

Notice to Members

JANUARY 2005

SUGGESTED ROUTING

Legal and Compliance
Senior Management

KEY TOPICS

Arbitration
Dispute Resolution
Eligibility of Arbitration Claims

GUIDANCE

Arbitration Time Limits

NASD Amends Rule Governing Time Limits for Submission of Arbitration Claims; **Effective Date: May 1, 2005**

Executive Summary

The Securities and Exchange Commission (SEC) has approved amendments to Rule 10304 of the NASD Code of Arbitration Procedure (Code) relating to time limits on the submission of claims in arbitration.¹ The amendments clarify that arbitrators, and not courts, will determine whether a claim is ineligible for arbitration under the rule; make clear that dismissal of a claim on eligibility grounds in arbitration does not preclude a claimant from pursuing the claim in court; provide that, by requesting dismissal of a claim under the rule, the requesting party is agreeing that the claimant may withdraw all related claims without prejudice and may pursue all of the claims in court; and state that the six-year time limit on the submission of claims does not apply to any claim that is directed to arbitration by a court of competent jurisdiction upon request of a member or associated person. Rule 10304, as amended, is included in this Notice as Attachment A.

The effective date of this rule change is **May 1, 2005**, for all claims filed with NASD on or after that date.

Questions/Further Information

Questions regarding this *Notice* can be directed to Jean I. Feeney, Vice President and Chief Counsel, Dispute Resolution, at (202) 728-6959 or jean.feeney@nasd.com; or Laura Gansler, Assistant General Counsel, Regulatory Policy and Oversight, at (202) 728-8275 or laura.gansler@nasd.com.

Background and Discussion

Who Makes Eligibility Determinations

Rule 10304 provides that a claim is ineligible for arbitration under the Code if six or more years have elapsed from the occurrence or event giving rise to the claim. Currently, this rule does not state whether the eligibility of a claim is determined by arbitrators or by the courts; however, it is NASD's practice that arbitrators resolve questions concerning whether a particular claim falls within the six-year time limit. The issue of whether arbitrators or courts should determine the eligibility of a claim generated a significant amount of collateral litigation, and was eventually addressed by the United States Supreme Court in December 2002. In *Howsam v. Dean Witter Reynolds, Inc.*,² the Supreme Court determined that the issue of whether a claim is time-barred under Rule 10304 is a matter for arbitrators to decide. Therefore, to provide additional notice and guidance to parties on this issue, NASD is amending Rule 10304 to provide explicitly that the arbitrators make eligibility determinations.

Effect of Arbitrator's Dismissal of Claim as Ineligible

NASD is amending Rule 10304 to clarify that the dismissal of a claim on eligibility grounds does not prohibit a party from pursuing the claim in court. This clarification is necessary because some courts, relying on the "election of remedies" doctrine, have held that claims dismissed as ineligible in arbitration may not be litigated in court. Therefore, Rule 10304 is being amended to state that, under NASD rules, the ineligibility of a claim under Rule 10304 is not intended to prevent a party from filing the claim in court.³

In order to protect parties from having to litigate related claims in two forums at the same time, NASD also is amending Rule 10304 to provide that, by requesting dismissal of a claim on eligibility grounds in the NASD forum, the respondent is agreeing that the claimant may withdraw all related claims without prejudice and may pursue all of the claims in court.⁴ This provision will provide significant protection against involuntary splitting ("bifurcation") of claims, yet continue to allow arbitrators to decide questions of eligibility under Rule 10304.

Applicability of Eligibility Rule to Claims Ordered to Arbitration by Court

NASD is modifying Rule 10304 to provide that the six-year time limit on the submission of claims will not apply to any claim that is directed to arbitration by a court of competent jurisdiction upon request of a member or associated person. Currently, Rule 10304 does not apply to any claims ordered to arbitration by a court. Under the Supreme Court's decision in *Howsam* that eligibility is an issue for the arbitrators, not courts, to resolve, this provision would mean that the eligibility rule could not be applied by either the court or the arbitrators to any claims compelled to arbitration. Under the amendment, however, a member or associated person that compels a claim to arbitration may not then seek to dismiss the claim in arbitration on eligibility grounds. The SEC recently approved a corollary rule filing that amends Rule 3110(f) to require member firms seeking to compel arbitration of claims initiated in court to arbitrate all of the claims contained in the complaint if the customer so requests (regardless of whether such claims would otherwise be time-barred by the eligibility rule).⁵

NASD believes that, by clarifying the scope and application of Rule 10304, the rule amendments will streamline the administration of arbitrations as well as reduce the cost and delay caused by collateral litigation.

Effective Date Provisions

The rule amendments will become effective on **May 1, 2005**. The amendments will apply to claims filed with NASD Dispute Resolution on or after the effective date.

Endnotes

- 1 Exchange Act Rel. No. 50714 (Nov. 22, 2004), 69 Fed. Reg. 69971 (Dec. 1, 2004) (File No. SR-NASD-2003-101).
- 2 537 U.S. 79 (2002).
- 3 The claims would still be subject to applicable statutes of limitations in court.
- 4 See note 3 above.
- 5 *Notice to Members 05-10*; see Exchange Act Rel. No. 50713 (Nov. 22, 2004), 69 Fed. Reg. 70293 (Dec. 3, 2004) (File No. SR-NASD-98-74).

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ATTACHMENT A

New text is underlined; deletions are in brackets.

10304. Time Limitation Upon Submission

(a) No dispute, claim, or controversy shall be eligible for submission to arbitration under this Code where six (6) years have elapsed from the occurrence or event giving rise to the act or dispute, claim or controversy. The panel will resolve any questions regarding the eligibility of a claim under this Rule.

(b) Dismissal of a claim under this Rule does not prohibit a party from pursuing the claim in court. By requesting dismissal of a claim under this Rule, the requesting party agrees that if the panel dismisses a claim under the Rule, the party that filed the dismissed claim may withdraw any remaining related claims without prejudice and may pursue all of the claims in court.

(c) This Rule shall not extend applicable statutes of limitations[, nor shall it apply to any case which is directed to arbitration by a court of competent jurisdiction]; nor shall the six-year time limit on the submission of claims apply to any claim that is directed to arbitration by a court of competent jurisdiction upon request of a member or associated person.