

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-59672; File No. SR-FINRA-2009-013)

April 1, 2009

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change to Amend the Tolling Provisions in Rules 12206 and 13206 of the Codes of Arbitration Procedure for Customer and Industry Disputes

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”) on March 11, 2009, the proposed rule change as described in Items I, II, and III below, which Items have been substantially prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

FINRA Dispute Resolution is proposing to amend the tolling provisions in Rules 12206 and 13206 of the Code of Arbitration Procedure for Customer Disputes (“Customer Code”) and for Industry Disputes (“Industry Code”), respectively, to clarify that the rules toll the applicable statutes of limitation when a person files an arbitration claim with FINRA.

Below is the text of the proposed rule change. Proposed deletions are in brackets.

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12206. Time Limits

(a) – (b) No change.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

(c) Effect of Rule on Time Limits for Filing Claim in Court

The rule does not extend applicable statutes of limitations; 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. However, [where permitted by applicable law,] when a claimant files a statement of claim in arbitration, any time limits for the filing of the claim in court will be tolled while FINRA retains jurisdiction of the claim.

(d) No change.

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(d) No change.

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II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the

proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Currently, Rule 12206, the “eligibility rule,” provides that, “no claim shall be eligible for submission to arbitration under the Code where six years have elapsed from the occurrence or event giving rise to the claim.”<sup>3</sup> The eligibility rule does not extend applicable statutes of limitation, but Rule 12206(c) does provide that, “where permitted by applicable law, when a claimant files a statement of claim in arbitration, any time limits for the filing of the claim in court will be tolled while FINRA retains jurisdiction of the claim.”<sup>4</sup> This means that, where permitted by applicable law, state statutes of limitation will be tolled (i.e., temporarily suspended) when a person files an arbitration claim with FINRA.

For many years, FINRA has interpreted the rule to mean that any applicable statutes of limitation would be tolled in all cases when a person files an arbitration claim with FINRA. In Friedman v. Wheat First Securities, Inc., however, the court found that the phrase “where permitted by applicable law,” means that state or federal law, as applicable, must permit tolling expressly, or the period will not be tolled.<sup>5</sup> In light of the court’s interpretation of the phrase and the negative effect it could have on investors’ arbitration claims, FINRA is

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<sup>3</sup> FINRA describes the eligibility rule using the rule number from the Customer Code for simplicity. However, the proposal also applies to the identical eligibility rule of the Industry Code. See Rule 13206.

<sup>4</sup> See also Rule 13206(c) of the Industry Code.

<sup>5</sup> 64 F. Supp. 2d 338 (S.D.N.Y. 1999). The case involved claims under Section 10(b) of the Securities Exchange Act of 1934.

proposing to remove the phrase, “where permitted by applicable law,” from Rules 12206(c) and 13206(c) to make tolling automatic as part of the arbitration agreement.

The Friedman court granted the defendant’s request to dismiss the plaintiff’s complaint on statute of limitations grounds. In arguing against dismissal, the plaintiff sought to rely on old Rule 10307(a)<sup>6</sup> of the Code of Arbitration Procedure, which was updated and is currently designated as Rules 12206(c) and 13206(c), to support his position that filing an arbitration claim tolls the applicable statute of limitations.<sup>7</sup> The court determined, however, that the language of old Rule 10307(a) does not toll the statute of limitations unless such tolling is “permitted by applicable law.”<sup>8</sup> After further analysis, the court found that no federal or state statute tolled the applicable statute of limitations and granted the defendant’s dismissal request.<sup>9</sup>

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<sup>6</sup> Rule 10307(a) (Tolling of Time Limitation(s) for the Institution of Legal Proceedings and Extension of Time Limitation(s) for Submission to Arbitration) states in relevant part that:

Where permitted by applicable law, the time limitations which would otherwise run or accrue for the institution of legal proceedings shall be tolled where a duly executed Submission Agreement is filed by the Claimant(s). The tolling shall continue for such period as the Association shall retain jurisdiction upon the matter submitted.

<sup>7</sup> 64 F. Supp. 2d at 343.

<sup>8</sup> Id.

<sup>9</sup> Id. at 347.

Other courts have reached the same conclusion in interpreting old Rule 10307(a) and the phrase “where permitted by law.” In Individual Securities v. Ross,<sup>10</sup> the plaintiff, in appealing a judgment of a New York district court that dismissed the complaint as time-barred, claimed that the statute of limitations was tolled while his matter was in arbitration with then-NASD.<sup>11</sup> The court cited old Rule 10307(a) and noted that the “where permitted by law” language referred to the applicable law in New York, which prevented tolling of the limitations period.<sup>12</sup> In Rampersad v. Deutsche Bank Securities, Inc.,<sup>13</sup> the court, citing Friedman, determined that, used in a similar context, the phrase meant that federal law, not state law, governs the availability of tolling the limitations period in a Section 10(b) cause of action.<sup>14</sup>

FINRA is concerned that courts may begin citing this interpretation to dismiss claims filed in court, as would otherwise be permitted under the eligibility rule.<sup>15</sup> FINRA does not

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<sup>10</sup> 1998 U.S. App. Lexis 12618.

<sup>11</sup> On July 26, 2007, the Commission approved a proposed rule change filed by NASD to amend NASD’s Certificate of Incorporation to reflect its name change to FINRA in connection with the consolidation of the member firm regulatory functions of NASD and NYSE Regulation, Inc. See Securities Exchange Act Rel. No. 56146 (July 26, 2007), 72 FR 42190 (August 1, 2007) (SR-NASD-2007-053).

<sup>12</sup> Id.

<sup>13</sup> 2004 U.S. Dist. Lexis 5031. The case also involved claims under Section 10(b) of the Securities Exchange Act of 1934.

<sup>14</sup> Id. In this case, the plaintiff filed an arbitration claim against the defendants at the New York Stock Exchange, Inc. (“NYSE”). The plaintiff argued that the limitations period should have been tolled under New York law for the period during which the arbitration was pending, and cited NYSE Rule 606(a), which is similar to old Rule 10307(a), and states in pertinent part:

Where permitted by law, the time limitation(s) which would otherwise run or accrue for the institution of legal proceedings, shall be tolled when a duly executed Submission Agreement is filed by the claimants.

<sup>15</sup> The rule states that “dismissal of a claim under this rule does not prohibit a party from pursuing the claim in court. By filing a motion to dismiss a claim under this rule, the

believe this outcome would be consistent with the original intent of the tolling provision or of amendments to the eligibility rule that allow customers to take their claims to court if their claims are dismissed in arbitration on eligibility grounds.<sup>16</sup> Rather, FINRA believes that, in such a situation, the rule should be read to provide that a firm or associated person has implicitly agreed to suspend any statute of limitations defense for the time period that the matter was in FINRA's jurisdiction. Amending the eligibility rule, as proposed, would make this clear.

Moreover, FINRA is concerned that the Friedman interpretation could limit or foreclose customers' access to other judicial forums to address their disputes, which would be an unfair result. Most brokerage firms require customers to arbitrate their disputes, a process that can take more than a year. Customers may be disadvantaged in a subsequent court proceeding if the panel dismisses the arbitration case on eligibility grounds and the statute of limitations is not tolled for the period of time that the customers were in arbitration. In addition to being an unfair result, FINRA believes this would undermine the intent of the eligibility rule, which gives customers the option of taking their claims to court when a case is dismissed on eligibility grounds.

Therefore, FINRA is proposing to delete the phrase "where permitted by applicable law" from Rules 12206(c) and 13206(c). FINRA notes that the Friedman interpretation suggests that, but for the phrase, the rule would be read as an explicit agreement between the

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moving party agrees that if the panel dismisses a claim under this rule, the non-moving party may withdraw any remaining related claims without prejudice and may pursue all of the claims in court." See also Rule 13206(b).

<sup>16</sup> See Securities Exchange Act Rel. No. 50714 (November 22, 2004), 69 FR 69971 (December 1, 2004) (SR-NASD-2001-101).

parties to toll the statute of limitations period.<sup>17</sup> FINRA believes that the proposed rule change would leave the parties in the same position in court as they were at the start of the arbitration with regard to any statutes of limitation: the time period before the claim was filed in arbitration would not be extended by the proposed changes, but applicable statutes of limitation would not run while the matter was in arbitration.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>18</sup> which requires, among other things, that the Association's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The proposed rule change is consistent with FINRA's statutory obligations under the Act to protect investors and the public interest because the proposal would preserve fairness in the arbitration process by ensuring that investors maintain their right to have their claims heard in court by tolling the applicable statutes of limitation while the dispute is in arbitration.

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<sup>17</sup> Friedman, 64 F. Supp. 2d 338, 343 n.4 (1999). The court indicates that it likely would accept the amended language as representing an agreement of the parties:

The precise meaning of Rule 10307(a) is not entirely clear. If the phrase "where permitted by applicable law" did not precede the remainder of the paragraph, the rule would simply be read as an explicit agreement between the parties to toll the limitations period, regardless of what the applicable state or federal tolling principles provide. However, by including the phrase the drafters seemed to limit tolling to situations in which tolling is expressly permitted by applicable law, thereby making an explicit agreement between the parties unnecessary.

<sup>18</sup> 15 U.S.C. 78o-3(b)(6).

B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received by FINRA.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:



Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2009-013 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2009-013. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 am and 3:00 pm. All comments received will be posted without change; the Commission does

not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to the File Number SR-FINRA-2009-013 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>19</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>19</sup> 17 CFR 200.30-3(a)(12).