Broom v. Morgan Stanley DW, Inc.

No. 82311-1

MADSEN, C.J. (dissenting)—The majority fails to give effect to the parties' contractual agreement to arbitrate under the National Association of Securities Dealers Code of Arbitration Procedure (NASD Code). The problem with the majority's approach is that NASD Code section 10304 *expressly* addresses time limitations and NASD Code section 10324 *expressly* grants the power to the arbitrators to interpret and apply all provisions under the NASD Code. The arbitrators had the authority to interpret the parties' contractual agreement to arbitrate. Rather than permitting the arbitrators to exercise their authority to interpret and apply NASD Code section 10304, the majority instead determines itself whether state limitations of actions will apply. Because the majority takes for itself the arbitrators' power and responsibility, its decision is contrary to arbitration law and the public policy on which it rests.

Analysis

The majority determines that vacation for legal error is appropriate and that the legal error here is that the arbitrators exceeded their powers. *See* former RCW 7.04.160(4)(a) (1943) (court may vacate an arbitration award where the arbitrators

exceeded their powers), *repealed by* Laws of 2005, ch. 433, § 50. I disagree.

"[A]rbitration stems from a contractual, consensual relationship." *Balfour, Guthrie & Co. v. Commercial Metals, Inc.*, 93 Wn.2d 199, 202, 607 P.2d 856 (1980). An arbitration agreement is valid, enforceable, and irrevocable unless there are grounds to revoke the agreement. Former RCW 7.04.010 (1947), *repealed by* Laws of 2005, ch. 433, § 50; *see* RCW 7.04.060(1) (current codification of this principle); *Barnett v. Hicks*, 119 Wn.2d 151, 154, 829 P.2d 1087 (1992). The parties' contract here *mandates* that issues of time limitations are subject to arbitration. Thus, questions of time limitations were expressly within the powers of the arbitrators. Accordingly, deciding whether statutes of limitations applied to bar claims was not, contrary to the majority, in excess of the arbitrators' powers. Under the parties' contract, the meaning of NASD Code section 10304 was also for the arbitrators to resolve.

The parties agreed to submit this matter to arbitration under the standard NASD arbitration agreement. NASD Code section 10304, which governs the issue here, states:

> **10304. Time Limitation Upon Submission**
>
> (a) No dispute, claim, or controversy shall be eligible for submission to arbitration under this Code where six (6) years have elapsed from the occurrence or event giving rise to the act or dispute, claim or controversy. The panel will resolve any questions regarding the eligibility of a claim under this Rule.
>
> . . . .
>
> (c) This rule shall 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.

(Emphasis added.)

Because the parties explicitly agreed to section 10304, the court should defer to the arbitrators' decision, particularly given the nature of time limitations in the arbitration context. This very question was before the United States Supreme Court in *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79, 85, 123 S. Ct. 588, 154 L. Ed. 2d 491 (2002). There, the Court held that "applicability of the NASD time limit rule is a matter presumptively for the arbitrator, not for the judge." *Id*. Among other reasons for this holding, the Court said that "the NASD arbitrators, comparatively more expert about the meaning of their own rule, are comparatively better to apply it. In the absence of any statement to the contrary in the arbitration agreement, it is reasonable to infer that the parties intended the agreement to reflect that understanding." *Id*.

It is undisputedly the province of the arbitrators to interpret and apply contracts for arbitration. Indeed, the United States Supreme Court pointed out in a very recent case that grounds for vacation do not arise when an arbitrator interprets and applies the parties' agreement. *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, __ U.S. __, 130 S. Ct. 1758, 176 L. Ed. 2d 605 (2010). Moreover, NASD Code section 10324 expressly provides that "arbitrators shall be empowered to interpret and determine the applicability of all provisions under this Code." The NASD arbitrators were best positioned, and had the authority under the contract, to interpret and apply the terms of the parties' agreement on time limitations. That is what the arbitrators did, after considering the parties' extensive briefing and arguments regarding the applicability of state statutes of

limitations.

The Court also determined in *Howsam* that its holding was compelled by the decisions of numerous state courts under the Revised Uniform Arbitration Act of 2000 (RUAA), which sought to "'incorporate' the holdings of the vast majority of state courts and the law that has developed under the [Federal Arbitration Act, 9 U.S.C. § 1]," [and which] states that an 'arbitrator shall decide whether a condition precedent to arbitrability has been fulfilled.'" *Howsam*, 537 U.S. at 85 (quoting RUAA § 6(c) & cmt. 2, 7 U.L.A. 12-13 (Supp. 2002)). The Court noted that comments to RUAA also say that "'issues of procedural arbitrability, *i.e.*, whether prerequisites such as *time limits* . . . and other conditions precedent to an obligation to arbitrate have been met, are for the arbitrators to decide.'" *Id*. (quoting RUAA § 6 cmt. 2, 7 U.L.A. 13 (emphasis added)).

This case is not governed by the Washington revised uniform arbitration act, chapter 7.04A RCW (Wa-RUAA), as the majority notes. The Wa-RUAA has replaced the Washington Arbitration Act (WAA), former chapter 7.04 RCW. The WAA applies here. But as the majority also notes, the portions of the two acts respecting the ground for vacating arbitration awards that is relied on in this case are the same under the two acts. Majority at 4 n.1. Significantly, the Wa-RUAA provides in addition that "[a]n arbitrator shall decide whether a condition precedent to arbitrability has been fulfilled." RCW 7.04A.060. This is the language relied on by the Court in *Howsam* when it determined that the arbitrator and not a court is to decide time limitations questions under NASD Code section 10304. Thus, the Wa-RUAA has *both* (a) the provision that the

Court held in *Howsam* means that the arbitrator decides time limitations questions and (b) the *same vacation provision* that existed in the WAA and is relied on here, former RCW 7.04.160(4). RCW 7.04A.901 provides that "[i]n applying and construing this uniform act, consideration must be given to the need to promote uniformity of the law with respect to the subject matter among states that enact it."

From these elements, it becomes apparent that the majority has misapplied the WAA's standards for vacation of an arbitration award. The relevant vacation provisions in Wa-RUAA, RCW 7.04A.230, do not permit a court to conclude that an arbitrator's resolution of questions under NASD Code section 10304 is a legal error requiring vacation because another Wa-RUAA provision, RCW 7.04A.060(3), provides that arbitrators determine whether conditions precedent to arbitrability have been satisfied (construed to include time limitations questions). If the standard for vacation relied upon would not permit vacation under the Wa-RUAA, how is it that the very same standard permits vacation under the WAA? Put another way, under the majority opinion the standard for vacation at issue here under the WAA would not apply to permit vacation under these same facts if the issue arose under the Wa-RUAA. Because there is no indication that such a sea change was intended by the legislature when it enacted the Wa-RUAA, and the standard for vacation is the same, the court should decline the parties' invitation to turn a question involving a condition precedent to arbitration into a legal error justifying vacation.

The majority states, however, that although the arbitrators had the authority to

interpret section 10304, they could not do so in violation of state case law that holds that state statutes of limitations do not apply in arbitration. Although I do not agree with the majority's apparent belief that any legal determination an arbitrator makes is subject to revision by this court, it is not necessary to resolve this issue here. Here, the question involves applicability of state statutes of limitations and the effect of an arbitration agreement providing that limitations questions are for the arbitrator.

Under our precedent, parties may agree to a contractual limitations period that is shorter than provided by statute, provided that the shorter time frame is not unreasonable or prohibited by contract or public policy; this principle applies in arbitrations. *See McKee v. AT&T Corp.*, 164 Wn.2d 372, 399, 191 P.3d 845 (2008); *Adler v. Fred Lind Manor*, 153 Wn.2d 331, 356, 103 P.3d 773 (2004); *accord Beroth v. Apollo College, Inc.*, 135 Wn. App. 551, 562, 145 P.3d 386 (2006). This being the case, there is no legal bar to parties agreeing to submit limitations periods to arbitration.

Pursuant to the parties' agreement in this case, the arbitrators' concluded that state statutes of limitations apply, effectively "shortening" the limitations period from "none" (under the majority's analysis) to the limitations periods set by state statutes. There is no statute that prohibits the parties' agreement or the arbitrators' application of the state statutes of limitations. The periods of limitations are manifestly not unreasonable or contrary to public policy because they are the very limitations periods established by the legislature for the particular claims at issue.

Although the majority acknowledges that the parties may agree to apply state

statutes of limitations, majority at 15, it nevertheless decides that the arbitrators' lacked discretion to apply the state statutes of limitations, apparently on the basis that the specific statutes of limitations were not expressly made part of the parties' agreement. The majority says that "the power to interpret [the] code . . . does not equate to a power to contravene state law." Majority at 15 n.3. But the parties agreed to submit limitations questions to arbitration—thereby agreeing to the arbitrators' decisions on applicable limitations periods. And as explained, parties may lawfully agree to shorten limitations periods *without* "contraven[ing] state law."

The majority's decision conflicts with the parties' contractual agreement to submit the time limitations issues to the arbitrator and it conflicts with provisions in the WAA and the Wa-RUAA concerning vacation of arbitration awards when arbitrators exceed their powers. It also conflicts with the public policies underlying the legal principles governing arbitration.

Our state law favors the use of arbitration where the parties agree by contract to submit disputes to arbitration. The court has noted the importance of encouraging parties to arbitrate in "our ever more litigious society." *Boyd v. Davis*, 127 Wn.2d 256, 262, 897 P.2d 1239 (1995). "Arbitration is attractive because it is a more expeditious and final alternative to litigation." *Id*. Key to preserving arbitration as an effective form of alternative dispute resolution is refusing to permit litigation of issues that have appropriately been the subject of arbitration under the terms of the parties' contractual agreement to arbitrate.

Public policy favoring arbitration is particularly well-served when court dockets are particularly stressed, as they are under current budgetary restrictions. Unfortunately, at present, due to budget limitations, some courts in our state have been forced to delay civil litigation, sometimes indefinitely, in order to accommodate requirements for timely criminal proceedings. Under such circumstances, it is even more important to adhere to the public policy favoring arbitration.

> The very purpose of arbitration is to avoid the courts insofar as the resolution of the dispute is concerned. The object is to avoid what some feel to be the formalities, the delay, the expense and vexation of ordinary litigation. Immediate settlement of controversies by arbitration removes the necessity of waiting out a crowded court docket.

Barnett, 119 Wn.2d at 160 (citations omitted).

Finally, the majority has not considered the impact of the Federal Arbitration Act, 9 U.S.C. § 1 *et seq*. (FAA, the Act). Although my primary disagreement with the majority is that the arbitrators, not the court, should decide whether state statutes of limitations apply under the parties' arbitration agreement, I believe that the standards for vacation that apply under the FAA apply in this case.

Congress enacted the FAA "[t]o overcome judicial resistance to arbitration," *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 443, 126 S. Ct. 1204, 163 L. Ed. 2d 1038 (2006), and to declare "'a national policy favoring arbitration' of claims that parties contract to settle in that manner," *Preston v. Ferrer*, 552 U.S. 346, 352, 128 S. Ct. 978, 169 L. Ed. 2d 917 (2008) (quoting *Southland Corp. v. Keating*, 465 U.S. 1, 10, 104 S. Ct. 852, 79 L. Ed. 2d 1 (1984)). Section 2 of the Act provides that an arbitration

agreement in "a contract evidencing a transaction involving commerce" is valid, irrevocable, and enforceable, except for revocation on grounds applicable to any contract. 9 U.S.C. § 2.

Because the brokerage agreement giving rise to the dispute here involves transactions impacting interstate commerce, the FAA applies to this NASD arbitration, as numerous cases show. *See*, *e.g.*, *ON Equity Sales Co. v. Pals*, 528 F.3d 564 (8th Cir. 2008); *Lincoln Nat'l Life Ins. Co. v. Payne*, 374 F.3d 672 (8th Cir. 2004); *Liberte Capital Group, LLC v. Capwill*, 148 Fed. Appx. 413 (6th Cir. 2005) (unpublished); *MONY Sec. Corp. v. Bornstein*, 390 F.3d 1340 (11th Cir. 2004); *Wash. Square Sec., Inc. v. Aune*, 385 F.3d 432 (4th Cir. 2004); *IDS Life Ins. Co. v. Royal Alliance Assocs., Inc*., 266 F.3d 645 (7th Cir. 2001); *Decker v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 205 F.3d 906 (6th Cir. 2000). This court has also determined that under the FAA all claims arising under a written brokerage agreement must be settled by arbitration in accord with the terms of the agreement. *Garmo v. Dean Witter, Reynolds, Inc.*, 101 Wn.2d 585, 586, 681 P.2d 253 (1984).

Although the respondents argued to the Court of Appeals that the FAA does not govern this matter, the FAA was clearly invoked during the arbitration proceedings and the respondents themselves stated in a brief filed in that proceeding that "the Federal Arbitration Act controls NASD arbitrations." Clerk's Papers at 162.

The respondents seem to believe, however, that the FAA does not "preempt" state law on the scope of review, i.e., it does not "preempt" state law on vacation of arbitration

of awards. However, if the FAA applies, so do its provisions on vacation and modification. The FAA does not permit vacation of an arbitration award under an "error of law" standard. Section 10 of the FAA contains very narrow grounds for vacating an award and review is under a highly deferential standard. "Courts are generally prohibited from vacating an arbitration award on the basis of errors of law or interpretation, and the express terms of 9 U.S.C. §§ 10 and 11 have been deemed the exclusive grounds for vacation or modification." *Ainsworth v. Skurnick*, 960 F.2d 939 (11th Cir. 1992); *see*, *e.g.*, *Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987, 994 (9th Cir. 2003); *George Watts & Son v. Tiffany & Co*., 248 F.3d 577 (7th Cir. 2001).

Under the FAA, too, the superior court erred in vacating the arbitration award.

Conclusion

The parties contractually agreed to submit questions of time limitations to arbitration. The issue whether any of the plaintiffs' claims were barred by state statutes of limitations was properly before the arbitrators and was fully briefed and argued. However, the majority disregards the arbitrators' express authority under the parties' agreement to interpret and apply NASD Code section 10304. The majority's decision conflicts with established principles of law respecting agreements to shorten limitations periods, arbitration, and the policies underlying these legal principles.

I would reinstate the arbitration award on the basis that vacatur was improper.

For the reasons stated in this opinion, I dissent.

AUTHOR:
Chief Justice Barbara A. Madsen

WE CONCUR:
Justice Susan Owens

Justice Mary E. Fairhurst

Justice James M. Johnson