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NOTE

BEYOND MASTROBUONO: A PRACTITIONERS’ GUIDE TO ARBITRATION, EMPLOYMENT DISPUTES, PUNITIVE DAMAGES, AND THE IMPLICATIONS OF THE CIVIL RIGHTS ACT OF 1991

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I. INTRODUCTION

A. A Road Map For the Practitioner

On March 6, 1995, the Supreme Court of the United States decided Mastrobouono v. Shearson Lehman Hutton, Inc. The Court granted certiorari to help resolve a circuit split regarding the availability of punitive damages in arbitrations where the governing state law prohibits arbitrators from making such an award. The decision in Mastrobouono, however, will not end the debate. Because the arbitration agreement reflects the wishes of the parties, it often has a more

2. “We granted certiorari because the Courts of Appeals have expressed differing views on whether a contractual choice-of-law provision may preclude an arbitral award of punitive damages that otherwise would be proper.” Id. at 1215 (citation omitted).
3. The phrase “arbitration agreement” is often used to refer to the arbitration provisions
significant impact on the process than any legislative or judicial pro-
nouncements.4

This Note will discuss the current state of pre-dispute arbitration
agreements, the ramifications of Mastrobuono, and a number of al-
ternatives that are available to Congress, state legislatures, the judi-
ciary, and private parties as they attempt to exercise control over the
arbitral process. Finally, this Note will address the punitive damages
provisions of Title VII of the Civil Rights Act of 19916 and the im-
lications that the existence of these non-compensatory remedies may
have on the ability of employers to enforce arbitration agreements.7
In addition, the Note occasionally intertwines issues of traditional
securities arbitration with modern employment dispute arbitration.
Since the case law in each area draws its findings on the same basic
arbitration principles, the intertwining was done in an effort to inte-
grate all of the available information on the subject to provide a
complete practitioners' guide.

This Note will not espouse any political ideology, unlike much
of the recent academic literature on the subject.8 Notwithstanding any

4. See id. at 572; infra notes 148-67 and accompanying text.
5. "Pre-dispute" arbitration agreements are agreements made before any conflicts arise. The parties agree to submit some or all potential disputes to arbitration. Pre-dispute agree-
ments dominate the case law on arbitration because, as a general matter, if both parties agree
to use arbitration after the nature of a claim is known, the agreement is made with full
awareness of the implications of arbitration. Specifically, pre-dispute agreements generate 95%
of arbitrations heard by the American Arbitration Association. See Arbitration: AAA General
(Feb. 16, 1995).
7. The arbitration provisions of most employment agreements can be utilized by the
employer or the employee. However, employees are much more likely to want a chance to
present their claim to a jury. See infra note 162 and accompanying text. As a result, the
employer is generally the party seeking to enforce an arbitration agreement.
8. The political debate is easily found. See, e.g., Stephen A. Plass, Arbitrating, Waiving
and Deferring Title VII Claims, 58 BROOK. L. REV. 779 (1992) (arguing that the decision in
Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20 (1991), improperly restricts individual
rights in union and non-union settings by allowing mandatory arbitration in employment dis-
putes); Julie A. Friedlander, Note, Punitive Damages As a Remedy for Discrimination Claim
Arbitrations in the Securities Industry, 23 HOFSTRA L. REV. 225 (1994) (criticizing the al-
leged unfairness of pre-dispute arbitration agreements and disagreeing with New York's com-
mon law rule which prohibits arbitrators from awarding punitive damages); Wrongful Dis-
charge: Adoption of Model Termination Act 'Win-Win' Proposition, ACLU Director Says,
act which would require arbitration of all employment termination disputes).
court decisions—including *Mastrobuono*—private parties have tremendous flexibility in controlling their own fate in arbitration by negotiating agreements to their liking. As such, what "ought to be" is of little use to the legal practitioner. The purpose of this Note is to help practitioners and academics focus their arguments on the issues that will confront employment dispute arbitration in the future. *Mastrobuono* just touched the surface; the more critical issues are yet to come.

**B. A General Introduction**

In ancient times, an arbitrator heard one party's argument and made a decision. After being required to listen to the other side, the arbitrator complained that, in the future, "[he] only wanted to hear one side of the case . . . hearing two sides confused him." The fear, echoed by many plaintiffs' attorneys and at least one in-house counsel for a securities firm, is that some of today's arbitrators possess the same meager level of interest in making fair and reasoned decisions. Heightening the concerns of many about the arbitral process is that arbitration agreements are form contracts which are rarely negotiated. In addition, the courts have held that absent agreement to a "trial by battle or ordeal or . . . by a panel of three monkeys," parties to arbitration agreements are generally free to agree to anything.


10. Confidential Telephone Interview with in-house counsel for brokerage firm (Oct. 1994). This is by no means an indictment of the arbitral process as a whole, but the constraints on the judiciary offer greater protection to control erroneous findings through appeal. Whereas a wayward judge is easily corralled, to overturn an arbitrator's ruling is much more difficult. See infra notes 315, 320-23 and accompanying text.


While the fairness of the arbitration process as a whole can be debated, it is an issue which will not be resolved by any one article or single court. Furthermore, opinion offers little guidance to those who practice in the field. It will be necessary for the practitioner to effectively respond to Mastrobuono and to prepare for the likely debate about the availability of punitive damages in arbitration when claims are made under the specific punitive damages provisions of the Civil Rights Act of 1991. Although the courts have shown little inclination to interfere with arbitration agreements signed in a typical commercial deal, the courts may be inclined to carve out exceptions to the general rule when bargaining power is grossly unequal. Recent case law seems to indicate that in the alternative dispute resolution arena, the greatest public policy concerns are in cases of mandatory employment dispute arbitration. As such, employment dispute arbitration may be the fertile ground for legal innovation with regard to the availability of punitive damages.

Although much of the case law utilized in this Note comes from employment dispute cases, the procedural rules of the arbitral bod-

13. The Supreme Court has been clear in its opinion that arbitrators are presumed to be fair. See Mastrobuono v. Shearson Lehman Hutton, Inc., 115 S. Ct. 1212, 1217 n.4 (1995); Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 634 (1985). Even the Supreme Court admitted that its decision in Mastrobuono failed to address all the relevant issues related to the advisability of allowing arbitrators to decide all disputes. Mastrobuono, 115 S. Ct. at 1215 n.1. Given the recent case law, however, practitioners should assume that any civil dispute is a proper subject for arbitration. See infra notes 25-33, 37-43 and accompanying text.


15. See infra notes 137-42 and accompanying text.

16. 42 U.S.C. § 1981b(1)-(3) (Supp. V 1993). The Civil Rights Act of 1991 is of importance because it is one of the only statutes that has an explicit provision for punitive damages.

17. See infra notes 25-33 and accompanying text.

18. See generally infra notes 49-59 and accompanying text.

19. See, e.g., Prudential Ins. Co. of Am. v. Lai, 42 F.3d 1299, 1305 (9th Cir. 1994) (holding that the plaintiff-employees did not knowingly waive their rights); Higgins v. Superior Ct., 1 Cal. Rptr. 2d 57, 63 (Ct. App. 1991) (ordered not officially published) (holding that the agreement only encompassed business matters).
ies do not differ significantly with regard to different causes of action. The resolution of the employment arbitration debate may impact the future of the entire arbitral process, just as the outcomes of cases like *Mastrobuono*, which generally evaluate the availability of punitive damages, are likely to effect the employment debate.

II. A BRIEF SUMMARY OF MODERN-DAY ARBITRATION

A. The Arbitrability of Private Disputes

The Federal Arbitration Act ("FAA") provides that if parties have agreed to arbitrate their disputes, such an agreement will be enforceable by the courts. Virtually all types of claims have been compelled to arbitration, although many authors continue to argue that certain causes of action should not be arbitrable. The courts

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25. Technically, most courts issue an order to stay judicial proceedings pending the outcome of arbitration. However, "filing a motion to compel arbitration" is the common language used by many practitioners and in most of the current literature and case law on arbitration.

26. Authors have persistently questioned the arbitrability of many disputes, especially with regard to employment disputes. For the most outspoken proponent's view, see Heidi M.
have accepted contract claims, antitrust claims, copyright claims, ERISA claims, racketeering claims and securities law claims, among many others. Furthermore, as arbitration has


32. Claims under the Securities Act of 1933 (the "33 Act"), 15 U.S.C. § 77a-77aa
gained judicial acceptance, pre-dispute arbitration agreements are becoming popular in many new areas of business and industry.

B. The Arbitrability of Employment Disputes

If parties contractually agree to arbitrate future disputes, those disputes will be arbitrable when problems arise. Specifically, the Supreme Court’s decision in Gilmer v. Interstate/Johnson Lane Corp. upheld the ability to arbitrate employment discrimination cases. Other courts, many following Gilmer, have repeatedly held (1988), and the Securities and Exchange Act of 1934 (the "34 Act"), 15 U.S.C. § 78a-78ll (1988 & Supp. V 1993), are arbitrable. See Rodriguez de Quijas, 490 U.S. at 482-85 (holding that claims made under the '33 Act and the '34 Act were arbitrable); Shearson/American Express Inc. v. McMahon, 482 U.S. at 238 (holding that a claim alleging a violation of the '34 Act was arbitrable); Singer v. E.F. Hutton & Co., 699 F. Supp. 276, 278 (S.D. Fla. 1988) (holding that a claim alleging a violation of § 12(2) of the '33 Act was arbitrable). See generally Hermann, supra note 26, at 699-706 (detailing the history of Shearson/American Express Inc. v. McMahon and Rodriguez de Quijas).

33. See generally infra note 34.


37. Id. (upholding the arbitrability of a claim made under 29 U.S.C. §§ 621-34 (1988),
that employment-related claims are proper subjects for arbitration.\textsuperscript{38} Courts have explicitly held that claims are arbitrable if based on state anti-discrimination statutes,\textsuperscript{39} the Age Discrimination and Employment Act,\textsuperscript{40} the Americans with Disabilities Act,\textsuperscript{41} restrictive non-competition covenants,\textsuperscript{42} and discrimination claims under Title VII of the Civil Rights Act.\textsuperscript{43} Notwithstanding the legal and moral concerns of requiring employees to sign pre-dispute arbitration agreements as a condition of employment, such agreements are becoming popular, even beyond the securities industry.\textsuperscript{44} More and more businesses will


\textsuperscript{42} See, e.g., \textit{In re} Sprinzen, 389 N.E.2d 456, 460 (N.Y. 1979); see also Erving v. Virginia Squires Basketball Club, L.P., 468 F.2d 1054, 1069 (2d Cir. 1972) (holding enforceable an arbitration agreement used to settle a dispute that arose when Julius Erving left the Squires, mid-contract, to play for the Atlanta Hawks).


attempt to limit their exposure to employment litigation by utilizing arbitration.45

Generally, most courts have utilized the same standards for enforcing employment dispute arbitration agreements as those used to evaluate typical contracts.46 Therefore, absent a declaration that the contracts are unconscionable,47 pre-dispute arbitration agreements are enforceable and binding on employees.48 In rare cases, courts have refused to compel arbitration where the agreement was vague, ambiguous, or unenforceable because a party was coerced into signing,49 or when the arbitration of a claim would conflict with public policy.50 This judicial hesitancy to compel arbitration has been most evident in employment and discrimination cases or other situations where adhesion contracts have been at issue.51


47. See Ware, supra note 3, at 543.

48. See supra notes 35-43 and accompanying text.

49. See, e.g., Farrand v. Lutheran Bhd., 993 F.2d 1253, 1255 (7th Cir. 1993) (holding that employment disputes were not arbitrable because NASD arbitration rules did not specifically cover such disputes); Prudential Ins. Co. of Am. v. Lai, 42 F.3d 1299, 1303-05 (9th Cir. 1994) (affirming Farrand and holding that the plaintiff-employees did not knowingly waive their rights); Krescock v. Bankers Trust Co., No. 92 C-7994, 1993 U.S. Dist. LEXIS 11685, *3-6 (N.D. Ill. 1993) (supporting Farrand's analysis and denying arbitrability because the NASD arbitration rules did not adequately define which parties were covered), aff'd, 21 F.3d 176 (7th Cir. 1994); Higgins v. Superior Ct., 1 Cal. Rptr. 2d 57, 63 (Ct. App. 1995) (ordered not officially published) (holding that the agreement only encompassed business matters); Shaw v. Kuhnle & Assoc., Inc., 698 P.2d 880, 881 (N.M. 1985) (holding that the moving party lacked standing in the state court to compel arbitration); see also Cerissa Anderson, Split Over Retroactivity of NASD Arbitration Rule, N.Y. L.J., Feb. 14, 1994, at 1 (reporting on several cases brought by F.N. Wolf & Co. against its former brokers which yielded inconsistent results). But see F.N. Wolf & Co. v. Bowles, 610 N.Y.S.2d 757, 759-60 (Sup. Ct. 1994) (finding fault with Farrand, 993 F.2d at 1253). The NASD quickly clarified its arbitration rules in reaction to Farrand to specifically include employment related claims. See infra notes 143-45 and accompanying text.


51. See Harold Brown, Punitive Damages and Contractual Arbitration, N.Y. L.J., Jan. 28, 1993, at 3, 29; see also Rosmarin, supra note 26, at 1595-96 & n.9 (describing the prevalence of adhesion contracts in consumer transactions). But see Gilmer v. Inter-
In light of the trend among businesses to use arbitration to resolve employment disputes, the California court's aberrant treatment of this issue deserves some mention. Recently, in *Prudential Insurance Co. of America v. Lai*, the Ninth Circuit Court of Appeals issued an opinion seemingly at odds with *Gilmer v. Interstate/Johnson Lane Corp.* Although two Prudential employees signed an agreement identical to the one in *Gilmer*, the court in *Prudential* excused the employees from being bound by the agreement they signed, asserting that

> even assuming that [the] appellants were aware of the nature of the U-4 form, they could not have understood that in signing it, they were agreeing to arbitrate sexual discrimination suits. The U-4 form did not purport to describe the types of disputes that were to be subject to arbitration.

This statement by the court is clearly not in line with *Gilmer* and its progeny. Although some will undoubtedly claim that the *Prudential* court's assertions are also at odds with the general philosophy of the Supreme Court's decision in *Mastrobuono*, which held that ambiguities in arbitration agreements result in more, rather than less, issues that are subject to arbitration.

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52. 42 F.3d 1299 (9th Cir. 1994).
54. Compare *Gilmer*, 500 U.S. at 23 with *Prudential Ins. Co. of Am.*, 42 F.3d at 1305. In both cases, the employees signed the Uniform Securities Registration Form U-4, which contains the following language: "I agree to arbitrate any dispute, claim or controversy that may arise between me and my firm . . . that is required to be arbitrated under the rules, constitution, or by-laws of the [registering] organization . . . ." Form U-4: Uniform Application For Securities Industry Registration or Transfer (1991) [hereinafter U-4 Application] (on file with the Hofstra Law Review); see also infra note 67 and accompanying text (describing the securities industry's registration process).
55. *Prudential Ins. Co. of Am.*, 42 F.3d at 1305. One possible explanation for the aberrant decision in *Prudential* may be found in the facts of the case. The two female plaintiffs were recent immigrants alleging serious sexual harassment, including rape. See Marian Raab, *Arbitration Ruling Faces New Appeal*, NAT'L LJ., Jan. 9, 1995, at B1. The nature of the claims may have influenced the outcome.

In addition, the case had a procedural irregularity, though its impact is unclear. Justice Aldisert participated in oral argument and then recused for the decision, causing a situation whereby Justice Norris concurred in the decision without being present for oral arguments. See *Prudential Ins. Co. of Am.*, 42 F.3d at 1301 n.*.

56. See supra notes 36-43 and accompanying text; see also Kinnebrew v. Gulf Ins. Co., No. CA 3:94-CV-1517-R, 1994 U.S. Dist. LEXIS 19982, at *6 (N.D. Tex. Nov. 23, 1994) (holding that an arbitration policy was valid even though the company "unilaterally distributed the policy to employees without explaining its effect and without seeking their express agreement").

The *Prudential* court's assertions are also at odds with the general philosophy of the Supreme Court's decision in *Mastrobuono*, which held that ambiguities in arbitration agreements result in more, rather than less, issues that are subject to arbitration. See *Mastrobuono v. Shearson Lehman Hutton*, Inc., 115 S. Ct. 1212 (1995).
court’s references to ambiguous National Association of Securities Dealers ("NASD") rules provide the justification for its decision,\(^7\) as the dissent aptly pointed out, if \textit{Farrand v. Lutheran Brotherhood}\(^8\) were still good law, the lengthy discussion of other issues would have been unnecessary.\(^9\) Thus far, no other courts have followed California’s lead.

\section*{C. The Securities Industry and Arbitration}

The securities industry utilized arbitration as early as the late 1800’s.\(^6\) Currently, the industry uses arbitration as its predominant form of dispute resolution to resolve client complaints\(^6\) through the use of the arbitration rules of the various exchanges.\(^6\) In fact, the widespread use of arbitration agreements in the industry\(^6\) is one reason why a vast majority of the case law of non-union arbitration comes directly from challenges to pre-dispute agreements signed by or with securities firms.\(^6\) A typical client agreement contains the following language:

\begin{itemize}
  \item \textit{See Prudential Ins. Co. of Am., 42 F.3d at 1305.}
  \item 993 F.2d 1253 (7th Cir. 1993); \textit{see supra note 49 and accompanying text; infra notes 143-45 and accompanying text (discussing the \textit{Farrand} decision in greater detail).}
  \item Prudential Ins. Co. of Am., 42 F.3d at 1306 (Norris, J., concurring) (criticizing the basis for the majority’s decision and criticizing the other justices for “engag[ing] in appellate fact-finding . . . even though the district court never made a finding on the issue”).
  \item \textit{See Katsoris, supra note 22, at 1114 (citing PHILIP J. HOBLIN, SECURITIES ARBITRATION: PROCEDURES, STRATEGIES, CASES 1-2 (1988)).}
  \item Client complaints may involve charges of churning, violations of the securities laws, unauthorized trading, and other improper activity on the part of the broker or the securities firm. \textit{See generally} Michael S. Wilson, \textit{Note, Punitive Damages in the Arbitration of Securities Churning Cases,} 11 REV. LITIG. 137, 139-43 (1991) (detailing the process of churning in the industry); \textit{NASD Solicits Public Comment on Approaches Governing Award of Punitive Damages in Arbitration.}, 94-54 NASD \textit{NOTICE} TO MEMBERS 319, 322 (July 1994) [hereinafter NASD \textit{NOTICE}] (reporting on the high volume of arbitrations filed in the securities industry).
  \item \textit{See Hermann, supra note 26, at 717 (reporting on a study which indicated that the overwhelming majority of brokers require arbitration agreements). Many firms, however, do not require arbitration agreements for their basic “cash” accounts. See Giltenan, supra note 12 at 196; John F.X. Peloso & Stuart M. Sarnoff, \textit{Punitive Damages in Arbitration}, N.Y. L.J., Aug. 18, 1994, at 27 n.23.}
  \item \textit{See Abrams, supra note 22, at 521 n.4; Bernstein & Ramsfelder, supra note 38, at 17.}
\end{itemize}
This agreement . . . shall be governed by the laws of the State of New York. . . . Any controversy arising out of or relating to [the client's] accounts . . . shall be settled by arbitration in accordance with the rules then in effect, of the National Association of Securities Dealers, Inc. or the Board of Directors of the New York Stock Exchange, Inc. and/or the American Stock Exchange Inc. as [the client] may elect. . . .

More recently, the industry has extended the use of arbitration to employment disputes. For registered employees, the arbitration provisions are contained in the U-4 registration applications. For non-registered employees, the arbitration provisions are contained in employment applications or in separate alternative dispute resolution policies. Language similar to the following is typical:


The typical language will probably become atypical rather quickly. The Supreme Court held that this type of agreement was too vague to exclude punitive damages. See Mastrobuono v. Shearson Lehman Hutton, Inc., 115 S. Ct. 1212 (1995). The agreements are likely to change to reflect the Court's holding, except that exchange rules against limiting provisions may prevent the agreements from becoming as explicit as the Court suggested. See infra notes 151-67 and accompanying text.

66. Generally, brokers, traders, analysts, business managers, and executives are required to register with the exchanges with which their firms conduct business. See generally Friedlander, supra note 8, at 225-26.

67. See U-4 Application, supra note 54; see also Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 23 (1991) (citing to the U-4 Application and NYSE Rule 347); Bender v. Smith Barney, Harris Upham & Co., 789 F. Supp. 155, 159 (D.N.J. 1992) (noting that even the brokerage firms are bound by the U-4 Application's provisions). See generally Friedlander, supra note 8, at 225-26 & nn. 1-9 (describing the process by which employees register in the securities industry with the U-4 Application).

68. See Mago v. Shearson Lehman Hutton, Inc., 956 F.2d 932 (9th Cir. 1992) (holding that an employment application could serve as an enforceable arbitration agreement).
I hereby agree that any controversy arising out of or in connection with my compensation, employment or termination of employment shall be submitted to arbitration before the National Association of Securities Dealers, Inc., the New York Stock Exchange, Inc. or the American Stock Exchange, Inc. and be resolved in accordance with the rules, then in effect, of such entities. . . . This provision applies to any claims or actions under Title VII, the ADEA or any other state or local discrimination statute.69

Although some authors may claim that the issue of the arbitrability of employment-related claims is "an unsettled question,"70 the attorneys representing the securities industry (and most courts, for that matter) believe that any issue may be compelled to arbitration.71 Furthermore, waiver of the right to judicial resolution may be possible without the traditional requirement of a signed agreement. Following the principles of Gilmer v. Interstate/Johnson Lane Corp.,72 a federal court in Mago v. Shearson Lehman Hutton, Inc.73 ruled that a signed employment application containing arbitration provisions was sufficient to qualify as an enforceable contract to compel the arbitration of a discrimination claim.74 Recently, one court even compelled arbitration of an employment dispute despite the fact that there was no written agreement between the parties.75

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70. Bompey & Pappas, supra note 26, at 197; see supra note 26 and accompanying text.

71. Telephone Interviews with brokerage firms' in-house and outside counsel (Fall 1994) (responding uniformly with statements such as: "Of course [employees] have to arbitrate discrimination claims."); see also supra notes 25-33, 37-43 and accompanying text.


73. 956 F.2d 932 (9th Cir. 1992).

74. Id. at 935. When the author worked in the industry, he heard firm attorneys tell many adversaries that arbitration would be compelled, frequently with little resistance. Mago, being one of the few cases decided on this limited issue, may be unique simply because the practitioners in the field are no longer challenging the issue.

To combat the propensity to arbitrate employment discrimination claims, many cite to the Federal Arbitration Act and its specific wording which prohibits its application to "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce." However, the employment contract exclusion only applies to employment agreements made with workers actually engaged in the transport of interstate commerce. Although the Supreme Court avoided the issue in *Gilmer* because it was not raised in the lower court, it stated in dicta that the issue was not applicable because the arbitration provisions were contained in a registration agreement between the New York Stock Exchange and Mr. Gilmer, instead of an employment contract between the firm and its employee. Subsequently, lower courts have held that the interstate commerce language in the employment contract exclusion refers to "actual interstate commerce," and thus, only prevents the enforcement of arbitration agreements with interstate haulers and similar workers. Pre-dispute arbitration agreements are enforced regularly to compel arbitration for the vast majority of employees who have signed such agreements.

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79. See *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 25 n.2 (1991). But see *id.* at 36-43 (Stevens, J., dissenting, joined by Marshall, J.) (arguing that meeting the requirements of § 1 is a condition precedent to the arbitrability of employment disputes).
82. See *supra* notes 36-43 and accompanying text.
III. PUNITIVE DAMAGE AWARDS IN ARBITRATION

The Federal Arbitration Act\(^3\) provides that an arbitrator is empowered to award any remedy and thus, pursuant to section 9 of the Act, punitive damages are available in arbitration.\(^4\) Although the arbitration rules of the Chicago Board of Trade specifically provide for punitive damages,\(^5\) the award rules of the other major exchanges are silent on the issue.\(^6\) Recently, several of the arbitral bodies have made attempts to prohibit arbitration agreements from limiting damages, ostensibly to guarantee the availability of punitive damages.\(^7\) Nonetheless, and notwithstanding the Mastrobuono decision, punitive damages are not available in all arbitrations.\(^8\)

Two factors have regularly impeded arbitrators' ability to award punitive damages. First, the public policy of many states prohibits arbitrators from awarding punitive damages.\(^9\) Second, the arbitration agreement may contain specific provisions preventing the arbitrator from awarding punitive damages.\(^10\)

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85. See Arbitration, Chicago Bd. Trade R. & Regs. Man., ch. 6, ¶ 601.01-02 (Nov. 1, 1992) (allowing clients punitive damages up to twice the amount of actual damages).
87. See Rules: Arbitration, Chicago Bd. Options Ex. Guide (CCH) ¶ 2540B (Dec. 20, 1994) (covering only pre-dispute agreements with clients); Rules of Fair Practice, Nat’l Ass’n Sec. Dealers Man. (CCH) ¶ 2171 (Nov. 7, 1994) (generally prohibiting arbitration agreements that limit damages); General Rules: Arbitration, N.Y.S.E. Guide (CCH) ¶ 2636 (Nov. 1994) (covering only pre-dispute agreements with clients); see also infra notes 165-66 and accompanying text (detailing the implications of arbitral body rules that conflict with agreement provisions).
88. See infra notes 168-96 and accompanying text.
89. See infra note 105 and accompanying text; see also infra notes 183-84 and accompanying text (detailing how the Mastrobuono decision does not render state arbitration rules moot).
90. See infra notes 154-57, 164 and accompanying text.
A. How Did We Get in This Mess Anyway?

Garrity v. Lyle Stuart, Inc.91

Most arbitration agreements in the securities industry, including those for employment-related disputes, specify that the rules of the American Arbitration Association ("AAA"), NYSE, or NASD are to be used and that the agreement is governed by New York law.92 At present, the provisions of the FAA,93 the NASD arbitration rules,94 and the NYSE arbitration rules95 permit arbitrators to award punitive damages. However, when coupled with a contractual New York choice-of-law, punitive damages are, arguably, unavailable.

In Garrity v. Lyle Stuart,96 New York's highest court held that arbitrators have "no power to award punitive damages."97 Following the Garrity decision, some courts have held that, if a party must submit a claim to arbitration and must use New York law, punitive damages are unavailable.98 The Garrity court held that punitive damages


95. General Rules: Arbitration, N.Y.S.E. Guide (CCH) ¶ 2627 (Nov. 1994); id. ¶ 2636 (covering only pre-dispute agreements with clients); see Fahnstock & Co. v. Walmat, 935 F.2d 512, 519 (2d Cir.) (illustrating that even the NYSE award form includes a line for punitive damages), cert. denied, 502 U.S. 924 (1991), and cert. denied, 502 U.S. 1120 (1992).


97. Id. at 794.

98. See, e.g., United States Fidelity & Guar. Co. v. DeFluiter, 456 N.E.2d 429, 432-33 (Ind. CIR. App. 1983) (holding that choosing a forum without punitive damages constitutes a
are a sanction reserved to the state, and as such, the state is the only entity with authority to mete out such a punishment. An arbitrator is unable to make an award to society because of the private nature of the proceedings, and thus, the court held that punitive damage awards in arbitration constitute a private remedy and are prohibited as a matter of public policy.

In support of Garritty, the Securities Industry Association ("SIA") claims that the existence of the Securities and Exchange Commission ("SEC") and its regulatory authority is a sufficient deterrent to wrongdoing, eliminating the need for punitive damages. Arbitration does not foreclose or even impede regulatory or disciplinary action by the SEC, the Equal Employment Opportunity Commission, or other agencies which are free to institute litigation or issue administrative fines and penalties.

waiver of such damages). New York choice-of-law is used so frequently that Michael Crotty, the American Bankers' Association's deputy general counsel for litigation, reportedly claimed that one of the advantages of arbitration is that "'[t]here are no punitive damages." Tips from ABA's Compliance Conference, A.B.A. BANKING J., Sept. 1994, at 38. The Supreme Court would likely differ with Mr. Crotty. See Mastrobuono v. Shearson Lehman Hutton, Inc., 115 S. Ct. 1212 (1995).


100. See Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378, 1387 (11th Cir. 1988).

101. See Garritty, 353 N.E.2d at 794-95. One reporter hypothesized that the court in Garritty was trying to guarantee that unchecked arbitration was not used to give a windfall to plaintiffs so that they could "retire to Boca Raton." Punitive Battle Builds to a Climax, WALL ST. LETTER, Aug. 29, 1994, at 8 [hereinafter Punitive Battle]; see Compliance & Legal Div., Sec. Indus. Ass'n, Authorizing Recovery of Punitive Damages in Securities Arbitration Proceedings: A Legal and Policy Analysis 2 (undated and unpublished draft report, on file with the Hofstra Law Review) [hereinafter SIA Draft Report] (arguing that precluding punitive damages in arbitration merely impedes "the opportunity to reap a super-compensatory windfall benefit").


103. See Gilmer v. Interstate/Johnson Lane Corp., 895 F.2d 195, 197-98 (4th Cir. 1990), aff'd, 500 U.S. 20, 28-29, 32 (1991); Discrimination in Securities Industry Subject of Probe, EEOC Official Reports, Daily Rep. for Execs. (BNA) No. 182, at A-25 (Sept. 22, 1994); see, e.g., Silberman et al., supra note 44, at 1550; Anderson, supra note 49, at 1; Peloso & Samoff, supra note 63, at 3. Although the Federal Department of Labor will not be deterred, some state labor departments will cease their investigations when an arbitration is pending. Confidential Telephone Interview with in-house counsel to brokerage firm (May 1995).

104. See Mark Berger, Can Employment Law Arbitration Work?, 61 U. MO. KAN. CITY L. REV. 693, 719 (1993); Piskorski & Ross, supra note 26, at 210; Peloso, supra note 92, at 5 (stating that "it is unnecessary and unreasonable for a civil court or an arbitration panel to
The public policy of many other states supports New York's public policy espoused by *Garrity*.

Theoretically, if an agreement is covered by a limiting state statute, any arbitration award of punitive damages would be unenforceable because the law should be applied faithfully, even in a state that allows such awards.

Courts outside New York, however, have not always upheld *Garrity*.

The circuit split culminated when the Supreme Court heard *Mastrobuono v. Shearson Lehman Hutton, Inc.*

105. Arkansas, Colorado, Indiana, Minnesota, Nebraska, New Mexico, New Hampshire, and West Virginia have similar policies. See McLeroy v. Waller, 731 S.W.2d 789, 792 (Ark. Ct. App. 1987) (holding that the arbitrators were not able to award punitive damages because they were not empowered to decide a tort claim); United States Fidelity & Guar. Co. v. DeFluiter, 456 N.E.2d 429, 432 (Ind. Ct. App. 1983) (describing Indiana's policy as prohibiting arbitrators from awarding punitive damages); School City v. East Chicago Fed'n of Teachers, Local 511, 422 N.E.2d 656, 663 (Ind. Ct. App. 1981) (same); Shaw v. Kuhnel & Assoc., Inc., 698 P.2d 880, 882 (N.M. 1985) (supporting *Garrity*, in dicta); Anderson v. Nichols, 359 S.E.2d 117, 121 n.1 (W. Va. 1987) (holding that punitive damages "are beyond the scope of the arbitrator's power"); SIA Opposition, supra note 102, at 1184 (quoting the SIA as claiming that *Garrity*-like policies exist in Colorado, Minnesota, Nebraska, New Mexico and New Hampshire). See generally NCR Corp. v. Sac-Co., Inc., 43 F.3d 1076, 1081-82 (6th Cir. 1995) (Wellford, J., concurring) (supporting, in dicta, the philosophy expressed in *Garrity*); Davis, supra note 20, at 64-65 & nn. 85-88; Seamons, supra note 104, at 406; Slipanovich, *supra* note 91, at 963-70. But see Kennedy, Matthews, Landis, Healy & Pecora, Inc. v. Young, 524 N.W.2d 752, 755 (Minn. Ct. App. 1994) (holding that in Minnesota, arbitrators may award punitive damages, and that even if prohibited, such an award would be a non-reviewable mistake of law by the arbitrator).

106. See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Barnum, 616 N.Y.S.2d 857, 863 (Sup. Ct. 1994); see also infra notes 113-17 and accompanying text (describing the failure of the courts to follow this basic choice of law premise).

107. See, e.g., Todd Shipyards Corp. v. Cunard Line, Ltd., 943 F.2d 1056, 1062-63 & n.6 (9th Cir. 1991); Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378, 1387 (11th Cir. 1988).

B. The Circuit Split

One could easily assume that an award of punitive damages would be void if the agreement specifies governing law of a state that prohibits arbitrators from awarding punitive damages. Inasmuch as the provisions of the Federal Arbitration Act only provide procedural guidelines, one is forced to look to state law for substantive guidance. At least one commentator has suggested that there is no conflict between the FAA and state law with regard to the issue of punitive damages:

"If the parties choose in their agreement to be governed by state law on the arbitrability of punitive damages, courts must apply that state law even though the agreement involves interstate commerce. In such a situation, state law would ultimately govern the punitive damages question even though, as an initial matter, federal law is controlling."

The circuit courts have not consistently prohibited punitive damage awards, however, finding that if the rules of an arbitral body allow punitive damages, such an award is available notwithstanding state law. In addition, one of California's appellate courts held that the FAA and its "body of federal substantive law" would preempt any attempts by a state to limit such an award if an agreement "contemplated punitive damages."


In Mastrobuono, the Supreme Court listed one of the "differing" opinions as that of the Seventh Circuit in Pierson v. Dean Witter Reynolds, Inc., 742 F.2d 334 (7th Cir. 1984), holding that punitive damages were available, notwithstanding a New York choice-of-law. Mastrobuono, 115 S. Ct. at 1215. Given the Seventh Circuit's holding in Mastrobuono, however, Pierson was already overturned. See Mastrobuono, 20 F.3d at 713.

112. J. Alexander Sec., Inc. v. Mendez, 21 Cal. Rptr. 2d 826, 829-30 (Ct. App. 1993), review denied, No. S035102, 1993 Cal. LEXIS 6354 (Nov. 24, 1993), and cert. denied, 114 S. Ct. 2182 (1994). Notwithstanding its holding that the FAA preempted state law, the court discussed the California public policy favoring the awarding of punitive damages. Id. at 1093.
The circuit split\textsuperscript{113} and the issue of federal preemption\textsuperscript{114} have been discussed \textit{ad nauseam} in other forums. Simply put, the circuit courts in the First, Eighth, Ninth, and Eleventh Circuits, and California's appellate courts rejected the position that a particular choice-of-law requires that they deny enforcement of an arbitrator's award of punitive damages.\textsuperscript{115} The Second Circuit (the geographic home of \textit{Garrity}) and the Seventh Circuit followed New York choice of law by refusing to enforce punitive damage awards.\textsuperscript{6} This untenable situation left the courts and the brokerage firms in a quandary.\textsuperscript{7} The issue was first addressed by the Supreme Court when it considered the petition for certiorari in \textit{J. Alexander Securities, Inc. v.}
Mendez. In response to the denial of certiorari, Justice O'Connor and Chief Justice Rehnquist vehemently dissented, imploring the Court to address the circuit split. Notwithstanding the fact that certiorari was denied in J. Alexander Securities on June 6, 1994, and Mastrobuono was already decided by the Seventh Circuit at that time, the Court accepted the Mastrobuono petition for certiorari four months later.

C. Mastrobuono Resolves the Split—In a Manner of Speaking

The core of the debate during oral arguments in Mastrobuono was focused on the language in the arbitration provisions of the Shearson Lehman Hutton Client Agreement signed by Antonio and Diane Mastrobuono in 1985. The couple closed their account in 1987 after sustaining significant losses, which they attributed to the actions of their broker and the negligent supervision by Shearson management. Eventually, an arbitrator awarded $159,327 in compensatory damages and $400,000 in punitive damages to the couple. The district court and the Seventh Circuit Court of Appeals both refused to enforce the award of punitive damages. The case was then appealed to the United States Supreme Court. Id. at 1214-15.
Diane Mastrobuono. The Justices appeared to be fixated on the agreement’s lack of explanation of the New York choice-of-law clause and the apparent conflict between the choice-of-law and the arbitration rules of the NASD. Although counsel for Lehman Brothers vehemently denied that the agreement was ambiguous, Justices Ginsberg and Breyer repeatedly questioned him on that matter. Evidently, all but Justice Thomas agreed with Justices Ginsberg and Breyer; the Supreme Court held for Mr. and Mrs. Mastrobuono and enforced the arbitrator’s award of punitive damages.

Although the Supreme Court’s decision in Mastrobuono may appear to direct the courts on how to resolve conflicts between state law and the FAA, such a conclusion overstates the breadth of the Court’s decision. The Court held that a contract governed by New York law “need not be read [as] . . . an unequivocal exclusion of punitive damages claims.” The Court cautioned, however, that it was reviewing the case de novo, and merely established the vagueness of the contract at bar. Only three limited conclusions can be gleaned from the Court’s decision. The Court held that punitive damages are available in an arbitration if:

(1) the contract at issue is the same as the Shearson Lehman Hutton

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124. See Supreme Court Notes, supra note 119.
125. Id.
126. Although the case is entitled “Mastrobuono v. Shearson Lehman Hutton, Inc.,” because of a number of mergers and asset sales, the case was handled by Lehman Brothers, Inc., a successor company to Shearson Lehman Hutton. Joseph Polizzotto, Managing Director & Deputy General Counsel of Lehman Brothers, appeared on behalf of the firm. 115 S. Ct. at 1214.
127. See Supreme Court Notes, supra note 119.
128. Mastrobuono, 115 S. Ct. 1212 (8-1 decision) (Thomas, J., dissenting).
129. Id. at 1217.
130. Id. at 1217 n.4.
131. One general holding that can be found in the pages of Mastrobuono was already assumed by many to be a foregone conclusion: parties can agree to virtually anything in an arbitration agreement. The Court finally rendered null and void the most frequently cited piece of Garrity dicta. In Garrity v. Lyle Stuart, Inc., 353 N.E.2d 793 (N.Y. 1976), the New York Court of Appeals held that an arbitrator could not award punitive damages “even [if] agreed upon by the parties.” Id. at 795. Virtually every court or commentator that has discussed Garrity has used this quote to explain the reaches of New York’s prohibition against arbitrators awarding punitive damages. The quote is now a nullity because the Supreme Court held that “if contracting parties agree to include claims for punitive damages within the issues to be arbitrated, the FAA ensures that their agreement will be enforced according to its terms even if a rule of state law would otherwise exclude such claims from arbitration.” Mastrobuono, 115 S. Ct. at 1216.
Client Agreement in *Mastrobuono*;

(2) the contract merely makes “reference to ‘the laws of the State of New York,’” without more explicit language to explain the implications of the choice-of-law with regard to the availability of punitive damages; or

(3) the contract does not specify which provisions will take priority while incorporating state law that restricts punitive damage awards and arbitration procedures that allow punitive damages.

Not surprisingly, a number of issues, such as federal preemption, remain unresolved. The Court merely held that the phrase “the laws of the State of New York” was not unequivocal enough to overcome the federal presumption favoring the arbitrability of all matters, including punitive damages. By issuing such a limited ruling, the Court guaranteed that this issue will be re-litigated again and again, based on different agreements and different state law.

IV. BEYOND *MASTROBUONO*

A. The Immediate Effects

Most of the debate about mandatory arbitration and punitive damages had assumed that one change in the law or a single pivotal court decision, like *Mastrobuono*, would resolve this entire issue. While the *Mastrobuono* decision will provide some temporary solutions to the conflict over the availability of punitive damages in arbitration, those effects will be limited. The greatest immediate implica-

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132. 115 S. Ct. at 1216. *But see* Dean Witter v. Trimble, No. 119930/94, 1995 N.Y. Misc. LEXIS 402, at *7 & n.4 (Sup. Ct. June 13, 1995) (Solomon, J.) (stating in dicta that a state court would “not be bound to interpret” an identical agreement “the same way as the U.S. Supreme Court did in *Mastrobuono*” because contract interpretation is a state court’s function). Although many practitioners applaud Justice Solomon’s resolve, even those representing the securities industry doubt that she would ever be upheld on appeal if she ruled that an agreement identical to the one in *Mastrobuono* did not allow for punitive damages in arbitration. Telephone Interviews with in-house and outside counsel to brokerage firms (Aug. & Sept. 1995).

133. 115 S. Ct. at 1217.

134. *Id.* at 1219.


tion of Mastrobuono is that it will keep the attorneys for the securities industry very busy.

First, the Mastrobuono decision will necessitate the review of all arbitration agreements. The brokerage firms will change their agreements to explicitly limit punitive damages.137 Second, plaintiffs’ attorneys are likely to claim that the Mastrobuono decision proves that Garrity v. Lyle Stuart is preempted by the Federal Arbitration Act. Although the ruling in Mastrobuono was limited to an outdated Shearson Lehman Hutton agreement,138 the securities industry will be answering punitive damage claims in arbitration pleadings for some time to come. Additionally, Mastrobuono will cause a surge in the number of amended arbitration pleadings. As plaintiffs’ attorneys see an opening for an award of punitive damages, they will amend their claims and try to get punitive awards while the door is still open. Practitioners should already recognize that arbitration is a private process governed largely by the agreement between the parties. Accordingly, private parties will always be able to write provisions into an agreement which can at least mitigate the effects of legislation, judicial intervention, or both.139

Even before the Supreme Court granted certiorari in Mastrobuono,140 the securities exchanges and legislatures (both federal and state) began to explore the possibility of initiating legislation to prevent employers from limiting damages or, for that matter, compelling arbitration of employment disputes.141 Because of its limited

137. See Siegel, supra note 92, at 4; Williams, supra note 113, at 53. See generally infra notes 151-57, 164 and accompanying text. But see infra note 165 and accompanying text (discussing exchange rules which could limit the ability of brokerage firms to change their agreements).

138. Smith Barney, the firm that bought Shearson’s retail brokerage division, has already changed its client agreement to explicitly define the implications of choosing “the laws of the State of New York” as including “the law of New York regarding damages recoverable in arbitration.” Client Agreement, supra note 65, ¶ 7. Although such an agreement would probably satisfy the standards established in Mastrobuono, plaintiff’s attorneys are likely to argue that the agreements are substantially similar to the agreement in Mastrobuono in an effort to get arbitrators to award punitive damages.

139. One of the main criticisms of employment-related pre-dispute arbitration agreements is that the agreements are not negotiated. See supra note 51 and accompanying text. Therefore, the fear is that the employers will start to include specific provisions to limit the arbitrators’ authority: See infra notes 151-53 and accompanying text.

140. 115 S. Ct. 305 (1994).

141. Bills have been proposed to prohibit agreements that limit an arbitrator’s authority, to allow arbitrators to award punitive damages in all employment-related disputes, to overturn Gilmer, and to prohibit the arbitrability of Title VII claims when the plaintiff objects. See infra notes 202-05 and accompanying text.
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scope, the Mastrobuono decision is not likely to prevent or impede legislative, administrative, or private action. As such, practitioners must be aware that their work has just begun and academics must be prepared to argue for and against the intervening actions by private parties that will alter the nature of the debate. Over the coming years, many steps will be taken to affect the arbitral process; the legal community must be prepared for anything and everything.

B. Private Mechanisms for Change

1. Exchange Rule-Making

The reaction of the self-regulatory organizations—the stock exchanges—can be swift. For example, the NASD revised its rules to eliminate the impact of Farrand v. Lutheran Brotherhood within months after Farrand appeared to invalidate the arbitrability of employment disputes. The effects of Mastrobuono or proposed legislation are likely to be mitigated by a similarly quick reaction by the NASD and the other exchanges. Although the exchanges do not rigidly follow the lead of the SIA, even before the Mastrobuono decision was issued, the SIA was pressuring the exchanges to change their rules to explicitly prohibit arbitrators from awarding punitive damages. That pressure will assuredly increase as the implications of Mastrobuono are felt. In the short term, some arbitrators will issue awards for punitive damages. How the securities exchanges will react

142. Not waiting for the impact of Mastrobuono, some private parties have already taken steps to limit arbitrators' authority. See infra notes 154-67 and accompanying text.
143. See, e.g., Katsoris, supra note 22, at 1116.
144. 993 F.2d 1253, 1255 (7th Cir. 1993) (holding that employment disputes were not arbitrable because NASD arbitration rules did not specify the arbitrability of such disputes); see McMahan Sec. Co. v. Forum Capital Mkts. L.P., 35 F.3d 82, 88-89 (2d Cir. 1994). Courts have subsequently held that the original NASD rules did cover employment disputes or that the new rules should be applied retroactively. See, e.g., F.N. Wolf & Co. v. Bowles, 610 N.Y.S.2d 757 (Sup. Ct. 1994).
146. Even before the decision was issued by the Court in Mastrobuono, the NASD was already evaluating its options with regard to punitive damages. See, e.g., NASD Notice supra note 61, at 319.
147. See infra note 151. See generally SIA Opposition, supra note 102; SIA Assails Report on Legitimacy of Punitive Damage Awards, SEC. Wk., Aug. 23, 1993, at 3 [hereinafter SIA Assails].
should be evident in the coming years.

2. Contractual Prohibition of Punitive Damages

The assumption has been made that if state laws which prohibit punitive damages were overturned or rendered moot by a decision like Mastrobuono, punitive damages would be available in arbitration. The lower courts' disagreement over the implications of the silence of an arbitration agreement on the issue of punitive damages only delayed action by contracting parties. Now that Mastrobuono has unequivocally stated that silence in an agreement means that punitive damages may be awarded by an arbitrator, the brokerage firms will act quickly.

Impatient for judicial resolution, the securities dealers have begun to pressure the exchanges, change their agreements, and take other steps to limit arbitrators' authority to award punitive damages. One firm has explicitly defined the implications of New York choice of law, while another has included language in its alternative dispute resolution policy to preclude arbitrators from awarding punitive damages in any cases whatsoever. Because courts will generally enforce restrictive provisions in arbitration agreements, the door is open for the securities dealers to act. Arbitration agreements are

148. See generally Friedlander, supra note 8, at 17, 24; Franklin, supra note 12, at 5 (reporting on the New York County Lawyers' report).
149. See Ware, supra note 3, at 537-39 (discussing the varying decisions, some that infer an arbitrator's authority to award punitive damages, and others that refuse to enforce awards unless the agreement explicitly contemplated such an award).

One plaintiff's attorney assumes that the NASD members will get their way and force the exchange to change their rules, but he predicts that the industry will likely get such a move "rammed down their throats." Punitive Battle, supra note 101, at 8; see also Rooney, supra note 92, at 20 (quoting a plaintiff's attorney as suggesting that "if the industry wishes 'to restrict the arbitrators' power to grant punitive damages, they should do so explicitly in the arbitration agreement'). The Supreme Court would probably agree that parties should explicitly include their wishes if they want to preclude an award of punitive damages. Mastrobuono, 115 S. Ct. at 1216.

152. Smith Barney's agreement is now "governed and construed in accordance with the laws of the State of New York, including, but not limited to, the law of New York regarding . . . damages recoverable in arbitration . . . ." Client Agreement, supra note 65, ¶ 7.
153. "The arbitrator shall not have the authority to award punitive damages to either party . . . ." Brokerage Policy, supra note 69, § C(20)(B). Similar limiting agreements are frequently used in consumer transactions. See Rosmarin, supra note 26, at 1620.
154. Parties "may limit by contract the issues which they will arbitrate." Mastrobuono,
enforceable even if they include provisions which limit the arbitrator’s ability to award punitive damages. In Szuts v. Dean Witter Reynolds, Inc., the Eleventh Circuit Court of Appeals held that:

[B]ecause arbitration is a creature of contract, the parties, when incorporating any set of arbitration rules by reference in an arbitration agreement, are free to include provisions in conflict with certain provisions of rules incorporated by reference; the specific provisions in the arbitration agreement take precedence and the arbitration rules are incorporated only to the extent that they do not conflict with the express provisions of the arbitration agreement.

In an earlier decision, while attempting to mitigate the effects of Garrity, the Eleventh Circuit admitted that “of course, the Arbitration Act would not override a clear provision in a contract prohibiting arbitrators from awarding punitive damages.” Now that the Supreme Court has shown an inclination to permit arbitrators to award punitive damages notwithstanding state law, the industry as a whole and its individual members will move to include provisions in all of their agreements which will explicitly prohibit arbitrators from awarding punitive damages. Given that industry agreements, and employment agreements in general, are rarely negotiated, the new restrictive provisions would quickly become the norm were it not for the NASD Rules of Fair Practice. Restrictive provisions will become the norm for businesses that are not constrained by exchange rules which


155. See, e.g., Mastrobuono, 115 S. Ct. at 1216; J. Alexander Sec., Inc. v. Mendez, 21 Cal. Rptr. 2d 826, 832 (Ct. App. 1993) (holding that federal preemption allowed punitive damages, but implying that J. Alexander would have prevailed if a specific punitive exclusion were included in the agreement), review denied, No. S035102, 1993 Cal. LEXIS 6354 (Nov. 24, 1993), and cert. denied, 114 S. Ct. 2182 (1994). See generally Ware, supra note 3, at 535-36. With regard to the constraints of New York’s Garrity rule, even the Second Circuit, which has repeatedly upheld Garrity, stated, in dicta, that if a contract specifically provided for punitive damages, it would, as a matter of law, nullify Garrity. See Fahnstock & Co. v. Walmann, 935 F.2d 512, 518 (2d Cir.), cert. denied, 502 U.S. 924 (1991), and cert. denied, 502 U.S. 1120 (1992); supra note 131.

156. 931 F.2d 830 (11th Cir. 1991).
157. Id. at 831-32.
159. “Arbitration agreement terms expressly addressing punitive damages may be becoming more common.” Ware, supra note 3, at 536 n.33 (citing James W. Durham et al., ADR More Than a Means of Resolving Disputes, CORP. LEGAL TIMES, May 1994, at 1).
impact on their ability to control the arbitral forum.  

Initially, the securities industry chose New York choice of law to utilize Garrity and to avoid the unpredictability of jury awards. The entire industry has successfully used state law as a shield against many claims and damage awards. The securities industry chose New York law to enjoy the benefits that Garrity provides; now that "New York law" without other contractual language can no longer provide protection, the industry will explicitly protect itself from punitive damages by drafting agreements that contain limiting provisions.

In response to the inclusion of language in pre-dispute agreements that would limit punitive damage awards, a number of arbitral bodies adopted rules which prohibit arbitration agreements that limit an arbitrators' authority in such a way. Notably, the rules of the

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160. Many commentators who are opposed to the enforcement of pre-dispute employment arbitration agreements undoubtedly believe that such a reaction by the industry is unfair. See supra note 26 and accompanying text. Fair or not, practitioners must recognize that such alternatives are currently available and will be utilized wherever possible.


162. Employers choose arbitration because arbitrators are less likely to award high damage awards. See Katsoris, supra note 22, at 1140 n.149; Piskorski & Ross, supra note 26, at 209; Giltenan, supra note 12, at 196; Holmes, supra note 44, at A1, B6; Novack, supra note 44, at 125; Seiberg, supra note 44, at 2 (quoting a bank spokesman); see also Franklin, supra note 12, at 5-6 (reporting on a survey finding that punitive awards by arbitrators are rare); Opportunity Knocks, INVESTORS’ BUS. DAILY, Dec. 13, 1994, at A4 (implying that the construction firm of Brown & Root chose arbitration specifically to "avoid high punitive damage awards"); Punitive Battle, supra note 101, at 8 (pointing to an increase in punitive awards by arbitrators over the six month period ending June, 1992). But see Neil Vidmar, Are Juries Competent to Decide Liability in Tort Cases Involving Scientific Medical Issues? Some Data From Medical Malpractice, 43 EMORY L.J. 885, 907 (1994) (claiming that data does not support the hypothesis that juries award larger punitive damage awards than arbitrators).


164. See generally Anthony M. Sabino, Awarding Punitive Damages in Securities Industry Arbitration: Working for a Just Result, 27 U. RICH. L. REV. 33, 68-70 (1992) (suggesting that firms should include punitive damage exclusions to avoid the debate over choice of law). In light of Mastrobuono, many firms will probably be taking Mr. Sabino’s advice.

other arbitral bodies do not specify the penalty for non-compliance with the rules related to limiting an arbitrator's authority. As the parties in Mastrobuono realized, however, it is better to resolve such a conflict explicitly in the arbitration agreement. There is little doubt that Shearson would have prevailed had the agreement specifically prohibited punitive damages and explicitly superseded the NASD arbitration rules.

C. Judicial/Legislative Alternatives

1. Mastrobuono: A Poor Example of Judicial Resolution

Although many commentators had assumed that the Supreme Court would resolve the circuit split, the Court in Mastrobuono proved the soothsayers wrong. The Court did, however, illustrate that any attempts at judicial resolution will have a great impact on the business community. In an amicus brief submitted to the Court, the Securities and Exchange Commission urged the Supreme Court to look to the specific wording of the contract at bar. During oral arguments, the Justices of the Supreme Court spent a great deal of time discussing this very issue. As such, it is not surprising that...
the Court ruled the way it did—reviewing the contract *de novo* and finding ambiguities. Practitioners already know that contract formation can be critical. To avoid uncertainty, parties to arbitration agreements will have to make sure that their agreements with regard to punitive damages are clear and explicit.

In *Mastrobuono*, the Supreme Court held that the arbitration agreement between the parties was ambiguous on three fronts. First, the Court held that the phrase, “the laws of the State of New York” was insufficient, by itself, to be an unambiguous prohibition against the arbitrator awarding punitive damages. Second, the Court construed the agreement against the drafter, Shearson, because of an internal conflict between the language of the agreement and the arbitral rules. Finally, the Court upheld the punitive damages award by the arbitrator when it “harmonize[d]” the internal conflict and read the agreement to have one meaning. Although the Court could have, and possibly should have, deferred to the arbitrator’s contract interpretation, it chose instead to review the agreement itself and leave the greater questions of arbitral authority unanswered.

Some lower courts have held that arbitrators should decide all conflicts between the contract, the arbitration rules and the law because of the federal policy favoring arbitration. Others have held

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provisions, “the ambiguity should be resolved against the drafting party,” and citing Baker v. Sudick, 208 Cal. Rptr. 676, 681 (Ct. App. 1984)).

171. See id.
172. This could be called the “and I really mean it” philosophy of contract formation. As opposed to saying “this contract is governed by New York law,” the contracts will read “this contract is governed by New York law, which prohibits the arbitrator from awarding punitive damages; furthermore, punitive damages will be unavailable under this contract, notwithstanding any changes in New York law or any issues of federal preemption which might seem to validate such an award.” See generally Louis B. Kimmelman & Bonnie L. Hobbs, O’Melveny & Myers, *Punitive Damages in Arbitration* 4-5 (Mar. 24, 1995) (on file with the Hofstra Law Review); C. Evan Stewart, *No Longer 'Simple' 'Quick' 'Informal' or 'Inexpensive',* N.Y. L.J., June 15, 1995, at 5, 8.

174. Id. at 1217-18.
175. Id. at 1219.
176. Id.
177. The Court probably left many practitioners questioning whether the decision it reached would have been more appropriate for the Supreme Court of New York. In New York, the supreme court is the lowest civil level in the state court system and is the court where factual issues are normally determined.

178. See 115 S. Ct. at 1217 n.4.
179. See, e.g., Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378, 1388 (11th Cir. 1988); J. Alexander Sec., Inc. v. Mendez, 21 Cal. Rptr. 2d 826, 832 (Ct. App. 1993), review
that if the contract does not specify the availability of punitive damages, an award of such damages is beyond the authority of the arbitrator. Unfortunately, the Court's decision in Mastrobuono does not address any of these larger issues about the arbitrability of punitive damages. Practitioners had already started changing their agreements in advance of the Mastrobuono decision. By using the ambiguity in the agreement as the main focus of its decision, the Court's decision resolves nothing: the debate will continue. The Court merely guaranteed that every minor ambiguity in arbitration agreements will spark litigation and ensured the continued employment of many arbitration practitioners.

As many commentators predicted, Mastrobuono does not provide clear guidance to the lower courts. State courts reviewing challenges to arbitral awards of punitive damages under the FAA may not necessarily reach the same conclusion as did the Supreme Court concerning the meaning of a New York choice-of-law provision. For instance, a New York court presented with the same facts as Mastrobuono could find, as a matter of contract construction, that the inclusion of a New York choice-of-law provision in a contract incorporates New York law with respect to the power of arbitrators to award punitive damages.

As parties begin to use the Mastrobuono decision to try to limit an arbitrator's power to award punitive relief or to challenge a punitive award, federal and state courts will soon have to confront these unresolved issues.

Already, Mastrobuono has provided evidence that attempts to resolve complex issues through the courts may fail. Although the majority of post-Mastrobuono cases that are on-point with regard to punitive damages have followed the Court's lead, several New

181. See supra notes 152-53 and accompanying text.
183. See supra note 135 and accompanying text.
184. KIMMELMAN & HOBBS, supra note 172, at 5 (footnote omitted).
185. E.g., Davis v. Prudential Sec., Inc., 59 F.3d 1186, 1189 (11th Cir. 1995) (affirming a punitive award because the arbitration clause was "virtually identical to the clause at issue
York cases have found room to distinguish situations from that in *Mastrobuono*. In *Dean Witter Reynolds, Inc. v. Trimble,* Trimble filed a claim for punitive damages in an American Stock Exchange arbitration pursuant to the "AMEX Window" because there was no arbitration agreement between the parties. Distinguishing the case from *Mastrobuono*, the Trimble court dismissed the punitive damages claim and held that, in New York, arbitrators are not empowered to award punitive damages. The court proclaimed in dicta that:

> Even if the instant case involved a standard-form contract with the identical New York choice of law clause, this court would not be bound to interpret it in the same way as the U.S. Supreme Court did in *Mastrobuono*, since the interpretation of contracts is a matter of state law.

In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Levine,* the administratrix of an estate filed a claim against Merrill on behalf of the estate for churning a brokerage account, failure to supervise, and a number of other acts of malfeasance. The court dismissed the causes of action based on the relevant statute of limitations but asserted that "both these claims [for punitive damages and attorney's fees] are barred in arbitration under New York law, which is applicable by virtue of the choice-of-law clause, and because [the brokerage client] resided in New York.”

In *Smith Barney, Inc. v. Sacharow,* the court highlighted a way to distinguish some agreements from that which was at issue in

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188. Id. at *5-7.
189. Id. at *7 n.4.
191. Id. (citation omitted).
Mastrobuono. While attempting to reconcile Mastrobuono with Smith Barney, Harris, Upham & Co. v. Luckie,193 a recent decision by the New York Court of Appeals, the Sacharow court held that Mastrobuono would not necessarily apply if the arbitration agreement at bar provide[d] that New York law governs "the agreement and its enforcement" (emphasis in original). Therefore, as Chief Judge Kaye noted in her occurrence [sic] [in Luckie] "the parties can fairly be understood to have agreed that all of New York arbitration law (including the provisions of CPLR Article 75 which allow a party to first litigate statute of limitations issues in court) would apply."194

Mastrobuono mandated the availability of punitive damages because the agreement at issue was too vague.195 If language regarding an "agreement and its enforcement" is sufficiently explicit, then language that talks about the "rights and liabilities" of the parties should also be sufficiently distinct from the agreement in Mastrobuono.196 Unfortunately, although many expected Mastrobuono to resolve the debate over punitive damages, the Court's decision made it abundantly clear that judicial resolutions will not always provide complete and understandable answers to legal problems. As such, in the debate over punitive damages, the short-term solutions are likely to come in other arenas.

2. Prohibit Arbitration of Employment Disputes: The Plaintiff Bar's Dream197

If the Supreme Court broadens the "employment contract" exclusion of the FAA, many employment disputes may not be arbitrable.198 In theory, such a decision by the Court would invalidate any pre-dispute arbitration agreements made between employers and employees. This assumption is flawed, however, because the Supreme Court has already suggested that independent agreements with a third

197. Currently, virtually all employment disputes are arbitrable. See supra notes 36-43 and accompanying text. This section is included as a general guide to the practitioner and as an outlook to the future.
198. 9 U.S.C. § 1 (1988); see supra notes 76-81 and accompanying text.
party securities exchange do not qualify as employment agreements.\textsuperscript{199} There is nothing to prevent employers in other industries from requiring registration with an industry association to parallel the third party U-4 registration agreements that the Court pointed to in \textit{Gilmer} to avoid having to confront the section 1 exclusion.\textsuperscript{200} Nonetheless, the exclusion has not been applied by the lower courts and is unlikely to be broadened any time soon.\textsuperscript{201}

Several legislative initiatives over the past few years have attempted to limit the arbitrability of employment disputes.\textsuperscript{202} On the state and federal level, politicians have been concerned about the potential for coercion in the signing of mandatory pre-dispute arbitration agreements. In 1994, legislation was introduced in Congress to prohibit employers from requiring employees to sign arbitration agreements as a condition of employment.\textsuperscript{203} Both the House and the Senate bills would have invalidated any pre-dispute arbitration agreements for claims made under Title VII of the Civil Rights Act, the Age Discrimination and Employment Act, and the Americans with Disabilities Act and for claims made against government contractors.\textsuperscript{204} The House bill went further, having included claims under

\begin{itemize}
\item \textsuperscript{199} See \textit{Gilmer v. Interstate/Johnson Lane Corp.}, 500 U.S. 20, 25 n.2 (1991) (holding that a broker's U-4 registration agreement with a securities exchange which required arbitration of all employment disputes was not a contract of employment between the broker and his firm).
\item \textsuperscript{200} For example, the construction firm of Brown & Root could help form an industry-wide construction organization. Brown & Root could then require all its employees to register with the organization as a condition of employment. Similar to the U-4 Application, the construction industry registration form would require the arbitration of all disputes between members, including employment disputes. The agreement would easily fit in the loophole created by the language of the Court in \textit{Gilmer}.
\item \textsuperscript{201} See supra notes 76-81 and accompanying text. Although \textit{Gilmer} inspired a lengthy dissent on this issue, one of the dissenters was the late Justice Thurgood Marshall. \textit{Gilmer}, 500 U.S. at 36 (Stevens, J., dissenting, joined by Marshall, J.).
\item In many cases, employers could still rely on state arbitration statutes to enforce their employment agreements, bypassing the FAA. See \textit{Bompey & Pappas}, supra note 26, at 203; Bernstein & Ramsfelder, \textit{supra} note 38, at 17 n.10 (describing the arbitration statutes in New Jersey and 15 other states).
\item \textsuperscript{202} Federal legislation would be necessary to stem the tide of employment dispute arbitration. \textit{"Gilmer makes it virtually impossible, as a practical matter, to establish inherent conflict under the congressional intent standard. Unless a congressional statute's text or legislative history establishes an exception to the FAA mandate, claims under the statute will almost inevitably be arbitrable in accordance with the mandate."} Abrams, \textit{supra} note 22, at 551.
\item \textsuperscript{204} See H.R. 4981, 103d Cong., 2d Sess. §§ 2-6, 9 (1994); S. 2012, 103d Cong., 2d
the Equal Pay Act and the Family and Medical Leave Act.\textsuperscript{205} The recent changes in the political make-up of Congress, however, have put these Democratic-sponsored ideas in jeopardy.

The goals of most of the recent legislative initiatives, however, are inapposite to the goals of the FAA.\textsuperscript{206} In addition, the Civil Rights Act of 1991 includes language encouraging arbitration, bolstering the federal policy favoring arbitration and unburdening the judiciary.\textsuperscript{207} The Equal Employment Opportunity Commission is already looking to alternatives like arbitration to help alleviate some of the pressure of its backlog.\textsuperscript{208} If the proposed prohibition on the arbitrability of employment disputes were successful, the administrative agencies and the judiciary would incur an even greater burden.\textsuperscript{209}

Any federal legislative initiatives will most likely be accomplished through changing the individual anti-discrimination statutes and not the FAA itself.\textsuperscript{210} The courts have generally interpreted the FAA as favoring arbitration "unless Congress itself has evinced an intention to preclude a waiver of judicial remedies."\textsuperscript{211} To change the FAA would upset the general philosophy behind the statute, which favors arbitrating all issues. In addition, a change in the FAA would not prevent the enforcement of an arbitration agreement under state law.\textsuperscript{212}

\textsuperscript{205} See H.R. 4981, 103d Cong., 2d Sess. §§ 7-8 (1994).
\textsuperscript{208} See Novack, supra note 44, at 124.
\textsuperscript{209} This added burden is suggested as one reason why the courts may be reluctant to remove cases from arbitration, notwithstanding public policy concerns. The concern of collapsing the overburdened judiciary may take precedence over the public policy concerns of arbitrating employment disputes, with or without punitive damages. Telephone Interview with D. Scott Wise, Davis, Polk & Wardwell, attorney for defendant in Mulder v. Donaldson, Lufkin & Jenrette, 611 N.Y.S.2d 1019 (Sup. Ct. 1994), aff'd, 623 N.Y.S.2d 560 (App. Div. 1995) (Mar. 7, 1995) [hereinafter Wise Interview].
\textsuperscript{210} This is suggested by Abrams, supra note 22, at 578-84; see, e.g., H.R. 4981, 103d Cong., 2d Sess. §§ 2-9 (1994); S. 2012, 103d Cong., 2d Sess. §§ 2-6 (1994).
On the state level, the issue of pre-dispute arbitration agreements is being discussed. However, even in California, the leaders are not necessarily in favor of abandoning the entire alternative dispute resolution process for employment disputes.

Some have suggested that when punitive damages are at issue and are unavailable, the plaintiff should be allowed to opt out of the arbitration altogether, even if employment disputes are generally arbitrable. Currently, the only alternative utilized by the courts is to compel arbitration and to deny enforcement of any punitive awards. If a plaintiff is permitted to remove all arbitrable claims by raising a single claim for punitive damages, forum shopping would become prevalent, as punitive damages claims would be included in complaints solely to avoid the arbitral forum. The availability of such an alternative would violate the general principles of the FAA favoring arbitration, but since it does not seem that the Congressional initiatives will succeed, employment dispute arbitration is here to stay.

3. Hearing Punitive Awards Separately: The Bifurcated Proceeding

In a landmark decision in securities arbitration, the Supreme Court in Dean Witter Reynolds, Inc. v. Byrd ruled that arbitration proceedings can be bifurcated from judicial proceedings when both arbitrable and non-arbitrable claims are involved. Byrd involved two claims against a broker, one for breach of contract and the other for violations of the Securities and Exchange Act of 1934 (the

__generally Bales, supra note 26, at 1910-12.__

213. See, e.g., KY. REV. STAT. ANN. § 336.700 (Baldwin Supp. 1994) (prohibiting employers from requiring the execution of an arbitration agreement as a condition of employment). Any state statute, however, may confront serious federal preemption problems.

214. While the courts in California seem to favor judicial resolution, its governor has proposed the increased use of alternative dispute resolution and the limitation of punitive damages. See Dana Wilke, Governor Asks Steps for Revival of Economy, SAN DIEGO TRIBUNE, Jan. 10, 1995, at A-1.


218. Id. at 216-17. The implications of Byrd have been analyzed more recently. See Stifel, Nicolaus & Co. v. Woolsey & Co., No. 94-6122, 1994 U.S. App. LEXIS 36090 (10th Cir. Dec. 21, 1994) (holding that a state court action could proceed, despite the claim by one party that NASD arbitration was required); American Shipping Line v. Massan Shipping Indus., 885 F. Supp. 499, 502-03 (S.D.N.Y. 1995); Schumacher, supra note 114, at 471-74 (discussing Byrd and the bifurcation issue).
At the time, private causes of action based on violations of securities laws were not arbitrable. The Court held that the '34 Act claim could be heard separately even though virtually identical issues were subject to arbitration, notwithstanding the inefficiency created by holding two hearings on such similar matters.

Recently, courts have found little reason to bifurcate claims, because virtually all disputes are now arbitrable. There is little question, however, that non-arbitrable claims may proceed before a judge simultaneously with arbitrable claims proceeding before an arbitrator. This presents an apparently simple solution to any prohibition against arbitrators awarding punitive damages: hear the issue of punitive damages in a court while the rest of the claim is heard in arbitration. In fact, the NASD proposed this bifurcated scenario as an alternative to regularly disallowing punitive damages.

Bifurcating punitive damage claims into two proceedings, however, presents some serious problems. First, split proceedings would defeat the basic purposes of having a single, complete, limited-review arbitral process. Second, the bifurcation alternative fails to meet

219. See Byrd, 470 U.S. at 214-16 (discussing the arbitrability of the '34 Act, 15 U.S.C. §§ 78j(b), 78o(c) & 78t (1988)).


221. See Byrd, 470 U.S. at 217.

222. See supra notes 25-33 and accompanying text (non-employment disputes); supra notes 36-43 and accompanying text (employment disputes).


224. See NASD NOTICE, supra note 61, at 333 (proposing bifurcation, but seemingly with both proceedings heard in arbitration).

225. See United States Fidelity & Guar. Co. v. DeFluiter, 456 N.E.2d 429, 432-33 (Ind. Ct. App. 1983) (holding that further proceedings would violate the principles of res judicata and collateral estoppel); Stipanowich, supra note 91, at 1000; Ware, supra note 3, at 541 n.47; SIA Assails, supra note 147, at 3; SIA Opposition, supra note 102, at 1184; Wise Inte-
the basic requirements for withstanding a motion to dismiss for failure to state a claim.\textsuperscript{226} Since punitive damages (or damages in general) are insufficient to establish an independent cause of action,\textsuperscript{227} the claim for punitive damages cannot be independently maintained in court.\textsuperscript{228} Notwithstanding the apparent impossibility of conducting such a proceeding, a number of courts have asserted the ability to hold bifurcated hearings for punitive damages.

a. The New York Courts—Unapplied Dicta\textsuperscript{229}

A number of courts in New York have compelled the arbitration of discrimination claims while reserving the right to rehear and decide View, supra note 209 (arguing that such a proceeding would make sure that the benefits of arbitration were "reduced to a nullity"). But see Katsoris, supra note 22, at 1140 (suggesting that judicial review of punitive damages "would not be too disruptive of arbitration's quest for speed and economy"); Franklin, supra note 12, at 6 (reporting on a proposal by the New York County Lawyers' Association that would provide for judicial review of punitive damage awards).

\textsuperscript{226} See Fed. R. Civ. P. 12(b)(6). Speaking at a symposium sponsored by the New York Stock Exchange, Paul Dubow, an attorney for Dean Witter, commented on this issue:

I don't know how we could have a contract, and perhaps you've thought of a way . . . which provides for an appeal to the courts, because the statutes don't allow that. You could provide for a trial de novo, I believe. You could have a contract that provided for a trial de novo in court if a punitive damage award was rendered, but you can't provide, as far as I can figure out, for an appeal. You have to amend the statutes to do that, and that may be a major process.

\textit{NYSE Symposium, supra} note 104, at 1665.

\textsuperscript{227} See Wiltman v. Fahnestock & Co., 792 F. Supp. 31, 32-33 (E.D. Pa. 1992), aff'd, 989 F.2d 490 (3d Cir. 1993); Kessler, No. 84 Civ. 282-CSH, slip op. at *1 (S.D.N.Y. Sept. 10, 1984) (available on LEXIS); Westwood Inc. v. Cal Togs, Inc., No. 82 Civ. 0584 (GLG), slip op. at *1 n.1 (S.D.N.Y. Sept. 30, 1982) (available on LEXIS); Diker v. Cathray Constr. Corp., 552 N.Y.S.2d 37, 38 (Sup. Ct. 1990) (holding "that there is no separate cause of action to recover punitive damages"); see also, Villinger/Nicholls Dev. Co. v. Meleyco, 37 Cal. Rptr. 2d 36, 37 (Ct. App. 1995) (holding that a proceeding to confirm an arbitration award is not an "action" where added claims for punitive damages can be asserted); United States Fidelity & Guar. Co., 456 N.E.2d at 432 (prohibiting "claims for damages arising out of the same incident [from being brought] in piecemeal fashion in successive suits").

\textsuperscript{228} State courts in New Mexico have not applied this basic principle of pleadings. See \textit{infra} notes 252-62 and accompanying text.

\textsuperscript{229} This discussion of New York cases should not be confused with the Supreme Court's reference to "New York's bifurcated approach" in \textit{Mastrobuono}. Mastrobuono v. Shearson Lehman Hutton, Inc., 115 S. Ct. 1212, 1219 (1995). The Court was referring to the New York's apportionment of power between arbitrators and the courts with regard to their respective abilities to award punitive damages, not to the bifurcation discussed in this section of the Note.

The "unapplied dicta" is the language used by some New York courts which proclaim the authority to bifurcate a claim for punitive damages. To date, no bifurcated bench trial has ever occurred; as such, the courts' assertions are mere dicta.
the issue of punitive damages separately. Although one commentator recently implied that the bifurcated proceeding "has occurred in New York," the applicable case law does not appear to support this position. No New York court has ever actually had a bifurcated court proceeding in this context.

Although several New York courts have asserted the ability to bifurcate, to date, no bench trials have ever occurred. For example, in DiCrisci v. Lyndon Guaranty Bank, a judicial hearing on punitive damages was unnecessary because the plaintiff failed to obtain any compensatory damages at arbitration and chose to abandon her action for punitive damages. In American Transit Insurance Co. v. Associated International Insurance Co. an order to compel arbitration was issued on December 15, 1994 containing vague language which could arguably support bifurcation. However, it is likely that there has not yet been an opportunity to address the bifurcation issue because the case has apparently not yet gone to trial. Singer v. Salomon Brothers was settled prior to the arbitration hearing, rendering the judges' bifurcation dicta moot. Arbitration is still pend-


Commentators have also presented the bifurcated award proceeding as a simple solution. See Ware, supra note 3, at 541 n.47 (asserting that "[a]n arbitration agreement could conceivably deny the arbitrator the power to award punitive damages, but preserve the right to recover them in court"); Wilson, supra note 61, at 162-63.

231. Ware, supra note 3, at 541 n.47.


235. "Actions may be stayed temporarily pending arbitration proceedings where the resolution of the issues in the latter may also resolve and render academic issues in the former." 621 N.Y.S.2d at 3 (quoting Corbetta Constr. Co. v. George F. Driscoll Co., 233 N.Y.S.2d 225, 228 (App. Div. 1962)).

236. Although the author made several attempts to contact both parties, the status of the case is still undetermined.


238. Telephone Interview with Theodore Rogers, Sullivan & Cromwell, counsel to
ing in *Chisolm v. Kidder, Peabody*,\(^{239}\) effectively leaving the courts far from accepting an isolated claim for punitive damages from Mr. Chisolm.\(^{240}\)

The one case which is most likely to resolve the bifurcation debate is *Mulder v. Donaldson, Lufkin & Jenrette*.\(^{241}\) In *Mulder*, the trial judge accepted a claim for punitive damages and denied a motion to dismiss, holding that the situation justified an exception to the procedural rule that would normally prevent a damages claim from being maintained as an independent cause of action.\(^{242}\) In a lengthy and confusing decision, the appellate division in New York held that a punitive damages claim could not be maintained separately, but it could be attached to a substantive claim “even though [the] plaintiff is precluded from recovering compensatory damages on that substantive cause of action.”\(^{243}\) In light of *Mastrobuono*, Donaldson, Lufkin & Jenrette filed a motion to compel arbitration on the punitive damages claim. If the trial judge rules that punitive damages are now arbitrable,\(^{244}\) *Mulder* will join its brethren as unapplied dicta.\(^{245}\)

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\(^{240}\) Telephone Interview with Richard Kelly, in-house counsel for Kidder, Peabody, (Sept. 8, 1995). Mr. Kelly indicated that although the case was headed to arbitration, a date had not been set. *Id.*


\(^{242}\) “Thus, the usual rule on punitive damages does not apply and plaintiff may maintain the first cause of action for punitive damages.” *Mulder*, 611 N.Y.S.2d at 1022; *see Whistleblowing Brokerage Employee May Seek Punitive Damages for Firing*, 26 Sec. Reg. & L. Rep. (BNA) 836, 837 (1994).

\(^{243}\) 623 N.Y.S.2d at 565.

\(^{244}\) The decision of Judge Schackman was pending when this Note went to press.

\(^{245}\) Although *Mulder* is not necessarily any more important that the other bifurcated cases, the unique road that the case traveled deserves some mention. Both sides have acted ethically, but the intervening decision in *Mastrobuono* created an advocacy shift by the parties which provides for an interesting, if not humorous, legal anecdote.

*Mulder*, alleging wrongful termination, filed for arbitration against his former employer, including a claim for punitive damages. At the arbitration hearing, Donaldson, Lufkin & Jenrette (“DLJ”) argued that the arbitrator was not empowered to award punitive damages because of the New York choice-of-law in the applicable arbitration agreement. Mulder argued that punitive damages were, or should be, available in the arbitral forum. The arbitrator
Regrettably, the general lack of appellate review of these cases has left a glaring mistake of law asserted in dicta unchallenged.\textsuperscript{246} Until a bench trial is held and the court's assertion of authority to hear a claim solely for punitive damages is challenged, the issue will remain unresolved. If \textit{Mulder}'s phantom cause of action theory becomes prevalent or the general rules of pleadings are changed, punitive damages could be maintained as a separate cause of action. As much as the brokerage firms would like to see punitive damages kept out of arbitration, a far worse fate would be to have \textit{de novo} trials on punitive damages for every case that is lost in arbitration.\textsuperscript{247} Unfortunately, "the process of meting out punishment for wrongdoing cannot be divorced from the process of deciding whether wrongdoing occurred."\textsuperscript{248} "As a practical matter, a finding of bad faith [by an arbi-
tator] would [be] useless to a court in deciding upon the amount of punitive damages to be awarded, and would not [advance a plaintiff’s] claim for punitive damages one whit. As such, bifurcation would create significant efficiency problems, but this solution could provide an answer to the civil rights dilemma described later in this Note. The dilemma occurs when a civil rights claim is compelled to arbitration where punitive damages can not be awarded. Without bifurcation, a court compelling such a claim to arbitration, in effect, dismisses the claim for punitive damages. Courts will be caught between the pro-arbitration philosophy of the FAA and the provisions of the Civil Rights Act which provide for the availability of punitive damages.

b. New Mexico Goes Splitsville

New Mexico has explicitly done what the court in Mulder suggests for New York. The New Mexico Supreme Court ruled that a cause of action may be sustained even if it only contains a claim for punitive damages. In *Stewart v. State Farm Mutual Automobile Insurance Co.*, the plaintiff was awarded $3,500 in compensatory damages from an arbitrator presiding over a disputed insurance claim. The arbitrator recognized that he was unable to award punitive damages, but suggested “that if a proper court found that punitive damages could be awarded,” then “the amount should be $25,000.” The New Mexico Supreme Court validated the lower court’s use of the arbitrator’s “advisory” opinion by confirming an award of $15,000 for punitive damages. Although the court did

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249. *Id.*

250. See *infra* notes 272-311 and accompanying text.


254. *Id.* at 1375. State Farm paid the compensatory damages before the case was appealed. *Id.*

255. *Id.* New Mexico is similar to New York in that arbitrators are unable to award punitive damages. “An arbitrator should not be given authority to award punitive damages. This power is reserved to the courts.” *Shaw v. Kuhnel & Assocs.*, Inc., 698 P.2d 880, 882 (N.M. 1985).

256. *Stewart*, 726 P.2d at 1375.

257. *Id.* at 1377-78.
not explicitly address the issue of maintaining a cause of action for damages alone, this is precisely what the court allowed.\textsuperscript{258}

c. Intra-Arbitral Review

One rather unique alternative to bifurcation, which includes judicial involvement, was described in \textit{Bonar v. Dean Witter Reynolds, Inc.}\textsuperscript{259} In \textit{Bonar}, an arbitrator’s punitive damage award was vacated because of significant misrepresentations made by an expert witness about his qualifications.\textsuperscript{260} The court referred the issue of punitive damages to a new arbitration panel empowered to decide the issue.\textsuperscript{261} This may be a viable alternative if the securities industry is eventually forced through legislation or action by the exchanges to allow the awarding of punitive damages in employment disputes.\textsuperscript{262}

d. A Practitioners’ Guide to Bifurcation

Although the bifurcation of punitive damage claims may only be possible in New Mexico and New York, there is no reason for any employer or business to get caught in a position where punitive damages are available. The reason to choose New York law was to compel all claims to arbitration and thereby estop any awards of punitive damages; bifurcation threatens to upset that goal. Therefore, if a party wishes to exclude punitive damages, it should do so explicitly, and not just with regard to the arbitrator’s authority. Practitioners should include language in arbitration agreements that punitive damages are unavailable for any claim, in any forum. If the preclusion of punitive damages through choice-of-law was defensible, it should be just as defensible if such exclusion is done explicitly.\textsuperscript{263}

\begin{itemize}
  \item \textsuperscript{258} The issue of maintaining an independent cause of action was not raised at any stage of the court proceedings. Telephone Interview with Janet Santillanes, attorney for Mike Stewart (Mar. 6, 1995). Ms. Santillanes added that even though a plaintiff needs an underlying substantive claim to assert punitive damages in New Mexico, a claim presented in arbitration can be used for that purpose. \textit{Id.}
  \item \textsuperscript{259} 835 F.2d 1378 (11th Cir. 1988).
  \item \textsuperscript{260} \textit{Id.} at 1386.
  \item \textsuperscript{261} \textit{Id.}
  \item \textsuperscript{262} See supra notes 202-16 and accompanying text.
  \item \textsuperscript{263} Practitioners may be uneasy about so explicitly excluding punitive damages. Confidential Telephone Interview with in-house counsel for brokerage firm (Mar. 13, 1995). This reluctance may indicate that there is a real conflict between any limiting arbitration agreements and the punitive damages provisions of the Civil Rights Act of 1991, 42 U.S.C. \textsection 1981b(1)-(3) (Supp. V 1993). See also supra note 165 and accompanying text (describing the rules of the various securities exchanges which could limit the ability of businesses in
\end{itemize}
4. Placing Caps on Punitive Damages

Allowing any punitive damages may not be terribly palatable to the securities industry, but some have suggested the limitation of the amount of punitive awards as a possible compromise.\textsuperscript{264} The NASD proposed limiting the amount of such damages relative to the amount of compensatory damages.\textsuperscript{265} The SIA suggested that the NASD impose even tighter limits with a cap of $100,000, but only if the SIA suggestion to prohibit punitive damages failed.\textsuperscript{266} Both suggestions, however, do nothing to address the conflict that such policies have with Title VII of the Civil Rights Act, which specifically allows for punitive damages.\textsuperscript{267}

The industry is not without its allies, however. The SIA may find support in the state legislatures and with the new Congress in its attempts to limit punitive damages.\textsuperscript{268} Currently, more than ten states have limits on the amount of punitive damages that may be awarded.\textsuperscript{269} Part of the Republican's "Contract With America" includes placing a cap on punitive damages, even below that now provided in the Civil Rights Act of 1991.\textsuperscript{270} As tort liability is reformed, arbitration awards are likely to follow suit.\textsuperscript{271}
D. The Implications of the Civil Rights Act of 1991

When *Gilmer v. Interstate/Johnson Lane Corp.* was decided by the Supreme Court, punitive damages were not at issue. It is only in the post-*Gilmer* era that punitive damages have been a statutorily guaranteed remedy under Title VII of the Civil Rights Act. In *Gilmer*, the Court found that arbitration was an acceptable forum because it did not conflict with Congressional intent and thus, did not constitute an impermissible "waiver of [the] judicial remedies for the statutory rights at issue." The Court allowed the arbitral process to be used because that forum could "provide a fair and complete hearing of claims and . . . afford broad relief to . . . claimants." In fact, the *Gilmer* Court reaffirmed the position that arbitration was appropriate because the "'remedial and deterrent function' of the underlying legislation could be maintained." Disallowing punitive damages based on governing state law or specific contractual exclusions creates a direct conflict with the full rights philosophy of the *Gilmer* decision.

*Gilmer* affirmed the burden of proof standards governing waivers of the judicial forum that the Supreme Court established in *Shearson/American Express Inc. v. McMahon*. In *McMahon*, the Court held that "the party opposing arbitration . . . [has the burden] to show that Congress intended to preclude a waiver of judicial reme-

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273. *Gilmer* was based on a claim under the Age Discrimination and Employment Act ("ADEA"), 29 U.S.C. §§ 621-34 (1988), which does not provide for punitive damages. *Id.*
276. Bompey & Pappas, *supra* note 26, at 199. The Supreme Court's holding was similar to the Fourth Circuit's earlier holding in *Gilmer*. The Fourth Circuit held that as "long as arbitrators possess the equitable power to redress individual claims of discrimination, there is no reason to reject their role in the resolution of . . . disputes." *Gilmer v. Interstate/Johnson Lane Corp.*, 895 F.2d 195, 199 (4th Cir. 1990), *aff'd*, 500 U.S. 20 (1991).
277. See 500 U.S. at 28 (quoting *Mitsubishi Motors Corp.*, 473 U.S. at 637). The Court also held that because the Equal Employment Opportunity Commission could still institute an action, control aspects would still exist notwithstanding the lack of a judicial forum. *Id.* at 32.
278. See Bompey & Pappas, *supra* note 26, at 209-10. When *Gilmer* was heard by the Fourth Circuit, the court assumed that the arbitrators were empowered to award liquidated damages. *Gilmer*, 895 F.2d at 200.
dies for the statutory rights at issue.\textsuperscript{280} The \textit{Gilmer} Court, in an analogous decision, held that the burden of proof had not been met by a plaintiff who did not want to arbitrate his claims.\textsuperscript{281} Neither the \textit{Gilmer} nor the \textit{McMahon} Court, however, confronted the issue that the arbitral forum might not be able to provide remedies equivalent to those available in the courts.\textsuperscript{282} In each case, the Court viewed the arbitral process merely as an alternative forum that was roughly equivalent in all respects.\textsuperscript{283}

With regard to the allowable waiver of rights and remedies, \textit{Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.}\textsuperscript{284} established the standard by which waivers must be judged. A waiver will be invalid if Congress did not intend to allow it, as evidenced by the "text or legislative history" of the statute.\textsuperscript{285} The text of the Civil Rights Act contains provisions for punitive damages, which would seem to qualify as a textual defense because "arbitration is inconsistent with the underlying purposes of a statute 'where arbitration is inadequate to protect the substantive rights at issue.'"\textsuperscript{286} To hold

\textsuperscript{280} Id. at 227; accord \textit{Gilmer}, 500 U.S. at 26; \textit{Mitsubishi Motors Corp.}, 473 U.S. at 628. "Congress' intent may be deduced from (1) the text of the statute; (2) the statute's legislative history; or (3) the 'inherent conflict between arbitration and the statute's underlying purposes.'" \textit{Fabian Fin. Servs. v. Kurt H. Volk, Inc. Profit Sharing Plan}, 768 F. Supp. 728, 731 (C.D. Calif. 1991) (quoting \textit{McMahon}, 482 U.S. at 227).

\textsuperscript{281} 500 U.S. at 35.

\textsuperscript{282} See \textit{Gilmer}, 500 U.S. at 26, 32 (holding that the rules of the applicable arbitration did not "restrict the types of relief an arbitrator may award"); \textit{McMahon}, 482 U.S. at 227, 230-31. However, \textit{Gilmer} involved a claim under the ADEA, which does not provide for punitive damages. See supra notes 272-74 and accompanying text; see also \textit{Kinnebrew v. Gulf Ins. Co.}, No. CA 3:94-CV-1517-R, 1994 U.S. Dist. LEXIS 19982, at *4-5 (N.D. Tex. Nov. 23, 1994) (holding that a "[p]laintiff does not forego 'substantive rights' when compelled to arbitrate under a more limited remedial scheme").

\textsuperscript{283} See \textit{Gilmer}, 500 U.S. at 34 n.5; \textit{McMahon}, 482 U.S. at 232 (concluding that "the streamlined procedures of arbitration do not entail any consequential restriction on substantive rights").

\textsuperscript{284} 473 U.S. 614 (1985).

\textsuperscript{285} Id. at 628. One commentator suggests that the Older Workers Benefits Protection Act ("OWBPA") contains waiver requirements that should be applied to pre-dispute arbitration agreements of Title VII claims. \textit{Belton, supra} note 45, at 961-64. The OWBPA is inapplicable to pre-dispute agreements, however, because of its purpose and timing. If it is held that arbitration does not constitute a foregoing of rights, then the OWBPA provisions do not come into effect, because they only invalidate improperly obtained waivers of rights. We must also remember that the ADEA does not allow punitive damages and thus, no substantive rights could conceivably be waived by arbitrating an ADEA claim. Philosophically, though, it indicates Congress's intent to preclude the easy waiver of substantive rights.

otherwise would imply that a pre-dispute arbitration agreement could waive the right to damages altogether, compensatory damages included. The courts would never enforce a contract containing such unconscionable provisions as to be in clear violation of public policy. Therefore, to prohibit punitive damages when such claims are made under the Civil Rights Act poses a dilemma.

Recently, courts have asserted that pre-dispute arbitration agreements are enforceable specifically because "a party does not forego the substantive rights afforded by the statute." Most courts assume that substantive rights have not been waived by a party agreeing to arbitration, give short shrift to the substantive rights issue, and quickly proceed to discuss the intent of Congress regarding the arbitrability of Title VII or other claims. Plaintiffs' attorneys have encouraged the courts' method of analysis by focusing on many of the issues already decided in Gilmer while virtually ignoring the critical relationship of substantive rights to the availability of statutory punitive damages. This failure of the plaintiffs' bar may explain the failure of the courts to adequately reconcile specific contractual exclusions of punitive damages with the availability of punitive damages under the Civil Rights Act and the language of the decisions in Gilmer, McMahon, and their progeny.

The proponents of eliminating punitive damages in arbitration continue to argue that there is no guaranteed right to punitive dam-

288. Scott v. Merrill Lynch, Pierce, Fenner & Smith, Inc., No. 89 Civ. 3749 (MIL), 1992 U.S. Dist. LEXIS 13749, at *21 n.10 (S.D.N.Y. Sept. 10, 1992); accord Willis v. Dean Witter Reynolds, Inc., 948 F.2d 305, 308 (6th Cir. 1991) (citing Mitsubishi Motors Corp., 473 U.S. at 628). Mitsubishi, a pre-Gilmer decision, established the appropriateness of the arbitration of statutory claims, but with the proviso that substantive rights were not therefore forfeited. See Mitsubishi, 473 U.S. at 628; Greenwood v. Sherfield, 895 S.W.2d 169, 172 (Mo. Ct. App. 1995). "However, 'the procedural provisions of the Federal Arbitration Act are not binding on state courts . . ., provided applicable state procedures do not defeat the [substantive] rights granted by Congress.'" Id. (quoting McClellan v. Barrath Constr. Co., 725 S.W.2d 656, 658 (Mo. Ct. App. 1987)) (alterations in original). But see generally Ware, supra note 3, at 542 (arguing that upholding an arbitrator's "error of law . . . deprives a party of the substantive right that would have been vindicated by a correct application of the law" and concluding that such a deprivation of substantive rights is equal to or greater than the deprivation incurred by waiving punitive damages in arbitration).
289. See, e.g., Bird, 926 F.2d at 120-21; Willis, 948 F.2d at 308-12.
290. See, e.g., Willis, 948 F.2d at 310.
291. At least one court has confronted the issue of substantive rights directly. See Kinnebrew v. Gulf Ins., No. CA 3:94-CV-1517-R, 1994 U.S. Dist. LEXIS 19982, at *5 (N.D. Tex. Nov. 23, 1994) (compelling arbitration without punitive damages because the plaintiff failed to show legislative intent to "preclude" her "waiver of judicial remedies").
es. Notwithstanding the recently published opinion in *Kinnebrew v. Gulf Insurance Co.*, the courts have not explicitly ruled on whether specific statutory grants of punitive damages under the Civil Rights Act qualify as substantive rights which are thus unwaiveable. The courts have generally enforced private agreements and state law as long as they are consistent with federal policy, but they have yet to address this apparent inconsistency. However, enforceability may be in doubt for arbitration agreements containing choice-of-law provisions or specific language which constitutes a waiver of the punitive damages available under the Civil Rights Act. Although the district court in *Kinnebrew* is the only court to have addressed this issue for employment disputes, at least one circuit court has not been silent on the ability to waive statutorily guaranteed remedies. In *Graham Oil Co. v. Arco Products Co.*, the Ninth Circuit held that an arbitration agreement was unenforceable if a party waived statutorily guaranteed remedies of punitive or exemplary damages.

292. See *SIA Assails*, *supra* note 147, at 3 (repeating that there is no right to punitive damages and that therefore, Garrity's critics are wrong); *SIA Opposition*, *supra* note 102, at 184.


294. See Baravati *v*. Josephthal, Lyon & Ross, Inc., 28 F.3d 704, 707 (7th Cir. 1994); *see also* Higgins *v*. Superior Court, 1 Cal. Rptr. 2d. 57, 62 (Ct. App. 1991) (ordered not officially published) (holding that arbitration does not conflict with the "important public policies" involved with Title VII claims).

295. Inadvertently, the Supreme Court may have addressed this issue in *Mastrobuono*. The court asserted that "it seems unlikely that petitioners... had any idea that by signing a standard-form agreement to arbitrate disputes they might be giving up an important substantive right." *Mastrobuono v. Shearson Lehman Hutton*, Inc., 115 S. Ct. 1212, 1219 (1995). If punitive damages are "important substantive rights" in a contract dispute based on inappropriate investment advice, then they would clearly be even more substantial when they are statutorily prescribed remedies under a civil rights act.

296. See *Berger*, *supra* note 104, at 720 (arguing that "[i]f arbitration is to be an adequate substitute for litigation, it is necessary that the arbitrator's remedies parallel those available to the courts").

While it may be rational to conclude that an employee's agreement to arbitrate waives his right to a judicial forum, there is no basis in the waiver to conclude that he also has agreed to forgo relief otherwise available under the statute. Such an approach would raise serious public policy concerns which might be sufficient to render the agreement to arbitrate unenforceable.

Id. at 720 n.173.


298. See *BLACK'S LAW DICTIONARY* 390, 392 (6th ed. 1990) (defining "punitive damages" and "exemplary damages" as equivalent terms).

299. See *Graham Oil Co.*, 43 F.3d at 1246.
Although referring to a franchise agreement, the *Graham Oil* court held that a waiver of “statutory remedies for . . . arbitrary or discriminatory termination” was unenforceable. The court cautioned that “the fact that franchisees may agree to an arbitral forum for the resolution of statutory disputes in no way suggests that they may be forced by those with dominant economic power to surrender the statutory-mandated rights and benefits that Congress intended them to possess.” The Ninth Circuit would undoubtedly hold that an arbitration agreement with a choice-of-law provision or specific provisions that preclude punitive damages would have the same effect, rendering the agreement invalid. Since the claims cannot be bifurcated in most jurisdictions, and assuming that punitive damages must be made available as a matter of public policy, only two options remain: allow arbitrators to award punitive damages or remove the entire action to court.

300. *Id.*

301. *Id.* at 1247 (emphasis added); see *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220, 227, 230-31 (1987) (arguing that a contract provision that “waive[s] compliance with [a] statutory duty,” is, *de facto* “void . . . whether voluntary or not”) (alteration in original); *Statement by Estreicher, supra note 26*, at D-2 (asserting that *Gilmer* precludes the waiver of “substantive entitlements”); see also *United Paperworkers Int’l Union v. Misco, Inc.*, 484 U.S. 29, 42-43 (1987) (holding that a refusal to enforce an arbitrator’s award based on public policy required a finding that the public policy was one that is specified in common or statutory law). The specific availability of punitive damages under the Civil Rights Act provides an appropriate analogy.

302. One of the reasons the Ninth Circuit may not have ruled so explicitly yet is because of the California court’s decision in *J. Alexander Securities*, which held that the New York *Garrity* rule did not apply. *J. Alexander Sec., Inc. v. Mendez*, 21 Cal. Rptr. 2d 826 (1993), review denied, No. S035102, 1993 Cal. LEXIS 6354 (Nov. 24, 1993), and cert. denied, 114 S. Ct. 2182 (1994). If specific contractual exclusions of punitive damages become common, the California courts will probably find that when applied in this context, such agreements would be violative of federal public policy.

303. *See supra* notes 217-51 and accompanying text. In addition, because of the general philosophy of the FAA favoring arbitrability, bifurcation is not likely to become widespread.


Before *Mastrobuono*, at least one court had made the assumption that, for *Gilmer* to conform with public policy, the arbitrator had to have the authority to award punitive damages for civil rights actions. *See Scott v. Farm Family Life Ins. Co.*, 827 F. Supp. 76, 79 (D. Mass. 1993). The *Scott* court noted that the plaintiff “also fears that the full range of damages will not be available to her, because in states like New York (where defendants reside), arbitrators cannot award punitive damages. The *Gilmer* Court, however, expressly rejected such arguments, finding that arbitrators can ably resolve issues of discrimination.” *Id.* The *Scott* court may have overlooked the fact that the statute at issue in *Gilmer* did not allow punitive damages.

305. Two courts in the early 1980’s held that the preclusion of punitive damages was
In light of Mastrobuono, allowing arbitrators to award punitive damages in the face of Garrity may be possible. However, an arbitrator would clearly exceed his authority if he awarded punitive damages where a contract contained an explicit prohibition against the arbitrator awarding such damages. If plaintiffs' attorneys start to tailor their arguments specifically to this issue of punitive damages availability, the courts may eventually have to grapple with the apparently conflicting public policies of the FAA, which upholds the right to contract, with those of the Civil Rights Act, which provides for stringent remedies to protect individuals from employment discrimination. If the courts determine that the unavailability of punitive damages is violative of public policy, they may then be compelled to sever arbitration clauses from employment agreements and hear entire civil rights claims in court. If punitive damages are indeed "important substantive right[s]" as the Supreme Court suggests, and are specifically provided for in the Civil Rights Act of 1991, it would seem that precluding them would invalidate arbitration as a roughly equivalent forum. This may be the critical issue that causes a reevaluation of Gilmer and its progeny.

The brief submitted by Shearson Lehman Hutton in Mastrobuono did not help the cause of the securities industry. In its brief, Shearson sought to distinguish Mastrobuono and to justify the implicit waiver of punitive damages by claiming that there were no statutorily guaranteed rights involved. Shearson's argument would seem to support the proposition that there is a public policy conflict, because the Civil Rights Act specifically provides for punitive damages. Plaintiffs' sufficient reason to force the entire matter into court. See Pierson v. Dean Witter Reynolds, Inc., 551 F. Supp. 497, 504 (C.D. Ill. 1982); Starkenstein v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 572 F. Supp. 189, 191-92 (M.D. Fla. 1983); see also Wilson, supra note 61, at 162-63 (claiming, however, that such an alternative is unlikely). But see Waltman v. Fahnestock & Co., 792 F. Supp. 31, 33 (E.D. Pa. 1992), aff'd, 989 F.2d 490 (3d Cir. 1993) (holding that notwithstanding the inability to obtain punitive damages, the issue must be arbitrated under NYSE rules).

Where courts in New York have been confronted with employment disputes and the inability to award punitive damages, several have taken the easy non-political way out by reserving authority to award punitive damages. See supra notes 217-51 and accompanying text. Any of the bifurcating courts may have been inclined to remove the entire case to court under a public-policy theory had they had no other option.


309. Mastrobuono, 115 S. Ct. at 1218.

attorneys should seize the opportunity. The plaintiffs' bar must stop complaining about being forced into arbitration and start developing policy theories beyond those that were rejected in Gilmer; the courts appear ready to accept the next wave of public policy arguments.

E. Other Issues

1. Why Do We Still Have Garrity Anyway?—Breitel's Paradox

None of the court decisions which prevent the award of punitive damages in arbitration have received as much attention as that in Garrity v. Lyle Stuart, Inc. After nineteen years, the New York Court of Appeals may be ready to overrule Garrity, but opportunities to do so are limited. Assuming that there are no questions raised about the integrity of the proceedings, an arbitrator's decision is only subject to review when the arbitrator has exceeded his authority. When punitive damages are not awarded because arbitrators believe that they lack authority, the proponents of overturning Garrity are caught in a paradox; appeal is only available when an arbitrator

311. Some may believe that the paradox has been resolved by Mastrobuono. However, in light of the limited holding by the Supreme Court, and the number of other states that have rules similar to those pronounced in Garrity, the problems presented by the paradox remain.

312. 353 N.E.2d 793 (N.Y. 1976); see Katsoris, supra note 22, at 1137-39 & n.145; supra note 105. Although Mastrobuono may have mitigated the effects of the paradox for New York, since Garrity has dominated the debate for so long, it is discussed here.

313. A number of commentators have called for its repeal. See generally Davis, supra note 20, at 62-64 & n.75; Ware, supra note 3, at 558-72. Garrity may be reviewable only by the courts or by amendment to New York's Constitution. The court in Garrity held that arbitrators were unable to award punitive damages, because to do so would violate the general function of the judiciary. 353 N.E.2d at 794. There is some doubt as to whether a law could overturn such a constitutionally-based decision about the role of the state judiciary.

314. Section 10 of the FAA provides that an arbitrator's award will only be vacated:

(1) Where the award was procured by corruption, fraud, or undue means.

(2) Where there was evident partiality or corruption in the arbitrators, or either of them.

(3) Where the arbitrators were guilty of misconduct . . . or of any other misbehavior by which the rights of any party have been prejudiced.

(4) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

exceeds his authority, but knowledgeable New York arbitrators have not awarded punitive damages because they thought that by doing so, they would exceed their authority. 315 Notwithstanding Mastrobuono, since punitive damage awards would normally be confirmed in federal court, there may still be little opportunity for the New York’s highest court to change its position.

Compounding the problems of the paradox are the holdings of some judges that if court action is ‘stayed pending arbitration,’ such a decision may not be reviewed until after the arbitration is complete. 316 After the arbitration, if the plaintiff still desires review of the Garrity issue, she would then have to appeal an award, which may not include punitive damages or even an explanation. 317 As a result, the likelihood of judicial review of Garrity by the New York courts is remote. 318

Additionally, review of arbitration awards is difficult because “[a]rbitrators are encouraged not to explain the reasons for their decisions” 319 and cannot be required to testify about those reasons. 320 Unless an arbitrator clearly exceeds his authority or issues a written

315. See Ware, supra note 3, at 532-33, 545 n.63; see also Franklin, supra note 12, at 6 (interviewing Professor Constantine Katsoris of Fordham University about his opinion that arbitrators are incorrectly not awarding punitive damages).
317. A number of attorneys question whether any party could justify the expense of such an appeal. Confidential Telephone Interviews with outside counsel to brokerage firms (May 1995).
318. But see supra notes 217-51 and accompanying text (outlining the limited use of the bifurcated proceeding and the potential that the New York Court of Appeals will get an opportunity to review its holding in Garrity).
319. Brodsky, supra note 117, at 3; see also Thomson, supra note 14, at 157-58 (concluding that arbitrators do not issue written opinions specifically to avoid being subject to appeal). See generally AMERICAN ARBITRATION ASSOCIATION, COMMERCIAL ARBITRATION RULES 16 (1984).
decision which exposes serious misconduct during the hearing, there will be no opportunity for review.\textsuperscript{321} Furthermore, even requiring a written opinion will not greatly increase the ability to review an incorrect decision by an arbitrator because courts generally do not question an arbitrator's rationale in making an award.\textsuperscript{322}

Notwithstanding the impact of \textit{Mastrobuono}, the solution to the paradox that has prevented New York's highest court from reviewing \textit{Garrity} is to call an arbitrator to testify about his decision not to award punitive damages and claim that he \textit{underceeded}\textsuperscript{323} his authority. No law or arbitral body rule prevents a party from calling an arbitrator to testify in court about his decision, as long as the arbitrator is willing. The arbitrator could testify that he failed to award punitive damages because he believed that such an award was prohibited.\textsuperscript{324} The arbitrator's testimony could be used to support the claim that the arbitrator underceeded his authority. Underceeding is a philosophical equivalent to exceeding, which can be tested by the courts.\textsuperscript{325} If an arbitrator fails to award punitive damages, his deci-

\textsuperscript{321} An extremely ambiguous ruling can cause review of an arbitrator's award. See Willoughby Roofing & Supply Co. v. Kajima Int'l, Inc., 598 F. Supp. 355, 356 (N.D. Ala. 1984), \textit{aff'd}, 776 F.2d 269 (11th Cir. 1985). With an ambiguous award, however, the court may opt to remand the case to the arbitrators for clarification. See \textit{9 U.S.C. § 11} (1988); \textit{see, e.g.}, Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378 (11th Cir. 1988).

\textsuperscript{322} During oral arguments in \textit{Mastrobuono}, Justice O'Connor supported the notion that wherever possible, arbitrators are given the benefit of the doubt, as it is assumed that they properly considered all issues submitted before them. \textit{See} Supreme Court Notes, \textit{supra} note 119. In its holding, the \textit{Mastrobuono} Court reasoned that "the only decision-maker arguably entitled to deference [was] the arbitrator." Mastrobuono v. Shearson Lehman Hutton, Inc., 115 S. Ct. 1212, 1217 n.4 (1995); \textit{accord} Siegel, 779 F.2d at 894; Dean Witter Reynolds, Inc. v. Bork, No. 91-0392, 1991 U.S. Dist. LEXIS 11907, at *5 (E.D. Pa. 1991); \textit{Willoughby Roofing & Supply Co.}, 598 F. Supp. at 357 ("[C]ourts must broadly construe the agreement and resolve all doubts in favor of the arbitrator's authority.").

A frequent author on the subject of arbitration feels that courts' deference to arbitrators' rationales is at the crux of the punitive damages debate. Confidential Interview with employment law attorney, New York, N.Y. (Nov. 8, 1994). He asserts that business would have little problem absorbing a few additional punitive damage awards by arbitrators; the real concern is the inability to review the award of an arbitrator that could be so excessive as to put the entire business in jeopardy. \textit{Id.} Judicial appeal, he states, offers a comfort level which can not be found in arbitration. \textit{Id.}

\textsuperscript{323} The term "underceed" is used as the antonym of exceed.

\textsuperscript{324} This was undoubtedly the belief of most arbitrators prior to the decision in \textit{Mastrobuono}. In Anderson v. Nichols, 359 S.E.2d 117 (W. Va. 1987), a case reviewing the decision of a three arbitrator panel, the dissenting arbitrator testified about the deliberations in an effort to help the losing party show bias on the part of one of the majority arbitrators. \textit{Id.} at 122-23. Although the court held against the moving party on the facts, the court accepted the arbitrator's testimony. \textit{Id.}

\textsuperscript{325} An arbitrator's award may be vacated by a court of competent jurisdiction if he
sion would normally not be reviewable, because inaction would be an allowable mistake of law and would most certainly not be an exceeding of authority. However, this undoubtedly means that the arbitrators who are knowledgeable about New York law, notwithstanding the limited decision in *Mastrobuono*, will rarely if ever present an opportunity for the Court of Appeals to overturn *Garrity*; hence, the paradox. In the same way that the *exceeding* arbitrator is responsible for a mistake about the limits of his power, the *underceeding* arbitrator should be controlled without having to consider such inaction a mistake of law. Arguably, the text of the FAA already contains language about underceeding when it states that an award can be vacated if "the arbitrators . . . so imperfectly executed [their powers] that a mutual, final and definite award" was not rendered. Failure to resolve the issue of punitive damages qualifies under this standard as a reason to vacate or review an arbitrator’s award.

One other possible solution to the paradox would be to claim that an arbitrator’s award which does not include punitive damages is inherently ambiguous and thus, reviewable. Otherwise, *Garrity* and other similar common law rules will remain immune from appellate review merely because a negative exertion of authority is not reviewable, by definition. *Garrity* will probably remain good law until a New York arbitrator takes a chance, awards punitive damages, and

326. The issue of punitive damages was raised on appeal in a case where the defendant contested an alleged award of punitive damages. See *Kalinich v. New York Stock Exchange*, 618 N.Y.S.2d 205 (App. Div. 1994) (upholding the arbitrator’s entire award, which did not explicitly award punitive damages). The case, however, is a family dispute where there are some serious questions as to whether or not punitive damages were actually awarded. See generally Mary Vobril, *Family Feud has Retiree Living at the Y*, NEWSDAY, Apr. 17, 1994, at A30 (detailing the turmoil in the Kalinich family).

Stephen Ware suggests that when arbitrators are prohibited from making punitive damage awards, they will compensate by awarding extra compensatory damages. Ware, *supra* note 3, at 545 n.63. But he did note that "(the New York Court of Appeals has had to remind New York courts that *Garrity* ‘should not be interpreted as an indication that whenever compensatory damages are somewhat speculative’ an arbitrator’s award may be vacated on the ground that ‘punitive’ damages were awarded.” *Id.* (quoting Board of Educ. v. Niagara-Wheatfield Teachers Ass’n, 389 N.E.2d 104, 106 (N.Y. 1979)).


328. *See NCR Corp. v. Sac-Co., Inc.*, 43 F.3d 1076, 1081 (6th Cir. 1995); *Siegel v. Titan Indus. Corp.*, 779 F.2d 891, 894 (2d Cir. 1985). This “inherently ambiguous” analysis could be used in an attempt to obtain punitive damages in cases that were decided prior to the Supreme Court’s holding in *Mastrobuono*. If the argument is accepted, plaintiffs could get a second chance at arbitrators who may now feel empowered to award punitive damages because of the Court’s decision.
the case is appealed in the state courts to the New York Court of Appeals.329

Breitel's Paradox existed before the Supreme Court issued its opinion in Mastrobuono.330 Although the impact of Garrity may no longer be as great,331 the solutions to the paradox offer options for practitioners. There have been thousands of arbitration awards in the past few years which did not include punitive damages; some for cause and some merely because the arbitrator believed he lacked the authority to do so. If plaintiffs wish to have their cases reviewed, the underceeding or inherently ambiguous philosophies may offer the only opportunity to get a second chance at a large punitive award. The filings may be used as leverage to gain additional compensation if for nothing more than nuisance value. For industry and corporate attorneys, the best defense is the one they never thought they would have to make: the arbitrator had the authority to award punitive damages at the first hearing.332 If the arbitrator had the power, and the courts generally do not question the rationale of an arbitrator,333 then the court must assume that the arbitrator knew he had the power and decided not to award punitive damages because they were not deserved. The defense bar can find comfort in the fact that few arbitrators have testified in the past and it does not seem likely that arbitrators will be rushing into court any time soon.

2. Note for the Practitioner: If All Else Fails, Pound the Table

Although the public policy debate is likely to be resolved in the courts, there are a number of theories available to the practitioner and to academics from which analogies may be drawn. Admittedly, the

329. Some practitioners have suggested that because arbitrators are selected by the parties, an arbitrator awarding punitive damages may never work again. Confidential Telephone Interviews with brokerage firms' in-house and outside counsel (Fall 1994).


331. But see Client Agreement, supra note 65, ¶ 7 (explicitly defining the implications of choosing "the laws of the State of the State of New York" as including "the law of New York regarding damages recoverable in arbitration"). If other agreements change similarly, the paradox is likely to continue.

332. The corporate attorney would be left claiming that the arbitration agreement was ambiguous and thus, in accord with Mastrobuono, should be interpreted as having permitted the arbitrator to make an award of punitive damages. This is exactly what happened on the remand of Mulder v. Donaldson Lufkin & Jenrette, 623 N.Y.S.2d 560 (App. Div. 1995). See supra note 245 and accompanying text.

333. See supra note 314.
Theories outlined below are on the fringes of the debate and may not be appropriate in many circumstances. They are presented not as complete analyses, but rather as "food-for-thought." It remains for the practitioner to assess an individual judge's level of tolerance for the following unique theories and whether analogy in a particular case may be appropriate.

a. Native American Law

In the field of Native American law, waiver of statutorily guaranteed remedies may be available as a quid pro quo to arbitration. Courts have held that a tribe can be held to have waived its sovereign immunity simply by entering into an arbitration agreement. A waiver of Title VII punitive damages pales in comparison to a waiver of sovereign immunity. It would be difficult to argue with a straight face that the availability of punitive damages is paramount to sovereign immunity. However, because sovereign immunity would void the enforceability of any arbitration agreement, its relevance here may be overstated—waiver may be a matter of necessity.

b. Sham Arbitrations Have Been Allowed

At least two courts have evaluated extremely restrictive in-house arbitration procedures and found them to be acceptable alternative forums. In Delaney v. Continental Airlines Corp., Thomas Delaney was precluded from pursuing a wrongful discharge action in court because he participated in the company's "Management Appeal Procedure" ("MAP"). The MAP consisted of a hearing before three Continental executives, two chosen by Continental and the third chosen by Mr. Delaney. In Fregara v. Jet Aviation Business

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335. See Vetter, supra note 334, at 182-85.
338. Id. at *1-2.
339. Id.
the court dismissed claims because Ronald Fregara did not avail himself of a mandatory internal review procedure with arbitrators just slightly more independent than those available to Mr. Delaney. Although Delaney involved a post-dispute agreement, both cases may point to the fact that an arbitration need not be as fair as many decisions suggest, or for that matter, fair at all. One could hardly claim that the elimination of the availability of punitive damages is a greater infringement upon the rights of an employee than being bound by the decision of a hearing panel of company executives.

c. Congress Did Not See Civil Rights as a Priority: Damages Must Be Waiveable

Congress excluded itself from the punitive damages provision of the Civil Rights Act of 1991. This may lend support to the argument that by exempting itself from the statute, Congress placed such a low value on the rights contained therein that they could be waived. If the entire argument against waiver is premised on the fact that Congress intended to preclude parties from waiving punitive damages as a remedy, Congress’s failure to grant such remedies in all circumstances may vitiate the argument that merely passing the provisions provided textual evidence of Congress’s intent.

d. Rights Are Always at Risk in Arbitration

If an arbitrator makes a mistake of law, or even an egregious error interpreting a contract, his decision is not subject to judicial review. This lack of judicial review inherently puts substantive rights at risk. The loss of general substantive rights due to an arbitrator’s error is arguably no different than the substantive rights that are lost by waiving punitive damages. When “one enters arbi-

341. “The Company Board of Adjustment consisted of four members, two of whom were selected by non-supervisory company personnel, elected annually by an employee vote, and two of whom were selected and appointed by the president of the company” with a fifth member selected by the four appointed members. Id. at 952.
343. Id.
344. See supra note 314 and accompanying text.
345. See Ware, supra note 3, at 542.
tration, one cannot turn back,” despite the possible loss of procedural protections. Therefore, the loss of punitive damages is not necessarily an unusual hardship.

e. Arbitrators Can Award “Punitive Damages” Even With a Contractual Exclusion

Arbitrators may be able to award punitive damages, as defined in the Civil Rights Act of 1991, on the theory that they are not “real” punitive damages. The so-called punitive damages could be reclassified as liquidated and treble damages that have been allowed even in the face of restrictive decisions like Garrity. “Only where the damages are . . . intended to be punitive should the courts vacate the award.” As long as the liquidated damages would be for the direct benefit of the employee involved, the courts have held such damages to be compensatory, no matter what they are called.

The legislative history of the Civil Rights Act indicates that Congress was concerned with making sure that adequate damages are available to individual plaintiffs. Congress was concerned with the inequity in the law prior to 1991, under which plaintiffs could only

346. Seamons, supra note 104, at 401-02 n.38.
347. But see Friedlander, supra note 8, at 9-10 & n.30 (describing punitive damages under the Civil Rights Act as meeting the traditional definition).
348. Garrity v. Lyle Stuart, Inc., 353 N.E.2d 793, 794 (N.Y. 1976) (clarifying that an industry-wide liquidated damages provision was enforceable); see John T. Brady & Co. v. Form-Eze Sys., Inc., 623 F.2d 261 (2d Cir. 1980) (following the holding in Garrity and holding that an arbitrator may award liquidated damages); see also Ehrich v. A.G. Edwards & Sons, 675 F. Supp. 559, 564 (D. S.D. 1987) (holding that an arbitrator may award RICO damages which “are punitive in nature”). “The Supreme Court expressly held that . . . RICO claims are arbitrable. Hence, since RICO awards treble damages to successful plaintiffs, and since treble damages are punitive in nature, no sound basis exists for arguing that public policy prohibits arbitrators from awarding such damages.” Kupperman & Freeman, supra note 165, at 1595.
351. See Belton, supra note 45, at 924-25 (arguing that the 1991 revisions were designed to “enhance remedies for victims of employment discrimination”). If the punitive remedies were indeed intended to benefit the individual and not society, then they may not be punitive damages in the traditional sense. See Stipanowich, supra note 91, at 987 (asserting that “[a]wards that appear to be punitive . . . may have been intended as compensation for loss of economic expectation, damages for mental distress, or recoupment of arbitration-related costs”); Richard P. Hackett, Note, Punitive Damages in Arbitration: The Search for a Workable Rule, 63 CORNELL L. REV. 272, 307 (1978) (asking “[i]s there any basis for characterizing the award as compensatory?”).
recover punitive damages for certain acts of discrimination. In addition, the different tax treatment of certain awards may lend credence to the argument that the punitive damages available under the Civil Rights Act are not treated like other punitive damages. This argument cuts both ways, however. Plaintiffs may argue to an arbitrator that he may award so-called punitive damages, even with a contractual exclusion. Defense attorneys may use the theory to limit judicial scrutiny by arguing that arbitrators are empowered to award all remedies available under the Civil Rights Act, and thus, there are no negative public policy implications to compelling the arbitration of employment disputes. In order for courts to rule on this innovative argument, they may have to decide the civil rights dilemma described earlier in this Note. It is likely, however, that any court addressing so-called punitive damages will answer the dilemma, if only in dicta.

V. CONCLUSION

While the debate about punitive damages in arbitration began long ago, the battle is about to begin. The greatest impact of Mastrobuono will be felt by the legal practitioners as they answer challenges to their old arbitration agreements and as they develop their new ones. If nothing else, the Supreme Court has given the entire field of arbitration lawyers a lesson in contract formation. As contracts are revised to meet the standards established by the Court in Mastrobuono, other issues, including a potential conflict with the Civil Rights Act, must be resolved. The proponents of arbitration, however, may not be pleased with the outcome as these issues are brought into focus.

Enforcing pre-dispute arbitration agreements strikes of unfairness, especially in employment disputes where damages are limited. Even the advocates for the securities industry will admit that it is impossible to argue that the process is fair to employees who must sign such agreements as a condition of employment. The moral and fairness issues have been argued ad nauseam by attorneys and commentators, with the courts taking little notice. In order to get the courts' atten-

352. See Belton, supra note 45, at 946-49.
354. Strong advocates of arbitration are left defending the virtues of the process and arguing that if it is unfair, it is no greater injustice than that which exists in other areas of the law.
practitioners will need to explore new avenues and focus on critical conflicts. The field is ripe for innovation—the ball is in the plaintiff bar's court.

Jordan L. Resnick

* This Note is dedicated to James R. Mayfield whose memory will always serve to remind the author that there are human consequences to all employment decisions.

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