S. HRG. 105–1020

MANDATORY ARBITRATION AGREEMENTS IN EMPLOYMENT CONTRACTS IN THE SECURITIES INDUSTRY

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FIFTH CONGRESS

SECOND SESSION

ON

AMENDING CERTAIN FEDERAL CIVIL RIGHTS STATUTES TO PREVENT THE INVOLUNTARY APPLICATION OF ARBITRATION TO CLAIMS THAT ARISE FROM UNLAWFUL EMPLOYMENT DISCRIMINATION BASED ON RACE, COLOR, RELIGION, SEX, NATIONAL ORIGIN, AGE, OR DISABILITY, AND FOR OTHER PURPOSES

JULY 31, 1998

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FRIDAY, JULY 31, 1998

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:20 a.m., in room 538 of the Dirksen Senate Office Building, Senator Alfonse M. D'Amato (Chairman of the Committee) presiding.

OPENING STATEMENT OF CHAIRMAN ALFONSE M. D'AMATO

The CHAIRMAN. I want to apologize to my colleagues for the delay. Unfortunately, due to the tragic death of two officers, we were forced to reschedule, and that's why we don't have nearly as many Members here as I believe we would have had. I think we would have had just about all of our Committee in attendance, were this hearing to have been held as originally scheduled.

Be that as it may, we have an impressive panel. Our first two witnesses are Senator Feingold and Congressman Markey.

I'm going to ask that the full text of my opening statement be placed in the record.

Let me begin by saying there is no place for discrimination in the workplace, or anywhere else. Discrimination undermines the very system of merit and individual achievement that makes America great. People should be judged on the basis of their ability, not on the color of their skin, gender, ethnic background, religious affiliations, or any other irrelevant basis. The practice of discrimination must not be tolerated, and we have to do all we can to ensure that discrimination has no place in the workplace.

For this reason, we need to address the abuses that persist in the modern working environment. We must ensure that every working man and woman has an opportunity for redress and access to the legal avenues needed to confront and prevent discrimination.

Mandatory arbitration of disputes is a longstanding practice in the securities industry. For years, employees in securities firms have been required to sign such an agreement as a condition of employment, mandating that all disputes be settled by way of arbitration, rather than litigation. Customer disputes, as well as disputes between securities firms, are also subject to arbitration.

There are those who believe that the arbitration process of the securities industry should exclude claims of discrimination. Let me make it clear: A system of arbitration which fosters discrimination

cannot and should not be continued. But the reality of our overburdened court system demonstrates that we need to allow for the option of arbitration where it is deemed appropriate.

It is my opinion that in some cases it may be appropriate. We will no doubt hear testimony today both from witnesses who agree with that proposition, as well as those who do not.

I want to thank my colleagues, and I want to commend Senator Feingold and Congressman Markey for focusing attention on this important matter. They have both studied this issue over a period of time, and are here to share their views.

I again thank my colleagues for being here today. I look forward to hearing their testimony.

We will turn to Senator Feingold.

OPENING STATEMENT OF RUSSELL D. FEINGOLD A U.S. SENATOR FROM THE STATE OF WISCONSIN

Senator FEINGOLD. Thank you very much, Chairman D'Amato, for calling this hearing on the issue of mandatory, binding arbitration of employment disputes in the securities industry.

Let me thank you, in particular, for you and your staff's courtesy in offering me the opportunity to ask questions. Unfortunately, because of my schedule, I won't be able to stay for that. But I am grateful for it and hope that I could submit some questions in writing, if that would be permissible to the Chair.

The CHAIRMAN. Absolutely.

Senator FEINGOLD. I must say that I am quite impressed with your concern and understanding of this important matter, and I do thank you for this hearing.

I also want to thank Congressman Markey for his leadership on this issue in the House.

There is a disturbing and growing trend in employment contracts, in particular within the securities industry. Many employers are conditioning employment or professional advancement upon their employees' willingness to submit claims of discrimination or harassment to mandatory arbitration, Mr. Chairman—I emphasize the word, mandatory—rather than pursuing their suits in the courts. Although several Fortune 500 companies utilize mandatory arbitration, the securities industry is unique in that it is the only industry which requires its employees to waive their rights to bring such claims in court as a precondition of employment.

Today, more than 550,000 registered representatives of the securities industry must resolve their employment disputes, including discrimination and sexual harassment claims, before an industry-sponsored arbitration panel. All securities industry employees are required to sign a Form U–4, which is the Uniform Application for Securities Industry Registration or Transfer. In other words, the Form U–4 is a regulatory safeguard that an employee is required to sign prior to gaining employment in the industry.

Unfortunately, the Form U–4 contains a clause which mandates that all such employees file any employment dispute—even a Federal civil rights or sexual harassment claim—before an arbitration panel.

An important point has to be made here—because the practice of requiring mandatory, binding arbitration is industry-sponsored,

employees cannot simply change firms to avoid arbitration. In short, if someone wishes to work within the securities industry, they have no choice but to acquiesce to this unfair and potentially biased practice.

Make no mistake, however. This problem is not limited to what we commonly consider the center of the securities industry, which is your State, New York. Rather, mandatory, binding arbitration of employment disputes affects people nationwide. Indeed, recently, a man who worked for a firm in my State, Wisconsin, was fired from his job. The man alleged that he was let go not for just cause, but because he was too old; therefore, he filed an age discrimination claim against his employer.

The plaintiff in this case felt that he should have the right to bring his civil rights claim in court, but a Court of Appeals for Wisconsin held that he was bound by the mandatory, binding arbitration clause in his employment contract and, thus, must submit his case to an arbitration panel.

The court did note that if this man's case were decided under Wisconsin law—that is, under the Wisconsin Arbitration Act—he would have had the right to file his claim in court. But because the Supreme Court held in *Southland Corp.* v. *Keating* that the Federal Arbitration Act preempts such State laws and because the Supreme Court held in *Gilmer* v. *Interstate/Johnson Lane Corp.* that such an age discrimination claim could be subject to compulsory arbitration pursuant to the arbitration agreement in the Form U–4, the court had no choice but to force the man to forego his right to file his claim in a court of law.

Mr. Chairman, to put an end to this troubling practice, I have introduced the Senate version of the Civil Rights Procedures Act—Representative Markey has sponsored the House companion bill. This measure would amend seven civil rights statutes to guarantee that a Federal civil rights or sexual harassment plaintiff can still seek the protection of the U.S. courts, rather than being forced into mandatory, binding arbitration. Simply stated, this bill would ensure that an employer cannot use her or his superior bargaining power to coerce her or his employees to capitulate to an agreement which diminishes their civil rights protections.

Representative Markey and I are by no means the only people that are concerned about this important issue. The Women's Legal Defense Fund, the Mexican American Legal Defense and Education Fund, the National Asian Pacific American Legal Consortium, the National Women's Law Center, the National Council of La Raza, the Coalition of Labor Union Women, the National Employment Lawyers' Association, the American Civil Liberties Union, the D.C. Lawyers' Committee for Civil Rights and Urban Affairs, Women Employed, and recently, the Attorney General in your home State of New York have noted their support for our bills.

As you know, Mr. Chairman, the New York Attorney General, Dennis Vacco, recently held a public hearing on the issue of discrimination and sexual harassment in the securities industry. In a letter sent to me last week by Attorney General Vacco, he noted the importance of this country's civil rights and sexual harassment laws and the need to protect such a plaintiff's right to bring her

or his suit in court. In addition, he also noted the "deficiencies of the arbitral process." These included:

> The inherent inequality of bargaining power between individual employees and employers necessitates the proscription of mandatory arbitration of employment discrimination claims;
>
> Discovery is typically more limited in arbitration than in court proceedings;
>
> Some remedies available in court, such as punitive damages, are not available in arbitration;
>
> The right to a trial by jury is not available in arbitration; and
>
> Arbitration proceedings are typically private in nature. Arbitration decisions are usually not required to be written and typically go unpublished. Moreover, arbitral decisions are subject to review only under limited circumstances. As a result: (1) arbitrators' decisions, as well as employers and their practices, are not subject to public scrutiny or accountability; (2) the failure of arbitrators to correctly interpret and apply the law is not subject to correction; and (3) the development of our civil rights laws is severely hampered.

While it is true that the National Association of Securities Dealers' proposed rule change eliminating the requirement of mandatory, binding arbitration was recently approved by the SEC, this rule change will not go into effect until January 1999. Moreover, many of the commentators have criticized the rule's implementation delay, and have argued that it is nothing more than a stall tactic by the industry to allow firms time to simply institute their own private binding arbitration rules.

The right to seek redress in a court of law—the right to a jury trial—is one of the most basic rights accorded to employees in this Nation. In the Civil Rights Act of 1991, Congress expressly created this right to a jury trial for employees when it overwhelmingly voted to amend Title VII of the Civil Rights Act of 1964.

The truth of the matter is that today the intent of the Civil Rights Act of 1991 and other civil rights and labor laws, such as the Age Discrimination in Employment Act of 1967, are being circumvented by the securities industry by requiring all employees to submit to mandatory, binding arbitration. In other words, the industry is compelling this practice without regard to the basic civil rights of American workers or their right to secure final resolution of such disputes in a court of law under the rules of fairness and due process.

How then does the practice of mandatory, binding arbitration comport with the purpose and spirit of our Nation's civil rights and sexual harassment laws? Mr. Chairman, the answer, in short—it does not.

I again want to thank you, Mr. Chairman, for calling this hearing. I hope we can work together to put an end to this disturbing practice which robs employees—especially the securities industry employees—of the full protection of our Federal civil rights and sexual harassment laws.

Mr. Chairman, I would ask at this point if we could enter into the record testimony and letters in support of our bill, S. 63, from Judith Appelbaum, Senior Counsel and Director of Legal Programs at the National Women's Law Center; Dennis Vacco, the New York Attorney General; Ellen Vargyas, Legal Counsel for the U.S. Equal Employment Opportunity Commission; Judith Lichtman, President of the National Partnership for Women & Families, and Thomas O'Keefe, the President of the National Association of Investment Professionals.

The CHAIRMAN. It is so ordered that they will all be entered into the record.

Senator FEINGOLD. Thank you.

The CHAIRMAN. Thank you, Senator. Thank you for your patience and continued commitment in this area. I'm deeply impressed.

Congressman Markey, it's good to see you.

Representative MARKEY. Thank you, Mr. Chairman.

The CHAIRMAN. It's good to have you with us.

OPENING STATEMENT OF EDWARD J. MARKEY A U.S. REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS

Representative MARKEY. Thank you, Mr. Chairman. Thank you very much for allowing me to testify here with Senator Feingold this morning.

Since the early 1990's, employers across the country have sought to circumvent our Nation's civil rights laws by forcing employees to sign away their fundamental rights to a court hearing.

The securities industry is the model, but this practice is now extending over to information industries. It is now spreading over into health care fields. It is spreading, in other words, from field to field, as employees are being asked to sign these contracts which waive their own rights; rights which anyone else in America would be able to enforce with regard to the civil rights protections that over the last generation we have worked very hard to put on the books.

As the securities precedent is set and emulated by other industries, this now looms as a threat to millions of Americans' ability to be able to exercise their rights to protect themselves against discrimination because of age, because of sex, because of race. Without action, those rights are going to be eroded significantly.

As a condition of employment or promotion, a growing number of employers are requiring workers to agree to submit any future claims of job discrimination to industry-sponsored, binding arbitration panels. Employees who sign these mandatory arbitration contracts give up their right to due process, trial by jury, the appeals process, full discovery, and other court provided rights. In essence, mandatory arbitration contracts reduce civil rights protections to the status of the company car, a perk which can be denied at will by the employer to the employee.

Just strip them of it. No, you have lost your ability to appeal, to be able to have any additional information. You lost your right because of your age, because of your sex, because of other things that we determine that in our judgment as the employer, you do not have the right to be able to exercise.

While this practice has become increasingly popular among employers in many fields, no industry has employed mandatory arbitration contracts to the same extent as the securities industry. The securities industry is the only industry which requires employees to sign away their civil rights as a condition of licensing. You don't get your license as a broker unless you sign away all of your rights. This licensing agreement is a take-it-or-leave-it offer. Potential employees can agree to mandatory arbitration or they can just seek another profession. There's an option for someone that has always

wanted to get into the financial services world—sign away all of your rights or just go find something else to do with the rest of your life.

Mandatory arbitration of civil rights is wrong even if the arbitration process were a balanced one, but too often it has only a semblance of impartiality. The securities industry, in particular, has transformed a potentially independent judicial environment into one where neutrality is virtually nonexistent. Rather than providing its employees with a quick, inexpensive, and fair alternative dispute resolution forum, Wall Street has established a system which is slow, costly, and often appears biased.

In 1994, I commissioned the General Accounting Office to carefully study Wall Street's arbitration system. The GAO found that an astonishing 89 percent of securities arbitrators were white men over the age of 60 with little or no expertise in the area of employment law. That's unfair to women, it's unfair to blacks, to Hispanics, to every minority. White men over the age of 60 are the jury in every single trial for most of these arbitration cases. At best, such a setting has the appearance of unfairness; at worst, it is a tainted forum in which an employee can never be guaranteed a truly fair hearing. Like forcing employees to buy goods at the company store, the price of such so-called justice is just too high for employees all across the financial services industry.

I am pleased that the securities industry has finally begun to take steps to eliminate its inequitable mandatory arbitration requirement from its licensing agreement, and I applaud the Securities and Exchange Commission's recent decision to approve the NASD's proposed rule change to eliminate the mandatory arbitration clause from its licensing agreement. I am also pleased to hear that the Board of the New York Stock Exchange is expected to vote on a proposal to eliminate its own mandatory arbitration requirement at their next Board meeting in September. I encourage the Board to act quickly to approve this rule change.

Despite the very positive steps taken by the NASD to eliminate its mandatory arbitration requirement, I have concerns about the much delayed implementation date of the NASD rule change. I am particularly worried that this delay may encourage securities firms themselves to use this period to impose individual mandatory arbitration contracts on their employees. Such action would eliminate any real benefit securities employees would have received as a result of the NASD rule change.

The waiting period is particularly questionable in light of a decision by the Ninth Circuit Court of Appeals regarding mandatory arbitration in the securities industry. In the case of *Duffield* v. *Robertson, Stephens & Company*, the court held that the securities industry licensing agreement directly violates the Civil Rights Act of 1991—the Ninth Circuit has just ruled on this. If this arbitration requirement was found to be illegal, why aren't we eliminating it entirely across the country?

Although the NASD will no longer require mandatory arbitration, the NASD arbitration forum will continue to be used by some individual securities firms which have imposed their own mandatory arbitration requirements. I am deeply concerned about the fairness of this forum and, in particular, about a recent NASD pro-

posal to place limitations on punitive damages that can be assessed in employment arbitration cases. I believe this proposal is inconsistent with every Supreme Court decision affirming the legitimacy of using arbitration. The Supreme Court has repeatedly stated that arbitration is acceptable because plaintiffs are entitled to the same rights they would receive in court. The industry cannot have it both ways; placing caps, limitations, on punitive damages while claiming to afford equal protection for those individuals who come before these panels.

As the securities industry begins to take action to eliminate its mandatory arbitration requirement and reform its arbitration system, we must ensure that Wall Street employees are provided with the same access to the courts afforded to other Americans who are subject to discrimination on the basis of race, age, sex, or disability. Workers on Wall Street and all financial services across the country, no matter what city in the country they work in, have a right to a fair, equitable, and voluntary forum in which to resolve discrimination claims.

I understand, Mr. Chairman, that today's hearing is an oversight hearing on arbitration in the securities industry. It is not focused on any particular legislation. But as Senator Feingold has stated, he and I have introduced, along with Representative Constance Morella, legislation which would make mandatory arbitration contracts unenforceable, and which would provide relief to those employees in every industry, not just the securities industry, but in every industry across the country who are required by their employer to sign mandatory arbitration contracts, and would guarantee that no one could be forced to choose between their civil rights and their job.

Mr. Chairman, by conducting this hearing today, you are helping to educate the American people about this growing phenomenon of a precondition being attached to someone being employed in the securities, information, health care fields, and others across the country. Senator Feingold, I think, has done an excellent job here in ensuring that we would have a good discussion. Without your help, of course, that would not be possible. I want to thank you so much for conducting today's hearing.

I agree with you that because of the unfortunate passing of the two heros protecting us here in the Capitol, the hearing has been delayed in such a way that some of the other Senators who wanted to be here could not. But your attention to this is very much appreciated, and I thank you so much.

The CHAIRMAN. Thank you very much, Congressman Markey. I want to thank both you and Senator Feingold.

Let me, if I might, refer, Congressman, to your written testimony. I don't mean to take anything out of context, but you state, "Rather than providing its employees with a quick, inexpensive, and fair alternative dispute resolution forum, Wall Street has established a system which is slow, costly, and often appears biased."

Is there, in your opinion, an alternative to this slow, costly procedure you speak of? I also note that my colleague, Senator Feingold, has referred, as you both have in your written testimony, to the courts.

In providing access for the settlement of disputes, are there any alternatives? Can you think of alternatives? Both you and Senator Feingold have referred to the overcrowded court system. Is there an alternative to what is basically a totally obnoxious practice, the signing away of rights?

You have stated that the GAO report of 1994, on this subject, indicates that the arbitration panels which have been set up are not what they should be. But is there an alternative to the possibility of protracted litigation? You have basically stated that people should not be forced to sign away their rights. I agree with that statement. What is the alternative?

Senator FEINGOLD. Mr. Chairman, I do think there is an alternative. My philosophy on this is——

The CHAIRMAN. By the way, we're not looking at the details of the legislation you have introduced.

Senator FEINGOLD. I'm not suggesting a legislative alternative. What I'm suggesting is that, of course, voluntary arbitration is an option, after the fact of discrimination, and is perfectly reasonable. If somebody believes that they would get adequate remedies and rights in that context, rather than going through the courts, I think that should be available and should be encouraged.

The issue here, though, is mandatory arbitration. I cannot say whether the process within the securities industry or the courts is slower, but I do know, as your Attorney General pointed out, that the remedies and the rights are significantly less in the context of this mandatory arbitration.

My answer would be that we should facilitate the opportunity for voluntary arbitration, but reserve the right for court action. That would provide, without passing any laws other than the ban on mandatory arbitration, an opportunity for a different forum than a court, if someone chose that.

The CHAIRMAN. Congressman Markey.

Representative MARKEY. The industry, not just the securities industry, but every industry argues that the system they have set up is wonderful and fair.

If that's the case, then why don't they allow for an individual who is an employee to decide if they want to put themselves inside of that wonderful and fair system? Why don't they make it voluntary if they're so confident of that?

I think just by giving the employee the ability to voluntarily choose that, would then force each one of these industries to make these forums much more neutral in terms of the likelihood of what the outcome would be.

What we have right now, of course, is a system where ironically it costs $3,000 to $4,000 per day for an employee in forum fees inside one of these mandatory arbitration settings, whereas it would only cost the same employee $150, $150 in a filing fee in court in order to bring their case.

The whole system is set up in a way right now which really doesn't make it voluntary, it doesn't make it fair, but I think just by making it voluntary, we would ensure that the arbitration process became fair.

The CHAIRMAN. Let me ask you one other thing.

You make mention that some of the contracts that people were made to sign, employment contracts in which they agreed to these provisions, at both the New York Stock Exchange and I think at Nasdaq, as of January 1999, would no longer be enforceable.

Is that correct?

If so, what you're asking is why not now?

Representative MARKEY. Why not now? Why not end it? We have just had the circuit court decision. They can make it immediately effective.

The CHAIRMAN. The circuit court decision in your opinion or your interpretation, Congressman, says that they're illegal in any event?

Representative MARKEY. That's correct.

We would have no guarantee at this point that it's going to spread across the rest of the country. It could take a lot of time for the individual employees to gain access to that protection.

The CHAIRMAN. Was that a unanimous decision? I'm trying to get a sense of what the courts are doing. Do you believe that the case will go to the Supreme Court? I know you have been following this and I would like to get your impression.

Do you think it will be affirmed?

Representative MARKEY. There is a pending appeal to the Supreme Court. The Supreme Court has yet to decide whether or not it is going to hear the case. Right now, the employees have had a huge victory in this Ninth Circuit.

The CHAIRMAN. I'm going to pose that question to our various panelists. The Executive Vice President for Dispute Resolution and Chief Hearing Officer at NASD Regulation will be present in the second panel, and I will raise that question.

If my colleagues want to join us, and I know, Senator, you have other pressing matters, and Congressman, I don't want to impose upon your time, but if there are any questions you would like to ask of the panelists, feel free to join us as we invite our second panel.

If you have anything additional, we will keep the record open to receive it and make it available to our other Committee Members. I want to thank both of you for your important work in this area.

I wish more of our colleagues were here, but I'm sure they will be following it through their staffs.

Senator FEINGOLD. Thank you, Mr. Chairman.

Representative MARKEY. The final point that I would make, Mr. Chairman, is that an employee has the same chance to beat an employer in these kind of forums as the Red Socks have of catching the Yankees this year. None. We're trying to level the playing field a little bit.

The CHAIRMAN. That's heresy at home.

Senator FEINGOLD. Mr. Chairman, the only other remark I would make, because you're asking questions about what the Supreme Court would do on this issue, it's a fair question, but I think your gut reaction is the right one. It doesn't matter what the current state of the law is. This is unacceptable.

We should make it illegal.

The CHAIRMAN. Oh, I have a feeling that the Supreme Court is going to concur. I really do. I believe that the Ninth Circuit opinion will be affirmed.

In terms of fairness, it seems to me that these mandatory agreements cannot be tolerated. It is the most involuntary act, to require someone to sign away his or her right to something that every other American, that everyone, should have as a condition of employment. It just seems to me that, on its face, this is something that is rather abhorrent.

I want to commend both of my colleagues and I'm looking forward to the testimony of our other panelists. Thank you for your great work.

I would ask our second panel to be seated, and we thank them for their participation.

On our second panel we will hear the testimony of: Isaac Hunt, Commissioner, U.S. Securities and Exchange Commission; Samuel Estreicher, Professor, New York University School of Law; Cliff Palefsky, Chairman, Securities Industry Arbitration Committee, who is testifying on behalf of the National Employment Lawyers' Association; Linda Fienberg, Executive Vice President for Dispute Resolution and Chief Hearing Officer, NASD Regulation; Stuart Kaswell, Senior Vice President and General Counsel, Securities Industry Association; Elizabeth Toledo, Vice President, National Organization for Women; and Robert Meade, Senior Vice President of the American Arbitration Association.

Commissioner Hunt, it's good to see you again. Your statement will be placed in the record as if read in its entirety, and we would appreciate your comments.

OPENING STATEMENT OF ISAAC C. HUNT, JR., COMMISSIONER U.S. SECURITIES AND EXCHANGE COMMISSION

Commissioner HUNT. Mr. Chairman, like you, I'm sorry there aren't more of your Members here to address this important topic, but I am pleased to offer my comments here today on behalf of the Securities and Exchange Commission concerning the requirement that securities industry employees arbitrate their statutory employment discrimination claims. The Commission commends the Committee for holding this hearing, and we thank you for requesting the Commission's views on this important topic.

Discrimination claims and their resolution touch on sensitive issues of race, gender, age, and workplace conduct. These issues are important to all Americans, not just those employed by the securities industry. But in the last few years, increased attention has been paid to the securities industries' process for resolving such claims.

Securities firms, the self-regulatory organizations, or SRO's, and the Commission have entered into a dialogue as to this process, as has the Equal Employment Opportunity Commission and civil rights and other organizations. The dialogue has been spirited but respectful. We all agree that securities industry employees deserve to work free of discrimination, but some of us differ as to how employees claiming to be the victims of such misconduct should seek redress.

Since coming to the Commission, I have very strongly supported ending the practice of mandatory arbitration for employment discrimination claims. Yet, my views on this subject were shaped long before I came to the Commission. You see, I was the dean of two

law schools and in that capacity I handled numerous employment-related issues.

In addition, in the mid-1980's, I served on several New York Stock Exchange-sponsored arbitration panels. While those panels involved customer rather than employment discrimination or other employment-related disputes, the experience gave me some insights that I believe I can fairly bring to the employment discrimination context.

Finally, like everyone else, I have had many personal life experiences which have influenced my views on topics touching on issues of race, gender, and age in American society.

I was delighted last month when the Commission approved an important change in the rules of the National Association of Securities Dealers. The NASD eliminated its requirement that securities industry employees arbitrate statutory employment discrimination claims under mandatory predispute arbitration clauses included in all securities industry employment agreements.

I congratulate Frank Zarb and Mary Schapiro, their colleagues, such as Ms. Fienberg, and the staffs of the NASD and the Commission for making this initiative come to pass.

The NASD's change is a good beginning. The NASD, after all, administers a very large number of arbitration claims because of its very large membership. The Commission now expects the other SRO's to adopt similar rule changes industrywide. Moreover, this change is a beginning for another reason. SRO rule changes in this area simply put firms and their employees in the position to decide which forum to use to resolve discrimination claims.

The practical effect of any SRO rule change is not certain. Firms simply may redraft their individual employment agreements so that job applicants would have to waive their rights to sue in court as a condition of employment, and those private agreements would not be governed by Commission or SRO regulations, but by contract law and the Federal Arbitration Act.

But not all firms will do that. Already one major broker–dealer firm has said that it will not require its employees to enter into predispute agreements requiring them to arbitrate statutory employment discrimination claims. The Commission also expects other firms to seriously consider giving their employees the option of going to court or going to arbitration under postdispute arbitration agreements.

As a personal matter, I believe that firms should negotiate with their employees on this issue rather than dictate a result. I applaud those firms willing to offer their employees a choice of fora, and I will be disappointed if only a few firms follow suit.

Let me make one thing very clear at this point, Mr. Chairman. The Commission's approval of the NASD's rule change does not indicate that we necessarily consider arbitration to be an inappropriate forum for resolving employment discrimination claims. Securities industry employees, if they wish, should be able to make such claims in arbitration fora. In this regard, the Commission is committed to ensuring that those fora are fair and equitable ones.

The Commission agrees with the SRO's that it is important for them to continue to look closely at their existing procedures concerning training, arbitrator selection, and administration for cases

involving employment discrimination claims. In fact, many SRO's already have expanded their arbitrator recruitment to reach out both to arbitrators with appropriate expertise and to greater numbers of women and minorities.

The Commission also is aware that a committee has been formed with representatives from NASD Regulation, the New York Stock Exchange, and others to study a host of issues related to the arbitration process. The Commission hopes that the results of the committee's efforts is that securities arbitration fora become more attractive to employees for the resolution of their discrimination disputes. If that result occurs, even those employees with a choice of fora may elect to use arbitration as an efficient and fair way to resolve their disputes.

Like the NASD's action approved by the Commission, S. 63, Senator Feingold's bill, distinguishes employment discrimination claims from other claims between employees and employers.

S. 63 would amend the principal Federal civil rights statutes and the Federal Arbitration Act to prevent the application of predispute arbitration clauses from claims that arise for alleged unlawful employment discrimination. The bill would prohibit employers from requiring employees to sign mandatory arbitration agreements as a condition of employment, so-called predispute agreements, but would permit employees and employers to enter voluntarily into arbitration agreements after a claim has arisen, so-called postdispute agreements.

The Commission believes the decision as to whether to amend the Federal civil rights laws and the Federal Arbitration Act is uniquely an issue for Congress to decide. The Commission supports S. 63 if the Congress believes it will enhance the civil rights of securities industry employees.

Notably, in formulating our approach to the NASD rule change, the Commission looked to the studies and to the conclusions of the Equal Employment Opportunity Commission, the Dunlop Commission, and others with expertise in this area. We also considered the views of employers and employees.

We understand that Congress will do the same in considering S. 63, and the Commission stands ready to provide the Congress and this Committee assistance on this important issue.

Once again, Mr. Chairman, the Commission thanks you for offering us the opportunity to appear here today and to provide our thoughts for your consideration.

Thank you very much.

The CHAIRMAN. Thank you very much, Commissioner.

I'm going to attempt to strike a little balance here, so let me recognize Samuel Estreicher, Professor at the New York University School of Law. I have no idea as to how Professor Estreicher is going to testify with respect to this issue.

I have not had an opportunity to review your remarks, so the fact that you're seated at the completely opposite end of Commissioner Hunt is my idea of attempting to get some balance out of this panel.

Professor Estreicher.

OPENING STATEMENT OF SAMUEL ESTREICHER
PROFESSOR, NEW YORK UNIVERSITY SCHOOL OF LAW

Mr. ESTREICHER. Thank you, Senator D'Amato. I applaud the Committee for looking into the issue of mandatory arbitration in the securities industry and for convening this hearing.

Since 1978, I have been teaching labor and employment law at New York University School of Law. I am also Executive Director of NYU's Center for Labor and Employment Law, but nothing I say today reflects the views of the Center. I am here in my individual capacity. In addition to teaching, I serve as counsel to a law firm in New York in the labor and employment field.

I have also been involved, since 1985, with the Center for Public Resources, which is a leading ADR organization in this country, and more recently with the American Arbitration Association in developing fair procedures for pre- and post-dispute mediation and arbitration of employment disputes.

It is my view that predispute agreements to arbitrate employment claims, whether they arise under a contract or under statute, provide a legitimate alternative to litigation with distinct advantages over litigation in that it is likely to offer the prospect of a quicker, less costly, less divisive, less distracting forum for the parties themselves, and often a desirable nonpublic resolution of the dispute. Such agreements, in my view, should be enforced with the important provisn that the procedures that are used conform with the adjudicative quality standards of the leading arbitration and ADR provider organizations, and here I have in mind the work of the American Arbitration Association, JAMS/Endispute, and the Center for Public Resources.

And the enforceability of such agreements is, indeed, the overwhelming view of the courts, beginning with the Supreme Court's decision in *Gilmer* v. *Interstate/Johnson Lane Corp.* and every other court of appeals that has looked at the issue.

There is one exception that has been mentioned earlier this morning, the *Duffield* case in the Ninth Circuit.

I have made a bet with Mr. Palefsky, to my right over here, that if the *Duffield* case is upheld by the Supreme Court, I will take him and his wife out to Lutece in New York and pick up the tab. That's how convinced I am that such an outcome will not occur.

Two or three weeks after *Duffield* was decided, the Third Circuit sitting in Philadelphia took sharp issue with *Duffield*. Every other circuit that has passed on the subject disagrees with *Duffield*.

The only circuit that hasn't ruled on the subject is our own circuit, Senator D'Amato, but it has ruled on this issue in the context of age discrimination claims. And the Second Circuit's view in such cases is that employers and employees can enter into valid, binding, mandatory predispute arbitration agreements whether those agreements cover contractual claims or statutory claims.

The CHAIRMAN. Let me ask you, Professor, at this point, someone wants a job, they're prepared for it, they're qualified, there's no doubt about their qualifications, and in every area they would be judged to be superior and well-qualified and would be hired.

Then they are presented with a form which says basically that they must agree that any disputes that arise will be settled by way of an arbitration proceeding.

Do you think that's voluntary?

Mr. ESTREICHER. Yes, I do.

The reasoning of the courts in these cases is that—and this is an important point that I think may have been obscured by earlier testimony—the only thing that is actually being waived is the judicial forum.

It is absolutely required that the arbitrators apply the relevant statutory law and if a violation is found, award statutory remedies. The only thing being waived is the particular forum——

The CHAIRMAN. In other words—I want to try to get this straight in my own mind—you are talking about a procedure that would guarantee adjudicative standards which would be used in a different process maybe, one that is less burdensome, less costly, and not completely in the public domain.

Would this process apply the applicable standards of law?

Mr. ESTREICHER. Absolutely.

The CHAIRMAN. And that's as a precondition.

Mr. ESTREICHER. Absolutely. That is a precondition of the leading arbitration services organizations.

The CHAIRMAN. Let me ask you this. Is that what we find today as applicable to the industry?

Is that prevalent? In other words, I made this note, adjudicative standards, and that just stuck with me, that this was important to be able to guarantee a process of highest impartial standards that the various groups recognize.

I mean, is that implicit?

Mr. ESTREICHER. First of all, adherence to these standards is the explicit requirement of these organizations before they will provide any arbitrators. Second, we are a very large country making generalization hazardous, but I would say that virtually every company that has adopted a predispute arbitration program, outside the securities industry, does conform to these adjudicative quality standards.

With the caveat, this is a very large country, I may have missed one or two.

The CHAIRMAN. Now let me ask you this. This may or may not be fair to you, I just don't know, but I know you will be able to handle it.

Mr. ESTREICHER. I hope so.

The CHAIRMAN. Yes, you will. You may not have looked at this closely, but I think you have. You knew we were going to talk about how this relates to the securities industry.

Does anybody here have one of these agreements? Mr. Palefsky, do you have one?

I mean, I see you hopping up and down. I'm going to call you next, don't worry.

[Laughter.]

Do you have one of these standard agreements? These agreements are standard, aren't they? Aren't these agreements standard as a condition of employment? Somebody must have one. The Uniform Application for Securities Registration or Transfer, is this the thing?

[Pause.]

You have to check all of these things. I mean, pages and pages. I will bet that very few people have ever read everything encompassed in this. This is it.

Ms. Fienberg, this is the document that is generally used by the industry. Is that correct?

Ms. FIENBERG. That is correct. And in that document, there is an arbitration clause. If you would like, I would be happy to read the provision.

The CHAIRMAN. Pardon me?

Ms. FIENBERG. If you would like, I would be happy to read the provision.

The CHAIRMAN. Would you do that?

Ms. FIENBERG. The provision in the form says:

I agree to arbitrate any dispute, claim, or controversy that may arise between me and my firm, or a customer, or any other person, that is required to be arbitrated under the rules, constitutions, or by-laws of the organizations indicated in Item 10 ...

Item 10 is where you check off whether you will be working for an NASD member, New York Stock Exchange member, or member of some other exchange.

... as may be amended from time to time and that any arbitration award rendered against me may be entered as a judgment in any court of competent jurisdiction.

That's on page 4 of the Form U–4 as it was revised in November 1991. It's a form that is approved by the Securities and Exchange Commission and is used by every self-regulatory organization and all 50 State regulators.

The CHAIRMAN. Professor Estreicher, let me go to the question.

Does this meet your standards? I mean, we're going to hear some people testify that there's a 1994 GAO finding that would seem to cast some doubt with respect to the objective standards that you have articulated, that would guarantee you the proper kind of judicial process, whether it be by arbitration or in a court of law.

Have those standards that you feel are necessary been met by the industry?

Mr. ESTREICHER. Up until now, no.

But I should say this——

The CHAIRMAN. Now, let me tell you something. It's very refreshing to have somebody as candid as you are, so up until now—no, go ahead.

Mr. ESTREICHER. Thanks to the work of Ms. Fienberg and others, I believe that things are changing for the better in the securities industry, because what is happening is that statutory discrimination claims are being taken out of the U–4 process, and this is the case with the NASD.

As you know, Senator D'Amato, the change will also be made for arbitration with the New York Stock Exchange. When that occurs, securities industry employers and securities industry employees will be precisely on the same footing as employers and employees in any other industry in the country.

That means that the securities industry would then, I think, have to develop procedures which conform to the adjudicative quality standards of the leading provider organizations or their awards will not be sustained in the courts.

I should add, though, that while some of the criticisms made of securities industry arbitration are legitimate, many of the assertions are also overblown, as I understand them. For example, with respect to the female composition of NASD arbitrators, as I understand it, the numbers are better than for the Federal District Bench across the country.

But I do think it is problematic to have these agreements required industrywide, as opposed to agreements struck by individual employers and employees, as a condition of employment. We should have a free marketplace among employers and that's important.

I think there's also a problem with the perception of fairness, not necessarily the actuality of fairness, but the perception of fairness when an industry self-regulatory organization develops the panel, and the parties have to choose the arbitrators from that panel.

The CHAIRMAN. I have one last question.

You heard Congressman Markey refer to the cost of arbitration as somewhere in the area of $3,000 a day that the claimant must now pay.

Is that correct?

Mr. ESTREICHER. Forum fees are not common outside of the securities industry at all. My understanding is that forum fees sometimes are waived by the arbitrators in securities cases in their awards, and I should point out that I think this is a problem that does need a legislative fix. The D.C. Circuit sitting here in this town, in an opinion by Judge Harry Edwards, a noted labor scholar before (and after) he ascended to the bench, has made clear that if the forum fees that are being assessed are higher than what a court would charge in civil cases, that feature of the agreement is not enforceable.

The CHAIRMAN. All right. I appreciate your candor, and it would appear to me that you have struck the proper balance, that what is going on and what exists at this time is really not right, it's not proper, and it does not give the kind of objective adjudicative standards that you could be supportive of.

But you're saying that the industry is now headed in the right direction.

Mr. ESTREICHER. If I may add, within 6 months or so, the situation in the securities industry will be the same as elsewhere and there is no need for a specific statute dealing with the securities industry.

The CHAIRMAN. Thank you, Professor Estreicher.

As I said, I'm going to try to get some balance as we go along.

I now call on Mr. Cliff Palefsky, the Chairman of the Securities Industry Arbitration Committee in San Francisco, California, who will be testifying on behalf of the National Employment Lawyers' Association. He was doing like a little Terentino in that seat.

[Laughter.]

Thank you.

Why don't you make whatever observations you have at this point, instead of reading your whole statement. I think it goes a little better. We will place you statement in the record as if read in its entirety. Go ahead.

Mr. PALEFSKY. I don't even have it in front of me.

The CHAIRMAN. Good, let me know what you're thinking.

OPENING STATEMENT OF CLIFF PALEFSKY, CHAIRMAN SECURITIES INDUSTRY ARBITRATION COMMITTEE ON BEHALF OF THE NATIONAL EMPLOYMENT LAWYERS' ASSOCIATION

Mr. PALEFSKY. Let me first allay some of your concerns. We, as employment lawyers, are not only lawyers but also psychiatrists and job counselors, and we know and passionately believe that our clients are better served by avoiding litigation, by resolving cases as quickly as possible and getting back to work.

In fact, I don't think there's an organization in this country that has done more to encourage the use of alternatives to litigation than NELA, and Mr. Meade from the Triple A can confirm that.

In California, I would say that 90 percent of all employment cases get mediated enthusiastically by both sides of the case, and 90 percent of them settle. We strongly encourage alternatives. It's a rare case where anyone benefits by going to court.

More importantly, though, this does not involve merely the issue of discrimination. It really involves the integrity of the laws passed by Congress.

Having had the chance to sit here this week and watch this process in detail, it reminded me of a few things. One is that when Congress passes laws to regulate a particular relationship, like the workplace, it's not up to the employer to pick and choose which sections of that law they want to comply with. When you allow the employer to unilaterally impose an arbitration agreement which not only sets the forum but sets the remedies, picks the arbitrators, and limits discovery, you are literally allowing the people you are regulating to opt out of the laws of Congress.

I also was present yesterday when you introduced a judicial candidate before the Judiciary Committee, and we all are very impressed with the deliberation and the care that goes into selecting judges because we know how hard it is to interpret the laws of Congress.

What we want is not additional rights; we want the laws of Congress interpreted by the judges appointed by the President, confirmed by the Senate, and the Supreme Court, not by retired bond traders, not by people with absolutely no legal background. It does a disservice to the very legislative process.

To put this in a proper social context, this is not a liberal or conservative issue, or a Republican or Democratic issue. In fact, the very first piece of the "Contract with America" that was passed and signed into law made Congress subject to the civil rights laws. Last year, the White House was made subject to the civil rights laws. We're sitting here now where the President of the United States has to sit for a deposition in a sex harassment case, but a branch manager at Smith Barney who operates a "Boom Boom Room" in his basement does not. There's something very skewed about the present situation.

Most importantly, I don't want you to think that it is the plaintiff's bar or the civil rights bar on one side and the academic and the neutral community on the other side. The National Academy of Arbitrators, which is probably the most distinguished professional organization of arbitrators in the world, has opposed mandatory arbitration as a condition of employment. They have specifically gone

to court, challenging the securities industry system, saying that that system in particular does not conform to the minimum standards necessary.

Professor Estreicher referred to those minimum standards. They were embodied in the Dunlop Commission, they are embodied in the due process protocol, both of which have been out for 4 years now.

I am very concerned because the securities industry system does not conform, and I'm concerned as to why they don't conform. It is important to note that the Triple A and JAMS/Endispute would not arbitrate a case today under the rules that are used in the securities industry.

My concern is that the reason that the due process protocol has not been adopted, the reason the securities industry does not have special employment rules that have been adopted——

The CHAIRMAN. You said the due process?

Mr. PALEFSKY. Protocol.

The CHAIRMAN. Protocol.

Mr. PALEFSKY. Probably 10 different organizations comprising the ABA, the Federal Arbitration and Mediation Service, the American Arbitration Association, the Defense Bar, and the Plaintiffs Bar, have all agreed on minimum standards of due process.

The CHAIRMAN. Let me ask you this. If the due process protocol were to be a part of this employment contract, what would your feeling be? Would that be wrong, would that be right?

Mr. PALEFSKY. If the decision to elect arbitration was voluntary, I think it would be a great development, because arbitration can be a good way to resolve certain cases.

One of the things which I really want to make clear to everyone is that arbitration is not just another forum. Like every other system, it has its advantages and disadvantages, and it would be malpractice for a practicing lawyer not to be aware of those distinctions. If I can characterize it, it's the difference between a justice system where reaching the legally correct result is the ultimate aim, versus a dispute resolution system where finality is the goal. There are many disputes where just getting it over, right or wrong, is your goal. That's what arbitration is.

Contrary to what Professor Estreicher said, the present standards in arbitration do not require arbitrators to either know or follow the law. An incorrect award that is incorrect on its face is not subject to review or appeal. In fact, unlike every other single arbitration forum in this country, the securities arbitrators are told in writing in advance that you are not bound by statutory law. That's a remarkable directive.

My concern is that we have been bringing this to their attention for 4 years now, and it's only when *20/20* or *The Wall Street Journal* makes enough noise, that we can get their attention.

With all due respect to the SEC, I appreciate Commissioner Hunt's statements. I agree with him, but we hope for and we need a lot more than wishful thinking from the SEC.

The courts are relying on the SEC to oversee this process and if, in fact, they think it's a good idea, we would ask them to respect the policy decisions of the EEOC, which said make the NASD rule change effective immediately.

The CHAIRMAN. I'm going to ask that we take a 3-minute recess. I have a telephone call to make, and if you would wait right here, it will only take 3 minutes and I'll be right back.

[Recess.]

The CHAIRMAN. All right, let's do a little something unusual. Who would like to be the next panelist to make their remarks?

[Laughter.]

I have never seen, in my 17 plus years here, anyone running one of these hearings ask for that help.

Who wants to volunteer? Who is waiting?

Ms. FIENBERG. I will be happy to address the Committee.

The CHAIRMAN. OK, very good.

Ms. FIENBERG. Thank you, Chairman D'Amato.

The CHAIRMAN. We will now hear from Linda Fienberg, the Executive Vice President for Dispute Resolution and Chief Hearing Officer of NASD Regulation.

OPENING STATEMENT OF LINDA D. FIENBERG EXECUTIVE VICE PRESIDENT, DISPUTE RESOLUTION AND CHIEF HEARING OFFICER, NASD REGULATION

Ms. FIENBERG. Thank you for inviting me to testify today. I appreciate the opportunity to be here on behalf of NASD Regulation.

First, let me say we operate the largest dispute resolution forum in the securities area. Last year, 6,000 claims were filed with us, which is about 90 percent of all claims filed with the SRO's. Most of our claims are investor claims, in fact, about 80 percent.

The CHAIRMAN. By the way, isn't there a clear distinction between employment dispute resolution as it relates to matters of discrimination, and then all those claims that fall into the area of whether or not the sale was or was not completed or whether somebody did something outside of the scope, whether it's a broker or otherwise, didn't follow the customer's instructions, et cetera? Can we all agree on that?

Mr. PALEFSKY. There is a definite distinction, but there is something in between like whistle-blower cases.

The CHAIRMAN. I'm not saying that we're taking in everything, but if 90 percent or so of the cases fall in with respect to whether or not a transaction was undertaken with the proper authority, the knowledge, or whether it was delegated, that's really a lot different, and I see the Professor's——

Mr. ESTREICHER. I'm not sure that's right, Senator D'Amato.

The CHAIRMAN. I have a feeling. Let me say this to you. I have a very strong feeling that there's a different standard.

I have no problem as it relates to seeing to it that you, number one, have the kind of system that you spoke to, one that guarantees, and I think both Mr. Palefsky and yourself, Professor, spoke to it, whether you have due process protocol or you have adjudicative standards that meet the levels that are going to try to get people real justice.

But, boy, I'll tell you, as it relates to whether or not someone has been discriminated against because of age or sex, I would be very, very careful before anybody has to sign an agreement that would limit their rights.

I just have a basic feeling about this.

As it relates to the process of monetary disputes, I think those are a lot easier and clearer to determine, and you can more easily set up ways in which to move that process.

If you had to litigate every single claim from a broker whose clients said, well, you didn't sell when I told you to, or you sold when I didn't tell you—there is no court system in the world that can handle that kind of thing. I think we have to make a distinction.

Mr. ESTREICHER. Could I swim upstream and attempt to counter that a bit?

The CHAIRMAN. Yes, I only took one labor law course, so——

Mr. ESTREICHER. Cases, as Justice Brennan said, are a collection of facts; they are factual disputes. And you can have a dispute between the company and the customer, there could be contractual theories coming out of those facts, there could also be theories under 10(b)(5) of the securities laws, and there could be theories under RICO, and there could be statutory claims.

And so too in employment discrimination cases. You look at most of the cases filed in the Federal District Courts in 1997. Most of those are garden variety factual disputes. The company says the employee did a lousy job. The employee says, no, I didn't. I was a decent employee; it must have been because of my age, my race, my disability.

Those are, I would submit to you, 95 percent of the employment claims. We're talking about facts and legal theories that come out of facts.

When you have an agreement, the arbitration agreement says that the entire factual dispute goes to arbitration.

The CHAIRMAN. Yes, Commissioner.

Commissioner HUNT. If I could disagree with the Professor as a former professor myself, I would argue that even though Congressman Markey talked about 80 percent of the arbitrators being white men over 60, I have always argued that they were uniquely unqualified to handle cases like this—the kind we're talking about—although probably adequate to handle the ordinary, run-of-the-mill broker–customer group to which you refer.

Even though the panels on which I served were more diverse than 80 percent 60-year-old white men—the New York Stock Exchange had a more diverse panel of arbitrators—I still would argue that the panels for either the broker–dealer community in NASD as presently constituted or the New York Stock Exchange or the other exchanges are ill-equipped to handle the kind of claims we're talking about, even though I would argue that they are equipped to handle the ordinary business dispute in the brokerage industry.

The CHAIRMAN. All right.

Ms. FIENBERG. I believe I can address that and talk about what it is that we have done already to change a lot of the perceptions I think have been given today, and things we are doing as we go forward.

Put in further context, of the 1,200 or so intra-industry disputes, those that involve employees and members, apart from the customer cases, only 139 of those filed last year, that's less than 2.3 percent, involved discrimination. Although we are making huge improvements in the fora to address these claims, they are a very, very small part of what we are about as a neutral forum.

There are a couple of things I think are important to keep in mind. It is only brokers who deal with the public in selling securities and their supervisors who are required to sign the Form U–4. Administrative and clerical people are not required to sign that document, and therefore are not required by the SRO's to arbitrate.

Further, the arbitration forums do not recognize class actions. Accordingly, any employee of a securities firm, albeit a registered or a nonregistered person, can bring a class action lawsuit to assert discrimination in any Federal or State court in the country.

I would like to talk specifically about changes we have made in the forum up to this date and changes we are making which we will be presenting to our Board in October and shortly thereafter to the SEC for approval. First, in our forum, in a discrimination case, and in most other kinds of employment cases, the panel of three arbitrators is a panel consisting of two of what we call public arbitrators and one industry arbitrator. The public arbitrators cannot have had any involvement with the securities industry or any conflicts in that regard.

Second, there is no limit in terms of substantive remedies, that is, compensatory damages or punitive damages, in our forum for employment cases, and none is contemplated.

There is in the Title VII Statute itself, which Congress passed, a $300,000 cap on punitive damages, and arbitrators would be expected to follow that law under Title VII. But there's no cap, apart from the laws Congress has passed, that applies to employment law in our forum and, as I said, none is contemplated.

Third, the roster has changed since the GAO report in 1994 which found that 89 percent of the people who were in both our and the New York Stock Exchange rosters were white males over the age of 60.

The CHAIRMAN. We're not condemning all white males who have reached the age of 60. I mean, Saturday, I'll be 61.

Ms. FIENBERG. Half of our discrimination claims are claims filed by white men over 40 alleging age discrimination. I think that gives another perspective to that.

But that aside, we are very, very interested across the board in having a diversified roster. We now have 16.3 percent women on our roster. That's still not sufficient and that's one of our major goals. Five percent of our roster consists of minorities.

When employment discrimination cases are filed, we attempt to panel those cases with people who have employment expertise and are representative of the diversity of the people who are involved in the lawsuit.

Further, all arbitration awards issued by the SRO are public. There was some indication from someone that these awards are not public. That's not true. All arbitration awards are public. We make them available to anybody who asks for them. The fact of an arbitration award is noted on every firm's CRD form.

Fourth, the win rate for customers and employees I submit is much higher in arbitration than it would be in court. Customers win approximately 60 percent of all arbitration cases filed at the NASD. That, in part, is because arbitrators apply equitable principles and try to do the right thing, and those figures wouldn't be nearly so high if they were in court.

In discrimination cases, employees win approximately 35 percent of the cases that go to award. Again, I believe they are much more successful in arbitration than they would be in court.

We have, in the last number of years, intensified our recruitment to increase the diversity. We have conducted training across the country in the employment law area. Those are the things we have already done, but we are looking at the due process protocol, and we expect to make recommendations to our Board for its October meeting that will endorse almost all aspects of that due process protocol.

The CHAIRMAN. Mr. Palefsky, how do you feel about that?

Mr. PALEFSKY. I think neutrality is a lot like pregnancy. You can't be half pregnant. You can't be half fair.

The CHAIRMAN. Good heavens, I give you the greatest opportunity and you just go with it. Don't be so understated.

[Laughter.]

Ms. FIENBERG. If I can say, I have a Board that I have to go to and I have to go to the SEC for approval, so obviously what I say about what we're going to do has to be somewhat guarded.

The CHAIRMAN. I want to ask this. What your problem is, is that Ms. Fienberg, when she talked about the due process protocol, said "almost" all aspects and you think it should be "all" aspects.

Is that correct?

Mr. PALEFSKY. That's right.

The CHAIRMAN. OK. If it were "all" aspects, if it was the whole protocol, how would you feel about that?

Mr. PALEFSKY. I would think that would be a dramatically positive development.

However, the author of the protocol, Arnold Zack, the President of the National Academy, says the first and foremost element is that there be a neutral organization selecting the arbitrators. I don't think that is yet on the agenda.

Ms. FIENBERG. Mr. Palefsky is not correct about that. I didn't get a chance to finish all of the things we are planning to do.

We are planning to establish specialized rosters of arbitrators who will hear these cases, who will be picked very similarly to the processes recently incorporated by the Triple A for these kinds of cases.

Also, we have filed part of our proposal of a list selection method of choosing arbitrators with the SEC for approval, where the parties will be given lists of arbitrators and will be able to choose.

The CHAIRMAN. Let me ask you one thing, and this is unfair, I think, to a certain extent.

You said most of the protocol. Are you familiar with that area? Can you share with us at this time why it's most and not all, because I gather, again, there are some similarities in terms of the points of views that Professor Estreicher and Mr. Palefsky have?

One thing is that this process must meet the test, the adjudicative standards test, of one that is going to seek justice.

So why not all of the protocol?

Ms. FIENBERG. We are in the process of examining that. I have to take my recommendations to a board. I have to go to the SEC for approval.

The CHAIRMAN. As Chairman of the Committee, and I am not Chairman of the Subcommittee on Securities, but I think when you start hedging like that, you give people reason to be insecure. I don't mean you personally, I think the Nasdaq people have been doing great things, particularly under the leadership of my friend and former colleague, colleague in terms of Government service, Frank Zarb. He does an excellent job.

I think he's brought great distinction in doing lots of things positively, but I don't think that you do yourself or your efforts, which seem to me to be very concentrated in a relatively short period of time, justice when you say "most of them" are included and "we're in the process of looking at them."

I understand you have to meet with your colleagues to further discuss the matter, but the SEC certainly is not going to, in any way, quarrel with you adopting all of the protocol. I can assure you of that, and I believe Commissioner Hunt would agree with that.

Is that correct, Commissioner?

Commissioner HUNT. I think that would be right.

The CHAIRMAN. They are certainly not going to dispute that.

I would just leave this to you, if you're moving in the right direction. I want to commend you to take a look at the total protocol. If you want to keep a system from being overburdened with costly litigation as it relates to the resolution of disputes with customers, et cetera, on the economic side, then I would suggest you use the total process.

Now, as it relates to the other areas, as it relates to discrimination, et cetera, I have to tell you that I wouldn't like having to sign away my right to bring a suit that every other American might have a right to bring.

But reasonable people might differ on that. Go ahead.

Ms. FIENBERG. I didn't mean to suggest, Senator, that we had rejected any parts of them. We are still in the evaluation process.

I guess I would rather be understated than overstated.

The CHAIRMAN. OK, sure.

Ms. FIENBERG. I don't have anything further to add, but I would be happy to answer any other questions you might have.

The CHAIRMAN. We are deeply appreciative of the facts that you bring, and the special knowledge and understanding you have on the subject. I think Mr. Kaswell almost volunteered before you did, but you got there first, so I'm now going to call Mr. Kaswell.

OPENING STATEMENT OF STUART J. KASWELL, SENIOR VICE PRESIDENT AND GENERAL COUNSEL SECURITIES INDUSTRY ASSOCIATION

Mr. KASWELL. Thank you, Mr. Chairman. My name is Stuart Kaswell, and I am Senior Vice President and General Counsel of the Securities Industry Association. The SIA commends you for holding today's hearing, and I appreciate the opportunity to testify.

The CHAIRMAN. Mr. Kaswell, do me a favor.

Mr. KASWELL. Yes, sir.

The CHAIRMAN. Boil it down, and let's talk about that part of the dispute resolution process that exists today as it relates to discrimination. At this point, that's what we're focusing on, and I don't want to get into the other area, OK?

Mr. KASWELL. Yes, sir.

The CHAIRMAN. Tell me, should the practice be continued as it is? Should it be changed? Where are we?

Mr. KASWELL. Well, sir, I think I can make a few points that address that issue. First, I want to correct one thing that some others have stated, and that is that by choosing arbitration, people are choosing their rights—they have to make a choice between their rights and their job, and we just don't agree with that. We think they are choosing their forum and not their rights.

The CHAIRMAN. Wait a minute. Can anybody get hired without signing this document and making a decision?

Mr. KASWELL. Senator——

The CHAIRMAN. Now, look.

Mr. KASWELL. May I make my statement?

The CHAIRMAN. This is my forum.

Mr. KASWELL. Yes, sir.

The CHAIRMAN. You don't have to testify, but I try to be fair. I really try.

But I want to know if somebody applies for a position and doesn't agree that all disputes, including those that cover whether or not they have been discriminated against because of age, race, creed, sex, et cetera, if that person doesn't sign and agree to arbitration, they don't get hired; do they?

Mr. KASWELL. Yes, sir, that's correct.

The CHAIRMAN. They don't get hired.

Mr. KASWELL. They do not get hired in the current situation, yes, sir, that's correct.

The CHAIRMAN. All right. You may think that's voluntary, but I don't believe it is. We may agree or not agree as to the proper forums to give people legal redress. That is, absolutely reasonable people can disagree. I'm telling you, however, that if a person is required to sign and say that I waive my rights to go to court as a condition of employment, I don't think it's voluntary.

If the whole industry has this as a pattern, how voluntary is it? What you're saying is, if you want to work in this industry, you have to give up the right that other people would maintain in other areas of employment. In other words, that they can bring suit; isn't that true?

Mr. KASWELL. Yes.

The CHAIRMAN. OK.

Mr. KASWELL. The situation now with the current Form U–4 has required all industry registered representatives to agree to arbitrate their disputes in an SRO-sponsored forum.

The CHAIRMAN. Right.

Mr. KASWELL. We have supported the change that has been discussed here.

The CHAIRMAN. All right.

Mr. KASWELL. For that reason, we understand it will now be a matter of agreement between the firm and the registered representative as to how they're going to handle the situation.

We already know that one firm, the largest in the industry, has said that they are not going to require registered representatives to sign predispute arbitration agreements, and others are exploring other alternatives outside SRO-sponsored fora.

We believe there is a lot of opportunity coming when this new rule takes effect in January, and that there will be competition and there will be alternatives available to people. I can't tell you that I know which ones will be available yet, but we're very hopeful.

The CHAIRMAN. Good. We came a long way.

Mr. KASWELL. I can be trained, sir.

[Laughter.]

The CHAIRMAN. Do you want to make some other points?

Mr. KASWELL. I have a couple of other points.

The CHAIRMAN. Sure.

Mr. KASWELL. With respect to the demographics that have been discussed here earlier, we looked at New York Stock Exchange arbitration cases involving women who alleged that they had been discriminated against, and we found that in 86 percent of those cases, the panels included a female arbitrator. We believe there is a big change taking place.

The CHAIRMAN. You are saying that there has been a change between the report of 1994 and the situation that exists today. I think Commissioner Hunt agrees with that as well.

Commissioner HUNT. I just thought that my experience was always that the New York Stock Exchange panels were much more diverse than the industrywide panels. There were always women and minorities represented on New York Stock Exchange panels.

Mr. KASWELL. We, like everyone else here, are just not satisfied that everything has gone as far as it should. We want to see more diversity.

The CHAIRMAN. But what do you think about the due process protocol? Shouldn't that be something that you operate by?

Mr. KASWELL. We are supportive. We haven't seen the proposal, so it's a little difficult to react with specificity.

We believe the NASD process is very fair. They have gone a long way and we will be looking to see that proposal.

The CHAIRMAN. OK.

Before I call on Ms. Toledo, I'm going to take another 2-minute break. I have another call to make.

I'm sorry, but everyone is leaving town, and we're trying to wrap things up. When I return, I would be interested in hearing your comments.

[Recess.]

The CHAIRMAN. We are now going to hear from Elizabeth Toledo, Vice President of the National Organization for Women.

OPENING STATEMENT OF ELIZABETH TOLEDO VICE PRESIDENT, NATIONAL ORGANIZATION FOR WOMEN

Ms. TOLEDO. Thank you. Patricia Ireland was called away on an emergency family matter.

The CHAIRMAN. I kept looking for her.

Ms. TOLEDO. I didn't look like her.

[Laughter.]

She regrets not being here.

Thank you for the opportunity to submit testimony on behalf of the National Organization for Women. I am Vice President of the largest group of feminist activists in the United States. Since NOW is dedicated to ending discrimination of all kinds, we are keenly in-

terested in ending mandatory arbitration in the securities industry, and nationwide.

We believe that due to mandatory arbitration, the securities industry is still dominated by white men. Women and people of color are forced to work in offices where many managers have little fear of—or respect for—civil rights laws. As a result, we have become engaged in many cases where women have suffered egregious discrimination with absolutely no recourse, and continue today to suffer great injustices.

Today, I want to focus on the impact of these policies on women and people of color in the industry itself, and to talk about the consequences for the industry and the Nation.

The human cost of this system has been high. It has created a hostile work environment of which many cases have arisen. We have heard today about the now infamous "Boom Boom Room."

Although the "Boom Boom Room" is perhaps the most notorious abuse at Smith Barney, it is not the most egregious. For example, complaints regarding pregnancy discrimination, sex discrimination, and sexual harassment include women like Roberta Thomann, a senior sales assistant when she went on an 8-week maternity leave, who reports that she was notified only days before her scheduled return to work that she would be demoted, whereas male employees who take medical leaves of absence had not historically been demoted.

Judith Mione, a 40-year veteran in the securities industry who has successfully completed the licensing exams for registered representatives under Uniform State Securities and Branch Office Manager, complains that she was repeatedly denied the opportunity to advance in managerial positions at Smith Barney. Even though men with less qualifications and experience were hired to fill such positions, and despite repeated applications and interviews, she was forced to take a position as a sales assistant. During one interview, Ms. Mione reports that she was told the ideal candidate would be "some guy with brass balls."

Lydia Klein, a Vice President in Smith Barney's main office in New York City, alleged that she was subjected to sexual harassment. According to the complaint she filed, male employees in her office sent her a calzone in the shape of a penis with ricotta cheese spurting out of one end. On another occasion, she received chocolate candy in the shape of a penis. She also complains that a male supervisor used to look at her breasts and comment, "Ooh, I love them." A male trader also stared at her breasts and would ask, "How they hanging?" Ms. Klein stated that men in the office often referred to women using derogatory terms for female genitalia too grotesque and too offensive to repeat.

All of the 23 named plaintiffs in the Smith Barney case chose the risky course of pursuing a class action suit in an effort to avoid the industry-sponsored mandatory arbitration. They opted for litigation even though the odds of certification of the entire class were very low, and despite the likelihood that their class, even if it was certified, would exclude many of the lower-level staff who were predominantly women.

Why did they choose this course? Perhaps it was because they did not believe in the validity of the arbitration system where they

knew that the majority of arbitrators had been white men over the age of 60, many of whom had been employed in the management ranks of securities firms. Perhaps they preferred litigation because arbitration is binding with no appeals process. Some of the women may seek justice in civil courts because arbitration panel members are not required to be trained or experienced in employment or discrimination law.

Clearly, mandatory arbitration has been bad for employees, and has also cost corporations money. Since the only way women and people of color can hope to have their day in court is to form a class and sue, companies—like Smith Barney—face expensive class action suits in Federal court. The plaintiffs in the Smith Barney case would never have initiated a class action if they could have had access to the courts. Ultimately, even billion-dollar Wall Street companies will benefit when arbitration is an option, not a mandate.

We applaud the recent changes that have been discussed by the NASD and the SEC today. Both have opted to remove the requirement that securities industry employees sign away their civil rights in exchange for a job.

Despite the anticipated changes, we believe it is urgent that Congress move forward to provide immediate relief to women in this industry, and to secure the rights for all employees on Wall Street and across the country. Securities firms have internal personnel policies that require the arbitration of employment discrimination complaints. While we applaud the action taken by the NASD and the SEC, it will prove to be little more than a hollow gesture to women and people of color in the industry who still are locked out of court and deprived of the right to argue their cases in front of an impartial jury and a jury of their peers.

Congress must take immediate action to insure that employees are entitled to the full benefits of the Nation's equal employment opportunity laws. Your failure to act would send a dangerous signal to employers in the securities industry and others.

Since 1991, a growing number of employers have been more motivated than ever to stay out of court. Increasingly, other employers are looking with envy at the securities industry system of mandatory arbitration. We have encountered numerous companies as diverse and varied as JCPenneys and Hooters who are trying to impose this unfair system on their employees, while they ask, quite reasonably, why is it that this system should apply only to the securities industry?

It is imperative that you safeguard the rights of all employees. I urge you to right the wrongs suffered by so many women and people of color by ending mandatory arbitration, first in the securities industry and ultimately in every industry throughout the country.

As we examine the continuing efforts by the industry to self-regulate, we urge you to ensure that they not control the forum and that the mandatory part of mandatory arbitration is removed.

Thank you.

The CHAIRMAN. Thank you very much.

I want to thank Mr. Robert Meade, Senior Vice President of the American Arbitration Association, for his patience, and call upon him now.

Mr. Meade.

OPENING STATEMENT OF ROBERT E. MEADE
SENIOR VICE PRESIDENT
AMERICAN ARBITRATION ASSOCIATION

Mr. MEADE. Mr. Chairman, thank you for this opportunity; I appreciate it. I'm going to touch on some of the developments in the securities area, but what I would like to do is to talk about the alternative and the due process protocol, and add some flesh to the bones of that.

The CHAIRMAN. I would appreciate that.

Mr. MEADE. I would like to remark, though, that this is a much larger issue than employment dispute arbitration. In May of this year, we issued a protocol governing consumer disputes, and today up in Toronto, the President of the American Arbitration Association, President of the American Bar Association, and President of the American Medical Association are issuing a protocol for the arbitration of health care disputes, patient disputes with doctors and with HMO's.

There is the idea of establishing minimum due process procedures and arbitrating individual disputes, whether it be consumer, employment, or health care, as subject to the attention of this association and many of the other organizations cooperating, including Mr. Palefsky's organization.

First, the AAA, my organization, we won't help you if your car breaks down, but we are a nonprofit——

The CHAIRMAN. I was going to do that, but I reconsidered and thought better of it.

[Laughter.]

Mr. MEADE. I saw it in your eyes, so I thought I would get there first.

We are a private, nonprofit 501(c)(3), headquartered in New York City. We have been there for over 70 years. I haven't been there 70 years, but we have been there. We do a great deal of research and development in developing fair dispute resolution procedures, not only arbitration, but mediation, negotiation, and all sorts of dispute resolution.

Last year, we administered well over 78,000 cases around the country and around the world, which represents about one-third of the cases filed in all Federal courts in the Nation. Fifteen thousand of those cases, by the way, were between individuals in labor organizations and companies where they had bargained for the right to arbitrate grievances. I believe that in the labor/management forum, parties feel that this is a very fair, economic, just way to resolve grievances in the employment setting.

Approximately 141 of those cases arose in the securities industry, however, I would say that none of those cases involved employment disputes; they were trading disputes.

There were 1,345 of the 78,000 that involved individual employment complaints outside of the labor/management setting, but only half of those 1,345 cases involved individuals affected by employer-promulgated plans. There is somewhat of a usage of private tribunals to resolve employment disputes, but I believe it's very small measured against the total usage.

Approximately 400 companies have worked with the Association over the past 4 years to design and implement employment dispute

programs. That would equate to covering about 4.5 million people, by a very rough measure.

I would comment that one of the companies we recently worked with was Merrill Lynch, mentioned here previously, I guess, perhaps not by name. On July 1, the beginning of this month, they implemented a new program covering employment disputes that allows the individuals who have signed the U–4 agreement to either opt to arbitrate before an independent agency, including the American Arbitration Association, or to go to the SRO or to court if they have a statutory issue.

So Merrill Lynch, for its some 40,000 employees—however many of those are governed by the U–4—I think is way out ahead of the game in terms of allowing employees with statutory issues to go either to a private forum, an SRO, or to court. That is already in place.

One of the things that we have been doing generally throughout the employment community is educating employers—and, to the extent possible, employees—in the use of alternative dispute resolution systems, mechanisms to resolve disputes on their own, short of having to go to external forums: the voluntary use of internal mediation; peer review, which is another form of dispute resolution; ombudsmen; et cetera, so working with the organizations and the employees to resolve employment disputes without having to go to the outside.

Our policy, the American Arbitration Association policy, on employment disputes is such that we require any company designing an employment dispute program to file a copy of that program with us 30 days prior to it going into effect. We review it for conformance with and adherence to the terms of the protocol which has been discussed here today, and the Association's employment dispute arbitration rules which incorporate the protocol.

The protocol touches upon a number of very basic issues and rights that the individual should have: First, it ensures that the plan clearly state that the individual has the right to counsel if he or she so wishes to be represented, either in a mediation, which is a nonbinding process, or in the arbitration. That has to be abundantly clear.

The plan cannot in any way, shape, or form, reduce the remedies that are available to the individual that would have been available by statute or in court. It can't shorten time limits to file, can't take away punitive damages, attorneys fees, any remedy, the right to reinstate back pay, front pay, et cetera. No remedies can be abridged through these programs.

The timeframe to file must be as allowed by statute. If you have 3 years under statute, you have 3 years under the programs, things of that nature.

The program should clearly state that this does not prevent an individual from filing her or his complaint with the EEOC, the NLRB, the State Human Rights Commission, or the New York City Human Rights Commission if you're in New York. It cannot prevent an individual from going to the agencies responsible for overseeing these programs.

Also, I would like to stress—I mentioned just one moment ago, mediation. We strongly urge, and I think virtually every company

we have worked with has adopted, a mediation step where the parties sit down at a table with a mediator and try to negotiate a settlement. That has been effective in over 90 percent of the cases that have been presented to mediators in a broad range of areas, including employment. It's a very important part of this.

We do administer programs—and this is where Mr. Palefsky and the AAA have had lengthy discussions—we will administer cases where employers mandate arbitration of employment disputes as a condition of employment, as long as they meet the requirements of the due process protocol.

The CHAIRMAN. Which you have just spelled out.

Mr. MEADE. Yes.

The CHAIRMAN. Ms. Toledo, what is your thinking about that?

You don't abridge anybody's rights. People can sue in any forum. But they set up a process whereby you minimize the necessity, the compulsion that people might feel, to take the matter to the courts. By the way, if they want to, they can.

Let me ask you to just think about that. I'll come back to you. You can gather your thoughts on it.

Mr. Meade, have the Nasdaq people or the New York Stock Exchange come to you for some advice as it relates to seeing to it that they have panels which meet the protocol test—fairness, people of ability, et cetera? This business of just having arbitrators, if you don't have the right pool then you have polluted the system.

You have to have a pool, and I think Commissioner Hunt has alluded to that. I think Professor Estreicher said that when he stated he wants to have the kind of judicial process that gives a person the best opportunity for real justice.

How would you work it? If you were going to advise, let's say, whether it's the Nasdaq or anybody else, how would they get their arbitrators to see to it that people are ensured a fair process? Let's suppose it's an employment matter that comes before you, how would you see to it that they have people who are qualified, who are going to give them an opportunity to use this process, and they can feel that their case is going to be heard on the merits?

People want their cases heard on the merits. How would you go about that?

Mr. MEADE. Let me quickly describe the model we use.

The CHAIRMAN. Sure.

Mr. MEADE. The due process protocol was signed by a group of people that negotiated over a period of about 10 months. It was an ecumenical group: Plaintiffs' counsel, labor, unions, corporate counsel, Federal Mediation Conciliation Service, and on and on.

We established a national advisory group which was replicated throughout the United States, of people to nominate and screen the arbitrators and mediators that would come on our employment panel. We created a new panel of approximately 600 people around the United States, based on the recommendation and nominations of people from various walks of life with various interests.

We also mandated that all of the people that came on that panel go through a standard training program that touched upon the process and the law so that we have now created this body, this national body of 600 people, diverse in gender, sex, culture, and background, but all must have 10 to 15 years of experience and a

great deal of familiarity with employment law, and be able to interpret the statutes and the law that's presented to them in the cases they hear.

The CHAIRMAN. Now, let me ask you this. In your due process protocol, if a person signs this, they can still then bring suit if they choose; is that correct?

Mr. MEADE. Not if the program is a mandatory program as a condition of employment. They can still bring suit, but whether or not the court will force them to arbitrate is another issue.

For example, Mr. Cole Burns has been referred to here in this Washington——

Mr. PALEFSKY. The due process protocol does not speak to voluntariness. It only speaks to once you're there, what's fair. The issue of whether it has to be voluntary or not was not something that the defense bar and the plaintiffs bar could agree upon.

Every other neutral entity and the arbitrators themselves have said it has to be voluntary. All of the fundamental underpinnings of arbitration, the limited review, the limited discovery, the risk of an incorrect result, are all dependent on a truly voluntary choice and the submission to someone that you have confidence in.

Mr. ESTREICHER. I want to correct something that Mr. Palefsky said on that. JAMS/Endispute, the National Academy, and AAA—all of them will administer these agreements if they conform to the due process standards.

It is true that the National Academy has taken a position in litigation that these agreements should not be imposed as a condition of employment, but the National Academy's members also administer these agreements.

Ms. TOLEDO. We would be opposed to any system that did not have a voluntary mechanism for entering into this system at its very earliest stages.

The CHAIRMAN. Yes, Mr. Meade.

Mr. MEADE. With respect to, as was mentioned, arbitrators' decisions, if an arbitrator in the employment context is dealing with a statutory issue, she or he must write an opinion that clearly addresses how she or he found under the statute, so that if, subsequently, a court takes a look at that decision, a court can decide whether or not the statutory issues were addressed.

Finally, with respect to the publication of awards, which has been an issue, our National Advisory Committee, which included Mr. Palefsky, has now recommended and we are pursuing finding an outside agency that will begin publishing decisions in this area, probably redacting the name of witnesses, and perhaps the name of the individual, but not the company or the arbitrator so that you can do research on how arbitrators are deciding cases.

Ms. FIENBERG. Not only have we published our awards for many years, but also we make available to all the parties in the forum all of the awards issued by an arbitrator when those arbitrators are on a list from which the parties can select their arbitrators. We have been doing that for many years.

Mr. PALEFSKY. There are very different kinds of awards. The protocol requires a reasoned explanation. Findings and conclusions of law are also required.

But the securities industry, on the other hand, has historically trained their arbitrators not to write opinions and to use only one-sentence awards like "all claims dismissed," specifically to frustrate an appeal.

There is a very big distinction. You can publish those awards, but you can't tell anything from reading them.

The CHAIRMAN. I am going to ask, Professor Estreicher, do you want to end the hearing with any summary that you would like to make? I will then continue on and ask each witness if they would like to include their summaries.

Mr. ESTREICHER. I see a lot of consensus on the need to move the ADR systems into conformity with these adjudicative quality or due process standards.

The CHAIRMAN. I think Ms. Toledo would agree with that.

Ms. TOLEDO. That's right.

Mr. ESTREICHER. The only question really is whether or not these agreements should be left as a matter of contract between the parties, or whether there should be some stipulation by Government that it's outside the realm of contract. That's a little bit of a loaded way of putting the point, but that's really the only question I hear that divides the panel.

Ms. TOLEDO. First of all, we feel very strongly that the industry should not continue to regulate itself, to be outside of the laws and regulations that Congress has set forth for the rest of the Nation. In no way should they regulate themselves.

They should not have any further ability to do anything that is not absolutely voluntary from the outset for employees. We see a very dramatic impact when that happens.

The CHAIRMAN. Mr. Palefsky.

Mr. PALEFSKY. Voluntariness is the one simple solution to everything. If the parties have the ability to themselves guarantee fairness, they will only agree to go if the arbitrator is properly trained, if the forum is fair, and if the right rules are there.

The point I would love to leave you with is—and it pains me to say this—I do not think that the industry should be allowed to run its own forum anymore. There may have been a reason many years ago, but in 1998, there are so many truly neutral forums.

You can see the distinction. I just think it's a huge mistake.

The CHAIRMAN. Professor Estreicher, do you agree with that?

Mr. ESTREICHER. Yes, I do.

The CHAIRMAN. Mr. Meade.

Mr. MEADE. Thank you for the opportunity and happy birthday.

The CHAIRMAN. Thank you, Mr. Meade.

Mr. Kaswell.

Mr. KASWELL. I agree, happy birthday, Senator.

We believe that a lot is about to change in this environment as the new rules take effect. There will be more choices available to people.

We would disagree with the characterization that the securities industry has some sort of hammerlock control over the arbitration fora that are SRO-sponsored. They report to the SEC, not to us.

Thank you.

The CHAIRMAN. Ms. Fienberg.

Ms. FIENBERG. I would only say that we do not consider ourselves to be an industry forum. We run a neutral forum.

The disproportionate number of awards for customers certainly demonstrates this. What happens is that the broker–dealer firms subsidize the cost of the forum; otherwise, it would be much more costly for investors to be able to bring their cases, either before the AAA or in court.

The CHAIRMAN. I would like to see you do something as an industry. It seems to me that mandatory arbitration makes a lot of sense as it relates to disputes that center around a business transaction.

I believe that you have a right to say, this is the way disputes are going to be settled. I honestly do.

As it relates to the terms of employment, I think that's a very different matter. It would appear that you would want to try to encourage a voluntary system that would be less costly to all concerned, and in which a person has a right to choose the forum that he or she might want.

That's a different area. That's my opinion. Indeed, if you have Merrill Lynch moving in that direction, I would hope that others would look at that.

In the fullness of time, I think you bring much more credibility, particularly given some of the egregious situations, and you always get egregious ones, as Ms. Toledo pointed out. But I believe there is a very clear distinction between those cases and the arbitration proceedings, 90 plus percent of them which center around business transactions.

It's that other area, the one which includes the possibility of people being forced into arbitration and of those who feel they have no recourse from an unjust process, that's a different matter. Those who believe they really have been discharged because of age, because of sex, that's a whole different matter. I feel it should have different treatment.

Commissioner HUNT. I wanted to say happy birthday too, since we share the same birth date and we both will be over the age of 60 tomorrow, but obviously I'm not white.

[Laughter.]

The CHAIRMAN. Commissioner Hunt, only you could get away with that.

[Laughter.]

Commissioner HUNT. I did want to say that your gut feeling about these contracts reminds me of a contractual doctrine, that is, contracts of adhesion by people with vastly different bargaining power, and that sounds like an unconscionable contract.

When you have Merrill Lynch dealing with one person, take it or leave it, because you have to sign this, some courts would have held that to be an unconscionable contract.

Your feeling, I think, Mr. Chairman, is right.

The CHAIRMAN. I want to thank all of the panelists for being so patient, for coming in on a Friday, not always an easy time.

I want to thank you for your candor, and I wanted it to be candid because I wanted to get a real feeling as to what the industry was doing, where you were moving, what the rules of the road are.

Professor Estreicher, I am extremely privileged to have met you in person. I have read about you, and to meet you is a wonderful thing.

Mr. Meade, I didn't get into the AAA, I was going to make that crack.

I want to say, Ms. Toledo, indeed, NOW is very fortunate to have someone such as yourself as the Vice President. Thank you very much for coming in.

Mr. Kaswell, you did a good job under difficult circumstances.

Ms. Fienberg, I think you continue to move the goals in the right direction.

I hope my colleagues will have an opportunity to review these matters when they return.

We stand in recess.

[Whereupon, at 12:12 p.m., Friday, July 31, 1998, the hearing was adjourned.]

[Prepared statements and additional material supplied for the record follow:]

PREPARED STATEMENT OF SENATOR ALFONSE M. D'AMATO

Today the Committee meets to examine an issue of great importance ... the use of mandatory arbitration agreements in the securities industry, especially as they relate to claims of discrimination.

There is simply no place for discrimination in the workplace, or anywhere else. Discrimination undermines the very system of meritocracy and individual achievement that makes America great. People should be judged on the basis of their ability, not on the color of their skin, gender, ethnic background, religious affiliations, or any other irrelevant basis. The practice of discrimination must not be tolerated, and we must do all that we can to ensure that discrimination has no place in the workplace.

For this reason, we need to address the genuine abuses that persist in the modern working environment, and we must ensure that every working man and woman has an opportunity for redress and access to the legal avenues needed to confront and prevent discrimination.

Mandatory arbitration of disputes is a longstanding practice in the securities industry. For years, employees in securities firms have been required to sign such an agreement as a condition of employment, mandating that all disputes be settled by way of arbitration, rather than litigation. Customer disputes, as well as disputes between securities firms, are also subject to arbitration.

There are those who believe that the arbitration process of the securities industry should exclude claims of discrimination. Let me make it clear: A system of arbitration which fosters discrimination cannot be permitted to stand. But the reality of our overburdened court system demonstrates that we need to allow for the option of arbitration where it is deemed appropriate.

The Federal securities laws, over which this Committee has jurisdiction, embody a unique scheme of self-regulation by the securities industry and markets subject to the authority of the Securities and Exchange Commission. As a result of concerns raised about the inclusion of discrimination claims in the industry's commonly used arbitration process, many changes have already been made.

Recently, the National Association of Securities Dealers changed its rule regarding its mandatory arbitration process. In addition, I was very gratified to receive a letter from the New York Stock Exchange announcing that at their September meeting, the NYSE Board expects, and I quote, "to submit our rule change to the SEC and have it in place by January 1, 1999." I look forward to hearing about these positive developments during the course of this hearing.

I want to commend Senator Feingold and Congressman Markey for focusing attention on this important matter. They have both studied the issue carefully and are here to share their views. I thank my distinguished colleagues for their diligence, and for joining us today. I look forward to hearing their testimony, as well as the testimony of our other distinguished witnesses, including Commissioner Hunt of the Securities and Exchange Commission.

PREPARED STATEMENT OF EDWARD J. MARKEY

A U.S. REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS

JULY 31, 1998

Mr. Chairman, Senator Sarbanes, Members of the Committee, good morning. I would like to thank you for holding this hearing this morning, so that we might have the opportunity to more fully examine the arbitration system of the securities industry and its inherent inequities.

Since the early 1990's, employers across the country have sought to circumvent our Nation's civil rights laws by forcing employees to sign away their fundamental rights to a court hearing. As a condition of hiring or promotion, a growing number of employers are requiring employees to agree to submit any future claims of job discrimination to binding arbitration panels. Employees who sign these mandatory arbitration contracts give up their right to due process, trial by jury, the appeals process, full discovery, and other court provided rights. In essence, mandatory arbitration contracts reduce civil rights protections to the status of the company car, a perk which can be denied at will.

And while this practice has become increasingly popular among employers in the fields such as information technology, health care, and engineering, no industry has employed mandatory arbitration contracts to the same extent as the securities industry. The securities industry is the only industry which requires employees to sign away their civil rights as a condition of licensing. Anyone wishing to work as

a registered representative for any securities firm in the United States must agree to submit future claims of job discrimination and sexual harassment to *industry-sponsored* arbitration panels. This licensing agreement is a take-it-or-leave-it offer; potential employees can either agree to mandatory arbitration or can seek another profession.

Mandatory arbitration of civil rights is wrong even if the arbitration process were a balanced one, but too often it has only a semblance of impartiality. The securities industry, in particular, has transformed a potentially impartial and independent judicial environment into one where neutrality and independence are virtually nonexistent. Rather than providing its employees with a quick, inexpensive, and fair alternative dispute resolution forum, Wall Street has established a system which is slow, costly, and often appears biased.

In 1994, I commissioned the General Accounting Office to carefully study Wall Street's arbitration system. The GAO found that an astonishing 89 percent of securities arbitrators were white men over the age of 60 with little or no expertise in the area of employment law. At best, such a setting has the appearance of unfairness; at worst, it is a tainted forum in which an employee can never be guaranteed a truly fair hearing. Like forcing employees to buy goods at the company store, the price of such so-called justice is just too high.

I am pleased that the securities industry has finally begun to take steps to eliminate its inequitable mandatory arbitration requirement from its licensing agreement, and I applaud the Securities and Exchange Commission's recent decision to approve the National Association of Securities Dealers' proposed rule change to eliminate the mandatory arbitration clause from its licensing agreement. I am also pleased to hear that the Board of the New York Stock Exchange is expected to vote on a proposal to eliminate its own mandatory arbitration requirement at their next Board meeting in September. I encourage the NYSE Board to act quickly to approve this rule change.

Despite the positive steps taken by the NASD to eliminate its mandatory arbitration requirement, I have concerns about the much delayed implementation date of the NASD rule change. Although the NASD Board voted to eliminate the mandatory arbitration requirement from its licensing agreement last August, the rule change approved by the SEC does not take effect until the beginning of 1999. I do not understand the rationale for requiring Wall Street employees to wait 18 months after the NASD voted to eliminate this requirement to fully exercise their constitutional and civil rights. This delay may merely encourage securities firms to use the interim period to impose individual mandatory arbitration contracts on their employees. Such action would eliminate any real benefit securities employees would have received as a result of the NASD rule change. Wall Street employees have waited long enough to receive their right to a day in court; they should not have to wait one more day to fully exercise their constitutional and civil rights.

The proposed waiting period is particularly questionable in light of a recent decision by the Ninth U.S. Circuit Court of Appeals regarding mandatory arbitration in the securities industry. In the case of *Duffield v. Robertson, Stephens & Company*, the court specifically examined the legality of the securities industry's licensing agreement, the Form U–4, and found that it was in violation of the Civil Rights Act of 1991. In its decisive ruling, the court stated that the "Form U–4 compels precisely what Congress intended to prohibit in the 1991 Act: mandatory arbitration requirements under which prospective employees agree as a condition of employment to surrender their rights to litigate future Title VII claims in a judicial forum and accept arbitration instead." If the mandatory arbitration requirement of the Form U–4 is of doubtful legality, why aren't we eliminating it immediately?

Although the NASD will no longer require its registered representatives to use the NASD arbitration forum, some individual securities firms will continue to use this forum to resolve employment disputes with employees who have signed company contracts with mandatory arbitration requirements. I'm very concerned about the fairness of this system and, in particular, about a recent NASD proposal to place limitations on punitive damages that can be assessed in employment arbitration cases. I believe this proposal, which would limit the sole recourse employees have to punish wrongful behavior by securities firms, is inconsistent with every Supreme Court decision affirming the legitimacy of using arbitration for statutory claims. The U.S. Supreme Court has repeatedly stated that arbitration is an acceptable forum for litigation *because* plaintiffs are entitled to the same rights and protections in arbitration as they receive in court. The industry can't have it both ways; placing caps on punitive damages while claiming to afford equal protection.

As the securities industry begins to take action to eliminate its mandatory arbitration requirement and reform its arbitration system, we must ensure that Wall Street employees are provided with the same access to the courts afforded to other

Americans who are subject to discrimination on the basis of race, age, sex, or disability. Workers on Wall Street must have a fair, equitable, and voluntary forum in which to resolve Title VII claims.

I understand that today's hearing is an oversight hearing on arbitration in the securities industry and is not focused on any particular legislation, but I have joined with Senator Feingold (D–WI) and Representative Constance Morella (R–MD) to introduce the Civil Rights Procedures Protection Act. Our legislation, which would make mandatory arbitration contracts unenforceable, would provide relief to those employees in every industry, including the securities industry, who are required by their employer to sign mandatory arbitration contracts and would guarantee that no one could be forced to choose between their civil rights and their job.

PREPARED STATEMENT OF ISAAC C. HUNT, JR.

COMMISSIONER, U.S. SECURITIES AND EXCHANGE COMMISSION

JULY 31, 1998

Summary

The Securities and Exchange Commission (Commission) has been a strong advocate for civil rights of securities industry employees. The Commission believes that in order to assure that securities industry employees are not subject to illegal discrimination, they deserve to have the opportunity to pursue their rights under the various Federal civil rights statutes.

- *Recent National Association of Securities Dealers, Inc. (NASD) Rule Change:* The Commission recently approved an important change to the rules of the NASD which eliminates the NASD's requirement that securities industry employees arbitrate statutory employment discrimination claims.
- *Civil Rights Procedures Protection Act of 1997:* The Commission believes that the decision as to whether to amend the Federal civil rights laws and the Federal Arbitration Act with respect to the arbitration of employment discrimination claims is uniquely an issue for Congress to decide. The Commission supports the bill if Congress believes it will enhance the civil rights of securities industry employees. The issue of whether employee discrimination disputes may be the subject of predispute arbitration contracts is important, and the Commission stands ready to assist the Congress as it moves forward on this issue.

Introduction

Chairman D'Amato, Senator Sarbanes, Members of the Committee, I appreciate the opportunity to testify on behalf of the Securities and Exchange Commission regarding the arbitration of employment discrimination disputes in the securities industry. Thank you, Chairman D'Amato, for requesting the Commission's views on this important and timely issue.

Under the leadership of Chairman Levitt, the Commission has been a strong advocate for civil rights of securities industry employees. The Commission firmly believes that securities industry employees deserve to work free of illegal discrimination. I and other members of the Commission have spoken out against discrimination in any form in our industry. The Commission, moreover, believes that in order to assure that securities industry employees are not subject to illegal discrimination, they deserve the opportunity to pursue their rights under the various Federal civil rights statutes through any available forum.

I. Recent NASD Rule Change

As I am sure you know, the Commission recently approved an important change to the rules of the National Association of Securities Dealers, Inc., which eliminates the NASD's requirement that securities industry employees arbitrate statutory employment discrimination claims.[1] This important rule change distinguishes discrimination claims from other employment related disputes, and removes the NASD's requirement that statutory employment discrimination claims be arbitrated. The

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[1] Securities Exchange Act Release Number 40109, 63 FR 35299 (June 29, 1998). Each self-regulatory organization (SRO) applies its own arbitration rules to its members. The NASD's arbitration rules, for example, generally provide that any dispute concerning the business of an NASD member, or arising out of the employment or termination of employment of an associated person, with certain exceptions, must be submitted to arbitration at the request of an investor, or in intra-industry cases, at the request of either party. The other SRO's, like the New York Stock Exchange (NYSE), have similar requirements.

rule change puts the vast majority of the securities industry in the position of many other industries; that is, it is designed to permit the disputing parties to decide for themselves how best to resolve their differences. The Commission has encouraged and expects the other SRO's to adopt similar rule changes industrywide.

The Commission's approval of the NASD rule change does not indicate that the Commission necessarily considers arbitration to be an inappropriate forum for resolving discrimination claims fairly. The U.S. Supreme Court has upheld contracts for the resolution of these claims within securities industry arbitration.[2] The Commission is committed to ensuring that securities industry arbitration is a fair and equitable forum for resolving the full range of disputes that arise between broker–dealers, their employees, and investors.

The NASD rule change is responsive to concerns raised by Members of Congress, the Equal Employment Opportunity Commission (EEOC), civil rights groups, and others that statutory employment discrimination claims should not be subject to arbitration by operation of SRO rules approved by the Commission pursuant to the Securities Exchange Act of 1934 (Exchange Act). The Commission noted in approving the NASD rule change that the statutory employment antidiscrimination provisions reflect Congress' express intention that employees should receive special protection from discriminatory conduct by employers.[3] Such statutory rights are an important part of this country's efforts to prevent discrimination. We encouraged and agreed with the NASD's determination that, in this unique area, it should not require arbitration.

The Commission believes that the securities industry and its employees should be free to the same extent as other industries and employees to use arbitration or any other alternative dispute mechanism to resolve disputes. The Commission is aware, of course, that the NASD's rule change does not affect private agreements that firms might enter into with their employees—these are governed by contract law and the Federal Arbitration Act. One practical effect of the NASD's rule change could be that many firms would simply require their employees to agree as a condition of employment to the arbitration of discrimination claims through separate agreements. I think a good indication that this will not happen is that one major broker–dealer employer already has stated that it will not require its employees to enter into predispute agreements requiring them to arbitrate statutory employment discrimination claims. We expect other firms also to consider seriously giving their employees the option of going to court or going to arbitration after a dispute arises. We expect to monitor with the SRO's changes in the use or the terms of separate employment contracts of securities firms with their employees to learn whether there are issues that should be addressed.

The Commission also agrees that it is very important for the SRO's to look very closely at their existing procedures concerning training, arbitrator selection, and administration for cases involving employment discrimination claims. In 1994, the Director of the Commission's Division of Market Regulation wrote to all of the SRO's that administer arbitration programs to encourage them to take aggressive action to train existing arbitrators or to recruit new arbitrators with expertise in discrimination law to assure party confidence in panels selected for these cases. He noted that at that time, when there were very few cases with discrimination claims on the SRO's dockets, arbitrators generally did not have a solid foundation in discrimination law. Moreover, he advised the SRO's to assure that training is developed to provide for a balanced presentation of the discrimination issues that may arise in industry disputes, and that recruiting efforts should be sensitive to the continuing need for balanced and impartial panels.[4] The Division's letter followed the General Accounting Office's (GAO) March 30, 1994 report entitled *Employment Discrimination: How Registered Representatives Fare in Discrimination Disputes.* The GAO had several suggestions for improving the administration of cases involving discrimination disputes that the Commission and SRO's implemented.

Since that time, we understand that the SRO's that have administered arbitration cases with discrimination allegations have in fact expanded their arbitrator recruitment to reach out both to arbitrators with appropriate expertise and to greater numbers of women and minorities. I think the SRO's have identified the fact that they need to strengthen even more their approach to resolving all employment law

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[2] *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991). Recently, several courts have reviewed the adequacy of SRO arbitration forums in the context of statutory discrimination cases. *Compare Desiderio v. NASD, Inc.*, 1998 WL 195271 (S.D.N.Y. April 27, 1998) *with Rosenberg v. Merrill Lynch, Pierce, Fenner and Smith, Inc.*, 995 F. Supp. 190 (D. Mass. 1998).

[3] 63 FR 35299, 35303 (June 29, 1998).

[4] *See, e.g.*, letter dated June 2, 1994 from Brandon Becker, Director, Division of Market Regulation, to Robert S. Clemente, Director of Arbitration, New York Stock Exchange.

cases. We are aware that currently a committee composed of representatives of the NASD Regulation, Inc. and the NYSE, as well as employment lawyers, an academic, and securities industry representatives, is studying these issues, including: arbitrator selection methods, disclosure issues, and whether or how to use a "due process protocol" used in other alternative dispute resolution forums, among other issues. I look forward to learning more about the committee's work, and hope that the result of its efforts is that the arbitration forums become more attractive for the resolution of discrimination disputes, and that employees will elect to use them, even if some of those employees also have the option to proceed in court.

II. Civil Rights Procedures Protection Act of 1997

The Commission's approval of the NASD's recent rule change removes any regulatory requirement that NASD member employees pursue their Federal civil rights claims in arbitration. Like the NASD's action approved by the Commission, S. 63, Senator Feingold's bill, distinguishes employment discrimination claims from other claims between employers and employees. The bill establishes special rules in the civil rights laws and Federal Arbitration Act for the resolution of these disputes. Securities industry employers and employees would be treated like any other industry group.

The decision as to whether to amend the Federal civil rights laws and the Federal Arbitration Act is uniquely an issue for Congress to decide. The Commission supports the bill if Congress believes it will enhance the civil rights of securities industry employees. In formulating its own approach to the NASD's rule, the Commission looked to the studies and conclusions of the EEOC, the Commission on the Future of Worker–Management Relations (Dunlop Commission), and others with expertise in this area,[5] and also considered the views of employers and employees. We understand that Congress will do the same in considering S. 63, and the Commission would be happy to assist you as Congress moves forward.

III. Background on Arbitration in the Securities Industry

I would also like to provide you with some regulatory background that may help you to understand the place of arbitration within the securities industry. A broker–dealer may not effect securities transactions through any employees who are not qualified by and registered with a national securities association—the NASD—or a national securities exchange—such as the NYSE.[6] As you know, under the Federal securities laws, broker–dealers have an independent obligation to supervise their employees. In the course of meeting this obligation, broker–dealers and their employees sometimes have disputes that relate to the firm's or employee's obligations under the Federal securities laws. Arbitration of these disputes, in which neither firms nor employees assert employment discrimination issues, generally provides fair, expert, and efficient dispute resolution.

The securities industry has relied on the expertise of arbitrators since at least 1872 to equitably resolve disputes with less disruption to the business of securities firms than court litigation may involve.[7] It is generally believed that solving securities disputes between securities industry parties within arbitral forums benefits the industry because such disputes can be more quickly and cost effectively resolved in those forums.

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[5] *See, e.g.*, Dunlop Commission, Report and Recommendations (1994); and Equal Employment Opportunity Commission, Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment (1997).

[6] *See, e.g.*, NASD Rule 1031 and NYSE Rule 311. One important way the Commission and SRO's encourage investor protection and healthy and vigorous securities markets is through requiring the registration of most securities industry personnel. Registration requirements permit the Commission, the SRO's, and State regulatory authorities to control who enters and exits the securities industry, and to track the activities of persons currently in the industry. Registration also empowers investors by providing them with background information—such as prior sanctions or criminal convictions—about the person who advises them on investing their savings.

Sections 6(c)(3)(B) and 15A(g)(3) of the Exchange Act permit the NYSE and NASD to establish registration requirements for their members and persons associated with their members. The NASD, other SRO's, and State regulatory authorities meet their registration obligations in part by requiring all applicants for registration as persons associated with a broker–dealer to complete and sign the Form U–4, the "Uniform Application for Securities Industry Registration or Transfer." Among other things, the Form U–4 includes an agreement by registered persons to arbitrate any claim that is eligible for arbitration under the rules of the SRO with which they register. As a result of the NASD's rule change, statutory discrimination claims will no longer be covered by this clause.

[7] *See* Constantine N. Katsoris, Foreword: New York Stock Exchange, Inc. Symposium on Arbitration in the Securities Industry, 63 Fordham L. Rev. 1501 (1995); Philip J. Hoblin, Securities Arbitration Procedures, Strategies, Cases 1–2 (2d ed. 1992).

As you know, the Commission carefully reviews and approves all SRO arbitration rules, and inspects their programs for the fair administration of them. The Commission's inspection staff conducts periodic reviews to assess the SRO's procedures to ensure the evenhanded administration of the arbitration rules. Arbitration has played, and will continue to play, an important part in resolving industry disputes.

The issue of whether employment discrimination disputes may be the subject of predispute arbitration contracts is very important. The Commission believes that the NASD's rule change and the decisions individual industry members are making in this area will help to provide industry employees with more meaningful choices on how to resolve disputes under the Federal civil rights laws. As a result of the rule change, employers and employees can negotiate over whether to resolve any statutory discrimination claims in a court of law or in arbitration. If some statutory employment discrimination cases remain in arbitration, the Commission believes the SRO's should continue to analyze closely their procedures to address whether they must be modified for these special cases.

Conclusion

We thank you for offering us the opportunity to appear here today, and to provide our thoughts for your consideration. The Commission and its staff stand ready to provide the Committee with assistance on this important issue.

PREPARED STATEMENT OF SAMUEL ESTREICHER *

PROFESSOR, NEW YORK UNIVERSITY SCHOOL OF LAW

JULY 31, 1998

Introduction

My name is Samuel Estreicher. Since 1978, I have been teaching labor and employment law at New York University School of Law. I am also the Faculty Director of NYU's Center for Labor and Employment Law and Institute of Judicial Administration. Since 1984, I have served as Counsel to Cahill Gordon & Reindel, a law firm in New York, where I handle labor and employment matters. In addition to my teaching, writing, and law practice, I am on the labor, employment, and commercial panels of the American Arbitration Association and on the panel of distinguished neutrals of the Center for Public Resources (where I also serve on CPR's Employment Disputes Committee). The views expressed are solely the author's and should not be attributed to any organization or other person.

I have long been engaged in exploration of the legal and policy issues in connection with predispute agreements to arbitrate statutory employment claims, including my work on the Center for Public Resources' Employment Disputes Committee in drafting model arbitration and mediation procedures and on the American Arbitration Association's National Employment ADR Task Force, Subcommittee on Rules and Procedures. I have also given testimony on this subject before Secretary of Commerce Brown's and Secretary of Labor Reich's Commission on the Future of Worker–Management Relations (Dunlop Commission) on September 29, 1994. I thank the Committee for this opportunity to testify on these issues, with particular reference to the situation in the securities industry. Chairman D'Amato and all the Members of the Committee are to be commended for holding this hearing on these important questions.

My views are set out in full in my recent article, "Predispute Agreements to Arbitrate Statutory Employment Claims," 72 N.Y.U.L. Rev. 1344 (Dec. 1997), which is enclosed and should be appended as an appendix to this testimony. I offer here only some highlights of the points made in the article.

A. The Courts are Basically Getting it Right in Enforcing Predispute Agreements to Arbitrate Statutory Employment Claims Because Such Agreements Further the Joint Interests of the Parties and Promote the Public Interest in Expeditious, Fair Resolution of Civil Rights Claims

Predispute agreements to arbitrate statutory employment claims are a legitimate alternative to litigation that offers the prospect of a quicker, less costly, less divi-

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* Professor of Law and Director, Center for Labor and Employment Law and Institute of Judicial Administration, New York University School of Law; Counsel, Cahill Gordon & Reindel. This testimony represents the views solely of the author and should not be attributed to the Center, Institute, my law firm, or any other organization. Address: 40 Washington Square So., New York, New York 10012; 212–998–6226 (tel.); 212–995–4341 (fax; email: <estreicher@turing.law.nyu.edu>.

sive, less distracting, and nonpublic resolution of employment disputes. Such agreements should be enforced provided that certain adjudicative quality standards (of the type proposed by the Dunlop Commission[1] and promulgated by leading arbitration services organizations like the American Arbitration Association[2] and JAMS/Endispute)[3] are met.

1. *The Overwhelming Weight of Judicial Authority Supports the Validity of Predispute Arbitration Agreements*

Building on the Supreme Court's decision in *Gilmer v. Interstate/Johnson Lane Corp.*,[4] the Federal courts of appeals have fairly uniformly held that these agreements are enforceable under the Federal Arbitration Act (FAA),[5] whether the claims sought to be arbitrated arise under contract law or Federal or State civil rights laws.[6] The one exception, a recent decision of the Ninth Circuit,[7] contends that Congress in §118 of the Civil Rights Act of 1991, *sub silentio* overruled *Gilmer*. The Ninth Circuit's reasoning is open to serious question,[8] and its decision is not likely to survive Supreme Court review.

2. *Such Agreements Further the Joint Interests of the Parties Without Effecting a Waiver of any Substantive Rights*

The reasoning of the courts in *Gilmer* and its progeny is that predispute arbitration agreements can further the joint interests of the parties without resulting in a waiver of any substantive rights. From a predispute perspective, the parties are better off because they have the option of a dispute resolution mechanism that is faster, less costly, and less divisive. No substantive waiver occurs because the arbitrator, under *Gilmer*, must have the authority to apply statutory standards and award statutory remedies if a violation is found. The only waiver that occurs is a waiver of the purely procedural right to a judicial forum. In essence, predispute arbitration agreements conforming to the adjudicative quality standards identified in *Gilmer*, and as promulgated by the AAA and JAMS/Endispute, function purely as an alternative forum-selection device.

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[1] See U.S. Dept's of Commerce and Labor, Commission on the Future of Worker–Management Relations, Report and Recommendations 31 (Dec. 1994).

[2] See American Arbitration Ass'n, National Rules for the Resolution of Employment Disputes (1996).

[3] See JAMS/Endispute Arbitration Policy (1996).

[4] 500 U.S. 20 (1991).

[5] 9 U.S.C. §§ 1 et seq.

[6] See *Seus* v. *John Nuveen & Co., Inc.*, 1998 U.S. App. LEXIS 11907 (3d Cir., June 8, 1998) (securities broker alleging Title VII and ADEA claims); *O'Neil* v. *Hilton Head Hosp.*, 115 F.3d 272 (4th Cir. 1997) (compelling arbitration of FMLA claim); *Patterson* v. *Tenet Healthcare*, 113 F.3d 832 (8th Cir. 1997) (former hospital medical technologist alleging Title VII and State civil rights law claims); *Great Western Corp.* v. *Peacock*, 110 F.3d 222 (3d Cir. 1997) (former mortgage consultant for mortgage company alleging sexual harassment claim under State law); *Cole* v. *Burns Int'l Sec. Servs.*, 105 F.3d 1465 (D.C. Cir. 1997) (former security guard alleging racial discrimination and harassment claims under Title VII and intentional infliction of emotional distress claims under State law); *Rojas* v. *TK Communications, Inc.*, 87 F.3d 745 (5th Cir. 1996) (former disk jockey for radio station alleging sexual harassment claim under Title VII); *Matthews* v. *Rollins Hudig Hall Co.*, 72 F.3d 50 (7th Cir. 1995) (former employee/consultant of insurance broker alleging ADEA and fraudulent inducement claims); *Asplundh Tree Expert Co* v. *Bates*, 71 F.3d 592 (6th Cir. 1996) (former chief executive of predecessor meter service company alleging contract claims).

[7] See *Duffield* v. *Robertson Stephens & Co.*, 1998 U.S. App. LEXIS 9284 (9th Cir., May 8, 1998).

[8] As the Third Circuit reasonably observed in *Seus*:

> Nor do we believe that this straightforward declaration of the full Congress [in §118 of the Civil Rights Act of 1991] can be interpreted to mean that the FAA is impliedly repealed with respect to agreements to arbitrate Title VII claims which were executed by an employee as a condition of securing employment. Thus, we respectfully disagree with the decision of the Court of Appeals for the Ninth Circuit in *Duffield* v. *Robertson Stephens & Co.*, 1998 U.S. App. LEXIS 9284, No. 97–15698, 1998 WL 227469 (9th Cir. May 8, 1998). As we understand the opinion in that case, the court reads the prefatory clause, "where appropriate and to the extent authorized by law," in light of the legislative history, as a codification of a particular view of the decisional law regarding Title VII arbitration as it existed prior to the Supreme Court's decision in *Gilmer*. To us, it seems most reasonable to read this clause as a reference to the FAA. ... Finally, even if we were to accept "authorized by law" as intended to codify case law, we would find the text incompatible with the notion that the law codified was case law inconsistent with a Supreme Court case decided 6 months before the passage of the [Civil Rights] Act.

1998 U.S. App. LEXIS 11907, *22.

3. Concerns Over the Adjudicative Quality of Securities Industry Arbitration Procedures are Premature in Light of Recent SEC Action

Legitimate, if overblown, concerns have been raised about the adjudicative quality of securities industry arbitration procedures, principally the fact that arbitration agreements were secured as a condition of registration with the self-regulatory organizations (SRO's) in the securities industry (the National Association of Securities Dealers (NASD) and the New York Stock Exchange (NYSE)) and the panels of arbitrators were selected by the SRO's themselves. However, in view of the recent SEC action[8] approving the change in NASD rules to remove arbitration of statutory employment claims from the reach of the NASD arbitration process, these concerns are premature. This is because we can anticipate similar action shortly by the NYSE, and when that occurs registered representatives in the securities industry will be in precisely the same position as the other employees in industries covered by the FAA—arbitration agreements entered into directly between the employer and the employee, with the arbitrations conducted pursuant to the adjudicative quality standards of the leading provider organizations.

I believe it is best to allow the parties—the employers and their employees—in the securities industry themselves to work out the dispute resolution procedures that best fit their joint objectives. In light of the above developments, there is certainly no warrant for special legislation targeting arbitration of employment claims in the securities industry.

B. The Policy Objections to Predispute Arbitration of Statutory Employment Claims Are Misplaced

Admittedly, people disagree passionately here. Let's consider some of the policy objections that have been raised.

1. A New Form of "Yellow Dog" Contract?

One source of criticism is suggested by the reference to "yellow dog" contracts. This conjures up the image of powerless workers giving up hard-fought rights in order to meet the bare necessities of life. The imagery is vivid but does not quite fit the facts. Arbitration involves a change in the forum—from the courts to a jointly selected neutral decisionmaker. It does not involve a waiver of substantive rights. When a contract provides for arbitration of statutory claims, the arbitrator must be empowered to apply statutory standards and award statutory remedies.

In the negotiation of employment contracts, there are some nonnegotiable terms established by law (*e.g.*, minimum wages, maximum hours, nondiscrimination rules), but areas of overwhelming importance to the employees (*e.g.*, compensation, pension benefits, job security) are left for the parties to negotiate by themselves. Little is gained by the "yellow dog" rhetoric. The policy question is whether there are strong reasons for placing the forum-selection topic outside of the realm of contract and thus into the nonnegotiable sphere. This is not current law, and the burden is on those seeking legal change to justify taking this matter out of the sphere of joint determination by the parties themselves.

2. Procedural Adequacy: Fresh Apples vs. Spoiled Oranges?

A second source of criticism points to the procedural inadequacy of arbitration: that the process is supposed to be informal, with scant opportunity for prehearing discovery and with little adherance to procedural scruples. Critics suggest a kind of second-class justice system.

Some of this criticism, too, is overblown. To a certain extent, apples are being compared—not with oranges—but with spoiled fruit. On the one hand, we are offered a picture of private litigation under ideal conditions (a world of substantial monetary claims warranting the attention of able advocates like Judith Vladeck and Cliff Palefsky, quick and cheap access to the courts, and hefty jury awards). On the other, arbitration is depicted at its worst (claimants without lawyers confronting their former employers in management-dominated industry panels, and proceedings rife with bias). This, too, is good rhetoric but, analytically, a mistake. We should be assessing the relative merits of litigation and arbitration under the real-life conditions that most employees and employers will face. For the average employee—whose claims will not warrant the attention of any sophisticated trial lawyers—arbitration offers a better adjudicative alternative than court litigation.

There are, of course, some important issues of procedural design that have to be considered. How extensive should the opportunity for discovery be in order to provide a meaningful hearing on statutory claims without at the same time replicating the costs and delay of a court action? Can we provide a mechanism for the publica-

[8] SEC Release No. 34-40109; File No. SR-NASD-97-77.

tion of awards—so that representatives of employers and employees can monitor the performance and impartiality of arbitrators, while preserving the benefits of low-visibility, informal claims resolution? Can the standard for judicial review of awards be modified to ensure some adherence to statutory requirements without converting arbitrators into trial courts? These questions should be addressed, and are being addressed by the leading provider organizations and in the courts, but they do not present a case for new legislation.

3. *Private Law?*

Opponents of arbitration assume a world dominated by private arbitration of statutory claims in which no public law, no guidance from prior decisions is generated. As with postdispute settlement agreements—clearly lawful at present—there would remain under any realistic scenario plenty of claims for the civil courts. Indeed, precisely because arbitration reduces costs for claimants as well as employers and provides only limited opportunity for judicial review, many firms will be reluctant to promulgate arbitration policies. In any event, even if the unimaginable were to occur, and all private claimants were confined to the arbitration forum, surely this would free up the resources of administrative agencies to pursue systemic litigation.

4. *Absence of Jury Trials*

A fourth objection highlights the absence of jury trials. Jury trials indeed play, and will continue to play an important role, in the overall system. But consider the following: First, civil litigation resulting in substantial jury awards is a realistic prospect for relatively few claimants. For the vast majority, a private lawyer cannot be secured and their claims will be addressed, if at all, by overworked, understaffed administrative agencies. These agencies—after considerable delay—typically offer little more than a perfunctory investigation.

Even where private lawyers can be secured, very few employment cases go to trial. The overwhelming number of these cases are resolved by dispositive motion.

Second, while some individuals with substantial claims—often, white senior managers with age discrimination grievances or, if they work in California, Michigan, and a few other places, wrongful dismissal allegations—may lose access to jury trials, the jury trial is a relatively recent innovation in employment law (introduced as late as 1991 for Title VII and ADA lawsuits). We should not assume jury trials are an essential feature of the employment law landscape. Major strides were made in the discrimination field for 25 years without resort to juries. Our basic labor laws do not provide for jury trials. European countries with wrongful dismissal laws rely on specialized labor tribunals (essentially tripartite arbitration boards), with well-defined, scheduled recoveries; there is no access to the ordinary civil courts, let alone civil juries, for such disputes.

From the employer's perspective, jury trials inject an element of uncertainty because of the unpredictability of jury awards and the risk that, in certain cases, juries will dispense their own view of social justice rather than finding facts in accordance with the law. This spectre of liability undermines society's interest in enabling firms to make sound personnel decisions and, as the Rand studies suggest, may have negative effects for the willingness of firms to hire additional workers. We have, in short, a system in which a few individuals in protected classes win a lottery of sorts, while others queue up in the administrative agencies and face reduced employment opportunities.

C. Where Does the Public Interest Lie?

Where does the public interest lie? I submit it lies in allowing maximum freedom of choice consistent with the substantive commitments of Federal and State civil rights and employment laws. Predispute arbitration agreements are not for every industry, every employer, or for every employee. There will be a good deal of variety in practice, with some eschewing arbitration in favor of mediation and nonbinding process while others embarking on internal dispute resolution systems culminating in a fair binding arbitration process. The civil rights enforcement agencies will be freed of perfunctory processing of routine claims, and will be able to pursue systemic wrongdoing.

Binding arbitration of public law disputes can be fairly conducted without sacrificing the substantive protections of employment laws or turning proceedings into full-fledged civil trials. Appropriate safeguards include:

- A competent arbitrator who knows the laws in question;
- A fair and simple method for exchange of information;
- A fair method of cost sharing to ensure affordable access to the system for all employees;
- The right to independent representation if sought by the employee;

- A range of remedies equal to those available through litigation;
- A written award explaining the arbiter's rationale for the result; and
- Limited judicial review sufficient to ensure that the result is consistent with applicable law.

Conclusion

A well-designed private arbitration alternative for employment claims is in the public interest. The law should encourage arbitration of employment disputes in a manner that satisfies the standards for a fair adjudication before a neutral arbiter empowered to apply the law and, where warranted, impose statutorily available remedies.

Thank you.

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Predispute Agreements to Arbitrate Statutory Employment Claims

Samuel Estreicher

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PREDISPUTE AGREEMENTS TO ARBITRATE STATUTORY EMPLOYMENT CLAIMS

SAMUEL ESTREICHER*

Over the last decade, the Supreme Court, through its interpretation of the Federal Arbitration Act of 1925 (FAA), has expanded the role of arbitration in the resolution of legal disputes, including disputes arising under federal and state statutes. Recently, much debate has arisen over the issue of whether the FAA applies to employment contracts, and whether employees can enter into binding predispute agreements to arbitrate statutory employment claims. In Gilmer v. Interstate/Johnson Lane Corp., *the Supreme Court held that under the FAA, employees could in fact enter into such predispute agreements. Because the agreement in* Gilmer *was not part of an employment contract, however, the Supreme Court left open a critical question, namely the scope of the FAA exclusion of employment contracts for certain employees engaged in foreign or interstate commerce. In this Article, Professor Estreicher first addresses the various public policy arguments raised by opponents of predispute agreements to arbitrate statutory employment claims. Addressing each one in turn, he concludes that where certain procedural safeguards are implemented, arbitration is indeed a proper forum for the resolution of statutory employment claims, and that predispute agreements to arbitrate provide valuable benefits for both employers and employees. Turning to the issue left open by the Court in* Gilmer, *Professor Estreicher explores the confusion surrounding the scope of the FAA exclusion of employment contracts, which in large part stems from an uncertain legislative history, and suggests that, given recent Court decisions and the policies underlying them, a narrow interpretation of the exclusion by the Supreme Court is probable. Professor Estreicher concludes by stressing that a proper arbitration system can advance the public policies contained in federal and state employment statutes.*

INTRODUCTION

The Supreme Court held in its 1991 ruling in *Gilmer v. Interstate/Johnson Lane Corp.*[1] that, in view of the strong federal policy in favor

* Professor of Law and Director, Center for Labor and Employment Law, New York University; Counsel, Cahill Gordon & Reindel. A.B., 1970, Columbia University; M.S. (Industrial Relations), 1974, Cornell University; J.D., 1975, Columbia University. An early version of these remarks was presented at the American Arbitration Association's "National Employment Enclave—The Faces of Conflict in the Workplace: The Future of Employment ADR," Sept. 22-23, 1995, and appeared in Proceedings of New York University 49th Annual Conference on Labor 93-121 (Samuel Estreicher ed., 1997). The author also filed an amicus brief on behalf of the California Employment Law Council in Duffield v. Robertson Stephens & Co., No. C95-0109 (N.D. Cal. filed Jan. 11, 1995), appeal docketed, No. 97-15698 (9th Cir. Apr. 23, 1997). The views expressed here are the author's and should not be attributed to any organization. The research assistance of Matthew Kramer and Jeffrey Hirsch of the NYU School of Law (Class of 1998) is gratefully acknowledged.

1 500 U.S. 20 (1991).

of arbitration embodied in the Federal Arbitration Act of 1925[2] (FAA), employees could enter into binding predispute arbitration agreements encompassing claims they have against their employers under the Age Discrimination in Employment Act of 1967[3] (ADEA) and, by extension, other federal and state employment laws. Because in *Gilmer* the arbitration agreement was part of a registration process with the New York Stock Exchange, rather than a contract of employment directly between Gilmer and his former employer, the Court was able to avoid construing the reach of the exclusion in § 1 of the FAA for "contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."[4]

Since, in the absence of FAA compulsion, predispute arbitration agreements covering statutory employment claims generally will be denied enforcement, the scope of the FAA § 1 exclusion will have important practical implications for the future of employment law arbitration. In post-*Gilmer* rulings to date, the District of Columbia, Third, Fourth, Fifth, Sixth, Seventh, and Eighth Circuits[5] have read the exclusion narrowly as limited to seamen, railroad workers, and other workers directly "engaged in" interstate commerce. Despite the clear trend of post-*Gilmer* decisions, however, there remains a good deal of uncertainty and controversy over whether predispute agreements to arbitrate statutory employment claims will or should be enforced.

This Article addresses some of the policy and legal questions concerning predispute agreements between employers and employees to

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[2] 9 U.S.C. §§ 1-16 (1994).

[3] 29 U.S.C. §§ 621-634 (1994).

[4] 9 U.S.C. § 1 (1994).

[5] See O'Neil v. Hilton Head Hosp., 115 F.3d 272, 276 (4th Cir. 1997) (compelling arbitration of claim under federal Family and Medical Leave Act (FMLA), 29 U.S.C. § 2611 (1994 & Supp. 1995)); Patterson v. Tenet Healthcare, Inc., 113 F.3d 832, 835-37 (8th Cir. 1997) (affirming dismissal by district court of hospital medical technician's action against former employer alleging violations of Title VII and state antidiscrimination law); Great W. Mortgage Corp. v. Peacock, 110 F.3d 222, 226-27 (3d Cir.) (affirming order of district court compelling arbitration of mortgage consultant's claims against employer pursuant to state sexual harassment law), cert. denied, 1997 U.S. LEXIS 6057 (Oct. 14, 1997); Cole v. Burns Int'l Sec. Servs., 105 F.3d 1465, 1470-72 (D.C. Cir. 1997) (affirming district court order compelling arbitration of discharged security guard's claims against former employer alleging racial discrimination and harassment in violation of Title VII and intentional infliction of emotional distress in violation of state law); Rojas v. TK Communications, Inc., 87 F.3d 745, 747-48 (5th Cir. 1996) (affirming dismissal by district court of disc jockey's action against former employer alleging sexual harassment in violation of Title VII); Matthews v. Rollins Hudig Hall Co., 72 F.3d 50, 53 n.3 (7th Cir. 1995) (reversing denial by district court of employer's motion to compel arbitration of former employee's ADEA and state law fraudulent inducement claims); Asplundh Tree Expert Co. v. Bates, 71 F.3d 592, 596-602 (6th Cir. 1995) (affirming district court order compelling arbitration of contract claims brought by chief executive officer against company which purchased his employer)

arbitrate future disputes, whether they arise as a matter of contract or under employment discrimination statutes or other employment laws. Policy considerations are considered at the outset because they are likely to influence heavily how the legal issues raised by *Gilmer* ultimately will be resolved.

I

THE CONTROVERSY OVER PREDISPUTE ARBITRATION AGREEMENTS

Postdispute agreements to arbitrate existing disputes, most would agree, do not raise especially difficult questions. At least since the Supreme Court's *Alexander v. Gardner-Denver Co.*[6] decision, the law on postdispute waivers has been relatively clear. Once disputes have arisen, plaintiffs may enter into "knowing and voluntary" waiver agreements in which they trade potential claims under federal laws like the ADEA,[7] Title VII of the Civil Rights Act of 1964,[8] and the Americans with Disabilities Act of 1990[9] (ADA) for monetary or other consideration. If claims can be traded for money, it should not be beyond the realm of contract for the parties to negotiate a fair postdispute adjudicative process.[10]

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[6] 415 U.S. 36 (1974).

[7] The Older Workers Benefit Protection Act, Pub. L. No. 101-433, § 201, 104 Stat. 978, 983-84 (1990) (codified as amended at 29 U.S.C. § 626(f)(1) (1994)), sets certain minimum standards for postdispute substantive waivers of ADEA claims.

[8] 42 U.S.C. §§ 2000e to 2000e-17 (1994).

[9] Title I of the Americans with Disabilities Act (ADA), containing the employment provisions, is codified at 42 U.S.C. §§ 12101-12117 (1994).

[10] This is the premise of the voluntary postdispute arbitration experiments of the EEOC and state agencies. See EEOC Policy Statement on Alternative Dispute Resolution, 3 EEOC Compliance Manual (BNA) N:3055 (July 17, 1995) (establishing EEOC commitment to Alternative Dispute Resolution (ADR) and setting guidelines for use); Agency is Committed to ADR But Questions Remain, Miller Says, Daily Lab. Rep. (BNA), Jan. 24, 1995, available in LEXIS, BNA Library, DLABRT File (describing ADR pilot program in which four EEOC districts offered mediation in selective discharge cases resulting in 52% settlement rate). For experience under the voluntary arbitration alternative authorized by New York's Human Rights Law, N.Y. Exec. Law § 297, subd. 4, par. A, subpar. ii (McKinney 1993), see Peter A. Prosper & Joel M. Douglas, The Arbitration of Human Rights Complaints: The New York Experience, Arb. J., Dec. 1992, at 26 (describing New York's program); Peter Blackman, Claimants Wanted: Project Tries to Convince Employees to Arbitrate, N.Y. L.J., May 26, 1994, at 5 (reporting that program is wanting for claimants because of minimal promotion and because in arbitration plaintiffs pay counsel, whereas when case is before administrative law judge, plaintiffs have access to free government counsel). For a discussion of the virtues of postdispute mediation, see Dwight Golann, Employment Disputes in Mediating Legal Disputes: Effective Strategies for Lawyers and Mediators (1996); Matthew W. Daus, Mediating Disability Employment Discrimination Claims, Disp. Resol. J., Jan. 1997, at 16, 17-19. For a model of postdispute procedures the author had a hand in drafting, see Center for Public Resources, Inc., Model

Predispute agreements to arbitrate claims arising under individual employment contracts also would seem relatively noncontroversial. If we put aside for the moment questions concerning the enforceability of such agreements under the FAA, state law would ordinarily be available to compel the parties to a contract to honor the dispute mechanism set out in the very instrument that creates the underlying substantive claim. There may be, however, cases at the margin where—because of problems of illusory promise or contracts of adhesion—generally applicable principles of state contract law preclude enforcement.[11] Also, the public policies of some states, as expressed in their arbitration statutes, may allow either party to an employment contract to disregard executory arbitration promises.[12]

However, a controversy is raging over the validity of *predispute* agreements to arbitrate *statutory* employment claims. It is here that distinguished plaintiffs' lawyers like New York's Judith Vladeck

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ADR Procedures: Employment Termination Dispute Resolution Agreement and Procedure (1990)

[11] Compare Gibson v. Neighborhood Health Clinics, 121 F.3d 1126 (7th Cir. 1997) (holding that arbitration clause was not enforceable because of lack of consideration in form of any reciprocal employer promise), and Heurtebise v. Reliable Bus. Computers, Inc., 550 N.W.2d 243, 247, 258 (Mich. 1996) (holding that there is no enforceable obligation under Michigan law to submit sex discrimination claim to arbitration where management reserved right to change employee handbook containing arbitration clause and handbook stated that it should not be construed as binding contract; three justices also found violation of state public policy), cert. denied, 117 S. Ct. 1311 (1997), with Lang v. Burlington N. R.R., 835 F. Supp. 1104, 1106 (D. Minn. 1993) (holding that mandatory arbitration policy added to employee handbook 26 years after plaintiff was hired constituted offer accepted by plaintiff through his continued employment and barred post-termination lawsuit, and finding no evidence that provision resulted from fraud or was "inherently unfair"), and Fregara v. Jet Aviation Bus. Jets, 764 F. Supp. 940, 952 (D.N.J. 1991) (finding that grievance and arbitration procedures spelled out in employee handbook providing for appeal to supervisor and then to company's board of adjustment, with provision for selection of impartial referee if board was deadlocked, must be exhausted before fired employee can sue for breach of contract, and stating that "there is nothing futile or illusory about this process"). See generally Samuel Estreicher, Arbitration of Employment Disputes Without Unions, 66 Chi.-Kent L. Rev. 753 (1990); Alfred G. Feliu, Legal Consequences of Nonunion Dispute-Resolution Systems, 13 Employee Rel. L.J. 83 (1987).

[12] Some state arbitration statutes exclude arbitration agreements contained in employment contracts or made a condition of employment. See, e.g., Ariz. Rev. Stat. Ann. § 12-1517 (West 1994); Iowa Code Ann. § 679.1(2)(b) (West 1987); Kan. Stat. Ann. § 5-401(c)(2) (Supp. 1996); Ky. Rev. Stat. Ann. § 417.050 (Michie 1992); S.C. Code Ann. § 15-48-10 (Law. Co-op. 1976 & Supp. 1997). These state law exclusions become material to the issue of arbitrability of employment claims only if the FAA is held not to apply to arbitration agreements contained in most employment contracts. For example, as the Supreme Court of Hawaii recently ruled in Brown v. KFC Nat'l Management Co., 921 P.2d 146 (Haw. 1996), reconsideration denied, 922 P.2d 973 (Haw. 1996), even where the state arbitration statute requires that the arbitration clause be in a written employment contract, "the FAA merely requires that the arbitration provision, but not necessarily the contract out of which the controversy arises, be in writing." Id. at 159. Hence, where the FAA applies, the limitations of state arbitration law have no practical effect.

charge that the law is sanctioning a new form of "yellow dog" contract.[13] Or, as San Francisco's Cliff Palefsky puts it, "an intellectual and legal scandal . . . is occurring in broad daylight."[14] Notably, opposition from the plaintiff's bar, civil rights groups, and advocacy groups led the Dunlop Commission on the Future of Worker-Management Relations (Dunlop Commission) to scuttle, at the eleventh hour, a recommendation that predispute agreements meeting certain quality standards should be enforced under existing law.[15] With mixed success, plaintiffs' lawyer groups have been pressuring organizations like J.A.M.S./Endispute and the American Arbitration Association (AAA) to decline the processing of predispute agreements.[16]

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[13] See Judith P. Vladeck, 'Yellow Dog Contracts' Revisited, N.Y. L.J., July 24, 1995, at 7. Professor Stone adopts similar rhetoric in Katherine Van Wezel Stone, Mandatory Arbitration of Individual Employment Rights: The Yellow Dog Contract of the 1990s, 73 Denv. U. L. Rev. 1017 (1996).

[14] Joyce E. Cutler, Arbitration Suits Challenge Mandatory Arbitration as Depriving Employees of Their Rights, Daily Lab. Rep. (BNA), Mar. 3, 1995, available in LEXIS, BNA Library, DLABRT File (quoting Cliff Palefsky of McGuinn, Hillsman & Palefsky). Mr. Palefsky represents plaintiffs in the pending challenges in Duffield v. Robertson Stephens & Co., No. C95-0109 (N.D. Cal. filed Jan. 11, 1995) (order compelling arbitration), appeal docketed, No. 97-15698 (9th Cir. Apr. 23, 1997). Burton v. A.F.M. Servs., No. 965632 (Cal. Super. Ct. filed Dec. 6, 1994), appeal docketed, No. A073922 (Cal. Ct. App. Apr. 18, 1996).

[15] For the author's testimony before the Dunlop Commission, see Statement by Professor Samuel Estreicher to the Commission on the Future of Worker-Management Relations Panel on Private Dispute Resolution Alternatives, reprinted in Daily Lab. Rep. (BNA), Sep. 30, 1994, available in LEXIS, BNA Library, DLABRT File. His views on the Dunlop Commission's report are set out in Samuel Estreicher, The Dunlop Report and the Future of Labor Law Reform, 12 Lab. Law. 117 (1996), earlier versions of which were published, all under the same title, in Contemporary Issues in Labor and Employment Law: Proceedings of New York University 48th Annual National Conference on Labor 291-311 (Bruno Stein ed., 1996); Regulation, Mar. 1995, at 28; and Daily Lab. Rep. (BNA), June 5, 1995, available in LEXIS, BNA Library, DLABRT File.

[16] Several plaintiffs' bar and union representatives participated in Due Process Protocol for Mediation and Arbitration of Statutory Arbitration Disputes, in 9A Lab. Rel. Rep. (BNA) No. 142, at 534:401 (May 9, 1995) [hereinafter Due Process Protocol]. However, this group could not reach consensus on whether predispute agreements to arbitrate statutory employment claims could be required as a condition of employment. See id. In July 1997, the EEOC restated its long-standing opposition to "agreements that mandate binding arbitration of discrimination claims as a condition of employment." EEOC Policy Statement on Mandatory Arbitration, reprinted in Daily Lab. Rep. (BNA) No. 133, at E-4 (July 11, 1997). Two months earlier, the National Academy of Arbitrators had adopted a similar position. See National Academy of Arbitrators' Statement and Guidelines Adopted May 21, 1997, Daily Lab. Rep. (BNA) No. 103, at E-1 (May 29, 1997).

Effective June 1, 1996, the American Arbitration Association (AAA) issued new national rules for the resolution of employment disputes. See American Arbitration Ass'n, National Rules for the Resolution of Employment Disputes (1996) [hereinafter AAA 1996 Rules]. The Association's policy is to "administer dispute resolution programs which meet the due process standards as outlined in these rules and the *Due Process Protocol*. This includes pre-dispute, mandatory arbitration programs, as a condition of employment." Id. at 3-4. The AAA rules were recently amended "to address technical issues." See Ameri-

II

The Case for Facilitating Predispute Agreements Conforming to Certain Adjudicative Quality Safeguards

I do not share the position of these critics. In my view, arbitration of employment disputes should be encouraged as an alternative, supplementary mechanism—in addition to administrative agencies and courts—for resolving claims arising under public laws as well as contracts. It is an alternative that offers the promise of a less expensive, more expeditious, less draining and divisive process, and yet still effective remedy. Private arbitration will never, and should not, entirely supplant agency or court adjudication. But if properly designed, private arbitration can complement public enforcement and, at the same time, satisfy the public interest objectives of the various statutes governing the employment relationship.

Admittedly, arbitration of public law disputes is not the same thing as arbitration of contractual disputes. The public policies behind the laws require that certain adjudicative quality standards be met. But these standards can be provided without turning arbitral proceedings into full fledged civil trials. The essential safeguards (drawing largely from the Dunlop Commission's report[17]) include:

- no restriction on the right to file charges with the appropriate administrative agencies;
- a reasonable place for the holding of the arbitration;[18]
- a competent arbitrator who knows the laws in question;[19]
- a fair and simple method for exchange of information;

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can Arbitration Ass'n, National Rules for the Resolution of Employment Disputes (Including Mediation and Arbitration Rules) 4 (1997) [hereinafter AAA 1997 Rules]. Similarly, J.A.M.S./Endispute, while expressing concern "when a company requires all of its employees to arbitrate all employment disputes as an exclusive remedy," apparently will process disputes arising under such programs if a "minimum set of procedures or standards of procedural fairness" are met. These standards are set out in the organization's policy on employment arbitration. See J.A.M.S./Endispute Arbitration Policy, in 9A Lab. Rel. Rep. (BNA), Mar. 26, 1996, at 534:521.

[17] See U.S. Dep'ts of Commerce and Labor, Commission on the Future of Worker-Management Relations, Report and Recommendations 31 (Dec. 1994).

[18] Although this item is not mentioned in the Dunlop report, employers should not be able by means of an arbitration clause to compel claimants to litigate in a distant, inconvenient forum in circumstances where an express choice of forum clause having the same effect would be unenforceable. See Paul D. Carrington & Paul H. Haagen, Contract and Jurisdiction, 1996 Sup. Ct. Rev. 331, 385-88 (criticizing Supreme Court's failure to address forum location issue, which was not briefed, in Doctor's Associates, Inc. v. Casarotto, 116 S. Ct. 1652 (1996)).

[19] Rule 11(a)(i) of the AAA 1997 Rules requires that "[a]rbitrators serving under these rules shall be experienced in the field of employment law." AAA 1997 Rules, note 16, at 15.

- a fair method of cost sharing to ensure affordable access to the system for all employees;[20]
- the right to independent representation if sought by the employee;
- a range of remedies equal to those available through litigation;
- a written award explaining the arbitrator's rationale for the result;[21] and
- limited judicial review sufficient to ensure that the result is consistent with applicable law.[22]

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[20] For example, Brown & Root, a maintenance, construction, and temporary staffing company, pays the costs of the arbitration, except for the expenses of witnesses produced by the employee and a $50 fee paid by the employee (or former employee) if the proceeding is initiated by the employee or the result of a demand served on the company by the employee. See Brown & Root, Inc., Dispute Resolution Plan and Rules 17 (1994) (on file with the *New York University Law Review*). This company also established a benefit plan to reimburse 90% of attorney's fees incurred up to an annual cap of $2500 per year, with a $25 deductible paid by the employee. See Brown & Root, Inc., Employment Legal Consultation Plan 4-5 (1994) (on file with the *New York University Law Review*). In Cole v. Burns Int'l Sec. Servs., 105 F.3d 1465, 1485 (D.C. Cir. 1996), Chief Judge Edwards held for the court that, where the predispute agreement is silent or ambiguous on this question and arbitration "occurs only at the option of the employer," the court would interpret the agreement to require the employer to assume the arbitrator's fees and expenses. The court stated:

> Cole could not be required to arbitrate his public law claims as a condition of employment if the arbitration agreement required him to pay all or part of the arbitrator's fees and expenses. In light of this holding, we find that the arbitration agreement in this case is valid and enforceable. We do so because we interpret the agreement as requiring Burns Security to pay all of the arbitrator's fees necessary for a full and fair resolution of Cole's statutory claims.

Id.

[21] Rule 32 of the AAA 1997 Rules departs from the Association's customary no-opinion approach in commercial arbitrations and requires that "[t]he award shall be in writing and shall be signed by a majority of the arbitrators and shall provide the written reasons for the award unless the parties agree otherwise." AAA 1997 Rules, supra note 16, at 24. The Association's *Guide for Employment Arbitrators* (effective for cases filed on or after June 1, 1997) further states, "The award must include a statement regarding the disposition of any statutory claims." American Arbitration Ass'n, Guide for Employment Arbitrators 16 (1997).

[22] The Supreme Court's *Gilmer* decision states: "'[A]lthough judicial scrutiny of arbitration awards necessarily is limited, such review is sufficient to ensure that arbitrators comply with the requirements of the statute' at issue." Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 32 n.4 (1991) (quoting Shearson/American Express Inc. v. McMahon, 482 U.S. 220, 232 (1987)).

The appropriate standard for review of arbitration of public law disputes remains an important unresolved issue. Some lower courts have recognized a "manifest disregard" standard, a judicially created addition to the statutory grounds for vacating an award set forth in the FAA. See, e.g., Siegel v. Titan Indus. Corp., 779 F.2d 891, 892-93 (2d Cir. 1986) (applying manifest disregard standard in arbitration to determine value of stock held by shareholder). The "manifest disregard" standard requires a showing that "the arbitrator 'understood and correctly stated the law but proceeded to ignore it.'" Id. at 893 (quoting Bell Aerospace Co. v. Local 516, 356 F. Supp. 354, 356 (W.D.N.Y. 1973), rev'd on other grounds, 500 F.2d 921 (2d Cir. 1974)). The Second Circuit has left open the question of

Not all companies will be willing to subject their supervisory decisions to a neutral outside arbitrator under these conditions, even if by doing so they could avoid the risks and expense of jury trials. The limitations of arbitration are reciprocal; many companies and employees may be reluctant to submit to final, binding determinations with only limited opportunity for correction by the courts.[23]

But where companies are willing to establish programs conforming to these quality safeguards, the question is whether the law should facilitate or obstruct their establishment. Consider the controversy over workers' compensation laws earlier in this century.[24] From an ex post perspective—after an accident has occurred—workers with serious injuries able to command the attention of competent trial lawyers have a better chance at substantial recoveries before a jury rather than under an administrative system. Yet from an ex ante perspective—before an accident has occurred—the workers' compensation system offers systematic advantages over tort suits, whether the objective is delivering compensation or promoting workplace safety, for both workers and their employers. Of course, the tradeoff in the con-

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whether the "manifest disregard" standard is appropriate for arbitration of certain federal statutory claims. See DiRussa v. Dean Witter Reynolds Inc., No. 96-9068, 1997 U.S. App. LEXIS 20505, at *6-*10 (2d Cir. Aug. 5, 1997) (noting that "manifest disregard" doctrine is "severely limited"); cf. Chisolm v. Kidder Peabody Asset Management, Inc., 966 F. Supp. 218, 222-27 (S.D.N.Y. 1997) (applying, though questioning suitability of, "manifest disregard" standard for such claims).

Framed for contractual disputes, the "manifest disregard" standard may be too deferential for arbitration of public law claims. By analogy to the National Labor Relations Board's policy of deferring to labor arbitration awards that resolve statutory issues, a preferable approach would be to require that arbitrators give reasons for their disposition of statutory claims and to confirm awards only if they are not "clearly repugnant to the purposes and policies of the Act." Spielberg Mfg. Co., 112 N.L.R.B. 1080, 1082 (1955). (In 1984, the Board softened its own test. "Unless the award is 'palpably wrong,' i.e., unless the arbitrator's decision is not susceptible of an interpretation consistent with the Act, we will defer." Olin Corp., 268 N.L.R.B. 573, 574 (1984) (footnote omitted)). The D.C. Circuit's *Cole* decision stated (in dictum): "[A]rbitration of statutory claims [is] valid only if judicial review under the 'manifest disregard of the law' standard is sufficiently rigorous to ensure that arbitrators have properly interpreted and applied statutory law." *Cole*, 105 F.3d at 1487.

[23] For a survey of employer practices, see U.S. General Accounting Office, Pub. No. GAO/HEHS-95-150, Employment Discrimination: Most Private-Sector Employers Use Alternative Dispute Resolution (Report to Congressional Requesters) (July 5, 1995). The 1995 survey found that 10% of firms used arbitration as a dispute resolution mechanism for their nonunion employees, and in one-fourth to one-half of those firms, arbitration was mandatory. See id. at 7. In 1997, the GAO updated its survey, finding that, of firms reporting the use of ADR for employment disputes, 19% used arbitration. See U.S. General Accounting Office, Pub. No. GAO/GGD-97-157, Alternative Dispute Resolution: Employers' Experiences with ADR in the Workplace 2 (Aug. 1997).

[24] See generally Lawrence M. Friedman, A History of American Law, 587-88 (1974); Richard A. Epstein, The Historical Origins and Economic Structure of Workers' Compensation Law, 16 Ga. L. Rev. 775 (1982).

text of arbitration of employment disputes is different because arbitration will not proceed on a no-fault basis. Nevertheless, employment arbitration also offers systematic advantages over lawsuits for both workers and their employers. The policy question is this: are workers (and firms) generally better off—is the overall system of rights and remedies for employment disputes enhanced—if the law permits companies to establish binding predispute employment dispute systems that satisfy adjudicative quality safeguards?

III

Objections to Predispute Arbitration Agreements

Admittedly, people disagree passionately here. Some of the objections that have been raised include the following.

A. A New Form of "Yellow Dog" Contract?

One source of criticism is suggested by Judy Vladeck's reference to "yellow dog" contracts,[25] a phrase conjuring the image of powerless workers forced to sell their industrial birthright in order to meet the bare necessities of life. The imagery is vivid but does not quite fit the facts. What was wrong with "yellow dog" contracts in our earlier labor history was that they were used by employers as purely strategic devices to blunt unionization. These agreements served no interest of employers other than that of thwarting the associational freedom of their employees. Employers sought by these clauses to lay a predicate for obtaining injunctions against labor unions which, by the mere act of attempting, even peacefully, to organize their workforce, could be found to have engaged in tortious inducement of breach of contract. Once public policy evolved in support of the right of workers to form independent organizations—or, as of the enactment of the Norris-LaGuardia Act of 1932,[26] the right at least to be free of court injunctions in the peaceful pursuit of organizing objectives—these clauses were properly deemed to serve no legitimate interest of employers.

By contrast, predispute arbitration, if properly designed, can offer ex ante advantages for both parties to the contract. Moreover, such

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[25] The "yellow dog" label has a long industrial history. It also has entered political lore. William Safire reminds us of the story about Tom Heflin, a senator from Alabama (and uncle of Howell Heflin), who tried to discourage southern Democrats from bolting the party when it nominated Al Smith, a Catholic, a wet, and (worst of all) a New Yorker. Heflin is reputed to have said, "I'd vote for a yellow dog if he ran on the Democratic ticket." See William Safire, On Language: Blue Dog Demo, N.Y. Times, Apr. 23, 1995, § 6, at 20. In short, it is not the label but the substance that counts.

[26] Norris-LaGuardia Act, ch. 90, 72 Stat. 70 (1932) (codified as amended at 29 U.S.C. §§ 101-115 (1994)).

arbitration involves a change in the forum only—from the courts to a jointly-selected neutral decisionmaker. It does not involve the waiver of substantive rights.[27] When a contract provides for arbitration of statutory claims, the arbitrator must be empowered to apply statutory standards and, if a violation is found, to award statutory remedies.[28]

A variant of the "yellow dog" theme is that workers cannot meaningfully enter into binding arbitration agreements because of an inherent inequality of bargaining power. Professor Grodin argues the following, for example:

> Before a dispute arises, it is impossible for a party to assess precisely what is being waived and the probable effect of the waiver—even if his or her attention is focused on the issue. In the employment context this is especially a problem for the employee: while the employer can take into account statistical probabilities affecting all its employees, the employee's ability to predict what may happen to him or her individually is beyond the scope of such analysis. Moreover, while a post-dispute agreement to arbitrate is likely to be the product of true negotiations against the backdrop of threatened litigation, pre-dispute agreements to arbitrate are far more likely to be part of a package of provisions imposed by the employer on a take it-or-leave it basis.[29]

It is not clear why most job applicants or employees cannot make a rational decision whether they prefer to preserve rights to sue in

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[27] As the Supreme Court stated in *Gilmer*, "'By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial forum.'" Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991) (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985)).

[28] But see DeGaetano v. Smith Barney Inc., No. 95 Civ. 1613, 1996 U.S. Dist. LEXIS 1140, at *18 (S.D.N.Y. Feb. 5, 1996) (holding that although arbitration procedure did not allow arbitrator to award injunctive relief, attorney's fees, or punitive damages, "[t]he mere fact that these statutory remedies may be unavailable in the arbitral forum does not in itself establish that Title VII claims must be resolved in a court of law"). It is unclear whether this ruling is consistent with the Supreme Court's approach in the *Gilmer* decision. See supra note 27 and accompanying text. Conceivably, the failure to award attorney's fees or punitive damages in an appropriate case still would be grounds for vacating the award. Cf. DiRussa v. Dean Witter Reynolds, Inc., No. 96-9068, 1997 U.S. App. LEXIS 20505, at *10-*14 (2d Cir. Aug. 5, 1997) (declining to vacate award in plaintiff's favor that did not provide attorney's fees because plaintiff had failed to make clear to arbitrators that attorney's fees were mandatory award for prevailing plaintiffs under ADEA). Amicus Brief of California Employment Law Council at 20-24, Duffield v. Robertson Stephens & Co., No. C95-0109 (N.D. Cal. filed Jan. 11, 1995), appeal docketed, No. 97-15698 (9th Cir. Apr. 23, 1997) (arguing that, in view of § 4 of FAA, procedural adequacy of arbitration should be resolved through judicial review rather than at motion to compel arbitration stage).

[29] Joseph R. Grodin, Arbitration of Employment Discrimination Claims: Doctrine and Policy in the Wake of *Gilmer*, 14 Hofstra Lab. L.J. 1, 29 (1996). Professors Carrington and Haagen adopt a similar view in Carrington & Haagen, supra note 18, at 87-88.

court in the event of an employment dispute rather than work for an employer that requires arbitration of such disputes.[30] Neither the fact that the rights given up may not seem particularly valuable to the employee in view of the low probability attached to the eventuality of a dispute,[31] nor that some employers will insist on arbitration as a precondition, seems a compelling reason to negate an agreement in the joint interests of both parties.[32]

In several areas our laws do stipulate minimum conditions that are nonwaivable features of the employment bargain.[33] Employees have rights to organize independent unions, to be paid statutorily declared minimum wages, to be free of discrimination on account of race, sex, national origin, age, and disability, and so forth. But in many other areas of vital importance to employees—such as the basic economic terms of the relationship, whether it be compensation, benefits, or job security—the law allows the parties to negotiate a contract that meets their joint objectives.

The pertinent question is whether, in the overall mix, the nature of the forum for future disputes is a subject that may be determined by contract or whether this term belongs to the nonwaivable, nonmodifiable category and, hence, is outside of the realm of contract. The answer cannot be supplied simply by speaking in terms of a nonwaivable "right" to go to court, for that in a sense begs the question. Rights are created by statute or decision and are the result of policy judgments. A judgment has to be made on the merits whether the benefits of allowing the parties to shape their own dispute resolu-

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[30] Where all employers in a given industry require predispute arbitration agreements as a condition of employment, the employee's practical ability to shop for employers that will not require arbitration is substantially diminished. The *Duffield* litigation, see supra note 14, raises this issue in the securities industry context, where all registered representatives for now—see infra note 34, must agree to arbitration of employment claims as a condition of employment in that industry. See Plaintiff-Appellant's Opening Brief at 54-59, Duffield v. Robertson Stephens & Co., No. C95-0109 (N.D. Cal. filed Jan. 11, 1995), appeal docketed, No. 97-15698 (9th Cir. Apr. 23, 1997) (arguing that industry-wide requirement of predispute arbitration agreements forced upon plaintiff the "Hobson's choice" of forfeiting constitutional rights or forfeiting employment in securities industry).

[31] See Mayer G. Freed & Daniel D. Polsby, Just Cause for Termination Rules and Economic Efficiency, 38 Emory L.J. 1097, 1105-07 (1989) (discussing "perceptual distortion" argument for mandating "just cause" termination rules).

[32] Again, at the margin there may be situations where, under the jurisdiction's general law of contracts, the conditions for a valid, enforceable agreement are not met. The question here is whether, as Professors Grodin, see Grodin, supra note 29, at 20-28, and Carrington and Haagen, see Carrington & Haagen, supra note 18, at 401, suggest, we should assume that all predispute arbitration agreements insisted upon by employers as a condition of employment are unenforceable contracts of adhesion.

[33] For a critical view of such regulations, see Christopher T. Wonnell, The Contractual Disempowerment of Employees, 46 Stan. L. Rev. 87 (1993).

tion mechanism outweigh the attendant costs to the parties and to the public policy objectives of the statutes in question.

B. Procedural Adequacy: Fresh Apples Versus Spoiled Oranges?

A second source of criticism points up the supposed deficiencies of arbitration: that the process is supposed to be informal, with scant opportunity for prehearing discovery and little adherence to evidentiary scruples. The suggestion is that arbitration is a kind of second-class justice system.

Much of this criticism, too, is overdrawn. To some extent, apples are being compared not with oranges but with spoiled fruit. On the one hand, we are offered a picture of private litigation under ideal conditions (a world of substantial monetary claims warranting the attention of able advocates like Vladeck and Palefsky, quick and cheap access to the courts, and hefty jury awards). On the other hand, arbitration is depicted at its worst (claimants without lawyers confronting their former employers in skewed industry panels[34] and proceedings rife with bias). This is good rhetoric but, analytically, a mistake. We should be assessing the relative merits of litigation and arbitration under the real-world conditions that *most* employees and employers will face.

The assertion is often made, for example, that under arbitration employers enjoy systematic advantages as "repeat players" that would not be available in civil litigation. Although having some force in the context of industry panels, the point is considerably overstated if arbitration is conducted, as is likely, before arbitrators chosen by the parties on an ad hoc basis. An employer may be a repeat player in the sense that it likely will be arbitrating disputes with more than one employee (or former employee), but arbitrators chosen on prior occasions are unlikely to be deemed acceptable by claimant representatives. Moreover, the real repeat players will be the lawyers for both defense and plaintiff bars in the area—such as the members of the National Employment Lawyers Association, a plaintiff group—who can be counted on to share information within their group about the track records of proposed arbitrators.

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[34] In May 1997, the National Association of Securities Dealers (NASD) formed a special panel to consider whether the NASD should continue to require predispute agreements to arbitrate employment discrimination claims. See Patrick McGeehan, Bias Panel Is Formed by NASD, Wall St. J., May 29, 1997, at C1. Three months later, the NASD proposed eliminating from its U-4 registration form any requirement that registered representatives must agree to arbitrate their statutory employment discrimination claims. See George Gunset, Securities Group Yields on Suits, Chi. Trib., Aug. 8, 1997, § 3, at 1.

There are, of course, some important issues of procedural design that have to be considered. How extensive should the opportunity for discovery be in order to provide a meaningful hearing without at the same time replicating the costs and delay of a court action? Can we provide a mechanism for publication of awards, so that representatives of employers and employees can monitor the performance and impartiality of arbitrators, while still preserving the benefits to both parties of low visibility, informal claims resolution? Can the standard for judicial review of awards be modified to ensure adherence to statutory requirements without converting arbitrators into administrative law judges writing detailed opinions? These questions should be addressed; they do not, however, present insurmountable barriers.

C. *Private Law*

Opponents also assume a world dominated by private arbitration of statutory claims in which no public law, no guidance from prior decisions, is generated.[35] Mandatory publication of awards is a close question, for such a requirement would diminish an important benefit of the arbitration alternative. But the private law objection plainly overshoots the mark. As with private postdispute settlement agreements, which also preempt a publicly accessible decision on the merits—and are clearly lawful at present—there would remain under any realistic scenario plenty of claims for the civil courts. Indeed, precisely because arbitration reduces access costs for claimants in addition to other costs faced by employers, many firms will be reluctant to promulgate arbitration policies. In any event, even if the unimaginable were to occur, and all private claimants were confined to arbitration,[36] surely this would free up the resources of administrative agencies to pursue systemic litigation.

D. *Absence of Jury Trials*

A fourth objection highlights the absence of jury trials. Jury trials indeed play, and will continue to play, an important role in the overall system. But consider the following:

First, civil litigation resulting in substantial jury awards is a realistic prospect for relatively few claimants. For the vast majority, a private lawyer cannot be secured and their claims will be addressed, if at

[35] See, e.g., Owen M. Fiss, Against Settlement, 93 Yale L.J. 1073, 1089-90 (1984) (criticizing those advocating emphasis on settlement rather than adjudication because settlement fails to fulfill essential public law function).

[36] Widespread resort to private arbitration of statutory employment claims, however, would change the calculus and support an argument for mandatory publication of awards.

all, by overworked, understaffed administrative agencies. These agencies—after considerable delay—typically offer little more than a perfunctory investigation.

Second, while some individuals with substantial claims—often white senior managers with age discrimination grievances[37] or, if they work in California, Michigan, and a few other places, wrongful dismissal allegations—may lose access to jury trials, the jury trial is a relatively recent innovation in employment law (introduced as late as 1991 for Title VII and ADA lawsuits).

We should not assume that jury trials are an essential feature of the employment law landscape. Major strides were made in the discrimination field for over twenty-five years without resort to juries. Our basic labor laws do not provide for jury trials.[38] European countries with wrongful dismissal laws rely on specialized labor tribunals (essentially tripartite arbitration boards), with well-defined, scheduled recoveries; there is no access to the ordinary civil courts, let alone civil juries, for such disputes.[39]

Jury trials have their downside. They inject an element of uncertainty because of the unpredictability of juries and the risk that, in certain cases, jurors will dispense their own view of social justice rather than make appropriate findings of fact in accordance with the law. This specter of liability undermines society's interest in enabling firms to make sound personnel decisions and, as RAND Institute studies[40] suggest, may have negative effects on the willingness of firms to hire additional workers. In short, we have a system in which a few individuals in protected classes win a lottery of sorts, while others queue up in the administrative agencies and face reduced employment opportunities.

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[37] See, e.g., Michael Schuster & Christopher S. Miller, An Empirical Assessment of the Age Discrimination in Employment Act, 38 Ind. & Lab. Rel. Rev. 64, 68 (1984) (indicating that majority of complaints under the ADEA are filed by male professionals and managers, and inferring from indirect evidence that most such plaintiffs are white).

[38] See, e.g., National Labor Relations Act of 1935, ch. 372, 49 Stat. 449 (codified as amended at 29 U.S.C. §§ 151-169 (1994)); Railway Labor Act of 1926, ch. 347, 44 Stat. 577 (1926) (codified as amended at 45 U.S.C. §§ 151-188 (1994)).

[39] See Samuel Estreicher, Unjust Dismissal Laws: Some Cautionary Notes, 33 Am. J. Comp. L. 310, 313, 315, 316 (1985) (describing use of specialized boards and tribunals to adjudicate such matters in Britain, Germany, and France).

[40] See James N. Dertouzos & Lynn A. Karoly, RAND Inst. No. R-3989-ICJ, Labor-Market Responses to Employer Liability 46-61 (1992) (arguing that state adoption of wrongful termination doctrine reduces aggregate employment); see also James N. Dertouzos, Elaine Holland & Patricia Ebener, RAND Inst. No. R-3602-ICJ, The Legal and Economic Consequences of Wrongful Termination 48 (1988).

E. "Voluntary" Agreements?

Some have suggested that predispute arbitration agreements should be enforceable only when truly "voluntary"; presumably, any evidence of insistence by employers would taint the validity of such agreements.[41] There is certainly a justification for requiring a "knowing" waiver for ensuring that arbitration clauses make it clear if their intended scope encompasses statutory employment claims.[42] Moreover, arbitration clauses should be invalidated if they fail to satisfy general principles of contract law, in the absence of other circumstances indicating that the employee understood what he was waiving. But to go further and insist that these clauses will be upheld only if they satisfy some vague test for "voluntariness" is problematic.

What will be deemed a "voluntary" agreement will be subject to the vagaries of after-the-fact litigation. It is unclear, for instance, whether under this standard applicants could be required to agree to an arbitration clause as a condition of employment, whether improvements in benefits could be exchanged for agreements to submit future disputes to arbitration, or whether voluntary agreements would ever be found except for a narrow category of high level executives. A "voluntariness" test injects an additional element of uncertainty—on top of the doubts under existing law over whether these agreements are binding. This additional layer of uncertainty will have the effect of discouraging such agreements.

A voluntariness standard also detracts from the desired uniformity of internal dispute resolution programs if predispute agreements will be upheld for some employees but not others who are similarly

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[41] See, e.g., Lewis Maltby, Paradise Lost—How the *Gilmer* Court Lost the Opportunity for Alternative Dispute Resolution to Improve Civil Rights, 12 N.Y.L. Sch. J. Hum. Rts. 1, 10 (1994) (arguing that best approach is to allow only "knowing and voluntary" waivers of statutory rights); Lewis L. Maltby, American Civil Liberties Union, Statement of the American Civil Liberties Union Submitted to the Commission on the Future of Worker-Management Relations 4 (Apr. 6, 1994) (on file with the *New York University Law Review*) (insisting that ADR programs are only acceptable if truly "voluntary")

[42] The Ninth Circuit, in Prudential Ins. Co. of Am. v. Lai, 42 F.3d 1299 (9th Cir. 1994), held that a waiver of the judicial forum must be a knowing one, and because the NASD rules at the time did not expressly refer to arbitration of employment claims, there was no knowing waiver in that case. See id. at 1304-05. On October 1, 1993, the Securities and Exchange Commission amended its NASD rules to provide "for the arbitration of any dispute, claim or controversy arising out of or in connection with the business of any member of [NASD] or arising out of the employment or termination of employment of associated person(s) with any member." Kuehner v. Dickinson & Co., 84 F.3d 316, 320-21 (9th Cir. 1996) (enforcing arbitration under new rule); see Williams v. Cigna Fin. Advisors, Inc., 56 F.3d 656, 658 (5th Cir. 1995) (quoting amended NASD rule). See supra note 34 for discussion of subsequent proposal by NASD to eliminate from its registration forms any requirement that registered representatives agree to arbitrate statutory employment discrimination claims.

situated in a particular workforce. A dispute resolution system, like a pension plan, is what economists call a "collective" or "public" good. It is efficiently provided, if at all, on a collective basis. This is because the costs of such a program (an in-house claims processing office, ombudsmen, possible mediators, etc.), even when justified by the collective benefits to the affected employees, typically exceed the benefits to individual employees. Piecemeal application of a dispute resolution program could threaten to unravel the program for all other similarly situated employees.

We should face up to the policy question of whether, in the overall mix, predispute arbitration, if conducted under the right standards, is socially desirable, rather than introduce a voluntariness standard that seeks indirectly to achieve the same outcome as a flat prohibition of such agreements.

IV

THE SUPREME COURT'S *GILMER* DECISION

The Supreme Court, in a number of rulings over the last decade, has interpreted the FAA as a broad statement of congressional policy in favor of agreements to arbitrate both existing and future statutory and contractual claims. The Court's recognition of a strong federal presumption of arbitrability culminated in the 7-2 ruling in 1991 in *Gilmer v. Interstate/Johnson Lane Corp.*[43]

Robert Gilmer was hired by Interstate as a Manager of Financial Services in 1981. As a condition of his employment, he was required to register as a securities representative with several stock exchanges, including the New York Stock Exchange (NYSE). The NYSE required an agreement to arbitrate "any dispute, claim or controversy" arising between him and Interstate.[44] The NYSE's Rule 347 expressly required arbitration of any dispute "arising out of the employment or termination of employment of such registered representative."[45] Discharged six years later at age sixty-two, Gilmer filed an age discrimination charge with the EEOC and then brought suit under the ADEA in the federal district court in North Carolina. Interstate then filed a motion to compel arbitration under the FAA. The district court denied the motion.[46] It cited the Supreme Court's 1974 decision in *Alexander v. Gardner-Denver Co.*,[47] which held that union-represented employees who pursued arbitration under collective bargaining

[43] 500 U.S. 20 (1991).
[44] Id. at 23.
[45] Id.
[46] See id. at 24.
[47] 415 U.S. 36 (1974).

agreements could not be precluded from bringing suits on their independent statutory claims.[48] The Court of Appeals reversed, finding nothing in the text, legislative history, or purposes of the ADEA to prevent arbitration of age bias claims.[49] Writing for himself and six others, Justice White agreed that arbitration could be compelled.[50]

V

LEGAL CHALLENGES FORECLOSED BY *GILMER*

Gilmer left certain issues open, but others were clearly resolved. In all likelihood, registered representatives in the securities industry—who are now required by third party registration organizations to enter into predispute arbitration agreements over claims arising out of their employment—will have to pursue their statutory employment (and other) claims in arbitration.[51]

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[48] See *Gilmer*, 500 U.S. at 24 (citing *Gardner-Denver*). The courts of appeals are presently divided over whether *Gilmer* requires a reconsideration of *Gardner-Denver*'s holding, at least in a case where the collective bargaining agreement authorizes the arbitrator expressly to consider statutory claims and the individual employee to pursue arbitration irrespective of the union's wishes. Compare, e.g., Brisentine v. Stone & Webster Eng'g Corp., 117 F.3d 519, 526-27 (11th Cir. 1997) (arbitration clause does not bar ADA lawsuit where employee has not "agreed individually to the contract containing the arbitration clause"; the agreement does not "authorize the arbitrator to resolve federal statutory claims"; and the agreement does not "give the employee the right to insist on arbitration if the federal statutory claim is not resolved to his satisfaction in any grievance process"), and Pryner v. Tractor Supply Co., 109 F.3d 354, 363 (7th Cir. 1997) (labor arbitration does not preclude lawsuit of Title VII and ADA claims unless employee "consents to have them arbitrated"), with Martin v. Dana Corp., 114 F.3d 421 (3d Cir. 1997) (requiring arbitration of Title VII claim where collective agreement authorizes arbitrator to resolve statutory claim and employee can insist on arbitration), vacated & reh'g en banc granted, No. 96-1746, 1997 WL 368629 (3d Cir. July 1, 1997), and Austin v. Owens-Brockway Glass Container, Inc., 78 F.3d 875, 879 (4th Cir.), cert. denied, 117 S. Ct. 432 (1996) (requiring arbitration of Title VII and ADA claims where collective agreement requires that employer comply with "all laws preventing discrimination").

For an alternative to *Gardner-Denver* in the union-represented sector, see Committee on Labor and Employment Law of the Association of the Bar of the City of New York, Arbitration of Statutory Discrimination Claims Under Collective Bargaining Agreements: Comments to the Secretary of Labor on the Report and Recommendations of the Commission on the Future of Worker-Management Relations, 51 Record of N.Y.C.B.A. 154 (Mar. 1996) (offering interesting "election of remedies" proposal).

[49] See Gilmer v. Interstate/Johnson Lane Corp., 895 F.2d 195, 197 (4th Cir. 1990).

[50] See *Gilmer*, 500 U.S. at 23.

[51] If the NASD proposal to eliminate mandatory arbitration of discrimination claims, see supra note 34, is ultimately approved by the SEC, registered representatives who are required by their employers to agree to predispute arbitration clauses will be treated the same as employees in other industries subject to the FAA. Note should also be taken of the *Duffield* litigation, see supra note 14, where plaintiff argued that *Gilmer* involved only a rejection of facial challenge to securities industry arbitration in a context where the record was bare regarding procedural deficiencies of arbitration under NASD or NYSE auspices. See Plaintiff-Appellant's Opening Brief at 38-39, Duffield v. Robertson Stephens &

There is also no persuasive basis for treating Title VII, the ADA, the Family and Medical Leave Act,[52] or laws like the Employee Polygraph Protection Act[53] differently than the ADEA[54]—particularly in view of the Supreme Court's statement that the party opposing arbi-

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Co., No. C95-0109 (N.D. Cal. filed Jan. 11, 1995), appeal docketed, No. 97-15698 (9th Cir. Apr. 23, 1997).

Moreover, in a recent pair of rulings authored by Judge Reinhardt, panels of the Ninth Circuit appear to have extended the *Lai* requirement of a "knowing waiver" to require that "the employee must explicitly agree to waive the specific right in question." Nelson v. Cyprus Bagdad Copper Corp., 119 F.3d 756, 760-62 (9th Cir. 1997) (employee handbook required that new employee "read and understand" its contents but did not explicitly require that employee agree to its contents); Renteria v. Prudential Ins. Co. of Am., 113 F.3d 1104, 1106-08 (9th Cir. 1997) (registered representative did not make "knowing waiver" because she signed U-4 agreement prior to October 1, 1993 amendment of NASD Code, even though document bound plaintiff to arbitrate all disputes listed in NASD Code "as may be amended from time to time"). Other courts are likely to find a "knowing waiver" if the arbitration agreement expressly refers to employment disputes, whether or not the specific statute that is the basis for a later claim is explicitly listed. See, e.g., Mugnano-Bornstein v. Crowell, 677 N.E.2d 242 (Mass. App. Ct. 1997) (finding employee, by signing arbitration agreement specifically referring to employment disputes, to have agreed to submit sexual harassment and gender discrimination claims to arbitration).

[52] 29 U.S.C. §§ 2601-2653 (1994).

[53] 29 U.S.C. §§ 2001-2009 (1994).

[54] For an attempt to distinguish claims under Title VII from claims under ADEA for arbitrability purposes, see Patrick O. Oudridge, Title VII Arbitration, 16 Berkeley J. Emp. & Lab. L. 209 (1995).

Hortatory language endorsing alternative dispute resolution in provisions of the Civil Rights Act of 1991, Pub. L. No. 102-166, § 118, 105 Stat. 1071, 1081 (1991) (codified at 42 U.S.C. § 12212 (1994)), cannot fairly be read to change preexisting law with respect to predispute arbitration. Because Congress did not amend Title VII to *restrict* arbitration—indeed, section 118 is, if anything, supportive of arbitration "[w]here appropriate and to the extent authorized by law"—statements such as those contained in the conference committee report on the pre-*Gilmer* 1990 version of the 1991 law do not resolve the arbitrability issue:

> The Conferees emphasize . . . that the use of alternative dispute resolution mechanisms is intended to supplement not supplant, the remedies provided by Title VII. Thus, for example, the Conferees believe that any agreement to submit disputed issues to arbitration, whether in the context of a collective bargaining agreement or in an employment contract, does not preclude the affected person from seeking relief under the enforcement provisions of Title VII. This view is consistent with the Supreme Court's interpretation of Title VII in *Alexander v. Gardner-Denver* . . . . The Conferees do not intend *this section* to be used to preclude rights and remedies *that would otherwise be available*.

Conf. Rep. on S. 2104, Civil Rights Act of 1990, reprinted in 136 Cong. Rec. H8050 (daily ed. Sept. 26, 1990) (submitted by Rep. Hawkins) (emphasis added). In the debates over the 1991 law, some legislators were supportive of *Gilmer*. See 137 Cong. Rec. H9548 (daily ed. Nov. 7, 1991) (remarks of Rep. Hyde); 137 Cong. Rec. S15,478 (daily ed. Oct. 30, 1991) (remarks of Sen. Dole). Others were disapproving. See 137 Cong. Rec. H9530 (daily ed. Nov. 7, 1991) (remarks of Rep. Edwards); Stephen Breyer, On the Uses of Legislative History in the Interpretation of Statutes, 65 S. Cal. L. Rev. 845, 845-46 (1992) (quoting Judge Harold Leventhal's observation that legislative history of this type is akin to "looking over a crowd and picking out your friends").

tration bears the heavy burden of showing that "'Congress itself has evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue.'"[55] And, not surprisingly, the courts of appeals have so ruled.[56]

After *Gilmer*, if the FAA is held to apply, broad arguments based on the supposed inferiority of arbitration as a mechanism for adjudicating statutory claims or on the inherent inequality of bargaining power between the parties—despite Justice White's characterization of Gilmer as "an experienced businessman"[57]—will be unavailing. Nor is there any probability of success in pressing the view, in the absence of clear statutory language precluding or limiting arbitration, that policies against prospective waivers of rights and remedies in the federal statute in question override the FAA's presumption of arbi-

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[55] Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991) (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985)).

[56] See, e.g., Patterson v. Tenet Healthcare, Inc., 113 F.3d 832 (8th Cir. 1997) (requiring arbitration of Title VII and state law discrimination claims; finding support in section 118 of the Civil Rights Act of 1991); Great W. Mortgage Corp. v. Peacock, 110 F.3d 222 (3d Cir.) (requiring arbitration of claim brought under New Jersey Law Against Discrimination), cert. denied, 1997 U.S. LEXIS 6057 (Oct. 14, 1997); Pritzker v. Merrill Lynch, Pierce, Fenner & Smith Inc., 7 F.3d 1110 (3d Cir. 1993) (requiring arbitration of claims under Employee Retirement Income Security Act); Saari v. Smith Barney, Harris Upham & Co., 968 F.2d 877 (9th Cir. 1992) (requiring arbitration of claim of retaliation for refusal to take lie detector test allegedly in violation of Employee Polygraph Protection Act); Alford v. Dean Witter Reynolds, Inc., 939 F.2d 229 (5th Cir. 1991) (requiring arbitration of claims under Title VII); see also McNulty v. Prudential-Bache Sec. Inc., 871 F. Supp. 567 (E.D.N.Y. 1994) (requiring arbitration of sales representative's claim that he was demoted for failure to meet production quota on account of time out for jury service allegedly in violation of federal Jury Systems Improvement Act, 28 U.S.C. § 1875 (1994)).

[57] *Gilmer*, 500 U.S. at 33. Although Justice White's opinion appears to leave open some room, the context makes clear that challenges to arbitration agreements covered by the FAA are confined to the narrow straits of § 2 of the statute:

> [T]he FAA's purpose was to place arbitration agreements on the same footing as other contracts. Thus, arbitration agreements are enforceable save upon such grounds as exist at law or in equity for the revocation of any contract. Of course, courts should remain attuned to well-supported claims that the agreement to arbitrate resulted from the sort of fraud or overwhelming economic power that would provide grounds for revocation of any contract. There is no indication in this case, however, that Gilmer, an experienced businessman, was coerced or defrauded into agreeing to the arbitration clause in his registration application. As with the claimed procedural inadequacies discussed above, this claim of unequal bargaining power is best left for resolution in specific cases.

Id. (internal quotes and citations omitted). States can apply customary contract doctrines such as fraud and unconscionability. However, as the Court reaffirmed in Doctor's Assocs., Inc. v. Casarotto, 116 S. Ct. 1652, 1656-57 (1996), the FAA preempts any state law that targets arbitration agreements for different regulatory treatment than other contracts. See infra note 93. For a survey of state law contract defenses, see Jonathan E. Breckenridge, Note, Bargaining Unfairness and Agreements to Arbitrate: Judicial and Legislative Application of Contract Defenses to Arbitration Agreements, 1991 Ann. Surv. Am. L. 925, 973-81.

trability. These arguments were expressly rejected in *Gilmer*.[58] The Court reaffirmed that a no-waiver policy in a statute ordinarily refers to substantive rights and not the right to a judicial forum, and that arbitration is strongly presumed to be as competent as a civil court or administrative agency in adjudicating statutory rights. Thus, the Fifth Circuit has ruled that the safeguards Congress enacted for waivers of "any" rights under the ADEA in the Older Workers Benefit Protection Act of 1990[59] (OWBPA) refer only to waivers of substantive rights and do not apply to predispute waivers of a judicial forum.[60]

VI

The Critical Open Question: The Scope of the § 1 Exclusionary Clause

Gilmer did leave open one very important issue for our purposes—the applicability of the exclusion in § 1 of the FAA. This provision states that "nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."[61] Justice White noted for the Court that the § 1 issue had not been raised below.[62] In any event, he added, the arbitration promise in this case was not contained in an employment agreement between Gilmer and his former employer. Rather, "the arbitration clause at issue is in Gilmer's securities registration application, which is a contract with the securities exchanges, not with Interstate."[63]

Justice White's reasoning leaves room for improvement. It could be argued that the securities registration was tantamount to an employment agreement; since Gilmer did not otherwise have an employment agreement, he had to sign the registration statement as a condition of employment, and the arbitration clause included disputes arising out of his employment with Interstate. Moreover, Interstate is a member organization of the exchanges that require execution of the registration statement. (Also, Justice White's citations to lower court decisions did not support his reading of what constitutes a "contract of employment" for purposes of the § 1 exclusion.[64]) Perhaps this

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[58] 500 U.S. at 26.

[59] 29 U.S.C. § 626(f)(1) (1994).

[60] See Williams v. Cigna Fin. Advisors, Inc., 56 F.3d 656 (5th Cir. 1995).

[61] 9 U.S.C. § 1 (1994).

[62] See *Gilmer*, 500 U.S. at 25 n.2.

[63] Id.

[64] See id. (citing Dickstein v. duPont, 443 F.2d 783 (1st Cir. 1971)); Matison v. Prudential-Bache Securities, Inc., 654 F. Supp. 101 (W.D.N.C. 1987); Legg, Mason & Co. v. Mackall & Coe, Inc., 351 F. Supp. 1367 (D.D.C. 1972); Tonetti v. Shirley, 219 Cal. Rptr. 616 (Ct. App. 1985). These decisions acknowledged that employment contracts were involved.

proves nothing more than that the Supreme Court is infallible because it is final, not the other way around.

A. *Arbitration Required by Third Party Organizations*

If the Supreme Court ultimately resolves the issue it left open by holding that predispute agreements to arbitrate statutory employment claims are enforceable only when those agreements are required by third party registration organizations, the reach of the *Gilmer* decision effectively will be limited to registered representatives in the securities field.[65] The Court is not likely to accept agreements among employers to establish third party organizations whose only purpose is to secure arbitration promises from employees of the participating employers.[66] Such arrangements, in all likelihood, will be viewed as subterfuges. Few, if any, industries are like the securities industry in maintaining self-regulatory organizations with licensure and other functions that operate under the sanction of federal law and with the imprimatur of a federal regulatory agency.

B. *Arbitration Pursuant to State Statutes*

It has been urged that, whatever the scope of the § 1 exclusion, state arbitration statutes—many of which do not contain a similar exclusionary clause[67]—are available to enforce predispute arbitration

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but read the exclusionary clause as limited to employees in transportation industries. See Estreicher, supra note 11, at 753-54.

[65] But cf. supra note 34.

[66] For example, Garry Ritzky is a risk and human resources manager for Turner Brothers Trucking Inc., a company that participates in a peer review adjudication program maintained by Employment Dispute Resolution, Inc. (EDR), an alternative dispute resolution firm based in Atlanta. Ritzky writes:

> This company operates as a third-party entity that contracts with employees and employers separately to provide binding arbitration of all employment-related disputes, including personal injury, age, race, sex, disability and religion. The concept is based on the third-party arrangement used by stockbrokers . . . and all investors who use their services.

Garry M. Ritzky, Reducing Employment-Related Litigation Risks, Risk Mgmt., Aug. 1994, at 49, 50 (discussing benefits of employment dispute resolution). The program comes complete with a defense fund shared by participating employers and involves training of employees who become adjudicators available for other companies. EDR provides a list of three trained nonexempt employees from other companies, three trained management employees from other companies, and three retired judges/attorneys. EDR, founded by Lynn Laughlin (formerly counsel with the Jackson Lewis firm), is reported to have a half dozen companies as clients in addition to Turner. See Wade Lambert, Employee Facts to Arbitrate Sought by Firms, Wall St. J., Oct. 22, 1992, at B1; see also Stephanie Overman, Why Grapple with the Cloudy Elephant?: Alternative Dispute Resolution, HR Magazine, Mar. 1993, at 60.

[67] See supra note 12.

clauses.[68] The FAA by itself would not preempt state laws *enforcing* arbitration agreements excluded from its reach.[69] These state laws thus could be invoked to compel compliance with promises to arbitrate claims arising under state common law and employment statutes. It is unclear, however, whether they provide a basis for requiring arbitration of claims under *federal* statutes that by their terms contemplate judicial remedies for violations. *Gilmer* and its antecedents relied on a federal presumption of arbitrability based on the FAA, requiring evidence that "Congress itself has evinced an intention to preclude a waiver of judicial remedies for the statutory rights at issue."[70] Presumably, that presumption would be unavailable if the arbitration agreement falls within the § 1 exclusion. The issue would then turn on whether—without regard to a federal presumption of arbitrability—the particular federal law precludes binding predispute arbitration agreements.

C. *Alternative Readings of § 1*

On the FAA's applicability, two different textual readings of the § 1 exclusion are available. One position argues that "employment contracts," in ordinary parlance, means all employment contracts, and that the phrase "workers engaged in foreign or interstate commerce" should be taken to embrace all workers in industries that are subject to the reach of the commerce power of Congress. On this view, as Justice Stevens urged in his *Gilmer* dissent, § 1 reflects Congress's central purpose in the FAA to enforce "commercial" contracts among merchants, not agreements between employers and employees.[71]

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[68] See, e.g., Todd H. Thomas, Using Arbitration to Avoid Litigation, 44 Lab. L.J. 3, 13-14 & n.58 (1993).

[69] As the Court noted in Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ., 489 U.S. 468 (1989), the FAA "contains no express pre-emptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration." Id. at 477. *Volt* held that parties to an arbitration agreement covered by the FAA could elect to be governed by a state arbitration statute because such choice of law clauses did not conflict with the pro-arbitration policy of federal law. See id. at 479.

[70] Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 26 (1991) (citing Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 628 (1985)).

[71] See id. at 39 (Stevens, J., dissenting). In his dissent, Justice Stevens also quoted a portion of the hearings on the proposed bill:

> The trouble about the matter is that a great many of these contracts that are entered into are really not [voluntary] things at all. Take an insurance policy, there is a blank in it. You can take that or you can leave it. The agent has no power at all to decide it. Either you can make that contract or you can not make any contract. *It is the same with a good many contracts of employment.* A man says, "These are our terms. All right, take it or leave it." Well, there is nothing for the man to do except to sign it; and then he surrenders his right to

The alternative reading—embraced in virtually all of the post-*Gilmer* decisions in the lower courts—maintains that Congress used limiting language in § 1 to exclude only contracts of employment for "seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce."[72] On this account, the reference to seamen and railroad employees suggests that Congress intended to exclude only employment contracts of classes of workers directly engaged in interstate transportation rather than of all workers in industries "affecting" commerce. Moreover, in view of Supreme Court decisions from the period, Congress might have understood the term "engaged in foreign or interstate commerce" to connote only workers "engaged in interstate transportation, or in work so closely related to it as to be practically a part of it."[73] Thus, the Sixth Circuit stated in *Asplundh Tree Expert Co. v. Bates*:[74]

> We conclude that the exclusionary clause of § 1 of the Arbitration Act should be narrowly construed to apply to employment contracts of seamen, railroad workers, and any other class of workers actually engaged in the movement of goods in interstate commerce in the same way that seamen and railroad workers are. We believe this interpretation comports with the actual language of the statute and the apparent intent of the Congress which enacted it. The meaning of the phrase "workers engaged in foreign or interstate commerce" is illustrated by the context in which it is used, particularly the two specific examples given, seamen and railroad employees, those being two classes of employees engaged in the movement of goods in commerce.[75]

The post-*Gilmer* decisions also rely on precedents originating in the 1950s[76] that considered the FAA's applicability to disputes arising

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have his case tried by the court, and has to have it tried before a tribunal in which he has no confidence at all.

Id. (emphasis added) (quoting Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial Arbitration: Hearings on S. 4213 and S. 4214 Before a Subcomm. of the Senate Comm. on the Judiciary, 67th Cong. 9 (1923) (statement of Sen. Walsh)).

[72] 9 U.S.C. § 1 (1994).

[73] Shanks v. Delaware, Lackawanna, & W. R.R. Co., 239 U.S. 556, 558 (1916) (construing Federal Employers' Liability Act of 1908).

[74] 71 F.3d 592 (6th Cir. 1995).

[75] Id. at 600-01.

[76] See Signal-Stat Corp. v. Local 475, United Elec. Radio & Mach. Workers of Am., 235 F.2d 298, 302 (2d Cir. 1956) (determining that employees of automotive electrical equipment manufacturers were not involved in interstate commerce and hence not within § 1 exclusion); Tenney Eng'g, Inc. v. United Elec. Radio & Mach. Workers of Am., 207 F.2d 450, 452-53 (3d Cir. 1953) (holding that employees engaged in production of goods for subsequent sale in interstate commerce were not exempt under § 1).

These rulings were reaffirmed in later cases. See, e.g., Miller Brewing Co. v. Brewery Workers Local Union No. 9, 739 F.2d 1159, 1162 (7th Cir. 1984) (explaining that § 1 exclu-

under collective bargaining agreements prior to the Supreme Court's 1957 decision in *Textile Workers Union of America v. Lincoln Mills of Alabama*.[77] Fearful that the anti-arbitration premises of state common law would undermine labor arbitration, the courts in these cases strove mightily to preserve some role for the FAA in enforcing arbitration promises in collective agreements.[78] They did so by reading § 1 either as inapplicable to collective bargaining agreements altogether or as limited to employees in particular transportation industries. The Supreme Court's tour de force in *Lincoln Mills*—recognizing a federal common law of collective bargaining contracts under section 301 of the Labor Management Relations Act[79]—essentially removed the need for such creative readings.

Despite its pedigree, the "transportation industry only" reading of § 1 suffers from at least two problems. It requires, as the Sixth Circuit noted (by way of dicta) in *Willis v. Dean Witter Reynolds, Inc.*,[80] that the term "commerce" in § 1 be read narrowly while construing expansively the "transaction involving commerce" language in

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sion applied only to workers in transportation industries); Erving v. Virginia Squires Basketball Club, 468 F.2d 1064, 1069 (2d Cir. 1972) (holding exclusionary language of § 1 not to apply to contract of professional basketball player); Dickstein v. duPont, 443 F.2d 783, 785 (1st Cir. 1971) (explaining that § 1 exemption applied only to employees involved in, or closely related to, actual movement of goods in interstate commerce).

[77] 353 U.S. 448 (1957).

[78] The union in *Lincoln Mills* offered the FAA as an alternative basis for enforcing the employer's executory promise to arbitrate. See David E. Feller, End of the Trilogy: The Declining State of Labor Arbitration, Arb. J., Sept. 1993, at 18, 19 (discussing union reliance primarily on section 301 of the Labor Management Relations Act of 1947, ch. 120, 61 Stat. 136, 156-57 (codified as amended at 29 U.S.C. § 185 (1994)), "because of the hostility of the courts to arbitration under the FAA. As a back-up [the union] also argued that the exclusion in Section 1 of the FAA of contracts of employment applied only to individual contracts and was inapplicable to collective bargaining agreements."). The union also relied, in the alternative, on the "transportation industry only" reading of § 1:

> [If] the Court should find that the exemption of contracts of employment contained in Section 1 of the Act was intended to exempt all labor arbitration because those who drafted it would not have recognized the distinction between collective agreements and contracts of hire, then, on the same principles, the exemption should be read as covering only what it was intended to cover, that is, contracts of seamen, railroad employees, and other workers engaged directly in foreign or interstate commerce. It cannot simultaneously be urged that the 1925 exemption should be read as it would have been read in 1925, but that the class of workers affected by the exemption should not be limited to the class of workers intended to be covered by the 1925 language. The workers in this case are not engaged in interstate commerce. They are engaged in industry affecting interstate commerce . . . .

Petitioner's Brief at 58-59, *Lincoln Mills* (No. 211).

[79] 29 U.S.C. § 185 (1994).

[80] 948 F.2d 305 (6th Cir. 1991).

§ 2, which defines the FAA's substantive reach.[81] Indeed, the Supreme Court in *Allied-Bruce Terminix Cos., Inc. v. Dobson*[82] held that the language of § 2 should be read broadly as coextensive with the reach of the Commerce Clause—even though the pre-New Deal Congress that passed the Act in 1925 was working with a narrower conception of the commerce power.[83]

Another difficulty with the "transportation industry only" reading is the absence of evidence that such a limitation reflects a discernible purpose of Congress. While it is hard to assume Congress would have any purpose to exclude arbitration agreements signed by highly-placed executives, it is no less difficult to attribute to Congress some purpose for excluding individual employment contracts of seamen, railroad employees, and others directly engaged in interstate shipment of goods while covering individual employment contracts of all others who work for firms subject to its commerce power. In a 1953 ruling, the Third Circuit attempted to justify such line drawing by noting that Congress had provided grievance machinery for seamen and railroad workers and presumably sought to exclude from the FAA workers "as to whom special procedure for the adjustment of disputes had previously been provided."[84]

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[81] See id. at 310-11. Section 2 makes enforceable a written arbitration provision in "a contract evidencing a transaction involving commerce." 9 U.S.C. § 2 (1994).

[82] 513 U.S. 265 (1995).

[83] See id. at 275. Thus, Professor Finkin argues:

> In 1925, Congress had no power to legislate regarding contracts of employment of accountants or secretaries even if they worked for railroads or steamship companies, or of deliverymen if they did not cross state lines. It was irrelevant whether or not the statute dealt with employees "in" interstate commerce, "engaged in" interstate commerce, or who were "involved in" interstate commerce, for however the statute was phrased, these employees were wholly outside the power of Congress to regulate at the time, and Congress could not have intended to include them. It should follow that as the Court expanded the scope of the commerce power to reach all these employees, the scope of the exemption expanded as well, leaving their status just as Congress contemplated, *i.e.*, as not reached by the arbitration act.

Matthew W. Finkin, Employment Contracts Under the FAA—Reconsidered, 48 Lab. L.J. 329, 333 (June 1997).

A somewhat different argument for excluding FAA coverage is suggested by Rushton v. Meijer, Inc., No. 199684, 1997 WL 476366, at *9 (Mich. App. Aug. 19, 1997) (arguing that store's floor detective's duties "did not facilitate, affect, or arise out of interstate or foreign commerce"). The suggestion cannot be squared, however, with the Supreme Court's *Dobson* ruling.

[84] Tenney Eng'g, Inc. v. United Elec. Radio & Mach. Workers of Am., 207 F.2d 450, 452 (3d Cir. 1953). As the court stated in *Tenney*:

> Seamen constitute a class of workers as to whom Congress had long provided machinery for arbitration. In exempting them the draftsmen excluded also railroad employees, another class of workers as to whom special procedure for the adjustment of disputes had previously been provided. Both these classes of

Both readings of the § 1 exclusion are hampered by a murky legislative history. What evidence there is suggests only that the exclusionary clause was inserted in response to objections from organized labor—principally voiced by Andrew Furuseth, then-head of the Seafarers' Union—that the FAA would somehow operate as a "compulsory labor" measure. The original bill, introduced in 1922, did not contain the exclusionary clause.[85] In the congressional hearings, representatives of the American Bar Association (ABA), which had been actively involved in the drafting process, urged that labor's concern was misplaced:

> It was not the intention of this bill to make an *industrial arbitration* in any sense; and so I suggest that . . . if your honorable committee should feel that there is any danger of that, they should add to the bill the following language, "but nothing herein contained shall apply to seamen or any class of workers in interstate and foreign commerce." It is not intended that this shall be an act referring to *labor disputes*, at all. It is purely an act to give the merchants the right or the privilege of sitting down and agreeing with each other as to what their damages are, if they want to do it.[86]

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workers were engaged directly in interstate or foreign commerce. To these the draftsmen of the Act added "any other class of workers engaged in foreign or interstate commerce." We think that the intent of the latter language was, under the rule of ejusdem generis, to include only those other classes of workers who are likewise engaged directly in commerce, that is, only those other classes of workers who are actually engaged in the movement of interstate or foreign commerce or in work so closely related thereto as be in practical effect part of it. The draftsmen had in mind the two groups of transportation workers as to which special arbitration legislation already existed and they rounded out the exclusionary clause by excluding all other similar classes of workers.

Id. at 452-53. The Sixth Circuit quoted this passage with approval in Asplundh Tree Expert Co. v. Bates, 71 F.3d 592, 598 (6th Cir. 1995).

Chief Judge Edwards of the D.C. Circuit and Chief Judge Posner of the Seventh Circuit take a similar view in, respectively, Cole v. Burns Int'l Sec. Servs., 105 F.3d 1465, 1471 (D.C. Cir. 1997) (upholding parties' arbitration agreement and supporting narrow reading of exclusionary clause based in part on reasoning of *Tenney*) and Pryner v. Tractor Supply Co., 109 F.3d 354, 358 (7th Cir. 1997) (finding that legislative history supports narrow reading of exclusionary clause).

[85] See Sales and Contracts to Sell in Interstate and Foreign Commerce, and Federal Commercial Arbitration: Hearings on S. 4213 and S. 4214 Before a Subcomm. of the Senate Comm. on the Judiciary, 67th Cong. 9 (1923) (statement of W.H.H. Piatt, chairman of the Committee of Commerce, Trade, and Commercial Law of the American Bar Association).

[86] Id. (emphasis added).

When the bill was reintroduced in December 1923, it contained the exclusionary clause.[87] Apparently, organized labor was satisfied because it played no role in the subsequent hearings.

Based on a review of the *internal* proceedings of the American Federation of Labor and the Seafarer's Union, the argument has been offered that labor's objections were misstated by the ABA representatives.[88] On this account, the unions' principal concern was not that the FAA would mandate "industrial arbitration" of labor disputes but rather that ship masters would be able to foist arbitration and compulsory service on seamen who were required by federal law to have individual contracts of hire. Accordingly, the § 1 exclusion should be read as a response to broad-based concerns over the inherent inequality of individual workers' bargaining power.[89]

There is, unfortunately, little, if any, evidence that Congress in 1925 shared this understanding when it enacted the FAA.[90] If the is-

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[87] See Arbitration of Interstate Commercial Disputes: Joint Hearings on S. 1005 and H.R. 646 Before the Subcomms. of the Comms. on the Judiciary, 68th Cong. 2 (1924) (including recitation of bill text that contained exclusionary clause).

[88] See Matthew W. Finkin, "Workers' Contracts" Under the United States Arbitration Act: An Essay in Historical Clarification, 17 Berkeley J. of Emp. & Lab. L. 282, 295-96 (1996).

[89] Consider Judge Posner's reaction to Professor Finkin's essay in Pryner v. Tractor Supply Co., 109 F.3d 354 (7th Cir.), cert. denied, 1997 WL 275009 (Oct. 14, 1997):

> Professor Finkin argues that the prevailing view, which limits the exclusion in section 1 to employment contracts in transportation, is wrong. His review of the legislative history . . . has persuaded him that Congress's intention was to exclude *all* employment contracts. Yet, as he acknowledges, the impetus for the exclusion came entirely from the seafarers union, concerned that arbitrators would be less favorably inclined toward seamen's claims than judges were. Judges favored such claims, the union thought, in part because of a tradition that seamen were "wards in admiralty," in part because of peculiarities of maritime law that would make it easy to slip an arbitration clause into a maritime employment contract without the seaman's noticing it, and in part because the maritime employment relation was already heavily regulated by federal law. It was soon noticed that the railroad industry's labor relations were also heavily regulated—by a statute (the Railway Labor Act) that included provisions for compulsory arbitration of many disputes. Motor carriers were not yet comprehensively regulated, but it may have seemed (and was) only a matter of time before they would be; hence the expansion of the exclusion from seamen to railroad to other transportation workers. It seems to us, as it did to the Third Circuit [in the *Tenney* decision], that this history supports rather than undermines limiting "engaged in foreign or interstate commerce" to transportation.

Id. at 358.

[90] Professor Finkin acknowledges:

> No "paper trail" has been left of the history of the exemption. A search of the files of the Commerce Department, the Senate Judiciary Committee, then Secretary Hoover, Senator Walsh (who left a voluminous archive), the legislative files of the AF of L, and Victor Olander (for the files of the [International Seamen's Union]) yielded a scanty record bearing upon the Act and *no record whatsoever concerning the exemption*.

sue of interpretation turns on the specific intent of Congress at the time, the most that can be said is that Congress intended to exclude disputes involving collective bargaining agreements from the reach of the FAA.[91] Yet the language that Congress used in the exclusionary clause cannot easily be made to fit an exclusion limited to labor disputes, even if this were Congress's principal focus in 1925.

The Supreme Court will have to choose between two alternatives. One interpretation of the exclusionary clause essentially reads the FAA out of the picture for all employment disputes outside of the security industry. The second offers a narrow reading of the clause that seeks to preserve a substantial role for the FAA in this area.

Although prediction is a hazardous enterprise—especially when dealing with the Supreme Court—a broad interpretation of the exclusion is improbable. The Court would have to reject the essential thrust not only of *Gilmer* but also its prior ruling in *Perry v. Thomas*,[92]

Finkin, supra note 88, at 295 n.61 (emphasis added). For Senator Walsh's statement, see supra note 71.

[91] See United Paperworkers Int'l Union, AFL-CIO v. Misco, Inc., 484 U.S. 29, 40 n.9 (1987) (quoting § 1 exclusion and observing that "the federal courts have often looked to the [FAA] for guidance in labor arbitration cases"). The clear implication is that § 1 excludes collective bargaining agreements.

Consider also the Fourth Circuit's assessment of the legislative purpose in United Elec. Radio & Mach. Workers of Am. v. Miller Metal Prods., 215 F.2d 221 (4th Cir. 1954):

> It appears that the exclusion clause of the Arbitration Act was introduced into the statute to meet an objection of the Seafarers International Union; and certainly such objection was *directed at including collective bargaining agreements rather than individual contracts of employment under the provisions of the statute*. The terms of the collective bargaining agreement become terms of the individual contracts of hiring made subject to its provisions and the controversies as to which arbitration would be appropriate arise in almost all instances, not with respect to the individual contracts of hiring, but with respect to the terms engrafted on them by the collective bargaining agreement. It is with respect to the latter that objection arises to the compulsory submission to arbitration which the Arbitration Act envisages. *No one would have serious objection to submitting to arbitration the matters covered by the individual contracts of hiring divorced from the provisions grafted on them by the collective bargaining agreements*.

Id. at 224 (emphasis added) (quoted with approval in Kropfelder v. Snap-Tools Corp., 859 F. Supp. 952, 957 (D. Md. 1994)).

On the other hand, the Court in *Miller Metal Products* was "[not] impressed by the argument that the excepting clause of the statute should be construed as not applying to employees engaged in the production of goods for interstate commerce as distinguished from workers engaged in transportation in interstate commerce, as held by the majority in Tenney . . . ." *Miller Metal Products*, 215 F.2d at 224. Attempting to qualify this language, the district court in Kropfelder v. Snap-on Tools Corp., 859 F. Supp. 952 (D. Md. 1994), suggested, "[t]hat statement was made in the context of arbitration agreements contained in collective bargaining agreements." Id. at 957 n.11.

[92] 482 U.S. 483 (1987) (holding that FAA preempted anti-arbitration provision of California wage payment law so as to compel arbitration).

which likewise involved statutory employment claims. Moreover, although one can say that the Court simply would be interpreting the scope of the § 1 exclusion—an issue not squarely resolved in any prior ruling—the underlying policy justification that would be attributed to Congress for such a broad reading clashes with much of the reasoning that undergirds the Court's FAA jurisprudence. The Justices would be, in a sense, disowning their earlier pronouncements of arbitral competence—that arbitration is not a disfavored institution for resolving statutory claims and that generalized concerns over inequality of bargaining power cannot be raised to prevent arbitration (unless the federal statute in question evinces a clearly stated policy against arbitration or the contract would be invalid under the state's general law of contracts).[93] In addition to the obstacles created by prior rulings, the caseload and "litigation explosion" considerations that implicitly prompted the Court in the first place to find in the FAA a broadly preemptive pro-arbitration sword argue against a broad reading of the exclusion which is compelled neither by text nor available legislative history.

VII

Role of Public Policy Considerations

It is important to remember, however, that, irrespective of the scope of the exclusionary clause, the federal agencies enforcing the employment statutes have an important role to play in the process of ensuring that arbitration of statutory claims broadly conforms to the public policies contained in those laws.

A. Anti-Retaliation Provisions

If we decide as a policy matter that predispute agreements are enforceable, even if insisted upon as a condition of employment, that determination should foreclose use of the anti-retaliation provisions of the employment laws[94] to attack, without more, such insistence on

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[93] In Doctor's Associates, Inc. v. Casarotto, 116 S. Ct. 1652 (1996), the Supreme Court examined a Montana statute that declared arbitration clauses unenforceable unless they contained a prominent notice on the first page of the agreement stating that the contract was subject to arbitration. The Court held (8-1) that the statute was preempted by § 2 of the FAA, 9 U.S.C. § 2 (1994), because it singled out arbitration for regulation not applicable to contracts generally. See id. at 1656-57.

[94] Section 704(a) of Title VII provides in pertinent part that an employer may not discriminate against the employee (or former employee) "because he has opposed any practice made an unlawful employment practice by this subchapter [so-called opposition clause], or because he has made a charge, testified, assisted, or participated in any manner in an investigation, proceeding, or hearing under this subchapter [so-called participation clause]." 42 U.S.C. § 2000e-3(a) (1994). The legal issue would be whether an employer's

the agreement itself. These provisions should not be used as a backdoor vehicle for relitigating the policy judgment already made. If an employer has a right under the FAA to insist on a predispute arbitration clause, the refusal to hire a job applicant who declines to agree to such a clause cannot be actionable retaliation under the discrimination laws.

There would, however, be some role for the anti-retaliation provisions. As the *EEOC v. River Oaks Imaging and Diagnostic*[95] litigation in Texas makes clear, employers should not be able to use arbitration agreements as a club to retaliate against employees who have filed charges with the EEOC.[96]

B. *Right to File Charges with the EEOC*

A more productive route for regulatory oversight is provided by the right of claimants to file charges with the EEOC and other enforcement agencies even when they have signed predispute arbitration agreements. Under current law, employees may not waive, and employers cannot require waiver of, the right to initiate a proceeding with the EEOC and other agencies.[97] The filing of a charge gives the

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insistence on a predispute arbitration clause, or in its adherence once a dispute has arisen, violates either the "opposition" or "participation" clause.

[95] Civ. A. No. H-95-755, 67 Fair Empl. Prac. Cas. (BNA) 1243 (S.D. Tex. Apr. 19, 1995) (granting preliminary injunction preventing employer from requiring employees to agree to dispute resolution procedure that interferes with employees' right to file complaints with EEOC).

[96] Consider, however, some of the decisions rejecting an "election of remedies" approach for union-represented employees. See, e.g., EEOC v. Board of Governors of State Colleges and Univs., 957 F.2d 424 (7th Cir. 1992) (holding that collective bargaining agreement prohibiting grievances from proceeding to arbitration if employee filed lawsuit or age-bias charge with EEOC violated ADEA); EEOC v. General Motors Corp., 826 F. Supp. 1122 (N.D. Ill. 1993) (determining that employer violated anti-retaliation provisions of Title VII and ADEA by withdrawing access to internal dispute resolution procedure when employees filed charges with EEOC). Employers (and unions) should be prevented from withholding contractual processes simply because employees have filed charges with the EEOC or other enforcement agencies. But query whether the anti-retaliation provisions should bar the parties to a collective bargaining relationship from establishing a program for internal resolution of disputes that, if invoked by employees, forecloses any later court suit, provided that the arbitrator has the authority to consider statutory issues and award statutory remedies for violations. For a related proposal, see *supra* note 48.

[97] See Older Workers Benefit Protection Act, 29 U.S.C. § 626(f)(4) (1994) (stating that "No waiver may be used to justify interfering with the protected right of an employee to file a charge or participate in an investigation or proceeding conducted by the [EEOC]."); EEOC v. Cosmair, Inc., 821 F.2d 1085, 1089-90 (5th Cir. 1987) (holding employee waiver of right to file charge with EEOC void as against public policy). The validity of postdispute settlement agreements that preclude the filing of charges with the EEOC is the subject of EEOC v. Astra U.S.A., Inc., 929 F. Supp. 512 (D. Mass. 1996) (issuing preliminary injunction restraining employer from enforcing settlement agreements prohibiting employees from assisting EEOC in its investigation of sexual harassment charges), aff'd in part and

agency an important window of opportunity to monitor employer practices (including the fairness and integrity of arbitration procedures) and to decide whether to file a lawsuit. Even if the courts ultimately hold, as Judge Sprizzo did in the *EEOC v. Kidder, Peabody & Co.*[98] litigation, that the EEOC has no authority to seek monetary relief for an employee who has agreed to arbitrate his employment dispute, the agencies retain authority to pursue injunctive relief where appropriate and sue on behalf of employees who have not agreed to submit disputes to arbitration.[99]

C. *Promulgation of Quality Standards by Agency Rulemaking*

Another route would be for the EEOC and other agencies to use their rulemaking authority (if they have it), or at least to issue regulatory guidance (if they do not), to set the quality standards that should govern arbitration of statutory employment claims. One step they could readily take is to endorse the model procedures of dispute resolution organizations like the AAA[100] and the Center for Public Resources[101] (and those suggested by the Dunlop Commission and the Due Process Protocol). "Moral suasion," to use a term favored by Felix Frankfurter, would go a long way to improve the process.[102]

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vacated in part, 94 F.3d 738 (1st Cir. 1996) (dissolving injunction but affirming that nonassistance covenants prohibiting employee communication with EEOC are void as against public policy).

[98] No. 92 Civ. 9243, 1997 WL 620809 (S.D.N.Y. Oct. 6, 1997) (holding that EEOC may not seek only monetary relief on behalf of individual employees who have signed binding predispute arbitration agreements); accord EEOC v. Frank's Nursery & Crafts, Inc., 966 F. Supp. 500 (E.D. Mich. 1997).

[99] The Supreme Court in *Gilmer* stated that "arbitration agreements will not preclude the *EEOC* from bringing actions seeking class-wide and equitable relief," Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 32 (1991), but did not resolve whether such agreements could preempt an EEOC action seeking monetary relief on behalf of individual employees who had agreed to arbitration. Cf. EEOC v. Harris Chernin, Inc., 10 F.3d 1286, 1290-92 (7th Cir. 1993) (holding that prior ADEA judgment precluded subsequent EEOC action seeking individual relief for employee, as opposed to injunctive relief against further violation). Because in the *Kidder, Peabody* litigation the employer had gone out of business, and no theory of successor liability was pursued against the purchaser of its assets, the EEOC conceded that it lacked any basis for seeking injunctive or other prospective relief. See EEOC v. Kidder, Peabody & Co., No. 92 Civ. 9243, 1997 WL 620809 (S.D.N.Y. Oct. 6, 1997).

[100] See supra note 16.

[101] See Center for Public Resources, Institute for Dispute Resolution, Employment ADR: A Dispute Resolution Program for Corporate Employers (1995).

[102] Rather than play this leadership role in prodding companies to develop arbitration systems meeting essential adjudicative quality standards, the EEOC is content to rail against the prevailing winds and state its implacable opposition to predispute arbitration of employment discrimination claims. See EEOC Policy Statement on Mandatory Binding Arbitration, reprinted in Daily Lab. Rep. (BNA) No. 133, at E-4 (July 11, 1997) (setting forth position that agreements mandating binding arbitration of discrimination claims as

Conclusion

A well-designed private arbitration alternative for employment claims is in the public interest and is achievable. The law should encourage, rather than hinder, arbitration of employment disputes that are conducted in a manner that satisfies the standards for a fair hearing before a neutral arbiter empowered to apply the law and, where warranted, to award statutory remedies.

condition of employment are contrary to the policy of the employment discrimination laws).

PREPARED STATEMENT OF CLIFF PALEFSKY

CHAIRMAN, SECURITIES INDUSTRY ARBITRATION COMMITTEE

ON BEHALF OF THE

NATIONAL EMPLOYMENT LAWYERS' ASSOCIATION

JULY 31, 1998

Introduction

The National Employment Lawyers Association (NELA) is an organization of over 3,000 of this country's leading civil rights and employment lawyers. NELA's members include not only attorneys in private practice but also lawyers on the staffs of the Equal Employment Opportunity Commission and various State antidiscrimination agencies. We are the attorneys to whom Congress looks for help in enforcing our Nation's civil rights and labor laws.

The NELA strongly supports all *voluntary* forms of alternative dispute resolution, including arbitration and mediation. In fact, NELA has been in the forefront nationally in encouraging mediation as a preferred method for resolving employment disputes. We helped draft the Due Process Protocol for the Resolution of Statutory Disputes and worked closely with the American Arbitration Association in the development of their specialized employment arbitration rules and procedures.

Because there appears to be such a great disparity between the public perception of arbitration and its day to day reality, both legal and factual, it is important to begin these comments by setting forth some basic facts about the process which are often misunderstood.

Unlike our constitutionally defined civil justice system, arbitration is not designed with the primary goal of achieving the legally correct result. Its primary objective is finality and economy in achieving that finality. Although most of the general public is unaware of the fact, arbitrators are not required to know or follow the law. Moreover, a legally incorrect ruling cannot be appealed or rectified. The law is clear that a decision reached through binding arbitration must be confirmed even if there is an error of fact or law on the face of the award that causes substantial injustice to the parties.

Litigants for whom a quick and final decision is of primary importance, who do not require much discovery to establish their cases, and who are willing to risk a decision that could impose a result contrary to law, are certainly entitled to opt for binding arbitration of their claims, and indeed it may well be the most logical forum for the resolution of certain kinds of disputes. But the compulsory submission of all claims, including civil rights claims, whistle-blower claims, and ERISA claims, by employees as a condition of employment is another matter entirely. The problem is even more acute when the forum is controlled by the employers and does not conform to consensus minimum standards of due process.

Simply put, you cannot allow the entity being regulated by your legislation to unilaterally opt out of the requirements of that legislation.

Proponents of mandatory arbitration mistakenly assert that arbitration is "just another forum" and that substantive rights are not lost in that forum. These claims are simply not true. Employees lose the right to have the employment laws passed for their protection correctly enforced, which is the ultimate substantive right.

It does employees little good to have numerous protective statutes enacted by Congress for their benefit, if the arbitrators by whom those statutes are enforced are selected exclusively by their employers and are permitted to ignore or misapply these laws at their own discretion. Yet this is precisely the situation which is faced by employees in the securities industry arbitration context and, since courts are essentially powerless to review or correct decisions reached through such binding arbitration, arbitrators are unchecked in their power to ignore or misapply statutory law, including the civil rights laws.

Securities industry arbitrators are explicitly instructed in their *Arbitrator's Manual* that they have no obligation to follow statutory law. Even if an individual arbitrator feels morally obligated to follow the law, however, he or she may make an error of law. In such an instance, it is virtually impossible to overturn even the most blatant errors of law, since the standard of review is exceedingly narrow. As several cases have established, that standard requires that the arbitrator: (a) knew the law; (b) found it applicable to the facts at issue; and, nevertheless, (c) specifically chose to ignore it. Not surprisingly, such a restrictive standard of "manifest disregard [of] the law" is nearly impossible to meet. This leads to such outlandish results as *DiRussa* vs. *Dean Witter* (121 F.3d 818 (2nd Cir. 1997)), in which the arbitrator failed to award attorneys fees to a prevailing plaintiff in a discrimination case, in plain violation of the statutory requirement. The arbitrator's erroneous decision was

affirmed by the court, which stated that even though the arbitrator was clearly wrong under the law, the court could not reverse or correct his decision since there was no clear proof that he had "known" the law and then had intentionally "disregarded" it.

Correction of an erroneous arbitral decision is also rendered virtually impossible by the fact that arbitrators are not required to set forth any written explanation of their decision, so there is rarely anything to review anyway. More significantly, securities industry arbitrators have historically been trained and encouraged *not* to provide written findings in order to frustrate judicial review. Most arbitration awards in the securities industry fora are not even written by the arbitrator. They are usually drafted by staff using boiler plate language that makes it impossible to determine what was or was not decided. The consequent lack of effective judicial review is particularly serious in arbitrations which have been unilaterally imposed by one party on the other in a forum controlled by the stronger party.

Furthermore, the costs to an employee to vindicate his or her rights in the arbitration forum are exorbitant, despite industry rhetoric to the contrary. An employee does not have to pay a Federal court judge to hear his or her discrimination claim; access to the public courts is free, once the initial $150 filing fee is paid. By contrast, employees who are required to submit such claims to securities industry arbitration face exorbitant "forum" costs—a $500 initial filing fee, and then between $1,500 and $3,000 *per day* in arbitration forum fees. The result is that, over the course of a typical securities industry arbitration, a plaintiff may ultimately be liable for tens of thousands of dollars in forum fees *even if he or she prevails*. Forum fees in discrimination cases in the securities industry are routinely in excess of $20,000, and several have been in excess of $40,000, $60,000, or even, as in the case of *Wolfe* vs. *Schwab*, *$82,000*.

These outlandish costs and fees imposed on those who have been compelled to arbitrate their claims act as a significant barrier to employees who wish to exercise their statutory rights. Indeed, several circuit courts have recently found that there is no precedent in American jurisprudence for charging a citizen for the right to have statutes enacted for his or her protection enforced and that such costs cannot be imposed. *Cole* vs. *Burns International Security*, 105 F.3d 1465 (D.C. Cir. 1997); *Paladino* vs. *Avnet Computer*, 134 F.3d 1054 (11th Cir. 1998). Despite the clear holding of two circuit courts of appeal that such fees are in fact illegal, the NASD not only continues to charge these unconscionable fees for the vindication of statutory rights, but has asked for the right to increase them.

It is also important to note that, in arbitration, discovery is significantly limited, which unfairly burdens employees seeking to vindicate statutory rights. Arbitration works best when the parties have equal access to the evidence necessary to prove their claims—in contract or construction disputes, for example, where extensive discovery is not necessary. An employee plaintiff, on the other hand, generally needs fairly extensive discovery if he or she is going to establish a discrimination claim. Such a plaintiff not only has the burden of proof, but also must, in many employment cases, prove "state of mind" by circumstantial evidence, show "pretext" by the employer to disprove the stated reason for discharge, and/or show a "pattern" of discriminatory conduct. Without full and complete discovery, such proof is extremely difficult to establish. This imbalance of access to evidence is exacerbated in the employment context by the fact that employee-plaintiffs' attorneys are ethically precluded from informally contacting most of the defendant's current employees.

In litigation, such essential discovery is easily obtained under the Federal (or applicable State) Rules of Civil Procedure. Arbitration, however, typically permits very little, if any, discovery, and whatever limited discovery is allowed is left to the discretion of the arbitrator (depositions, for example, which are often the only method for obtaining critical evidence from employee witnesses, are often either prohibited altogether or severely limited in arbitration). These limitations on discovery in arbitration inevitably, and very heavily, favor the employer in any employee/employer dispute, since *the employer usually controls almost all of the critical evidence*. Securities arbitrators have historically been trained to permit depositions only for the purpose of preserving testimony of witnesses unavailable for the actual arbitration. Therefore, employees often hear many of the stated reasons for their discharge for the first time at the arbitration hearing itself, with no effective method of cross-examination. It must be noted that the securities industry has steadfastly refused to adopt the expanded discovery provisions of the due process protocol which have been adopted by the American Arbitration Association and every other truly neutral ADR provider.

A further obstacle to employees in arbitration is the fact that arbitrators are not required to follow the established rules of evidence. This can, and often does, mean that the employee/plaintiff loses the benefit of significant evidentiary protections. In

sexual harassment cases, for example, consensual sexual activity by the plaintiff with persons other than the harasser is excluded under Federal law and in many State jurisdictions as irrelevant and invasive of the plaintiff's right to privacy. Yet an arbitrator in such a case, under no obligation to comply with such an evidentiary restriction, may allow the employer to forage where it desires in a plaintiff's private conduct.

Extensive documentation now exists as to the fundamental inequity of mandatory securities industry arbitration of employees' statutory claims. Many recent studies, surveys, and articles by professional neutrals and academics have demonstrated conclusively that mandatory arbitration of statutory claims places the employee/plaintiff at a *severe disadvantage* and that outcomes in mandatory arbitrations are consistently far more favorable to employers than to employees when compared to the results reached in similar cases brought in a public court—which is precisely why the industry has fought so hard to maintain the present system.

Evidence of this disadvantage to the employee/plaintiff includes:

1. "Repeat User Bias." Many scholars and commentators have for some time expressed concern that, since arbitrators rely on repeat business for income, there is a potential for "repeat user bias" by arbitrators, *i.e.*, a natural tendency to favor the party which has the potential for using the arbitrator's services again (D. Schwartz, *Enforcing Small Print to Protect Big Business: Employee and Consumer Rights Claims in an Age of Compelled Arbitration*, 1997 Wisc. L.R. 33, 73–81, 122–23 (1997); J. Sternlight, *Panacea or Corporate Tool?: Debunking the Supreme Court's Preference for Binding Arbitration*, 74 Wash. U. L.Q. 637, 647–52 (1996)). It goes without saying that, in the employment setting, the "repeat users" are the employers. Significantly, there now exists an empirical study by Professor Lisa Bingham of the University of Indiana School of Public Policy which demonstrates that this *"repeat user bias" does in fact exist in employment arbitration* (L. Bingham, *Employment Arbitration: The Repeat Player Effect*, Emply.Rts. & Empl.Policy Journal 1 (1997)). The importance of this study is enormous in any consideration of employer-mandated arbitration in the securities industry, since it statistically confirms the reality of structural bias in favor of the employer in employment arbitration. Securities industry employers also have extensive databases of arbitrators' prior awards and proclivities, which gives them a major advantage in the selection process.

2. Several studies and surveys confirm that employers are far more successful in arbitration than they are in court before a jury. Employers not only win more often in arbitration; employees who do manage to prevail are awarded far less in damages (D. Schwartz, *Enforcing Small Print to Protect Big Business—cited above*; R. Alleyne, *Statutory Discrimination Claims: Rights "Waived" and Lost in the Arbitration Forum*, 13 Hofstra Labor L.J. 381 (1996); Bompey & Pappas, *Is There A Better Way? Compulsory Arbitration of Employment Discrimination Claims After Gilmer*, 19 Emp.Rel.L.J. 197 (1994)). These findings are consistent with studies indicating that, when a petition to compel arbitration is filed, it is always the *employer* who is seeking to compel arbitration, while the employee is inevitably attempting to bring his or her claims in Federal or in State court (D. Schwartz, *Enforcing Small Print to Protect Big Business*, Bompey & Pappas, *Is There A Better Way?—both cited above*). Employers would hardly be uniformly seeking an arbitration forum unless they correctly understood it to give them an advantage over employees.

3. Counsel for employers repeatedly and publicly recommend that their employer clients use mandatory arbitration for discrimination claims. These attorneys unabashedly base this advice on the fact that, in arbitration, employers will win more and pay less in damage awards when they lose, be far more likely to avoid an assessment of punitive damages, and even possibly succeed in discouraging the employee from pursuing a claim altogether, given the costs and obstacles imposed by arbitration (D. Schwartz, *Enforcing Small Print to Protect Big Business*, Bompey & Pappas, *Is There A Better Way?—both cited above*, and BNA Employment Discrimination Report, 1996, Vol. 6, p. 875, summarizing comments by Paul Cane, a management employment law attorney, in a speech before a conference sponsored by the Labor and Employment Law Section of the State Bar of California).

On the other hand, Government agencies and commissions, academics, and professional arbitration organizations have gone on record as strongly opposing mandatory employment arbitration of statutory claims.

The *Equal Employment Opportunity Commission*, the agency charged by Congress with responsibility for enforcing this Nation's civil rights laws, has issued an extensive policy statement dealing with mandatory arbitration. While strongly supporting the utilization of *voluntary* ADR procedures, the EEOC stated that, "Agreements that mandate binding arbitration of discrimination claims as a condition of employment are contrary to the fundamental principles evinced in the Federal anti-

discrimination statutes," and are thus both illegal and unenforceable. EEOC, Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment, 133 Daily Lab.Rep. (BNA) E–4 (July 11, 1997). This EEOC policy was approved unanimously by the Republican and Democratic appointees to the Commission.

Among the EEOC's objections are that arbitration is not governed by the statutory requirements and standards of Title VII; it is conducted by arbitrators given no training and possessing no expertise in employment law; and it forces employees to pay exorbitant "forum fees" in the tens of thousands of dollars, greatly discouraging aggrieved employees from seeking relief.

The *National Academy of Arbitrators*, the leading and most respected national organization of professional labor–management arbitrators and the body which gave labor arbitration its credibility, has taken the historic step of passing a resolution condemning mandatory arbitration of statutory employment disputes. In 1997, the Academy stated that it, "opposes mandatory employment arbitration as a condition of employment when it requires waiver of direct access to either a judicial or administrative forum for the pursuit of statutory rights" (National Academy of Arbitrators Statement and Guidelines, 103 Daily Lab.Rep. (BNA) E–1 (May 29, 1997)). The Academy has expressed strong concern that mandatory arbitration often results in arbitral fora which do not provide elements of fundamental fairness to employees, and in which arbitrators are often not able or willing to enforce the claimed statutory rights. In fact, the Academy took the unprecedented step of filing a brief in the matter of *Duffield* v. *Robertson Stephens* (1998 U.S. App. LEXIS 9284 (9th Cir. 1998)) *asserting that the securities industry arbitration system and its procedures were not adequate to vindicate statutory rights.*

Recently, the *Society of Professionals in Dispute Resolution*, this country's other leading organization of professional neutrals, announced that it, too, opposed mandatory employment arbitration. In a January 1998 policy statement issued by its Board of Directors, the organization stated that it, "is in substantial agreement with the position taken by the National Academy of Arbitrators in opposition to agreements imposing arbitration of statutory rights as a condition of employment." Statement on Arbitration of Statutory Rights Imposed as a Condition of Employment, Approved by SPIDR Board of Directors January 24, 1998.

The requirement of voluntariness is also supported by the recommendations of the "Commission on the Future of Worker–Management Relations" (*the "Dunlop Commission"*), a blue-ribbon Presidential commission consisting of business and labor leaders, of Government officials, and of professional neutrals. In its December 1994 "Report and Recommendations," the Commission stated that, "Binding arbitration agreements should not be enforceable as a condition of employment." Commission on the Future of Worker–Management Relations: Report and Recommendations (December 1994), also expressing concern as to:

> The potential for abuse of ADR created by the imbalance of power between employer and employee, and the resulting unfairness to employees who, voluntarily or otherwise, submit their disputes to ADR. These concerns are obvious if the process is controlled unilaterally by employers, such as when employees are required to sign mandatory arbitration clauses as a condition of employment.

Indeed, the Dunlop Commission specifically singled out the securities industry in its report. The Commission stated that, "With respect to the securities industry, the Commission believes employees of securities firms should not be required as a condition of employment to arbitrate disputes arising under Federal or State employment laws."

The *National Labor Relations Board* has also challenged mandatory employment arbitration agreements as being illegal. In a 1996 report, the General Counsel of the NLRB concluded that mandatory, binding arbitration clauses, imposed as a condition of employment, violated the National Labor Relations Act. NLRB General Counsel Report, 1996 Daily Lab.Rep. 36 E–4, E–6,7 (Feb. 23, 1996).

The *General Accounting Office* has similarly determined that securities industry arbitrators were frequently not qualified or properly trained to decide discrimination cases. General Accounting Office, Report HEHS–94–17, *Employment Discrimination: How Registered Representatives Fare in Discrimination Disputes* (March 30, 1994).

Additionally, a number of the country's most prominent employment law professors and legal scholars have written law review articles in which they conclude that mandatory arbitration of statutory employment claims—imposed by employers as a condition of employment—is unlawful. Their reasons include the absence of a "voluntary" waiver of rights, a lack of constitutional due process in the arbitration sys-

tem, the basic conflict with the purposes and language of the civil rights laws, and the fact that the Federal Arbitration Act (FAA) does not apply to employment contracts. (R. Alleyne, *Statutory Discrimination Claims*, L. Bingham, *Employment Arbitration: The Repeat Player Effect—both cited above*; P. Carrington & P. Haagen, *Contract and Jurisdiction*, 1996 Sup.Ct.Rev. 331, 344–45 (1997); J. Grodin, *Arbitration of Employment Discrimination Claims: Doctrine and Policy In Wake of Gilmer*, 14 Hofstra Labor L.J. 1 (1996); S. Hoffman, *Mandatory Arbitration: Alternative Dispute Resolution or Coercive Dispute Suppression?*, 17 Berk.J.Empl. & Lab.L. 131 (1996); R. Reuben, *Public Justice: Toward a State Action Theory of Alternative Dispute Resolution*, 85 Calif.L.Rev. 3 (1997); D. Schwartz, *Enforcing Small Print to Protect Big Business*, J. Sternlight, *Panacea—both cited above*; J. Sternlight, *Rethinking the Constitutionality of the Supreme Court's Preference for Binding Arbitration: A Fresh Assessment of Jury Trial, Separation of Powers, and Due Process Concerns*, 72 Tulane L.R. 1, 7 (1977); S. Ware, *Employment Arbitration and Voluntary Consent*, 25 Hofstra L.Rev. 83 (1996).)

Arbitration is only viable, from either a legal or policy perspective, if it is the result of a truly voluntary agreement by the parties, who are aware of arbitration's strengths and limitations, and who have freely decided to use that process to settle a particular dispute. Without this element of a knowing, voluntary agreement, there is no legal or moral justification for enforcing an arbitration agreement.

As the National Academy of Arbitrators has stressed:

> The strength and justification for the enforcement of agreements to arbitrate, and for the limited judicial review of arbitration awards, rests on the foundation that agreements to arbitrate be voluntary ... unless a party has agreed to arbitrate, it will not be compelled to do so. Likewise, the immunity from judicial review of an arbitrator's alleged error of law or fact is premised on the voluntary choice of the parties to submit to an arbitrator's judgment. Without the voluntariness of the arbitration agreement, the public policy favorable to arbitration lacks a foundation. (Academy Amicus Brief in *Duffield*, *cited above*.)

Aside from general concerns about mandatory arbitration required as a condition of employment, the securities industry arbitration systems involve certain unique features distinguishing them from other arbitration systems administered by neutral entities.

For the past 10 years, I have been the Chair of NELA's Securities Industry Arbitration Committee. In that capacity, I have been extensively involved in monitoring the rules, procedures, and results of securities industry arbitrations. I have had numerous meetings and discussions on the topic of arbitration of employment disputes with executives in charge of the NASD and NYSE arbitration systems. I have had meetings and discussions with the staff of the Securities and Exchange Commission and I have frequently been asked by the SEC to comment on changes to arbitration rules proposed from time to time by the various self-regulatory organizations.

I am also co-counsel for the plaintiff in *Duffield* vs. *Robertson Stephens* (USDC/NDCal. Case No. C95–0109–EFL, filed 1/11/95), in which the Ninth Circuit unanimously held that the securities industry could not compel arbitration of discrimination claims through the use of the Form U–4. In the course of my representation of Ms. Duffield, I took the depositions of the heads of the arbitration programs at both the NASD and the NYSE and reviewed the arbitration awards, procedures, and all of the training materials used in the securities industry since 1990. The extensive record we developed in *Duffield* was submitted to and relied upon by Federal Judge Nancy Gertner in her landmark decision in *Rosenberg* v. *Merrill Lynch* (76 FEP 681 (D.Mass. 1998).)

In *Rosenberg*, after reviewing the actual structure, operations, and results of the securities arbitration system as the Supreme Court had invited in *Gilmer* v. *Interstate/Lane Johnson Corp.* (500 U.S. 20 (1991)), Judge Gertner determined that the Exchange's system was structurally biased against employees and fell outside "contemporary standards of arbitral impartiality" due to the industry's domination of the system. There is no question that Judge Gertner was correct in her analysis.

A review of the awards I have obtained demonstrates that even when plaintiffs prevail in securities industry arbitration, they are frequently not awarded attorneys' fees and costs as required by the civil rights laws. As already noted, forum fees have been as high as $42,600, $42,900, $49,000, and even $82,000. My review of these awards demonstrated that many cases have hearings stretching over months, with lengthy breaks between the sessions. This sort of scheduling makes it very difficult to present evidence coherently and for the arbitrators to keep the facts of a particular case in mind.

In building our record in *Duffield*, we also discovered that the NASD requires a special review by its staff of any award of attorneys' fees or punitive damages before such an award is issued, since in the NASD forum attorneys' fees or punitive damages are considered "extraordinary awards." This review is not provided for in any published rules of the exchange. The purported reason for the review is to assure that the award of these damages or fees has a legal basis. It is telling, however, that no such review is conducted for any other issue—including situations in which claims are dismissed in their entirety without any explanation at all.

Over the past several years, the NASD, at the industry's insistance, has discussed proposals to cap punitive damages in their arbitration forum, even though every judicial opinion on the subject confirms that this is not permissible. The first recommendation to that effect was made by their Lawyers Advisory Committee. A similar recommendation was then formally made by the Ruder Committee. After being soundly rejected by the Securities Industry Conference on Arbitration and even by the New York Stock Exchange itself, which deemed such an intrusion into substantive rights completely inappropriate for a theoretically neutral provider, the NASD Board of Governors went ahead and unilaterally approved a proposed rule change which has been submitted to the SEC. This rule change would cap punitive damages at $750,000 or two times special damages in customer cases, *whichever is less*, and the staff is considering a similar proposal for employment cases. These efforts have created a culture within the securities industry and its arbitration systems in which punitive damages are discouraged and, in fact, rarely awarded.

Most significantly, the securities industry fora stand alone in their refusal to endorse, use, or conform to the Due Process Protocol for the Arbitration of Statutory Disputes. This means there is significantly less discovery, reasoned awards are not provided, and complicated legal issues are resolved by unqualified, industry affiliated arbitrators who have no legal training and are told they are not required to follow the laws passed by Congress or the decisions of the U.S. Supreme Court.

Even when plaintiffs prevail on discrimination claims in the securities industry system, it is evident that Federal discrimination laws are not being properly enforced and Title VII claimants rarely receive their full statutory remedies. I am not aware of any discrimination case in which remedial relief has been ordered to improve hostile or discriminatory working environments.

A further impediment to securities industry employees is the fact that the existence of compulsory arbitration before securities industry arbitrators makes it more difficult for a plaintiff to obtain legal help in pursuing his or her claims due to the accurate perception of unfair results, fewer awards, and lower damages resulting from such arbitrations. Based on my own extensive experience and on my conversations with plaintiff attorneys from across the country, I believe that the requirement that a claim be arbitrated in the securities industry forum deters plaintiff counsel from accepting cases that they might otherwise take on. It is thus more difficult for securities industry employees to find attorneys willing to represent them in that forum. Those who are successful in obtaining counsel have to be advised that, even if they prevail, there is no assurance that they will recover forum fees or attorneys' fees, even if such recovery is provided by statute. I am aware of far too many cases where women were advised to abandon apparently valid and substantiated discrimination and harassement claims if the only forum available to them was the securities industry arbitration forum.

Finally, and of ultimate importance, is the fact that a justice system must not only be fair in fact, but must also be *perceived* to be fair, if it is to fulfill its purpose. That perception does not exist any longer with regard to the industry-controlled securities arbitration system. It is my experience that the securities industry arbitration forum is correctly perceived by both management and employee counsel as a more favorable forum for employers than the Federal courts. I have, in fact, participated in numerous presentations at the American Bar Association and other meetings where that exact statement was made. On more than one occasion I have had defense counsel in a securities industry case say to me, "What's this case worth, it's going to arbitration?"

It is now unfortunately well established that, due to the continued domination and overreaching by the industry in the operation of the system and the repeated promulgation of rule changes intended to deprive employees and customers of substantive statutory rights, the securities systems have lost the "perception of fairness," not only in the eyes of the ADR community, but of the public, the media, and, increasingly, the courts as well, as evidenced by the recent Second Circuit opinion in *Halligan* vs. *Kidder Peabody*, in which the court vacated an arbitration decision because the arbitrators had dismissed a compelling age discrimination case with no explanation whatsoever. Even the Second Circuit, which has been historically supportive of arbitration, is now telling the industry, "Enough is enough."

Conclusion

The bottom line is that, no matter what you think of arbitration, in 1998 there is no longer any justification for allowing the securities industry to control its own mandatory forum. This affront to law and basic principles of justice has gone on far too long, despite repeated demands by the EEOC, civil rights organizations, and the professional neutral community for reform. It is necessary that Congress perform its oversight function and protect the legal and constitutional rights of securities industry employees and the investing public.

When the Nation's leading academics and arbitrators summon the moral courage to publicly proclaim that the securities system is unfair and take the extraordinary step of opposing the securities arbitration system in court in order to preserve the credibility of "fair" arbitration, their message cannot be ignored. When *The Wall Street Journal*, *The New York Times*, *USA Today*, *"20–20,"* and other major national news sources feature prominent exposés on the abuses of mandatory arbitration, and the securities arbitration system in particular, then all fair-minded people must take note. For in the end, ensuring the integrity of the laws passed by Congress and assuring the public of the integrity of our Nation's markets must be your goal. The investing public will be right in asking: "If we can't trust the industry to operate a justice system without taking unfair advantage, how can we trust them with our money?"

Thank you for your consideration. I would be pleased to meet with members of your staff if you desire more information and documentation regarding the matters I have addressed.

PREPARED STATEMENT OF LINDA D. FIENBERG

EXECUTIVE VICE PRESIDENT, DISPUTE RESOLUTION AND CHIEF HEARING OFFICER
NASD REGULATION

JULY 31, 1998

Summary

NASD Regulation operates the largest dispute resolution forum in the United States for securities market participants. NASD Regulation handles 90 percent of all securities arbitration claims filed with the self-regulatory organizations (SRO's) annually. In 1997, 6,000 arbitration claims were filed with NASD Regulation, most of them involving investor disputes; only 20 percent (about 1,200 claims) involved intra-industry disputes (member–member or employee–member) and, of these, only 139—about 2.3 percent of all claims—alleged employment discrimination.

For many years, the SRO's have required registered persons (individuals working for a broker–dealer and engaged in the securities business) to arbitrate employment disputes. The registered persons sign a uniform registration Form U–4 used by all SRO's and State securities regulators, agreeing to arbitrate all disputes between the employee and a customer, firm, or other registered person.

Judicial Rulings. In 1991, the Supreme Court held in the *Gilmer* case that claims of age discrimination were subject to mandatory arbitration under SRO rules where the employee had signed a Form U–4. *Gilmer* has since been expanded by Federal courts in most circuits to cover other claims of discrimination under various Federal and State statutes.

Arbitration Policy Task Force. In September 1994, the NASD formed a task force to study NASD arbitration policy, chaired by former SEC Chairman David S. Ruder. The 1996 Task Force Report focused on investor arbitration, but found that employment arbitration offers the same advantages of speed and reduced costs, that statutory discrimination claims are usually interwoven with industry specific issues, and that arbitration is fully capable of protecting the public rights expressed in the anti-discrimination statutes. It recommended that employment disputes remain eligible for arbitration, but suggested that the NASD continue to monitor this evolving area.

Advisory Committee on Employment Discrimination Claims. NASD Regulation established an advisory committee in May 1997 to consider the issues relating to mandatory arbitration of employment discrimination claims. After considering the views presented to it during a 2-day meeting, and in light of the public perception that civil rights claims may present important legal issues better dealt with in a judicial setting, the NASD Board determined in August 1997 to remove the mandatory arbitration requirement from NASD's rules.

NASD Rule. The SEC approved the NASD's rule proposal to eliminate mandatory arbitration of statutory employment discrimination claims under NASD rules on June 22, 1998, effective January 1, 1999.

Working Group on Employment Discrimination Claims. NASD Regulation has convened a working group to consider procedural enhancements for the arbitration of discrimination claims. It is considering: panel composition for discrimination cases, a special roster of employment arbitrators, model arbitration disclosures for employees, the application of new investor arbitration rules to employment arbitration, and a requirement that firm arbitration agreements select a forum that meets certain procedural standards.

Introduction

I am Linda D. Fienberg, Executive Vice President for Dispute Resolution and Chief Hearing Officer of NASD Regulation. I thank the Committee for this opportunity to testify on the role of the NASD in the resolution of discrimination claims by employees of the securities industry.

The NASD, working with other regulators, with the industry, and employee representatives, has been active in addressing concerns about the mandatory arbitration of employment discrimination claims in the securities industry, and welcomes this opportunity to report to the Committee on its efforts.

The NASD

Let me first briefly outline the role of the NASD in the regulation and operation of our securities markets. Established under authority granted by the 1938 Maloney Act Amendments to the Securities Exchange Act of 1934, the NASD is the largest self-regulatory organization, or SRO, for the securities industry in the world. Although not funded by taxpayer dollars, the activities of all SRO's are subject to Federal oversight by the Securities and Exchange Commission. Every broker–dealer in the United States that conducts a securities business with the public is required by law to be a member of the NASD. The NASD's membership comprises more than 5,500 securities firms that operate in excess of 67,000 branch offices and employ more than half a million registered securities professionals.

The NASD is the parent company of The Nasdaq Stock Market, Inc. and NASD Regulation, Inc. These wholly-owned subsidiaries operate under delegated authority from the parent, which retains overall responsibility for ensuring that the organization's statutory and self-regulatory functions and obligations are fulfilled.

The NASD is governed by a 27-member Board of Governors, a majority of whom are not affiliated with the securities industry. Board members are selected from leaders of industry, academia, and the public. Among many other responsibilities, the Board, through a series of standing and select committees, monitors trends in the industry and promulgates rules, guidelines, and policies to protect investors and ensure market integrity.

NASD Regulation is responsible for the regulation of the securities activities of broker–dealers and for the surveillance, oversight, and enforcement of trading rules of The Nasdaq Stock Market. It also operates the largest dispute resolution forum in the United States for participants in the securities markets. NASD Regulation carries out all of its examination, disciplinary, and other regulatory responsibilities through its Washington, D.C. headquarters and 13 district offices located in major cities throughout the country. Through close cooperation with Federal and State authorities and other self-regulators, overlap and duplication are minimized, freeing governmental resources to focus on other areas of securities regulation.

NASD Regulation Dispute Resolution Program

NASD Regulation offers a dispute resolution program, governed by the NASD's *Code of Arbitration Procedure*, as a service to all investors, firms, and registered persons. NASD Regulation's program includes two nonjudicial methods of resolving disputes: arbitration and mediation.

Arbitration is a nonjudicial dispute resolution mechanism that determines liability and damages. In arbitration, an impartial person or panel hears all sides of the issues as presented by the parties, studies the evidence, and then decides how the matter should be resolved. Arbitration is final and binding, subject to review by a court only on a very limited basis.

Mediation is an informal, voluntary approach in which a mediator facilitates the negotiations between adverse parties, helping them to find their own mutually acceptable resolution.

Generally, nonjudicial dispute resolution methods (called alternative dispute resolution or ADR) such as arbitration and mediation are faster and less expensive than State or Federal court litigation. They also are less formal than court proceedings. NASD Regulation arbitrators and mediators are carefully selected from a broad cross-section of people; they are not employees of the NASD but, rather, serve as neutrals for an honorarium. In all NASD arbitration cases involving a customer and

in all employment discrimination cases, the arbitration panel hearing the claim must have a majority of public (that is, nonindustry) members on the panel.

NASD Regulation operates the largest dispute resolution forum in the United States for participants in the securities markets. NASD Regulation now handles approximately 90 percent of all securities arbitration claims filed with the SRO's annually. In 1997, 6,000 arbitration claims were filed with NASD Regulation, most of them involving investor disputes. Only about 20 percent (or 1,200) of the claims involved intra-industry disputes and, of those, only 139—less than 3 percent of our total claims—alleged employment discrimination.

Securities Industry Employment Arbitration

Now, I would like to describe briefly the background of employment arbitration in the securities industry. For many years, the securities industry SRO's, such as the stock exchanges and the NASD, have required registered representatives and principals to arbitrate employment disputes. This requirement is imposed when registered persons (individuals working for a broker–dealer and engaged in the securities business) sign a uniform registration form known as the Form U–4; this regulatory form is used by all SRO's and State securities regulators. Administrative and clerical employees who work for a broker–dealer are not required to register and thus do not sign a Form U–4. By signing the Form U–4, each registered person agrees to arbitrate, according to the rules of the organizations with which the employee is to be registered, all disputes that may arise between the employee and a customer, member firm, or other registered person.

Judicial Rulings

In 1991, the Supreme Court held in the *Gilmer* case[1] that claims of age discrimination were subject to mandatory arbitration under the New York Stock Exchange's (NYSE) arbitration rules where the employee had signed a Form U–4.

Soon after the *Gilmer* decision was announced, a court in California noted some differences between the arbitration rule language of the NYSE and the NASD. It determined that the NASD's rule, which required arbitration of disputes "arising out of or in connection with the business of any member," was meant to encompass only disputes over business transactions and was not specific enough to require registered persons to arbitrate employment disputes.[2]

In the wake of the California case, the NASD added to its *Code of Arbitration Procedure* specific language mirroring the NYSE language and clarified that employment disputes were meant to be covered by the Form U–4 arbitration agreement. The new language covered all disputes "arising out of the employment or termination of employment of associated persons." In its rule filing with the Securities and Exchange Commission, the NASD described the types of employment disputes that might be included in the requirement, such as those arising under Title VII of the Civil Rights Act of 1964, the Age Discrimination in Employment Act, and other similar equal employment opportunity statutes. The SEC approved the rule change as being consistent with the Securities Exchange Act of 1934, and the rule has been in effect since October 1, 1993.

The holding in the Supreme Court's 1991 *Gilmer* case has since been applied to cases arising under NASD's rules and has been expanded by Federal courts in most circuits in securities and nonsecurities cases to encompass claims of discrimination under various Federal and State statutes.[3]

However, the Ninth Circuit recently held in its May 8 *Duffield* decision[4] that, following the United States Civil Rights Act of 1991, employers may not, as a condition of employment, compel individuals to waive their right to a judicial forum in cases alleging employment discrimination. The Ninth Circuit is the only U.S. Court of Appeals to reach this conclusion. A month after the *Duffield* decision was issued, the Third Circuit in its *Seus* decision disagreed with the Ninth Circuit's interpretation

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

[2] *Higgins* v. *Superior Court of Los Angeles County*, No. B057028 (Cal. App. Oct. 8, 1991), review denied and decision ordered not officially published, 1 Cal. Rptr. 2d 57 (1992).

[3] *See, e.g., Cole* v. *Burns International Security Services*, 105 F.3d 1465 (D.C. Cir. 1997); *Seus* v. *John Nuveen & Co., Inc.*, 1998 U.S. App. LEXIS 11907, 1998 WL 294020 (3d. Cir. June 8, 1998); *Austin* v. Owens-Brockway Glass Container, Inc., 78 F.3d 875 (4th Cir. 1996); *Alford* v. *Dean Witter Reynolds, Inc.*, 939 F.2d 229 (5th Cir. 1991); *Willis* v. *Dean Witter Reynolds, Inc.*, 948 F.2d 305 (6th Cir. 1991); *Metz* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 39 F.3d 1482 (10th Cir. 1994); *Bender* v. *A.G. Edwards & Sons, Inc.*, 971 F.2d 698 (11th Cir. 1992).

[4] *Duffield* v. *Robertson Stephens & Co.*, No. 97–15698, 1998 U.S. App. LEXIS 9284 (9th Cir. May 8, 1998).

of the 1991 amendments and sided with the majority of circuits in holding that the Form U–4 arbitration agreement is enforceable as to Title VII claims.[5]

Arbitration Policy Task Force

In September 1994, the NASD formed the Arbitration Policy Task Force to study NASD arbitration policy generally and to suggest reforms. The Task Force, chaired by former SEC Chairman David S. Ruder, delivered its report to the NASD Board of Governors in January 1996.[6] Although the Task Force focused on investor arbitration, it found that employment arbitration offers the advantages of speed and cost that are associated with customer arbitration, and that statutory discrimination claims are usually interwoven with industry specific issues. The Task Force also believed that arbitration's equitable approach to dispute resolution is fully capable of protecting the important public rights expressed in the antidiscrimination statutes. The Task Force report recommended that employment-related disputes, including statutory discrimination claims, remain eligible for arbitration with a number of enhancements to the arbitration process, many of which were recommended elsewhere in the report.

While the number of employment discrimination claims filed with the NASD has grown over the past 5 years, it still represents a very small fraction of overall claims:

NASD Employment Discrimination Claims 1993–97					
	1993	1994	1995	1996	1997
Employment discrimination claims	40	48	65	109	139
Percent of total NASD arbitration claims	.7%	.9%	1.1%	1.9%	2.3%

Nevertheless, there are many groups and individuals who believe that statutory discrimination claims should not be subject to mandatory predispute arbitration agreements.

Advisory Committee on Employment Discrimination Claims

Responding to continuing interest in the issue of employment arbitration by the news media, the Equal Employment Opportunity Commission, employee organizations, and the new NASD and NASD Regulation leadership, we assembled a six-member Advisory Committee on Employment Discrimination Claims in May 1997. The Advisory Committee was established to assist NASD Regulation in considering suggested enhancements to the employment arbitration process. It was made up of two members appointed from the NASD Regulation Board (one an industry member representing a member firm and one a public member who was a former State securities commissioner) and four other members of the public with distinguished backgrounds in business or academia.

The Advisory Committee held a 2-day meeting in Washington and heard from representatives of civil rights organizations, the Equal Employment Opportunity Commission, general counsels of member firms, lawyers who represent employees, employee organizations, lawyers who represent firms, and arbitration experts. The Committee then met with NASD's senior management to discuss the major issues.

After considering all of the views presented, and in light of the public perception that civil rights claims may present important legal issues better dealt with in a judicial setting, the NASD and NASD Regulation Boards made the determination in August 1997 to remove the mandatory arbitration requirement from NASD's rules. In particular, the Boards approved the following proposals to:

- Amend NASD rules to remove from the mandatory arbitration requirement all employment discrimination and sexual harassment claims under Federal, State, or local statutes.
- Keep all other types of employment disputes in arbitration.
- Require that any firm arbitration agreements select an arbitration forum meeting certain procedural standards to be recommended by a newly formed Working Group, subject to approval by the NASD Board and the SEC.
- Provide for better disclosure of rights and arbitration features to all registered persons.

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[5] *Seus v. John Nuveen & Co., Inc.*, 1998 U.S. App. LEXIS 11907 (June 8, 1998).

[6] I served as a member of the Task Force and as its reporter. In that capacity, I was the principal author of the report.

- Work with other securities regulators (SRO's, the SEC, and the North American Securities Administrators Association) so that Form U–4:
  - Informs applicants they must arbitrate all disputes with customers and all nondiscrimination employment disputes, and
  - Compares the features of arbitration with court proceedings.

NASD Rule

The rule proposal to eliminate mandatory employment discrimination arbitration under NASD rules was submitted to the SEC on October 17, 1997, and published in the *Federal Register* on December 17, 1997. The rule proposal was approved by the SEC on June 22, 1998.

The NASD originally requested that the rule become effective 1 year from SEC approval to allow firms and employees to prepare for the rule's implementation. However, in light of comments received in response to the SEC's publication of the rule proposal, and in consultation with the SEC staff, the NASD amended its proposal in April to set the effectiveness of the rule for January 1, 1999. The rule will apply to all claims filed on or after that date without regard to either the date of the alleged discrimination or the date the employee signed the Form U–4.

Working Group on Employment Discrimination Claims

NASD Regulation has convened a Working Group on Employment Discrimination Claims to consider procedural enhancements to the arbitration process. This 10-member group includes representatives from securities firms, lawyers who represent employees, neutrals (arbitrators and mediators), and the NYSE. In particular, the group has been considering various aspects of a due process protocol that several dispute resolution organizations have adopted.

This Working Group has met numerous times and will make general suggestions to the NASD staff, which will in turn present recommendations to the NASD Board this fall. The enhancements being considered by the Working Group include recommendations on:

- Panel composition for employment discrimination cases;
- Selection of arbitrators for a specialized employment roster;
- Model disclosures for employees about arbitration and the effect of signing arbitration agreements;
- Guidelines about how new investor arbitration rules apply to employment arbitration; and
- A possible requirement that any arbitration agreements used by firms select, as the arbitration forum, either an SRO or another forum that meets procedural standards adopted by the NASD Board.

Conclusion

In conclusion, NASD Regulation continues to support its dispute resolution program as an efficient and fair method to resolve employment discrimination disputes. We believe we have a responsibility to provide a forum for the resolution of disputes for employees who choose arbitration over court or who enter into private agreements with their employer to arbitrate those disputes. At the same time, we already have taken steps to remove from NASD rules the mandatory arbitration requirement for employment discrimination claims, and we are moving forward expeditiously to enhance further the arbitration forum in ways that should make it even more attractive to employees.

The NASD thanks the Committee for this opportunity to discuss the evolution of its dispute resolution program for employment discrimination cases and the issues surrounding it. I would be pleased to respond to any questions you may have.

PREPARED STATEMENT OF STUART J. KASWELL

SENIOR VICE PRESIDENT AND GENERAL COUNSEL, SECURITIES INDUSTRY ASSOCIATION

JULY 31, 1998

I. Introduction and Background

The Securities Industry Association (SIA)[1] appreciates the opportunity to testify on the role of arbitration in resolving civil rights disputes in the securities industry.

[1] The SIA brings together the shared interests of nearly 800 securities firms, employing more than 380,000 individuals to accomplish common goals. SIA members—including broker–dealers, investment banks, specialists, and mutual fund companies—are active in all markets and in all

We commend Chairman D'Amato and all the Members of the Committee for holding this hearing on this important issue.

In a debate marked by stark differences of opinion, there is one fact about which there can be no dispute—all forms of discrimination should be eradicated, not only in the securities industry, but in society as a whole. This is the very premise of our civil rights laws. SIA and its members wholeheartedly embrace this goal. However, we reject the unfounded leap taken by some that Congress should now force all disputes involving allegations of discrimination into court. As our testimony will establish, the court system is neither the best, nor the only proper, means by which workplace discrimination may be effectively redressed. The erroneously drawn conclusion that arbitrating employment discrimination disputes in the securities industry will somehow erode congressional efforts to eliminate discrimination is not supported by the data or by common sense.

The issue being examined at this hearing is identical to that which was broached by one court, when it stated:

> [T]here is no disagreement among the members of this Court about the general proposition that racial, gender, and all other forms of invidious discrimination, are ugly realities that cannot be countenanced and that should be redressable through the widest possible range of remedies (citation omitted). However, the issue before us is not whether discrimination is a social evil that should be eradicated with whatever tools we have. Rather, the issue is whether, under existing precedent, the important public policies underlying [the Civil Rights Laws] of the Federal Civil Rights Act may be deemed to override the "emphatic national policy favoring arbitration" [citations omitted], as reflected in the [Federal Arbitration Act].[2]

II. Statement of Position

The employees of SIA member firms frequently arbitrate all claims arising out of their employment or termination of employment, including claims arising under the Federal antidiscrimination laws. Until only recently, securities industry employees agreed to arbitrate their claims by virtue of registering with a self-regulatory organization (SRO) whose rules require arbitration through the execution of a Uniform Application for Securities Industry Registration (or Form U–4), or in some cases, by executing a private agreement to arbitrate with his or her firm. In June of this year, however, the SEC approved a rule change proposed by the National Association of Securities Dealers (NASD), which removed from the NASD's Code of Arbitration the requirement that employees must arbitrate statutory claims of employment discrimination. That rule becomes effective on January 1, 1999 such that, on and after that date, claims may be filed in court for past conduct if they are within the applicable statutes of limitations and meet other statutory requirements and no other predispute arbitration agreements apply. SEC Release No. 34–40109; File No. SR–NASD–97–77.

In proposing the rule change, the NASD reiterated its belief that its arbitration system is fair and provides many benefits to employees as well as to securities firms, and that the rule change should not in any way indicate a lack of confidence in the SRO arbitration system. SEC Release No. 34–40109; File No. SR–NASD–97–77, pp. 7, 12. Moreover, although many urged the SEC and the NASD to invalidate even *private* agreements to arbitrate statutory discrimination claims, the SEC declined to do so. Indeed, the NASD has expressly stated that "such [private] agreements would not be affected by this rule change." NASD Notice to Members 98–56, July 1998, p. 2.

Although a staunch supporter of arbitration, the SIA supported the change proposed by the SEC insofar as it purported only to remove the mandatory requirement from the NASD's rules. In its January 18, 1998 comment letter to the SEC, SIA stated that it supports "the rule in its current form and commends the [SEC] staff on its efforts to balance the competing concerns of arbitration's critics with those who believe in its efficiency, fairness, and propriety for resolving all manner of employment claims." SIA Comment Letter to Jonathan Katz, Secretary of the SEC, dated January 18, 1998, p. 1.

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phases of corporate and public finance. In the United States, SIA members collectively account for approximately 90 percent, or $100 billion, of securities firm's revenues. They manage the accounts of more than 50 million investors directly and tens of millions of investors indirectly through corporate, thrift, and pension plans, and account for $270 billion of revenues in the U.S. economy.

[2] *Fletcher v. Kidder, Peabody*, 81 N.Y. 2d 623, 636, 601 N.Y.S. 2d 686, 692 (1993) (arbitrability of racial and gender discrimination claims governed by presumption of arbitrability established by the FAA).

This hearing today therefore arises at a somewhat unique time. The SEC's adoption of the rule proposed by the NASD, which will become effective in just a few short months, evinces a sharp departure from the system by which virtually all claims in the securities industry have been arbitrated. In addition, and as will be discussed more fully below, the SRO's have been working hard, with both the industry and with those that represent employees, to assure that fairness in this system is maximized. To that end, changes have been made and further changes are now being studied and, where appropriate, will be made to improve the arbitration system even further.

In light of the fluidity of change in this area, it is premature to make any wholesale changes. It has been less than 2 months since the SEC approved the NASD's proposed rule change, and by its terms, the rule will not become effective for another six (6) months (January 1, 1999).

Although one of the securities industry's largest members has announced publicly that it does not intend to require its employees to arbitrate their employment discrimination claims by private agreement, the majority of the industry's firms have apparently not yet decided whether or not they will do so. Accordingly, many new opportunities will arise for firms and employees to address this issue. Until the industry and its employees have had sufficient opportunity to respond to this new and significant change, it would be premature for Congress to take further action at this juncture.[3]

These developments are occurring at a time when the current court system for resolution of employment claims is long, burdensome, and expensive—an unfortunate reality that benefits neither the employee nor employer. Courts simply cannot manage their current caseload, save any influx of cases that further change would engender. Moreover, and as discussed below, even *without* an increase in volume in caseload, however, the court system has not been shown to be a particularly hospitable environment for discrimination claims.

Arbitration's vocal detractors have unabashedly assumed—without any meaningful supportive data—that the judicial system is the best forum for resolving these disputes, and therefore, they argue, is the most effective way to further the goals of our civil rights laws. This argument is based in neither fact nor reality insofar as statistics and the reality of an overburdened and problematic court system demonstrate quite the contrary.

In this statement, SIA intends to:

(i) Review the statutory and judicial bases for arbitration of employment discrimination disputes;

(ii) Explore the safeguards and improvements instituted and being contemplated by the various fora that hear securities arbitration cases involving civil rights claims;

(iii) Address why maintenance of the current system of arbitration is vital to further the important policies established by Congress and implemented by the U.S. Supreme Court; and

(iv) Demonstrate that the arbitration process is superior and more equitable to employees than litigating such claims in court.

III. Long Endorsed by Congress and the Courts, Arbitration is a Fair and Efficient Means of Resolving Civil Rights Claims

A. *Congress Has Expressly Endorsed Arbitration of Employment Discrimination Claims*

Those who oppose arbitration as a forum for resolving civil rights or employment discrimination claims assert that arbitration of employment discrimination disputes runs contrary to congressional intent and deprives individuals of substantive statutory rights. To the contrary, Congress long ago endorsed the resolution of statutory claims by arbitration, which included employment discrimination claims. Congress enacted the Federal Arbitration Act (FAA)[4] in 1925 specifically to encourage the enforcement of arbitration agreements and to make agreements to arbitrate enforceable to the same extent as other contracts. As the U.S. Supreme Court and count-

[3] As this Committee is aware, bills have been introduced in each of the last two Congresses that would have barred mandatory arbitration of employment discrimination claims pursuant to private agreements. No action was taken on the bills. *See, e.g.*, H.R. 4981, 103d Cong., 2d Sess. (1994); S. 2405, 103d Cong., 2d Sess. (1994); S. 366, 104th Cong., 1st Sess. (1995).

[4] 9 U.S.C. § 1, *et seq.*

less courts have noted, the FAA thus constitutes a "congressional declaration of a liberal Federal policy favoring arbitration agreements."[5]

Arbitration's critics not only ignore Congress' longstanding endorsement of arbitration but also foster a view that is inconsistent with the national trend to resolve disputes through alternative means of dispute resolution.

More specifically, in 1991, Congress enacted the Civil Rights Act of 1991 (the "Act"),[6] which amended various civil rights laws, by adding a provision endorsing arbitration as a fair and effective means of resolving employment discrimination disputes. Section 118 of the Act provides as follows:

> Where appropriate and to the extent authorized by law, the use of alternative means of dispute resolution, including settlement negotiations, conciliation, facilitation, mediation, fact-finding, mini trials, and arbitration, is encouraged to resolve disputes arising under the Acts or provisions of Federal law amended by this title.[7]

Since the passage of the 1991 Civil Rights Act, many courts have recognized that Section 118 constitutes a clear congressional endorsement of arbitration, including arbitration of employment discrimination claims pursuant to predispute arbitration agreements.[8] More fundamentally, the Supreme Court noted in 1995 that Congress' purpose in enacting the FAA was "to overcome courts' refusal to enforce agreements to arbitrate."[9] As a Federal appellate court recently held, "the FAA not only reversed the judicial hostility to the enforcement of arbitration contracts, but also created a rule of contract construction favoring arbitration."[10]

B. *The Courts Have Approved of Arbitration as an Effective and Fair Means of Resolving Employment Discrimination Claims*

Critics also argue that an employee who agrees to arbitrate discrimination claims gives up important statutory rights. As the Supreme Court has expressly disavowed such rhetoric, so too should this Committee. The Supreme Court held, "[b]y agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial forum."[11]

In *Gilmer*,[12] the Court upheld the arbitration of an age discrimination claim pursuant to a Form U–4 agreement. After reiterating Congress' strong endorsement of arbitration agreements, and rejecting criticisms of the arbitration process, the Court stated that "[s]uch generalized attacks on arbitration 'res[t] on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complaints,' and as such, they are 'far out of step with our current strong endorsement of the Federal statutes favoring this method of resolving disputes.'"[13] Notably, the Court considered the arbitration procedures used by the self-regulatory organizations in detail and rejected criticisms of them.[14]

On cue from *Gilmer* and its endorsement of mandatory arbitration of discrimination claims,[15] Federal courts have widely upheld the use of mandatory arbitration

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[5] *Moses H. Cone Memorial Hospital* v. *Mercury Construction Corp.*, 460 U.S. 1, 24 (1983).

[6] Pub. L. No. 102–166, 105 Stat. 1045 (codified in 42 U.S.C. § 2000e, *et seq.* (1991)).

[7] *Id.* at § 118. Some critics of arbitration argue that Section 118 should not be construed as an endorsement of mandatory arbitration agreements. *See Duffield* v. *Robertson Stephens & Co.*, 1998 WL 230891 (9th Cir. 1998), *appeal pending*. We think the more compelling view is that which was expressed recently by the Third Circuit Court of Appeals in *Seus* v. *John Nuveen*, 1998 WL 294020, at *8 (3d Cir. June 8, 1998). Expressly disagreeing with the *Duffield* Court, the Third Circuit held that, "on its face, the text of § 118 evinces a clear congressional intent to encourage arbitration of Title VII and ADEA claims, not to preclude arbitration. ... Nor do we believe this straightforward declaration of the full Congress can be interpreted to mean that the FAA is impliedly repealed with respect to agreements to arbitrate Title VII claims which were executed as a condition of securing employment." *See also* cases cited *infra*, fn. 8.

[8] *See, e.g., Seus* v. *John Nuveen*, 1998 WL 294020, at *8; *Austin* v. *Owens Brockway Glass Container, Inc.*, 78 F.3d 875, 881 (4th Cir. 1996) (holding that the language of the 1991 Act "could not be any more clear in showing congressional favor toward arbitration" and that agreements to arbitrate both Title VII and Americans with Disabilities Act statutory claims were enforceable), *Maye* v. *Smith Barney Inc.*, 897 F. Supp. 100, 107 (S.D.N.Y. 1995), *request for leave to appeal denied*, 903 F. Supp. 570 (S.D.N.Y. 1995) (referring to "seemingly unambiguous congressional endorsement of arbitration in § 118").

[9] *Allied-Bruce Terminix Cos.* v. *Dobson*, 513 U.S. 265, 115 S. Ct. 834, 838 (1995).

[10] *Kuehner* v. *Dickinson & Co.*, 84 F.3d 319, 320 (9th Cir. 1996).

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

[12] *Id.* at 20.

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

[14] *Id.* at 30–32.

[15] *Id.* at 26–28.

for a wide range of Federal civil rights claims.[16] Thus, it bears repeating that substantive rights are not waived by virtue of mandatory arbitration: "By agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial forum. It trades the procedures and opportunity for review of the courtroom for the simplicity, informality, and expedition of arbitration."[17]

IV. Relegating Civil Rights Claims to the Already Overburdened Court System Will Not Further the Laudable Purposes of the Civil Rights Laws

It is counterintuitive to argue, on the one hand, that the goals of the civil rights laws are paramount while, on the other hand, blindly to insist that a system which is demonstrably slower and less fair, is the best means to further those goals. Yet this is precisely the illogical argument fostered by some who oppose arbitration. This being said, there is compelling evidence that the Federal courts are not the purveyors of blind justice that plaintiffs' lawyers and other critics of arbitration would have us believe. The court system is far from the flawless, time efficient, or impartial forum that opponents of arbitration claim it to be.

Indeed, the Federal Judiciary itself recently has acknowledged that, with respect to all manner of discrimination claims, there exists perceptible bias in the judicial treatment of parties, witnesses, and counsels throughout the Federal court system. Report of the Second Circuit Task Force on Gender, Racial, and Ethnic Fairness in the Courts, June 1997 (the "Second Circuit Study"). The Second Circuit Study found that judges often express open hostility to employment discrimination claims and their litigants. In the study, trial judges "expressed their belief that the proliferation of small cases involving individual claimants, including employment discrimination cases, clog the Federal courts and divert the attention of judges away from larger, more significant civil cases."[18] Similarly, trial judges "exhibited impatience" with employment discrimination claims to the point where one district court judge is reported to have unexpectedly awarded summary judgment to the defendants despite the fact that neither side requested such a ruling, nor had addressed any of the significant issues in the cases other than jurisdictional ones.[19] "These preliminary indications in the ... study raise a concern that, when, an employment discrimination case is properly before a Federal court, a judge's belief that the matter is too trivial for his or her attention may too easily translate into actual unfairness to a litigant as the case proceeds through the system."[20]

In this context of judicial hostility to discrimination claims, a noted Federal district court judge held, in dismissing a Title VII claim for racial discrimination:

> This is another example where the Nations antidiscrimination laws are being misused. Here, a U.S. district court is asked to involve itself in a minor internal employee assignment decision. ... It would be hoped that at some point Congress would review the law in this area and make the necessary adjustment to eliminate these meritless, lottery-type cases.[21]

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[16] *See, e.g., Seus* v. *John Nuveen*, 1998 WL 294020 (3d Cir. June 8, 1998) (Title VII); *Patterson* v. *Tenet Healthcare, Inc.*, 113 F.3d 832 (8th Cir. 1997) (Title VII); *Cole* v. *Burns International*, 105 F.3d 1465 (D.C. Cir. 1997) (Title VII); *Gelenia* v. *Bob Baker Toyota*, 915 F. Supp. 201 (S.D. Cal. 1996) (Americans with Disabilities Act); *Williams* v. *Katten Muchin & Zavis*, 837 F. Supp. 1430 (N.D. Ill. 1993) (Older Workers' Benefits Protection Act); *Byrd* v. *Shearson/ LehmanAmerican Express, Inc.*, 926 F.2d 116 (2d Cir.), *cert. denied*, 501 U.S. 1251 (1991) (ERISA); *Nghiem* v. *NEC Elec., Inc.*, 25 F.3d 1437 (9th Cir. 1994) (Title VII); *Saari* v. *Smith, Barney, Harris Upham & Co.*, 958 F.2d 877 (9th Cir.), *cert. denied*, 506 U.S. 986 (1992) (Employee Polygraph Protection Act); *McNulty* v. *Prudential-Bache Sec., Inc.*, 871 F. Supp. 567 (E.D.N.Y. 1994) (Protection of Jurors' Employment Act); *Great Western Mortgage Corp.* v. *Peacock*, 110 F.3d 222 (3d Cir.), *cert. denied*, 118 S. Ct. 299 (1997) (New Jersey Law Against Discrimination). *But see Prudential Ins. Co. of Am.* v. *Lai*, 42 F.3d 1299 (9th Cir. 1994), *cert. denied*, 516 U.S. 812 (1995); *Duffield* v. *Robertson Stephens*, 1998 WL 230891 (9th Cir. May 8, 1998), *appeal pending*; *Rosenberg* v. *Merrill Lynch*, 995 F. Supp. 190 (D. Mass. January 26, 1998), *appeal pending*.

[17] *Gilmer*, 500 U.S. at 26 (quoting *Mitsubishi Motors Corp.* v. *Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985). *See also Kuehner*, 84 F.3d at 316 (holding that NASD arbitration "does not affect [claimant's] substantive rights ...").

[18] As noted in the Second Circuit Study, from 1970 to 1989, the number of employment discrimination classes filed in Federal courts increased by a staggering 2,166 percent, as compared with the 125 percent increase in the overall civil caseload for that same time period. *Id.* at fn. 82.

[19] *Id.* at 90.

[20] *Id.*

[21] *King* v. *Georgetown University Hospital*, 1998 WL 341556 (D.D.C. June 16, 1998).

Thus, while employees and their lawyers seeking to avoid arbitration contend that arbitration is unfair simply because it is not litigation, there is credible evidence to suggest that the crushing discrimination caseload in Federal courts has caused judges to look askance at even meritorious discrimination claims, and that this attitude may result in unfairness in the eventual result.

Arbitration, by contrast, seeks to resolve disputes fairly, quickly, and efficiently, as recognized by the statistics set forth below as well as in a 1996 study by the Arbitration Policy Task Force to the Board of Governors of the NASD, which stated that "arbitration of employment related disputes offers advantages in terms of speed and cost . . . [and that] arbitration's essentially equitable approach to dispute resolution is fully capable of vindicating the important public rights expressed in anti-discrimination statutes."[22]

A. Arbitration is Swifter and Less Expensive Than Court Litigation

Employees alleging workplace discrimination, potentially out of work and lacking in funds, would most surely echo the truism that "justice delayed is justice denied." Claims brought in the overburdened court system typically are not resolved for several years. Even the staunchest of critics cannot genuinely contend that such delays serve the greater good of eradicating workplace discrimination as Congress intended with its passage of the various civil rights statutes.

The civil trial process for employment claims is long and burdensome. Even those employers who prevail after a jury trial sustain immense costs and disruption in doing so. Faced with the prospect of huge costs even if they win, many employers choose to settle meritless claims rather than fight them in court. Arbitration, by contrast, offers all parties a faster and more efficient means of resolving claims. We establish below, with reference to governmental and other unbiased third-party statistics, that:

(1) Employees prevail more frequently before arbitration panels than before juries;
(2) Discrimination claims brought in arbitration are resolved more quickly than court actions;
(3) In arbitration, the employees are virtually assured that their discrimination claims will be heard insofar as prehearing dismissal motions are virtually nonexistent. By contrast, in court, such motions are common and very often granted;
(4) If arbitration is not an available alternative, employees' claims would be bifurcated, the cost prohibitions of which may result in the abandonment of otherwise valid claims; and
(5) The more informal arbitration procedures favor employees, who generally have more limited resources than do their employers.

A comparison of the results of discrimination claims brought before the New York Stock Exchange (NYSE) and the National Association of Securities Dealers (NASD), with those brought in the U.S. District Court for the Southern District of New York (SDNY) demonstrates that the important goal of eradicating discrimination is well served by the arbitration process, which results in awards to claimants more often than the court process.[23] After identifying all claims in which any type of workplace discrimination was alleged (including discrimination based on age, race and color, sex, national origin, disability, and religion), the SIA staff examined all of the decisions rendered since February 24, 1992 in arbitrations administered by the NYSE (the "NYSE Study") and by the NASD (the "NASD Study"). SIA staff compared these results with the results of all SDNY discrimination claims that culminated in a trial verdict since February 24, 1992 (the "SDNY Study").[24]

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[22] January 1996 Report of the Arbitration Policy Task Force to the Board of Governors of the NASD (Ruder Report), at 119.

[23] The SDNY was selected because the largest number of employees in the securities industry are within the jurisdiction of that Court. Also, data necessary to analyze employment discrimination claims was available from the Clerk's office of the SDNY.

[24] The following methods were used to ensure that the list of employment discrimination decisions rendered by panels in the NYSE, NASD, and in the SDNY during the time period studied was complete. For the NYSE, the *Securities Arbitration Commentator* (SAC)—an independent publication—provided us with all employment discrimination decisions. To be as complete as possible, we then reviewed every discrimination decision from February 24, 1992 through December 31, 1996 on file in the NYSE library at 20 Broad Street in New York, New York. For decisions rendered from January 1, 1997 through May 31, 1998, we requested and received copies from the Director of Arbitration, Robert Clemente, at the NYSE. The NYSE issued a total of 65 employment discrimination decisions during the time period. With regard to NASD

Continued

Both studies examined cases completed through May 31, 1998. The results are as follows:

Forum	Length of Time From Inception To Disposition	Percent of Cases Where Employee Prevailed
NYSE	15.6 months	38.46%
NASD	17.8 months	32.57%
SDNY	27.5 months	22.12%

The NYSE Study shows that the average length of time between the filing of a statement of claim in a discrimination case and the rendering of an award after hearing is 15.6 months. Similarly, the NASD Study reveals that, on average, discrimination cases are resolved in that forum in 17.8 months.

Conversely, resolution of discrimination claims in the overburdened court system is appreciably slower, taking more than 2 years (27.5 months to be precise) to resolve. Such a calculation is in accord with the fact that, in the SDNY, civil cases generally (that is, those *not* limited to discrimination cases) proceed from inception to trial in 27 months.[25] When the time associated with first exhausting administrative remedies in the EEOC and then fighting an employer's appeals is considered, it is even clearer that arbitrations afford aggrieved individuals much quicker resolutions of their claims.[26] In SRO arbitrations, claimants are not required to exhaust their administrative remedies before filing a statement of claim, and appeals from adverse arbitration decisions are rare.

Nor can it be said that overcrowded court dockets and increasing case delays are soon to be a thing of the past. Court statisticians openly recognize that the delays in court are on the rise due to the increased volume of civil cases in general and employment cases in particular. The number of new civil cases filed in the Federal courts has quadrupled since 1960.[27] Employment discrimination cases commenced in the district courts have risen from 10,771 in 1992 to 23,796 in 1997, an increase of 121 percent.[28] This surge of new job discrimination claims has led a panel of Federal judges to propose that the EEOC be required to investigate cases much more thoroughly before allowing workers to bring lawsuits.[29]

A faster resolution of employment discrimination disputes not only has the obvious direct benefit of compensating an aggrieved employee as quickly as possible, but has several other tangible benefits as well. Many of the problems associated with delay, such as witnesses' inability to recall facts, difficulty of locating witnesses and documents, and the attendant increases in costs and illogical results are reduced by a more expedient disposition. Delays can also result in substantial disruption of the employer's business and of the employee's ability to earn a livelihood. These factors substantially increase the cost of litigating an employment discrimination claim in court, as compared to arbitration. Such a waste of resources, by both employers and

awards, SAC provided us with all employment discrimination decisions. As a check on the completeness of SAC's compilation, we requested that the NASD provide us with all awards in which discrimination was alleged, which they did. The NASD issued a total of 132 awards for the period February 24, 1992 through May 31, 1998. Finally, with respect to the SDNY aspect of the survey, we relied on the Clerk's office of the SDNY to provide us with a computer printout of employment discrimination cases which had been tried by a judge or jury through March 1997. That printout included the necessary data regarding time to judgment and disposition. For the period April 1, 1997 through May 31, 1998, we utilized PACER, a court-based computer system, to obtain a list of all cases that had proceeded to judgment whose civil cover sheet categorized the action as an employment discrimination matter. For each of the 113 cases on the list obtained through PACER that went to trial, we studied either the docket sheets and/or other relevant court documents to ascertain the necessary data.

[25] *1995 Federal Court Management Statistics*, Administrative Office of the United States Courts, Leonidas Ralph Mechan, Director, p. 48.

[26] Appeals of adverse jury decisions add an additional 11.3 months from the filing of a notice of appeal to final disposition. *1996 Judicial Business of the United States Courts*, Report of the Director Leonidas Ralph Mechan, p. 105.

[27] *Judges Proposing To Narrow Access To Federal Court*, NYT, 12/5/94, Section A, Page 1, Column 3.

[28] *1996 Judicial Business of the United States Courts*, Report of the Director Leonidas Ralph Mechan, p. 139; U.S. Government Statistics published at *www.uscourts.gov*, Table C–2A, as of July 22, 1998.

[29] *Judges Proposing To Narrow Access To Federal Court*, NYT, 12/5/94, Section A, Page 1, Column 3

employees, is to nobody's benefit and would be substantially reduced by continuing to permit less costly and more time efficient arbitrations to resolve discrimination claims.

B. *Employees Alleging Discrimination Fare Better in Arbitration*

The arguments against arbitration of employment discrimination disputes in the securities industry are grounded on the mistaken premise that the process yields unfair results to employees. This is not so.

Employees alleging job discrimination benefit substantially when their claims are heard in arbitration. Thus, employees alleging discrimination before the NYSE and NASD panels prevail far more frequently than do employees whose discrimination claims are heard by juries. As established in the chart, an employee who brings a discrimination claim in arbitration before a NYSE panel is almost twice as likely to prevail before a panel in that forum than would that same employee before a jury. These results put to rest the mistaken belief that employees cannot get a fair hearing before an SRO panel. Indeed, the fact that employees alleging discrimination prevailed in thirty-eight percent (38.46 percent) of the decisions rendered by NYSE panels and thirty-two percent (32.57 percent) of the NASD decisions, as compared with a twenty-two percent (22.12 percent) win rate in the SDNY leaves little doubt that critics' concerns about so-called industry-dominated arbitration proceedings are inaccurate, to say the least.

C. *Employees Enjoy Numerous Other Benefits in Arbitration*

In addition to these efficiency and fairness benefits, employees who utilize arbitration enjoy numerous other benefits than do their counterparts in court. In court proceedings, employers are frequently successful in having discrimination claims dismissed on a motion to dismiss or a motion for summary judgment. Indeed, according to statistics compiled by the U.S. Bureau of Justice Statistics, during fiscal year 1995, Federal district courts dismissed 10,904 discrimination cases such that only 1,021 discrimination cases actually went to trial.[30] In fiscal year 1996, only 6.3 percent of employment discrimination cases reached trial.[31] Similarly, a study of sex and age discrimination claims found that motions to dismiss were successful forty-six percent (46 percent) of the time and summary judgment motions were successful fifty-nine percent (59 percent) of the time.[32]

Corroborating this fact is an analysis of 3.7 million Federal district court cases done by the Administrative Office of the United States Courts, assembled by the Federal Judicial Center and disseminated by the Inter-University Consortium for Political and Social Research via the Internet. This data showed that of the 2,595 statutory employment discrimination cases terminated in 1994 that were not settled or dismissed on other grounds, almost 70 percent were decided on pretrial motions. Out of that 70 percent, employers prevailed in nearly 98 percent of those pretrial motions while plaintiffs succeeded in just over 2 percent.[33]

Such is surely not the case in arbitration where employees in all but the rarest cases will have the opportunity to present their case at a hearing. As arbitration practitioners will readily acknowledge, prehearing dismissal rulings are rare. The rules of the NYSE, for instance, do not even provide for motions for summary judgment or dismissal and, in actual practice, prehearing dismissals are virtually nonexistent. The implication of this fact is that claims which would otherwise have been dismissed in court on legal grounds are presented to arbitrators, allowing the claimants an opportunity which he or she may otherwise not have had—an opportunity to persuade the arbitrators that "fairness" dictates that relief should be granted, even where the strict legal elements may be lacking.

Moreover, since discrimination claims are often brought in conjunction with other employment claims, such as breach of contract, tort, and wage and hour claims, removing discrimination claims from arbitration would cause a bifurcation of disputes between employers and employees. The resulting bifurcation is wasteful to all parties, risks the anomaly of conflicting decisions arising out of the same facts, and is particularly onerous to the party which is less able to bear the burden of parallel proceedings—typically, the employee.

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[30] Letter dated April 15, 1997, from John Scalia, Statistician, Bureau of Justice Statistics.

[31] *1996 Judicial Business of the United States Courts*, Report of the Director Leonidas Ralph Mechan, p. 160.

[32] *Employment Discrimination Against Midlife and Older Women, Volume I: How Courts Treat Sex and Age Discrimination Cases*, a report by the Women's Legal Defense Fund for the American Association of Retired Persons, 1996, p. 28.

[33] Theodore Eisenberg & Kevin Clermont, Federal District Court Civil Cases (ascertained from Web site at address: *http://teddy.law.cornell.edu:8090/questata.htm*, visited as of August 19, 1997).

Another benefit of arbitration relates to the less stringent rules regarding the admissibility of documents at arbitration hearings. At the hearing, the strict rules of evidence used by courts do not apply. As the U.S. Supreme Court noted in *Gilmer*,[34] this is a distinct advantage for employees, as it allows them to put before the arbitrators all manner of "evidence" that would not be admissible in court. Similarly, the limited availability of hearsay objections and other technical objections and devices makes the process more "user-friendly" and therefore readily accessible to employees. In short, these reduced formalities of SRO arbitration favor the party with more limited resources—typically, the employee.

V. Criticisms of the Arbitration Process are Misplaced

As established above, there are many benefits of arbitration. Turning from the benefits of arbitration to the unfounded criticisms of the process itself, the following discussion endeavors to correct some of the more frequently espoused criticisms of arbitration.

Critics frequently claim that the arbitrators who hear employment discrimination cases are not well trained. This is not true. The SRO's that currently administer securities arbitration cases sponsor training programs on employment discrimination law for which they actively recruit participants. As the Ruder Report noted, in 1994 alone, the NASD conducted training sessions on employment arbitration that were attended by approximately 700 arbitrators.[35] As one example of the training that is given, both the NASD and NYSE have participated in a training program sponsored by the Association of the Bar of the City of New York, a neutral body made up of representatives of employers and employees. Lawyers representing both employers and employees conduct each training session. The result, in the words of an independent publication that reviewed one of the sessions of that program, was "commendably objective."[36] The NASD prepared professionally edited videotape of the Association of the Bar training program, which it uses in its training sessions throughout the country. Other training efforts continue as well, as discussed below.

The criticism of the supposed lack of training by arbitrators is also logically unsound. Since juries have no training in discrimination law, there is no reason to suppose that a judge's instructions to a jury concerning the law leave the jury any more informed than arbitrators; particularly when arbitrators—unlike juries—frequently have received specific training in this area.

Critics also argue that arbitration is unfair because arbitrator pools are not as diverse as jury pools. The SEC, in commenting on a draft of the GAO Report, dispelled this very notion, stating that "GAO focused its attention on some aspects of the general operation of the forums, particularly issues related to the composition of the arbitrator pool, and *again did not find problems that affected any particular cases*."[37] In that same comment, the SEC further noted that there was not "any indication of bias in the administration of the [discrimination] claims" that the GAO reviewed.

Moreover, criticisms that many of the arbitrators are older, white males and the implication that this demographic profile precludes them from rendering fair decisions in discrimination actions are—ironically—based on discriminatory and offensive stereotypes. Indeed, it is just such an unfounded presumption that led the Supreme Court to hold that gender and race based exclusions of potential jurors is an unconstitutional practice.[38] Moreover, the Supreme Court repeatedly has "decline[d] to indulge the presumption that the parties and arbitral body conducting a proceeding will be unable or unwilling to retain competent, conscientious, and impartial arbitrators."[39] In all events, such criticisms are misplaced in light of the commendable efforts by the NASD and NYSE to diversify their arbitrator pools and to increase the extent of training provided to their arbitrators—training which is certainly not available to jurors.[40] This criticism also ignores the practical reality that arbitration

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[34] 500 U.S. at 31.

[35] Ruder Report at p. 117.

[36] *Arbitration Training: Employment Law Seminar*, Sec. Arb. Commentator, June 1993, at 8.

[37] Letter from Robert L.D. Colby, Deputy Director, Securities and Exchange Commission, to Linda G. Morra, Director, Education and Employment Issues, U.S. General Accounting Office (Dec. 30, 1993) (Appendix XII to 1994 GAO Report) (emphasis added).

[38] *See, e.g., Batson* v. *Kentucky*, 476 U.S. 79 (1986) (potential jurors not subject to peremptory challenges on account of race based on the assumption that a potential juror of a particular race cannot impartially consider merits of case is invalid and unconstitutional); *Edmonson* v. *Leesville Concrete Co.*, 500 U.S. 614 (1991) ("*Batson*" rule extended to private civil cases such that the exercise of peremptory challenges to exclude potential jurors based on race deemed unconstitutional); *J.E.B.* v. *Alabama*, 511 U.S. 127 (1994) (gender-based exclusion from jury is unconstitutional).

[39] *Gilmer*, 500 U.S. at 30; *Mitsubishi Motor Corp.*, 473 U.S. at 634.

[40] *Arbitration Training: Employment Law Seminar*, Sec. Arb. Commentator, June 1993, at 8.

panels ordinarily include a lawyer and an experienced business person, both of whom typically have a reasonable understanding of what the antidiscrimination laws require in terms of conduct and behavior.

The "older white male" stereotype is also factually unfounded. In a survey that was done relative exclusively to gender discrimination claims, the SIA analyzed every NYSE arbitration decision from January 1992 through September 1997 where a woman claimed discrimination. In 86 percent of those cases, the arbitration panels included a female arbitrator, as shown on the following chart. The NYSE has made concerted efforts to expand arbitration panels to include female arbitrators and, judging by the numbers, these efforts have succeeded.

Date of Decision	Total	Number of Awards to Claimants	Percentage of Awards in Favor of Claimants	Percentage of Panels Including Female Arbitrators
1992–1997	22	12	54%	86%

This same analysis of NYSE arbitrations evidences a strong track record of success by women in that forum. During the past 5 years, women asserting discrimination claims in NYSE arbitrations received an award in 54 percent of the cases that went to a hearing. This success rate is especially significant considering that, as previously noted, unlike claims litigated in court, claims heard in arbitration are rarely dismissed on motions prior to a hearing.

It also simply is not true that industry employees dominate arbitration hearings, as some critics assert. NASD and NYSE rules require that two of the three arbitrators assigned to hear each employment case must come from *outside* the securities industry. The one arbitrator who is from the industry cannot be associated with the firm involved in the case, and, like all arbitrators, must abide by rules requiring him or her to disclose "any circumstances which might preclude such arbitrator from rendering an objective and impartial determination."[41] The fact that one impartial arbitrator is knowledgeable about how the securities industry works therefore serves to benefit all parties. Furthermore, each party has the unlimited right to challenge the selection of any arbitrator for cause, as well as the right to make one "peremptory" challenge, *i.e.*, to remove an arbitrator without having to offer a reason.

Critics also claim that the public nature of a court proceeding acts as a deterrent to discriminatory practices. This criticism is outdated in that arbitration awards are publicly available and are, in fact, often publicized. A finding of discrimination remains a deterrent to future discrimination, regardless of whether the proceeding itself is open to the public. Furthermore, the relatively private nature of the arbitration process may actually encourage employees to pursue their discrimination claims in arbitration rather than endure the public nature of a plenary trial.

The arbitration process also gives employees an extensive opportunity to collect evidence. Employees are given broad leeway to demand and receive all manner of pertinent documents and information from employers prior to the hearing, often without the sort of limitations to which they would be subject in court cases.

Also misplaced is the suggestion that court is preferable to arbitration for employees because some jury awards are larger than arbitration awards. Moreover, even when jury verdicts are aberrationally high, they are frequently reduced or nullified by the court or on appeal, as confirmed in a recent study performed by the *National Law Journal*. This study examined employment discrimination verdicts of $1 million or more which were rendered during 1996 and 1997, and found that damages were fully reversed in about 80 percent of the 35 cases that had gone through post-trial motions.[42] Notably, this same study reinforced the pervasive judicial hostility to employment cases, particularly by Federal judges, as discussed above. One of the reasons cited in the study for these frequent, and sometimes automatic, reductions or reversals is Title VII's $300,000 cap for punitive and emotional distress damages. In short, the suggestion that the interests of a small minority of employees who may win substantial jury verdicts should dominate over the interests of the vast majority

[41] *See, e.g.*, NYSE Arbitration Rules, Rule 610(a); NASD Code of Arbitration Procedure, § 10312(a).

[42] *Judges Slash Worker Awards*, National Law Journal, April 20, 1998, p. 1.

of employees, who benefit from having a quicker, fairer, and more efficient mechanism for resolving employment discrimination claims, should be rejected.[43]

VI. The Securities Industry Is Working to Foster a Workplace Environment That Promotes Tolerance and Respect for All its Employees, Thereby Promoting the Very Goals of the Civil Rights Laws

As noted, SIA and its members deplore gender discrimination and intolerance of all kinds. Although it is important to punish discriminatory behavior, SIA believes that it is at least as important for the securities industry to recruit, hire, promote, and retain qualified women and minority employees. To that end, the SIA itself has established a high-level Diversity Committee to focus members' attention on these issues. SIA is actively working with its membership to increase the ranks of women and minorities in the industry and to assure that all employees enjoy a working environment in which they can maximize their success and advancement. SIA last year produced and disseminated a video focusing on the importance of creating diversity within our industry and stressing the commitment of our firms to that value. The video highlights the positive attitudes of senior management in our industry about diversity, both in terms of women and minorities.

Most importantly, the securities firms themselves are keenly aware of the importance of full participation by women and minorities in their industry. To that end, firms have taken an energetic and proactive approach to developing programs and initiatives designed to recruit, train, develop, and retain women and minorities. The securities industry has been aggressively pursuing a proactive agenda to help foster positive development, support, and understanding of employment and diversity policies amongst its ranks of executives, managers, and staff. Those diversity efforts focus on all aspects of employment, including recruitment, hiring, development, retention, and promotion.

While it may be beyond the scope of this hearing, we believe it may be helpful to provide general information about the many types of initiatives and programs undertaken by its member firms. Of course, the specific programs and initiatives that have been undertaken vary greatly based on the differing needs and resources of the firms. Indeed, since the size and business focus of SIA's 800 members do vary to such an extreme degree—ranging from firms with 50,000 employees operating from 550 offices to firms with two employees—it is simply not possible to describe the programs in terms that are applicable to all members.

Recruitment. With an eye toward recruitment, securities firms have tailored and expanded traditional recruitment programs to attract more female and minority candidates. In the interest of diversity and, specifically, with respect to recruitment, some firms have created advertising campaigns targeted at female and minority candidates. Others publish career opportunity brochures that specifically target and encourage women and minorities to enter careers that in the past may have been considered inhospitable to women and minorities. Securities firms have increased their use of women-owned search firms that focus specifically on placing women in the industry and some firms hold special meetings on college and graduate school campuses for women students. Some have formed alliances with minority MBA associations at major business schools in an effort to become acquainted with their pools of qualified female and minority candidates. As part of some firms' recruiting efforts, securities firms have participated in community outreach programs, internships and internal programs designed to provide women and minorities with a head start in obtaining permanent employment positions in the securities industry.

Retention. With respect to retention efforts, that is, programs designed to assure that a firm's culture encourages the advancement of women and minorities once at a firm, managers are encouraged to develop all their employees to increase their skills and chances for success within the firm. At many firms, diversity programs are complemented by mentorship programs to assist new employees and junior professionals in their early career development.

Environment. Securities firms work very hard to encourage an environment that welcomes a diverse workforce. Programs designed to heighten the sensitivity and awareness of diversity-related issues in the workplace have become an important part of training at many firms. Securities firms were among the leaders in American industry in developing such diversity programs. These programs include mandatory diversity and other training seminars to increase sensitivity to gender and minority-

[43] While plaintiffs' lawyers may benefit from a system which dismisses many cases but which holds out the hope of million-dollar verdicts, plaintiffs themselves benefit more in a system which gives them a better chance at having their "day in court" and at obtaining a rational judgment in their favor.

related issues in the workplace. At many major firms, such diversity programs are provided to line and support staff as well.

Policies and Procedures. The strong written policies prohibiting discrimination that exist throughout the industry are also a testament to the industry's focus on diversity-related issues. In order to communicate a clear and strong message to employees and management that they will not condone a discriminatory work environment, most firms have policies specifically stating this value. The firms assure their employees that if discriminatory conduct is found to have occurred, prompt and appropriate remedial action will be taken. SIA's member firms urge employees who believe they have been discriminated against to come forward, make known their grievance, and take care to assure their employees that there will be no retaliatory action for lodging a complaint. Employees at many firms have a variety of paths they may follow to raise concerns and are free to choose whichever is most comfortable for them. For instance, an employee may have the option of speaking with their immediate supervisor, the next level of management, their human resources representative, or the legal department of the firm. The existence of established policies and procedures to air employment grievances is disseminated in new hire packages, by posting it in common work areas, and/or by publication in regular internal employee communications. At some member firms, this message is delivered directly by senior management.

Investigating Allegations. Our firms are committed to investigating all claims of gender discrimination or harassment and in many firms, written internal firm procedures require a prompt and careful investigation once a complaint is received. Investigations are customarily led by human resources professionals supported by attorneys who are trained in conducting such investigations. Once the investigation is completed and if wrongdoing is uncovered, the appropriate disciplinary action is taken. Some examples of appropriate action include counseling, reduction in compensation, demotion, and, of course, termination.

While the securities industry is committed to providing workplaces free of sexual harassment and discrimination, even the strongest of commitments cannot guarantee that there will never be any instance of discrimination. Our industry employs hundreds of thousands of men and women and there will invariably be isolated problems at a given firm or branch office. Despite the existence of individualized instances of misconduct, such misconduct is, unfortunately, not unique to our industry but is problematic in almost all industries, and even in Government. While we will never be able to guarantee that isolated instances will never occur, we *can* state unequivocally that these problems are not systemic or pervasive. Thus, the point is not that instances of sexual harassment and other forms of invidious discrimination unfortunately exist in all industries and in society generally, but that securities firms actively address the issue and, to this end, cultures, work environments, and procedures are progressing toward a sea change in the workforce in this country.

VII. Wholesale Changes to a System That Works Well are Unnecessary, Particularly Where Improvements Have Been Implemented and Further Changes are Being Examined

While arbitration provides an attractive and fair alternative to court litigation, the securities industry is on record as being ready to work with Congress, the SEC, the EEOC, and the SRO's to develop ways in which to improve the process. Rather than changing a system that has proven to be effective and fair, SIA has advocated that a concerted effort be made to improve certain aspects of the process. SIA letter, dated April 25, 1997, to Mary Schapiro, President, NASD Regulation. Virtually all of the changes endorsed by the industry have been or are being considered by the SRO's. These improvements include: (i) increasing the extent and quality of arbitrator training with respect to applicable employment law; (ii) mandatory and automatic prehearing exchange of relevant documents; (iii) increasing efforts to form a diverse pool of arbitrators from which panels are chosen to encourage demographic diversity of panels; and (iv) altering the method of arbitrator selection such as furnishing parties with an increased number of challenges or utilizing the list method of selection of arbitrators.

By way of background as to the changes that have been made and are being made to the arbitration process; in January 1996, the Ruder Report was issued. That report studied the NASD's securities arbitration process and recommended reforms. The eight-person task force, chaired by David S. Ruder, former Chairman of the SEC, concluded their investigation by issuing over 75 recommendations for changes and improvements to the NASD's dispute resolution forum. Since mid-1996, the NASD has been reviewing and implementing those recommendations. According to a report recently issued by NASD Regulation, "the process has involved exposing the central recommendations to the constituents who use the forum in an effort to test

the viability of the recommendations and to build a consensus for change." NASD Regulation Dispute Resolution: Status of Arbitration Policy Task Force Recommendations, p. 1, April 1998 (NASDR Status Report).

Among the areas covered in the NASDR Status Report, is arbitrator training. According to the report, NASD Regulation conducts over 200 arbitrator training programs annually in over 40 cities nationwide. NASD Regulation conducts training programs for new arbitrators and for more experienced arbitrators who want to chair panels. NASD Regulation involves local practitioners in the development and delivery of training seminars on special topics such as employment law, discovery, or damage calculations. In addition, NASD Regulation trains arbitrators to function as co-trainers with a comprehensive Train-The-Trainer course. To supplement the individual programs, NASD Regulation publishes *The Neutral Corner*, a newsletter for all arbitrators and mediators. *The Neutral Corner* provides updates on new rules and policies and expert guidance on the dispute resolution processes.

Another area stressed in the NASDR Status Report which may have an impact on the arbitration of civil rights claims is mediation. NASD Regulation has worked very hard to develop a voluntary, nonbinding mediation program. In this format, the parties control the dispute resolution process, including case scheduling, neutral selection, and the outcome of the case. Investors, brokerage firms, registered representatives, and attorneys are beginning to explore ways to use and benefit from the mediation alternative. According to the NASDR Status Report, volume in mediation has grown steadily since the start of NASD Regulation's program. Since the beginning of the mediation program in 1995, over 1,500 cases have closed, with a steady 80 percent settlement rate.

In sum, it would be both frustrating and ironic if Draconian change were imposed when the majority of the recommendations made by the GAO and by the Ruder Task Force have yet to be fully implemented by the SRO's, and at a time when those changes are supported by the securities industry. The industry has been working with the SRO's to craft change that will benefit the system and improve the perception that it is unfair while at the same time, maintaining the efficiency of the process. Until the modifications have been implemented and, perhaps more importantly, monitored in terms of their impact on public perception of the system, it is premature to abandon the process.

The suggested improvements will help make an excellent arbitration system even more effective. The changes proposed can only enhance Congress' efforts to combat employment discrimination and protect the Nation's employees.

VIII. Conclusion

In sum, maintaining the industry's ability to privately contract with their employees and maintaining arbitration as a viable forum for resolution of these disputes is essential to reduce the costs, in terms of both money and human resources, incident to court-based litigation, and to ensure the equitable resolution of discrimination claims in the securities industry. The arguments against permitting employees to arbitrate discrimination disputes ignore: (1) the confidence placed in the arbitration process by the Supreme Court; (2) the documented success of SRO arbitration panels in resolving discrimination claims fairly and efficiently; (3) the increasing inability of the Federal courts to resolve such claims fairly, effectively, and efficiently; and (4) the unwieldy bifurcation of claims that will result if plaintiffs are given the option of bringing employment discrimination claims in court.

Arbitration of discrimination disputes in the securities industry has been a success for all parties and should be permitted to continue since it provides an effective forum for vindicating statutory claims and does not diminish the employee's substantive legal rights.

We appreciate the opportunity to testify on this important issue and welcome any questions from the Committee.

PREPARED STATEMENT OF ELIZABETH TOLEDO

VICE PRESIDENT, NATIONAL ORGANIZATION FOR WOMEN

JULY 31, 1998

Introduction

Good morning, and thank you for the opportunity to submit testimony on behalf of the National Organization for Women (NOW), the largest group of feminist activists in the United States. Since NOW is dedicated to ending discrimination of all kinds, we have a keen interest in ending the mandatory arbitration of employment discrimination disputes in the securities industry.

Today, you will likely hear a lot of detailed discussion about the *merits vel non* of mandatory arbitration, what is required by justice versus what is currently allowed by law. I believe that the arguments about the flaws in the current securities industry system are well-known and, in any case, can be better presented by others. I want to concentrate on the direction and the consequences of the debate for the industry and the Nation.

Arbitration Overhaul is Long Overdue

Thanks to mandatory arbitration, the securities industry is still a field dominated by white men. Women and people of color are forced to work in offices where managers have little fear of—or respect for—civil rights laws because they know they are essentially immune. When employees sign the Form U–4, they sign away their rights. As a result, the securities industry is able to bypass the very system established to protect the most basic of rights: the civil courts. Without the deterrent effect of the courts, discrimination has been allowed to fester—on Wall Street and throughout the industry—denying women and people of color access to the most lucrative positions in the field.

After listening to the stories of women who have suffered great injustices in the securities industry, NOW's leaders and members have reached a clear conclusion: Mandatory arbitration effectively guts the civil rights laws and allows the securities industry to lag behind other professional fields in hiring, working conditions, and promotion of women and people of color.

The human cost of this unjust system has been high. The industry-sponsored system of mandatory arbitration has created a hostile work environment for women and people of color. The list of complaints is endless. One recent case in which NOW was involved serves as an all too typical example.

The "Boom Boom Room"—a fraternity house style retreat for male brokers only, housed in the basement of a Smith Barney branch office in Garden City, New York, complete with a toilet hanging from the ceiling and an oversized trash can used to serve Bloody Marys—was, perhaps, the most notorious abuse in that firm, but not the most egregious. We need only read the 94-page complaint in the class action suit against Smith Barney to get a snapshot of the living hell women were forced to endure. The complaints include pregnancy discrimination, dead-end career tracks for women, and, of course, sexual harassement.

Roberta Thomann was a senior sales assistant when she went on an 8-week maternity leave. Thomann reports that only days before her scheduled return to work, she was notified that she would be demoted. According to Thomann, male employees who took medical leaves of absence were not demoted.

Judith Mione, a 40-year veteran in the securities industry who has successfully completed the Series 7 (Registered Representative), Series 63 (Uniform State Securities), and Series 8 (Branch Office Manager) licensing examinations, complains that she was repeatedly denied the opportunity to advance into managerial positions at Smith Barney—even though men with less qualifications and experience were hired to fill such positions. Despite her repeated applications and interviews, Ms. Mione said she was forced to take a position as a sales assistant. During one interview, Ms. Mione reports she was told that the ideal candidate would be "some guy with brass balls"—clearly not Ms. Mione.

Lydia Klein, a Vice President in Smith Barney's main office in New York City, allegedly was subjected to sexual harassment. According to the complaint she filed, male employees in her office sent her a calzone in the shape of a penis with ricotta cheese spurting out of one end. On another occasion, she received chocolate candy in the shape of a penis. She also complained that a male supervisor used to look at her breasts and comment, "Ooh, I love them." A male trader also stared at her breasts and would ask, "How they hanging?" Ms. Klein stated that men in the office often referred to women using euphemisms for female genitalia too grotesque and too offensive to repeat.

All of the 23 named plaintiffs in the Smith Barney case chose the risky course of pursuing a costly class action suit over industry-sponsored mandatory arbitration. They chose litigation even though the odds of class certification were low, and despite the likelihood that their class would exclude lower-level staff who are predominantly women. Why? Perhaps it is because the majority of arbitrators are white men over the age of 60, many of whom have been employed in the management ranks of securities firms. Maybe they prefer litigation because arbitration is binding with no appeals process. Some of the women may seek justice in the civil courts because arbitration panel members are not required to be trained or experienced in employment discrimination law. Under industry rules, arbitrators are not even required to uphold the law.

Clearly, mandatory arbitration is bad for employees, and it can also cost corporations money. Since the only way women and people of color can have their day in court is to form a class and sue, companies—like Smith Barney—face expensive class action suits in Federal court. The plaintiffs in the Smith Barney case never would have initiated a class action if they could have had access to the courts. Ultimately, even billion-dollar Wall Street companies will benefit when arbitration is an option—not a mandate.

The National Association of Securities Dealers (NASD) and the U.S. Securities and Exchange Commission (SEC) have come to realize that mandatory arbitration is a bad business practice. Both have opted to remove the requirement that industry employees sign away their civil rights in exchange for a job. The New York Stock Exchange (NYSE) is expected to follow suit at its next Board meeting. While the change in industry requirements represents a tremendous step forward, it by no means signals an end to mandatory arbitration.

Congressional Action is Necessary

Despite the anticipated changes in the Form U–4, most women and people of color employed in the securities industry still will not have access to the courts. The NASD's and the SEC's rule changes will not make mandatory arbitration on Wall Street go away. Securities firms—like Smith Barney—have internal personnel policies that require the arbitration of employment discrimination complaints. While we applaud the action taken by the NASD and the SEC, it will prove to be little more than a hollow gesture to the women and people of color in the industry who still are locked out of court and deprived of the right to argue their cases in front of an impartial judge and a jury of peers.

Congress must take immediate action to insure that securities industry employees are entitled to the full benefits of the Nation's equal employment opportunity laws. It is in the best interest of the employees, of the firms, and of the Nation to pass legislation.

Your failure to act would send a dangerous signal to employers in the securities industry and others. Since 1991, when Congress for the first time gave women and people of color a right to trial by jury and damages in employment discrimination cases under Title VII of the 1964 Civil Rights Act, a growing number of employers are motivated to stay out of court. Increasingly, we see other employers looking with envy at the securities industry's system of mandatory arbitration. Numerous companies as different as JCPenneys and Hooters now are trying to impose this unfair system on their employees as they ask, not unreasonably, why it should apply only to the securities firms.

Conclusion

Senators, it is incumbent upon you to reaffirm your commitment to the civil rights laws of this country. It is imperative that you safeguard the rights of all employees. I urge you to right the wrongs suffered by so many women and people of color by ending mandatory arbitration—first in the securities industry—and ultimately in every industry throughout the country.

Thank you.

PREPARED STATEMENT OF ROBERT E. MEADE

SENIOR VICE PRESIDENT, AMERICAN ARBITRATION ASSOCIATION

JULY 21, 1998

Summary

Often cited as a more effective option than traditional litigation, ADR programs calling for the administrative services of the American Arbitration Association to resolve nonunion workplace disputes have been implemented by nearly 400 large corporations covering approximately 4 million employees worldwide. The number of companies adopting employment ADR plans is expected to grow exponentially in the coming years. The AAA also conducts training programs in conflict avoidance and dispute resolution techniques for human resource managers and supervisors for companies including Boeing, General Electric, and Merrill Lynch.

As of July 1998, Merrill Lynch now includes the AAA as an optional forum for its employees, making it the first Wall Street firm to give its employees the option of resolving disputes through an independent agency not affiliated with the securities industry.

The Association's experience and belief is that any ADR method used in the employment context is most effective when the parties knowingly and voluntarily agree on the process, and have confidence in the neutrality of the mediator or arbitrator and the procedures and institution under which their case is being administered.

The AAA's policy on employment ADR is guided by the state of existing law, as well as its obligation to act in an impartial manner. In following the law, and in the interest of providing an appropriate forum for the resolution of employment disputes, the Association administers dispute resolution programs which meet the due process standards as outlined in its *National Rules for the Resolution of Employment Disputes* and the *Due Process Protocol*, developed in cooperation with representatives from the American Bar Association, the American Civil Liberties Union, and others.

If the Association determines that a dispute resolution program on its face substantially and materially deviates from the minimum due process standards of the *National Rules for the Resolution of Employment Disputes* and the *Due Process Protocol*, the Association will decline to administer cases under that program.

Introduction

Good morning. My name is Robert Meade. I am a Senior Vice President of the American Arbitration Association. The leader in conflict management since 1926, the American Arbitration Association is a not-for-profit, public service organization dedicated to the resolution of disputes through the use of negotiation, mediation, arbitration, and other voluntary dispute settlement techniques. In 1997, more than 78,000 cases were administered by the Association in a full range of matters, including 141 securities cases and 1,345 nonunion employment disputes for companies in a wide range of industries. Through 37 offices nationwide, and cooperative agreements with arbitral institutions in 38 other nations, the AAA provides a forum for the hearing of disputes, rules, and procedures, and a roster of impartial experts to hear and resolve cases.

Often cited as a more effective option than traditional litigation, ADR programs calling for the administrative services of the American Arbitration Association to resolve nonunion workplace disputes have been implemented by nearly 400 large corporations covering approximately 4 million employees worldwide. The number of companies adopting employment ADR plans is expected to grow exponentially in the coming years.

Within the securities industry, brokerage house employees were historically required to resolve disputes through one of the self-regulatory organization (SRO) arbitration forums. This month, however, Merrill Lynch became the first Wall Street firm to give its employees the option of resolving disputes through an independent agency not affiliated with the securities industry, through the SRO's, or through court. In a departure from industry practice, Merrill Lynch has included the AAA as an optional forum for its employees. Their program should serve as a model for other Wall Street firms.

In addition, the AAA has commenced a conflict avoidance and dispute resolution training and education program for several hundred supervisors and human resource managers at Merrill Lynch. Conducted under the auspices of the American Arbitration Association's Center for Educational Outreach, the goal of the training is to educate executives, managers, and human resources staff in mediation and arbitration processes to enable them to better communicate their program to employees and better facilitate program implementation. In the past several months, the AAA has conducted similar training programs for The Boeing Company, General Electric, and United Parcel Services.

Since the 1991 U.S. Supreme Court ruling in *Gilmer* v. *Interstate/Johnson Lane*, the lower Federal courts have generally enforced employer-imposed ADR programs, as long as the programs are fair. In the *Gilmer* decision, the Supreme Court refused to invalidate *Gilmer's* agreement with the New York Stock Exchange that he would arbitrate disputes with his employer simply because he was obliged to sign it in order to work as a securities dealer whose trades were executed on the Exchange.

AAA's Policy on Employment ADR

The AAA's policy on employment ADR is guided by the state of existing law, as well as its obligation to act in an impartial manner. In following the law, and in the interest of providing an appropriate forum for the resolution of employment disputes, the Association administers dispute resolution programs which meet the due process standards as outlined in its *National Rules for the Resolution of Employment Disputes* and the nationally-recognized *Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship*. The *Due Process Protocol* was developed by a task force composed of individuals representing management, labor, employment, civil rights organizations, private administrative agencies, and Government, including the American Arbitration Association, American Bar Association; and American Civil Liberties Union in May 1995.

Notification

If an employer intends to utilize the dispute resolution services of the Association in an employment ADR plan, it shall, at least thirty (30) days prior to the planned effective date of the program:

(1) Notify the Association of its intention to do so; and
(2) Provide the Association with a copy of the employment dispute resolution plan for review. If an employer does not comply with this requirement, the Association reserves the right to decline its administrative services.

If the Association determines that a dispute resolution program on its face substantially and materially deviates from the minimum due process standards of the *National Rules for the Resolution of Employment Disputes* and the *Due Process Protocol*, the Association will decline to administer cases under that program. To date, the American Arbitration Association has refused to administer nearly a dozen employment programs when the companies, for example, tried to limit remedies or shorten the statute of limitations for filing a claim.

Designing a Fair and Equitable ADR Program

Descriptions of the full range of legally available ADR options and a checklist of considerations for employers are included in *Resolving Employment Disputes—A Practical Guide*, developed by the Association in order to assist companies and their legal counsel in the responsible development of ADR plans. For example, ADR plans shall:

- Give employees clear notice of their right of representation;
- Allow for the same remedies and relief that would have been available to the parties had the matter been heard in court;
- Provide time frames that are consistent with applicable statutes of limitation; and
- Provide adequate notice to employees prior to the plan implementation.

In addition:

- In-house dispute resolution procedures, such as open door policies, ombuds, peer review, and internal mediation are encouraged.
- An external mediation component to resolve disputes not settled by the internal dispute resolution process is recommended.
- Programs which use arbitration as a final step may employ:
  - Predispute, final and binding arbitration;
  - Predispute, nonbinding arbitration;
  - Postdispute, final and binding arbitration; or
  - Postdispute, nonbinding arbitration.

The Association's experience and belief is that any ADR method used in the employment context is most effective when the parties knowingly and voluntarily agree on the process, and have confidence in the neutrality of the mediator or arbitrator and the procedures and institution under which their case is being administered.

Panel of Experts

In addition to the development of the *National Rules for the Resolution of Employment Disputes* and the *Due Process Protocol*, the American Arbitration Association has put together a first-rate, national panel of 600 employment law experts—diverse in gender and ethnicity and highly qualified with more than 10–15 years experience to resolve these disputes. The arbitrators were all required to attend the AAA's uniform, consistent training programs. Anyone who selects arbitrators on our panel to resolve their dispute can have confidence in their fairness, their integrity, and their qualifications and experience.

To review and monitor ongoing developments in the use of arbitration and mediation to resolve employment disputes, the American Arbitration Association has a National Employment Advisory Council, borne out of the Employment ADR Conclave hosted by the AAA in 1995 in Washington, D.C.

Finally, the Association has led the way for the responsible development of ADR. In 1996, the AAA was named by the Massachusetts Commission Against Discrimination to administer its ADR system, and we have helped the Department of Labor and the Equal Employment Opportunity Commission in having a dialogue on the important emerging issues for employment ADR.

STATEMENT OF JUDITH C. APPELBAUM

SENIOR COUNSEL AND DIRECTOR OF LEGAL PROGRAMS
NATIONAL WOMEN'S LAW CENTER

JULY 31, 1998

On behalf of the National Women's Law Center, a nonprofit organization that has been working for over 25 years to advance and protect the legal rights of women, I appreciate the opportunity to express our views on mandatory arbitration of employment disputes in the securities industry. We have long supported efforts to end the practice of requiring that any employees, including those in the securities industry, sign away their civil rights by agreeing to submit all employment discrimination claims to mandatory arbitration.

Our Nation's civil rights statutes codify a commitment to fundamental principles of equal opportunity and fairness in the workplace, and provide both substantive and procedural protections for employees who experience discrimination on the job. Requiring that employees forfeit their civil rights as a condition of employment is inconsistent with this statutory framework and the national commitment it reflects.

Mandatory arbitration is unfair to individual claimants in employment discrimination cases in a number of ways. Employees forced to submit their discrimination claims to arbitration lack any guarantee that the substantive protections of Title VII and other civil rights statutes will be correctly and consistently applied; they forgo the procedural safeguards these laws afford, such as full discovery and application of the rules of evidence; they are less likely, on prevailing, to receive the full measure of their damages or attorneys' fees; they lose the opportunity for a full airing of their disputes; they are deprived of judicial review of the merits of their claims except in the most extreme cases of legal error; and they often pay forum fees many times greater than court filing costs—indeed, often in the thousands of dollars, and sometimes even when the claimant prevails. Especially in combination, these features of arbitration make it more difficult for claimants to redress their injuries.

In addition, mandatory arbitration undermines the broader public interest in deterring and preventing discrimination. One of the underlying goals of private employment discrimination suits is to vindicate the important national public policy against discriminatory employment practices. But when discrimination claims are resolved behind closed doors without the benefit of public scrutiny, and when there is no judicial oversight to guarantee consistent and correct application of the law, employers are not forewarned about the consequences of their actions and future violations are less likely to be deterred.

Supporters of mandatory arbitration argue that the arbitration of employment disputes is fair and impartial to all concerned. They also contend that arbitration offers a number of advantages to claimants because it *is* generally faster, cheaper, and less formal than litigation in court. If these assertions are true, however, then there is no reason to *compel* employees to agree to arbitration as a condition of their employment, because an employee with a discrimination complaint will have every incentive to voluntarily agree, after the dispute arises, to submit it to arbitration on mutually agreeable terms. A strong reason for industry representatives to insist on *mandatory* arbitration of employment disputes is that in reality the deck is stacked, as we believe it is, in the employer's favor.

We praise the decision of the National Association of Securities Dealers (NASD), recently approved by the Securities and Exchange Commission (SEC), to lift the NASD rule that required those registered with it to arbitrate all employment discrimination claims. The NASD's elimination of this requirement, which we had long advocated, is a significant step forward.

The NASD's move, however, does not fully address the problem. First, individual securities firms may still attempt to require their employees to submit to predispute arbitration agreements. These employees will be no better off than if the NASD rule were still in place. They will still be forced to forfeit the right to adjudication of their allegations in a court of law. Particularly in an industry that has been characterized by numerous accounts of egregious sexual harassment and other forms of discrimination against women, this is not acceptable. See, for example, "Wall Street Fails to Stem Rising Claims of Sex Harassment and Discrimination," *Wall Street Journal*, May 24, 1996.

Second, neither employment discrimination nor the practice of imposing mandatory arbitration of discrimination claims is limited to the securities industry. Numerous employers in a variety of sectors of the economy have attempted to require workers to consent to mandatory arbitration as a condition of employment. These workers, as much as those in the securities industry, have a right to the full and fair adjudication of their discrimination complaints in open court. And while some

recent judicial decisions have ruled that employers may not require workers, as a condition of employment, to waive their rights to bring future claims under Title VII of the Civil Rights Act of 1964 (see, *e.g.*, *Duffield* v. *Robertson Stephens & Company*, 1998 WL 227469 (9th Cir.)), this principle is not yet established either with respect to all of the civil rights laws nor in all of the circuits.

It is for these reasons that we strongly support S. 63, the Civil Rights Procedures Protection Act, introduced by Senator Feingold. This bill would ensure that an employee with an employment discrimination claim, in the securities industry or any other, would be able to assert her rights under our civil rights laws and take full advantage of the substantive and procedural protections that these laws provide. This measure would not prohibit claimants and employers from agreeing *voluntarily* to take a dispute to arbitration after the dispute arises. But it would expressly prohibit mandatory predispute arbitration agreements that bar the courthouse door to employees who have experienced sexual harassment or other forms of discrimination on the job. It is an important piece of legislation and we hope it will soon be enacted into law.

Thank you for providing us with the opportunity to express our views.

Dennis C. Vacco
Attorney General

STATE OF NEW YORK
OFFICE OF THE ATTORNEY GENERAL

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July 20, 1998

Senator Russell Feingold
United States Senate
SH-716 Hart Senate Office Building
Washington, D.C. 20510-4904

Re: The Civil Rights Procedures Protection Act of 1997 (S. 63)

Dear Senator Feingold:

The issue of mandatory arbitration of statutory employment discrimination claims was recently visited by the National Association of Securities Dealers, Inc. (NASD), which proposed a change to its rules that would eliminate the requirement that such claims be arbitrated. Last month, the NASD's proposed rule change was approved by the United States Securities & Exchange Commission (SEC). It is scheduled to take effect on January 1, 1999. The elimination of securities industry arbitration of certain disputes is a great victory for employees of that industry who have long been subjected to an arbitration process that many believe is unfair. At the first opportunity, I supported the NASD's proposed rule change by written comments to the SEC (a copy of these comments is attached).

I would like to record my support for your bill, the Civil Rights Procedures Protection Act of 1997, for many of the same reasons I advocated against the imposition of mandatory arbitration in the securities industry. There is no question of the immense importance of the right to equal employment opportunity regardless of race, color, religion, sex, national origin, age or disability. Indeed, there is an overwhelmingly strong public policy to protect victims of discrimination as evidenced by federal and state civil rights laws which have guaranteed the right to equal opportunity in the workplace for more than thirty years.[1] The bill would amend

[1] See, e.g., the Equal Pay Act of 1963, as amended, 29 U.S.C. §206(d), Title VII of the Civil Rights Act of 1964, 42 U.S.C. §2000e, et seq. and the Civil Rights Act of 1991, the Age Discrimination in Employment Act of 1967, as amended, 29 U.S.C. §621, et seq., the Americans with Disabilities Act of 1990, 42 U.S.C. §12101 et seq., and New York's Human Rights Law §296(1).

120 Broadway, New York, NY 10271-0332 • (212) 416-8050

numerous federal civil rights statutes -- Title VII of the Civil Rights Act, the Age Discrimination in Employment Act, the Rehabilitation Act, the Americans with Disabilities Act, the Equal Pay Act, and the Family and Medical Leave -- and the Federal Arbitration Act to prevent the arbitration of employment discrimination claims, unless agreements to arbitrate are voluntarily entered into after such claims arise. While the rationale for my support may be generally applicable to both your efforts and the NASD's rule change, importantly, the legislation you have proposed would have more far reaching consequences than the NASD's rule change. Indeed, your bill would prevent all employers, rather than just securities industry employers, from requiring employees to agree to arbitrate employment discrimination claims.

Many of the deficiencies that present themselves in arbitral forums affiliated with the securities industry are evidenced in other arbitral forums too, making mandatory arbitration of employment discrimination disputes unfair no matter what the forum. Commonly cited deficiencies of the arbitral process include the following:

- Discovery is typically more limited in arbitration than in court proceedings.
- Some remedies available in courts, such as punitive damages, are not available in arbitration.
- The right to a trial by jury is not available in arbitration.
- Arbitration proceedings are typically private in nature. Arbitral decisions are usually not required to be written and typically go unpublished. Moreover, arbitral decisions are subject to review only under limited circumstances. As a result: (1) arbitrators' decisions, as well employers and their practices, are not subject to public scrutiny or accountability; (2) the failure of arbitrators to correctly interpret and apply the law is not subject to correction; and (3) the development of our civil rights laws is severely hampered.

In addition to these deficiencies, the inherent inequality of bargaining power between individual employees and employers necessitates the proscription of mandatory arbitration of employment discrimination claims. This unequal bargaining power results in the arbitral process being unilaterally imposed on employees by employers as either conditions for hire or prerequisites to continuing employment. While I recognize that arbitration can be a fast, cost-effective way to resolve disputes and that, generally, a strong federal policy favoring arbitration

agreements exists, I strongly believe that it is unfair to demand the use of arbitration in the context of employment discrimination disputes. Of course, should employees and employers wish to resolve their claims through arbitration, they should be free to do so. However, because of the imbalance of power in employer-employee relationships, I support agreements to arbitrate only if they are voluntary and entered into after disputes have arisen. Notably, the Civil Rights Procedures Protection Act of 1997 would not prohibit employees and employers from entering into agreements to arbitrate disputes after disputes arise.

In light of the above, I strongly support the Civil Rights Procedures Protection Act of 1997 and commend you for your positive efforts to protect employees in their workplaces.

Should you or your staff wish to discuss this issue further, please feel free to contact me or my Civil Rights Bureau Chief, Chevon Fuller, at (212) 416-8250.

Sincerely,

DENNIS C. VACCO
ATTORNEY GENERAL

COMMENTS OF NEW YORK STATE ATTORNEY GENERAL DENNIS C. VACCO ON THE PROPOSED CHANGE TO RULE 10201 OF THE RULES OF THE NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

New York State Attorney General Dennis C. Vacco submits the following comments to the Securities and Exchange Commission ("SEC") on the proposed change to Rule 10201 of the Rules of the National Association of Securities Dealers, Inc. ("NASD"). Currently, the NASD requires that all registered brokers, as a condition of employment in the securities industry, agree to arbitrate all employment claims. The rule change, which the SEC published on December 17, 1997, would eliminate the NASD's requirement that statutory employment discrimination claims be arbitrated.

Attorney General Dennis Vacco, who supports the overwhelmingly strong public policy to protect victims of discrimination, strongly opposes mandatory arbitration of employment discrimination disputes, commends and supports the NASD's lead to eliminate it, and urges the SEC to approve the rule change.[1] He believes, however, that the proposed rule change would better serve the equal opportunity rights of employees in the workplace if it: (1) was expanded to cover employment related common law claims; (2) prohibited private pre-dispute agreements; (3) encouraged private post-dispute agreements that preserve statutory protections and remedies; and (4) became effective three (3) months after SEC approval. The Attorney General urges the NASD to revise the proposed rule change to reflect these suggestions as detailed below.

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[1] The strong public policy to protect victims of discrimination is evidenced by the federal and state civil rights laws which have been enforced in this nation's courts for more than thirty years. See, e.g., the Equal Pay Act of 1963, as amended, 29 U.S.C. §206(d), Title VII of the Civil Rights Act of 1964, 42 U.S.C. §2000e, et seq. and the Civil Rights Act of 1991, the Age Discrimination in Employment Act of 1967, as amended, 29 U.S.C. §621, et seq., the Americans with Disabilities Act of 1990, 42 U.S.C. §12101 et seq., and New York's Human Rights Law §296(1).

I. The Proposed Rule Eliminating Mandatory Arbitration Should Be Adopted

The Attorney General supports the NASD's proposal to eliminate mandatory arbitration, as the process is not well-adapted for claims of employment discrimination. Although arbitration can be an efficient way to resolve broker-customer disputes in the securities industry, employees and others have challenged its fairness in employment-related disputes. Indeed, they have raised countless arguments about its deficiencies, particularly with respect to sensitive claims such as those involving sexual harassment. Complaints concerning the arbitration process focus primarily on the lack of procedural protections and on limitations placed on discovery and on remedies.[2]

The Attorney General finds that the most disturbing deficiency of mandatory arbitration in the securities industry is that industry arbitrators lack the training and experience that are essential to interpreting and applying employment discrimination law. Ironically, interpretation of discrimination laws is necessary because they are so broad.[3] Statutory interpretation and application, however, are roles typically given to our courts. Indeed, courts have developed many important legal doctrines relating to employment discrimination through judicial interpretations. Appellate review has contributed greatly to the development of those doctrines. For example, in Meritor v. Savings Bank, F.B. v. Vinson et. al., 477 U.S. 57 (1986), the United States Supreme Court first defined sexual harassment as a form of sex discrimination. Moreover, when the United States Supreme Court

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[2] Harvard Law Review Association, Development in the Law of Employment Discrimination: Mandatory Arbitration of Statutory Employment Disputes, 109 Harv. L. Rev. 1670, 1679-1683 (May 1966).

[3] See Alexander v. Gardner-Denver Co., 415 U.S. 36, 57 (1974) ("The resolution of statutory or constitutional issues is a primary responsibility of the courts, and judicial construction has proved especially necessary with respect to Title VII, whose broad language frequently can be given meaning only by reference to public law concepts").

failed to recognize pregnancy discrimination as a form of sex discrimination, Congress enacted the Pregnancy Discrimination Act of 1978.[1] Industry arbitrators' lack of specialized knowledge and training seriously disadvantages employees forced to have their employment disputes heard by them.

The securities industry's support for mandatory arbitration is hardly surprising considering that employers in the industry typically fare well in arbitrating employment discrimination claims. Surveys show that employers enjoy a greater chance of success in arbitration than in court before a jury, and that the sizes of damage awards in arbitrations are smaller than in jury trials.[2] In 1994, the U.S. General Accounting Office (the "GAO") issued a report ("GAO Report") concerning the use of arbitration in the securities industry. The GAO's findings amply demonstrate how the system inevitably favors the industry. In its report, the GAO concluded, among other things, that 89% of New York-based arbitrators in the securities industry were white males with an average age of sixty (60). The report also showed that the industry did not routinely assess the arbitrators' expertise in the subject matter of the disputes when assigning them to panels.[3]

Other deficiencies in the mandatory arbitration process as it exists today include that: (1) it does not require that arbitrators follow employment discrimination laws; (2) it does not require that arbitrators state the reasons for their decisions in written opinions; (3) arbitrators do not usually follow the rules of evidence and often allow any type of proof as evidence; (4) discovery is more limited than in court proceedings; (5) victims

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[1] See, e.g., General Electric Co. v. Gilbert, 429 U.S. 125 (1978); Nashville Gas Co. v. Satty, 434 U.S. 136 (1977). See also, the Pregnancy Discrimination Act of 1978, 42 U.S.C. §2000e(k), contained in the Civil Rights Act of 1964.

[2] Stuart H. Bompey; Andrea H. Stempel, Four Years Later: A Look at Compulsory Arbitration of Employment Discrimination Claims After Gilmer v. Interstate/Johnson Lane Corp., 21 Employee Rel. L.J. 21, 43 (Sept. 1995).

[3] The GAO Report at 8 & 12

fear based treatment resulting from closed hearings; and (6) arbitration awards are generally final and binding.

Because of these shortcomings, the Attorney General supports the NASD's proposal to eliminate mandatory arbitration of employment discrimination claims in the securities industry, as it is an unfair forum for employees that seriously detracts from the substantive rights provided for them by the legislature in our discrimination laws.

II. NASD's Proposed Rule Should Be Revised to Reflect The Attorney General's Recommendations

A. The Proposed Rule Should Include Related Common Law Claims

The Attorney General believes that the NASD's proposed rule change, which applies only to claims alleging "employment discrimination or sexual harassment in violation of a statute," is too narrow. This office recommends that the SEC broaden the rule to include common law claims which relate to employment discrimination claims.

Naturally, related common law claims often join statutory claims of employment discrimination. These common law claims include wrongful termination and intentional infliction of emotional distress.[7] While the proposed rule change allows employees to bring statutory employment discrimination claims in court, it still requires them to arbitrate any related common law claims they may have against their employers. Splitting such claims into separate forums duplicates the fact finding process of claims which, by nature, inextricably intertwine. Moreover, the duplicity would prove extremely costly and time-consuming to employees, and would impose undue hardship on them. Consequently,

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[7] Other employment-related common law claims include defamation, negligent supervision, invasion of privacy, tortious interference with economic opportunity. This list, however, is not meant to be exhaustive.

the proposed rule change would compel employees to drop their common law claims, or to arbitrate their statutory employment discrimination claims.

The Attorney General, therefore, recommends that the proposed rule change also eliminates mandatory arbitration of common law claims which relate to statutory employment discrimination claims.

B. The Proposed Rule Should Prohibit Private Pre-Dispute Arbitration Agreements

The Attorney General supports the employee's choice to resolve employment claims through arbitration and to enter agreements reflecting that choice. Nevertheless, the Attorney General strongly recommends limiting private arbitration agreements to circumstances where the agreement is voluntary and entered into after a dispute has arisen ("post-dispute agreements"). The Attorney General doubts that pre-dispute agreements are truly voluntary, due to the unequal bargaining power between employers and employees. Should the proposed rule become effective without this modification, employers can easily maintain the status quo by imposing pre-dispute agreements on registered representatives as conditions for hire and as conditions to maintaining employment. The fact that many securities industry employers already impose such agreements on non-registered employees supports the likelihood that they will impose such agreements on registered employees.

Opposition to pre-dispute arbitration agreements is widespread. Those opposed include some members of Congress, the Equal Employment Opportunity Commission ("EEOC"), and the Commission on the Future of Worker-Management Relations ("Dunlop Commission").[1] Legislation was introduced earlier this year in both the House of Representatives and the Senate that would prohibit parties from entering into agreements to resolve employment discrimination claims, unless they voluntarily enter

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[1] The Dunlop Commission was appointed by the Secretary of Labor and the Secretary of Commerce to, among other things, research alternative means to resolve employment disputes. Id. at 14, quoting the Dunlop Report at 32.

such agreements after such claims arise." The EEOC is "on record in strong support of voluntary alternative dispute resolution programs that resolve employment discrimination disputes in a fair and credible manner, and are entered into after a dispute has arisen."[10] Additionally, in its December 1994 Report and Recommendations, the Dunlop Commission stressed that "[e]mployees required to accept binding arbitration of [employment discrimination disputes] would face what for many would be an inappropriate choice: give up your right to go to court, or give up your job."

C. The Proposed Rule Change Should Clarify that Voluntary, Post-Dispute Arbitration Agreements May Not Limit Statutory Rights

The Attorney General supports voluntary post-dispute agreements to arbitrate employment disputes only to the extent that such agreements preserve the substantive protections and remedies afforded by statutes, and he encouraged the NASD to amend their proposal to include such protections. In DeGaetano v. Smith Barney, Inc., 96 Civ. 1613 (S.D.N.Y., Nov. 5, 1997) (Cote, J.), a recent federal court decision involving a challenge by an employee to Smith Barney's arbitration policy, the court found Smith Barney's arbitration policy void as against public policy to the extent that it waived plaintiff's right to obtain attorney's fees as a prevailing Title VII plaintiff.[11] Judge Cote reasoned that "the fee shifting provision of Title VII is a critical component of Congress's comprehensive statutory scheme for uncovering, redressing, and deterring unlawful employment discrimination in the American workplace."[12] "Contractual clauses purporting to mandate arbitration of statutory claims as a condition of employment are enforceable only to the extent that the arbitration preserves the

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[9] H.R. 983 and S. 63, 105th Congress (1997).

[10] The EEOC's Policy Statement on Mandatory Binding Arbitration of Employment Discrimination Disputes as a Condition of Employment at 16.

[11] DeGaetano v. Smith Barney, Inc., at 5.

[12] Id. at 14.

substantive protections and remedies afforded by the statute."[13] Judge Cote declared.

D. The Proposed Rule Change Should Become Effective Three (3) Months After It Is Adopted

The Attorney General recommends that the NASD's proposed rule change become effective three months after approval by the SEC, as opposed to one year as suggested by NASD. The NASD contends that a one year period would "permit employees and firms to determine what agreements they might wish to reach with regard to dispute resolution." However, should individual firms decide to require private arbitration agreements as part of employment contracts, three months should provide them with sufficient time to implement the necessary policy changes. Moreover, because using post-dispute agreements, which can easily drafted on an "as needed" basis, is a viable option, the need for a one year delay in the rule's implementation is eliminated. Indeed, when an employment dispute arises, the parties involved may then weigh the pros and cons of arbitration. Furthermore, due to the recent, considerable public attention on mandatory arbitration in the securities industry, both firms and employees have had adequate notice to prepare for its potential and seemingly likely elimination.

The NASD also suggests that if they implement the proposed rule one year from the date of Commission approval, then the NASD will have time to make "enhancements" to the arbitration forum. Such promised improvements include increased diversity on their arbitration panels and specialized training of its arbitrators. The Attorney General strongly commends the NASD's commitment to improve the quality of its arbitration forum, however, this office sees no need to postpone giving employees the right to take their grievances to court to allow the NASD time to better its arbitration system.

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[13] Id. at 24.

III. CONCLUSION

New York State Attorney General Dennis C. Vacco urges the SEC to approve the proposed rule change to eliminate mandatory arbitration of employment discrimination claims in the securities industry, provided that the changes recommended above are incorporated in the rule change.

DENNIS C. VACCO
Attorney General of the
State of New York

December 17, 1997

U.S. EQUAL EMPLOYMENT OPPORTUNITY COMMISSION
Washington, D.C. 20507

March 20, 1997

Mary L. Schapiro
President
National Association of Securities Dealers
Regulation, Inc.
1735 K Street, N.W.
Washington, D.C. 20006

Re: Mandatory Arbitration of Statutory Employment Discrimination Claims

Dear Ms. Schapiro:

The U.S. Equal Employment Opportunity Commission strongly opposes the mandatory arbitration of employment discrimination claims. I have attached, for your information, a copy of EEOC's resolution setting forth this position. The EEOC is in the process of developing guidance in support of its resolution and I will ensure that you are provided with a copy of that guidance as soon as it is adopted.

To date, we have made EEOC's views known to NASD informally through conversations with Linda Fienberg and other members of your staff. We have appreciated their availability and responsiveness in discussing these important questions. However, some of the statements made in the March 11, 1997, letter to you from the Securities Industry Association (SIA), urging that NASD maintain the mandatory arbitration of employment discrimination disputes, are of sufficient concern to warrant a more formal response.

In particular, SIA's position appears to be based on two overlapping propositions which, in effect, serve as book-ends to its argument. According to the SIA, "[a]rbitration is in fact the least expensive, most efficient and fairest means of resolving employment disputes" and "the current court system for adjudicating discrimination claims allows for 'legalized blackmail.'" (SIA letter at 1 and at 9-10). There is certainly an important policy debate to be had on the question of mandatory arbitration of employment discrimination claims, and we are not unmindful of the developing case law. Nonetheless, these two statements are nothing short of breathtaking in their disregard of the profound importance that the judicial system has played -- and continues to play -- in the enforcement of our civil rights laws. They are similarly remarkable for their willingness to totally discount the very real limitations of arbitration processes.

Without belaboring the point, it is beyond dispute that Congress expressly intended the courts to play a central role in the development and enforcement of the employment discrimination statutes. The courts have well served this purpose in several principal ways. First, the judicial system has provided a fair and publicly accountable forum for the resolution of many thousands of disputes over the past thirty years. Second, in clarifying the responsibilities and obligations of the parties through the public process of litigation, they have provided invaluable assistance in preventing and deterring future discrimination. Moreover, the courts have proved instrumental in the development of the law. For example, the doctrine that sexual harassment violates Title VII developed as a result of case law.

As a direct result of the judicial enforcement of the laws, we have witnessed a dramatic change in the demographics of the American workplace. Unfortunately, of course, the struggle to eliminate discrimination is far from over. And the courts are continuing to play a vital role. Just consider the important gains made for minorities and women through the federal court litigation of recent cases such as Texaco and Publix, as well as the importance of pending litigation such as EEOC's case involving Mitsubishi.

Similarly, whatever one thinks of the value of arbitration — and the Commission is squarely on the record in support of voluntary ADR — it is beyond dispute that arbitration carries with it a number of significant limitations. While arbitration may sometimes be less expensive and more efficient than litigation, this is certainly not always the case. In addition, important fairness questions are raised regarding arbitrator impartiality and qualifications; lack of reasoned decisions and substantive appeals; limited discovery; limited recovery of remedies and attorney's fees, and the imposition of forum fees. The SIA does not serve itself well by ignoring these very real concerns.

While my intent is not to respond point by point to SIA's letter, there is one more matter that warrants attention. The SIA's suggestion that Congress has expressly endorsed mandatory employment arbitration systems is simply wrong. Nothing in the Civil Rights Act of 1991 endorses pre-dispute agreements requiring arbitration of employment discrimination disputes as a condition of employment. Section 118 is framed in general terms and only "encourages" the use of ADR "where appropriate and to the extent authorized by law." Indeed, the legislative history demonstrates that Congress' interest was focused on voluntary ADR. See Prudential Insurance Co. V. Lai, 42 F 3d 1299, 1305 (9th Cir. 1994)("Speaking of proposed section 118, Senator Dole explicitly declared that the arbitration provision of [the Civil Rights Act of 1991] encourages arbitration only 'where the parties knowingly and voluntarily elect to use these methods.'") Moreover, Congress specifically rejected an earlier version of the arbitration provision that would have encouraged the use of prospective mandatory arbitration. H.R. Rep. No. 102-40, 102nd Cong., 1st Sess., pt. 1, at 104 (1991), 1991 U.S.C.C.A.N. Leg. Hist. 549, 642. Furthermore, the Federal Arbitration Act, which was passed long before Title VII was even contemplated, cannot under any stretch of analysis be said to expressly support mandatory arbitration of employment discrimination disputes.

As NASD continues to consider the extremely important issues raised in connection with mandatory arbitration of employment discrimination disputes, I urge you to keep carefully in mind the role of the federal courts in the enforcement of the civil rights laws as well as the limitations of arbitration systems.

If I can be of any further assistance, please do not hesitate to call on me.

Sincerely,

Ellen J. Vargyas
Legal Counsel

Attachment

cc: Honorable Arthur Levitt
Chairman, Securities and
Exchange Commission

Linda Fienberg
Executive Vice President
NASD Regulation, Office of
Dispute Resolution

Stuart J. Kaswell
Senior Vice President
and General Counsel
Securities Industry Association

National Partnership
for Women & Families

July 24, 1998

The Honorable Russ Feingold
United States Senate
716 Hart Senate Office Building
Washington, D.C. 20510

Dear Senator Feingold:

As the Senate Banking Committee considers S. 63, the Civil Rights Procedures Protection Act, we write to urge that the Senate pass this important civil rights legislation. S. 63 would prevent employers from forcing workers to give up their right to go to court -- and accompanying legal protections -- when they have job discrimination claims.

In a disturbing trend, more and more employers require workers to agree -- as a condition of hiring or promotion -- that any and all future employment disputes will be settled through mandatory, binding arbitration. Such mandatory arbitration undermines fundamental principles established by the hard-fought civil rights battles of the last 30 years.

Mandatory arbitration allows defendants to escape one of the key legacies of the Civil Rights Act of 1964, which first provided job discrimination victims with the right to have their claims heard in court by judges sworn to apply and uphold the law. Mandatory arbitration further enables employers to bypass some of the most important protections of the Civil Rights Act of 1991, which provided for jury trials and fuller remedies for discrimination victims.

Mandatory arbitration seeks to replace our public system of justice in the courts with a private system. Yet the courts have played a critical role in vindicating the civil rights of bias victims -- including, for example, developing the legal standards against sexual harassment and publicly highlighting employers' responsibility to maintain a discrimination-free workplace. Of course, this work is not yet done, as courts continue to evaluate serious claims of discrimination in the Mitsubishi and Texaco cases, among others.

Equally disturbing, mandatory arbitration often allows employers to limit dramatically the remedies and procedural protections available to discrimination victims. For example, some mandatory arbitration programs limit or deny compensatory and punitive damages -- denying the very remedies that the Civil Rights Act of 1991 extended to victims of harassment and other forms of discrimination. Arbitrators also lack the authority to issue the injunctive relief that is routinely available in the courts to end discriminatory practices and prevent their recurrence. Moreover, the federal rules of evidence -- that can be so important in protecting against intrusive inquiries into harassment victims' private sexual histories -- do not apply in arbitration

1875 Connecticut Avenue, NW / Suite 710 / Washington, DC 20009 / 202.986.2600 / Fax 202.986.2539 / Web Site http://www.nationalpartnership.org

proceedings.

While we believe that alternative dispute resolution -- when fully voluntary and properly designed -- can in many cases helpfully resolve employment disputes, mandatory arbitration forces workers to abandon their access to the courts and accompanying legal safeguards. S.63 would prevent such unfairness and restore the protections of our civil rights laws. Please support the Civil Rights Procedures Protection Act.

Sincerely,

Judith L. Lichtman

Judith L. Lichtman
President

NAIP

The National Association of Investment Professionals

12684 Ermine Place Suite 201, St. Paul, MN 55124
Phone: (612) 322-6267
E-Mail: tokeefe@naip.com

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July 30, 1998

Senate Committee on Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Bldg
Washington, DC 20510-6075

Official Statement of The National Association of Investment Professionals (NAIP) on Mandatory Arbitration in the Securities Industry.

Dear Senators:

As the President of the National Association of Investment Professionals, I would like to thank the Banking Committee for conducting the hearing scheduled now for Friday, July 31, 1998, on mandatory arbitration in the securities industry, and the opportunity to respond on this issue. Our hope is that NAIP be invited to offer testimony as Congress conducts future hearings on this matter.

The National Association of Investment Professionals (NAIP) is a professional society which is dedicated to promoting the interest of the 550,000 registered representatives in this country with regulators and legislators. Registered Representatives "constitute approximately 32 percent of securities industry employees in the largest 50 securities firms in the United States", according to the General Accounting Office. Our mission is to enhance the image of registered employees and to help them become more competent in serving the investing public.

The discussion before this body involves the complex issue of ensuring a citizen's constitutional and statutory rights, and the judiciary's commitment to enforcing arbitration agreements. Our position is against pre-dispute mandatory arbitration in the securities industry, and think that employees should have a choice of forums when filing any type of employment claim.

Sincerely,

Thomas S. O'Keefe

President

STATEMENT OF THE ISSUES

1. Whether federal civil rights law and state statutory law, precludes enforcement of a pre-dispute arbitration agreement that purports to waive the judicial right of action provided to most citizens in this country.

2. Whether the mandatory arbitration of statutory claims related to employment are inconsistent with the intent of Congress and the understanding of the Supreme Court.

3 Whether a forum operated by the SRO's is adequate to vindicate the statutory rights of those involved, and whether other grounds exists for Congress to deny the enforceability of pre-dispute arbitration agreements given the fact that the NASD and NYSE forums suffer from an inert structural bias and that the SEC does not systematically check employment arbitration cases than have been heard through the NASD and NYSE forums.

ARGUMENTS

THE RESOLUTION OF STATUTORY ISSUES IS A PRIMARY RESPONSIBILITY OF THE COURTS.

The Supreme Court emphasized in Alexander v. Gardner-Denver Co., 415 U.S.36 57 (1974, "the resolution of statutory or constitutional issues is a primary responsibility of the courts.

One of the primary advantages that the Judicial process has over arbitration is the public nature of the hearing. This is achieved first through publishing decisions of the court. Judicial authority is then subject to public scrutiny and to a system-wide set of checks and balances designed to ensure uniform expression of and adherence to statutory principles. Arbitrators are not subject to this vital public scrutiny.

When courts fail to interpret or apply the statutory law in accordance with the public values underlying them, they are subject to correction by higher level courts and by Congress. Those wronged in the arbitration systems run by the NASD or NYSE have little chance of winning an appeal in a higher court because arbitrators are not mandated to submit a written decision.

The courts also play a critical role in preventing and deterring violations of law, as well as providing remedies for discrimination victims. By establishing precedent, the courts give valuable guidance to persons and entities covered by the laws regarding their rights and responsibilities, enhancing voluntary compliance with the laws. By awarding damages, back pay, and injunctive relief as a matter of public record, the courts not only compensate victims of defamation, etc., but also provide notice to the community, in a

very tangible way, of the costs of these infractions through publicity in the media which is also not present at arbitrated hearings.

By issuing public decisions and orders, the courts also provide notice of the identity of violators of the law and their conduct. Executives at securities firms, and the firms themselves are now rarely disciplined by the NASD because of the in-bred, club-like culture that exists between the SEC, NASD, and member firms of the NASD. It has been demonstrated through this country's history that the risks of negative publicity and a blemished business reputation can be powerful influences on behavior. This powerful force should be allowed to work in the securities industry as it does in any other.

On the other hand, the arbitral process allows – by design – for minimal, if any, public accountability of arbitrators or arbitral decision-making. Unlike his or her counterparts in the judiciary, the arbitrator answers only to the private parties to the dispute and not to the public at large. The Supreme Court explained it :

> *A proper conception of the arbitrator's function is basic. He is not a public tribunal imposed upon the parties by superior authority which the parties are obliged to accept. He has no general charter to administer justice for a community which transcends the parties. He is rather part of a system of self-government created by and confined the parties...*
>
> United Steelworkers of Am. V. Warrior and Gulf NAvigation Co. 363 U.S. 574, 581 (1960) (quoting from Shulman, Reason, Contract, and Law in Labor Relations, 68 Harv. L. Rev. 999, 1016 (1955)

As previously stated arbitrators do not have to provide a written opinion to support an arbitration decision. Furthermore, awards are not made public without the consent of the parties. Judicial review of arbitral decisions is limited to the narrowest of grounds. (See Federal Arbitrations Act) Higher courts then are unable to act to correct errors in statutory interpretation.

Pre-Dispute Binding Arbitration

The Dunlop Commission strongly recommended that binding arbitration agreements not be enforceable as a condition of employment:

> *The public rights embodied in state and federal employment law – such as freedom from discrimination in the workplace...– are an important part of the social and economic protections of the nation. Employees required to accept binding arbitration of such disputes would face what for many would be an inappropriate choice: give up your right to go to court, or give up your job.*
>
> *Dunlop Report at 32*

The Brock Commission (see supra n.13) agreed with the Dunlop opposition to mandatory arbitration of employment disputes and recommended that all employee agreements to arbitrate be voluntary and post-dispute. And finally, the National Academy of Arbitrators recently issued a statement opposing mandatory arbitration as a condition of employment "when it requires waiver of direct access to either a judicial or administrative forum for the pursuit of statutory rights" See National Academy of Arbitrators' Statement and Guidelines (adopted May 21, 1997)

MANDATORY ARBITRATION OF STATUTORY CLAIMS IS INCONSISTENT WITH THE INTENT OF CONGRESS AND THE UNDERSTANDING OF THE JUDICIARY.

The courts of this country are under the impression that forum fees are paid by the employer, not the employee (see Cole v. Burns at pg. 1468, Federal Reporter). Yet employees in the securities industry routinely pay forum fees of $20,000, $40,000, $60,000 or more to have their cases heard. In the Cole case the judges opine that the Supreme Court never would have approved of mandatory arbitration in *Gilmer* had they thought the employee would have had to pay for the right to be heard. Concerning this issue *Cole* states:

> *However, there is no reason to think that the Court would have approved a program of mandatory arbitration of statutory claims in Gilmer in the absence of employer agreement to pay arbitrators' fees. Because public law confers both substantive rights and a reasonable right of access to a neutral forum in which those rights can be vindicated, we find that employees cannot be required to pay for the services of a "judge" in order to pursue their statutory rights.*

NASD AND NYSE ARBITRATION FORUMS SUFFER FROM STRUCTURAL BIASES AND THE SEC DOES NOT MONITOR EMPLOYMENT CASES.

The public plays no role in the selection of arbitrators: indeed they are hired, trained and initially selected for panel membership by the NASD or NYSE – the broker/dealer membership association , (80% of all securities arbitrations are held in these fora).

So while the courts are charged with giving force to public values reflected in the law, the arbitrator proceeds from a far narrower perspective: resolution of the immediate dispute. The arbitrators "perspective" is another issue worth noting. In a 1994 report issued by the General Accounting Office :

> *NYSE and NASD do not systematically collect demographic data on arbitrators in their pools. We estimate that most of the NYSE New York arbitrators (about 89 percent of 726 at the end of 1992) are white men, averaging 60 years of age.*

I point this out to underscore the dependency these arbitrators may have on the income they receive as arbitrators in retirement from their former full-time positions. Many of these arbitrators depend on the income they receive as arbitrators to supplement their retirement income. Because they want to be picked as arbitrators repeatably, many of them are afraid of making large awards against the brokerage firms. As a result, arbitrators tend to reach decisions that are favorable to the industry, i.e., employees received only small or partial award in cases which they won. (See May 12, 1992 General Accounting Office report).

The employer accrues a valuable structural advantage because it is a "repeat player" Brokerage firms are a party to arbitration in all disputes with its employees in contrast to the "one-shot player" According to Lisa Bingham in her unpublished study "Employment Arbitration: The effect of repeat-player status, employee category and gender on arbitration outcomes" cannot be underestimated:

> *The employee is generally less able to make an informed selection of arbitrators than the employer, who can better keep track of an arbitrator's track record. In addition, results cannot but be influenced by the fact that the employer, and not the employee, is a potential source of future business for the arbitrator.*

Another important work on the analyses of mandatory arbitration is the Commission on the Future of Worker-Management Relations, which was appointed b the Secretary of Labor and the Secretary of Commerce to , in part, address alternative means to resolve workplace disputes. This Commission found that the recent employer experimentation with arbitration has produced a range of programs that include "mechanisms that appear to be of dubious merit for enforcing the public values embedded in our laws" Dunlop Report at 27. The GAO , surveying private employers' use of ADR mechanisms, found that existing employer arbitration systems vary greatly and that most "do not conform to standards recommended by the Dunlop Commission to ensure fairness. (See "Employment Discrimination; Most Private-Sector Employers Use Alternative Dispute Resolution" at 15, HEHS-95-150 (July 1995)

NASD and NYSE arbitrators are also reluctant to issue sanctions for NASD Arbitration Rules violations, and in ruling against the firms even in the most egregious of claims.

Lack of SEC Monitoring

Under the 1934 Act the SEC had the responsibility to monitor the SRO's. The SEC does not include employment disputes as part of it's inspection program however. The March 30, 1994 GAO Report address this as follows:

> *SEC's oversight of the securities industry's arbitration programs focuses on customer-firm disputes, as opposed to employee-employer disputes, such as discrimination disputes.*

Furthermore, the SEC does not require the SRO's to report this information. As a result, the SEC has no information to assess TRENDS in employment cases. The GAO believes that having the SRO's track this data would enable them to select discrimination cases for review. We believe the same could apply to all employment cases.

The GAO's recommendation included establishing a formal inspection cycle for conducting inspections so that the SRO's would be more inclined to respond expeditiously to SEC recommendations made during previous inspections.

CONCLUSION

Individual civil rights and the public interest are harmed by the unilateral imposition of mandated binding arbitration agreements, whether enforced by the NASD or through employment contracts. The intent of common law is to promote the common good of all the citizens of this country, not exempt a special few who think they are above its' regulations. Individuals in the securities industry should also not be deprived of vindicating their statutory rights in the courts if that is the forum which best addresses their individual employment claim. If the court system is not the best forum, then individuals should have the choice of a neutral third party forum to have their claim heard in like that run by the American Arbitration Association (AAA).

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