v. *Rose*, 496 U.S. 356, 369 (1990) (a "state court may not deny a federal right"); *Testa* v. *Katt*, 330 U.S. 386, 394 (1947) ("State courts are not free to refuse enforcement of [a federal] claim").

For these reasons, the decision below cannot be reconciled with this Court's precedents under the FAA and should be summarily reversed. The law is settled, the material facts are not in dispute, and the decision below is clearly in error. See Eugene Gressman et al., *Supreme Court Practice* 350 (9th ed. 2007); cf. *Citizens Bank* v. *Alafabco, Inc.*, 539 U.S. 52 (2003) (per curiam) (summarily reversing lower court's misapplication of this Court's arbitration precedents); *Major League Baseball Players Ass'n* v. *Garvey*, 532 U.S. 504 (2001) (per curiam) (same). Consistent with *Dean Witter* and *Arthur Andersen*, the Court should reverse the decision below and remand with instructions to determine whether respondents' malpractice and aiding-and-abetting claims are derivative, and if so, to compel arbitration of those claims.

5. Alternatively, the Court should grant plenary review. Contrary to respondents' contention, the issue before this Court is whether it was appropriate as a matter of federal law under the FAA for the court to refuse to compel arbitration of respondents' malpractice and aiding-and-abetting claims without deciding whether they were direct or derivative. As to that question, the decision below conflicts with numerous federal circuit court decisions holding that (1) the FAA requires courts to compel arbitration of arbitrable claims even if they are presented in a lawsuit that involves nonarbitrable claims, Pet. 18; and (2) the FAA requires courts to enforce arbitration agreements against nonparties when the contract is enforceable against them under traditional principles of state law, *id*. at 22–23.

This Court's review is necessary to restore uniformity among the lower courts as to these important and recurring issues under the FAA.

CONCLUSION

The Court should grant the petition for certiorari and summarily reverse the decision below, or alternatively, accept the case for plenary review.

Respectfully submitted,

JOHN K. VILLA
DAVID A. FORKNER
WILLIAMS & CONNOLLY LLP
725 Twelfth Street, NW
Washington, DC 20005
(202) 434-5117

EDWARD A. MAROD
GUNSTER
777 S. Flagler Drive
Suite 500 East
W. Palm Beach, FL 33401
(561) 655-1980

CARTER G. PHILLIPS*
PAUL J. ZIDLICKY
ERIC D. MCARTHUR
SIDLEY AUSTIN LLP
1501 K Street, NW
Washington, DC 20005
(202) 736-8000
cphillips@sidley.com

GARY F. BENDINGER
GREGORY G. BALLARD
SIDLEY AUSTIN LLP
787 Seventh Avenue
New York, NY 10019
(212) 839-5300

Counsel for Petitioner

September 27, 2011

*Counsel of Record