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I. INTRODUCTION

Quick, easy and inexpensive are buzzwords often used to describe arbitration. As the Supreme Court observed, arbitration is favored because of its "simplicity, informality and expedition."[1] In most cases, arbitration allows a dispute to proceed from birth to resolution more quickly and with fewer costs than it could in the courts.[2]

As simple, informal, and expeditious as arbitration may be, the parties must still agree to and enter into arbitration to realize its full benefits.[3] The more hurdles placed in the path to the arbitration forum, the more expensive the ultimate resolution.

In securities arbitration disputes, a split in the federal circuits arose over whether an arbitrator or a court should determine if the National Association of Securities Dealers Code of Arbitration Procedure ("NASD Code") Section 10304 barred the bringing of a claim that was more than six years old.[4] While some courts have held the issue was a procedural one for the arbitrator to decide,[5] others have held that it was a substantive issue for the courts to decide.[6]

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1. Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc., 473 U.S. 614, 628 (1985). The informality and expeditiousness of arbitration has been questioned by many. *See, e.g., Report of the Arbitration Policy Task Force to the Board of Governors National Association of Securities Dealers, Inc., reprinted in* Fed. Sec. L. Rep. (CCH) [1995-1996 Transfer Binding], P87,735, at 87,433 (Mar. 6, 1996) [hereinafter *Task Force Report*] ("the increasing litigious nature of securities arbitration has gradually eroded the advantages of SRO arbitration."); C. Evan Stewart, *No Longer Simple, Quick, Informal or Inexpensive*, N.Y. L.J., June 15, 1995, at 5; Susan Antilla, *Wall Street, The Next Magic Bullet? Mediation*, N.Y. TIMES, Feb. 5, 1995, § 3, at 3; Bill Barnhart, *Few Satisfied with Securities Arbitration*, CHI. TRIB., Aug. 22, 1994, § 3 (Business); Jay Matthews, *Arbitration Cases Grow in Number and Complexity*, WASH. POST, Jan. 9, 1994, at H01.

2. See, e.g., Lynn Katzler, *Should Mandatory Written Opinions be Required in All Securities Arbitrations?: The Practical and Legal Implications to the Securities Industry*, 45 AM. U. L. REV. 151, 184 n.227 (1995) (citing a study that revealed that the average securities arbitration costs $12,000 less than a court proceeding and takes less time to conclude).

3. Mitsubishi, 473 U.S. at 628.

4. See *infra* notes 134 – 40 and accompanying text.

5. Katzler, *supra* note 2.

Obviously, the resolution of the time eligibility rule by the court delays the resolution of the dispute diminishes the benefits and duplicates the efforts of arbitration.

This note focuses on the Supreme Court's resolution of the circuit split and the practical effects to the investor of the decision. This note discusses briefly the history of arbitration in Part II. In Part III, the NASD Code § 10304 and its application is laid out. In Part IV, the interpretation of NASD Code § 10304 by the circuit courts is examined. The facts, procedural history and the majority opinion of *Howsam v. Dean Witter Reynolds, Inc.* are discussed in Part V. Finally, the impact on the individual investor is discussed in Part VI.

II. HISTORICAL BACKGROUND

a. Origins of Arbitration

Arbitration has been in existence for hundreds of years.[7] The origins of arbitration can be traced back to Roman and Canon law.[8] In the common law, private arbitration first was used to resolve disputes in the fourteenth century.[9] Most of the early private arbitration proceedings took place within trade groups.[10] These trade groups established standards of business behavior and procedures for resolving disputes.[11] Community elders, serving as arbitrators, resolved disputes by applying formal and informal community norms.[12]

Beginning in the seventeenth century, many merchant and craft guilds in England used arbitration to resolve disputes.[13] These groups preferred arbitration for two reasons.[14] First, the guilds believed that courts lacked the requisite knowledge to effectively resolve trade disputes.[15] Second, the court system was slow and cumbersome and, as a result, expensive.[16] In contrast, the arbitrators were experts in the various trades, and drew on customary trade practices as

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6. *Id.*
7. *See* Julius Henry Cohen & Kenneth Dayton, *The New Federal Arbitration Law*, 12 VA. L. REV. 265, 266 (1926).
8. Katherine Van Wezel Stone, *Rustic Justice: Community and Coercion Under the Federal Arbitration Act*, 77 N. C. L. REV. 931, 969 (1999).
9. *Id.* at 969-70.
10. *Id.* at 970.
11. *Id.*
12. *Id.*
13. Stone, *supra* note 8, at 970.
14. *Id.*
15. *Id.*
16. *Id.* at 970-71.

sources of law.[17] These informal arbitral forums eventually became the London Court of International Arbitration.[18]

In the United States, arbitration developed in a similar manner.[19] During the colonial period, certain trade groups used arbitration to resolve disputes among their members.[20] In 1768, the New York Chamber of Commerce created a system to "settle business disputes according to trade practice rather than legal principles."[21] Trade association arbitration continued to grow. By 1927, the American Arbitration Association's Year Book on Commercial Arbitration in the United States listed over one thousand trade associations that employed a system of arbitration for dispute resolution.[22]

b. Tension Between the Courts and Private Arbitration in the Early Nineteenth Century

Despite the growth of arbitration, it remained in tension with the courts. Common law courts refused to order specific performance on agreements to arbitrate.[23] Courts believed arbitration agreements were subject to the "revocability doctrine", i.e., an agreement to arbitrate was revocable by either party until an award was given.[24] According to the "revocability doctrine," the agreement to arbitrate created an agency relationship between the parties and the arbitrator. This agency relationship could be terminated at any time by either party without the threat of damages.[25] As a result, a party lacked the ability to enforce an agreement to arbitrate.[26]

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17. *Id.* at 971.

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id, (*quoting Linda R. Singer, *Settling Dispute: Conflict Resolution in Business, Families and the Legal System* 5 (1990)) [internal quotations omitted].

22. *See* American Arbitration Association, Year Book on Commercial Arbitration in the United States (1927).

23. *See, e.g., In re* Smith & Service, 25 L.R. 545, 547 (Q.B.D. 1890) ("A Court of Equity had no power to decree specific performance of an agreement to refer to arbitration . . .").

24. While common law courts would not grant specific enforcement to a promise to arbitrate, once arbitration was held and an award was rendered, most courts would enforce it. *See* Brazill v. Isham, 12 N.Y. 9, 10 (1854) (dismissing the trial court judgment in favor of a valid arbitral award); Reizenstein v. Hahn, 12 S.E. 43, 44 (N.C. 1890) (affirming the lower court's enforcement of an arbitration award). At common law, arbitral awards were binding, and in many jurisdictions they could be converted into a judgment of the court. *See* Red Cross Line v. Atlantic Fruit Co., 264 U.S. 109, 121-23 (1924).

25. 77 Eng. Rep. 595, 596 (K.B. 1609).

Throughout the nineteenth century the revocability doctrine held strong and American courts refused to recognize arbitration agreements. The courts justified the doctrine by reasoning that the parties were not able to "oust the court of the jurisdiction" by private contract.[27] This ouster rationale was adopted by the Supreme Court in *Line Insurance Co. v. Morse*.[28] The Court held "agreements in advance to oust the courts of jurisdiction conferred by law are illegal and void."[29] The "ouster rationale" was the primary justification for the revocability doctrine.[30]

c. Federal Arbitration Act

i. Purpose of the Act

In 1925, the Federal Arbitration Act ("FAA") was enacted to end the courts' hostility toward arbitration.[31] The FAA made agreements to arbitrate enforceable in federal court by putting them on the "same footing as other contracts."[32] The FAA was intended to overcome the "jealousy of the...courts for their own jurisdiction."[33] This jealousy of courts for their own jurisdiction was so strongly rooted in the judicial system that only an act of Congress could overcome it.[34]

"It is, however, fair to assume from that an agreement like this, which leaves the disposition of the whole matter to arbitration is not a bar to an action in court, even if it may support an action for breach of the agreement. In such a case, when no arbitration has been actually begun and expenses incurred, only nominal damages could be recovered."
Aktieselskabet Korn-Og Foderstof Kompagniet v. Rederiaktiebolaget Atlanten, 250 F. 935, 937 (2d Cir. 1918)

26. *See Brazill*, 12 N.Y. at 14; *Reizenstein*, 12 S.E. at 44.

27. Line Ins. Co. v. Morse, 87 U.S. 445, 451 (1874) ("[A]greements in advance to oust the courts of the jurisdiction conferred by [the] law are illegal and void.").

28. *Id.* at 445.

29. *Id.* at 451.

30. *See* Linda R. Hirschman, *The Second Arbitration Trilogy: The Federalization of Arbitration Law*, 71 VA. L. REV. 1305, 1318-19 (1985).

31. Scherk v. Alberto-Culver Co., 417 U.S. 506, 510 (1974).

32. H.R. Rep. No. 68-96 (1924). "The need for the law arises from the anachronism of our American law. Some centuries ago, because of the jealousy of the English courts for their own jurisdiction, they refused to enforce specific agreements to arbitrate upon the ground that courts were there by outset from their jurisdiction. This jealousy survived for so long a period that the principle became firmly embedded in the English common law was adopted with it by the American courts. The courts have felt that the precedent was too strongly fixed to be overturned without legislative enactment, although they have frequently criticized the rule and recognized its illogical nature and the injustice which results from it. This bill declares simply that such agreements for arbitration shall be enforced, and provides a procedure in the Federal courts for their enforcement." *Id.*

33. *Id.*

34. *Id.*

In passing the FAA, Congress stated that it was doing so "simply [so] that such agreements for arbitration shall be enforced."[35]

Section 2 of the FAA is its primary substantive provision.[36] It provides:

> A written provision in any...contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such a contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.[37]

The FAA accomplished the goal of putting agreements to arbitrate on the same footing as other agreements. Arbitration is now the judicially preferred method of dispute resolution.[38] In the landmark case, *Moses H. Cone Memorial Hospital v. Mercury Construction Corporation*[39] the Court confirmed that the FAA creates a "liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary."[40] In addition, the Court held that any doubt concerning substantive arbitrability, i.e. whether a claim was suitable for arbitration, should be decided in favor of arbitration.[41]

The effect of *Moses H. Cone Memorial Hospital* was not immediately known since the case was brought in federal court.[42] A year later in *Southland Corporation v. Keating*, the Supreme Court confirmed that the FAA must be

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35. *Id.*

36. Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24 (1983).

37. 9 U.S.C. § 2 (2002).

38. Dennis P. O'Leary, PaineWebber Inc. v. Elahi: The *First Circuit Provides a Return for Investors and Allows Them Their Day in Arbitration*, 32 NEW ENG. L. REV. 553, 560 (1998).

39. *See Moses H. Cone Mem'l Hosp.*, 460 U.S. at 1.

40. *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24.

41. *Id.* at 24-25 (stating that "[f]ederal law in the terms of the Arbitration Act governs that issue [the issue of whether the dispute was arbitrable] in either state or federal.... Section 2 is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary. The effect of the section is to create a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act.... The Arbitration Act establishes that, as a matter of federal law, 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.").

42. The result of *Moses H. Cone Memorial Hosp.* was not apparent inasmuch as that case was brought in federal, not state court. *Southland Corp. v. Keating*, 465 U.S. 1, 35 (1984) (O'Connor, J., dissenting).

applied in state court as well.[43] The Court held that pursuant to the FAA, courts had the power to create a body of federal substantive law that must be applied in both federal and state courts.[44] The result is preemption of state laws that are contrary to the FAA.[45]

In *Allied-Bruce Terminix Company v. Dobson*, the Court was asked to overrule *Southland* because the FAA was not a substantive statute, but a procedural statute, and, as such, it should be limited to enforcement in the federal courts.[46] The Court's refusal to overrule *Southland* solidified the position the FAA.[47] The decisions in *Moses H. Cone Memorial Hospital* and *Southland* demonstrated the Court's readiness to fortify the role of the FAA and recognize the Congressional intent to place agreements to arbitrate on the "same footing as other contracts."[48]

These decisions strongly influenced the Court's decision to endorse securities arbitration. The next section discusses the relationship between securities arbitration and the FAA.

ii. Securities Arbitration and the FAA

1. Overview

When a customer signs up for a securities account he/she is required to sign a non-negotiable brokerage agreement with the brokerage house.[49] The agreement often contains an arbitration clause requiring the parties to arbitrate all disputes. If arbitration is needed, it is conducted by one of the securities industry's self-regulated organizations ("SRO").[50] The investor often chooses which SRO will administer the arbitration from a list provided in the brokerage agreement. The number of SROs that the brokerage firm can list in its agreement is

43. *Southland Corp.*, 465 U.S. at 12. In *Southland*, convenience store franchisees sued the franchisor for, *inter alia*, fraud, breach of contract, and violations of the California Franchise Investment Law. *Id.* at 4. A provision of the California Franchise Investment Law did not allow arbitration of claims that arose from it. *Id.*

44. *Id.* at 12.

45. *Id.* at 16. The Court held that California law was preempted by the FAA. Accordingly, the Court stated "Congress intended [the FAA] to foreclose state legislative attempts to undercut the enforceability of arbitration agreements." *Id.* The Court reached this conclusion to prevent forum shopping. *Southland Corp.*, 465 U.S. at 15.

46. *Allied-Bruce Terminix Co. v. Dobson*, 513 U.S. 265, 272 (1995). The Court refused to overrule *Southland* because nothing had changed in the ten years to erode its authority. *Id.*

47. *Id.* at 281.

48. H.R. Rep. No. 96 (1924).

49. Guy Nelson, *The Unclear "Clear and Unmistakable" Standard: Why Arbitrators, Not Courts, Should Determine Whether Securities Investor's Claim is Arbitrable*, 54 VAND. L. REV. 591, 592 (2001).

50. *Id.*

expansive, as it includes all the major stock exchanges (NYSE, AMEX, etc.) and the NASD.[51] Each SRO is about the same, but there may be some variation due to the fact that each individual SRO has its own set of procedural rules governing the arbitration proceeding.[52]

Today, courts favor the brokerage firm arbitration agreements outlined above. But, as the next section shows, that has not always been the case.

2. The *Wilko* Doctrine

The first case dealing with an arbitration clause in a brokerage agreement was *Wilko v. Swan*.[53] The issue in the case was simply whether an agreement to arbitrate a future securities dispute was enforceable.[54] The Court held that such an agreement was not enforceable because a pre-dispute arbitration agreement deprived the investor of the right to seek redress in the courts.[55] In addition, it deprived an investor of that right when "he/she is less able to judge the weight of the handicap" that arbitration would place on him/her."[56] The Court in *Wilko* had a strong distrust of arbitration.[57] This distrust was based on the belief that arbitrators may not understand the law and, as a result, misapply it.[58] Furthermore, arbitrators rarely issued written opinions discussion the reasoning behind their decisions, thus it was difficult for courts to review the decisions.[59] The *Wilko* Court's distrust of arbitration's ability to be an adequate alternate forum held strong for the next 30 years.[60]

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51. *Id.* at 592-93.

52. *Id.* For a history of securities arbitration see Norman S. Poser, *Making Securities Arbitration Work*, 50 SMU L. REV. 277, 280-87 (1996).

53. Wilko v. Swan, 346 U.S. 427 (1953) (holding that courts should not enforce pre-dispute arbitration agreements). Wilko was induced to buy stock of a company through false representations. *Id.* at 428-29 Wilko brought suit claiming damages due to the false representations. *Id.* The respondents moved to have the case arbitrated as required by the parties' agreement. *Id.* at 429

54. *Id.* at 430.

55. *Id.* at 438.

56. *Id.* at 435.

57. CHRISTOPHER R. DRAHOZAL, COMMERCIAL ARBITRATION: CASES AND PROBLEMS 145 (Matthew Bender & Company, Inc. 2002). *See also* Stephan J. Ware, *Default Rules from Mandatory Rules: Privatizing Law Through Arbitration*, 83 MINN. L. REV. 703, 719-22 (1999) (concluding that most arbitration decisions will be upheld by the courts even if arbitrators do not apply the law or apply the law incorrectly).

58. DRAHOZAL, *supra* note 57, at 145.

59. *Id.*

60. Relying on *Wilko*, courts of appeals held that a wide array of federal statutory claims could not arbitrated: antitrust, *see e.g.*, Am. Safety Equip. Corp. v. J.P. Maquire & Co., 391 F.2d 821 (2d Cir. 1968); Sec. Exch. Act of 1943, McMahon v. Shearson/American Exp., Inc., 788 F.2d 94,96

3. 1985: The Abolishment of the *Wilko* Doctrine[61]

Beginning in the 1970's, the Court began chipping away at the Court's *Wilko*'s policy of distrust toward arbitration and permitted the arbitration of some statutory claims.[62] In 1974, the Court in *Scherk v. Alberto-Culver Company* found that a claim under the Securities Exchange Act of 1934 could be arbitrated.[63] The Court distinguished Wilko by the fact that the transaction in *Scherk* was an international transaction.[64] The nature of the transaction (international vs. domestic) allowed the Court to avoid its decision in *Wilko* and affirm an agreement to arbitrate.[65]

In 1985, the Court heard two cases in the same term that dealt with the arbitration of claims arising from international transactions that would put *Wilko*'s anti-arbitration stance in serious doubt. The first case was *Dean Witter Reynolds, Incorporated v. Byrd*.[66] In *Byrd*, the issue was whether claims arising from an international transaction should be bifurcated to allow federal claims to be heard by a court, while state claims are heard by an arbitrator as agreed.[67] The Court held that this bifurcation was required by the FAA "even [though] the result would be the possibly inefficient maintenance of separate proceedings in different forums."[68] In essence, the Court held that arbitration agreements were to be enforced, even though such enforcement caused delay and duplication of effort.[69]

(2d Cir. 1986), *rev'd*, 482 U.S. 220 (1987); Commodities Exchange Act, Marchese v. Shearson Hayden Stone, Inc., 734 F.2d 414, 419-21 (9th Cir. 1984); racketeering (RICO), Page v. Moseley, Hallgarten, Estabrook & Weeken, Inc., 806 F.2d 291, 298-300 (1st Cir. 1986); patent, Beckman Instruments, Inc. v. Technical Dev. Corp., 433 F.2d 55, 63 (7th Cir. 1970), *cert. denied*, 401 U.S. 976 (1971); copyright, Kamakazi Music Corp. v. Robbins Music Corp., 522 F. Supp. 125, 137 (S.D.N.Y. 1981), *aff'd*, 684 F.2d 228 (2d Cir. 1982); non-core bankruptcy proceedings, Zimmerman v. Continental Airlines, 712 F.2d 55, 59 (3d Cir. 1983), *overruled*, Hays & Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 885 F.2d 1149, 1155 (3d Cir. 1989); Title VII, Utley & Goldman Sachs & Co., 883 F.2d 184, 187 (1st Cir. 1989), *cert. denied*, 493 U.S. 1045 (1990); age discrimination, Nicholson v. CPC Int'l Inc., 877 F.2d 221, 231 (3d Cir. 1989); ERISA, Barrowchough v. Kidder, Peabody & Co., 752 F.2d 923, 941 (3d Cir. 1985), *overruled*, Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 7 F.3d 1110 (3d Cir. 1993).

61. Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213, 217 (1985) (holding that arbitrable and non-arbitrable claims must be tried separately by court and arbitration panel, "even where the result would be the possibly inefficient maintenance of separate proceedings in different forums").

62. *See Scherk*, 417 U.S. at 506 (holding that an international transaction could be arbitrated).

63. *Id.* at 515-17

64. *Id.*

65. *Id.*

66. *Byrd*, 470 U.S. at 213.

67. *Id.* at 214.

68. *Id.* at 217.

69. *Id.*

The second case was *Mitsubishi Motors Corporation v. Soler Chrysler-Plymouth Inc.*.[70] At issue was whether a court should enforce an agreement to arbitrate an antitrust claim that arose from an international transaction.[71] The Court held that the dispute must be arbitrated because this was the only way to retain predictability for parties to international agreements.[72] The Court recognized that arbitration was capable of handling complex factual and legal issues.[73] Similarly, the Court held that streamlined procedures of arbitration did not infringe on substantive rights.[74] Finally, there was no reason to assume arbitrators would disregard the law from the outset.[75] If they did, the judicial review, although limited, offered sufficient protection.[76]

The Court in *Byrd* directly attacked the *Wilko* decision.[77] The *Wilko* Court stated that arbitration was not competent to handle complex cases; the *Byrd* Court stated that it could. The *Wilko* Court stated that arbitration infringed on substantive rights, the *Byrd* court found it did not. Although the *Wilko* Court held that arbitrators often disregard the law, the *Byrd* Court held that they do not. However, the *Byrd* Court did not specifically overrule *Wilko*. That would come four years later.

Two years after *Byrd*, the Court decided *Shearson/American Express v. McMahon*.[78] The issue presented was whether claims brought under the Exchange Act of 1934 could be arbitrated.[79] The Court held that they could be arbitrated.[80] The Court reasoned that the *Wilko* Court had "a general suspicion of the desirability of arbitration and the competence of arbitral tribunals."[81]

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70. *Mitsubishi Motors Corp.*, 473 U.S. at 614.

71. *Id.* at 624.

72. *Id.* at 629.

73. *See id.* at 633-34 (stating that "potential complexity should not suffice to ward off arbitration").

74. *Id.* at 628 (recognizing that "[b]y agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.").

75. *Id.* at 636-37, n.19 (declining to assume that arbitration will not be resolved in accordance with statutory law, but reserving consideration of "effect of an arbitral tribunal's failure to take cognizance of the statutory cause of action on the claimant's capacity to reinitiate suit in federal court").

76. *Id.* at 638.

77. DRAHOZAL, *supra* note 56, at 145.

78. Shearson/American Express Inc. v. McMahon, 482 U.S. 220 (1987).

79. *Id.* at 225.

80. *Id.* at 238.

81. *Id.* at 231. Justice Frankfurter noted in his dissent in *Wilko* that the Court's opinion was not based on facts, either "in the record. . .or] in the facts of which [it could] take judicial notice. . .

Since *Wilko*, the Securities and Exchange Commission had been given additional power to review arbitration procedures to ensure they properly protected consumers.[82] This added protection was enough to overcome *Wilko's* "general suspicion" of arbitration, thus the concerns voiced by the *Wilko* Court no longer existed.[83]

The Court's decision in *McMahon* cast serious doubt on the continuing validity of *Wilko* itself. In 1989, the Court resolved this uncertainty in *Rodriguez de Quijas v. Shearson/American Express.*[84] The *Rodriguez* Court addressed the issue of whether an agreement to arbitrate claims under the Securities Act of 1933 was enforceable.[85] The Court held that agreements to arbitrate claims under the Securities Act of 1933 were fit for arbitration.[86] In so holding, the Court stated "*Wilko* was incorrectly decided and is inconsistent with the prevailing uniform construction of other federal statutes governing arbitration agreements."[87] This sweeping language effectively overruled *Wilko*[88].

In *Rodriguez*, the Court finally overruled *Wilko* and its questionable suspicion of securities arbitration.[89] The overruling of *Wilko* removed all restrictions, except those included in the FAA itself, to the arbitration of securities law disputes.[90] The *Rodriguez* Court's acceptance of arbitration for the resolution of securities disputes was more in "step with [the] current strong endorsement" of arbitration.[91]

The importance of *McMahon* and *Rodriguez*, respectively, was demonstrated by the increase in securities arbitration after each decision. The number

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," that "the arbitral system. . .would not afford the plaintiff the rights to which he is entitled. Wilko v. U.S., 346 U.S. 427, 439 (Frankfurter, J., dissenting).

82. *McMahon*, 482 U.S. at 238 (stating that "the SEC has sufficient statutory authority to ensure that arbitration is adequate to vindicate Exchange Act rights").

83. *Id.* (holding "agreements to arbitrate Exchange Act claims 'enforce[able] . . . in accord with the explicit provisions of the Arbitration Act.'") (quoting Scherk v. Alberto-Culver Co., 417 U.S. 506, 520 (1974)).

84. Rodriguez de Quijas v. Shearson/American Express, Inc., 490 U.S. 477, 478 (1989). The resolution of this issue would either affirm or overturn *Wilko*.

85. *Id.* at 478. The resolution of this issue would either affirm or overturn *Wilko*. *Id.* at 479 (stating that the Court granted certiorari on the case to determine if the cases subsequent to *Wilko* had overturned *Wilko*'s principle).

86. *Id.* at 481 (holding that the "outmoded presumption of disfavoring arbitration proceedings is set to one side").

87. *Id.* at 484.

88. *Id.*

89. *Id.*

90. The FAA provides that a predispute resolution arbitration agreement "shall be valid, irrevocable, and enforceable, save upon grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2 (2003). In *Rodriquez*, the Court recognized that the FAA provided for the nullification of those agreements that were reached through fraud or disproportionate bargaining power. *Rodriquez*, 490 U.S. at 483-84.

91. *Rodriquez*, 490 U.S. at 481 (stating that the anti-arbitration approach of *Wilko* "has fallen far out of step with [the] current strong endorsement of the federal statutes favoring" arbitration).

of matters arbitrated doubled in the first year after *McMahon* was decided[92] and continued to increase after *Rodriguez*.[93] The growth has continued to this day as evidenced by the fact that the NASD handled over 7000 cases in 2001.[94]

III. NASD § 10304: THE "TIME ELIGIBILITY" RULE

In adopting a pro-arbitration doctrine, the Court was careful to point out that arbitration does not result in any loss of a substantive right.[95] Arbitration was described as a "special kind of forum-selection clause"[96] where a party "trades the procedures and opportunity for review of the courtroom for the simplicity, informality and expedition of arbitration."[97] This conclusion was reached by the Court without examining any of the specific procedures that SROs developed to govern the arbitration proceeding.[98] The rest of this paper focuses on the NASD Code of Procedure § 10304 and the question of whether the arbitrator or the court should decide the issue raised by this specific provision.

a. NASD § 10304

The NASD Eligibility Rule in § 10304 provides as follows:

> 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. This section shall not extend applicable statutes of limita-

92. John P. Cleary, *Filling Mastrobuono's Order: The NASD Arbitration Policy Task Force Ensures the Enforceability of Punitive Damages Awards in Securities Arbitration*, 52 BUS. LAW. 199 (1996).

93. *Id.* In 1987, the NASD handled less than 3000 cases. In 1996, the NASD handled over 6000 cases.

94. *See* NATIONAL ASSOCIATION OF SECURITIES DEALERS, 2001 ANNUAL FINANCIAL REPORT 5 (2001).

95. *Rodriquez de Quijas*, 490 U.S. at 481; *McMahon*, 482 U.S. at 229 (1987). A securities industry member stated that "the way arbitration was sold to both the Supreme Court and the SEC was that essentially you have the same rights in arbitration as you would in court." Constantine N. Katsoris, *New York Stock Exchange, Inc. Symposium on Arbitration in the Securities Industry*, 63 FORDHAM L. REV. 1499, 1523 (1995) (panelist Mr. Page).

96. *Rodriguez de Quijas*, 490 U.S. at 483 (quoting *Scherk*, 417 U.S. at 519 (1974)).

97. *See, supra,* note 1.

98. The Court maintains that the FAA requires enforcement of agreements to arbitrate, but it does not prescribe the procedures that govern the arbitration proceeding. *See e.g.*, Volt Info. Sci., Inc. v. Bd. of Tr. of Leland Stanford Junior Univ., 489 U.S. 468 (1989) ("There is no federal policy favoring arbitration under a certain set of procedural rules; the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate.").

> tions, nor shall it apply to any case which is directed to arbitration by a court of competent jurisdiction.[99]

The rule is clear. No claim may be submitted to arbitration if six years have elapsed from the date of the occurrence or event that gave rise to the claim.[100] The date of the securities purchase normally marks the commencement of the time limit.[101] In short, investors must submit their claims within six years of the securities purchase.[102]

The six-year limit is not the only potential time limit on a claim. Section 10304 also states that the "section shall not extend applicable statutes of limitations."[103] There are two possible situations where this clause will be relevant. First, if an investor submits a claim to arbitration within the six-year limit, but the statute of limitations limit has run, the claim is barred.[104] Second, if the investor does not submit a claim within the six-year limit, but the statute has not expired, the claim is likewise barred.[105]

b. Application of NASD Code § 10304

Few statutes of limitations span more than six years.[106] However, an extension of the statute may be granted for many reasons, including the failure to discover the injury.[107] For example, the four-year statute of limitations for a civil RICO claim may be extended for a variety of reasons.[108] In the Second Circuit, "each time a plaintiff discovers, or should have discovered," a new injury caused by a RICO violation a new four year statute of limitations begins.[109] In New York,[110] breaches of contract and fiduciary duty have a six-year statute of limitation, but it does not begin to accrue until damages occur.[111] The statute

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99. NASD Code of Arbitration Procedure, § 10304 (July 1996).

100. Margaret M. Harding, *The Cause and Effect of the Eligibility Rule in Securities Arbitration: The Further Aggravation of Unequal Bargaining Power*, 46 DEPAUL L. REV. 109, 141 (1996).

101. *Id.*

102. *Id.*

103. NASD Code of Arbitration Procedure, § 10304 (July 1996).

104. Harding, *supra* note 100, at 141.

105. *Id.* at 141-42.

106. *Id.* at 142.

107. *Id.*

108. *Id. See also* Rotella v. Wood, 528 U.S. 549, 552 (2000).

109. Harding, *supra* note 100, at 142. *Citing* Bingham v. Zolt, 66 F.3d 553, 559 (1995) (stating this rule is known as the "special accrual rule").

110. Harding, *supra* note 100, at 142. Most customer agreements specify New York as the parties' choice of law. *See also* Seth E. Lipner & Herbert M. Deutsch, *The Statute of Limitations and Securities Arbitration: Law, Practice and Procedure*, at 5 (PLI CORP. LAW AND PRACTICE COURSE HANDBOOK SERIES NO. 819, July-Aug. 1993).

111. Harding, *supra* note 100, at 142.

of limitations for fraud is either six years from the injury or two years from the discovery of the fraud.[112]

These principles that extend statute of limitations do not apply to NASD Code § 10304.[113] As these examples show, an investor could have a claim that is not barred by the applicable statute of limitations, but is barred by NASD Code § 10304.

The SRO time eligibility rule is more likely to be applied when state common law or federal law claims are involved, rather than securities related claims. In the securities context, the statutes of limitations have relatively short time periods and tolling is impossible because tolling principles are inapplicable.[114] For example, a party must bring a cause of action arising under section 10(b) and Rule 10b-5 of the Exchange Act within one year of discovery and within three years of the actual event or occurrence.[115] The same is true for claims arising under sections 11 and 12(2) of the Securities Act.[116]

However, even though the NASD Code § 10304 is not applicable in the federal securities context it plays an important role in securities litigation. There are many claims, such as breach of contract and fraud, that have statutes of limitations that may be tolled beyond six years. Thus, NASD Code § 10304 plays an integral part in determining whether such claims may be brought before an arbitrator.

As a result, the question of who decides whether NASD Code § 10304 has expired, thus barring a claim, is of crucial importance to the investor. The next section discusses this issue and demonstrates its importance.

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112. *Id.*
113. *Id.*
114. *Id.*
115. *Id.* at 143. *See also* Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350, 361 (1996).
116. Harding, *supra* note 100, at 143. *See* 15 U.S.C. § 77m (2003).

IV. DETERMINING THE MEANING OF NASD CODE § 10304

a. Should the arbitrator or the court decide the eligibility of a claim?

Generally, courts will apply the letter of the law with less deference to what is "fair, just or sensible under the circumstances."[117] On the other hand, arbitration allows for "more simplicity, informality and expedition."[118] Consequently, an investor, with less time and money to expend in dispute resolution may fair better with an arbitrator than a judge.[119]

Until courts began addressing NASD Code § 10304, it appeared that the FAA required that the arbitrator, not the court, decide if a claim was time barred.[120] As is discussed in the next section, the courts believed that a timeliness issue was one of "procedural arbitrability" for the arbitrator to decide.

b. Timeliness is an issue of "procedural arbitrability"

In *John Wiley & Sons, Inc. v. Livingston*, the issue was whether an arbitrator or a court should determine if a claim was forfeited because notice of a claim was not filed with the Union Shop Steward within four weeks of the event or occurrence.[121] The Court held that the arbitrator should determine the timeliness issue.[122] In doing so, the Court drew a distinction between "substantive arbitrability" issues and "procedural arbitrability" issues.[123] While the courts are to

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117. Harding, *supra* note 100, at 145. *See also* Perry E. Wallace, Securities Arbitration After McMahon, Rodriquez and the New Rules: Can Investors' Rights Really Be Protected?, 43 VAND. L. REV. 1199, 1248 (1990).

118. See, *supra*, note 1..

119. Mitsubishi Motors Corp., 473 U.S. at 628.

120. Harding, *supra* note 100, at 145. *See, e.g.*, Local 285, Serv. Employees Int'l Union v. Nonotuck Res. Assocs., Inc., 64 F.3d 735, 740 (1st Cir. 1995); Washington-Baltimore Newspaper Guild, Local 35 v. Washington Post, 959 F.2d 288, 291 (D.C. Cir. 1992); Shearson Lehman Hutton, Inc. v. Wagoner, 944 F.2d 114, 121 (2d Cir. 1991); General Promotional Employees of Affiliated Indus., Local Union No. 744 v. Metropo. Distrib., Inc., 763 F.2d 300, 303 (7th Cir. 1985); Nursing Home & Hosp. Union No. 434 v. Sky Vue Terrace, Inc., 759 F.2d 1094, 1097 (3d Cir. 1985); County of Durham v. Richards & Assocs., 742 F.2d 811, 815 (4th Cir. 1984); Commerce Park at DTW Freeport v. Mardian Const. Co., 729 F.2d 334, 339 (5th Cir. 1984); Belke v. Merrill Lynch, Pierce, Fenner & Smith, 693 F.2d 1023, 1028 (11th Cir. 1982); O'Neel v. National Ass'n of Sec. Dealers, Inc., 667 F.2d 804, 807 (9th Cir. 1982).

121. John Wiley & Sons, Inc. v. Livingston, 376 U.S. 543, 544 (1964).

122. *Id.*

123. *See, e.g.*, Auto., Petroleum & Allied Indus. Employees Union, Local No. 618 v. Town & Country Ford, Inc., 709 F.2d 509, 510-11 (8th Cir. 1983). "Substantive arbitrability" is the resolution of the issue of whether the subject matter of the claim can be arbitrated according to the agreement. *Id.* "Procedural arbitrability" is the resolution of the procedural questions, such as whether a six-year time limit prevents a claim from being submitted to arbitration. *Id.*

determine "substantive arbitrability," in the cases where the arbitrability of the subject matter is clear there often arises a question over whether the procedures of arbitration have been followed.[124] The Court left these procedural issues up to an arbitrator because it was more likely to require partial or complete determination of the merits.[125] In addition, the separation of "procedural issues" would not only create the complex task of dividing up related issues, but also require duplication of effort.[126]

As a result of *John Wiley*, a time eligibility issue, such as the one presented by NASD Code § 10304, was deemed by most courts to be a procedural issue and subject to the arbitrator's jurisdiction.[127] As the First Circuit stated, "Thirty years of Supreme Court and federal circuit precedent have established that issues concerning the timeliness of a filed grievance are 'classic' procedural questions to be decided by an arbitrator...."[128] As a result, the classification of a question as "substantive" or "procedural" is central to whether the arbitrator or the courts have jurisdiction. If an issue is deemed to be a substantive question, then there must be clear and unmistakable evidence that the parties intended for the arbitrator, not the court, to decide the issue. The clear and unmistakable evidence principle is discussed in the next section.

c. Clear and Unmistakable Principle

The test used to resolve the issue of who, the court or the arbitrator, determines if a substantive claim is eligible for arbitration was first articulated in

124. *John Wiley*, 376 U.S. at 558. "While the courts have the task of determining "substantive arbitrability," there will be cases in which arbitrability of the subject matter is unquestioned but a dispute arises over the procedures to be followed. In all of such cases, acceptance of Wiley's position would produce the delay attendant upon judicial proceedings preliminary to arbitration." *Id.*

125. *Id.*

126. *Id.*

127. *See, e.g.*, County of Durham v. Richards & Assocs. Inc., 742 F.2d 811, 815 (4th Cir. 1984).

128. Local 285, Serv. Employees In'tl Union v. Nonotuck Resource Assocs., Inc., 64 F.3d 735, 739 (1st Cir. 1995). This result was reached if the time eligibility issue arose under a contractual provision, an SRO rule, or a state statute of limitations. *See, e.g., id.* (stating an agreement incorporated two-year statute of limitations and the issue of timeliness was for the arbitrator); *Town & Country Ford, Inc.*, 709 F.2d at 512 (discussing whether contract provision containing time limitation was for arbitrator); Belke v. Merrill Lynch, Pierce, Fenner & Smith, 693 F.2d 1023, 1028 (11th Cir. 1982) (finding that arbitrator should decide issue of whether claim was brought in accordance with contract time limitation); O'Neel v. Nat'l Ass'n of Sec. Dealers, Inc., 667 F.2d 804, 807 (9th Cir. 1982) (holding that arbitrator must decide whether claim is timely as required by five-year limitation on submission); Shearson Lehman Hutton, Inc. v. Wagoner, 944 F.2d 114, 121 (2d Cir. 1991) (stating that "any limitations defense—whether stemming from the arbitration agreement, arbitration association rule, or state statute—is an issue to be addressed by the arbitrators").

AT&T Technologies, Inc. v. Communications Workers of America.[129] In *AT&T Technologies*, the issue was who should determine whether the parties intended to arbitrate grievances concerning layoffs and who would decide the merits of the matter.[130] The Court held the court was to decide if a party agreed to arbitrate a particular claim, unless the parties "clearly and unmistakably" agreed otherwise.[131] The court may not rule on the merits of the case.[132] Thus, once a court determines that the agreement requires arbitration of the substantive issues, then the arbitrator is to determine all "procedural" questions which grow out of the dispute and bear on its final disposition."[133]

In *First Options of Chicago, Inc. v. Kaplan*, the Court affirmed *AT&T Technologies* by holding that the "clear and unmistakable" requirement ensured that the intentions of the parties determined the issue of whether or not the parties agreed to arbitrate.[134] A party must only be required to arbitrate those substantive issues that he or she agreed to arbitrate.[135] As a result, the courts must interpret silence or ambiguity on the question of "who" decides the question of substantive arbitrability in favor of the courts.[136] This principle protects "unwilling parties...[from] arbitrate[ing] a matter they reasonably would have thought a judge, not an arbitrator, would decide."[137]

Although the application of this precedent to the SRO time eligibility rule seems to require the arbitrator to determine a question of timeliness because it is a procedural issue, a split in the circuits developed.[138] Five federal circuits determined that courts should decide the issue as to whether a claim was barred by NASD Code § 10304 because it was a substantive issue.[139] Another five federal

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129. AT&T Techns, Inc. v. Communications Workers, 475 U.S. 643 (1986).
130. *Id.* at 645-46.
131. *Id.* at 648-49.
132. *Id.* at 640-50.
133. *John Wiley*, 376 U.S. at 557.
134. First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 943 (1995).
135. *Id.* at 945.
136. *Id.*
137. *Id.*
138. Harding, *supra* note 100, at 147.
139. *See, e.g.*, PaineWebber, Inc. v. Hofmann, 984 F.2d 1372 (3d Cir. 1993); Dean Witter Reynolds, Inc. v. McCoy, 995 F.2d 649 (6th Cir. 1993); Smith Barney, Inc. v. Sarver, 108 F.3d 92 (6th Cir. 1997); Edward D. Jones & Co. v. Sorrells, 957 F.2d 509 (7th Cir. 1992); Cogswell v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 78 F.3d 474 (10th Cir. 1996); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Cohen, 62 F.3d 381 (11th Cir. 1995).

In addition, the state courts are split on the question of who should decide a SRO time eligibility issue. *See, e.g.*, Cigna Fin. Advisors v. Rosen, No. CV 94 0705235S (Conn. Super. Ct. Jun. 12, 1997), 1997 Conn. Super. LEXIS 1634 (holding that courts decide eligibility question); Citibank v. Crowell, Weedon & Co., 4 Cal. App. 4th 844 (Cal. App. 1992) (construing identical language in Municipal Securities Rulemaking Board Arb. Code, rule G-35, Sec. 6, holding courts decide); Smith Barney, Inc. v. Keeney, 570 N.W.2d 75 (Iowa 1997) (holding arbitrators decide); Shahan v. Staley, 188 Ariz. 74, 932 P.2d 1345 (Ariz. App. 1997) (to same effect).

circuits held to the contrary, finding that the question was for the arbitrators to decide because it was a procedural issue.[140]

Not only are circuits split on the outcome, but they were also divided as to the reasoning used to reach the outcome. For example, the First Circuit held that the question of timeliness is for the arbitrator, unless the parties clearly and unmistakably express intent to make it a question for the court.[141] The Second Circuit found that arbitrators should decide the issue because it found the provision to be ambiguous and applied the contract interpretation principle of *contra proferentum*.[142] The Fifth Circuit reasoned that the decision was for the arbitrator because SRO time eligibility is a question of procedural rather than substantive arbitrability.[143] The Eighth Circuit found that the NASD Code § 10304 rule is clearly an issue for arbitrators because NASD Code § 10324 of the SRO arbitration procedural code required such a result.[144]

This split was resolved by the Supreme Court in *Howsam v. Dean Witter Reynolds, Inc.* The facts and discussion of that case are laid out in the next section.

V. *HOWSAM V. DEAN WITTER REYNOLDS, INC.*

In *Howsam v. Dean Witter Reynolds, Inc.*, the Supreme Court answered the question of who should determine whether a court or an arbitrator should primarily interpret and apply NASD Code § 10304. The Court ultimately held that the matter was for the arbitrator. The facts of the case are presented next, followed by an analysis of the opinion, and finally the impact of the decision is addressed.

140. *See, e.g.*, PaineWebber Inc. v. Elahi, 87 F.3d 589 (1st Cir. 1996); PaineWebber Inc. v. Bybyk, 81 F.3d 1193 (2d Cir. 1996); Smith Barney Shearson, Inc. v. Boone, 47 F.3d 750 (5th Cir. 1995); FSC Sec. Corp. v. Freel, 14 F.3d 1310 (8th Cir. 1994); O'Neel v. Nat'l Ass'n of Sec. Dealers, Inc., 667 F.2d 804 (9th Cir. 1982).

141. *Elahi*, 87 F.3d at 599.

142. *Bybyk*, 81 F.3d at 1199.

143. *Boone*, 47 F.3d at 753-54.

144. *Freel*, 14 F.3d at 1310 (basing its holding on the fact that § 10324 unambiguously grants arbitrators power to decide all issues under the Code).

a. Facts and Procedural History

i. Facts

In 1986, after her husband's death, Karen Howsam ("Howsam") opened a securities account for herself and her family with Dean Witter Reynolds, Inc. ("Dean Witter").[145] When Howsam opened the account, two brokers for Dean Witter advised her to invest in four limited partnerships.[146] For the next eight years, Dean Witter continued to invest Howsam in the four limited partnerships and Dean Witter brokers continued to advise her that the investments were of good value and right for Howsam's investment needs.[147]

In 1992, Howsam entered into a new client agreement with Dean Witter.[148] The agreement required that Howsam arbitrate any disputes that may arise between Dean Witter.[149] Specifically, the agreement stated that Howsam must arbitrate "all controversies" that arose from "any account maintained...; any transaction...;" or any controversy that involved the performance or breach of the agreement.[150] In addition, the agreement required that New York law be used in construing and enforcing the agreement.[151]

In late 1994, Howsam closed her accounts with Dean Witter when she learned her investments were unsound and took her money to another investment firm.[152]

On March 7, 1997, Howsam began arbitration regarding Dean Witter's recommendation to invest in the four limited partnerships.[153] The arbitration took place before the NASD pursuant to the 1992 agreement.[154] Howsam alleged that Dean Witter made material misrepresentations before she purchased the investments; Dean Witter knew that the investments were not right for her investment

145. Dean Witter Reynolds, Inc. v. Howsam, 261 F.3d 956, 958 (10th Cir. 2001).
146. *Id.*
147. *Id.*
148. *Id.*
149. *Id.*
150. *Id.* The relevant part of the agreement provided that "The Client agrees that all controversies between the Client and Dean Witter and/or any of its officers, directors, or employees, present or former, concerning or arising from (i) any account maintained with Dean Witter by Client; (ii) any transaction involving Dean Witter and Client, whether or not such transaction occurred in such account or accounts; or (iii) the construction, performance or breach of this or any other agreement between us, whether such controversy arose prior to, on or subsequent to the date hereof, shall be determined by arbitration before any self-regulatory organization or exchange of which Dean Witter is a member. The Client may elect which of these arbitration forums shall hear the matter . . . ." *Id.*
151. *Id.*
152. *Id.*
153. *Id.*
154. *Id.*

needs.[155] In addition, Howsam alleged that Dean Witter misrepresented the truth regarding the soundness of the investments after she had purchased them.[156] As a result of these misrepresentations Howsam alleged that she did not have the opportunity to learn that the investments were failing until late 1994.[157]

In order to arbitrate her claims, Howsam executed an agreement with the NASD.[158] The agreement stated that the arbitration would be conducted in accordance with the NASD rules and procedures.[159] In addition, the NASD agreement stated that "the undersigned parties hereby state that they have read the procedures and rules" of the NASD.[160] The NASD Code § 10304 provides that no "dispute, claim or controversy" is eligible for arbitration if it is more than six years old.[161]

ii. Procedural History

1. District Court

Dean Witter, based on this provision, requested declaratory relief from the district court stating Howsam's claims were not timely, and, thus, not subject to arbitration by the NASD.[162] Dean Witter argued that the question of timeliness was for the court, not the arbitrators, to decide.

In response, Howsam filed a motion to dismiss for lack of jurisdiction.[163] Howsam argued that the district court did not have jurisdiction to decide the timeliness issue because the parties had agreed to submit all account disputes to arbitration in their 1992 agreement.[164] Howsam also argued that the 1992

155. *Id.*
156. *Id.*
157. *Id.*
158. *Id.* at 958-59.
159. *Id.* at 959. Specifically, the agreement stated: "The undersigned parties hereby submit the present matter in controversy, as set forth in the attached statement of claim, . . . to arbitration in accordance with the Constitution, By-Laws, Rules, Regulations, and/or Code of Arbitration Procedure of the sponsoring organization." *Id.*
160. *Id.* Specifically, "The undersigned parties hereby state that they have read the procedures and rules of the sponsoring organization relating to arbitration." *Id.*
161. *See* NASD Code § 10304 (stating that "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.").
162. *Howsam*, 261 F.3d at 959.
163. *Id.*
164. *Id.*

agreement required New York state law govern any dispute.[165] New York state law required that the arbitrator resolve the timeliness issue under § 10304 of the NASD Code.[166]

The district court granted Howsam's motion.[167] That court determined that the language of the agreement provided "clear and unmistakable" proof that the parties intended to submit all the issues, including arbitrability, to the NASD arbitrators.[168]

2. Tenth Circuit Court of Appeal

On appeal to the Tenth Circuit Court of Appeal, Dean Witter argued that the 1992 agreement did not "clear[ly] and unmistakabl[y]" demonstrate the parties' intent to have the substantive question of arbitrability resolved by the arbitrator, rather than the court.[169]

The circuit court first determined that NASD Code § 10304 involved the "subject matter jurisdiction" of the arbitrator because the six-year time limit was a "substantive limit" on claims that could be submitted to arbitration.[170] As such, it was a question of substantive arbitrability, rather than procedural arbi-

165. *Id.*

166. *Id. See also* Smith Barney Shearson Inc. v. Sacharow, 689 N.E.2d 884 (N.Y. 1997). In *Sacharow*, New York's highest court reviewed an arbitration agreement which stated that "'any controversy . . . shall be settled by arbitration' in accordance with the rules of the NASD Code," and which provided that all disputes would be governed by New York law. *Sacharow*, 689 N.E.2d at 885. The *Sacharow* court acknowledged that arbitrability is ordinarily a question for the courts under New York law, but noted that "an . . . exception has evolved which recognizes, respects and enforces a commitment by the parties, nevertheless, to arbitrate even that issue when they 'clearly and unmistakably [so] provide.'" Id. at 887 (quoting *AT&T Technologies*, 475 U.S. at 649). Relying upon the Second Circuit's opinion in *Bybyk*, 81 F.3d at 1199, the New York Court of Appeals held that the words "any and all controversies" were expansive enough to "'encompass disputes over whether a claim is timely and whether a claim is within the scope of arbitration.'" *Sacharow*, 689 N.E.2d at 887 (quoting *Bybyk*, 81 F.3d at 1199). The court further noted that "the appropriate remedy for the party alleging a violation of [§ 10304] of the NASD Code 'is to defend the arbitration action on timeliness grounds, not to enjoin arbitration altogether.'" Id. (quoting *Bybyk*, 81 F.3d at 1200).

167. *Howsam*, 261 F.3d at 960.

168. Dean Witter Reynolds, Inc. v. Howsam, No. 97-WM-1463, slip op. at 2-4 (D. Colo. June, 28, 1999).

169. *Howsam*, 261 F.3d at 960. Dean Witter also argued that the district court erred in two other ways. *Id.* First, Howsam's motion to dismiss was, "in effect, a motion to dismiss pursuant to Rule 12(b)(6)," and, as a result, no reference to the 1992 agreement could be made because Dean Witter had not brought it into issue in the complaint. *Id.* The Court held that the district court's review of the 1992 access agreement was proper, regardless of whether Howsam's motion was considered under Rule 12(b)(1) or Rule 12(b)(6). *Id.* at 962. Second, even if the court could look at the 1992 agreement it was irrelevant because it had been superceded by the 1997 agreement to submit the issue to NASD arbitration. *Id.* at 960. Thus, the 1992 agreement was no longer controlling. *Id.* The Court held that the 1992 access agreement, as supplemented by the 1997 submission agreement, was the operative agreement between the parties. *Id.* at 963.

170. *Id.* at 965.

trability.[171] According to *First Options*, questions of substantive arbitrability were presumed to be decisions for the court, not the arbitrator.[172] Of course, parties to the contrary, could rebut this presumption with a showing of clear and unmistakable intent. [173]

The court then determined that § 10304 of the NASD Code, which was incorporated in Howsam's agreement with Dean Witter, did not provide clear and unmistakable evidence that the parties intended the arbitrators to decide a question of arbitrability.[174] The language of NASD Code § 10304, stating that "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" could only be reasonably interpreted as a "substantive limit on the claims that the parties have contracted to submit to arbitration."[175] The court concluded that NASD Code § 10304 defines the "substantive jurisdiction" of the arbitrator, thus the courts must determine the issue of whether a claim is time barred under NASD Code § 10304.[176]

The court also dismissed the argument that NASD Code § 10324, which states that "arbitrators shall be empowered to interpret and determine the applicability of all provisions under [the NASD Code]"[177], provided clear and unmistakable evidence that an arbitrator should resolve the timeliness question.[178] The court cited *Cogswell v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, which had reasoned that NASD Code § 10324 did not specifically refer to the question of who should decide the timeliness under NASD Code § 10304, but was a general provision.[179] Furthermore, because NASD Code § 10324 was a general provision, principles of contract interpretation require that the specific provisions take precedence over the more general provisions and NASD Code § 10304 was a specific provision addressing an arbitrator's jurisdiction.[180]

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171. *Id.*
172. *Id.* at 964.
173. *Id.*
174. *Id.* at 965.
175. *Id.* [internal citations omitted].
176. *Id.* [internal citations omitted].
177. *See* NASD Code § 10324.
178. *Howsam*, 261 F.2d at 965.
179. Cogswell v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 78 F.3d 474, 479, 480 (10th Cir. 1996). In *Cogswell*, the court dealt with NASD Code §§ 15 and 35. Effective July 1, 1996, the NASD initiated a new numbering system under which NASD Code § 15 was changed to NASD Code § 10304 and NASD Code § 35 was changed to NASD Code § 10324. The text of both sections remained the same, therefore, the case law applies equally.
180. *Id.*

Lastly, the court held that the agreement between Howsam and Dean Witter did not provide "clear and unmistakable" evidence that the parties intended the arbitrator, rather than the court, to determine the issue of timeliness.[181] The court found no language in the contract that specifically referred to arbitrability.[182] The court held that the language in the contract that stated that both parties had "waived their right to seek remedies in court" was ambiguous and doubted that Howsam intended to waive all her access to the courts.[183] The court reasoned that such a reading of the provision would result in Howsam losing any right to compel arbitration, vacate an award if the arbitrator exceeded his/her powers, or seek enforcement of the award.[184]

The Tenth Circuit recognized that the Courts of Appeals were evenly split on whether NASD Code § 10304 was a substantive eligibility requirement that must be determined by the courts.[185] The Supreme Court granted certiorari to resolve this disagreement among the Courts of Appeals.[186]

181. *Howsam*, 261 F.3d at 968.
182. *Id.* at 969.
183. *Id.*
184. *Id.*
185. *Id.* at 969-70.
186. *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 82-83 (2002).

b. Analysis of the Supreme Court Opinion

i. Discussion of the Majority Opinion[187]

1. The Issue

The Court began by providing the principles that would define the issue. Primarily, no person can be forced to arbitrate, unless there was a valid contract requiring arbitration.[188] When there was a valid contract for arbitration, the courts favored arbitration to litigation in almost all instances.[189] There was, however, a well-established exception to the policy of favoring arbitration.[190] This exception applied when there was a question of substantive arbitrability, i.e. whether the parties agreed to arbitrate the subject matter of the dispute.[191] In such a situation, the courts did not favor arbitration, but reserved the issue for

187. Justice Thomas reached the same conclusion as the Court by applying New York State law to the question presented. *Howsam*, 537 U.S. at 87 (Thomas, J., concurring). Justice Thomas began his concurring opinion by stating that arbitration was a "matter of contract." *Id.* As such, any agreement to arbitrate controversies must be enforced just as any other contract would be enforced. *Id. See Volt*, 489 U.S. at 468. Specifically, the contract must be enforced according to its terms. *Howsam*, 537 U.S. at 87 (Thomas, J., concurring). If the contract contained a choice-of-law provision, then the courts must enforce this provision and the law of jurisdiction selected must be applied to the agreement. *Id. See also Volt*, 489 U.S. at 478-79 (enforcing choice-of-law provision that required the application of state procedural law to the arbitration proceeding); *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 67 (1995) (Thomas, J., dissenting) (stating that a choice-of-law provision must be enforced). Justice Thomas concluded that enforcement of the choice-of-law provision "easily resolve[d] the question presented in this case." *Howsam*, 537 U.S. at 87 (Thomas, J., concurring). Justice Thomas pointed out that the agreement before the Court provided that it "shall be construed and enforced in accordance with the laws of the State of New York." *Id.* The State of New York Court of Appeals held on two occasions that time limit rule of NASD Code § 10304 is for the arbitrator, rather than the court. *Id. See* Smith Barney Shearson Inc. v. Sacharow, 689 N.E.2d 884 (N.Y. 1997). Howsam and Dean Witter agreed that New York law should govern any dispute. *Id.* This term of the agreement must be enforced. *Id.* Thus, Justice Thomas concluded that the question is for the arbitrator as required by New York State law. *Id.*

188. *Howsam*, 537 U.S. at 83.

189. *Id.* ("The Court has. . .long recognized an enforced a 'federal policy favoring arbitration agreements.'" (quoting Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24-25 (1983))).

190. *Howsam*, 537 U.S. at 83 (stating that it is "clear that there is an exception to [the policy favoring arbitration]).

191. A question of arbitrability is simply a question of whether or not the parties agreed to arbitrate the particular dispute. *See Howsam*, 537 U.S. at 82-83.

the courts.[192] Only if there was "clear and unmistakable" intent by the parties to arbitrate questions of substantive arbitrability did courts allow an arbitrator to settle the issue.[193]

With these principles clearly expressed, the Court stated that the issue in the case was whether there was clear and unmistakable intent by Howsam and Dean Witter to arbitrate the issue of substantive arbitrability.[194]

2. Narrow Scope of Substantive Arbitrability

After framing the issue, the Court turned to substantive arbitrability.[195] The scope of substantive arbitrability issue was central because if the issue was not a question of substantive arbitrability, then it was presumptively for the arbitrator. Justice Breyer noted that any preliminary dispositive question could be a question of substantive arbitrability because the answer to the question determines whether arbitration happens or not.[196] However, such a broad interpretation was conclusively not desirable because every preliminary question would be decided by the court and arbitration's benefit of quick adjudication of disputes would be lost.[197] Accordingly, the Court narrowly interpreted the issue of substantive arbitrability.[198]

This narrow interpretation required that an issue be arbitrated, unless three conditions were met. First, the issue must be of such a character that the parties "would likely have expected a court" to decide the issue.[199] Second, the parties were not "likely to have thought that they had agreed that an arbitrator would [decide the issue]."[200] Finally, allowing the court to decide the issue "avoids the risk of forcing parties to arbitrate" an issue they had not agreed to arbitrate.[201]

3. When the Question of Substantive Arbitrability Exception Applied

The Court determined that there were two issues that courts had the sole power to resolve. The first was whether a party was bound by an arbitration

192. *Howsam*, 537 U.S. at 83 (stating that the "'the question of arbitrability,' is 'an issue for judicial determination....'" (quoting *AT&T Technologies*, 475 U.S. at 649. *See also First Options*, 514 U.S. at 944.

193. *Howsam*, 537 U.S. at 83 (quoting *AT&T Technologies*, 475 U.S. at 649.)

194. *Howsam*, 537 U.S. at 83.

195. *Id.*

196. *Id.*

197. *Id.*

198. *Id.* (stating that questions of arbitrability are limited in scope). *See also First Options*, 514 U.S. at 942.

199. *Howsam*, 537 U.S. at 83.

200. *Id.*

201. *Id.* at 83-84.

agreement.[202] The second was whether an arbitration clause was applicable to a particular dispute.[203] These issues fell within the issue of substantive arbitrability because courts usually decided them, the parties expected a court to decide them, and giving a court jurisdiction avoided the risk of unwanted arbitration.[204]

4. When the Question of Substantive Arbitrability Exception Did Not Apply

The question of substantive arbitrability exception did not apply in other general situations "where parties would likely expect an arbitrator" to decide the matter.[205] For instance, "procedural questions" that develop during the dispute and affect the outcome of the dispute were for the arbitrator.[206] In addition, any "allegations of waiver, delay, or a like defense to arbitrability" were for the arbitrator to decide.[207]

The substantive arbitrability questions were reserved for the court and the procedural arbitrability questions were reserved for the arbitrator.[208] Procedural questions such as if "*time limits*, notice, laches, estoppel, and other conditions precedent" were met were reserved for the arbitrator.[209]

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202. *Id.* at 84 (stating that a "gateway dispute about whether the parties are bound by a given arbitration clause. . . [is] for a court to decide."). *See First Options*, 514 U.S. at 943-46 (holding that a court should decide whether non-signatories to an arbitration agreement are bound by the arbitration agreement); *John Wiley*, 376 U.S. at 546-47 (holding that a court should decide the question of whether an arbitration agreement survived a corporate merger).

203. *Howsam*, 537 U.S. at 84. *See, e.g., AT&T Technologies*, 475 U.S. at 651-52 (holding that courts should decide whether labor-management layoff dispute is within scope of arbitration agreement); Atkinson v. Sinclair Refining Co., 370 U.S. 238, 241-244 (1962) (holding that courts should decide whether claims for damages caused by breach of no-strike agreement are covered by arbitration clause for various "grievances").

204. *See Howsam*, 537 U.S. at 84.

205. *Howsam*, 537 U.S. at 84.

206. *Id.* (quoting *John Wiley*, 376 U.S. at 557 (holding that an arbitrator should decide whether prerequisite steps required for arbitration were fulfilled)).

207. *Howsam*, 537 U.S. at 84 (quoting *Moses H. Cone Mem'l Hosp.*, 460 U.S. at 24-25). The Revised Uniform Arbitration Act of 2000 has codified these holdings when it states that an "arbitrator shall decide whether a condition precedent to arbitrability has been fulfilled." REVISED UNIF. ARBITRATION ACT § 6(c) cmt. 2, 7 UNIF. ADOPTION ACT § 12-13 (Supp. 2002).

208. *Howsam*, 537 U.S. at 84-85 (quoting from REVISED UNIF.ARBITRATION ACT § 6 cmt. 2, 7 UNIF. ADOPTION ACT at § 13 (Supp. 2002) (emphasis in original).

209. *Howsam*, 537 U.S. at 85 (quoting from REVISED UNIF. ARBITRATION ACT § 6 cmt. 2, 7 UNIF. ADOPTION ACT at § 13 (Supp. 2002) (emphasis in original)).

5. Application of Precedent to *Howsam*

The Court followed its own precedent and held that the NASD Code § 10304 issue was a matter "presumptively for the arbitrator, not for the judge."[210] The Court emphasized that "the time limit rule closely resembles [other] gateway questions not found to be questions of arbitrability."[211] For instance, *Moses H. Cone Memorial Hospital* held that gateway questions of "waiver, delay, or a like defense" were reserved for the arbitrator.[212] These gateway issues were an integral part of the controversy that brought the parties to arbitration, and, as such, went to the heart of the matter.[213]

The Court held that NASD Code § 10304 issue was a "procedural question" rather than a "substantive question."[214] As such, the Court did not have to look to whether there was "clear and unmistakable" evidence of intent on the part of the parties to send the issue to the arbitrator because "procedural issues" were presumptively for the arbitrator to decide.[215]

6. NASD Arbitrators: Best Interpreters of NASD Rules

After holding that the NASD Code § 10304 issue was presumptively for the arbitrators to decide, the Court reasoned that it made sense to allow NASD arbitrators to resolve issues involving NASD Rules.[216] Comparatively, these arbitrators were in the best position to interpret and know the meaning of their own rule.[217] Therefore, they were the proper party to apply the rule.[218]

The Court inferred that the parties, when making the agreement, were aware that the NASD arbitrators were the most qualified to deal with the NASD rules.[219] As a result, it was reasonable to infer that the parties would desire

210. *Howsam*, 537 U.S. at 85.
211. *Id.*
212. *Id.* at 85. *See e.g. Moses H. Cone Memorial Hospital*, 460 U.S. at 24-25 ("The Arbitration Act establishes that, as a matter of federal law, 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.").
213. *Howsam*, 537 U.S. at 85. *See also John Wiley*, 376 U.S. at 559 (A dispute over waiver, delay, or time limits is an "aspect of the [controversy] which called the grievance procedures into play.").
214. *Howsam*, 537 U.S. at 85.
215. *Id.*
216. *Id.* ("The NASD arbitrators, comparatively more expert about the meaning of their own rule, are comparatively better able to interpret and to apply it.").
217. *Id.*
218. *Id.*
219. *Id.*

NASD arbitrators to resolve any dispute regarding NASD rules.[220] Thus, in the absence of any statement to the contrary, the NASD arbitrators were the arbiters of NASD questions.[221]

"This result", the Court stated, "secures a fair and expeditious resolution" of the issue because it allowed the most informed decision-maker to resolve the controversy.[222] This was a goal of both the courts and arbitration.[223]

7. "Eligible" for Arbitration

The Court next turned to Dean Witter's argument that the NASD Code § 10304 time limitation issue was for the courts, even if the Court took the pro-arbitration position.[224] Dean Witter argued that Howsam signed the Uniform Submission Agreement with the NASD in 1997.[225] The agreement incorporated the NASD Code into Howsam and Dean Witter's agreement.[226] Dean Witter pointed out that the NASD Code § 10304 used the word "eligible".[227] As a result, Dean Witter claimed that word demonstrated the parties intent to have the courts resolve the time limit before arbitration.[228]

The Court dismissed this argument by stating that parties to arbitration agreements "normally expect a forum-based decisionmaker to decide forum-specific" conditions to arbitration.[229] In addition, Dean Witter's argument that the word "eligible" created an anti-arbitration position was countered by § 10324 of the NASD Code which stated that "arbitrators shall be empowered to interpret and determine the applicability" of any rule in the Code.[230]

220. *Id.* (stating "it is reasonable to infer that the parties intended the agreement to reflect" the understanding that the NASD arbitrators were best qualified to settle questions regarding NASD rules).

221. *Id.* (adding that "[i]n the absence of any statement to the contrary in the arbitration agreement" the parties intended NASD arbitrators to settle a controversy over NASD rules).

222. *Id.* ("And for the law to assume an expectation that aligns (1) decisionmaker with (2) comparative expertise will help better to secure a fair and expeditious resolution of the underlying controversy – a goal of both arbitration systems and judicial systems alike.").

223. *Id.*

224. *Id.* at 86.

225. *Id.*

226. *Id.*

227. *Id.*

228. *Id.*

229. *Id.*

230. *Id.* (quoting the NASD Code § 10324).

VI. IMPACT

The Court was correct in holding that the arbitrator should determine whether a claim was timely under NASD Code § 10304. By holding that NASD Code § 10304 time issue was a "procedural question", the Court ensured that mini-trials over timeliness would be avoided, thus saving both time and money for all parties involved. The decision also guaranteed that agreements to arbitrate will be treated as all other agreements. And lastly, the decision extinguished any chance that courts may undermine the FAA through the expansion of the issue of substantive arbitrability.

a. Mini Trials

In holding that NASD Code § 10304 timeliness is a procedural one to be decided by an arbitrator, the Court avoided mini-trials. A mini-trial occurs when a court is asked to determine whether a claim must be submitted to arbitration, whether under a substantive question or a procedural question. If the mini-trial involves a procedural question, such as the time limitation of NASD Code § 10304, then the court is often required to partially or completely look into the merits of the case.[231] This mini-trial is unproductive because it causes delay, harms the investor greater than the brokerage firm, and mini-trials crowd the dockets.

i. Time is Money

Benjamin Franklin said, "Remember that time is money."[232] In dispute resolution, time is money. An attorney bills the client for time spent researching and advocating for the client. The client's time spent resolving a dispute is time that is diverted from being productive, i.e., making money. In short, the more time the parties spend resolving the dispute the more the resolution costs.

A characteristic of arbitration, contributing to its desirability, is that it allows the parties to resolve disputes more quickly, and more cheaply.[233] But, the benefits of arbitration are reduced if mini-trials of preliminary issues are permitted or required. For example, in *Howsam,* Dean Witter brought the parties into court to resolve the issue of whether the NASD Code § 10304 time bars a claim.[234] The Tenth Circuit took over four years decide the case and over a year

231. See *John Wiley*, 376 U.S. at 557 (stating that procedural issues often grow out of the dispute itself and "bear on its final disposition").

232. JOHN BARTLETT, FAMILIAR QUOTATIONS (Emily Morris Beck, ed. (14th ed. 1968).

233. *See, e.g., Katzler, supra* note 2, at 197, 184, n.227 (citing a study that revealed that the average securities arbitration costs $12,000.).

234. *Howsam*, 261 F.3d at 959.

later the Supreme Court announced its opinion.[235] *Howsam* illustrates that when most issues submitted to the courts can take years to resolve. This time spent resolving a "gateway" issue can cost the parties a significant amount of money.

The costs are not limited only to the individual parties, but the costs of a mini-trial affect society as a whole. If parties spend more time resolving disputes, then they spend less time being productive, (i.e., innovating, inventing, producing, servicing, etc.) However, if the parties proceed immediately to arbitration for resolution of the entire dispute, less time is spent resolving the dispute. If less time is spent in resolution of the dispute, then less money is spent. The money conserved by quick resolution of a dispute allows parties to use those resources in more productive ways.

The Court, by holding that NASD Code § 10304 issue is a procedural one for the arbitrator, avoids these mini-trials. The practical effect is a more efficient use of resources by both the parties individually and society as a whole.

ii. The Investor is Harmed Most by Delay

The Court's holding protects consumers because delay will harm the investor more than the brokerage firm. The investor, generally, has a limited amount of money to expend resolving a dispute. In contrast, the brokerage firm has more funds to expend and is less affected by a delay. The practical result is that the investor may be forced to abandon a claim because the potential benefit received in resolving the dispute is outweighed by the actual cost of resolving the dispute. This result is unfavorable for three reasons.

The first reason is based on the somewhat utopian idea that a remedy for a wrong should not be available only to those who can afford it. In many cases, if a mini-trial is held the investor is deprived of a remedy because he/she does not have the money necessary to go to the courts for resolution of a gateway issue, then on to arbitration to resolve the actual dispute. In short, as costs to the investor increase, the availability of the remedy to the investor decreases or is eliminated.

Second, the brokerage firm may deliberately drag out the court proceedings to erode the investor's funds. The Court in *John Wiley* recognized this risk when it noted that "the opportunities for deliberate delay" caused by "such delay may entirely eliminate the prospect of a speedy arbitrated settlement...to the

235. *Id.* The initial case was filed in April or May of 1997. The Tenth Circuit decision was filed on August 9, 2001. *Id.* at 956. The Supreme Court filed its decision on December 10, 2002. *Howsam*, 537 U.S. at 79.

disadvantage of the parties."[236] The disadvantage is clearly the increased costs of delay.[237] This disadvantage is disproportionately placed on the investor, who often has fewer resources. Thus, the brokerage firm may find it advantageous to willfully delay arbitration. The brokerage firm will find it even more advantageous if it is found in the wrong and forced to pay damages to an investor.

Finally, the abandonment of the claim may harm future investors. For example, if the brokerage firm misrepresents the value of investments, but an investor abandons the claim against the firm due to cost, the brokerage firm is unlikely to change its practices, especially if such practices were profitable. As a result, other investors may fall prey to the misrepresentation until an investor found it worthwhile to pursue a claim against the brokerage firm.

iii. Crowding the Dockets

The Court's decision to allow arbitrators to decide whether a claim is time barred by the NASD Code § 10304 helps alleviate the crowding of courts' dockets.

The dockets of the district courts are becoming more and more crowded each year. The time spent to resolve the time eligibility issue of the NASD Code § 10304 is both costly and unneeded. It is costly because the courts must take the time to examine the issues of law and fact. Procedural issues often require the court to delve into the merits of the case taking a significant amount of time and effort. This time and effort is unnecessary because an arbitrator will often "reconsider the ground covered by the court insofar as it bore on the merits of the dispute."[238] For example, the court will have to determine when the agreement between the parties was formed and the date of injury. This inquiry mirrors that which the arbitrator will be considering in the arbitration that will follow. The time spent by the courts looking into the issue of timeliness is an unneeded duplication of effort.[239]

In addition, arbitrators are fully capable of resolving the timeliness issue in a proper manner. In fact, the Court in Howsam stated that the expertise of the arbitrators in interpreting the NASD rules makes it preferable for them to resolve the issue.[240] NASD arbitrators are experts in the meaning of their own rules making them the ideal interpreters of NASD Code § 10304.[241]

236. *John Wiley*, 376 U.S. at 558.
237. *Id.*
238. *Id.*
239. *See id.*
240. *Howsam*, 537 U.S. at 85 (stating that "arbitrators...[are] comparatively more expert about the meaning of their own rule, [and] are comparatively better able to interpret and to apply it").
241. *Id.*

The Court's decision alleviates the crowding of the dockets by placing the interpretation of the NASD Code § 10304 timeliness provisions in the capable hands of the arbitrators.

b. FAA Mandates Favoring Arbitration Agreements

The Court's decision protects the FAA's primary purpose, of putting agreements to arbitrate on the same plane as other agreements.[242] Stated another way, the FAA strives to scrupulously protect the intent of the parties. And, the intent of the parties is best determined by their agreement.

In most instances, the brokerage firm prepares the securities agreement. The agreement often incorporates arbitration rules, such as the NASD Code, without discussion or explanation.[243] Thus, an investor is likely unaware or has no knowledge of the contents of the NASD Code § 10304.

If the investor reads anything, it will be the agreement. The language of most standard pre-dispute arbitration clauses used in the securities industry state that "all controversies" shall be submitted to arbitration.[244] This is the language that the investor is most likely to read and understand.[245] The specifics of the eligibility rule, in most instances, are not brought to the investor's attention and the investor is unlikely to peruse the NASD Code of Arbitration Procedure.[246] As a result, it is demonstrably illogical and unfair to rely on NASD Code § 10304 to determine what the investor's intent was when he/she signed the agreement.[247]

In Howsam's case, the agreement did not specify the particular SRO.[248] Rather, Howsam had a choice of which SRO should administer the arbitration proceeding.[249] The agreement did not discuss the rules of any particular SRO or alert the investor to the fact that most have a time eligibility rule similar to the NASD Code § 10304. Of course, providing a consumer with all the SROs' rules may not serve any purpose other than curing insomnia and may be economically infeasible, but the fact remains that the investor has no knowledge of the rules that may apply to the arbitration.

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242. *See Byrd*, 470 U.S. at 219. The Court concluded that the foremost purpose of the FAA was to ensure that the agreements to arbitrate were enforced by the courts. *Id.* at 219.

243. *See* Harding, *supra* note 100, at 155-56.

244. *See id.*

245. *See* id.

246. *See id.*

247. *See id.*

248. *Howsam*, 537 U.S. at 82.

249. *Id.*

The investor's lack of information is compounded by the investor's lack of power to change the agreement. The time limitation is not explicitly stated in the agreement and agreed upon in mutual, arms-length negotiation.[250] The brokerage firm usually provides the agreement on a "take it or leave it" basis and offers no opportunity to the investor to alter the agreement. Thus, is it disingenuous to pronounce that the investor is prevented from bringing a claim in arbitration by any time limitation other than the applicable state or federal statute of limitation.[251] Such a result unfairly deprives an investor of the arbitral forum they believed they agreed upon.

In sum, the investor is aware that the agreement states that "all controversies" will be arbitrated. Thus, the agreement, not the rules incorporated into the agreement, should be the evidence of party intent. The Court's decision protects the investor by ensuring that the agreement remains the primary source of the intent of the parties.

c. Threat of Courts Undermining FAA

Lastly, the Court's decision protects the FAA from being undermined by the judiciary. Congress enacted the FAA to reduce the judicial hostility toward arbitration's ability to resolve disputes on the merits. This hostility has been largely replaced, but the timeliness issue of § 10304 may allow courts to hide their hostility behind a cloak of goodwill. For example, if a court believed that an arbitrator would not strictly follow the law, but find for an especially sympathetic party, the court could resolve the merits of the dispute by finding the claim untimely. The court could accomplish this surreptitiously when it looks into the facts underlying timeliness issue. Courts examining the many facts dispositive to both the timeliness issue and the merits of the dispute could reach a conclusion under the guise of timeliness when actually ruling on the merits of the dispute.

If the courts were allowed to cross into arbitration's jurisdiction by way of the timeliness issue, they could undermine the FAA's primary purpose, which is to put agreements to arbitrate on the same plane as other agreements. The Court ensured against such a result by allowing the arbitrator to decide the procedural question of the NASD Code § 10304.

VII. CONCLUSION

The Court's decision makes entering arbitration easier, quicker and less expensive. The overall practical effect is to eliminate mini-trials that cost money,

250. *See* Harding, *supra* note 100, at 155-56.
251. *See id.*

harm investors disproportionately and crowd the dockets. The decision also ensures that the FAA's policy of putting agreements to arbitrate on the same footing as other agreements continues to be upheld. And lastly, the decision closes the door on any possibility of judicial hostility toward securities arbitration.