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JUDICIAL REVIEW OF ARBITRATION AWARDS: MANIFEST DISREGARD OF THE LAW*

Norman S. Poser[†]

INTRODUCTION

Two recent Second Circuit decisions involving claims of age discrimination, *DiRussa v. Dean Witter Reynolds, Inc.*¹ and *Halligan v. Piper Jaffray, Inc.*,² raise the perplexing question of what is the proper scope of judicial review of arbitration awards.³ Speed, economy, and finality, the principal goals of arbitration, suggest that judicial review should be narrow; on the other hand, fairness and justice require that there be meaningful review of awards, particularly when a party is asserting statutory rights.⁴

In fact, judicial review of arbitration awards is strictly limited.⁵ It is well established that a court may not modify or vacate an award simply because the arbitrator made an error, misinterpretation, or misapplication of law. The award may be vacated only if the proceeding was tainted with corruption, misconduct or bias; if the arbitrator exceeded his or her authority; or if the arbitrator acted

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¹ 121 F.3d 818 (2d Cir. 1997), cert. denied, 118 S. Ct. 695 (1998).

² 148 F.3d 197 (2d Cir. 1998).

³ Arbitrators' decisions are commonly referred to as "awards," even where the arbitrators deny any recovery to the claimant.

⁴ See Harry T. Edwards, *Alternative Dispute Resolution: Panacea or Anathema?*, 99 HARV. L. REV. 668, 679 (1986) ("Inexpensive, expeditious, and informal adjudication is not always synonymous with fair and just adjudication."). Judge Edwards sits on the District of Columbia Circuit Court of Appeals.

⁵ For a discussion of judicial review under the Federal Arbitration Act ("FAA"), see *infra* text accompanying notes 147-184.

in "manifest disregard of the law."⁶ Under Second Circuit law, "manifest disregard" means that (1) the arbitrators knew the law, "yet refused to apply it or ignored it . . . ; and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case."⁷

The two Second Circuit opinions, both written by Judge Wilfred Feinberg,⁸ attempted to apply the "manifest disregard" standard, with results that were strikingly different. In *DiRussa*, the court's strict application of the standard resulted in the denial of the claimant's rights under a federal anti-discrimination statute. In *Halligan*, the court employed the manifest disregard standard to enforce the claimant's rights under the same statute, but it had to ignore precedent to do so. These cases amply demonstrate that, at least in the context of arbitrations based on statutory discrimination claims, manifest disregard is not an appropriate standard of review, and the courts should explicitly recognize this.

Raymond DiRussa and Theodore Halligan were both long-time employees of brokerage firms who initiated arbitrations against their firms for violation of the Federal Age Discrimination in Employment Act of 1967 ("ADEA").⁹ As a condition of employment, DiRussa and Halligan were required to register with the New York Stock Exchange ("NYSE") and the National Association of Securities Dealers ("NASD") and to sign an application form with these organizations that included an agreement to arbitrate any dispute that might arise in connection with their employment.¹⁰

In *DiRussa*, the arbitration panel appointed by the NYSE ruled in his favor and awarded him damages but refused to award attorney's fees, notwithstanding a provision of the ADEA requiring that a successful claimant receive reasonable attorney's fees. The district court denied a motion to modify or vacate the award, and the Second Circuit affirmed. The Second Circuit found that the arbitrators' failure to award attorney's fees was clearly erroneous.

⁶ See *Merrill Lynch, Pierce Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930 (2d Cir. 1986).

⁷ *Halligan*, 148 F.3d at 202 (citing *DiRussa*, 121 F.3d at 821).

⁸ In addition to Judge Feinberg, the *DiRussa* panel consisted of Judges Oakes and Leval, while the *Halligan* panel consisted of Judge Kearse and District Court Judge Barrington Parker, sitting by designation.

⁹ 29 U.S.C.A §§ 621-634 (1985).

¹⁰ The defendants in the two cases were member firms of both the NYSE and the NASD. The NYSE and the NASD register employees of their member firms by using Form U-4, which includes an arbitration clause.

Nevertheless, it held that the arbitrators did not act "in manifest disregard of the law" because, although DiRussa raised the issue of attorney's fees at the arbitration hearing, he did not "communicate . . . to the arbitrators that the ADEA mandated such an award to a prevailing party."¹¹

In *Halligan*, the employee initiated an arbitration with the NASD. At the hearing, he presented strong (though contested) evidence supporting his age discrimination claim, but the arbitration panel nevertheless denied him any relief. The district court refused to vacate the award for manifest disregard of the law on the ground that its role was not to second-guess the arbitrators' fact-finding. The Second Circuit reversed, holding that the court reviewing the award may consider the arbitrators' failure to explain their decision in concluding that they acted in manifest disregard for the law.¹²

The issue of the scope of review of arbitration decisions cannot be considered in isolation. It arises in these and many other cases, in situations where employees have been required to agree to mandatory arbitration as a condition of employment. Moreover, DiRussa and Halligan's claims were based on the violation of a federal statute that specifically gives employees redress for discrimination based on age. These types of disputes involve issues with which securities arbitrators are unlikely to have knowledge or experience.

Thus, in order to properly address the problems with the manifest disregard standard in this setting, it is necessary first to discuss three related issues: (1) should an arbitration clause in an employment agreement be enforceable, particularly where the employee is required to sign the agreement as a condition of his or her employment? (2) even if such an arbitration clause is generally enforceable, should arbitration of a claim brought by an employee under a federal or state anti-discrimination statute be mandatory? (3) is the standard of competence applicable to an arbitrator deciding an employment discrimination claim adequate?

It is the thesis of this Article that the manifest disregard standard for judicial review of arbitration awards should be replaced by a standard that would require the reviewing court to modify or vacate an award if the award egregiously departs from established legal principles, even if the arbitrator is ignorant of the correct law. Because such a standard would still be considerably narrower than

¹¹ *DiRussa*, 121 F.3d at 823.

¹² *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197 (2d Cir. 1998).

the scope of review that an appellate court applies to the judgment of a trial court, it would not seriously undercut the policy favoring finality of arbitral decisions. Although the need for a new standard of review is clearest in the case of claims involving statutory rights, the proposed standard would apply to all arbitration awards.

Part I of this Article describes the *DiRussa* and *Halligan* decisions. Part II discusses the arbitrability of employment agreements under the FAA. Part III reviews current law and practices regarding the arbitration of employment discrimination claims. Part IV discusses the competence of NASD and NYSE arbitrators to decide such claims. Following the discussion of these background issues, Part V returns to the principal issue of the *DiRussa* and *Halligan* cases: the appropriateness of the "manifest disregard of the law" standard for vacating or modifying an arbitration award. Finally, Part VI formulates a proposed standard of review that recognizes both the importance of finality of arbitral decisions and the need to provide the parties in an arbitration with the same fundamental rights they would enjoy in a court proceeding.

I. THE *DIRUSSA* AND *HALLIGAN* DECISIONS

A. *DiRussa v. Dean Witter Reynolds, Inc.*

In 1992, Raymond DiRussa, age fifty-eight, was the branch manager of the Morristown, New Jersey office of Dean Witter Reynolds, Inc. ("DWR"), one of the largest brokerage firms in the country. DiRussa had been with the firm for almost forty-two years. On May 8, 1992, the firm demoted DiRussa to the position of account executive (i.e., salesman).¹³ DiRussa challenged his demotion by filing charges of employment discrimination with the Equal Employment Opportunity Commission ("EEOC") and with the New Jersey Division on Civil Rights.¹⁴ When the EEOC declined to pursue DiRussa's claim, he initiated an NASD arbitration proceeding against DWR and Lawrence Solari, a regional director of DWR.¹⁵

¹³ Petition for Certiorari at 3, *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818 (2d Cir. 1997), cert. denied, 118 S. Ct. 695 (1998).

¹⁴ *Id.*

¹⁵ The EEOC cannot obtain monetary relief from a brokerage firm on behalf of a person asserting claims under the ADEA if that person has entered into a valid arbitration agreement. See *Equal Employment Opportunity Comm'n v. Kidder, Peabody & Co., Inc.*, 979 F. Supp. 245, 247 (S.D.N.Y. 1997).

The arbitration panel consisted of three arbitrators, all from the securities industry, two of whom were lawyers, including one who had prior experience in employment law.¹⁶ DiRussa claimed he had been demoted because of his age, in violation of the ADEA and the New Jersey Law Against Discrimination ("NJLAD").¹⁷ After seven days of hearings held over a six-month period, the arbitration panel found in DiRussa's favor and awarded him \$200,000 in damages against both defendants and an additional \$20,000 against Solari. However, the arbitrators denied DiRussa's request for an award of \$249,010.50 in attorneys' fees and explicitly denied all other relief.¹⁸ As is customary in securities-industry arbitrations, the arbitrators did not file a written opinion containing findings of fact or conclusions of law.¹⁹ Thus, the arbitrators' reasons for denying DiRussa's request for attorneys' fees are not known.

DiRussa moved in federal district court to modify or vacate the award insofar as it denied attorney's fees on the ground that the ADEA requires the award of reasonable attorney's fees to a party who recovers a judgment under the statute.²⁰ The district court found that the "factual predicate" of DiRussa's claim that the ADEA mandated an award of attorney's fees to a successful claimant was "entirely accurate," and that "it is difficult to imagine a more 'well defined, explicit and clearly applicable' provision of governing law than the ADEA's mandate that successful age discrimination claim-

DiRussa was required to arbitrate his claim because he had signed a Form U-4 when he registered with the NYSE, as he was required to do in order to work as a "registered representative" for an NYSE member firm. The U-4 contained an arbitration agreement. See text accompanying *infra* note 75.

¹⁶ Petition for Certiorari at 3.

¹⁷ N.J. STAT. ANN. §§ 10:5-1 to 10:5-42 (West 1993). The district court's opinion stated that DiRussa claimed that he had been wrongfully terminated because of his age. *DiRussa v. Dean Witter Reynolds, Inc.*, 936 F. Supp. 104, 106 (S.D.N.Y. 1996), *aff'd*, 121 F.3d 818 (2d Cir. 1997), *cert. denied*, 118 S. Ct. 695 (1998). The Second Circuit's opinion, however, refers only to his claim that he was demoted from the position of branch manager to that of account executive. *DiRussa*, 121 F.3d at 820. Because the district court sealed the record of the case, it is not possible to ascertain whether DiRussa was terminated as well as demoted.

¹⁸ *DiRussa*, 121 F.3d at 820.

¹⁹ Petition for Certiorari at 3.

²⁰ Section 216(b) of the Fair Labor Standards Act, 29 U.S.C. § 216(b) (1994), which is incorporated by reference in § 626(b) of the ADEA, 29 U.S.C. § 626(b) (1994), provides that "[t]he court . . . shall, in addition to any judgment awarded to the plaintiff . . . allow a reasonable attorney's fee to be paid by the defendant, and costs of the action." *DiRussa*, 936 F. Supp. at 106.

ants such as plaintiff recover attorney's fees."²¹ Nevertheless, the court refused to vacate or modify the award, on the ground that the claimant's counsel never argued to the arbitrators that an award of counsel fees was mandatory.²² Thus, "the arbitrator's rejection of plaintiff's claim for attorney's fees under the ADEA does not fall within any of the limited grounds for vacating an arbitration award found in the . . . FAA."²³ The district court also placed the file under seal, so that none of the documents generated by the arbitration and litigation, other than the court's opinion, were placed in the public file.²⁴

A panel of the Second Circuit unanimously affirmed the district court's decision. The panel agreed with the district court's view that the governing law requiring an award of attorney's fees was "well defined, explicit and clearly applicable."²⁵ However, the court found itself powerless to disturb the arbitral decision rejecting DiRussa's application for attorney's fees, even though it was clearly erroneous. According to the court, the arbitrators' error did not fall within one of the grounds for vacatur or modification of an arbitration award set forth in the FAA, nor did the arbitrators act in manifest disregard of the law, a non-statutory ground for setting aside an arbitral award that has been adopted by most of the circuit courts, including the Second Circuit.²⁶ Although the arbitrators failed to apply a "well defined, explicit and clearly applicable" rule of law, their failure did not constitute manifest disregard of the law because "at no point did DiRussa communicate . . . to the arbitrators that the ADEA mandated such an award to a prevailing party."²⁷ Finally,

²¹ *DiRussa*, 936 F. Supp. at 106.

²² See *id.* at 107. Plaintiff's counsel's submissions on attorney's fees dealt only with the NJLAD, which provides that in such cases "the prevailing party may be awarded a reasonable attorney's fee as part of the costs." N.J. STAT. ANN. § 10.5-27.1 (West 1993) (emphasis added).

²³ *DiRussa*, 936 F.Supp. at 106.

²⁴ *Id.* at 108. Because the district court placed the file under seal, none of the briefs, other than the Petition for Certiorari to the Supreme Court and the Opposition to the Petition for Certiorari, are available for inspection.

²⁵ *DiRussa*, 121 F.3d at 822 (quoting *DiRussa*, 936 F. Supp. at 106).

²⁶ *Id.* at 822-23.

²⁷ *Id.*

the court held that the district court did not abuse its discretion in ordering that the file be sealed.²⁸ The Supreme Court denied DiRussa's Petition for Certiorari.²⁹

B. Halligan v. Piper Jaffray, Inc.

Theodore Halligan had worked at Piper Jaffray, Inc. for almost twenty years as a salesman of equity investments to financial institutions when, according to his ADEA claim, he was terminated because of his age. At the time of his termination, he was sixty-nine years of age.³⁰ He was one of the firm's top salesmen, earning nearly \$500,000 a year. Halligan initiated an arbitration before the NASD.³¹ Halligan and other witnesses testified at the hearing that several Piper Jaffray personnel had expressed their intention to oust Halligan because of his age.³² All of the Piper personnel who testified at the hearing denied making these statements. Piper claimed that Halligan had chosen to retire; it also argued that his poor performance and health justified terminating him. Various witnesses testified, however, that Halligan was always able to perform his job. After Halligan left the firm, the firm assigned his customers' accounts to two younger men.³³

After forty-nine hearing sessions over a two-year period,³⁴ the arbitration panel, without writing an opinion explaining its decision, denied Halligan any relief. A district court judge refused to vacate the award on the ground that the arbitrators manifestly disregarded the law since there was support for the arbitrators' conclusion and, furthermore, the court's role was not to weigh the conflicting evi-

²⁸ *Id.* at 827-28. The issue of the sealing of the record of the case is beyond the scope of this article.

²⁹ Petition for Certiorari.

³⁰ Brief of Petitioner-Appellant at 8, *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197 (2d Cir. 1998).

³¹ Halligan died before the arbitration was concluded, and his widow continued the arbitration. *Halligan*, 148 F.3d at 198.

³² For example, Halligan testified at the hearing that Tad Piper, the CEO of the firm, had told him "you're too old. Our clients are young and they want young salesmen," and that Bruce Huber, his supervisor, told him "we want you out of here quickly." *Id.* Piper and Huber denied making such remarks. *Id.* A former client of Halligan testified that Huber said that Halligan "would get put out to pasture because he was getting old." *Id.* at 199.

³³ *Id.* at 198-99.

³⁴ Brief of Petitioner-Appellant at 1.

dence.³⁵ The Second Circuit reversed, holding that the arbitrators' denial of any relief to Halligan constituted manifest disregard of the law. The court distinguished *DiRussa*, which had been decided about a year earlier,³⁶ on the ground that in *Halligan* counsel for both parties agreed on the applicable law and explained it to the arbitrators. In view of this and the "strong evidence that Halligan was fired because of his age," the court stated, in peculiarly hesitant language: "we are inclined to hold that they ignored the law or the evidence or both."³⁷

The Second Circuit noted that the Supreme Court had previously upheld the arbitrability of an ADEA discrimination claim on the assumption that the claimant would not forgo the substantive rights afforded by the statute, stating: "This case puts those assumptions to the test."³⁸ Departing from precedent, the court heavily stressed the fact that the arbitrators, following the usual custom in arbitrations, did not write an opinion explaining their conclusions.³⁹ While conceding that arbitrators are under no obligation to write opinions, the court said:

where a reviewing court is inclined to find that arbitrators manifestly disregarded the law or the evidence and that an explanation, if given, would have strained credulity, the absence of explanation may reinforce the reviewing court's confidence that the arbitrators engaged in manifest disregard.⁴⁰

It is not clear whether the court intended the above-quoted language to apply only to the review of arbitration awards in discrimination cases, to arbitration awards in statutory claims, or to all arbitration awards.

The *Halligan* court did not clearly identify the law that it believed the arbitrators disregarded. The Second Circuit's opinion suggests that it believed that the arbitrators disregarded the applica-

³⁵ *Halligan v. Piper Jaffray, Inc.*, No. 96 Civ. 4472, 1997 WL 181028 (S.D.N.Y. Apr. 15, 1997), *rev'd*, 148 F.3d 197 (2d Cir. 1998).

³⁶ *DiRussa* was decided in the Second Circuit on August 5, 1997, and *Halligan* on July 9, 1998.

³⁷ *Halligan*, 148 F.3d at 204 (emphasis added).

³⁸ *Id.* (citing *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991)).

³⁹ The American Arbitration Association ("AAA") discourages its arbitrators from writing opinions for the very reason that, if arbitrators explained the rationale for their decisions, this could provide the losing party with grounds for seeking judicial review of awards. AAA, A GUIDE FOR SECURITIES ARBITRATORS SERVING UNDER THE AAA'S SECURITIES ARBITRATION RULES 32-33 (1993).

⁴⁰ *Halligan*, 148 F.3d at 204.

ble law as to the burden of proof in an ADEA case, but the *Halligan* court made no attempt to demonstrate, as prior Second Circuit precedents require, that the disregarded law was "well defined, explicit, and clearly applicable."⁴¹

In fact, the law governing the burden of proof in cases brought under the ADEA is far more complex than the relatively simple question that was at issue in *DiRussa*: whether a prevailing party was entitled to attorneys' fees. Most courts, including the Second Circuit, have applied to ADEA cases the burden-of-proof formula that the Supreme Court established in *McDonnell Douglas Corp. v. Green*,⁴² *Texas Dep't. of Community Affairs v. Burdine*,⁴³ and *St. Mary's Honor Center v. Hicks*,⁴⁴ for cases brought under Title VII of the Civil Rights Act of 1964.⁴⁵ Under that formula, an employee must plead and prove four elements in order to establish a prima facie case: (1) the employee was a member of a protected class (in the case of age discrimination, over forty years of age); (2) the employee was qualified for the job; (3) the employee was adversely affected by the employer's action; and (4) the employer continued to seek someone with qualifications similar to those that the em-

⁴¹ See *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930, 934 (2d Cir. 1986). *Halligan* argued before the district court that the arbitrators manifestly disregarded the rule that, once *Halligan* had introduced direct evidence of discrimination, Piper bore the burden of proof that his claim was without merit and that Piper had not met its burden of proof. The district court rejected this argument on the ground that "the record of the arbitration proceedings does not indicate the Panel's awareness, prior to its determinations, of the standards for burdens of proof." 1997 WL 181028, at *3.

The Second Circuit made the following comment on the district court's statement:

The record indicates that counsel for both parties generally agreed on the applicable law (and still do on appeal), and explained it to the arbitrators. It is true that the district court stated that the record "does not indicate the Panel's awareness, prior to its determinations, of the standard for burden of proof." If this observation meant that counsel did not explain the law sufficiently to the arbitrators, it is not correct. Perhaps the district court meant that the arbitrators did not state that they were ignoring the relevant standards for burdens of proof. That is true, but we doubt whether, even under a strict construction of manifest disregard, it is necessary for arbitrators to state that they are deliberately ignoring the law.

148 F.3d at 204.

⁴² 411 U.S. 792 (1973). In *Bay v. Times Mirror Magazines, Inc.*, 936 F.2d 112 (2d Cir. 1991), the court applied the *McDonnell Douglas* analysis in an ADEA case. *Accord DeNovellis v. Shalala*, 124 F.3d 298 (3d Cir. 1997); *Rothmeier v. Investment Advisors, Inc.*, 85 F.3d 1328 (8th Cir. 1996); *Loeb v. Textron, Inc.*, 600 F.2d 1003 (1st Cir. 1979).

⁴³ 450 U.S. 248 (1981).

⁴⁴ 509 U.S. 502 (1993).

⁴⁵ 42 U.S.C. §2000e et seq. (1994).

ployee possessed.⁴⁶ If the employee establishes a prima facie case, the burden of production shifts to the employer to articulate some legitimate, nondiscriminatory reason for the employee's termination sufficient to raise a genuine issue of fact as to whether it discriminated against the employee.⁴⁷ If the employer carries this burden, the presumption of discrimination "simply drops out of the picture," and the employee must then prove that the employer intentionally discriminated against him. The burden of production then shifts back to the employee to show that the employer's explanation was not the true reason for the employment decision. The Court stated in *Hicks*:

At the close of the defendant's case, the court is asked to decide whether an issue of fact remains for the trier of fact to determine. None does if, on the evidence presented, (1) any rational person would have to find the existence of facts constituting a prima facie case, and (2) the defendant has failed to meet its burden of production—i.e., has failed to introduce evidence which, *taken as true*, would *permit* the conclusion that there was a nondiscriminatory reason for the adverse action. In that event, the court must award judgment to the plaintiff as a matter of law. . . . If the defendant has failed to sustain its burden but reasonable minds could *differ* as to whether a preponderance of the evidence establishes the facts of a prima facie case, then a question of fact *does* remain, which the trier of fact will be called upon to answer.⁴⁸

Although the burden of production shifts back and forth, the ultimate burden of persuasion rests on the employee to prove that the employer intentionally discriminated against him.⁴⁹

⁴⁶ Applying the fourth prong of the *McDonnell Douglas* test to ADEA cases has caused problems for the courts, because this prong has often been interpreted to require that the employer had given the job to someone outside the protected class. In an ADEA case, this would mean that an employee who was fired could not establish a prima facie case of age discrimination unless the employer gave his job to a person of under forty years of age. In *O'Connor v. Consol. Coin Caterers Corp.*, 517 U.S. 308 (1996), the Supreme Court held that in an ADEA case it is not necessary for the plaintiff to show that the person hired to replace him was under forty, only that the replacement was substantially younger than the plaintiff. *Id.* at 312-13.

The arbitrators' decision in *Halligan* was made on March 19, 1995, before the *O'Connor* decision, which was made on April 1, 1996. It is possible, therefore, that the arbitrators denied any relief to Halligan because they did not believe that he had established the fourth prong of the *McDonnell Douglas* test. Since the law on this point was not clear until the Supreme Court clarified it in *O'Connor*, the arbitrators' decision, even if it was erroneous, did not constitute manifest disregard under existing precedents.

⁴⁷ *McDonnell Douglas*, 411 U.S. at 802.

⁴⁸ *Hicks*, 509 U.S. at 509-10.

⁴⁹ *Id.* at 507; see also *Chisolm v. Kidder, Peabody Asset Management, Inc.*, 966 F. Supp. 218, 228 (S.D.N.Y. 1997), *aff'd*, No. 97-7828, 1998 WL 695041 (2d Cir. July 28,

It should be apparent from the above that the law applicable to proving age discrimination is complex and lacks that crystalline clarity that the Second Circuit has in the past regarded as essential for vacatur based on manifest disregard of the law.⁵⁰ Furthermore, it is by no means clear that the arbitrators in *Halligan* disregarded this law when they denied any recovery to the claimant. For example, they may have believed that the claimant was unable to establish a prima facie case, that the respondents had successfully rebutted the plaintiff's prima facie case, or that the claimant had failed to meet its ultimate burden of persuasion.

Although the Second Circuit ostensibly based its vacatur of the award on the ground of manifest disregard, it seems more likely that the court believed that the arbitrators' denial of recovery to the claimant was contrary to the weight of the evidence.⁵¹ If the same case had been heard by a judge and jury instead of by arbitrators, and the jury had rendered a verdict for the defendant, the trial court might have granted the plaintiff a judgment notwithstanding the verdict on the ground that no reasonable jury could have found in the defendant's favor.⁵² Under the prevailing interpretation of the FAA, however, a court is not permitted to vacate an award simply because the arbitrators made erroneous findings of fact or law.⁵³

1998) (unpublished opinion) (citing *McDonnell Douglas*, 411 U.S. at 802).

⁵⁰ See Kenneth R. Davis, *The Stumbling Three-Step, Burden-Shifting Approach in Employment Discrimination Cases*, 61 BROOK. L. REV. 703 (1995). It is an indication of the complexity of the law in this area that *Hicks* was decided by a 5-4 majority of the Court and that in *Price Waterhouse v. Hopkins*, 490 U.S. 228 (1989) (another leading case on the question of the requisite burden of proof in Title VII cases), the Justices wrote four separate opinions covering 65 pages of the U.S. REPORTS: Justice Brennan wrote the opinion of the Court; Justices O'Connor and White wrote separate concurring opinions; and Justice Kennedy wrote a dissenting opinion.

⁵¹ The district court stated: "There is support for [Piper's] argument in the record, although there is also support for [Halligan's] claim. Determining the credibility of conflicting witnesses is a key component of an arbitration panel's duty, and crediting one witness over another does not constitute manifest disregard of the law." *Halligan v. Piper Jaffray, Inc.*, No. 96 Civ. 4472, 1997 WL 181028, at *3 (S.D.N.Y. Apr. 15, 1997), *rev'd*, 148 F.3d 197 (2d Cir. 1998).

⁵² Under Rule 50 of the Federal Rules of Civil Procedure, if "there is no legally sufficient evidentiary basis for a reasonable jury" to decide an issue in a party's favor, the trial judge

may determine the issue against that party and may grant a motion for judgment as a matter of law against that party with respect to a claim or defense that cannot under the controlling law be maintained or defeated without a favorable finding on that issue.

FED. R. CIV. P. 50.

⁵³ See *Miller v. Prudential Bache Sec., Inc.*, 884 F.2d 128, 130-31 (4th Cir. 1989);

Although the court paid lip service to the manifest disregard standard, it appears to have based its decision on the premise that, if the same case had been tried in a federal court, the plaintiff would have prevailed, and that a claimant asserting a statutory right should not be deprived of that right because he has submitted the matter to arbitration.

II. ARBITRABILITY OF EMPLOYMENT AGREEMENTS

As litigation becomes more expensive and time-consuming, it has become increasingly common for parties to enter into agreements to arbitrate any future disputes that may arise between them. Arbitration is supposed to be cheaper, faster, less disruptive, and more flexible than litigation.⁵⁴ It is well established today that agreements to arbitrate future disputes are generally enforceable. The FAA⁵⁵ makes arbitration agreements involving interstate commerce as enforceable as other contracts, and many states have similar statutes.⁵⁶ The Supreme Court has declared that the FAA is a "congressional declaration of a liberal federal policy favoring arbitration agreements."⁵⁷ To implement this policy, the federal courts give a generous interpretation to such agreements: any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.⁵⁸ Moreover, in the securities industry, arbitration has become the preferred method by which brokerage firms resolve disputes with their customers and with their employees.⁵⁹

The first question raised by *DiRussa* and *Halligan* is whether the FAA requires enforcement of an employee's agreement to arbitrate future disputes. The overriding purpose of the FAA, which was enacted in 1925, was to overcome the traditional hostility of the

French v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 784 F.2d 902, 906 (9th Cir. 1986).

⁵⁴ See *Allied-Bruce Terminix Cos., Inc. v. Dobson*, 513 U.S. 265, 280 (1995) (quoting H.R. REP. NO. 97-542, at 13 (1982)).

⁵⁵ 9 U.S.C. § 1 et seq. (1994).

⁵⁶ See, e.g., CAL. CIV. PROC. CODE § 1281 (West 1982); FLA. STAT. ANN. § 682.02 (West 1998); 710 ILL. COMP. STAT. 5/1 (West 1992); N.Y. C.P.L.R. 7501-14 (McKinney 1986); 42 PA. CONS. STAT. ANN. § 7303 (1982); TEX. CIV. PRAC. & REM. CODE ANN. § 171.001 (West 1997).

⁵⁷ *Moses H. Cone Mem'l Hosp. v. Mercury Const. Corp.*, 460 U.S. 1, 24 (1983).

⁵⁸ *Id.* at 24-25.

⁵⁹ U.S. GEN. ACCOUNTING OFFICE REPORT TO CONGRESSIONAL REQUESTERS, EMPLOYMENT DISCRIMINATION: HOW REGISTERED REPRESENTATIVES FARE IN DISCRIMINATION DISPUTES, Pub. No. GAO/HEHS-94-17, 57 (1994) (hereinafter GAO *Discrimination Report*).

courts to arbitration.⁶⁰ The FAA extends to all arbitration agreements that come within the full reach of the Commerce Clause of the Constitution.⁶¹

The broad congressional policy favoring arbitration is, however, subject to one important qualification. By its terms, section 1 of the FAA provides that the statute does not apply to "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." Although the Supreme Court has never construed this exclusionary clause, the lower federal courts have given it a narrow interpretation. Employing the canon of statutory or contractual construction known as *ejusdem generis* ("of the same kind"), the courts have interpreted the general term "any other class of workers" as being restricted by the more specific language that precedes it: i.e., to workers employed in interstate commerce *like* sailors and railway workers.⁶² Thus, the circuit courts that have considered the question have held that the exclusion is restricted to workers actually engaged in the movement of goods in interstate commerce.⁶³ The courts have sup-

⁶⁰ See *Allied-Bruce*, 513 U.S. at 270-71.

⁶¹ *Perry v. Thomas*, 482 U.S. 483, 490 (1987).

⁶² See *Rojas v. TK Communications, Inc.*, 87 F.3d 745, 748 (5th Cir. 1996); *Asplundh Tree Expert Co. v. Bates*, 71 F.3d 592, 598 (6th Cir. 1995); *Signal-Stat Corp. v. Local 475, United Elec., Radio and Mach. Workers of Am.*, 235 F.2d 298 (2d Cir. 1956); *Tenney Eng'g, Inc. v. United Elec. Radio & Mach. Workers of Am.*, 207 F.2d 450, 452 (3d Cir. 1953). See Jeffrey W. Stempel, *Reconsidering the Employment Contract Exclusion in Section 1 of the Federal Arbitration Act: Correcting the Judiciary's Failure of Statutory Vision*, 1991 J. DISP. RESOL. 259, for a comprehensive discussion of the exclusionary clause.

⁶³ See *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1471 (D.C. Cir. 1997) ("[E]very circuit to consider this issue squarely has found that section 1 of the FAA exempts only the employment contracts of workers actually engaged in the movement of goods in interstate commerce."). In *Cole*, the court based a narrow reading of the exclusionary clause on the rule of *ejusdem generis* ("of the same kind") and also on the canon of statutory interpretation that a statute should be construed to give a meaning to every word. *Id.* at 1470-71. If the words "any other class of workers engaged in foreign or interstate commerce" . . . extended to all workers whose jobs have any effect on commerce, the specific inclusion of seamen and railroad workers would have been unnecessary." *Id.* at 1470. See generally *Paladino v. Avnet Computer Tech.*, 134 F.3d 1054, 1060-61 (11th Cir. 1998). *Paladino* states that all but one of the circuit courts have construed the exclusionary clause narrowly. *Id.* (Cox, J., concurring). The single dissenting court was apparently the Fourth Circuit. See *United Elec. Radio & Mach. Workers of Am. v. Miller Metal Prods., Inc.*, 215 F.2d 221, 224 (4th Cir. 1954). However, in view of subsequent Supreme Court decisions favoring arbitration, *Miller* no longer has any force. See *O'Neil v. Hilton Head Hosp.*, 115 F.3d 272, 274 & n.1 (4th Cir. 1997). In *Willis v. Dean Witter Reynolds, Inc.*, 948 F.2d 305, 311-12 (6th Cir. 1991), the court found that the exclusionary clause covered all employment contracts. However,

ported this statutory interpretation, which seems inconsistent with the plain language of the statute, with various arguments. Some courts have reasoned that the strong federal policy in favor of arbitration requires a narrow reading of the exclusion for employment contracts.⁶⁴ Other courts have suggested that the term "workers" refers only to blue-collar employees and does not include salesmen and others with managerial responsibilities,⁶⁵ or that persons such as stockbrokers who do not physically transport goods across state lines are not engaged in interstate commerce.⁶⁶

Two strong arguments can be made, however, against a narrow construction of the exclusionary clause. First, it is anomalous to interpret the term "interstate commerce" in a radically different way in two sections of the same statute. Section 2 of the FAA, which contains the basic operative language of the statute, provides that an arbitration agreement "evidencing a transaction involving [interstate] commerce" shall be enforceable to the same extent as any other contract.⁶⁷ As stated earlier, the Supreme Court has held that this provision should be given a broad interpretation, which extends the reach of the FAA to the limits of the Commerce Clause of the Constitution.⁶⁸ On the other hand, section 1, which expressly excludes employment contracts of workers engaged in interstate commerce

in *Asplundh*, the Sixth Circuit declined to follow *Willis*, on the ground that its broad interpretation of the exclusionary clause was dictum. 71 F.3d at 596-97.

In 1993, the New York Court of Appeals stated: "A majority of the lower Federal courts that have considered the issue have held that the exclusion . . . extends to employment contracts in all industries." *Fletcher v. Kidder, Peabody & Co., Inc.*, 619 N.E.2d 998, 1005 (N.Y. 1993) (citing *Willis*). This statement appears to have been incorrect when it was made and is clearly incorrect today.

⁶⁴ See, e.g., *O'Neil*, 115 F.3d at 274.

⁶⁵ See, e.g., *Bernhardt v. Polygraphic Co. of Am., Inc.*, 218 F.2d 948, 951-52 (2d Cir. 1955), *rev'd on other grounds*, 350 U.S. 198 (1956).

⁶⁶ See, e.g., *Dickstein v. DuPont*, 443 F.2d 783, 785 (1st Cir. 1971). Professor Stempel points out the absurdity of this position:

[T]he broker who uses a long distance phone and the mail to consummate the sale of \$100,000 of federally regulated securities from a California buyer to a New York seller is not engaged in interstate commerce because she does not engage in physical movement of items across state lines. However, the letter carrier who lives in Lincoln, Nebraska, picks up mail at the central post office there, and then delivers it in a residential area of Lincoln is a worker engaged in interstate commerce.

Stempel, *supra* note 62, at 289.

⁶⁷ 9 U.S.C. § 2 (1994).

⁶⁸ See *Perry v. Thomas*, 482 U.S. 483, 490 (1987); see also *Allied-Bruce Terminix Cos., Inc. v. Dobson*, 513 U.S. 265, 274 (1995).

from the reach of the FAA, has been interpreted much more narrowly, so as to include only workers engaged in the physical transportation of goods across state lines.

Second, the legislative history of the FAA's exclusionary clause, while sparse, suggests that Congress intended to make arbitration agreements between merchants enforceable but not to extend the reach of the statute to labor disputes or employment contracts. At the time of the enactment of the FAA, members of various industries "supported industry-wide agreements to arbitrate because of the speed, economy, privacy, and finality of arbitration, and also the knowledge that disputes would be decided by representative individuals in the industry who could be expected to know far more about the particular industry than laypersons selected haphazardly as jurors in court cases."⁶⁹ It does not appear, however, that Congress intended the Act to apply to contracts of employment. The employment exclusion was first suggested in the course of Senate hearings on the bill that became the FAA. The following dialogue took place between Mr. Piatt, who represented the committee of the American Bar Association that had drafted the bill, and Senators Sterling and Walsh:

Mr. Piatt: [T]here is [a] matter I should call to your attention. Since you introduced this bill there has been an objection raised against it that I think should be met here, to wit, the official head, or whatever he is, of that part of the labor union that has to do with the ocean—the seamen—

Sen. Sterling: Mr. Furuseth?

Mr. Piatt: Yes, some such name as that. He has objected to it, and criticized it on the ground that the bill in its present form would affect, in fact compel, arbitration of the matters of agreement between the stevedores and their employers. Now, it was not the intention of the bill to have any such effect as that. It was not the intention of this bill to make an industrial arbitration in any sense; and so I suggest that in as far as the committee is concerned, if your honorable committee should feel that there is any danger of that, they should add to the bill the following language, "but nothing herein contained shall apply to seamen or any class of workers in interstate and foreign commerce." *It is not intended that this shall be an act referring to labor disputes at all.* It is purely an act to give the merchants the right or the privilege of sitting down and agreeing with each other as to what their damages are, if they want to do it. Now, that is all there is to this.

Sen. Walsh: This has occurred to me. I see no reason at all—I see none now; there may be some reason but I see no reason now—why,

⁶⁹ Norman S. Poser, *When ADR Eclipses Litigation: The Brave New World of Securities Arbitration*, 59 BROOK. L. REV. 1095, 1095-96 (1993).

when two men voluntarily agree to submit their controversy to arbitration, they should not be compelled to have it decided that way.

Mr. Piatt: Yes, sir.

Sen. Walsh: The trouble about the matter is that a great many of these contracts that are entered into are really not voluntary at all.⁷⁰

The concern expressed by Senator Walsh as to the voluntariness of employment contracts applies fully to DiRussa's and Halligan's situations. Their decisions to arbitrate their age discrimination claims, rather than to bring lawsuits in federal court, were not voluntary in any meaningful sense since they were required to sign arbitration agreements as a condition of employment in the securities industry. However, even if the FAA's exclusionary clause could be construed to cover stockbrokers' employment agreements, it is not clear that DiRussa and Halligan's obligation to arbitrate was based on an employment agreement. It was based on a written application that they were required to complete with the NYSE and the NASD (of which their employers were members) when they applied for employment. The Securities Exchange Act of 1934 (the "1934 Act") requires virtually all broker-dealers to be members of the NASD,⁷¹ and most large broker-dealer firms choose also to be member firms of the NYSE. Under the rules of these two self-regulatory organizations ("SROs"), any dispute between a member firm and an "associated person," arising out of the associated person's employment or termination of employment, must be arbitrated if either party demands arbitration.⁷² The term "associated person" includes any person who is engaged in the investment banking or securities business on behalf of a member firm of the NASD or NYSE and is therefore required by the rules of the organization to apply to be registered with it.⁷³ As so-called "registered representatives," DiRussa and Halligan were required by NASD and NYSE rules to sign the Uniform Application for Securi-

⁷⁰ *Hearings on Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial Arbitration, Before the Senate Comm. of the Judiciary*, 67th Cong. 9 (1923) (emphasis added).

⁷¹ 15 U.S.C. § 780(b)(8) (1994) requires that any broker-dealer that has dealings in securities, other than in commercial paper and similar instruments, not on a stock exchange of which it is a member must be a member of a registered national securities association. The NASD is the only such association that has ever been registered with the SEC.

⁷² NYSE Const. art. XI, § 1; NYSE RULES 600(a), 347; NASD RULES 10101(b), 10201(a).

⁷³ NASD Bylaws art. I(q); NYSE RULE 10.

ties Industry Registration or Transfer. This application form, which is designated as Form U-4, includes the following provision:

I agree to arbitrate any dispute, claim or controversy that may arise between me or my firm, or a customer, or any other person, that is required to be arbitrated under the rules, constitutions, or bylaws of the organizations with which I register . . . as may be amended from time to time and that any arbitration award rendered against me may be entered as a judgment in any court of competent jurisdiction.⁷⁴

By signing the Form U-4, registered employees such as DiRussa and Halligan agree to be bound by the arbitration provisions of the SRO, even if they do not sign an employment agreement containing an arbitration clause with the member firm that employs them. It can therefore be argued that the obligation of a registered employee to arbitrate disputes with his or her employer does not fall within the FAA's employment exclusion because the obligation to arbitrate is based on the application to register with the SRO as a broker and the agreement to be bound by the rules of the SRO, not on any agreement with the employer.⁷⁵ Alternatively, the employer may be able to enforce the arbitration clause in the Form U-4 on the ground that the employer is a third-party beneficiary of the agreement between the registered employee and the SRO.⁷⁶

In *Gilmer v. Interstate/Johnson Lane Corp.*,⁷⁷ which like the *DiRussa* and *Halligan* cases involved a brokerage-firm employee's claim against his employer under the ADEA, the Supreme Court declined to consider the question whether the exclusionary clause of the FAA excludes from the coverage of the FAA all "contracts of employment" or only contracts of workers in the transportation industries. The Court concluded that the exclusionary clause did not apply to *Gilmer's* arbitration agreement because it was contained

⁷⁴ NYSE RULE 345.12; NASD RULE 1140(c).

⁷⁵ *Metz v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 39 F.3d 1482, 1488 (10th Cir. 1994); *Schooley v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 867 F. Supp. 989, 991-92 (W.D. Okla. 1994). The requirement of the NASD and NYSE that a member-firm employee sign the Form U-4 is not an unconstitutional condition of employment. *Illyes v. John Nuveen & Co., Inc.*, 949 F. Supp. 580, 583-84 (N.D. Ill. 1996).

⁷⁶ *Stone v. Pennsylvania Merchant Group, Ltd.*, 949 F.Supp. 316 (E.D. Pa. 1996).

⁷⁷ 500 U.S. 20 (1991).

not in an employment agreement with the firm but in the Form U-4 registration application.⁷⁸ As Professor Jeffrey Stempel has pointed out, Gilmer's employer

gets to enforce the arbitration clause of a contract it did not sign but Gilmer is not permitted to invoke a statutory exclusion based on that same contract. [This result] seems grossly unfair by modern standards. At a minimum, it is a clear victory for formalism over functionalism and equity.⁷⁹

Compulsory arbitration of employment-related disputes is a cause for concern. Under the FAA, the basis for compelling arbitration is that the parties have voluntarily agreed to arbitrate and that arbitration agreements should be enforced to the same extent as other contracts. However, the fact that employment by a brokerage firm as a registered representative is conditioned on the employee's signing a Form U-4 means that the agreement can hardly be considered a voluntary one in any meaningful sense of the word.⁸⁰ Although the use by brokerage firms of standard-form customer agreements containing an arbitration clause raises the question of whether the customer freely gave his informed consent to the agreement, the element of coercion is much more palpable for an employee than it is for an investor.⁸¹ An investor may be able to find a brokerage firm that does not require an arbitration agreement or, in any case, may make investments without using a brokerage firm; but a person who wishes to make his living in the securities industry has no choice but to agree to arbitrate future disputes. The courts have given scant attention to these considerations in their eagerness to compel arbitration.

⁷⁸ *Id.* at 25 n.2.

⁷⁹ Stempel, *supra* note 62, at 277.

⁸⁰ This observation of course applies to the arbitration of any employment dispute, not just disputes involving claims of discrimination. However, the New York Court of Appeals has pointed out that in several recent federal decisions "the arbitration agreement contained in the U-4 Form was enforced even though the agreement had been signed as a condition to becoming a registered representative and a refusal to sign would have meant exclusion from the industry." *Fletcher v. Kidder, Peabody & Co., Inc.*, 619 N.E.2d 998, 1004 (N.Y. 1993).

⁸¹ In *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987), the Supreme Court held that an agreement between a brokerage firm and a customer to arbitrate future disputes, including claims arising under the 1934 Act, was enforceable.

III. ARBITRATION OF DISCRIMINATION CLAIMS

DiRussa and Halligan's claims were not ordinary employment disputes. They were claims based on violations of a federal statute that specifically gives employees redress for discrimination based on age. Compulsory arbitration of such claims raises public policy and practical concerns that are not present in run-of-the-mill brokerage-firm employment disputes such as those involving wrongful discharge, disagreements over commissions or other compensation, or solicitation of a firm's customers by a former employee in violation of an employment agreement. Arbitrators who are capable of resolving employment disputes may not have the necessary competence to deal with discrimination claims.⁸² Many NYSE and NASD arbitrators are not lawyers, let alone lawyers with expertise in enforcement of anti-discrimination statutes. Beyond the question of technical competence, the arbitrators, who are selected by securities-industry organizations (i.e., organizations whose members are the employers), may lack the insight, experience, and empathy to fully understand discrimination claims. As the United States General Accounting Office has reported, the panels that arbitrate discrimination cases have little racial or sexual diversity, being composed principally of white males, averaging sixty years of age, who receive little or no training in the discrimination laws.⁸³

Nevertheless, the Supreme Court's uncritical policy favoring the enforcement of arbitration agreements extends to discrimination

⁸² See *infra* Part IV.

⁸³ See GAO *Discrimination Report*, *supra* note 59, at 8-9; Margaret A. Jacobs, *Little Diversity Found on Panels For Securities-Firm Arbitration*, WALL ST. J., Apr. 1, 1994, at B3. Several months after the GAO Report was published, the Wall Street Journal reported that the NASD and NYSE had responded to the criticism by increasing the number of arbitrators receiving training in discrimination law and by stepping up efforts to recruit arbitrators with diverse backgrounds. Margaret A. Jacobs, *Judges Appear to be Growing Skeptical of Arbitration*, WALL ST. J., Dec. 22, 1994, at B2 [hereinafter *Judges Appear*].

Arbitration panels composed primarily of elderly white males may well be favorably disposed to claimants in ADEA cases. Nevertheless, the problems with compulsory arbitration in this area have been summarized as follows:

Those with grievances and their representatives say the industry picks its arbitrators from a Wall Street "old boy" network that is especially unlikely to look favorably on discrimination claims, requires little-to-no knowledge of employment law, conducts its operations in secret and explicitly tells its mediators they neither have to follow the law nor explain their decisions.

Barbara Presley Noble, *Attacking Compulsory Arbitration*, N.Y. TIMES, Jan. 15, 1995, sec. 3, p. 21.

claims. In *Gilmer v. Interstate/Johnson Lane Corp.*⁸⁴ the Court held that an employee of a brokerage firm must arbitrate a claim against the firm based on federally prohibited age discrimination. *Gilmer* is perhaps the most extreme example of the Court's adherence to what one writer has justifiably called "a doctrine of absolute deference to arbitrability—regardless of subject matter."⁸⁵ In *Gilmer*, a former executive of an NYSE member firm filed suit in a federal district court against the firm under the ADEA,⁸⁶ charging that the firm had terminated his employment because of his age.⁸⁷ The firm filed a motion to compel arbitration on the ground that Gilmer had agreed to arbitrate any future employment-related disputes when he signed the registration application on a Form U-4. The Supreme Court held, by a 7-2 majority,⁸⁸ that claims under the ADEA were arbitrable.

The Court's opinion in *Gilmer* consisted largely of citing its previous decisions that upheld arbitration agreements and that gave a broad interpretation to the FAA. Thus, the court stated at the outset: "It is by now clear that statutory claims may be the subject of an arbitration agreement, enforceable pursuant to the FAA" and recited that in recent years it had held enforceable agreements to arbitrate claims under the Sherman Antitrust Act, the Racketeer Influenced and Corrupt Organizations ("RICO") statute, the Securities Act of 1933, and the 1934 Act.⁸⁹ Conceding that the ADEA is designed not only to address individual grievances but also to address important social policies, the Court cited *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,⁹⁰ in which it had upheld the arbitrability of a claim under the antitrust laws, to support the view that there is no inherent inconsistency between these policies and enforcing agreements to arbitrate age discrimination claims.⁹¹ Similarly, the Court, refuting Gilmer's argument that arbitration would undermine the role of the EEOC in enforcing the ADEA,

⁸⁴ 500 U.S. 20 (1991).

⁸⁵ Jay R. Sever, *The Relaxation of Inarbitrability and Public Policy Checks on U.S. and Foreign Arbitration: Arbitration Out of Control?*, 65 TUL. L. REV. 1661, 1672 (1991).

⁸⁶ 29 U.S.C. § 621 et seq. (1985).

⁸⁷ Before bringing suit, Gilmer filed an age discrimination charge with the Equal Employment Opportunity Commission ("EEOC"). *Gilmer*, 500 U.S. at 23.

⁸⁸ Justice White wrote the majority's opinion. Justice Stevens wrote a dissent, which was joined by Justice Marshall. *Gilmer*, 500 U.S. at 22.

⁸⁹ *Id.* at 26.

⁹⁰ 473 U.S. 614 (1985).

⁹¹ *Gilmer*, 500 U.S. at 27-28.

cited the *Shearson/American Express, Inc. v. McMahon*⁹² and *Rodriguez de Quijas v. Shearson/American Express, Inc.*⁹³ In *McMahon* and *Rodriguez de Quijas*, the Court upheld where it upheld agreements to arbitrate claims arising under the federal securities statutes notwithstanding the important role played by the Securities and Exchange Commission ("SEC") in enforcing these laws, as support for its ruling that "the mere involvement of an administrative agency in the enforcement of a statute is not sufficient to preclude arbitration."⁹⁴ The Court found nothing in the ADEA to indicate that Congress intended to preclude arbitration; in fact, the ADEA's "flexible approach to resolution of claims," including conciliation, conference, and persuasion, suggests that arbitration is consistent with the statutory scheme of the ADEA.⁹⁵

The Court also rejected Gilmer's challenges to NYSE arbitration procedures:

[I]n our recent arbitration cases we have already rejected most of these arguments as insufficient to preclude arbitration of statutory claims. Such generalized attacks on arbitration "res[t] on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants," and as such, they are "far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes."⁹⁶

In particular, the Court dismissed Gilmer's assertion that NYSE arbitration panels would be biased, that the limits on discovery would make it more difficult to prove discrimination, that the absence of opinions by the arbitrators would result in a lack of public knowledge of employers' discriminatory policies, and that arbitration procedures do not provide for broad equitable relief and class actions.⁹⁷ The Court also cited its opinions in *McMahon* and *Rodriguez de Quijas* to support the proposition that inequality in bargaining power, absent a showing of coercion or fraud, is not a sufficient reason to refuse to enforce arbitration agreements in the employment context.⁹⁸

⁹² 482 U.S. 220 (1987).

⁹³ 490 U.S. 477 (1989).

⁹⁴ *Gilmer*, 500 U.S. at 28-29.

⁹⁵ *Id.* at 29.

⁹⁶ *Id.* at 30 (quoting *Rodriguez de Quijas*, 490 U.S. at 481).

⁹⁷ *Id.* at 30-32.

⁹⁸ *Id.* at 32-33.

Emboldened by the Supreme Court's uncritical attitude toward arbitration, hundreds of employers in many industries have inserted mandatory arbitration clauses in standard contracts with employees,⁹⁹ and the courts have interpreted *Gilmer* to cover other types of discrimination claims. Following *Gilmer*, several lower federal courts have held that claims of race and sex discrimination made by employees or former employees of brokerage firms against the firms pursuant to Title VII of the Civil Rights Act of 1964¹⁰⁰ are arbitrable.¹⁰¹ Similarly, an employee's claim that a brokerage firm fired him for taking time off in order to serve as a juror, in violation of the federal Jurors' Act,¹⁰² was held to be arbitrable.¹⁰³ The New York Court of Appeals has held that the FAA, as interpreted by the U.S. Supreme Court in *Gilmer*, requires the arbitration of race and sex discrimination claims brought under state law by registered employees of securities firms.¹⁰⁴

The SRO rules that force all employment discrimination suits, including those based on race and sex as well as on age, into arbitration have received a lot of unfavorable public attention.¹⁰⁵ A number of sex-discrimination suits by employees against brokerage

⁹⁹ Jacobs, *Judges Appear, supra* note 83, at B2. Interestingly, the AAA has indicated that it will refuse to administer mandatory arbitrations of patients' disputes with health-care providers. Margaret A. Jacobs, *American Arbitration Association To Change Policy on Health Care*, WALL ST. J., July 1, 1998, at B5.

¹⁰⁰ 42 U.S.C. § 2000e *et seq.* (1994).

¹⁰¹ See, e.g., *Metz v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 39 F.3d 1482 (10th Cir. 1994) (claim of sex discrimination is arbitrable); *Kidd v. Equitable Life Assurance Soc'y of the U.S.*, 32 F.3d 516 (11th Cir. 1994), *appeal after remand*, 119 F.3d 11, *cert. denied*, 118 S. Ct. 626 (1997) (race discrimination); *Alford v. Dean Witter Reynolds, Inc.*, 975 F.2d 1161 (5th Cir. 1992); *Bender v. A.G. Edwards & Sons, Inc.*, 971 F.2d 698 (11th Cir. 1992); *Willis v. Dean Witter Reynolds, Inc.*, 948 F.2d 305 (6th Cir. 1991); *Satarino v. A.G. Edwards & Sons, Inc.*, 941 F. Supp. 609 (N.D. Tex. 1996) (Americans with Disabilities Act); see also *Ludwig v. Equitable Life Assurance Soc'y of the U.S.*, 978 F. Supp. 1379 (D. Kan. 1997) (rejecting employee's argument that arbitration agreement was not valid because she did not know she was forgoing her right to sue in federal court).

¹⁰² 28 U.S.C. § 1875 (1994).

¹⁰³ *McNulty v. Prudential-Bache Sec., Inc.*, 871 F. Supp. 567 (E.D.N.Y. 1994).

¹⁰⁴ See *Fletcher v. Kidder, Peabody & Co., Inc.*, 619 N.E.2d 998 (N.Y. 1993). The New York Court of Appeals found that *Gilmer* required it to overrule its earlier decision in *Matter of Wertheim & Co. v. Halpert*, 397 N.E.2d 386 (N.Y. 1979), where it had held that pre-dispute agreements to arbitrate discrimination claims were unenforceable "because of the strong public policies embodied in Federal, State and local antidiscrimination laws." *Fletcher*, 619 N.E.2d at 1000.

¹⁰⁵ Patrick McGeehan, *Bias Panel Is Formed By NASD*, WALL ST. J., May 29, 1997, at C1.

firms have reinforced an image of the securities industry as "a male bastion hostile to women."¹⁰⁶ Meanwhile, the Chairman of the Securities and Exchange Commission, the New York Attorney General, the American Arbitration Association, and other groups have exerted pressure on the securities industry to replace mandatory arbitration of employment disputes with a voluntary arbitration system.¹⁰⁷

Courts, regulators, and even brokerage firms themselves, apparently responding to such criticism and pressure, have begun to place some limits on compelling brokerage-firm employees to arbitrate discrimination claims. Two Ninth Circuit decisions are particularly significant. In *Prudential Insurance Co. v. Lai*,¹⁰⁸ two female sales representatives of Prudential brought an action against Prudential and their immediate supervisor in a California state court on a variety of state-law claims, alleging that the supervisor had raped, harassed, and sexually abused them. Relying on the *Gilmer* holding, the firm moved in federal district court to compel arbitration, since the plaintiffs had signed Form U-4s containing arbitration agreements.¹⁰⁹

The Ninth Circuit found in the employees' favor, holding that, even after the *Gilmer* decision, "employees cannot be bound by an agreement to arbitrate employment discrimination claims unless they knowingly agreed to arbitrate such claims."¹¹⁰ On the basis of the plaintiffs' allegations, they did not knowingly agree to arbitrate because of the following alleged factual circumstances: when they signed the Form U-4, they were told only that they were applying

¹⁰⁶ Patrick McGeehan, *Smith Barney Moves Toward Sex-Bias Accord*, WALL ST. J., Aug. 19, 1997, at C1.

¹⁰⁷ See Patrick McGeehan, *Smith Barney Diversity Plan Represents a Major Leap for Women on Wall Street*, WALL ST. J., Nov. 19, 1997, at B2; *Voluntary Arbitration In Worker Disputes Endorsed by 2 Groups*, WALL ST. J., June 20, 1997, at B2. The Report of the Ruder Committee, published by the NASD in 1996, commented:

The requirement that employees arbitrate employment related disputes, especially claims arising from federal anti-discrimination statutes, has been criticized in many arenas. Labor representatives, academics, federal agencies and commissions, members of Congress, and the press have criticized various aspects of compulsory employment arbitration.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC., SECURITIES ARBITRATION REFORM: REPORT OF THE ARBITRATION POLICY TASK FORCE TO THE BOARD OF GOVERNORS, at 115-16 (1996) [hereinafter *Ruder Report*].

¹⁰⁸ 42 F.3d 1299 (9th Cir. 1994).

¹⁰⁹ *Id.* at 1301.

¹¹⁰ *Id.* at 1304.

to take a test which Prudential required for their employment; they were told to sign the forms without being given an opportunity to read them; arbitration was never mentioned to them; and they were not given a copy of the *NASD Manual*, which contains the terms of the arbitration agreement.¹¹¹

In *Duffield v. Robertson Stephens & Co.*,¹¹² the Ninth Circuit took an additional step beyond its decision in *Lai*, holding that the compulsory arbitration provision of the Form U-4 was unenforceable as applied to Title VII claims. The court based its decision largely on its reading of the legislative history of the Civil Rights Act of 1991, which indicated that Congress did not intend that a person could waive his or her right to bring Title VII claims in court.¹¹³ While recognizing that the general federal policy in favor of arbitration would ordinarily apply to the compulsory arbitration of civil rights claims, the court stated that, in view of the manifest intent of Congress, it was not free to apply the pro-arbitration policy to a Title VII claim.¹¹⁴

Similarly, a Massachusetts district court recently decided that a brokerage-firm employee could bring a sex discrimination claim

¹¹¹ *Id.* at 1301. In an unpublished opinion, a divided panel of the Sixth Circuit held that a sexual harassment claim brought under Title VII by an employee of a brokerage-firm was arbitrable. *Cosgrove v. Shearson Lehman Brothers*, 105 F.3d 659, 1997 WL 4783 (6th Cir.) (unpublished decision), *cert. denied*, 118 S. Ct. 169 (1997). The court distinguished *Lai* on the grounds that the arbitration clause in *Lai* did not "describe the types of disputes that were to be subject to arbitration" and "did not even refer to employment disputes." *Id.* at *6 (quoting *Lai*, 42 F.3d at 1305). In the case before the Sixth Circuit, on the other hand, "the arbitration agreement . . . specifically refer[s] to arbitration of 'any controversy arising out of or in connection with my compensation, employment or termination of employment.'" *Id.* at *2. The dissenting judge would have remanded the case to the district court for a finding of whether the claimant "was indeed aware that she would be waiving her right to bring a Title VII action in federal court merely by applying for a job with Shearson Lehman Brothers." *Id.* at *3; see also *DeGaetano v. Smith Barney, Inc.*, No. 95 Civ. 1613, 1996 WL 44226, at *7 (S.D.N.Y. Feb. 5, 1996) (distinguishing *Lai* on the ground that the agreement expressly described the types of disputes that would be subject to arbitration); *Pitter v. Prudential Life Ins. Co. of Am.*, 906 F. Supp. 130, 139 (E.D.N.Y. 1995) (rejecting the "implicit . . . suggestion" in *Lai* that "federal law favoring arbitration and requiring liberal construction of arbitration agreements is not applicable to statutory claims of discrimination.").

¹¹² 144 F.3d 1182 (9th Cir. 1998), *cert. denied*, No. 98-237, 1998 WL 467389 (U.S. Nov. 9, 1998).

¹¹³ *Id.* at 1190, 1195.

¹¹⁴ *Id.* at 1199. Nevertheless, the court held that "because no state action is involved there is no constitutional bar to employers requiring employees to agree in advance to arbitrate state-law tort and contract claims (other than for violation of a state civil rights law)." *Id.* at 1185.

under Title VII of the Civil Rights Act in federal court despite having signed a Form U-4 containing a standard arbitration clause.¹¹⁵ The court based its decision not only on the congressional intent as expressed in the legislative history of Title VII but also on a "structural bias" that it found in the NYSE arbitration system, in that it is dominated by employers (i.e., brokerage firms), one of which was the defendant in the litigation before the court.¹¹⁶ The court stated:

Dominance of an arbitral system by one side in the dispute does not comport with any model of arbitral impartiality, especially when that dominance takes the form of selecting the entire arbitrator pool, appointing the individual arbitration panels, and making important procedural and discovery decisions.¹¹⁷

. . .

Whatever the competence or fairness of individual arbitrators who participate [in] the NYSE system, its structural imbalance makes it an inadequate forum for vindicating civil rights.¹¹⁸

There are other signs that compulsory arbitration of employment discrimination claims is crumbling. In August 1997, the Board of Directors of the NASD voted to exclude discrimination (including sexual harassment) claims from the mandatory arbitration requirement of the Form U-4.¹¹⁹ After considering the proposal for nearly a year, the SEC approved it in June 1998.¹²⁰ Under the amended rule, firms are still free to require their employees to sign arbitration agreements covering discrimination and harassment disputes as a precondition of employment, but an employee no longer violates NASD rules by filing a lawsuit covering such a claim.¹²¹

¹¹⁵ *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 995 F. Supp. 190 (D. Mass. 1998); see also Margaret A. Jacobs, *Judge finds Merrill Lynch Can't Force Ex-Consultant to Arbitrate Bias Claim*, WALL ST. J., Jan. 27, 1998, at B8.

¹¹⁶ 995 F. Supp. at 207.

¹¹⁷ *Id.* at 211.

¹¹⁸ *Id.*

¹¹⁹ The rule change, which amends Rule 10201 of the NASD Code of Arbitration Procedure provides as follows:

(b) A claim alleging employment discrimination or sexual harassment in violation of a statute is not required to be arbitrated. Such a claim may be arbitrated only if the parties have agreed to arbitrate it, either before or after the dispute arose.

SEC Rel. No. 34-39421, 62 Fed. Reg. 242 (Dec. 10, 1997).

¹²⁰ SEC Rel. No. 34-40109, 63 Fed. Reg. 35299 (June 29, 1998). The SEC had published the proposed amendment (SR-NASD-97-77) for comment in December 1997. SEC Release No. 34-39421, 62 Fed. Reg. 242 (Dec. 10, 1997). For a discussion of the NASD proposal, see IX SEC. ARBITRATION COMMENTATOR, NO. 4 at 8 (Nov. 1997).

¹²¹ Patrick McGeehan, *NASD May Vote Today to Halt Mandated Harassment Arbitra-*

The rule change effectively leaves a brokerage-firm employee in a similar situation with respect to arbitration of discrimination claims as a brokerage-firm customer is with respect to all claims. Both employees and customers are compelled to arbitrate a dispute with the firm only if they have executed a valid arbitration agreement covering the dispute.¹²² Most firms require their customers to sign such agreements as a condition of opening and maintaining a brokerage account.¹²³ It is possible that the firms will impose the same requirement on their employees. Thus, if brokerage firms continue to require their employees to sign an arbitration agreement as a condition of employment, employees will still be under pressure to sign.¹²⁴ In September 1998, however, the NYSE board of directors went one step further than the NASD, voting to stop providing a forum for arbitration of discrimination claims unless the parties agree to arbitrate after the dispute has arisen.¹²⁵

In May 1998, Merrill Lynch, the largest brokerage firm in U.S., announced that it was adopting a new dispute resolution policy for employees' civil rights claims under which the employee would not be required to arbitrate such disputes. Merrill Lynch's initiative was part of its attempt to settle a putative class action suit in Illinois federal court, in which the plaintiffs claimed that the firm had systematically excluded women from employment opportunities and advancement and had retaliated against those who complained.¹²⁶

tion, WALL ST. J., Aug. 7, 1997, at B2; Patrick McGeehan, *NASD Set to End Practice of Submitting All Employment Disputes to Arbitration*, WALL ST. J., July 21, 1997, at A4; Floyd Norris, *Job Hunting to Be Harder for Errant Brokers*, N.Y. TIMES, Aug. 8, 1997, at D3.

¹²² Under the new NASD rule, any arbitration clause covering discrimination claims will have to be contained in the employment agreement between the brokerage firm and its employee, not in the Form U-4 that the NASD requires the employee to sign. The agreement to arbitrate might thus be subject to the exclusion contained in section 1 of the FAA for contracts of employees in interstate commerce. See *supra* text accompanying note 62.

¹²³ U.S. GEN. ACCOUNTING OFFICE REPORT TO CONGRESSIONAL REQUESTERS, *SECURITIES ARBITRATION: HOW INVESTORS FARE*, Pub. No. GAO/GGD-92-74, 28 (1992).

¹²⁴ However, legislation introduced in Congress in 1998 by Senator Feingold and Representative Markey would amend seven civil rights statutes to guarantee that federal discrimination claims could be brought in a federal court. Fed. Sec. L. Rep. (CCH) No. 1834 (Aug. 12, 1998) at 2.

¹²⁵ Patrick McGeehan, *Big Board Moves To End Practice on Arbitrations*, WALL ST. J., Sept. 4, 1998, at B6.

¹²⁶ *Merrill Adopts Dispute Resolution Program in Wake of Discrimination Suit Settlement*, 30 Sec. Reg. & L. Rep. (BNA) 822 (May 29, 1998); see also Patrick McGeehan, *Merrill Lynch Is Drafting a New Policy That Could Let Employees Sue in Court*, WALL

Under the new policy, if an employee's claim of discrimination could not be settled within the company, the employee would first be required to submit the dispute to mediation. Merrill Lynch would pay the costs of the mediation, including the mediator's fees. If the matter was still not resolved, the employee would have three options: to arbitrate before an industry self-regulatory organization such as the NASD; to arbitrate before the non-profit American Arbitration Association or JAMS/Endispute, a professional provider of dispute-resolution services; or to bring an action in court. Employee claims against Merrill Lynch not involving discrimination would continue to be subject to compulsory arbitration.¹²⁷

Salomon Smith Barney, also one of the largest brokerage firms, similarly settled a sex-discrimination class action by agreeing to establish a dispute-resolution system whereby employees would bring such claims to a forum not operated by the securities industry. Under the settlement, claimants will be permitted to take gender-based claims to a mediator. If mediation does not resolve the claim, it will then be brought to a panel of non-industry arbitrators.¹²⁸

These recent judicial and non-judicial developments apparently reflect a deep concern felt by many judges and regulators with an industry-wide system of dispute resolution that requires employees, as a condition of their employment, to submit statutory discrimination claims to binding arbitration in industry-sponsored forums.

Whether large employers such as Merrill Lynch and Salomon Smith Barney share this concern or are motivated principally by considerations of legal exposure, employee morale, or public relations perceptions, their elimination of mandatory arbitration in these cases is likely to be followed by other firms. Thus, although most securities-industry employees' claims will continue to be arbitrated, discrimination claims will now constitute a significant exception to this practice.

St. J., Jan. 22, 1998, at C1; *Merrill Lynch Drops Mandatory Arbitration Under Agreement Settling Discrimination Suit*, 30 Sec. Reg. & L. Rep. (BNA) 702 (May 8, 1998).

¹²⁷ *Merrill Adopts Dispute Resolution Program In Wake of Discrimination Suit Settlement*, 30 Sec. Reg. & L. Rep. (BNA) 822 (May 29, 1998).

¹²⁸ Patrick McGeehan, *Judge Approves Class-Action Settlement For Sex Harassment at Smith Barney*, WALL ST. J., July 27, 1998, at B4.

IV. COMPETENCE OF ARBITRATORS

Beyond the legal issues, the *DiRussa* and perhaps the *Halligan* cases raise questions about the competence of the arbitrators. In *DiRussa*, it is not clear why the arbitrators failed to apply a "well defined, explicit, and clearly applicable" provision of governing law:¹²⁹ namely, that a successful ADEA claimant is entitled to attorneys' fees. It also not clear why the arbitrators in *Halligan* rejected his age discrimination claim in the face of strong evidence supporting the claim. One would hope that most arbitrators believe that their decisions' virtual freedom from judicial review places a special burden on them to assure themselves that they are properly weighing the evidence and applying the law.¹³⁰ To do this, however, requires enough knowledge and understanding of the applicable law to enable the arbitrators to ask appropriate questions of the parties, witnesses, and attorneys; to understand and interpret the applicable law; and to apply the law correctly.¹³¹ It is possible, of course, that the virtual absence of judicial review encourages arbitrators to feel *less* responsibility to apply the law correctly. If the arbitrators do not understand the law, or if they misapply or fail to apply the law, claimants may be deprived of substantive rights that they would be entitled to in a court proceeding.¹³²

¹²⁹ 121 F.3d 818, 821 (quoting Merrill Lynch, Pierce, Fenner, & Smith, Inc. v. Bobker, 808 F.2d 930, 933-34 (2d Cir. 1986)).

¹³⁰ See *Cole v. Burns Int'l Sec. Serv.*, 105 F.3d 1465, 1488 (D.C. Cir. 1997) (Arbitrators are under a professional obligation "to handle statutory issues only if they are prepared to fully protect the rights of statutory claimants. To meet that obligation, arbitrators must educate themselves about the law.").

¹³¹ One commentator has stated that there are four kinds of situations that might possibly come under the heading of "manifest disregard": (1) the arbitrator simply applies the wrong law; (2) the arbitrator says he will apply the correct law but misapplies it; (3) the arbitrator says that the law is unsettled but applies the law he prefers; and (4) the arbitrator states the correct law, but then applies a different law. According to this writer, only the fourth kind of situation is clearly manifest disregard of the law. Marta B. Varela, *Arbitration and the Doctrine of Manifest Disregard*, 49 DISP. RESOL. J. 64, 67 & n.9 (1994) (citing Isabella de la Houssaye, Note, *Manifest Disregard of the Law in International Commercial Arbitrations*, 2 COLUM. J. TRANSNAT'L L. 449, 454 (1990)). *DiRussa* seems to involve an additional fifth category: the arbitrators simply failed to apply the applicable law.

¹³² For a debate between a lawyer who represents claimants and a lawyer who represents respondents on the competence of arbitrators in employment discrimination cases, see Symposium, *Employment Discrimination, New York Stock Exchange, Inc. Symposium on Arbitration in the Securities Industry*, 63 FORDHAM L. REV. 1613 (1995).

With the inception of mandatory securities arbitration in 1987, the problem of recruiting and training arbitrators became an urgent one. The caseload of the NASD and the other arbitration forums increased enormously, requiring these entities to expand their existing pools of arbitrators.¹³³ In 1995, over 6,000 cases were filed with the NASD, as compared to about 1,500 cases in 1986.¹³⁴ Furthermore, the difficulty experienced by the SROs in maintaining a sufficient number of qualified arbitrators was exacerbated by several factors other than the increased caseload, including the complexity of the issues involved in many of the cases coming before arbitration panels; new arbitration rules and procedures, particularly those calling for an increased opportunity for pre-hearing discovery; scheduling delays; the longer duration of arbitrations, partly as a result of the new rules; the demands imposed by mandatory training programs for arbitrators; and the low compensation of arbitrators.¹³⁵ In 1995, the NASD inaugurated an arbitrator recruitment plan, which was designed to increase the number, quality, and diversity of available arbitrators.

Few NASD or NYSE arbitrators, however, even if they are lawyers, and even if they have expertise in securities issues, are likely to have any substantial background in interpreting anti-discrimination statutes.¹³⁶ Despite improvements in recruitment and training of arbitrators, the NASD and NYSE exercise little control over their competence. They do not require that arbitrators of employment cases have any background or expertise in employment law or that they receive training in specific areas of the law.¹³⁷

¹³³ Eighty-three percent of all arbitrations administered by securities industry organizations are with the NASD, while most of the remainder are with the NYSE. NORMAN S. POSER, *BROKER-DEALER LAW AND REGULATION* 8-3 n.5 (Aspen Law & Business 2d ed. 1997).

¹³⁴ *Id.* at 8-3 to 8-5. Eighteen percent of these cases were disputes between broker-dealers and their employees. Most of the remainder were disputes between broker-dealers and customers. *Id.* at 8-3.

¹³⁵ See Robert S. Clemente, *Trends in Securities Industry Arbitration: A View of the Past, the Present, and the Future: "The Dream, the Nightmare, and the Reality,"* 68 N.Y. ST. B.J. 18 (Oct. 1996) (Mr. Clemente is Director of Arbitration of the NYSE).

¹³⁶ Symposium, *Employment Discrimination, New York Stock Exchange, Inc. Symposium on Arbitration in the Securities Industry*, 63 *FORDHAM L. REV.* 1613 (1995) (opening remarks of Professor Katsoris).

¹³⁷ *GAO Discrimination Report*, *supra* note 59, at 13; Megan L. Dunphy, *Mandatory Arbitration: Stripping Securities Industry Employees of Their Civil Rights*, 44 *CATH. U. L. REV.* 1169, 1198-1200 (1995). In October 1998, the NASD announced that it would develop a special roster of arbitrators trained and experienced in discrimination law and that it would adopt a requirement that panels hearing discrimination cases "be composed

The process whereby the SROs select arbitrators for particular cases does not ensure that an arbitrator in an employment case be knowledgeable about employment law.¹³⁸ One commentator has stated that arbitrators are far more likely than judges to rely extensively on treatises and leading cases on employment discrimination law, without citing to later cases decided by lower courts or less publicized decisions. "This means that an arbitrator's decision may be based on broad stroke principles to the exclusion of cases more analogous to the claim being decided."¹³⁹

The compensation that arbitrators receive from the NASD, \$225 per day, with the chairman of the panel receiving an additional \$50 per day, is considerably lower than the normal compensation of an active lawyer, securities professional, or even professor of finance or law. As a result, the NASD pool of arbitrators tends to be composed largely of retired persons and full-time professional arbitrators.¹⁴⁰ While such persons often bring substantial experience to their role as arbitrators, some of them may lack the vigor and breadth of outlook necessary to arbitrate a complex securities or employment case. Furthermore, persons who frequently serve as arbitrators may be subject to subtle pressures if a significant portion of their livelihood depends on that activity. In particular, if an arbitrator decides too many cases adversely to brokerage firms, he or she is likely to be challenged peremptorily by brokerage firms in future cases.¹⁴¹ The converse is less likely to be true because it is

of arbitrators who, in their private capacities, do not primarily represent employers or employees." *NASD Proposes Arbitration Changes For Industry Statutory Discrimination Claims*, 30 Sec. Reg. L. Rep. (BNA) 1472 (Oct. 9, 1998).

¹³⁸ Dunphy, *supra* note 137, at 1174.

¹³⁹ Richard H. Block & Elizabeth A. Barasch, *Practical Ramifications of Arbitration of Employment Discrimination Claims, Proceedings of 44th Annual Meeting of New York University's Conf. on Labor*, (1991), at 281, 294. An empirical study conducted in 1975 by Professor (now Judge) Harry T. Edwards showed that only a small percentage of the arbitrators surveyed could explain the current status of discrimination law or define relevant terms, and only about 72 percent of these arbitrators felt professionally competent to decide legal issues in employment discrimination cases. Sixteen percent had never read a judicial opinion on the subject, and most of these did not regularly read labor law advance sheets to keep abreast of current developments on discrimination law. Harry T. Edwards, *Arbitration of Employment Discrimination Cases: An Empirical Study, Proceedings of the 28th Annual Meeting of the National Academy of Arbitrators* (1976), at 71-72. These findings of course are more than twenty years old and may have limited value today.

¹⁴⁰ GAO *Discrimination Report*, *supra* note 59, at 57.

¹⁴¹ In an NASD or NYSE arbitration, each party has one peremptory challenge and an unlimited number of challenges for cause. NYSE RULE 609; NASD RULE 10311.

less feasible or cost-effective for investors' or employees' lawyers to investigate arbitrators' previous decisions and keep detailed records of them.

The NASD inaugurated a voluntary training program for arbitrators in 1985, making the program mandatory in 1993.¹⁴² According to the NASD's 1996 Ruder Report: "The mandatory program is typically a day long program and provides a basic overview of the securities arbitration process."¹⁴³ Unfortunately, requiring potential arbitrators to attend training sessions has deterred potential arbitrators from participating. Many of them apparently believe that neither the compensation they receive nor the frequency with which they serve on panels justifies attending the training sessions. When the program became mandatory in 1993, the pool of NASD arbitrators dropped from 7,000 to 2,400.¹⁴⁴

Improvement in the selection and training of arbitrators would be an important step toward avoiding erroneous arbitral decisions such as those that occurred in *DiRussa* and *Halligan*, but this is unlikely to be a *complete* solution. Justice Black pointed out more than thirty years ago that arbitrators "in all probability will be nonlawyers, wholly unqualified to decide legal issues."¹⁴⁵ Furthermore, arbitrators with extensive experience in employment law are often challenged by one or more parties to a dispute.¹⁴⁶ The availability of arbitrators competent to decide discrimination claims is likely to remain limited, given the heavy caseload of the SRO arbitration departments and the modest compensation that arbitrators receive.

Requiring arbitrators to be lawyers who are conversant with federal and state anti-discrimination statutes and judicial interpreta-

¹⁴² Deborah Masucci, *Securities Arbitration—A Success Story: What Does the Future Hold?*, 31 WAKE FOREST L. REV. 183, 199 (1996).

¹⁴³ *Ruder Report*, *supra* note 107, at 108. In addition to the introductory training session, the NASD offers a voluntary program for panel chairmen, as well as continuing education for arbitrators, which includes seminars and workshops. *Id.*; Masucci, *supra* note 142, at 199. For example, the NASD scheduled nineteen training sessions in eleven cities for the month of March 1997. See 8 SEC. ARBITRATION COMMENTATOR, NO. 8, at 18 (Dec. 1996).

¹⁴⁴ Masucci, *supra* note 142, at 199. By 1996, however, the size of the pool had risen to 4,600. *Id.* at 200; *Ruder Report*, *supra* note 107, at 102.

¹⁴⁵ *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 407 (1967) (Black, J., dissenting).

¹⁴⁶ Symposium, *Employment Discrimination New York Stock Exchange, Inc. Symposium on Arbitration in the Securities Industry*, 63 FORDHAM L. REV. 1501 (1995) (Foreword).

tions of these statutes seems impractical. Even if such persons could be found, they would require substantially higher compensation than the modest sum that the SROs pay their arbitrators. Raising the level of competence of arbitrators is a desirable goal, but there is no way of avoiding reliance on judicial review in order to guarantee that persons making discrimination claims before an arbitrator receive the same substantive rights as they would if they had brought their claims in court.

V. JUDICIAL REVIEW OF ARBITRATION AWARDS: MANIFEST DISREGARD OF THE LAW

The holdings of the *DiRussa* and *Halligan* cases focus on the scope of the judicial review of the arbitrators' decisions. Having been required to submit his statutory age discrimination claim to arbitration as a condition of his employment by an NYSE member firm, the Second Circuit panel held that DiRussa was not entitled to the rights afforded to him by the ADEA. To be more precise, the court held that DiRussa was entitled only to those protections of the ADEA that the arbitrators chose to allow him. Specifically, although the ADEA provides that a successful claimant is entitled to reasonable attorneys' fees, the arbitrators' denial of these fees was not reviewable by the court. An observer not familiar with American arbitration law might be surprised to learn that a reviewing court is powerless to vacate an arbitral award, even if the arbitrators made a clear error of statutory law.¹⁴⁷

In *Halligan*, the Second Circuit, without giving any explanation, reversed the usual presumption that protected arbitrators' awards. Previously, the courts held an arbitrator's decision would be confirmed if any rational basis for it could be found. The *Halligan* court concluded, to the contrary, that arbitrators who render an award that goes against the weight of the evidence acted in manifest disregard of the law unless they write an opinion pro-

¹⁴⁷ See *Miller v. Prudential Bache Sec., Inc.*, 884 F.2d 128, 130 (4th Cir. 1989); *French v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 784 F.2d 902, 906 (9th Cir. 1985). Under section 57 of the Arbitration Act of 1996 of the United Kingdom, a court is not necessarily bound by an arbitral decision. William W. Park, *The Interaction of the Courts and Arbitrators in England: the 1996 Act as a Model for the United States?*, 1 INT'L ARB. L. REV. 54, 63 n.114 (1998).

viding a rationale for the award. Although this decision appears sensible and just, it should be recognized as a radical departure from existing arbitration law.

Because speed, economy, and finality are the paramount goals of arbitration, the scope of judicial review of arbitral awards is narrow.¹⁴⁸ The FAA provides for only limited judicial review of arbitration awards.¹⁴⁹ The FAA lists four grounds for vacating an award: (1) where the award was procured by corruption, fraud or undue means; (2) where there was evident partiality or corruption in the arbitrators; (3) where the arbitrators were guilty of misconduct; (4) where the arbitrators exceeded their powers.¹⁵⁰ All but two circuit courts have held that, in addition to these four statutory grounds, an arbitral award may be vacated on a non-statutory ground: if the arbitrators acted "in manifest disregard of the law."¹⁵¹ However, in conformity with the Supreme Court's strong pro-arbitration policy, the federal courts have given almost unquestioning deference to arbitral awards and have construed manifest disregard narrowly.

¹⁴⁸ If the court can find any "argument that is legally plausible and supports the award," it must confirm the award. *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Jaros*, 70 F.3d 418, 421 (6th Cir. 1995).

¹⁴⁹ See *Loughridge v. Allen*, 25 F.3d 1057 (10th Cir. 1994) ("[N]o matter how dubious an arbitrator's decision might appear . . . if the arbitrator did not stray beyond the four corners of the agreement to find the essence of his decision, the arbitrator's award must be upheld. . . . This is so regardless that error has been committed or that a court would reach a contrary conclusion." (quoting *NCR Corp., E & M-Wichita v. International Ass'n of Machinists and Aerospace Workers*, Dist. Lodge No. 70, 906 F.2d 1499, 1504 (10th Cir. 1990)).

¹⁵⁰ 9 U.S.C. § 10(a)(1)-(4) (1994). In addition, a court may modify or correct an award on three grounds: (a) Where there was an evident material miscalculation of figures or an evident material mistake in a description of any person, thing, or property referred to in the award. (b) Where the arbitrators have awarded upon a matter not submitted to them (c) Where the award is imperfect in matter of form not affecting the merits of the controversy." 9 U.S.C. § 11(a)-(c) (1994).

¹⁵¹ Only the Fifth and Seventh Circuits have rejected the "manifest disregard" ground. *Baravati v. Josephthal, Lyon & Ross, Inc.*, 28 F.3d 704, 706 (7th Cir. 1994); *R.M. Perez & Assoc., Inc. v. Welch*, 960 F.2d 534, 539-40 (5th Cir. 1992). The Fifth Circuit, however, has stated that it will vacate an award if it is "fundamentally unfair" or if it violates a specific and clearly identifiable public policy. *Gulf Coast Indus. Workers Union v. Exxon Co., U.S.A.*, 991 F.2d 244, 249 (5th Cir. 1993); *R.M. Perez & Assoc. v. Welch*, 960 F.2d 534, 539-40 (5th Cir. 1992). The *Arbitrator's Manual*, compiled by members of the Securities Industry Conference on Arbitration, also states that an award may be vacated when an arbitrator manifestly disregards the law. *Arbitrator's Manual* at 26, 29 (1992).

DiRussa argued before the Second Circuit panel that the arbitrators' refusal to award him reasonable attorney's fees should be vacated or modified on two grounds: that the arbitrators exceeded their powers, and that they acted in manifest disregard of the law. In rejecting the argument that the arbitrators had exceeded their powers, the court gave a narrow interpretation to Section 10(a)(4) of the FAA, which permits vacatur of an award on such ground. The court's inquiry into deciding whether the arbitrators exceeded their powers focused on whether the arbitrators had the power to reach the issue of attorney's fees, not on whether the arbitrators correctly decided that issue. The parties had clearly submitted to the arbitrators the issue of whether DiRussa was entitled to attorney's fees, and this issue was properly before the arbitrators. Thus, the court found that the arbitrators did not exceed their powers when they decided not to award attorneys' fees, stating, "DiRussa's real objection appears to be that the arbitrators committed an obvious legal error in denying him attorney's fees. Section 10(a)(4) was not intended to apply to such a situation."¹⁵²

The Second Circuit's decision that the *DiRussa* arbitrators did not act in manifest disregard of the law raises difficult and troubling issues. The judicially created "manifest disregard" ground for vacatur represents an attempt by the federal courts to resolve the inherent contradiction between the goal that arbitrators faithfully and accurately apply the law and the absence of meaningful judicial

¹⁵² *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818, 824 (2d Cir. 1997), cert. denied, 118 S. Ct. 695 (1998). The court's rejection of DiRussa's argument that the arbitrators exceeded their authority seems correct. Admittedly, section 10(a)(4) of the FAA raises complex and important definitional questions. If, for example, an arbitration panel awards a claimant punitive damages despite the fact that the law applicable to the dispute does not permit arbitrators to make such an award, it has been held that the arbitrators exceeded their powers and that the award must therefore be vacated under section 10(a)(4). See *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 20 F.3d 713, 716 (7th Cir. 1994), *rev'd on other grounds*, 514 U.S. 52 (1995). It might be equally plausible, however, to say that the arbitrators simply made an error of law by awarding punitive damages, which would not be a ground for setting aside the award.

In *DiRussa*, however, the argument that the arbitrators lacked the power *not* to award attorney's fees seems a weaker example of lacking power than the punitive-damages example. It is easier to assert that a person lacks the power to *do* something than to assert he or she lacks the power *not to do* something. Arguably, however, if the *DiRussa* court had decided that the arbitrators' refusal to award attorney's fees exceeded their powers, the court's interpretation of section 10(a)(4) would have so broadened this provision that it could conceivably be made the basis for vacating any erroneous award. It is difficult to construe section 10 of the FAA, which carefully spells out narrow grounds for review of arbitral decisions, in a way that would permit such a result.

review to enforce this goal. Stated another way, the manifest disregard ground is an attempt to balance "the public interest in having arbitrators stay within the applicable law versus the public policy in favor of speedy and economical function of the arbitration process."¹⁵³

The manifest disregard standard had its origin in dictum in the Supreme Court's 1953 opinion in *Wilko v. Swan*.¹⁵⁴ In *Wilko*, the Court held that agreements to arbitrate disputes arising under the Securities Act of 1933 ("1933 Act") were unenforceable, essentially because, in the Court's view at that time, arbitration did not assure a purchaser of securities that he would receive the same rights under the statute that he would if he had brought suit in a federal court. The Court pointed to the narrow scope of judicial review of arbitration awards as a basis for its holding:

Even though the provisions of the Securities Act, advantageous to the buyer, apply, their effectiveness in application is lessened in arbitration as compared to judicial proceedings. . . . Power to vacate an award is limited [I]nterpretations of the law by the arbitrators *in contrast to manifest disregard* are not subject . . . to judicial review for error in interpretation.¹⁵⁵

Although the Supreme Court overruled *Wilko* in 1989, holding that agreements to arbitrate 1933 Act claims were enforceable,¹⁵⁶ it subsequently cited *Wilko's* manifest disregard dictum with approval.¹⁵⁷ The Court's observations concerning the limits of judicial review therefore remain pertinent.¹⁵⁸ As the *Wilko* Court suggested, manifest disregard requires more than a mere error or misunderstanding with respect to the law. In general, the courts will not vacate or modify an award unless the moving party can show that no proper basis for the award can be inferred from the facts of the case.¹⁵⁹ Given the fact that arbitrators seldom write opinions

¹⁵³ Varela, *supra* note 131, at 71 (citing *Sobel v. Hertz, Wamer & Co.*, 469 F.2d 1211, 1215 (2d Cir. 1972)).

¹⁵⁴ 346 U.S. 427 (1953), *overruled by* *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989).

¹⁵⁵ 346 U.S. at 435-37 (emphasis added).

¹⁵⁶ *Rodriguez de Quijas*, 490 U.S. at 477. Two years before *Rodriguez*, the Court, without formally overruling *Wilko*, had held that agreements to arbitrate 1934 Act claims were enforceable. *Shearson/American Express v. McMahon*, 482 U.S. 220 (1987).

¹⁵⁷ *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 942 (1995).

¹⁵⁸ *But see Baravati v. Josephthal, Lyon & Ross, Inc.*, 28 F.3d 704, 706 (7th Cir. 1994) (Supreme Court's overruling of *Wilko* also discredits its "manifest disregard" dictum).

¹⁵⁹ *Wall St. Assoc., L.P. v. Becker Paribas, Inc.*, 27 F.3d 845, 849 (2d Cir. 1994); see

explaining their decisions, there is little likelihood that a losing party in an arbitration will be able to persuade a reviewing court that the arbitrators manifestly disregarded the law. Consequently, although most circuit courts have adopted "manifest disregard of the law" as a non-statutory ground for vacating or modifying an award, until recently there have been few cases in which a court has set aside an arbitral award on this ground.¹⁶⁰ A recent example of such a case is the Eleventh Circuit's decision in *Montes v. Shearson Lehman Bros., Inc.*,¹⁶¹ where the record of the arbitration hearing showed that Shearson's attorney explicitly urged the arbitrators to disregard the law, and the court observed that "there [was] nothing in the record to show that they did not do so."¹⁶² But it must be exceedingly rare for an attorney to make the mistake of opening the door for vacatur in this way.¹⁶³

also *Edward D. Jones & Co. v. Schwartz*, 969 S.W.2d 788, 795 (Mo. Ct. App. 1998) (under federal law, an award may not be set aside for manifest disregard of the law unless the moving party can establish "that the arbitrators understood and correctly stated the law but proceeded to ignore it.").

¹⁶⁰ Only a few years ago, one writer stated: "[A]lthough the 'manifest disregard' of the law standard has been discussed in dozens of cases involving judicial review of arbitration awards resulting from securities disputes, no cases have been identified where a vacation of a securities arbitration award has been clearly upheld on appeal." Brad A. Galbraith, *Vacatur of Commercial Arbitration Awards in Federal Court: Contemplating the Use and Utility of the "Manifest Disregard" of the Law Standard*, 27 IND. L. REV. 241, 252 (1993). Although such cases are still rare, this statement could not be made today.

¹⁶¹ 128 F.3d 1456 (11th Cir. 1997).

¹⁶² *Id.* at 1459. *Montes* was the first case in which the Eleventh Circuit adopted the "manifest disregard" ground for vacating an arbitral award. The claimant had initiated the arbitration to recover overtime pay from her former employer, pursuant to section 207 of the Fair Labor Standards Act ("FLSA"), 29 U.S.C. §§ 201-219 (1994), which requires that covered employees receive overtime pay when they work more than 40 hours a week. The Shearson attorney argued to the arbitrators that "in this case the law is not right" and that the arbitrators were free to disregard the law and "do what is right and just and equitable." *Id.* at 1459. The Eleventh Circuit evidently found that the arbitrators had done just that. *Id.* at 1458-60.

¹⁶³ In *Cohig & Assoc., Inc. v. Stamm*, 149 F.3d 1190, No. 97-1119, 1998 WL 339472 (10th Cir. June 10, 1998) (unpublished decision), the court, in an unpublished opinion, refused to vacate an award in favor of a claimant under circumstances somewhat similar to those of *Montes*. The claimant, a 78-year-old retiree appearing pro se, stated in a written submission to the arbitrator that arbitration was not a legal action and requested that the arbitrator's decision "assure[s] the full responsibility towards the public and the good will and moral result." *Id.* at *6. The court held that the claimant was not asking the arbitrator to disregard the law but "was merely urging the arbitrator to consider the policy supporting his claim." *Id.* The court distinguished *Montes*: "In this case, neither the record nor the award indicates that the arbitrator viewed Mr. Stamm's innocuous statement as urging disregard of the law." *Id.*

The leading Second Circuit case before the *DiRussa* decision, *Merrill Lynch Pierce, Fenner & Smith, Inc. v. Bobker*,¹⁶⁴ defined the manifest disregard standard as follows:

The error must have been obvious and capable of being readily and instantly perceived by the average person qualified to serve as an arbitrator. Moreover, the term "disregard" implies that the arbitrator appreciates the existence of a clearly governing legal principle but decides to ignore or pay no attention to it To adopt a less strict standard of judicial review would be to undermine our well established deference to arbitration as a favored method of settling disputes when agreed to by the parties. Judicial inquiry under the "manifest disregard" standard is therefore extremely limited. The governing law alleged to have been ignored by the arbitrators must be well defined, explicit, and clearly applicable. We are not at liberty to set aside an arbitration panel's award because of an arguable difference regarding the meaning or applicability of laws urged upon it.¹⁶⁵

In *DiRussa*, the governing law that the arbitrators failed to apply met the stringent standard set forth in *Bobker*. The requirement of the ADEA that a successful party, such as *DiRussa*, be awarded attorney's fees was "well defined, explicit, and clearly applicable." However, the Second Circuit found that the arbitrators did not manifestly disregard the law "because there is no persuasive evidence that the arbitrators actually knew of—and intentionally disregarded—the mandatory aspect of the ADEA's fee provision."¹⁶⁶ Although *DiRussa's* attorney indicated several times dur-

¹⁶⁴ 808 F.2d 930 (2d Cir. 1986).

¹⁶⁵ *Id.* at 933-34; see also *Fahnestock & Co., Inc. v. Waltman*, 935 F.2d 512, 516 (2d Cir. 1991); *Carte Blanche (Singapore) Pte., Ltd. v. Carte Blanche Int'l, Ltd.*, 888 F.2d 260, 265 (2d Cir. 1989); *Advest, Inc. v. McCarthy*, 914 F.2d 6, 10 (1st Cir. 1990) ("In certain circumstances, the governing law may have such widespread familiarity, pristine clarity, and irrefutable applicability that a court could assume the arbitrators knew the rule and, notwithstanding, swept it under the rug. The case at bar, however, is not cut to so rare a pattern").

¹⁶⁶ *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818, 822 (2d Cir. 1997), cert. denied, 118 S. Ct. 695 (1998). In this regard, the district court stated:

I am not persuaded that the entitlement of an ADEA claimant to attorney's fees, which the statutory scheme provides by applying the FLSA to the ADEA, is 'capable of being readily and instantly perceived' by the average NASD securities industry arbitrator. . . . Plaintiff's counsel never argued to the arbitrators that an award of attorney's fees under the ADEA was mandatory.

DiRussa, 936 F. Supp. 104, 107 (S.D.N.Y. 1996).

A possible alternative basis for refusing to vacate the award might be that the arbitrators found that the respondents violated the New Jersey Law Against Discrimination, which does not require an award of attorneys' fees, but that they did not violate the ADEA. Since the arbitrators did not write an opinion, it is at least conceivable that this

ing the arbitration that he was "entitled" to attorney's fees under the ADEA (and the NJLAD),

at no point did DiRussa communicate . . . to the arbitrators that the ADEA mandated such an award to a prevailing party Nowhere [in DiRussa's brief to the arbitrators regarding attorney's fees] . . . does DiRussa either explain that the ADEA requires an award of attorney's fees or quote the language of the relevant ADEA section, which clearly communicates that principle.¹⁶⁷

Considering that the absence of formal pleading or evidentiary requirements is generally regarded to be one of the principal advantages of arbitration over litigation in court,¹⁶⁸ it is difficult to justify the fine distinction that the *DiRussa* court made between arguing to the arbitrators that the claimant is entitled to attorney's fees, on the one hand, and explaining to the arbitrators that the ADEA requires an award of attorney's fees, on the other. Presumably, if DiRussa's attorney had presented a copy of the ADEA to the arbitrators and pointed out to them the provision requiring an award of attorney's fees, the arbitrators' refusal to award the fees would have been manifest disregard of the law. However, the arbitrators' refusal to award fees after being told by DiRussa's attorney that he was entitled to them did not constitute manifest disregard. Such a fine distinction appears to be unduly formalistic. Although court proceedings have largely abandoned procedural and evidentiary formalism,¹⁶⁹ it appears, paradoxically, to survive, if not to flourish, in the supposedly more informal arbitration proceedings.¹⁷⁰

is what happened. Because the record of the case was sealed, it is impossible to know whether or not the respondents argued this theory before the court. In any event, neither the district court nor the appellate court mentioned this theory in their opinions.

¹⁶⁷ *DiRussa*, 121 F.3d at 823. In *DeGaetano v. Smith Barney, Inc.*, 983 F. Supp. 459 (S.D.N.Y. 1997), a case decided a few months after *DiRussa*, an employee of a brokerage firm prevailed in her arbitration claim of sexual harassment in violation of Title VII. As in *DiRussa*, the arbitration panel refused to award the claimant her attorney's fees, even though such an award to a prevailing plaintiff is mandatory under the Act. Distinguishing *DiRussa* on the ground that DeGaetano had brought the applicable law to the attention of the arbitrators, the district court held that the arbitrators had acted in manifest disregard of the law. *Id.* at 462-64.

¹⁶⁸ See *Allied-Bruce Terminix Cos. v. Dobson*, 115 S. Ct. 834 (1995) (quoting American Bar Association amicus brief which pointed out that one of the many advantages of arbitration over litigation is that it "can have simpler procedural and evidentiary rules").

¹⁶⁹ More than eighty years ago, Judge Benjamin Cardozo wrote: "The law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view today." *Wood v. Lucy, Lady Duff-Gordon*, 118 N.E. 214 (N.Y. 1917).

¹⁷⁰ Judge Selya of the First Circuit has pointed out that "securities arbitration . . . is

The consequence of allowing formalism to be introduced into arbitrations is likely to destroy the advantages of speed and economy that are the principal justifications for arbitration. If an attorney representing a client in an arbitration wishes to preserve the manifest disregard ground for review, he or she must be ever alert to the need to spell out every claim in detail and to cite to the arbitrators the text of every statute on which he or she is relying, even if this will prolong the proceedings and add to the parties' costs. A large premium is therefore placed on the skill and assiduousness of the lawyers. And what about a pro se claimant without legal skills or knowledge? If that claimant is himself unaware of the law, he or she of course cannot quote the relevant statute to the arbitrators, and the arbitrators therefore cannot manifestly disregard the law.¹⁷¹ However clear the law and its applicability to the case may be, the court is powerless to correct an arbitral error.

The manifest disregard of the law standard of review, as interpreted by the Second Circuit in *Bobker* and *DiRussa*, is based on an unstated premise of dubious validity: that arbitrators should maintain an attitude of passivity when hearing a case, and should sit back and consider only the testimony and documents that are brought to their attention. On the contrary, as I pointed out several years ago, if arbitration is to retain its special advantages over court proceedings, it is important that arbitrators take an active role at the hearing in ascertaining the relevant facts and the applicable law:

[A]rbitrators can maximize the unique benefits of arbitration, while preserving the fairness that is the goal of both arbitration and the legal process. Having observed a number of panels in action, I think the ones that operate most successfully are those whose members do not sit back passively and leave it to the opposing attorneys to run the show entirely. It is perhaps appropriate for a judge to take that stance, but not an arbitration panel.

The most effective panels take an active role throughout the proceedings. They ask searching questions of witnesses They cut through verbiage and legal technicalities and go right to the heart of the matter as quickly and efficiently as possible. Where appropriate, they use

coming to resemble the old tyranny, conventional adjudication" and that "[i]ncreasingly formalized procedural and evidentiary standards abound." Bruce M. Selya, *Arbitration Unbound?: The Legacy of McMahon*, 62 BROOK. L. REV. 1433, 1434, 1446 (1996).

¹⁷¹ Of course, a pro se claimant cannot claim an award of attorney's fees, but the manifest disregard ground for review potentially covers the disregard of any law.

and carefully consider the opinions and analysis of experts, but they don't allow long or unnecessary expositions of the obvious. In most cases, they reach a just result with a minimum of delay.¹⁷²

The *DiRussa* decision points in the opposite direction. It suggests that arbitrators are under no obligation to ascertain what the law is, even if a party argues that he or she has rights under a particular statute. In fact, it encourages arbitrators to be passive and even lazy, because the less they learn about the applicable law, the less likely it is that their award will be vacated or modified.

It is also questionable whether the *Bobker* and *DiRussa* courts' definition of the term "manifest disregard" is linguistically correct. "Disregard" does not only mean ignoring something that is brought to a person's attention. Used as a noun, "disregard" means the "lack of thoughtful attention or due regard,"¹⁷³ a definition that could well encompass the *DiRussa* arbitrators' failure to award attorney's fees after they had been told that *DiRussa* was entitled to them. "Manifest" means "clearly apparent to the sight or understanding; obvious."¹⁷⁴ Significantly, the Supreme Court's dictum in *Wilko*, which was the original source of the manifest disregard standard, does not identify the person to whom the disregard must be "manifest."¹⁷⁵ The *DiRussa* court assumed that the disregard must be manifest to the arbitration panel, but the language from *Wilko* quoted above suggests that it is not the arbitrators but the reviewing court to whom the disregard must be manifest. In other words, where the arbitrators failed to apply a federal statutory rule and their failure constituted clear error, as the Second Circuit conceded to be the case in *DiRussa*, a compelling argument can be made that the arbitrators acted in manifest disregard of the law.

The court's opinion in *Halligan* refers to a broader policy problem that is raised by the *DiRussa* court's narrow interpretation of the manifest disregard ground for vacatur.¹⁷⁶ Over the past two decades, the Supreme Court has repeatedly held that agreements to

¹⁷² Norman S. Poser, *The Proper Use of an Expert in Securities Arbitration*, Address at a Meeting of Arbitrators of the Nat'l Ass'n of Sec. Dealers (Oct. 16, 1991).

¹⁷³ THE AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE 538 (3d ed. 1992).

¹⁷⁴ *Id.* at 1093.

¹⁷⁵ See Kenneth R. Davis, *When Ignorance of the Law Is No Excuse: Judicial Review of Arbitration Awards*, 45 BUFF. L. REV. 49, 90-91 (1997) ("There is only one persuasive interpretation of 'manifest.' It denotes a clearly discernible error as opposed to one obscured by an unexplained award.")

¹⁷⁶ *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197, 203 (2d Cir. 1998).

arbitrate future disputes must be enforced, even though the dispute may involve the vindication of a party's rights under a federal statute. The Court has upheld agreements to arbitrate claims arising under the Sherman Act,¹⁷⁷ the Securities Exchange Act of 1934,¹⁷⁸ the Racketeer Influenced and Corrupt Organizations ("RICO") statute,¹⁷⁹ the Securities Act of 1933,¹⁸⁰ and the Age Discrimination in Employment Act.¹⁸¹ In each of these cases, the Court rigorously upheld the requirement of the FAA that agreements to arbitrate must be enforced to the same extent as other contracts.¹⁸² In cases where a conflict existed between this FAA policy and policies that favor judicial resolution of federally granted rights, the Court opted for the FAA and arbitration. If the parties had agreed to arbitrate a statutory claim, that agreement would be enforced to the same extent as any other arbitration agreement.

Each time the Supreme Court upheld an agreement to arbitrate a federal statutory claim, the Court stated an important corollary to its pro-arbitration holding, which was apparently intended to avoid the possibility that arbitrators might make decisions inconsistent with the provisions of federal law that were designed to protect certain categories of persons (e.g., investors in the case of the federal securities laws; older persons in the case of the ADEA). The Court stated that by agreeing to arbitrate the parties did not surrender their substantive rights under a federal statute. The arbitration agreement changed only the forum in which the dispute was to be heard; the substantive law governing the dispute remained the same, regardless of whether the dispute was tried before a court or a panel of arbitrators.¹⁸³ This apparently was how the Court at-

¹⁷⁷ *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985).

¹⁷⁸ *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987).

¹⁷⁹ *Id.*

¹⁸⁰ *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989).

¹⁸¹ *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991).

¹⁸² Section 2 of the FAA provides:

A written provision in . . . a contract evidencing a transaction involving [interstate or foreign] commerce to settle by arbitration a controversy thereafter arising out of such 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.

9 U.S.C. § 2 (1984).

¹⁸³ See, e.g., *Rodriguez de Quijas* 490 U.S. at 481 ("By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only

tempted to reconcile the potentially conflicting policies and requirements of the FAA, on the one hand, and of the particular federal regulatory statute, on the other. If, for example, an employee initiated an arbitration against his or her employer for violating a federal anti-discrimination statute, the arbitrators would be required to apply the same law to the dispute as a court would apply.¹⁸⁴ Thus, the claimant's rights would be vindicated, but the dispute would be resolved with all the advantages of economy, speed, privacy, and finality that arbitration is designed to provide.

This happy resolution of the competing policies of the FAA and the ADEA cannot be assured, however, if there is no effective judicial review of arbitrators' awards. The *DiRussa* court failed to confront this important issue; the *Halligan* court confronted the issue but tried unsuccessfully to force it into the Procrustean bed of manifest disregard of the law. A different standard of judicial review needs to be formulated in order to enable the courts to ensure that parties in arbitrations will not be deprived of fundamental rights.

VI. FORMULATING A NEW STANDARD OF JUDICIAL REVIEW

Every circuit court, with the exception of the Seventh Circuit, has supplemented the four statutory grounds of Section 10(a) of the FAA for vacating an arbitration award with a judicially created, non-statutory ground. Although the courts usually articulate the non-statutory ground as "manifest disregard of the law," some courts have applied other labels to it, either in combination with or as a substitute for the manifest disregard standard. Thus, courts have held that an arbitration award may be vacated if it violates public

submits to their resolution in an arbitral, rather than a judicial, forum.") (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985)).

¹⁸⁴ *Gilmer*, 500 U.S. at 26 (quoting *Mitsubishi Motors Corp.*, 473 U.S. at 628).

policy,¹⁸⁵ is completely irrational,¹⁸⁶ is arbitrary and capricious,¹⁸⁷ is fundamentally unfair,¹⁸⁸ is an abuse of discretion,¹⁸⁹ or does not "draw its essence" from the agreement to arbitrate.¹⁹⁰

Despite the deference that is normally given to arbitrators' awards, several courts have recognized that they must have the authority to overturn awards that are egregiously wrong. The framers of the FAA contemplated that the statute would enable business persons with comparable bargaining power to enforce arbitration clauses in commercial agreements, not that businesses would use it to require their customers and employees to arbitrate any future disputes, including disputes that might arise under federal regulatory or anti-discrimination statutes. Given the recent expansion of the FAA's scope, the Supreme Court has emphasized in *Gilmer* and other cases that when a party agrees to arbitrate a statutory claim, the party does not give up his or her substantive rights under the statute. Thus, the Court has suggested that a court reviewing an arbitration award must apply a standard of review that is broad enough to ensure vindication of statutory claims.

The *Halligan* decision, where the court, purporting to apply the manifest disregard standard, vacated an arbitration panel's award that went against the weight of the evidence is consistent with this view. Similarly, in the recent case of *Cole v. Burns Int'l. Sec. Serv., Inc.*,¹⁹¹ the District of Columbia Circuit expressly broadened the manifest disregard standard in statutory cases, holding that in such cases the court's review must be "sufficiently rigorous to ensure that arbitrators have properly interpreted and applied statutory law."¹⁹²

¹⁸⁵ *Rodriguez v. Prudential-Bache Sec., Inc.*, 882 F. Supp. 1202, 1208 (D.P.R. 1995) (citing *United Paper Workers' Int'l. Union, AFL-CIO v. Misco, Inc.*, 484 U.S. 29, 43 (1987)).

¹⁸⁶ *McLaughlin, Piven, Vogel, Inc. v. Gross*, 699 F. Supp. 55, 58 (E.D. Pa. 1988).

¹⁸⁷ *Brown v. Rauscher Pierce Refsnes, Inc.*, 994 F.2d 775, 779 (11th Cir. 1993).

¹⁸⁸ *Bowles Fin. Group, Inc. v. Stifel, Nicolaus & Co., Inc.*, 22 F.3d 1010, 1013 (10th Cir. 1994).

¹⁸⁹ *Jenkins v. Prudential-Bache Sec., Inc.*, 847 F.2d 631, 633-34 (10th Cir. 1988).

¹⁹⁰ *Michigan Mut. Ins. Co. v. Unigard Sec. Ins. Co.* 44 F.3d 826, 830-31 (9th Cir. 1995).

¹⁹¹ 105 F.3d 1465 (D.C. Cir. 1997).

¹⁹² *Id.* at 1487. In *Cole*, a Title VII case based on racial discrimination, the manifest disregard standard of review was a tangential issue. The plaintiff claimed his agreement to arbitrate was unenforceable because the arbitrator's rulings would not be subject to judicial review. *Id.* at 1486. In rejecting that argument, the court held that the manifest disregard standard, under the court's broadened interpretation, would adequately assure the plaintiff that his statutory rights would be protected. *Id.* at 1487.

Although both the *Halligan* and *Cole* courts ostensibly remain wedded to the manifest disregard standard, both courts have in fact adopted a new standard of review. In *Cole*, the District of Columbia Circuit stated that a modified manifest disregard standard would apply to statutory claims; in *Halligan*, the Second Circuit purported to be applying the traditional manifest disregard standard as interpreted by the Second Circuit in *Bobker* and *DiRussa* but instead applied a different standard *sub silentio*.¹⁹³

Halligan and *Cole* tell us that, regardless of whether arbitrators knew the law and disregarded it, an award will be vacated if the arbitrators deny a claimant statutory rights to which he or she is entitled. If this new standard of review had been applied in *DiRussa*, the Second Circuit would also have vacated the arbitrators' denial of DiRussa's attorneys' fees and would thus have prevented a shocking miscarriage of justice.

The courts should expressly adopt this broader standard of review for arbitrators' awards involving statutory claims. "Manifest disregard" is an unsatisfactory standard, the only justification for it being that the Supreme Court used the words in a dictum forty-five years ago, in a case that the Court subsequently overruled. Although the *Cole* redefinition of the standard of review was confined to "statutory cases in which an employee has been forced to resort to arbitration as a condition of employment,"¹⁹⁴ its broader scope of review should be extended to any claim based on a statute, whether or not signing an arbitration agreement was a condition of employment. This conclusion follows from several statements of the Supreme Court asserting that *non-employees* who bring claims under

¹⁹³ In *Chisolm v. Kidder, Peabody Asset Management, Inc.*, 966 F. Supp. 218 (S.D.N.Y. 1997), *aff'd*, No. 97-7828, 1998 WL 695041 (2d Cir. July 28, 1998) (unpublished opinion), the district court refused to vacate an arbitration award denying relief to a claimant under the ADEA. Although the court believed that the claimant "raises some important concerns regarding the adequacy of arbitration in this area," it stated that "Second Circuit precedent compels the conclusion that the standard of judicial review of arbitral decisions in cases involving statutory rights is no different from the extremely limited review used in arbitration generally." *Id.* at 219; see *Appellate Court Vacates Arbitration Award Citing Manifest Disregard*, 25 SEC. WEEK, NO. 29, at 4 (July 20, 1998).

¹⁹⁴ 105 F.3d at 1487.

the antitrust laws,¹⁹⁵ the securities laws,¹⁹⁶ and other statutes should not be deprived of their statutory rights because they have agreed to arbitrate their claims.

Furthermore, there are powerful reasons why the manifest disregard standard should be replaced by a broader standard for review of any arbitration award, whether or not based on a statutory claim. Because the manifest disregard standard protects an arbitral award from vacatur if the arbitrators did not know the law, it encourages arbitrators *not* to find out what the law is and at the same time penalizes parties who fail to bring the law to the arbitrators' attention, either because of the inexperience of, or an error by, counsel or because a party is acting *pro se*. Arbitrators should not be potted palms.¹⁹⁷ As decision-makers, they have an obligation to ascertain what the law is and to apply it correctly. This is true generally, but it is most important when the dispute is not between roughly equal commercial entities but between parties that are unequal in wealth and sophistication.¹⁹⁸

This conclusion does not ignore the strong policy in favor of the finality of arbitrations. An arbitral award should not be subject to the same standard of judicial review as that applied to a jury verdict or the trial court's judgment. The difficulty is how to formulate a standard of review of arbitral awards that reconciles the sometimes opposing policies of finality and justice. The federal courts have provided some guidance here, when they have articulated a non-statutory standard of review in such terms as irrationality, arbi-

¹⁹⁵ *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985).

¹⁹⁶ *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 481 (1989).

¹⁹⁷ Credit for this metaphor must be given to Brendan Sullivan, attorney for Oliver North in the televised Iran-Contra hearings of the 1980s.

¹⁹⁸ Professor Galanter has pointed out that the legal system favors the "haves" over the "have-nots," largely because the "haves" tend to be "repeat players" ("RP") who use the legal system frequently, whereas the "have-nots" tend to be "one-shotters" ("OS") who use the system only once or infrequently. Marc Galanter, *Why the "Haves" Come out Ahead: Speculations on the Limits of Legal Change*, 9 L. & SOC'Y REV. 95, 124 (1974). As a result, the "haves" enjoy "layers of advantages . . . which interlock, reinforcing and shielding one another." *Id.* Under Professor Galanter's formulation, a broker-dealer firm is likely to be an RP, while its employee is most likely an OS.

trariness, capriciousness, and fundamental unfairness. Perhaps the best articulation of such a standard was given by Chief Justice Ellen Peters of the Connecticut Supreme Court:

[T]he "manifest disregard of the law" ground for vacating an arbitration award is narrow and should be reserved for circumstances of an arbitrator's extraordinary lack of fidelity to established legal principles.

So delimited, the principle of vacating an award because of a manifest disregard of the law is an important safeguard of the integrity of alternate dispute resolution mechanisms. Judicial approval of arbitration decisions that so egregiously depart from established law that they border on the irrational would undermine society's confidence in the legitimacy of the arbitration process Furthermore, although the discretion conferred on the arbitrator by the contracting parties is exceedingly broad, modern contract principles of good faith and fair dealing recognize that even contractual discretion must be exercised for purposes reasonably within the contemplation of the contracting parties.¹⁹⁹

Although Judge Peters formulated her standard of review within the general framework of manifest disregard of the law, it is evident that she, like the *Halligan* court, was actually applying a different standard: extraordinary lack of fidelity to established legal principles; egregious departure from established law. This seems to be an appropriate standard of judicial review of arbitration awards for non-statutory as well as statutory cases. It ties the validity of arbitration awards to the legitimate expectations of both the parties and the public. Moreover, it does not permit an erroneous award to be confirmed simply because the losing party, or his or her attorney, failed to dot all his "i's" or cross all his "t's," or because the arbitrators did not have the capacity or the assiduousness to ascertain and apply the correct law.

Under the standard of review proposed here, the claimant in *DiRussa* would prevail. The arbitrators' failure to apply a totally clear, mandatory requirement of a federal statute that is designed to protect a disadvantaged class of persons constitutes an egregious departure from established law. Whether the claimant in *Halligan* would prevail under this standard is less certain, if only because the Second Circuit's opinion did not make clear its basis for vacating the award. If the reviewing court found that the arbitrators' denial of relief to the claimant was not simply erroneous but arbitrary or irrational, the award should be vacated.

¹⁹⁹ *Garrity v. McCaskey*, 612 A.2d 742, 747-48 (Conn. 1992) (emphasis added).

As Judge Peters suggests in the passage quoted above, the proposed standard of review is based, at least in part, on contractual grounds. Thus, it is consistent with the broad purpose of the FAA, namely, to make agreements to arbitrate as enforceable as other contracts. Arbitration is a creature of agreement, and, unless the parties to an arbitration expressly agreed that the arbitrators were not to be bound by established legal principles, it can be assumed that the parties did not intend that the arbitrators would decide any dispute between them in an arbitrary or irrational manner.

CONCLUSION

DiRussa and *Halligan* demonstrate, each in its own way, that the manifest disregard of the law standard of review of arbitration awards is inadequate and unsatisfactory. In *DiRussa*, strict adherence to the manifest disregard standard deprived the claimant of his statutory rights. In *Halligan*, the Second Circuit tacitly ignored the standard in order to allow the claimant to receive his statutory rights. The manifest disregard standard, as the Second Circuit has interpreted it in the past, requires a court to confirm an arbitration award despite the fact that such award is inconsistent with a federal statute, unless (1) the law and its applicability to the case are totally clear, and (2) the arbitrators understood the law but chose to disregard it. In arbitrations of statutory claims, the manifest disregard standard violates the precept announced by the Supreme Court when it declared that agreements to arbitrate statutory, including discrimination, claims were enforceable: "By agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum."²⁰⁰ By immunizing erroneous arbitral awards from vacatur unless the arbitrators are aware of their error, the manifest disregard standard brings the arbitration process into disrepute. It discourages arbitrators from assiduously ascertaining the correct law. Less capable and lazy arbitrators, who are unable or unwilling to discern the law, are less likely to have their decisions overturned than are those who are diligent. At the same time, the manifest disregard standard encourages lengthy arbitration proceedings, since an attorney cannot risk failing to provide the arbitrators

²⁰⁰ *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26 (1991) (quoting *Mitsubishi*, 473 U.S. at 628).

with every statutory provision, judicial decision, and administrative ruling that may have possible relevance. Thus, the manifest disregard standard not only introduces an unwelcome formalism into arbitration proceedings, but it unduly penalizes the pro se claimant and the claimant whose attorney is inexperienced or fails in his or her diligence.

The courts are beginning to reject manifest disregard as the proper standard of review in favor of a broader standard of review of arbitration awards. *Halligan* is an example of such a case, although Judge Feinberg purported to be applying the standard. It is time for the courts to frankly recognize, as the District of Columbia did in *Cole*, that the standard of review of arbitration awards in statutory cases should be broad enough to ensure the vindication of statutory rights. It should also be recognized that manifest disregard, as interpreted by the lower federal courts since it was first mentioned by the Supreme Court in dictum more than forty-five years ago, is an inadequate standard of review even in non-statutory cases. Under this standard, an error, no matter how serious, cannot be corrected if the arbitrators were not aware of it when they made their decision.

Judicial review of arbitration awards must be sufficient at least to require arbitrators to follow the general outlines of the law. An award should be vacated or modified if it shows an extraordinary lack of fidelity to established legal principles or an egregious departure from established law. This is a workable standard that represents an acceptable balance between the finality that is an important goal of arbitration and the accuracy and fairness that are fundamental to the rule of law.