SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 15

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JOSEPH GUNNAR & CO., LLC,

Petitioner,

- v -

PATRICIA I. RICE

Respondent.

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Index No.
651259/2014

DECISION and ORDER

Mot. Seq. 002

HON. EILEEN A. RAKOWER, J.S.C.

Petitioner, Joseph Gunnar & Co., LLC ("Gunnar" or "Petitioner"), brings this special proceeding for an Order, pursuant to CPLR §§ 7503(b) and 7502(b), staying the arbitration (the "Arbitration") between Petitioner and respondent Patricia I. Rice ("Respondent" or "Rice"), and dismissing certain causes of action asserted in the underlying statement of claims (the "Statement of Claims") for Arbitration as time-barred. Respondent, a financial services customer, initiated the Arbitration against Gunnar, Respondent's former broker-dealer, with the Financial Services Industry Regulatory Authority ("FINRA") under the arbitration number 14-00503, alleging, *inter alia*, causes of action sounding in fraud, breach of fiduciary duty, churning, negligence, and violations of General Business Law (GBL) § 349.

In support, Petitioner submits the affidavit of Joseph Alagna ("Alagna"), Petitioner's CEO; a copy of the statement of claim (the "Statement of Claim") in the underlying Arbitration; a copy of the profit and loss analysis prepared in connection with the Arbitration; a copy of FINRA's "Eligibility Rule", Rule 12206; and, a copy of the customer agreement (the "Customer Agreement"), dated November 17, 2005, between Rice and Gunnar.

Respondent opposes. Respondent filed an answer to Petitioner's petition. Oral Argument was heard on Petitioner's petition.

Under New York law, threshold issues concerning the timeliness of a party's demand for arbitration are for the court, and not the arbitrator, to decide. (CPLR

7502[b], 7503[b]). Under the Federal Arbitration Act ("FAA"), by contrast, the "resolution of a statute of limitations defense is presumptively reserved to the arbitrator, not a court." (*Matter of ROM Reins. Mgt. Co., Inc. v. Continental Ins. Co., Inc.*, 115 A.D.3d 480, 481 [1st Dep't 2014]). However, in keeping with FAA policy to enforce private agreements, an exception to the FAA's general rule reserving questions of timeliness to the arbitrator exists where parties explicitly agree to leave the issue of timeliness to the court. (*Diamond Waterproofing Sys. v. 55 Liberty Owners Corp.*, 4 N.Y.3d 247, 253 [2005]). For this reason, even if an agreement is subject to the FAA, "a choice of law provision which states that New York law shall govern both 'the agreement *and its enforcement*,' adopts as 'binding New York's rule that threshold Statute of Limitations questions are for the courts'". (*Id.* [emphasis in the original]).

The FAA applies to written arbitration provisions contained in contracts "evidencing a transaction involving commerce." (9 U.S.C. § 2). The words "involving commerce", like the phrase "affecting commerce", are broadly interpreted as signaling Congress's intent to exercise its Commerce Clause powers to the fullest extent. (*Diamond Waterproofing Sys. v. 55 Liberty Owners Corp.*, 4 N.Y.3d 247, 253 [2005]). Thus, where a contract containing an arbitration provision "affects" interstate commerce, disputes arising thereunder are subject to the FAA. (*Id.*). Consistent with this broad interpretation, "individual transactions do not need to have a substantial effect on interstate commerce in order for the FAA to apply." (*Cusimano v. Schnurr*, 120 A.D.3d 142, 148 [1st Dep't 2014] citing *Citizens Bank v. Alafabco*, Inc., 539 U.S. 52, 56 [2003]). Rather, in determining whether a contract containing an arbitration provision "involves commerce" within the meaning of the FAA, the "proper inquiry is whether the economic activity in question represents a general practice that bears on interstate commerce in a substantial way." (*Cusimano v. Schnurr*, 120 A.D.3d 142, 148 [1st Dep't 2014]).

Here, the Customer Agreement between Gunnar and Rice states that the agreement is entered into "for the purpose of purchasing and selling securities." The Customer Agreement contemplates financial transactions within a federally regulated industry, provides for extension of time applications to the committees of "any national securities exchange", and contains a "Disclosure and Certification" provision concerning compliance with United States Securities and Exchange Commission ("SEC") Rule 14(b)-1(o). The economic activity contemplated under the Customer Agreement represents general practices, i.e., purchasing and selling securities on a national exchange, that bear on interstate commerce in a substantial way. (*Imclone Sys. v. Waksal*, 22 A.D.3d 387 [1st Dep't 2005]). Accordingly, the

Customer Agreement "involves commerce" within the meaning of the FAA, and the parties' disputes arising under the Customer Agreement are subject to the FAA.

However, as far as the court's authority to decide threshold questions concerning the timeliness of Respondent's demand for Arbitration is concerned, the Customer Agreement explicitly states: "[t]his agreement *and its enforcement* shall be governed by the laws of the State of New York and its provisions shall be continuous." [emphasis added]. By using such "critical language" *vis-a-vis* the Customer Agreement and its enforcement, the Customer Agreement's choice of law provision, on its face, explicitly adopts as binding New York's rule that threshold Statute of Limitations questions are for the courts. (*Diamond Waterproofing Sys. v. 55 Liberty Owners Corp.*, 4 N.Y.3d 247, 253 [2005]). Accordingly, although the Customer Agreement is subject to the FAA, the Customer Agreement explicitly leaves the question of timeliness to the court.

Turning now to the issue of the Statute of Limitations, "churning" occurs when a securities dealer "abuses his customer's confidence for personal gain (e.g. to create commissions) by inducing transactions in the customer's account which are disproportionate to the size and character of the account." (*Newburger, Loeb & Co. v. Gross*, 563 F.2d 1057, 1069 [2d Cir. 1977]). In New York, the period of limitations for a churning claim, "involving alleged personal gain by the securities dealer through excessive trading activity, [runs] from the date when [Plaintiff], as investor[], [was] on notice, warranting inquiry, of the potential claim by receipt of trade confirmations or monthly statements detailing the allegedly excessive and unauthorized trading in their account, rather than from the date of the last trade." (*Kidder, Peabody & Co. v. McArtor*, 223 A.D.2d 502, 503 [1st Dep't 1996] *citing Newburger, Loeb & Co. v Gross,* 563 F.2d 1057, 1069 [1977]). However, courts have recognized that, in certain circumstances, "added experience and knowledge" may be necessary to ascertain a pattern of churning. (*Komanoff v. Mabon, Nugent & Co.*, 884 F. Supp. 848, 854 [S.D.N.Y. 1995]). As the Southern District explains:

> A claim of churning is based upon an excessive volume of discretionary trading in an account over a period of time. Discovery of the fraud requires not only knowledge that the trades have occurred, but also an awareness that the rate of trading activity is excessive in light of the dollar value of the account and the client's investment objectives.

(*Lang v. Paine, Webber, Jackson & Curtis, Inc.*, 582 F. Supp. 1421 [S.D.N.Y. 1984]). For this reason, a given confirmation slip or monthly statement may be

sufficient to bar a plaintiff from complaining about specific stock purchases reflected therein, and yet insufficient to put the plaintiff on inquiry notice of excessive trading on the plaintiff's account. (*Komanoff v. Mabon, Nugent & Co.*, 884 F. Supp. 848, 854 [S.D.N.Y. 1995] *citing Hecht v. Harris, Upham & Co.*, 430 F.2d 1202, 1209-10 [9th Cir. 1970]). Additionally, "a finding of churning, by the very nature of the offense, can only be based on a hindsight analysis of the entire history of a broker's management of an account and of his pattern of trading that portfolio, in comparison to the needs and desires of an investor." (*Komanoff v. Mabon, Nugent & Co.*, 884 F. Supp. 848, 854 [S.D.N.Y. 1995] *citing Nesbit v. McNeil,* 896 F.2d 380, 384 [9th Cir. 1990]).

Here, it is undisputed that Respondent's claims for "churning" must survive Petitioner's instant motion to dismiss because there are questions of accrual, and as to whether the alleged misconduct constitutes a "unified offense".

With respect to Respondent's remaining claims, Petitioner argues that Respondent's Statement of Claims asserts claims for breach of fiduciary duty, negligence/failure to supervise[1], and violations of GBL § 349, none of which are timely brought, under the three-year statute of limitations applicable to such claims. Additionally, Petitioner argues that Respondent's statement of claims asserts causes of action for breach of contract and fraud, both of which are time-barred to the extent that they arise from transactions which took place more than six years before Respondent filed the Statement of Claims.

GBL § 349, GBL § 349 prohibits "deceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service in this state." (GBL § 349[a]). Claims pursuant to General Business Law § 349 are governed by the three-year limitation period set forth in CPLR § 214(2). (*Morelli v. Weider Nutrition Group, Inc.*, 275 A.D.2d 607, 608 [1st Dep't 2000]). A private right of action to this statute exists under GBL § 349(h). (GBL § 349[h]). A private cause of action under GBL § 349 accrues when plaintiff is injured by a deceptive act or practice violating GBL § 349. (*Gaidon v. Guardian Life Ins. Co. of Am.*, 96 N.Y.2d 201, 210 [2001]). The date of discovery rule is not applicable and cannot serve to extend that limitations period. (*Wender v. Gilberg Agency*, 276 A.D.2d 311, 312 [1st Dep't 2000]).

[1] Respondent asserts that the Statement of Claims does not contain any negligence or negligent supervision claims. Accordingly, insofar as Respondent does not purport to assert causes of action for negligence or negligent supervision, the timeliness of any such claims is moot and need not be addressed.

Here, Respondent's Statement of Claims alleges that the churning activity in issue "did not cease until October 2008". Even accepting Respondent's allegations as true and drawing all inferences in favor of the non-moving party, Respondent's alleged injury first occurred, at the latest, in October 2008. Accordingly, Plaintiff's claims pursuant to GBL § 349 accrued more than three years before Plaintiff filed the Statement of Claims, and therefore are not timely brought.

As for Respondent's breach of fiduciary duty claims, the applicable period for breach of fiduciary duty claims generally depends upon the substantive remedy sought—where the relief sought is equitable in nature, the six-year limitations period in CPLR § 213(1) applies, while claims for breach of fiduciary duty that seek only monetary damages fall within the three-year period set forth in CPLR § 214(4). A cause of action for breach of fiduciary duty based on allegations of actual fraud is subject to a six-year limitations period. (*Kaufman v. Cohen*, 307 A.D.2d 113, 119 [1st Dep't 2003]). Here, drawing all inferences in favor of the non-moving party, Respondent's Statement of Claims alleges a cause of action for breach of fiduciary duty based allegations of actual fraud. Accordingly, Respondent's breach of fiduciary duty claim, as alleged, is timely brought.

As for Respondent's breach of contract claims, the statutory period for claims sounding breach of contract six years. (CPLR § 213[2]). Accordingly, Respondent's claims for breach of contract are timely, to the extent that these claims arise from breaches that allegedly took place in 2007 and/or 2008, within the limitations period.

Finally, with respect to Respondent's fraud claims, the statutory period for claims sounding in fraud is the later of six years from the date of accrual or two years from discovery. (CPLR § 213[8]). Here, to the extent that Respondent's Statement of Claims asserts a fraud arising from the claimed pattern of churning activity, which allegedly culminated in 2008, Respondent's claims for fraud are timely. Furthermore, although an arbitrator considering all of the evidence may find that the monthly statements, confirmations, or other correspondence respecting Rice's accounts with Gunnar put Respondent on inquiry notice as to Petitioner's alleged wrongdoing prior to 2008, this Court is unable to reach such a conclusion as a matter of law at this stage of the proceedings. Accordingly, Respondent's claims sounding in fraud may proceed to arbitration.

Wherefore it is hereby

ORDERED and ADJUDGED that Petitioner's petition is granted only to the extent that Respondent's claims for violations of GBL § 349 are dismissed; and it is further

ORDERED and ADJUDGED that the remaining claims in Respondent's Statement of Claims are severed and shall proceed to arbitration.

This constitutes the decision and order of the court. All other relief requested is denied.

DATED: February 13, 2015

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EILEEN A. RAKOWER, J.S.C.

HON. EILEEN A. RAKOWER