

The New York Court of Appeals Rules That an Employer's Statements on an NASD Form U-5 Are Protected by an Absolute Privilege in Defamation Lawsuits

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On March 29, 2007, the New York Court of Appeals held in *Rosenberg v. MetLife, Inc.*, USCOA, 2 No. 23 (Mar. 29, 2007), that an employer's statements on an NASD employee termination notice (Form U-5) are protected by an absolute privilege in defamation lawsuits, resolving a conflict among the New York Appellate Divisions.

NASD member firms are required by the rules of the NASD to file an accurate Form U-5 when a registered person's association with the broker-dealer is terminated. Despite this complete candor requirement, the courts of some states leave former employers vulnerable to suits for defamation based on information provided on the Form U-5 because they only protect such statements with a qualified privilege. Under the laws of most states, including New York, statements subject to a qualified privilege are still actionable if a plaintiff can demonstrate that the statements were made with malice. "In contrast, an absolute privilege immunizes a communicant from liability." This absolute privilege, however, is "generally reserved for communications made by individuals participating in a public function, such as executive, legislative, judicial, or quasi-judicial proceedings." In extending absolute immunity to Form U-5 reporting, the *Rosenberg* decision recognizes the public function of the Form U-5 reporting requirement and the need to encourage complete candor in such reporting.

Background

Following plaintiff's termination as a financial services representative, MetLife prepared a Form U-5 filing that stated as the reason for termination: "An internal review disclosed [the plaintiff] appeared to have violated company policies and procedures involving speculative insurance sales and possible accessory to money laundering violations."

The plaintiff filed a complaint in the United States District Court for the Southern District of New York, alleging multiple claims against MetLife, including a claim for defamation based on MetLife's statements on the Form U-5, which plaintiff claimed were made with malice.

On MetLife's motion, the court dismissed the plaintiff's defamation claim, holding that under New York law, MetLife's statements on the Form U-5 were protected by an absolute privilege. After MetLife prevailed on the remaining claims, the plaintiff appealed the court's ruling that MetLife's statements on the Form U-5 were absolutely privileged. The Second Circuit, finding differing opinions in the First, Second, and Fourth New York Appellate Divisions, certified the following question to the New York

Court of Appeals: “Are statements made by an employer on an NASD employee termination notice (‘Form U-5’) subject to an absolute or a qualified privilege in a suit for defamation?”

The Court’s Reasoning

Judge Graffeo, writing for the Court of Appeals in a 4–2 decision, recognized the strong public purpose behind the NASD’s “investigation and adjudication of suspected violations of the SEC’s laws and regulations as well as the NASD’s own rules,” which the court described as a “quasi-judicial process.” The court noted that “[t]he Form U-5 plays a significant role in the NASD’s self-regulatory process,” and that “[u]pon receipt of the Form U-5, the NASD routinely investigates terminations for cause to determine whether the representative violated any securities rules.” Therefore, the court held, “the compulsory Form U-5 can be viewed as a preliminary . . . step in the NASD’s quasi-judicial process.” “The Form U-5’s compulsory nature and its role in the NASD’s quasi-judicial process, together with the protection of public interests,” led the court to conclude that “statements made by an employer on the form should be subject to an absolute privilege.”

Significance

Public policy considerations strongly support application of an absolute privilege to Form U-5 reporting, and now the law of New York is clear on that issue. Other jurisdictions that frequently look to New York law on securities and other financial services industry matters will likely be encouraged to acknowledge that the potential for and implications of unethical behavior by brokers in the financial services industry warrant an absolute privilege to protect the public.

To view a copy of the court’s opinion, please visit
<http://www.nycourts.gov/ctapps/decisions/mar07/23opn07.pdf>.

For more information and guidance on Forms U-4 and U-5, please visit
http://www.nasd.com/RegulatorySystems/CRD/FilingGuidance/NASDW_005243.

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