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NOTE

PUNITIVE DAMAGES AS A REMEDY FOR DISCRIMINATION CLAIM ARBITRATIONS IN THE SECURITIES INDUSTRY

I. INTRODUCTION

In the securities industry, registered representatives—employees of broker-dealers who are licensed to execute securities transactions—must meet certain qualifications set by law or regulation before transacting business with a firm’s customers or selling securities to the public. To become a registered representative, a person must pass the Series 7 and Series 63 exams and register with an exchange, such as the New York Stock Exchange (“NYSE”), or with a Self-Regulatory Organization (“SRO”), such as the National Assoca-

1. A registered representative is an employee engaged in the solicitation or handling of accounts or orders for the purchase or sale of securities, or other similar instruments for the accounts of customers of his employer or in the solicitation or handling of business in connection with investment advisory or investment management services furnished on a fee basis by his employer. NEW YORK STOCK EXCHANGE, NEW YORK STOCK EXCHANGE GUIDE 2526 (1989).

2. A broker-dealer is “[a] securities brokerage firm, usually registered with the S.E.C. and with the state in which it does business, engaging in the business of buying and selling securities to or for customers.” BLACK’S LAW DICTIONARY 193 (6th ed. 1990). Merrill Lynch, Goldman Sachs, Bear Stearns, Dean Witter, Prudential Securities, Morgan Stanley, Paine Webber, J.P. Morgan, and Citibank are just a few examples of large, well known broker-dealers.

3. Black’s defines a registered representative as “[a] person who has met the qualifications set by law or regulations (of e.g. the SEC or the New York Stock Exchange) to sell securities to the public.” Id. at 1283.

4. A series 7 exam is the Full Registration/General Securities Representative exam. To pass the exam, one must have a basic understanding of the securities markets as well as the debt and equity instruments traded. Series 63 is the Uniform Securities Agent State Law Exam, which is commonly known as the Blue Sky exam. It allows registered representatives to transact business in other states besides their state of registration. In addition, specialty exams are given for Commodity Futures, Registered Options Principals, Branch Managers, and General Securities Principals, just to list a few. See FORM U-4, UNIFORM APPLICATION FOR SECURITIES INDUSTRY REGISTRATION OR TRANSFER (1991) [hereinafter FORM U-4].
ution of Securities Dealers ("NASD"). In addition, to apply for registration for the first time, or after an individual has filed and changes employment or association from one broker-dealer to another, he or she must file a U-4 form, the Uniform Application for Securities Industry Registration or Transfer.

The U-4 form is needed to keep a registered representative’s license current with the securities exchanges and with SROs through the Central Registration Depository. Disputes arise between firms and registered representatives involving a variety of subjects including: compensation, responsibility for customer losses, right to work product, enforceability of agreements not to compete, unjust termination, sexual harassment and discrimination. By signing the U-4 form, which is mandatory, the employee agrees to arbitrate all disputes which might arise through the general arbitration clause. The clause states:

I agree to arbitrate any dispute, claim or controversy that may arise between me and my firm, or a customer, or any other person, that is required to be arbitrated under the rules, constitutions, or by-laws of the organizations indicated in Item 10 as may be amended from time to time and that any arbitration award rendered against me may be entered as a judgement [sic] in any court of competent jurisdiction.

This type of general arbitration clause, which states that the parties agree to arbitrate “all disputes,” results in the forced arbitration of age, race and sex discrimination claims. However, a prob-

5. Registration can be with the American Stock Exchange, the Boston Stock Exchange, the Chicago Board Options Exchange, the Cincinnati Stock Exchange, the Midwest Stock Exchange, the National Association of Securities Dealers, the New York Stock Exchange, the Pacific Stock Exchange, or the Philadelphia Stock Exchange. Id.

6. How To Use Form U-4, in FORM U-4, supra note 4.

7. Id.


PUNITIVE DAMAGES

A discrimination claim is brought under a federal, state or local statute which allows for the recovery of punitive damages because the authority of arbitration panels to award punitive damages is still not a settled issue.11

While arbitration is recognized as a relatively efficient alternative to litigation,12 in this situation it may not provide adequate relief for the victims of discrimination. It is important for such victims to be able to recover punitive damages. By pursuing discrimination claims, victims seek not only liquidated and legal damages, such as lost wages, benefits, and pension rights; compensatory damages, such as pain, suffering, humiliation, mental or emotional distress; but they also seek punitive damages to deter their companies from engaging in such employment practices in the future.13 In order to achieve these goals, punitive damages must be an available remedy for arbitration panels. Not only would such awards be available to the victims in a judicial forum, but they would be able to argue their case to a jury that would likely be more sympathetic than an arbitration panel made up of industry insiders.14

11. For example, both the Civil Rights Act of 1991 and the New York City Human Rights Law provide for punitive damages as a remedy. 42 U.S.C. § 1981(a) (Supp. 1993); NEW YORK CITY, N.Y., ADMIN. CODE § 8-502 (1992). The Courts of Appeals for the 1st, 8th, 9th and 11th Circuits have held that arbitrators may award punitive damages based on broad arbitration clauses. See, e.g., Lee v. Chica, 983 F.2d 883 (8th Cir. 1993); Todd Shipyards Corp. v. Cunard Line, Ltd., 943 F.2d 1056 (9th Cir. 1991); Raytheon Co. v. Automated Bus. Sys., Inc., 882 F.2d 6 (1st Cir. 1989); Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378 (11th Cir. 1988). However, the Second Circuit, relying on New York State law, holds that arbitration panels cannot award punitive damages. See Fahnestock & Co., Inc. v. Waltman, 935 F.2d 512 (2d Cir. 1991). Under the Age Discrimination in Employment Act ("ADEA"), victims may recover lost wages, benefits, and pension rights, but compensatory damages such as pain, suffering, humiliation, mental or emotional distress, as well as punitive damages are not recoverable in ADEA actions. 29 U.S.C. §§ 621-634 (1993); see, e.g., Fellows v. Medford Corp., 431 F. Supp. 199 (D. Or. 1977).


13. See, e.g., Fellows, 431 F. Supp. at 201-02 (plaintiff allowed to recover lost wages, benefits, and pension rights under ADEA action but denied recovery for pain, suffering, humiliation, mental or emotional distress).

14. [In all arbitration matters between or among members and/or persons associated with members . . . the Director of Arbitration shall appoint a single arbitrator to decide the matter in controversy. The arbitrator chosen shall be from the securities industry. Upon the request of a party in its initial filing or the arbitrator, the Director of Arbitration shall appoint a panel of three (3) arbitrators, all of whom shall be from the securities industry.

This Note will examine the authority of arbitration panels in the securities industry to award punitive damages within the context of mandatory arbitrated discrimination claims. The positive and negative implications of granting arbitrators the power to award punitive damages will be evaluated. Federal law regarding the arbitrability of discrimination claims and the awarding of punitive damages will be examined. The strong federal policy towards enforcing arbitration agreements will be discussed as well as the policy of granting arbitration panels broad authority to award any remedy necessary, including punitive damages.

In addition, the state of the law in New York will be evaluated. Specifically, *Garrity v. Lyle Stuart, Inc.*, which established the New York rule that arbitrators have no power to award punitive damages, will be critiqued. Cases which expressly reject the rule will also be discussed.

The crux of the problem is that although a majority of Circuits allow punitive damages to be awarded by arbitrators, the Second Circuit applies New York Law and refuses to grant arbitrators such authority. This split between the Circuits over whether arbitrators have the authority to award punitive damages will be analyzed. Finally, this Note will end with proposed changes for the courts and the state and federal legislatures to expressly grant the authority to arbitrators to award punitive damages for discrimination claims.

II. ARBITRATION AND PUNITIVE DAMAGES IN GENERAL

A. Arbitration

Currently, arbitration, the most popular form of alternative dispute resolution used to replace plenary civil litigation, is flourishing under favorable federal and state legislation. It offers a relatively efficient alternative to lawsuits for resolving disputes between securities dealers and their employees. Although “[t]he viability of arbitration hinge[s] on the ability of [the] arbitrators to consider . . . ‘all disputes’ which [could] arise under the agreement, and their authority

16. Other forms of alternative dispute resolution include mediation, negotiation, med-arb (mediation and arbitration) and mini-trials.
18. See McGowan, supra note 12, at 110 (analysis of arbitration with regard to disputes between customers and broker-dealers).
to deal fairly and flexibly with the circumstances presented,“ it still remains a cost-effective alternative to plenary litigation. However, it should be noted that “if arbitrators cannot handle all disputes arising under the agreement (including claims for punitive damages)” efficiency may decrease and expenses increase “because litigants will be forced into the trial court[s] to resolve the remaining disputes.” Discrimination victims could be forced to undergo multiple adjudications or be denied the chance to recover punitive damages in any forum.

Plaintiffs could be barred from bringing suit in other forums for several reasons. Often an agreement to arbitrate is interpreted as a waiver of the right to seek punitive relief in any other forum. Also, a party may invoke collateral estoppel if the facts the plaintiff attempts to assert in litigation are identical to the facts which were previously arbitrated. And finally, if a claimant attempts to raise a new theory which could have been raised in arbitration, res judicata may be applied to bar the claim.

In 1925, Congress enacted the Federal Arbitration Act (“FAA”) and “formally recognized arbitration as a valid alternative to judicial dispute resolution.” The FAA established a federal policy favoring arbitration and required courts to rigorously enforce arbitration agreements. The purpose of the FAA was “to reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American

21. See Stipanowich, supra note 17, at 1011.
22. Id. at 963. Under the Garrity doctrine, courts have concluded that an arbitration clause waives a party’s right to seek punitive relief in another forum. However, some courts have declined to follow this doctrine. Id.
24. Id. at 541. However, it should be noted that “a court is not obligated to give res judicata effect to an arbitration proceeding, especially where it is unclear whether the arbitrators would have been able to grant the relief in question.” Id. at 542 (construing Blumenthal v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 910 F.2d 1049 (2d Cir. 1990)).
courts, and to place arbitration agreements upon the same footing as other contracts.\textsuperscript{28} While it is clear the Supreme Court intended that arbitration agreements should be enforced to resolve employment disputes in the securities industry,\textsuperscript{29} this favoring of arbitration as an alternative dispute resolution method should not be interpreted as evidence of the Court's willingness to limit the relief available to victims of employment discrimination. Since Congress has explicitly stated that victims of employment discrimination are entitled to punitive damages,\textsuperscript{30} courts should only enforce arbitration agreements if such damages are an available remedy.

\section*{B. Punitive Damages}

Punitive damages provide a civil source of public retribution and are designed to punish the wrongdoer and to deter the wrongdoer and others from repeating the same offense.\textsuperscript{31} In addition, "[p]unitive damages also provide an incentive to wronged parties to pursue causes of action where tangible harm and resulting damages are nominal but where the defendant's behavior subjects society to substantial risks."\textsuperscript{32} The Civil Rights Law of 1991, which specifically authorizes punitive damages as a remedy for discrimination claims under Title VII, is evidence of Congressional intent to discourage discriminatory employment practices.\textsuperscript{33}

Punitive damages are awarded as a means of deterring both the actual defendant (specific deterrence) and others (general deterrence) from committing similar acts.\textsuperscript{34} Specifically in discrimination cases, punitive damages should be used as a deterrent for future conduct of defendants. Unfortunately, if such damages are not an available remedy, the party in the lower bargaining position (in employment dis-

\begin{footnotes}
\item[29] See, e.g., id.
\item[31] Punitive damages "[u]nlike compensatory or actual damages... are based upon an entirely different public policy consideration—that of punishing the defendant or of setting an example for similar wrongdoers." BLACK'S LAW DICTIONARY 390 (6th ed. 1990); see also Stipanowich, supra note 17, at 955 (discussion of importance of punitive damages); James Hadden, Note, The Authority of Arbitrators to Award Punitive Damages: Raytheon Co. v. Automated Business Systems, 7 OHIO ST. J. ON DISP. RESOL. 337, 338 (1992).
\item[32] Stipanowich, supra note 17, at 956.
\item[34] Hadden, supra note 31, at 343.
\end{footnotes}
PUNITIVE DAMAGES

criminal cases this is almost always the employee) will not be able to prevent an employer's discriminatory practices. In addition, punitive damages "punish the culpable party and deter similar conduct in the future" while helping the victim to defray the expenses of arbitration.35

In formulating remedies, arbitrators need flexibility to deal with a variety of situations "including contingencies not contemplated by the drafters of the contract."36 In addition, since arbitrators are "often confronted with situations which the parties did not or could not anticipate, [their] remedy need not be specifically authorized by the agreement, but may be derived from the nature of the problem presented."37 Employees who sign the U-4 form probably do not anticipate employment discrimination, nor do they realize that the general arbitration provision means that they have agreed to arbitrate such a claim if it arises. Securities brokerage firms, however, are not currently required to disclose or explain to employees the implications of the standard arbitration clause included in the U-4 form, which is signed when registering with that firm.38 Employers, on the other hand, are aware that punitive damages are a statutory remedy and should not be able to avoid such possible sanctions by enforcing arbitration agreements.39

The recent due process challenges to punitive damage awards and general concern that punitive damages are out of control, demonstrates that the availability of punitive damages in arbitration is an issue of great interest.40 In addition, the limited judicial review of the amount of arbitration awards focuses attention on an arbitration panel's authority to award punitive damages.41 To deny arbitrators the authority to award punitive damages would be to declare, as a matter of public policy, that punitive damages are inappropriate for arbitration. This would conflict with the legislative and judicial policy favoring broad enforcement of arbitration clauses.42

35. Id. at 349.
36. See Stipanowich, supra note 17, at 979.
37. Id.
38. See, e.g., Bender v. Smith Barney, Harris Upham & Co., Inc., 789 F. Supp. 155, 159 (D.N.J. 1992) (holding there is no duty to explain the existence or scope of the U-4 form arbitration clause).
40. See Neesemann, supra note 23, at 575.
41. Id. at 576.
42. See Stipanowich, supra note 17, at 988.
Courts are often concerned with the potential manipulation of the arbitration panels by the party in the superior bargaining position.\textsuperscript{43} However, in the situation where an employee is suing his or her employer for discrimination, the party in the superior bargaining position is most likely to be the employer, or member firm. Therefore, the fear that “potential abuse would reduce confidence in the arbitration process” is not applicable to the employee/employer dispute because the employee will most likely not be in a position to manipulate the arbitration panel.\textsuperscript{44}

The unavailability of punitive damages in arbitration may become a strategic factor for parties who must choose between the arbitration method of dispute resolution and formal litigation.\textsuperscript{45} Many employers are fearful that juries will award large settlements in discrimination cases.\textsuperscript{46} An employer who faces the chance of a jury awarding punitive damages will likely instead enforce the arbitration agreement, especially in states like New York where arbitration panels do not have the authority to award punitive damages. This means that in some jurisdictions, by signing a U-4 form, an employee is in effect waiving his or her right to claim punitive damages.

However, it should be noted that a waiver is a voluntary and intentional relinquishment of a known right and by simply signing an ambiguous, mandatory agreement, employees may not have intended to relinquish their right to punitive damages.\textsuperscript{47}

One criticism of punitive damage awards by arbitration panels is the lack of judicial review. Although state laws often provide elaborate criteria for court awarded punitive damages, including the threshold levels of proof required and appellate review, few states impose any limitations on arbitration panel awards.\textsuperscript{48} The result is that arbi-

\textsuperscript{43} The \textit{Garrity} court was concerned that the party in the superior bargaining position would be able to manipulate or restrict the selection of the arbitration panel which by awarding punitive damages “displaces the court and the jury, and therefore the State, as the engine for imposing a social sanction.” Garrity v. Lyle Stuart, Inc., 353 N.E.2d 793, 796 (N.Y. 1976).

\textsuperscript{44} Hadden, supra note 31, at 343-44.

\textsuperscript{45} Id.


\textsuperscript{47} Since the U-4 form is silent and the rules, constitutions and by-laws of the regulatory organizations are ambiguous with regards to punitive damage awards, the waiver could not have been voluntary. See, e.g., Mark Weibel, \textit{Federal Securities Arbitration: Does It Provide Adequate Relief?}, 48 ARB. J., Mar 1993, at 60 (discussing customers not voluntarily relinquishing their rights by signing ambiguous agreements).

\textsuperscript{48} See, e.g., J. Stratton Shartel, \textit{Protections Are Needed Against Unchecked Punitive
PUNITIVE DAMAGES

The overturning of punitive damage awards given by arbitration panels is typically limited to situations where it can be demonstrated that the arbitrators were corrupt, or there has been a “manifest disregard of the law” or “substantial prejudice” to an aggrieved respondent.

III. FEDERAL LAW

The FAA requires federal courts to refer to arbitration all claims arising out of contracts containing a valid arbitration clause. By enacting the FAA, Congress intended to create a federal law which would unequivocally uphold agreements to arbitrate, and to “establish a public policy favoring arbitration and the enforceability of arbitration agreements.”

In accordance with the federal policy favoring arbitration, courts have held that the arbitration agreement provision within the U-4 form is governed by the FAA. In addition, courts, deferring to the perceived intent of Congress to encourage arbitration, have gradually expanded the role of arbitration in resolving disputes by holding that statutory claims may be the subject of an enforceable arbitration agreement.

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49. Id.


[a] written provision in ... a contract evidencing a transaction involving 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.

Id. (emphasis added).

52. See Weibel, supra note 47, at 56.


54. See Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 38 (1991); see also Ro-
FAA mandates that parties proceed to arbitration on all matters within the scope of their agreements, courts have held that statutory claims, such as race, sex, and age discrimination claims, can be compelled to go to arbitration under the general arbitration provision contained in form U-4.55

The use of arbitration as a dispute resolution technique typically arises from a general arbitration clause (similar to the arbitration provision included in form U-4) in a commercial contract which states that the parties agree to resolve "all disputes" through arbitration.56 In October, 1993, the NASD amended its Code of Arbitration Procedure to expressly provide that employment discrimination claims are eligible for submission to arbitration.57 The result is that the general arbitration provision now mandates the submission of discrimination claims to arbitration.

In *Gilmer v. Interstate/Johnson Lane Corp.*,58 the Supreme Court explained its reasoning for determining that arbitration clauses were enforceable in disputes involving employment discrimination.59 While admitting that all statutory claims may not be appropriate for arbitration, the Supreme Court held that once having bargained for arbitration of disputes, parties should be held to their agreements unless Congress has "evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue."60 In *Gilmer*, a case questioning the forced arbitration of an age discrimination claim under the Age Discrimination in Employment Act ("ADEA"), the court held that the plaintiff failed to establish that anything in the text

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55. See, e.g., *Gilmer*, 520 U.S. 20 (compelled arbitration of age discrimination claim); *Fletcher*, 619 N.E.2d 998 (compelled arbitration of race discrimination claim); *Reid v. Goldman, Sachs & Co.*, 590 N.Y.S.2d 497 (App. Div. 1992) (holding that registered representative, who was required to sign a U-4 form as a condition of employment, was compelled to arbitrate a state-based sex discrimination claim under the FAA).


57. According to the amended Code, arbitration is required for "any dispute, claim or controversy arising out of or in connection with the business of any member of the Association, or arising out of the employment or termination of employment of associated person(s) with any member . . . ." *NATIONAL ASS'N OF SEC. DEALERS, CODE OF ARBITRATION PROCEDURE § 1* (1993).


59. *Id.* at 26.

60. *Id.* (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985)).
of ADEA, or its legislative history, explicitly precluded arbitration. 61

While Congress may not have expressly excluded Title VII discrimina-
tion claims from arbitration, it is clear that by explicitly pro-
viding for punitive damages, such a remedy was necessary to insure
compliance with the statute. 62 Following the Gilmer Court's analysis
and conclusions, several courts have held that the arbitration provision
in the U-4 form compels the arbitration of Title VII claims. 63 Be-
cause courts have determined that Title VII claims are arbitrable, and
because Congress expressly provided for punitive damages, it follows
that the courts should infer that Congress must have intended that
arbitration panels have the authority to award punitive damages. This
conclusion has been reached by the First, Eighth, Ninth, and Eleventh
Circuits. 64

The power of arbitrators to award punitive damages is supported
by the federal policy in favor of a broad view of arbitrability. 65 The
Second Circuit, however, by applying New York law which prohibits
arbitration panels from awarding punitive damages, counters the Con-
gressional objective of preventing employment discrimination. 66

By relying on state law, the Second Circuit has rejected the clear
precedent of the First and Eleventh Circuits and has instead prohibit-
ed arbitrators from awarding punitive damages when the parties have
agreed that New York law shall govern the dispute. 67 Hence, the

61. Id. at 27.
62. "[T]he complaining party may recover compensatory and punitive damages." 42
63. See e.g., Bierdeman v. Shearson Lehman Hutton, Inc., 963 F.2d 378 (9th Cir. 1992);
Willis v. Dean Witter Reynolds, Inc., 948 F.2d 305 (6th Cir. 1991); Bender v. Smith Barney,
Title VII claims is not contrary to public policy).
64. See, e.g., Lee v. Chica, 983 F.2d 883 (8th Cir. 1993) (holding that under federal
law arbitrators had authority to award punitive damages to clients who had claimed against
securities firm and its agent); Todd Shipyards Corp. v. Cunard Line, Ltd., 943 F.2d 1056
(9th Cir. 1991) (finding arbitration panel had authority to award punitive damages in case
involving maritime breach of contract); Raytheon Co. v. Automated Bus. Sys., Inc., 882 F.2d
6 (1st Cir. 1989) (finding agreement to arbitrate between manufacturer and dealer empowered
arbitrators to award punitive damages); Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378
(11th Cir. 1988) (holding arbitrators had power to award punitive damages in favor of inves-
tor in dispute with securities broker).
65. Todd Shipyards Corp., 943 F.2d at 1063.
66. See Garrity v. Lyle Stuart, Inc., 353 N.E.2d 793 (N.Y. 1976); see also Barbier v.
Shearson Lehman Hutton, Inc., 948 F.2d 117 (2d Cir. 1991) (finding arbitrators exceeded
their authority in awarding punitive damages where parties choose New York law);
Fahnestock & Co., Inc. v. Waldman, 935 F.2d 512 (2d Cir. 1991) (holding punitive damages
portion of award was properly vacated pursuant to New York public policy precluding arbi-
trator from awarding punitive damages).
67. The Second Circuit determined that New York substantive law controlled the author-
Second Circuit's decision "has created a schism among the circuit courts where there was previous uniformity."  

Such a rule, which enforces an arbitration clause but at the same time prohibits arbitrators from considering punitive damages claims, frustrates the policies underlying and purposes served by punitive damages. Courts should be able to avoid enforcing an arbitration agreement if enforcement would provide automatic immunity from punishment and encourage intentional wrongdoing by protecting employers who practice discrimination from possibly having to pay punitive damages. Arbitration agreements should be unenforceable where substantive rights, embodied by an anti-discrimination statute, such as the Civil Rights Act of 1991, express a strong public policy which must be judicially enforced. Although the securities industry has argued that the presence of heavy securities regulation should exempt the industry from punitive sanctions in arbitration, the securities industry cannot thereby exempt itself from complying with federal anti-discrimination laws and continue unlawful practices with immunity.

However, denying a motion to compel arbitration when an employee claims punitive damages may not be a viable solution because it disregards the congressional intent of the FAA. The FAA clearly requires that arbitration clauses be read broadly and arbitration not be denied in the absence of clear and express exclusions. But depriving arbitral panels of the authority to impose punitive sanctions on defendants guilty of outrageous and intentional wrongdoing will, in effect, render such behavior unpunishable through arbitration.

IV. NEW YORK LAW

Modifying its own body of case law to comply with the Gilmer
decision, New York abandoned the precedent set by *Wertheim & Co. v. Halpert.* In *Wertheim,* the New York Court of Appeals held that the arbitration of an employment discrimination dispute was not enforceable under the arbitration clause included in the U-4 form on the grounds that an employer should not be able to force an employee to arbitrate a dispute which involved important public policies. Subsequently, the New York Court of Appeals, in *Fletcher v. Kidder, Peabody & Co.,* held that in light of the *Gilmer* decision, *Wertheim* should no longer be followed. Rather the court held that “the arbitrability of statutory discrimination claims is henceforth to be determined by reference to Congress’ intent with regard to alternative dispute resolution of that class of claims.”

In accordance with *Gilmer,* the consolidated litigations of a race discrimination case and a gender-based discrimination case which arose under Title VII of the Civil Rights Law required the plaintiffs to establish the existence of a congressional intent to override the general rule that anticipatory contracts to arbitrate are enforceable under the FAA. Although the legislative history of Title VII and its recent amendments “does not demonstrate that Congress affirmatively intended to authorize anticipatory agreements to arbitrate claims arising from the statute’s provisions,” there is nothing in the legislation’s language or history to indicate a congressional intent to foreclose the arbitration of race- and gender-discrimination claims.

Although New York compels such employment discrimination cases to go to arbitration, New York does not allow arbitration panels to award punitive damages. Since 1976, in the seminal case of *Garrity v. Lyle Stuart, Inc.,* New York courts have held that determination of punitive damages is best left to the judiciary, thereby restricting an arbitrator’s authority. The *Garrity* Court held that

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76. 397 N.E.2d at 387.
77. 619 N.E.2d 998 (N.Y. 1993).
78. Id. at 1000.
79. *Fletcher* was the consolidation of two discrimination actions, *Fletcher v. Kidder, Peabody & Co.,* which involved racial discrimination and *Reid v. Goldman, Sachs & Co.,* which involved gender-based discrimination. Id. at 1002.
80. Id. at 1003.
although arbitrators are generally free to fashion a remedy commensurate with the wrong, arbitrators have no power to award punitive damages, even if expressly agreed upon by the parties. Hence, under the Garrity rule, arbitrators acting pursuant to the law of New York may not award punitive damages. Basing its holding almost exclusively on public policy, the Garrity Court viewed punitive damages as a social exemplary remedy and, as such, punishable only by the state, as opposed to private individuals acting through the courts. The Garrity Court "based its belief on two factors: (1) that punitive damages would undermine the ongoing contractual relationship between parties, and (2) that granting such broad and unreviewable power to arbitrators in the form of punitive damages might make arbitration a "trap for the unwary.""

However, in the context of employment discrimination claims within the securities industry, these factors are not applicable. The ongoing contractual relationship between the parties is no longer a factor because, in most situations, once an employee has filed a complaint against his or her employer for discrimination, the employee/employer relationship is severed. In addition, the fear that "an award of punitive damages is unpredictable and uncontrollable because arbitrators follow no practical guidelines" and hence became a "trap for the unwary," is unwarranted. Securities brokerage firms should not be considered helpless in these situations because, as the employer, they are usually in the position of superior bargaining power and therefore maintain "influence over the arbitral process.""\textsuperscript{88}

A strict interpretation of the Garrity doctrine "would require aggrieved parties to assert claims of punitive damages in formal judicial proceedings while arbitrating other kinds of disputes."\textsuperscript{89} In addition, by limiting relief to compensatory damages, arbitration acts as an economic disincentive for aggrieved investors or employees to pursue claims.\textsuperscript{90} This result would be contrary to the federal policy of giving arbitrators full authority to deal with all disputes before them. Despite this, the prohibitory rule of not allowing arbitrators to

\textsuperscript{83} 353 N.E.2d at 794.
\textsuperscript{84} Id.
\textsuperscript{85} Id.
\textsuperscript{86} Hadden, supra note 31, at 348.
\textsuperscript{87} Wilson, supra note 20, at 150.
\textsuperscript{88} See id.
\textsuperscript{89} See Stipanowich, supra note 17, at 1007.
\textsuperscript{90} See Wilson, supra note 20, at 152.
award punitive damages, has been adopted by several other courts and jurisdictions.91

The Garrity rule is also problematic because it does not allow arbitrators to award punitive damages even when the parties expressly provided for such a remedy.92 The court explicitly stated that "[a]n arbitrator has no power to award punitive damages, even if agreed upon by the parties."93 Since Garrity is non-conforming with federal policy, several courts have refused to follow its lead and instead have held that arbitration panels can award punitive damages, thereby limiting the extent Garrity's influence.94

In Belko v. AVX Corp.,95 decided by the California Court of Appeals, the parties expressly conferred upon arbitrators the authority to impose punitive damages and therefore it was unnecessary for the court to determine whether the authority to award punitive damages can be implied solely from broad language in contractual agreements which do not expressly provide for such damages.96 However, the court held that "the most practical rule consistent with fairness is one which permits the parties to expressly confer the power to award punitive damages upon an arbitrator. In so doing, we reject the narrow view [that] an arbitrator may never award punitive damages expressed in Garrity . . . ."97

Furthermore, the court found "no public policy significant enough to restrict the right of contracting parties to vesting agreed upon arbitrators with the authority to consider and resolve claims for punitive damages."98 In addition, the court recognized that "several jurisdictions have confirmed punitive damages awards where contract language is broad enough to authorize arbitration of a punitive damages claim and it is just and equitable to do so."99 Clearly in employment discrimination situations, it is just and equitable to authorize

93. Id.
95. 251 Cal. Rptr. at 557.
96. Id. at 558 n.1.
97. Id. at 562.
98. Id. at 563.
99. Id. at 565 n.15.
arbitrators to award punitive damages where parties are bound by a broad arbitration provision.

Commentators have noted that "the Garrity doctrine may be seen as an anomaly, frustrating the goal[] of fairness . . . that [is] the essence of arbitration and undermining the valuable role that punitive damages play in deterring fraudulent or malicious conduct."\textsuperscript{100} However, the Garrity court failed to identify any legislative support for this articulation of public policy.\textsuperscript{101} The result of the Garrity doctrine is that arbitrators could be "faced with controversies involving fraud, oppression, malice, or bad faith, in which a judge might award punitive damages, and yet will be unable to do justice in a similar manner."\textsuperscript{102}

In addition, some courts have carried the Garrity doctrine to the extreme by concluding that "a party to an agreement containing an arbitration clause has waived the right to seek punitive relief in any forum."\textsuperscript{103} However, other courts have declined to follow Garrity by deferring to broad federal and state policies which encourage arbitration.\textsuperscript{104} In addition, although a recent attack on the Garrity rule in the New York courts failed, a concurring opinion called on the New York Court of Appeals to "reexamine the issue of whether punitive damages could be awarded by an arbitrator in securities disputes . . . ."\textsuperscript{105}

In contrast to New York's Garrity rule, the Court of Appeals for the First, Eighth, Ninth and Eleventh Circuits, relying on federal law, have held that arbitrators may award punitive damages based on broad arbitration agreements that incorporate rules authorizing the arbitrators to award any remedy or relief.\textsuperscript{106} However, the outcomes in these cases can be distinguished on a factual basis from Second

\textsuperscript{100} Stipanowich, supra note 17, at 959.

\textsuperscript{101} Id. at 961.

\textsuperscript{102} Id. at 982.


\textsuperscript{106} See, e.g., Lee v. Chica, 983 F.2d 883 (8th Cir. 1993); Todd Shipyards Corp. v. Cunard Line, Ltd., 943 F.2d 1056 (9th Cir. 1991); Raytheon Co. v. Automated Bus. Sys., Inc., 882 F.2d 6 (1st Cir. 1989); Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378 (11th Cir. 1988).
Circuit decisions interpreting arbitration agreements. In addition, the other circuits generally hold that "the FAA requires that federal law be applied to uphold the right of the arbitrator to award punitive damages . . ." The inter-circuit conflicts involving punitive damages awards generally result from state court decisions which hold that arbitrators do not have the authority to award punitive damages.

On the average, courts have determined that federal law permits arbitrators to award punitive damages in cases where it would have been an available remedy in court proceedings. Hence, since "federal law is generally more hospitable to the award of punitive damages in arbitration, the decision of whether state law applies in a particular case has become significant in resolving the issue of whether punitive damages may be awarded by arbitrators.

The brokerage houses have taken advantage of both substantive and procedural barriers to awarding punitive damages, by drawing up employee contracts that contain mandatory arbitration clauses. Such agreements are signed on a take-it-or-leave-it basis without any choice, discussion, or negotiation of the arbitration provision, or its meaning, extent, application, or ramifications. Considering the implications of the arbitration clause, it should be pointed out or highlighted to employees before they are asked to sign the agreement. Such broad arbitration clauses are often the product of unequal bargaining power of brokerage houses over its employees who have little or no opportunity to negotiate the terms of such contracts. However, courts have found that an arbitration agreement is not invalid merely because it was required of all registered brokers by NYSE rules.

Although under current rules of the NYSE and NASD such

107. See Neesemann, supra note 23, at 579.
108. Id. at 582.
110. See Neesemann, supra note 23, at 584-85 n.37.
111. Id. at 584-85.
112. See Wilson, supra note 20, at 138 (providing an analysis of broker-client agreements containing mandatory arbitration clauses).
113. See Neesemann, supra note 23, at 448.
114. Employees are forced to sign U-4 forms to transfer over their licenses without which they would be unable to transact securities business. See Barrowclough v. Kidder Peabody & Co., Inc., 752 F.2d 923, 937 (3d Cir. 1985) (holding arbitration agreement not invalid because it was "required of all registered brokers").
limitations are prohibited, proposals are being developed by the industry to place limitations on punitive damages within the stock exchange rules and NASD rules in the form of monetary caps or review proceedings. Commentators have noted that many securities industry firms fear a "runaway arbitration panel could put a firm out of business as the result of a staggering punitive damage award." However, firms in the securities industry should not be insulated from the repercussions from discriminatory employment practices which all other businesses are prohibited from doing.

One of the problems with arbitration awards is that arbitrators are under no obligation to give a reason for their decision. In general, an award will be upheld as long as it bears a logical relationship to the evidence or as long as it rests upon a rational basis. Courts have held that there is no general requirement that arbitrators explain the reasons for their award.

Arbitrators, who normally have special expertise in their respective industries, should be competent at discerning the limits of acceptable industry practice and determining the amount of punitive damages necessary for both punishing a particular defendant and deterring others in the industry. In this way, punitive awards would retain their character as a social sanction even when the award is affixed by an arbitration panel, rather than the court. The court’s role would be to confirm, vacate, modify and enforce the arbitration panel’s awards thereby preserving the state’s role as a force of social sanction.

117. Id.
118. See Weibel, supra note 47, at 62.
119. For example Ketchum v. Prudential-Bache Securities Inc., 710 F. Supp. 300, 303 (D. Kan. 1989) "undeniably establishes that arbitrators are not required to elaborate their reasoning in support of an award . . . . A rule requiring arbitrators to explain their awards would undermine the very purpose of arbitration, which is to provide a relatively quick, efficient and informal means of private dispute settlement." Weibel, supra note 47, at 64 n.70.
120. See e.g., Sobel v. Hertz, Warner & Co., 469 F.2d 1211, 1214 (2d Cir. 1972) (stating that there is no general requirement that arbitrators explain the reasons for their award); Ketchum, 710 F. Supp. at 303 (holding that arbitrators are not required to elaborate on their reasoning in support of an award).
121. See Wilson, supra note 20, at 154. In contrast, the New York state rule which prohibits arbitrators from awarding punitive damages allows firms to escape liability by merely agreeing to arbitrate discrimination claims and such a result constitutes a total frustration of the public policies and purposes served by punitive damage awards. Id.
122. Id. at 158.
123. Id.
However, one negative implication may be that as judicial review increases, judicial precedent and formalistic procedural rules could circumscribe the arbitrator's flexibility. Another alternative, would be to allow the arbitrator to recommend a punitive damages award amount which would then have to be confirmed by a federal district court. This would restore to punitive damages the element of social sanction by ensuring that the courts make the ultimate decision about damages awarded. However, the difficulty with this alternative is that judges should not award punitive damages without first hearing the evidence presented to the arbitrator and "[c]onducting a full hearing on the issue of punitive damages would increase the time and cost of litigation while undermining the efficiency of arbitration." If the current trend continues, arbitration panels will be granted the authority to "determine and assess punitive damages in appropriate cases."

Security arbitrations are conducted in accordance with the Uniform Code of Arbitration as developed by the Securities Industry Conference on Arbitration ("SICA"). Recently, SICA proposed a remedies provision for the Uniform Arbitration Code that would permit arbitrators to grant any remedy or relief that they deem just and equitable and that would be available were the matter in the court. In *Fahnestock & Co. v. Waltman*, the Second Circuit held that where the parties' arbitration agreement was silent with respect to the arbitrator's authority to award punitive damages, "state law relating to the propriety of a punitive damages award by arbitrators in the absence of an agreement on the subject is not preempted by any federal substantive law . . . ." By granting arbitration panels authority to award any remedy that would be available were the matter in court, the proposed remedy provision would answer the question as to the parties' intent and change the result in the Second Circuit.

124. *Id.* at 159.
125. *Id.* at 161.
126. *Id*.
127. *Id.* at 163.
129. *Id*.
130. See Neesemann, supra note 23, at 590.
131. 935 F.2d 512 (2d Cir. 1991).
132. *Id.* at 518.
133. See, e.g., Barbier v. Shearson Lehman Hutton, Inc., 948 F.2d 117 (2d Cir. 1991)
However, the issue of punitive damage awards in securities arbitration may be not be decided by the courts. In 1989 the rules of the NYSE, the American Stock Exchange ("AMEX") and the NASD were revised to state that the member organizations could not use arbitration agreements that limit the ability of arbitrators to make any award. Although member organizations cannot prohibit arbitrators from granting punitive damages by contract, they can get any such awards vacated by state courts if they include a choice-of-law provision which applies the law of a state, like New York, which does not allow arbitrators to award punitive damages. In addition, the SEC approved these revised rules and construes them to prohibit brokers from attempting to limit a customer's right to seek and an arbitrator's right to award, punitive damages.

V. CONCLUSION

The controversy over the authority of arbitration panels to award punitive damages reveals the basic tension between modern doctrine favoring the administration of justice by arbitrators and judicial perceptions regarding the inherent limitations of the arbitration process. The Garrity rationale is inconsistent with generally accepted concepts of arbitrability, broad remedy-making power and freedom from judicial oversight, which lie at the heart of the arbitration process. In addition, by relying on Garrity, the Second Circuit differs from other circuits which have considered the problem of whether or not to permit arbitration panels to award punitive damages.

Since New York does not allow punitive damages to be awarded by arbitration panels, discrimination claimants, who the securities industries mandates go to arbitration, are not permitted to recover punitive damages which Congress specifically authorized as a remedy in the Civil Rights Act of 1991. In order to discourage discrимi-

134. See Neesemann, supra note 23, at 590.
135. Id.
136. See Stipanowich, supra note 17, at 969.
137. Id.
nation in the workplace, Congress made violations of the Civil Rights Act more costly for companies with discriminatory practices. Congress, by not expressly exempting the Civil Rights Act from the Federal Arbitration Act—thereby allowing victims of discrimination to use a judicial forum, and collect punitive damages, rather than arbitration—did not intend to exempt the securities industry from compliance with the Civil Rights Act. The securities industry should not be granted immunity from punitive damage awards, which every other industry is subject to if they violate the Civil Rights Act. For this reason, New York Law should be changed, either by legislative intervention, expressly granting arbitrators the authority to award punitive damages, or by overturning the Garrity case.

Arbitrators should have the authority to formulate relief in the nature of punitive damages unless the parties have specifically agreed to the contrary; a contrary rule frustrates the ability of arbitrators to effect complete justice. "Denying punitive damages as a remedy forces aggrieved parties to undergo the expense of multiple adjudications or denies them the possibility of receiving punitive relief in any forum." Although proponents of the Garrity doctrine contend that inadequate standards exist for judicial review of punitive awards by arbitrators, it is unclear that the standards for rendition of such awards by juries and their subsequent review by judges provide any more protection for a defendant. If courts continue to force securities industry discrimination claims into arbitration, the arbitration panels must be granted the authority to award punitive damages.

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139. See Stipanowich, supra note 17, at 1010.
140. Id.
141. Id.