

August 28, 1995

Ms. Jean A. Webb
Secretariat
Commodity Futures Trading Commission
2033 K Street, N.W.
Washington, D.C. 20581

Re: National Futures Association: Proposed Amendments to Sections 6, 8, 10 and 12 of NFA's Code of Arbitration and Sections 5, 7, 10 and 12 of NFA's Member Arbitration Rules

Dear Ms. Webb:

Pursuant to Section 17(j) of the Commodity Exchange Act, as amended ("the Act"), National Futures Association ("NFA") hereby submits to the Commodity Futures Trading Commission ("Commission") proposed amendments to Sections 6, 8, 10 and 12 of NFA's Code of Arbitration ("Code") and Sections 5, 7, 10 and 12 of NFA's Member Arbitration Rules ("Member Rules") (collectively "arbitration rules"). The amendments contained herein were approved by NFA's Board of Directors on August 17, 1995. NFA respectfully requests Commission review and approval of the proposed amendments.

PROPOSED AMENDMENTS

The proposed amendments to Sections 6, 8, 10 and 12 of NFA's Code of Arbitration and Sections 5, 7, 10 and 12 of NFA's Member Arbitration Rules are as follows (additions are underscored and deletions are bracketed):

CODE OF ARBITRATION

* * *

Section 6. Initiation of Arbitration.

An arbitration proceeding under this Code shall be initiated as follows:

(a) Notice of Intent to Arbitrate.

If the two-year time limit under Section 5 of this Code is close to expiring, a person wanting to file a Demand for Arbitration [A person desiring arbitration under this Code] shall notify the Secretary, either in writing or orally, of such person's intent to arbitrate. The Secretary shall maintain a



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record of the receipt of each such notice[.] and shall promptly provide such person with a copy of this Code and a Demand for Arbitration form.

(b) [Documents Furnished.] Demand for Arbitration Pursuant to a Notice of Intent to Arbitrate.

[The Secretary shall promptly provide such person with a copy of this Code and a Demand for Arbitration.] If a person who files a notice of intent to arbitrate decides to proceed with NFA arbitration, such person shall, within 35 days after the date NFA provided the person with a copy of the Code and a Demand for Arbitration form under Section 6(a) above, serve a completed Demand for Arbitration on the Secretary.

(c) Demand for Arbitration.

[If such person wishes to proceed with the arbitration, such person, within 35 days after the date of transmittal by the Secretary under (b) above, shall serve the completed Demand for Arbitration on the Secretary together with the appropriate fee (see Section 11 below) and, in an arbitration under Section 2(a)(1)(ii) or 2(b) above, a copy of the agreement to arbitrate.] The Secretary shall promptly review each Demand for Arbitration for completeness. Any Demand for Arbitration which the Secretary deems to be incomplete, or which is not accompanied by the appropriate fee, shall be returned by certified mail. In that event, such person shall serve a completed Demand for Arbitration, together with any unpaid fee, within 20 days following transmittal by the Secretary. The Secretary shall reject any Demand for Arbitration which has not been timely filed, or for which the appropriate fee has not been paid.

* * *

(m) Consolidation and Joinder.

(1) When Demands for Arbitration involving common questions of fact or arising from the same act or transactions are received by the Secretary, the Secretary may, whether or not at the request of any party, order any or all of the proceedings to be consolidated for hearing in the interest of providing a fair, equitable, and expeditious procedure and may take such action concerning the proceedings herein as may tend to avoid unnecessary or unreasonable delay.



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(2) A party may join multiple claims in a single Demand if the claims involve common questions of fact, arise from the same act or transactions, are filed by the same person against the same Respondents (even if the person filing the Demand is acting in different capacities), or are filed on behalf of an individual and a corporation against the same Respondents if the individual is the sole shareholder of the corporation. The Secretary may, whether or not at the request of any party, order any or all joined claims to be separated in the interest of providing a fair, equitable or expeditious procedure or to avoid unnecessary or unreasonable delay.

* * *

Section 8. Pre-Hearing.

* * *

(e) Other Pre-Hearing Motions

Except as provided in Section 8(a)(2) above, a party has 10 days from the date a pre-hearing motion is received in which to serve a written response on the Secretary and all other parties. However, where a motion is received less than 20 days in advance of the date the hearing or summary proceeding is scheduled to commence, NFA may, in its discretion, require a written response within less than 10 days. No written replies to a party's response to a motion will be allowed except in the Panel's discretion.

* * *

Section 10. Award, Settlement and Withdrawal.

* * *

(b) Relief.

The award may grant or deny any of the monetary relief requested, and may include an assessment of interest, costs or fees (see Sections 11 and 12). A request for declaratory relief will only be heard by the arbitrators if the Respondent agrees to have the arbitrators hear the claim.

* * *



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Section 12. Arbitration Costs.

Costs which may be included in an award shall normally be limited to the cost of any transcript which a party may request (see Section 9(d)(4) above). A Panel may, however, assess against a party any one or more of the following other costs, upon a finding that such party's claim or defense was frivolous or was made in bad faith, or that the party engaged in willful acts of bad faith during the arbitration: Reasonable and necessary expenses incurred by (a) the arbitrators or (b) any other party or witness, including reasonable attorneys' fees. The Panel may also award attorneys' fees provided that a statutory or contractual basis exists for awarding such fees. Requests for attorneys' fees and costs incurred in the arbitration proceeding must be raised in the proceeding or they are waived.

* * *

MEMBER ARBITRATION RULES

* * *

Section 5. Initiation of Arbitration.

An arbitration proceeding under these Rules shall be initiated as follows:

(a) Notice of Intent to Arbitrate.

If the two-year time limit under Section 4 of these Rules is close to expiring, a person wanting to file a Demand for Arbitration [A person desiring arbitration under these Rules] shall notify the Secretary, either in writing or orally, of such person's intent to arbitrate. The Secretary shall maintain a record of the receipt of each such notice[.] and shall promptly provide such person with a copy of these Rules and a Demand for Arbitration form.

(b) [Documents Furnished.] Demand for Arbitration Pursuant to a Notice of Intent to Arbitrate.

[The Secretary shall promptly provide such person with a copy of these Rules and a Demand for Arbitration.] If a person who files a notice of intent to arbitrate decides to proceed with



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NFA arbitration, such person shall, within 35 days after the date NFA provided the person with a copy of the Code and a Demand for Arbitration form under Section 5(a) above, serve a completed Demand for Arbitration on the Secretary.

(c) Demand for Arbitration.

[If such person wishes to proceed with the arbitration, such person, within 35 days after the date of service by the Secretary under (b) above, shall serve the completed Demand for Arbitration on the Secretary together with the appropriate fee (see Section 11 below).] The Secretary shall promptly review each Demand for Arbitration for completeness. Any Demand for Arbitration which the Secretary deems to be incomplete, or which is not accompanied by the appropriate fee, shall be returned by certified mail. In that event, such person shall serve a completed Demand for Arbitration, together with any unpaid fee, within 20 days following service by the Secretary. The Secretary shall reject any Demand for Arbitration which has not been timely filed, or for which the appropriate fee has not been paid. [If no separate Notice of Intent has been received the Demand for Arbitration shall serve as the Notice of Intent.]

* * *

(m) Consolidation and Joinder.

(1) When Demands for Arbitration involving common questions of fact or arising from the same act or transaction are received by the Secretary, the Secretary may, whether or not at the request of any party, order any or all of the proceedings to be consolidated for hearing in the interest of providing a fair, equitable, and expeditious procedure and may take such action concerning the proceedings herein as may tend to avoid unnecessary or unreasonable delay.

(2) A party may join multiple claims in a single Demand if the claims involve common questions of fact, arise from the same act or transactions, are filed by the same person against the same Respondents (even if the person filing the Demand is acting in different capacities), or are filed on behalf of an individual and a corporation against the same Respondents if the individual is the sole shareholder of the corporation. The Secretary may, whether or not at the request of any party, order any or all joined claims to be separated in the interest of



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providing a fair, equitable or expeditious procedure or to avoid unnecessary or unreasonable delay.

* * *

Section 7. Pre-Hearing.

* * *

(e) Other Pre-Hearing Motions

Except as provided in Section 7(a)(2) above, a party has 10 days from the date a pre-hearing motion is received in which to serve a written response on the Secretary and all other parties. However, where a motion is received less than 20 days in advance of the date the hearing or summary proceeding is scheduled to commence, NFA may, in its discretion, require a written response within less than 10 days. No written replies to a party's response to a motion will be allowed except in the Panel's discretion.

* * *

Section 10. Award, Settlement and Withdrawal.

(b) Relief.

The award may grant or deny any of the [monetary] relief requested, and may include an assessment of interest, costs or fees (See Sections 11 and 12). A request for declaratory relief will only be heard by the arbitrators if the Respondent agrees to have the arbitrators hear the claim.

* * *

Section 12. Arbitration Costs.

A Panel may assess against a party any one or more of the following costs, upon a finding that such party's claim or defense was frivolous or was made in bad faith, or that the party engaged in willful acts of bad faith during the arbitration: Reasonable and necessary expenses incurred by (a) the arbitrators or (b) any other party or witness, including reasonable attorneys' fees. The Panel may also award attorneys' fees provided that a statutory or contractual basis exists for awarding such



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fees. Requests for attorneys' fees and costs incurred in the arbitration proceeding must be raised in the proceeding or they are waived.

EXPLANATION OF PROPOSED AMENDMENTS

- Costs and Fees in NFA Arbitration Proceedings

Section 12 of NFA's arbitration rules allows the arbitrators to award attorney's fees if a statutory or contractual basis exists for awarding them. Although NFA's arbitration rules do not specifically require it, in most cases requests for attorney's fees based on a contractual provision between the parties are filed in the arbitration proceeding itself. However, it has come to NFA's attention that these requests are sometimes being raised in a separate lawsuit after the arbitration case concludes. To illustrate, NFA is aware of situations where a customer files a claim against a Member and the customer is awarded nothing by the arbitrator. However, instead of asking for costs during the arbitration proceeding itself, the Member respondent files a separate lawsuit after the arbitration case closes asking a court to award it attorney's fees associated with the arbitration based on the parties' contract.

NFA is concerned that this is not an efficient use of resources. Furthermore, when customers come to NFA, they believe that all of the issues relating to the dispute will be resolved in the arbitration proceeding when, in fact, that may not be the case.

Therefore, NFA believes Section 12 of the arbitration rules should be amended to require all requests for costs and fees relating to a particular proceeding to be raised in the proceeding itself.

- Expanding the Relief Available Under the Member Rules

The Member Rules were originally designed so that arbitrating Member disputes would not interfere with NFA's ability to efficiently resolve customer claims. One example of NFA's attempt to keep the process relatively simple relates to the type of relief the arbitrators may grant. Under Section



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10(b) of the Member Rules, the arbitrators are authorized to award any of the monetary relief requested, including an assessment of interest, costs or fees. NFA's rules do not, however, permit the arbitrators to order a party to perform certain acts or cease certain conduct.

While this is adequate for most of the Member cases that NFA receives, several cases have been filed at NFA which include requests for such non-monetary relief. For example, a case that is currently pending at NFA involves a claim by a CPO/CTA Member firm and one of its APs against another AP of the firm. The case includes, among other things, allegations of misappropriation of a trading system. In addition to specified monetary damages, the claimants have requested that the arbitrators order the Member respondent to return to the Member claimants a valid version of the firm's trading software, including adequate training to trade the system effectively. Because the arbitrators cannot grant non-monetary relief, NFA informed the claimants that the arbitrators could not consider this request.

The Member Rules originally limited the available relief to monetary damages because of concerns that requests for equitable relief might lengthen the arbitration process and be beyond the expertise of NFA's arbitrators. However, NFA's experience over the last three years is otherwise. It seems that requests for equitable relief are closely intertwined with requests for monetary relief. Since the arbitrators would be required to hear essentially the same evidence in order to determine what should be awarded, the process is not lengthened. Furthermore, it is now clear that NFA Member arbitrators are sophisticated enough to deal with these issues. In fact, there has been one case filed under the Member Rules where NFA permitted a request for injunctive relief to be heard by the panel. In that case, the request was closely tied to the request for monetary relief and there was a written contract between the parties that was broader than our rules. NFA also felt that hearing the request for an injunction would not prolong the proceeding, and from what we can tell, it did not.¹

Other arbitration forums, such as the AAA, the NYSE and the NASD, allow their arbitrators to grant this type of relief

¹ In that case, the panel heard but did not grant the request for injunctive relief.



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and doing so does not appear to complicate the process at these forums. Therefore, NFA's Board modified Section 10(b) of the Member Rules to expand the type of relief that can be granted to include equitable relief. NFA believes that doing so will increase the efficiencies of NFA arbitration for resolving Member disputes.

- Codification of Current NFA Arbitration Policies and Procedures

Declaratory Relief

It is not unusual for NFA to receive a Demand where the claimant asks for "declaratory relief." In other words, the claimant will ask for a finding from the arbitrators that he does not owe the respondent any money concerning a particular matter. An example of a typical request for declaratory relief is a claim made by a customer requesting a determination from the panel that he does not owe a debit balance to a Member firm.

Since a request for declaratory relief generally takes the choice of forum away from the party who actually has the claim (e.g., the Member firm with the debit balance), it is NFA's longstanding interpretation and policy that a claim for declaratory relief can be heard at NFA only if the respondent also agrees to have it arbitrated here. However, NFA's rules do not specifically address this issue. Because this type of claim is periodically filed at NFA, the Board amended Section 10(b) of the arbitration rules to make it clear that NFA will only accept a claim for declaratory relief if the party the claim is against also agrees to have it heard at NFA.²

Pre-Hearing Motions

NFA's arbitration rules provide definite deadlines for filing and responding to requests to compel production of documents and information. On the other hand, the arbitration rules do not specifically address how much time a party has for filing

² NFA accepts a valid pre-dispute arbitration agreement as the other party's consent.



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and responding to other pre-hearing requests, such as a motion for sanctions or to dismiss a claim. Furthermore, the arbitration rules do not address whether the party who filed the motion may reply to the other party's response.

The fact that the arbitration rules do not contain provisions for filing and responding to non-discovery motions or for replying to a response to a motion is not a problem in most cases. NFA's practice is to set a date for a response once a motion has been received, and these deadlines are usually met. However, it is becoming more common for parties to request additional time to respond to a motion or for one party to ask to submit a reply to the other party's response to a motion. As a result, NFA is concerned that these situations may unnecessarily prolong the arbitration process. Furthermore, it is difficult for NFA to impose a deadline for responding to pre-hearing requests or to refuse to allow a party the opportunity to reply to a response when there is no corresponding rule to support NFA's position.

To address this situation, the Board amended Section 8(e) of the Code and Section 7(e) of the Member Rules to provide a deadline for a party to respond to other pre-hearing motions that are filed in a proceeding and to give NFA the authority to impose a shorter deadline for responding to a motion when the hearing date is close by. Furthermore, Sections 8 and 7 were amended to allow the party who files a motion to reply to the other party's response only if the arbitrators believe it will be helpful to them in deciding the motion.

Notice of Intent to Arbitrate

An arbitration proceeding is initiated under NFA's arbitration rules by filing a Demand for Arbitration. The arbitration rules also allow a party to file a notice of that person's intent to arbitrate. The purpose of a notice of intent is to give someone who is approaching but has not passed the two-year time limit enough time to review the rules and file the Demand before time runs out. Therefore, a party really only needs to file a notice of intent if he is approaching the two-year time limit for making a claim at NFA.

Unfortunately, many claimants and their attorneys mistakenly believe that a notice of intent must always be filed



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before a Demand, and this has caused some confusion. To clarify this situation, the Board amended Section 6(a), (b) and (c) of the Code and Section 5(a), (b) and (c) of the Member Rules to make it clear that an arbitration proceeding is initiated when a Demand is filed and that a person only needs to file a notice of intent if the two-year time limit is approaching.

Consolidation and Joinder

NFA's arbitration rules authorize NFA, in its discretion, to consolidate for hearing separate Demands for Arbitration involving common questions of fact or arising from the same act or transaction in the interest of providing a fair, equitable and expeditious procedure. An example of a situation where NFA would consolidate two cases is where a customer files a Demand against a Member firm for alleged wrongdoing in his account, such as unauthorized trading, and the Member firm files a separate Demand against the customer for a debit balance in the same account.

The arbitration rules do not allow the parties to consolidate the claims on their own by filing one Demand. However, it is NFA's experience that some parties do try to combine multiple claims for arbitration into one Demand. If the claims are related and essentially involve the same parties, NFA may permit the claims to be filed as one case if they meet the requirements for consolidation or are filed by the same person acting in different capacities (e.g., one Demand is filed by a person acting in an individual capacity and as a trustee). Similarly, NFA will allow a claimant to file one Demand for losses in both his individual account and a corporate account where he is the sole shareholder.

On the other hand, NFA does not consolidate claims that involve different accounts a customer had at different firms. For example, if Mr. ABC handled an account at LMN Company but then went to work for XYZ Corporation, NFA will not consolidate the customer's Demand against Mr. ABC and LMN Company with the Demand against Mr. ABC and XYZ Corporation. NFA's experience indicates that consolidating cases like these can be prejudicial to a respondent who is involved in one of the cases but not the other and can make the proceeding unwieldy. Furthermore, if a party attempts to file these claims as one Demand, NFA requires separate Demands to be filed before it will accept them.



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NFA believes that the procedures for consolidating cases work well. However, NFA's rules may not be as clear as necessary concerning what cases can be joined and staff's authority to require separate Demands. Therefore, the Board amended Section 6(m) of the Code and Section 5(m) of the Member Rules to clarify NFA's policy for joining claims.

NFA respectfully requests that the Commission review and approve the proposals contained in this submission and requests that they be declared effective upon Commission approval.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Daniel J. Roth', written over a horizontal line.

Daniel J. Roth
General Counsel

cc: Chairman Mary L. Schapiro
Commissioner Barbara Pedersen Holum
Commissioner Sheila C. Bair
Commissioner Joseph P. Dial
Commissioner John E. Tull, Jr.
Andrea M. Corcoran, Esq.
Alan L. Seifert, Esq.
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U.S. COMMODITY FUTURES TRADING COMMISSION

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March 12, 1996

Mr. Daniel J. Roth
General Counsel
National Futures Association
200 West Madison Street
Chicago, Illinois 60606

Re: Proposed Amendments to Code of Arbitration
Sections 6, 8, 10 and 12 and Member
Arbitration Rules Sections 5, 7, 10 and 12--
Arbitration Procedure Revisions

Dear Mr. Roth:

By letter dated August 28, 1995, and received by the Commission on August 30, 1995, the National Futures Association ("NFA") submitted the above-referenced proposed rule amendments pursuant to Section 17(j) of the Commodity Exchange Act ("Act").

Please be advised that on this date the Commission has determined to approve the above-referenced proposed rule amendments pursuant to Section 17(j) of the Act.

Sincerely,

Jean A. Webb
Jean A. Webb
Secretary of the Commission