

1999

## A Model for Arbitration: Autonomy, Cooperation and Curtailment of State Power

Kenneth

Follow this and additional works at: <https://ir.lawnet.fordham.edu/ulj>



Part of the [Dispute Resolution and Arbitration Commons](#)

---

### Recommended Citation

Kenneth, *A Model for Arbitration: Autonomy, Cooperation and Curtailment of State Power*, 26 Fordham Urb. L.J. 167 (1999).  
Available at: <https://ir.lawnet.fordham.edu/ulj/vol26/iss2/1>

This Article is brought to you for free and open access by FLASH: The Fordham Law Archive of Scholarship and History. It has been accepted for inclusion in Fordham Urban Law Journal by an authorized editor of FLASH: The Fordham Law Archive of Scholarship and History. For more information, please contact [tmelnick@law.fordham.edu](mailto:tmelnick@law.fordham.edu).

---

# A Model for Arbitration: Autonomy, Cooperation and Curtailment of State Power

## **Cover Page Footnote**

Associate Professor of Legal and Ethical Studies, Fordham University, Graduate School of Business Administration. B.A., State University of New York at Binghamton; M.A., University of California at Long Beach; J.D., University of Toledo College of Law.

# A MODEL FOR ARBITRATION LAW: AUTONOMY, COOPERATION AND CURTAILMENT OF STATE POWER

*Kenneth R. Davis\**

## Introduction

When I was five or six, my friend Sammy and I got into a disagreement over who had tied the superior knot with his shoelaces. We asked our friend Harry to decide the issue. After inspecting our handiwork, he noted that my knot had more sweeping loops, but that Sammy's was more symmetrical — the judicious (and appropriate) outcome: a tie. Satisfied that justice had been done, the three of us trotted to the schoolyard to play stickball.

This was my first experience with arbitration. Sammy and I had submitted our dispute to a non-judicial decision maker for binding determination. Despite our disagreement, we had managed to agree on a method to resolve the dispute. We had cooperated in the face of controversy by exercising our rights to enter into an arbitration agreement. Rather than submitting to rules imposed by a higher authority (mom or dad), we had set our own ground rules to attain justice, and, win or lose, we were willing to respect the outcome.

Commentators praise arbitration for its economy.<sup>1</sup> Compared to cumbersome litigation, arbitration saves time and money.<sup>2</sup> Arbitration avoids the formalities that hobble litigation from service of the pleadings through determination of the final appeal. Litigation begins with the filing of a summons and complaint, which must satisfy formal procedural requirements.<sup>3</sup> Mired in interminable dis-

---

\* Associate Professor of Legal and Ethical Studies, Fordham University, Graduate School of Business Administration. B.A., State University of New York at Binghamton; M.A., University of California at Long Beach; J.D., University of Toledo College of Law.

1. See generally 1 GABRIEL M. WILNER, *DOMKE ON COMMERCIAL ARBITRATION* § 1:01, at 2 (rev. ed. 1984); PHILIP J. HOBLIN JR., *SECURITIES ARBITRATION: PROCEDURES STRATEGIES CASES* §§ 2-4 to 2-5 (2d ed. 1992); *COMMERCIAL ARBITRATION FOR THE 1990s* 41-53 (Richard J. Medalie ed. 1991).

2. See, e.g., Norman S. Poser, *Making Securities Arbitration Work*, 50 *SMU L. REV.* 277, 278 (1996) (arguing that the speed and cost-effectiveness of arbitration will diminish if the courts meddle in the arbitral process).

3. See, e.g., FED. R. CIV. P. 4 (filing of complaint); FED. R. CIV. P. 8 (general notice pleading standard); FED. R. CIV. P. 9 (heightened pleading standard for matters such as fraud and breach of fiduciary duty).

covery and contentious motion practice, lawsuits trudge along at a frustrating pace toward trial, and even when the trial has concluded, appeals may delay ultimate resolution for years.<sup>4</sup> The time consumed in a complex litigation may entail the expenditure of a war chest. On the other hand, arbitration dispenses with formal pleadings, massive discovery, aggressive motion practice, and endless appeals.<sup>5</sup> The process hurries to conclusion.

Although arbitration is undoubtedly more efficient than litigation, efficiency is only one advantage of arbitration. Arbitration serves the fundamental values of cooperation, individual autonomy, and curtailment of governmental power. As the "shoelace" anecdote suggests, arbitration uniquely promotes two seemingly incompatible values: individual autonomy and cooperation.<sup>6</sup> While embroiled in a dispute, two parties agree freely on how to attain justice.<sup>7</sup> At a time when they are least likely to cooperate, their mutual desire for fairness, efficiency, and self-determination prompts them to devise jointly a course to resolve their controversy.<sup>8</sup> They provide the source of the power that will bind them:

---

4. See, e.g., Kenneth R. Davis, *When Ignorance of the Law Is No Excuse: Judicial Review of Arbitration Awards*, 45 *BUFF. L. REV.* 49, 53-55 (1997) [hereinafter *Judicial Review*] (describing the dilatory procedures that pervade litigation); Jethro K. Lieberman & James F. Henry, *Lessons from the Alternative Dispute Resolution Movement*, 53 *U. CHI. L. REV.* 424, 427 (1986) (commenting that the discovery process may consume years); Arthur R. Miller, *The Adversary System: Dinosaur or Phoenix*, 69 *MINN. L. REV.* 1, 9 (1984) (assailing the rampant use of discovery in stalling lawsuits); Jon O. Newman, *Rethinking Fairness: Perspectives on the Litigation Process*, 94 *YALE L.J.* 1643, 1644 (1985) (criticizing the overuse of depositions, which often yield little helpful information). But see Marc Galanter, *Reading the Landscape of Disputes: What We Know and Don't Know (and Think We Know) About Our Allegedly Contentious and Litigious Society*, 31 *UCLA L. REV.* 4, 61 (1983) (questioning the prevalence of discovery abuse); David M. Trubek, *The Costs of Ordinary Litigation*, 31 *UCLA L. REV.* 72, 89-96 (1983) (defending the reasonableness of most discovery practice).

5. See generally Constantine N. Katsoris, *An Arbitrator's Perspective*, in *SECURITIES ARBITRATION 1998: REDEFINING PRACTICES AND TECHNIQUES* at 312-314, *PLI Corporate Law and Practice Course Handbook Series Ord. No. B0-001K* (July-Aug. 1998) (commenting that "bloated" discovery lists "annoy the arbitrators" and that arbitrators generally defer most motions until after hearing the case).

6. Immanuel Kant believed that justice requires the blending of autonomy and cooperation. He said: "Justice is therefore the aggregate of those conditions under which the will of one person can be conjoined with the will of another in accordance with a universal law of freedom." *IMMANUEL KANT, THE METAPHYSICAL ELEMENTS OF JUSTICE* 34 (John Ladd trans. 1965).

7. This scenario assumes a post-dispute arbitration agreement. Pre-dispute arbitration agreements are perhaps even more prevalent than post-dispute arbitration agreements.

8. See *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 943 (1995) (commenting that "arbitration is simply a matter of contract between the parties; it is a way to resolve those disputes - but only those disputes - that the parties have agreed to

they select an arbitrator and invest him with decisionmaking authority.<sup>9</sup> Although the “shoelace” example pertains to post-dispute arbitration agreements, the same benefits flow from pre-dispute arbitration agreements, where parties exercise their autonomy to establish jointly a mutually advantageous method for resolving future disputes. Neither party relies on the power of the state to establish the rules of dispute resolution or to compel the other party to appear at a forum under state control.

This Article argues that arbitration agreements uniquely manifest individual autonomy and cooperation while limiting the reach of state adjudicative power over civil disputes. The state should therefore be prudent before refusing to limit arbitrability or entangling itself in the arbitral process. The courts, however, have a substantial role in determining the enforceability of arbitration agreements and reviewing awards. Judges should not enforce arbitration agreements that are vulnerable to contract defenses such as fraud, duress, or illegality.<sup>10</sup> They should, however, enforce all other arbitration agreements. Once arbitration proceeds, the state’s only role should be to assure that the arbitrator effectuated the contractual intent of the parties to the arbitration agreement. If an arbitrator fails to follow the agreement, he has frustrated the parties’ expression of autonomy and cooperation, and the court, when appropriately invoked, should intervene to achieve party intent.<sup>11</sup> When arbitrators fail to apply chosen law correctly, judicial review for errors of law may be required to meet the parties’ con-

---

submit to arbitration”); *Astoria Medical Group v. Health Ins. Plan of Greater New York*, 11 N.Y.2d 128, 132-33, 182 N.E.2d 85, 87, 227 N.Y.S.2d 401, 403-04 (1962) (stating that arbitration is “a creature of contract, a contract in which the parties themselves charter a private tribunal for the resolution of their disputes”); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 636 (1984) (noting that the contractual intent of the parties guides an international arbitral tribunal hearing the dispute); Soia Mentschikoff, *The Significance of Arbitration - A Preliminary Inquiry*, 17 LAW & CONTEMP. PROBS. 698, 699 (1952) (observing that arbitration entails an agreement contemplating binding authority of a nonjudicial decisionmaker); Thomas J. Stipanowich, *Punitive Damages and the Consumerization of Arbitration*, 92 Nw. U. L. REV. 1, 5 (1997) (“Arbitration remains first and foremost a creature of contract. Its shape and substance is formed by private agreement.”).

9. The rules of the American Arbitration Association (“AAA”), for example, provide that the arbitrating parties select the arbitrators. AAA RULES, RULE 13-15 & 54 (1998).

10. The FAA is consistent with this view, making arbitration agreements subject to common law contract defenses. 9 U.S.C. § 2 (1994).

11. Parties complaining of arbitrator error may bring such issues to the attention of the district court on a motion to vacate the award. 9 U.S.C. § 10 (1994). Section 10 provides for vacatur:

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

tractual expectations.<sup>12</sup> The state should not tamper with arbitration beyond this point.

This approach maximizes individual autonomy and cooperation while minimizing governmental interference. The state does not interfere, however, when it facilitates the achievement of party intent. As shown below, the courts, particularly the Supreme Court, have failed to find the proper level of governmental intervention into arbitration agreements. At first, the Court intruded into the realm of "private government," by refusing to permit arbitration of most federal claims.<sup>13</sup> Though conceding that arbitration was efficient, the Court condemned arbitration for potential unfairness. The last twenty years have ushered in a transformation in the Court's attitude; condemnation has fallen to preference.<sup>14</sup> In its enthusiasm for arbitration, the Court has set arbitrators free of legal oversight, relinquishing even a modest commitment to safeguarding the contractual intent of the parties.<sup>15</sup>

---

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

(3) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence material and pertinent to the controversy; or of any other misbehavior by which the rights of a party have been prejudiced.

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

*Id.*

12. See Davis, *Judicial Review*, *supra* note 4, at 123-29 (arguing that when parties arbitrate a statutory claim or include a choice-of-law clause in their agreement, the court, when properly invoked, must correct legal errors unless the arbitration agreement expressly waives judicial review).

13. See *Wilko v. Swan*, 346 U.S. 427 (1953) (refusing to enforce pre-dispute agreements to arbitrate claims arising under Section 12(2) of the Securities Act of 1933), *overruled by* *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989).

14. See *Mitsubishi Motors v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 626 (1984) (stating that party intent to arbitrate is "generously construed"); *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984) (declaring the "national policy favoring arbitration"); *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983) (proclaiming the "liberal federal policy favoring arbitration agreements," and instructing that "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration").

15. See *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 56 (1995) (weakening the FAA's commitment to party intent by announcing that "the FAA's pro-arbitration policy does not operate *without regard* to the wishes of the contracting parties"); (emphasis in original) Jeffrey W. Stempel, *Bootstrapping and Slouching Toward Gomorrah: Arbitral Infatuation and the Decline of Consent*, 62 BROOK. L. REV. 1381, 1401 (1996) (recognizing that the Supreme Court, in advancing an over-expansive view of the FAA, has abandoned fundamental principles of voluntary consent when evaluating whether an arbitration agreement is unconscionable).

Part I offers a justification for the thesis of this Article. The justification derives from economic theory and political philosophy. In Part II, the author uses the thesis of this Article to evaluate the Federal Arbitration Act. In addition, Part II applies the thesis of this Article to numerous issues that have dogged courts for decades, if not centuries. First, the author evaluates the public policy defense to arbitration, a doctrine now in disrepute, which, until the 1980s, foreclosed the arbitration of numerous federal statutory claims. Next, the author analyzes state law restrictions that apply specially to arbitration agreements. Third, the author discusses whether courts or arbitrators should decide threshold issues of enforceability such as fraud and unconscionability. Finally, the author examines whether punitive damages should be a remedy available to arbitrators. The Article concludes that arbitration policy should recognize, not only the value of autonomy and cooperation as manifested in arbitration agreements, but also the role of arbitration in curbing the scope of state power over civil disputes.

### I. A Theoretical Rational

Government is too big. This complaint resonates from the cornfields of Kansas to the financial markets of Wall Street. A regulatory web ensnares the business community. Taxes flatten our wallets. The lathe of lawmaking cuts into our civil rights, however theoretically inalienable those rights may be. All levels of government come under criticism, but the growing colossus in Washington has sparked unrelenting attack. Many in Congress, perhaps cynically, have joined in the self-deprecating call to limit the influence of the national government.<sup>16</sup> Bending to the public's disenchantment with the federal behemoth, even President Clinton, a long-time proponent of big government, advocated "government that is smaller, lives within its means, and does more with less."<sup>17</sup>

Far from a new phenomenon, distrust of expansive governmental power has occupied political thought since the Enlightenment.<sup>18</sup>

---

16. See, e.g., Statement of Senator Grams, 144 CONG. REC. S10-01 (Jan. 27, 1998) ("I am a Republican, elected by the people of Minnesota to carry out my promise to lower their taxes and reign in a federal government that has grown out of control.").

17. 33 *Weekly Compilation of Presidential Documents* 60, Administration of William J. Clinton, *Inaugural Address* (Jan. 20, 1997). President Clinton straddled the fence between supporting expansive or contracted federal power when he stated that "we have resolved for our time a great debate over the role of government. Today we can declare: Government is not the problem, and government is not the solution. We — the American people — are the solution." *Id.*

18. See *infra* notes 19-23 and accompanying text (discussing concerns of political philosophers over expansive state power).

John Locke believed that man's faculty for reason would reveal the natural principle of equality between men.<sup>19</sup> Yet he recognized the tendency of some selfishly to pursue their own interests to the exclusion of the interests of others. Observing that "[a]bsolute monarchs are but men,"<sup>20</sup> Locke cautioned against unlimited state power, because he feared that sovereigns might exploit the governed and deprive them of their natural rights of liberty and property.<sup>21</sup> Even more emphatically, Thomas Jefferson denounced excessive political power as the inevitable instrument of oppression.<sup>22</sup> He suggested that the "generalizing and concentrating [of] all cares and powers into one body" has "destroyed liberty and the rights of man in every government that has existed under the sun."<sup>23</sup>

---

19. JOHN LOCKE, *THE SECOND TREATISE OF GOVERNMENT: AN ESSAY CONCERNING THE TRUE ORIGINAL, EXTENT, AND END OF CIVIL GOVERNMENT*, reprinted in *LOCKE'S TWO TREATISES OF GOVERNMENT* §§ 4-7, at 287-89 (Peter Laslett ed., 2d ed. 1967). See J.W. GOUGH, *JOHN LOCKE'S POLITICAL PHILOSOPHY* 11 (2d ed. 1973) (explaining Locke's belief that moral law exists in nature and that one may discover this law through reason); A. JOHN SIMMONS, *THE LOCKIAN THEORY OF RIGHTS* 105 (1992) (discussing Locke's position that natural rights are subject to rational deduction).

20. LOCKE, *supra* note 19, § 13, at 294. Locke stated:

*Absolute monarchs are but Men, and if Government is to be the Remedy of those Evils, which necessarily follow from Mens [sic] being Judges in their own Cases, and the State of Nature is therefore not to be endured, I desire to know what kind of Government that is, and how much better it is than the State of Nature, where one Man commanding a multitude, has the Liberty to be Judge in his own Case, and may do to all his Subjects whatever he pleases, without the least liberty to any one to question or controle those who Execute his Pleasure?*

*Id.*

See Karen Iverson Vaughn, *The Economic Background to Locke's Two Treatises* 142, appearing in *JOHN LOCKE'S TWO TREATISES OF GOVERNMENT* (Edward J. Harpam ed., 1992) (commenting that Locke viewed all men, including sovereigns, as motivated by self-interest and prone to abuse untempered political power). Thomas Hobbes argued that man's natural selfishness impels those who desire the same things to seek the subjugation and destruction of competitors. THOMAS HOBBS, *LEVIATHAN* 87 (Richard Tuck ed. 1996) (1651). To remove themselves from perpetual warfare, men institute governments, which, if justly administered, stave off conflict and protect the rights of individuals by punishing offenders. See *id.* at 117.

21. LOCKE, *supra* note 19, § 13, at 294. Locke posited that pre-political man existed in a state of nature in which he enjoyed a perfect state of freedom. This freedom encompassed liberty and property rights. *Id.* § 4, at 287.

22. See LANCE BANNING, *JEFFERSON AND MADISON* 226 (1995) (quoting a letter from Thomas Jefferson to Joseph C. Cabell, February 2, 1816).

23. *Id.*

Economists, too, deplore a state bloated with power.<sup>24</sup> Milton Friedman argues that when the state controls the economy it becomes uncontrollable and dangerous.<sup>25</sup> A free market economy, says Friedman, deters the acquisition of unbridled state power.<sup>26</sup> He explains that “[b]y relying primarily on voluntary co-operation and private enterprise, in both economic and other activities, we can insure that the private sector is a check on the powers of the governmental sector.”<sup>27</sup> In this statement, Friedman identifies two forces that contain governmental expansion: cooperation and private enterprise, which together comprise the expression of individual autonomy in the market setting.

Contract is the tool that enables market participants to carve out spheres of private control.<sup>28</sup> An expression of autonomy, a contract represents the cooperation of two people with competing but compatible goals. It is the instrument that hinders the expansion of government into private affairs. Contracting parties agree on terms that will bind them. These terms — whether relating to price, delivery, breach, or dispute resolution — establish the self-imposed rules of the transaction. The contract provides the “law” governing the economic relationship.<sup>29</sup> Private law, the law of consenting, cooperating parties, displaces public law.

---

24. See *infra* notes 25-28 and accompanying text (discussing economic concerns of expansive state power).

25. See MILTON FRIEDMAN, *CAPITALISM AND FREEDOM* 4 (1962).

26. See *id.* at 2.

27. *Id.* at 3. Friedman argues that to protect freedom “the scope of government must be limited.” *Id.* at 2. Friedman believes that capitalism is a necessary pre-condition for freedom, but that capitalism is not a sufficient pre-condition to insure freedom. See *id.* at 10. He observes, for example, that the most oppressive totalitarian regimes in the twentieth century operated under a free market economy. See *id.* Robert Nozick argues that only a “minimal state” is justifiable. ROBERT NOZICK, *ANARCHY, STATE AND UTOPIA* 297 (1968). He advocates a state that functions like a “night watchman” whose only purpose is to protect one person from harming another. *Id.* at 26. See also ALLEN BUCHANAN, *ETHICS, EFFICIENCY AND THE MARKET* 64-65 (1985) (summarizing Nozick’s thesis that any governmental curtailment of individual rights is undesirable). Kurt Rothschild criticizes Nozick’s libertarianism, noting that markets require regulation in such areas as drug trafficking, minimum wage, and indentured servitude. See KURT W. ROTHSCHILD, *ETHICS AND ECONOMIC THEORY* 43-49 (1993).

28. See W. DAVID SLAWSON, *BINDING PROMISES* 9-11 (1996) (noting that before the eighteenth century a court would set a contract price if a party complained that a tradesman had overcharged, but that since that time freedom of contract has supplanted state control over contractual terms and relationships).

29. See Manfred Rehbinder, *Status, Contract, and the Welfare State*, 23 *STAN. L. REV.* 941, 942 (1971) (commenting that under classical contract law “the legal situation of the individual . . . is determined by his efficiency and capabilities in a capitalis-

Borrowed from economics and political philosophy, the argument against excessive state power presents compelling support for arbitration. Arbitration agreements result from the cooperation of two quarreling parties who desire a fair and efficient method of dispute resolution.<sup>30</sup> Spawned by private enterprise, such agreements express individual autonomy, the exercise of the right to contract.<sup>31</sup> The result of the cooperative exercise of individual contract rights is self-government. Frances Kellor, a scholar of arbitration, recognized this point when she commended those who agree to arbitrate because they have exercised "freedom, self-discipline, and self-regulation."<sup>32</sup> An advocate of arbitration, Kellor called "self-regulation" a natural right in a democratic society.<sup>33</sup> Such agreements, however, do not merely represent the cooperative exercise of free market contract rights of two contestants to a dispute. They are unique in mapping out spheres of private government usually reserved to the state: arbitration divests the government of civil adjudicative power.<sup>34</sup> Other approaches to dispute resolution

---

tic economy, an economic order that places the institution of contract at his disposal as the instrument of free and responsible determination of legal relations").

30. See Thomas J. Stipanowich, *Rethinking American Arbitration*, 63 IND. L.J. 425, 433 (1988) (remarking that, because arbitration is contractual, the parties can design the process to fit their needs).

31. See Edward M. Morgan, *Contract Theory and the Sources of Rights: An Approach to the Arbitrability Question*, 60 S. CAL. L. REV. 1059, 1070 (1987) (arguing that contract rights grow out of personal autonomy, which pre-dates the state). Since arbitration agreements are an expression of autonomy, Morgan reasons that claims entailing purely private conflicts should be arbitrable, since the agreement to arbitrate such disputes is an expression of natural rights. Claims arising from rights created by the state to benefit the public, as a matter of public policy, should not be arbitrable, since such claims do not arise from man's natural autonomy, but rather are artifacts of the state. See *id.*

32. FRANCES KELLOR, *AMERICAN ARBITRATION* 6 (1948).

33. *Id.* at 4. Though recognizing that the lack of arbitration organizations in early American history discouraged the use of arbitration, Kellor wonders nevertheless how a people so committed to freedom and self-regulation neglected arbitration until the twentieth century when it came into vogue. See *id.* at 5-6.

34. See *Graham v. Scissor-Tail, Inc.*, 171 Cal. Rptr. 604 (1981) (holding an arbitration clause unenforceable because the arbitral forum appeared biased); *Parson v. Ambros*, 121 Ga. 98 (1904) (warning that "[b]y first making the arbitration contract, and then declaring who should construe it, the strong could oppress the weak"). See generally IAN R. MACNEIL, *AMERICAN ARBITRATION LAW* 61 (1992) (surmising that some courts spurned arbitration agreements fearing that the powerful might force their weaker adversaries into arbitration, and then they might control the process of selecting arbitrators and improperly affect the outcome). See also Paul L. Sayre, *Development of Commercial Arbitration Law*, 37 YALE L.J. 595, 611 (1928) (Before the Twentieth century, English courts resisted enforcing arbitration agreements because "one of the parties [might have been] able to dictate almost his own terms to the other. The other party might well [have been] forced into an arrangement for arbitra-

such as negotiation, conciliation,<sup>35</sup> settlement, and mediation<sup>36</sup> may avert litigation, but none of these replaces the courthouse with a tribunal created by contract and tailored to the needs of the parties.<sup>37</sup> None confers binding authority on a person who has no connection to the state and who, to a significant extent, is free of the legal strictures — procedural, evidentiary, and substantive — that the state imposes on litigants.<sup>38</sup> Every year, parties remove hundreds of thousands of disputes from the courtroom to an arbitral forum.<sup>39</sup> State and federal power diminish when civil adjudication shifts from the public sector to the private sector.

---

tion which would [have been] inadequate to protect his rights.”). *Cf.* *Woodyard v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 640 F. Supp. 760, 766 (S.D. Tex. 1986) (declining to enforce an arbitration clause in a standard securities customer account agreement because the broker lulled the unsophisticated investor into acquiescence). *But cf.*, e.g., *Cremin v. Merrill Lynch, Pierce, Fenner & Smith*, 957 F. Supp. 1460, 1465 (N.D. Ill. 1997) (enforcing mandatory arbitration clause between broker and employee).

35. Conciliation is akin to mediation. The term is often used in the context of labor disputes where a neutral third party assists the parties to settle the dispute and avoid arbitration. *See* 1 WILNER, *supra* note 1, § 1:02, at 4-5 (observing that most commercial arbitrators do not seek to facilitate settlement).

36. *See* THOMAS H. OEHMKE, *COMMERCIAL ARBITRATION* § 2:01, at 1 (rev. ed. 1998) (explaining that “[m]ediation is a nonbinding process where a neutral assists the parties in reaching a settlement but has no authority to make a final and binding decision or award”).

37. The parties to an arbitration agreement can fashion the process to suit their goals. *See* *Volt Info. Sciences, Inc. v. Leland Stanford Junior Univ.*, 489 U.S. 468, 479 (1989) (noting that “parties are generally free to structure their arbitration agreements as they see fit”); BERTOLD H. HOENIGER, *COMMERCIAL ARBITRATION HANDBOOK* § 1.07, at 1-11 (rev. ed. 1991) (instructing that “the possibilities for custom tailoring [arbitration agreements] are almost endless”); Stipanowich, *supra* note 30, at 433 (stating that the parties can mold the arbitral process into the form they desire).

38. *See supra* notes 1-5 and accompanying text (discussing the informality of arbitration).

39. The AAA, a public service organization offering a wide range of dispute resolution options, is the most popular arbitral forum. *See* OEHMKE, *supra* note 36, § 20:01, at 1. The number of filings at the AAA in 1995 was 62,423. Telephone Interview with Barbara Brady, Director of Case Administration AAA (Aug. 26, 1996). AAA filings climbed to 72,200 in 1996. Telephone Interview with Luis Cruz, Assistant to Director of Case Administration AAA (Feb. 27, 1997). *See also* OEHMKE, *supra* note 36, § 20:01, at 1 (“While the majority of arbitration[s] . . . are administered by the [AAA], special tribunals exist, particularly those serving licensed professions.”). Securities self-regulatory organizations (“SROs”) such as the National Association of Securities Dealers and the New York Stock Exchange administer thousands of securities arbitrations annually. *See* Constantine N. Katsoris, *SICA: The First Twenty Years*, 23 *FORDHAM URB. L.J.* 483, 491 (1996) (reporting that between 1979 and 1996 a total of over 65,000 cases were filed with SROs); SEC. IND. CONF. ON ARB. 38 (10th Rep. July 1998) (reporting that in 1997 SROs received a total of 6,665 arbitration cases).

Some argue, however, that judicial power belongs under state control.<sup>40</sup> Heinrich Kronstein disdains arbitration for usurping judicial power from the state.<sup>41</sup> Because arbitrators are not bound by law,<sup>42</sup> or at least they believe themselves not to be bound, Kronstein brands arbitration a “lawless” form of “private government.” This failure to enforce the law, Kronstein argues, does not merely inflict injustice on the disputing parties, but also injures society. When law is not enforced, society suffers because legal norms erode. Legal norms need exercise like muscles, and they will atrophy from disuse. Judge Harry Edwards has expressed similar misgivings about arbitration, warning that arbitration may “endanger what the law has accomplished[,]” for arbitration replaces “the rule of law with nonlegal values.”<sup>43</sup> Owen Fiss, too, criticizes alternative dispute resolution (which subsumes arbitration) for depriving courts of the opportunity to clarify and develop the law. He contends that arbitration frustrates the judges’ role to “explicate and give force to the values embodied in authoritative texts such as the Constitution and statutes: to interpret those values and to bring reality into accord with them.”<sup>44</sup>

These scholars exaggerate when they link arbitration to the dissolution of values.<sup>45</sup> True, the evolution of common law is indispensable to our legal system. Contract law and tort law reflect the accumulation of centuries of judicial wisdom. Judicial decisions

---

40. See, e.g., Edward Brunet, *Questioning the Quality of Alternative Dispute Resolution*, 62 TUL. L. REV. 1, 19 (1987) (warning that “the legal norms that ADR ignores regularly could atrophy and become inefficacious”).

41. See Heinrich Kronstein, *Business Arbitration — Instrument of Private Government*, 54 YALE L.J. 36 (1944).

42. See, e.g., *Stroh Container Co. v. Delphi Indus.*, 783 F.2d 743, 751 n.12 (8th Cir.), cert. denied, 476 U.S. 1141 (1986) (stating that “the arbitration system is an inferior system of justice, structured without due process, rules of evidence, accountability of judgment [or] rules of law”); *Aimcee Wholesale Corp. v. Tomar Products, Inc.*, 21 N.Y.2d 621, 626, 237 N.E.2d 223, 225, 289 N.Y.S.2d 968, 971 (1968) (stating that “[a]rbitrators are not bound by rules of law”); 1 WILNER, *supra* note 1, § 25:01, at 391 (noting that “arbitrators need not follow otherwise applicable law when deciding issues before them unless they are commanded to do so by the terms of the arbitration agreement” (quoting *University of Alaska v. Modern Const., Inc.*, 522 P.2d 1132, 1140 (Alaska 1974))); Edward Brunet, *Arbitration and Constitutional Rights*, 71 N.C. L. REV. 81, 85 (1992) (recognizing that prevailing law permits arbitrators to ignore legal doctrine).

43. Harry T. Edwards, *Alternative Dispute Resolution: Panacea or Anathema?*, 99 HARV. L. REV. 668, 676-77 (1986). Judge Edwards cites the example of arbitrating disputes involving toxic waste. The arbitral award may contradict public law and may injure society by allowing dangerous practices to continue. See *id.* at 677.

44. Owen Fiss, *Against Settlement*, 93 YALE L.J. 1073, 1085 (1984).

45. See Davis, *Judicial Review*, *supra* note 4, at 83-85 (arguing that legal norms flourish even when the majority of disputes never reaches the courts).

scrape muddy statutes clean, and court declarations of unconstitutionality reverse legislative excesses.<sup>46</sup> But the venerable history of arbitration proves that legal norms retain their vitality despite the prevalence of nonjudicial decision-making.<sup>47</sup> If arbitration threatened society, our institutions would have disintegrated long ago. Congested court dockets provide judges with ample opportunity to nurture legal norms. Each year tens of thousands of cases go to final judgment — volumes of decisions cram law libraries. Like the universe itself, the law expands perpetually. We have enough public law. Few cases present issues of sufficient moment to demand the time of busy judges. Bringing every breach of contract case, every fraud case, and every negligence case to court would not advance values and norms, but would choke courts, which struggle to meet clogged calendars.<sup>48</sup>

Kronstein, however, argues more persuasively that arbitration carries the potential for abuse.<sup>49</sup> He is right in warning that the misuse of power extends beyond the halls of government. The wealthy or influential may corrupt the arbitral process to their advantage. The powerful may coerce their weaker adversaries into a private forum infused with bias; trade organizations may rig the system to favor members over nonmembers.<sup>50</sup>

---

46. Learned Hand toiled at the task of statutory construction. He described his work as follows:

In my own case the words of such an act as the Income Tax, for example, merely dance before my eyes in a meaningless procession: cross-reference to cross-reference, exception upon exception - couched in abstract terms that offer no handle to seize hold of - leave in my mind only a confused sense of some vitally important, but successfully concealed, purport, which it is my duty to extract, but which is within my power, if at all, only after the most inordinate expenditure of time.

GERALD GUNTHER, *LEARNED HAND* 467 (1994) (quoting Learned Hand, *Tribute to Thomas Swan*, 57 *YALE L.J.* 167, 169 (1947)).

47. See KELLOR, *supra* note 32, at 3-4 (tracing arbitration to the ancient Phoenician and Greek traders).

48. See Lieberman & Henry, *supra* note 4, at 424 (suggesting that most divorce, negligence and breach of contract cases do not present momentous issues requiring judicial comment).

49. See Kronstein, *supra* note 41, at 40. Kronstein also notes that faulty arbitration decisions may affect unrepresented third parties adversely. See *id.* at 58-59. The most salient example is antitrust decisions that have widespread economic consequences. Fiss, too, warns that nonjudicial resolutions of disputes may harm third parties. He offers racial discrimination cases as examples; a settlement may perpetuate abusive discriminatory practices. See Fiss, *supra* note 44, at 1085.

50. See Kronstein, *supra* note 41, at 40.

The courts must rescue the oppressed from overreaching.<sup>51</sup> This method of rescue may seem to contradict the thesis of this Article - keeping governmental involvement at the minimum level necessary to insure freedom of contract. Judicial review is, after all, a form of government involvement. Recommending such judicial intervention, however, does not betray this Article's thesis. Judicial action is necessary to protect contract rights. The common law principle of unconscionability does not tolerate coerced agreements.<sup>52</sup> Neither does contract law nor the Federal Arbitration Act ("FAA" or the "Act") countenance corrupt arbitral proceedings<sup>53</sup> or corrupt awards, both of which deny a party its reasonable contractual expectation of a fair hearing.<sup>54</sup> Coerced agreements contradict

---

51. The common law contract doctrine of unconscionability condemns agreements that result from unfair bargaining tactics and include unfair terms. See JOHN D. CALAMARI AND JOSEPH M. PERILLO, *THE LAW OF CONTRACTS* § 9-38, at 318 (2d. ed. 1977) (tracing the doctrine of unconscionability primarily to courts of equity); CORBIN ON CONTRACTS § 559B (Supp. 1997) (noting that only grossly unfair contracts are unenforceable under unconscionability doctrine); Arthur Allen Leff, *Unconscionability and the Code - The Emperor's New Clause*, 115 U. PA. L. REV. 485, 487 (1967) (coining the term "procedural unconscionability" to refer to predatory bargaining tactics and the term "substantive unconscionability" to refer to grossly unfair terms); John E. Murray, Jr., *Unconscionability: Unconscionability*, 31 U. PITT. L. REV. 1, 26 (1969) (proposing that only material terms should be subject to the unconscionability defense); Richard E. Speidel, *Unconscionability, Assent and Consumer Protection*, 31 U. PITT. L. REV. 359, 368-69 (1970) (arguing that a party raising an unconscionability defense should have to prove a prima facie case, that is, a substantial disparity between the value paid and the value received if the contract is enforced as written).

52. See Richard E. Speidel, *Afterword: The Shifting Domain of Contract*, 90 NW. U. L. REV. 254, 258 (1995) (observing that doctrines of unconscionability and public policy protect "freedom from contract," that is, freedom from predatory or illegal agreements).

53. Section 10 of the FAA provides for vacatur of an arbitration award "where an award was procured by corruption, fraud, or undue means," and "where there was evident partiality or corruption in arbitrators, or either of them." 9 U.S.C. § 10(1) & (2) (1994). See *infra* Part II.A (discussing the FAA).

54. Arbitration implies the right to a fundamentally fair hearing. See, e.g., *Yasuda Fire & Marine Ins. Co. v. Continental Casualty Co.*, 37 F.3d 345, 353 (7th Cir. 1994) (recognizing that courts have required arbitrators "to afford the parties a fundamentally fair hearing prior to awarding relief"); *Grovner v. Georgia-Pacific Corp.*, 625 F.2d 1289, 1290 (5th Cir. 1980) (noting that arbitration must provide "a fundamentally fair hearing"); *Totem Marine Tug & Barge v. North American Towing Inc.*, 607 F.2d 649, 651 (5th Cir. 1979) (observing that although arbitration "is much less formal than a trial in court," the process grants the parties the right to a "fundamentally fair hearing"); see generally IAN R. MACNEIL ET AL., *FEDERAL ARBITRATION LAW: AGREEMENTS, AWARDS, AND REMEDIES UNDER THE FEDERAL ARBITRATION ACT* § 32.3.1 (1994) (discussing the obligation of arbitrators to provide the parties with a fundamentally fair hearing); Kenneth R. Davis, *Due Process Right to Judicial Review of Arbitral Punitive Damages Awards*, 32 AM. BUS. L.J. 583, 601-602 (1995) (citing authority for the proposition that courts require arbitrators to provide parties with a fundamentally fair hearing).

freedom of contract, depriving the aggrieved party of choice. Freedom of contract includes the freedom not to contract.<sup>55</sup> Cooperation, too, is incompatible with coercion. Judicial intervention in these cases protects freedom of contract, and is therefore appropriate and necessary. Rather than arguing against such judicial intervention, the thesis of this Article requires it. The state must test arbitration agreements against the principles of contract law. The agreement must reflect the contractual intent of the parties, and it must not be unconscionable, illegal under ordinary contract principles,<sup>56</sup> or subject to any other contract defense.

## II. Applying the Model

One may evaluate existing arbitration law by measuring that law against the model of arbitration law proposed in this Article. Because the FAA is the foundation of federal arbitration law, the analysis begins with the Act. The analysis will then turn to some of the most controversial issues arising under arbitration law.

### A. The Federal Arbitration Act

Judicial disfavor with arbitration agreements began in seventeenth century England with the ouster-of-jurisdiction doctrine, and continued in the United States until the twentieth century.<sup>57</sup> This doctrine denied enforcement of freely negotiated arbitration

---

55. See Richard E. Speidel, *Contract Theory and Securities Arbitration: Wither Consent?*, 62 BROOK. L. REV. 1335, 1337 (1996) (noting that freedom of contract implies freedom from contract).

56. The illegality must derive from general contract law rather than from rules applicable only to arbitration agreements. See *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 685 (1996). Special rules limiting the range of arbitration agreements pose state interference with self-government and undue arrogation of state adjudicative power.

57. See, e.g., *Vynior's Case*, 77 Eng. Rep. 595, 597-601 (1906) (acknowledging the hostility of English courts to arbitration agreements); *Kill v. Hollister*, 1 Wils. K. B. 131, XCV Eng. Rep. 532 (1746) (refusing to enforce a pre-dispute arbitration agreement because "the parties cannot oust this court" of jurisdiction). But see *Kulukundis Shipping Co. v. Amtorg Trading Corp.*, 126 F.2d 978, 982-84 (2d Cir. 1942) (mocking the ouster-of-jurisdiction doctrine as an unprincipled rule of law). Although courts would not specifically enforce arbitration agreements, they would enforce awards rendered pursuant to such agreements. *Clapham v. Hingham*, 1 Bing. 86, 90, 130 Eng. Rep. 36, 37 (1922) (stating that, although arbitration agreements are revocable, arbitration awards are enforceable). See Leo Kanowitz, *Alternative Dispute Resolution and the Public Interest: The Arbitration Experience*, 38 HASTINGS L.J. 239, 252 (1987) (noting that under the ouster-of-jurisdiction doctrine English courts would not specifically enforce arbitration agreements but they would enforce awards). See generally 1 WILNER, *supra* note 1, § 3:01, at 21-23 (discussing the history of the judicial hostility toward arbitration agreements).

agreements. Passed in 1925, the FAA repudiated the ancient hostility toward arbitration.<sup>58</sup> Although it would take some time for this new policy to filter throughout the country,<sup>59</sup> the FAA announced that arbitration agreements were as enforceable as other contracts.<sup>60</sup> Section 2 of the FAA says that a written arbitration provision "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contracts."<sup>61</sup> This most significant section of the FAA establishes federal arbitration policy ensuring that "private agreements to arbitrate are enforced according to their terms."<sup>62</sup> Its purpose is merely to reject the courts' repugnance of arbitration and to make arbitration agreements enforceable,<sup>63</sup> not to place arbitration agreements beyond the power of state regulation.<sup>64</sup> The section, for example, does not insulate arbitration agreements from common law contract defenses, such as lack of consideration, fraud, duress, or the more general doctrine of unconscionability, which subsumes many other contract defenses.<sup>65</sup>

---

58. Ch. 213, §§ 1-15, 43 Stat. 883 (1925) (codified as 9 U.S.C. §§ 1-16 (1994)).

59. As late as 1953, the United States Supreme Court in *Wilko*, questioned the fairness of arbitration. See *supra* note 13.

60. See, e.g., *Wilko*, 346 U.S. 427, (refusing to enforce pre-dispute agreement to arbitrate claims arising under Section 12 (2) of the Securities Act of 1933); *American Safety Equip. Corp. v. J.P. Maguire & Co.*, 391 F.2d 821 (2d Cir. 1968) (refusing to enforce pre-dispute agreement to arbitrate claims arising under the Sherman Antitrust Act); *Aimcee Wholesale Corp. v. Tomar Prods. Inc.*, 21 N.Y.2d 621, 626, 237 N.E.2d 223, 225, 289 N.Y.S.2d 968, 970 (1968) (holding state law antitrust claim inarbitrable).

61. 9 U.S.C. § 2 (1988).

62. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 682 (1996) (quoting *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior College*, 489 U.S. 468, 479 (1989)); see H.R. REP. NO. 68-96, at 1-2 (1924) ("This bill declares simply that such agreements for arbitration shall be enforced, and provides a procedure in the Federal courts for their enforcement.").

63. See *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 478 (1989) ("The FAA was designed 'to overrule the judiciary's long-standing refusal to enforce agreements to arbitrate'" (citing *Dean Witter Reynolds Inc. v. Byrd* 470 U.S. 213, 219-20 (1985))). See also H.R. REP. NO. 68-96, at 1-2 (1924) ("The need for the FAA arises from . . . the jealousy of the English courts for their own jurisdiction . . . . This jealousy survived for so long a period that the principle became firmly embedded in the English common law and was adopted with it by the American courts. The courts have felt that the precedent was too strongly fixed to be overturned without legislative enactment.").

64. See *Volt Information Sciences*, 489 U.S. at 478-79 (holding California statute providing for stay of arbitration consistent with FAA). See also *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 58 (1995) (declining to hold that the FAA preempts state law prohibiting arbitrators from awarding punitive damages).

65. See *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 682 (1996) (quoting *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974)) (holding that the FAA "pre-

Section 2 is consistent with the thesis of this Article insofar as it gives arbitration agreements broad range over virtually all disputes, whether arising out of federal or state law, statute, or common law. The state should be wary of reserving spheres of conflict for the courts, and depriving participants in the marketplace the option of self-regulation. Only the courts, however, may determine whether the parties exercised freely their will to enter into an arbitration agreement.<sup>66</sup> Enforcing an agreement subject to a contract defense denies one of the parties freedom of contract. The courts must refuse to enforce legally defective arbitration agreements.<sup>67</sup> By making arbitration agreements subject to common law contract defenses, the FAA, as written, establishes the proper federal arbitration policy.<sup>68</sup>

The FAA, however, diverges from the thesis proposed in this Article insofar as it tolerates non-contractual state limitations on arbitration agreements.<sup>69</sup> Legal impediments to arbitration violate this thesis, and any such impediment should stand only if it promotes a policy that eclipses the policies served by arbitration: autonomy, cooperation, and the curtailment of state power. Though the FAA

---

clude[s] States from singling out arbitration provisions for suspect status, requiring instead that such provisions be placed 'upon the same footing as other contracts'"); see generally Stephen J. Ware, *Arbitration and Unconscionability After Doctor's Associates, Inc. v. Casarotto*, 31 WAKE FOREST L. REV. 1001 (1996) (recognizing that contract law defenses apply to arbitration agreements and all other agreements equally).

66. In *Prima Paint Corp. v. Food & Conklin, Mfg. Co.*, 388 U.S. 395 (1967), the Supreme Court erroneously held that arbitrators decide threshold issues of enforceability of arbitration agreements.

67. The Supreme Court's misguided arbitration policy might mislead some to conclude that arbitration agreements deserve a favored status exempting them from certain contract defenses. See *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983) (declaring that "as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration"). One might stumble deeper into this faulty conclusion by noting that the FAA provides for specific enforcement of arbitration agreements, a remedy unavailable in most breach of contract actions. 9 U.S.C. § 2 (1994). A simple observation refutes this point. Under traditional contract law, specific performance is available when money damages would provide inadequate relief. Much like an agreement to sell a Stradivarius violin or a controlling interest of stock in a closely held corporation, damages are insufficient to redress the breach of an arbitration agreement. The parties bargained for adjudication in an alternative forum; they bargained for privacy, efficiency and self-regulation. Since the injury occasioned by the breach is not reducible to dollars, specific performance is the appropriate contract remedy.

68. The Supreme Court, however, has in many cases misinterpreted the FAA, insulating arbitration agreements from certain contract defenses. See *infra* notes 142-157 and accompanying text.

69. See *infra* notes 118-129 and accompanying text (discussing the *Volt* decision).

embodies a pro-arbitration policy,<sup>70</sup> it permits state law to impose procedural limitations on arbitration.<sup>71</sup>

One suspect limitation appears in the text of Section 2, which provides for the enforcement only of written agreements to arbitrate,<sup>72</sup> though courts enforce such agreements even if not signed.<sup>73</sup> This Statute of Frauds intrudes on the freedom of parties to enter into arbitration agreements. Prudence might urge parties to reduce arbitration agreements to writing, but arbitration law should not foreclose the enforcement of oral agreements to arbitrate. Congress undoubtedly required arbitration agreements to be in writing, recognizing the significance of such agreements, which trim the procedural and substantive rights that accompany litigation. A strict writing requirement is not needed to protect parties who never agreed to arbitrate from dissembling adversaries. If a party admitted under oath that he had entered into an oral arbitration agreement, no sound policy reason would allow that party to avoid the agreement simply because it was not written.<sup>74</sup> The practical consequences of this Statute of Frauds are undoubtedly minor, since most parties formalize arbitration agreements, but the law should not impose such a restriction.<sup>75</sup> Yet such a Statute of Frauds removes some disputes from the private sector and places them in the public sector increasing the power of the judiciary.

Ostensibly applying the FAA, the United States Supreme Court has decided numerous issues shaping arbitration policy. Unfortunately, the Court has often failed to appreciate the purposes of the FAA and the Court has therefore misapplied the statute. Although some of these decisions advance the policies proposed in this Article, many conflict with these policies. The result is a crippled jurisprudence of arbitration.

---

70. See *infra* notes 94-96 and accompanying text.

71. See *infra* notes 118-129 and accompanying text.

72. 9 U.S.C. § 2 (1994).

73. See, e.g., *Valero Ref., Inc. v. M/T Lauberhorn*, 813 F.2d 60, 64 (5th Cir. 1987) (holding that arbitration agreements must be in writing but that they need not be signed); *McAllister Bros., Inc. v. A&S Transp. Co.*, 621 F.2d 519, 524 (2d Cir. 1980) (noting that a party may be bound to an unsigned arbitration agreement).

74. An analogy appears in the Uniform Commercial Code, which contains a statute of frauds requiring contracts for the sale of goods of \$500 or more to be in writing. See U.C.C. § 2-201 (1992). If, however, the party to be charged with the agreement admits in a pleading, in testimony, or in court that he entered into the agreement, the agreement is enforceable to the extent admitted. See U.C.C. § 2-201(3)(b) (1992).

75. See 1 WILNER, *supra* note 1, § 6:01, at 73 (commenting that oral arbitration agreements occur rarely except where an oral agreement extends an existing written arbitration agreement).

## B. The Public Policy Defense

Although now discredited by the Supreme Court, the public policy defense, when in vogue, prohibited the arbitration of numerous federal statutory claims.<sup>76</sup> The Court established the defense in *Wilko v. Swan*,<sup>77</sup> a securities arbitration case in which the Court held unenforceable a pre-dispute agreement to arbitrate a claim under Section 12(2) of the Securities Act of 1933 ("Securities Act").<sup>78</sup> Such agreements, the Court ruled, impermissibly waived rights guaranteed by the Securities Act.<sup>79</sup> Section 14 of the Act forbids such waivers,<sup>80</sup> and the Court concluded that a pre-dispute arbitration agreement waives the statutory right of access to the federal courts guaranteed under Section 22(a).<sup>81</sup> Rejecting the argument that arbitration is equivalent to litigation in a federal court,<sup>82</sup> the Supreme Court catalogued deficiencies of the arbitral process.<sup>83</sup> It cited, for example, the lack of legal training of many

---

76. See, e.g., *Wilko v. Swan*, 346 U.S. 427 (1953), *overruled by* *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989) (declining to enforce pre-dispute agreement to arbitrate claims under Section 14 of the Securities Act); *Page v. Mosely, Hallgarten, Estabrook & Weeden, Inc.*, 806 F.2d 291 (1st Cir. 1986) (holding RICO claims not arbitrable); *Beckman Instruments, Inc. v. Technical Dev. Corp.*, 433 F.2d 55, 63 (7th Cir. 1970), *cert. denied*, 401 U.S. 976 (1971) (holding patent validity questions inappropriate for arbitration); *Utley v. Goldman Sachs & Co.*, 883 F.2d 184 (1st Cir. 1989), *cert. denied*, 493 U.S. 1045 (1990) (holding that an arbitration agreement does not preclude access to a judicial forum for Title VII claims); *Nicholson v. CPC Int'l, Inc.*, 877 F.2d 221 (3d Cir. 1989) (holding Age Discrimination in Employment Act claims not arbitrable); *Barrowclough v. Kidder, Peabody & Co.*, 752 F.2d 923 (3d Cir. 1985) (holding ERISA claims arbitrable); *American Safety Equip. Corp. v. J.P. Maguire & Co.*, 391 F.2d 821 (2d Cir. 1968) (refusing to allow arbitration of claims arising out of the Sherman Antitrust Act).

77. 346 U.S. 427 (1953); see also *Pierson v. Dean, Witter, Reynolds, Inc.*, 742 F.2d 334, 339 (7th Cir. 1984) (rejecting the claim that an arbitration clause in a securities customer account agreement was unconscionable).

78. See *Wilko*, 346 U.S. at 438.

79. See *id.* at 434-35.

80. Section 14 provides: "Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void." 48 Stat. 84, 15 U.S.C. § 77n (1994).

81. See *id.* Section 22(a) provides: "The district courts of the United States . . . shall have jurisdiction . . . concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this [Act]." 15 U.S.C. § 77v(a) (1994).

82. See 1 WILNER, *supra* note 1, § 1:01, at 2 ("Arbitration, which involves a final determination of disputes, has elements of the judicial process. Although an alternative to judicial decision-making, it does not replace it in all aspects, but rather co-exists with court procedure as an adjunct and part of the American system of administering justice.").

83. See *Wilko*, 346 U.S. at 436.

arbitrators, and the failure of most awards to provide a rationale for the arbitrators' decision.<sup>84</sup>

The Court's attacks on the procedural adequacy of arbitration, whether justified or not, missed the point. Freely negotiated arbitration agreements that are not vulnerable to ordinary contract defenses deserve enforcement, even if the controversy implicates federal statutory claims.<sup>85</sup> If Congress foreclosed the arbitration of a particular claim, the Court would have to respect congressional intent, even though ill-advised. Were there such a statute, one would have urged its repeal, but no such statutory prohibition existed. The problem lay, not with Congress, but with the Court's interpretation of the Securities Act. Characterizing the right to bring a Section 12(2) claim in federal court as inalienable provided inadequate justification for denying arbitration. By this reasoning, few federal statutory claims would ever be subject to arbitration by operation of a pre-dispute agreement because most federal statutes provide for federal court jurisdiction.<sup>86</sup> Such a limitation on arbitration would dwarf freedom of contract, by eliminating the arbitrability of a host of federal claims. The right to sue in federal court would be converted into a requirement. Rather than having a choice of forum, parties would lose the option of adjudication at a non-public tribunal. The state would be creating a judicial monopoly over federal claims, bolstering its power, while weakening the right of marketplace participants to regulate their affairs.

A more sensible reading of the Securities Act forbids waiver of substantive rights, rather than procedural rights, conferred by the

---

84. *See id.*

85. Particularly in the area of antitrust law, many have disagreed with this position. One commentator, for example, has argued that accomplishing the goals of antitrust law is incompatible with arbitration. *See* Robert Pitofsky, *Arbitration and Antitrust Enforcement*, 44 N.Y.U. L. REV. 1072, 1076-81 (1969). He contends that court judgments, unlike arbitration awards, deter future violations and that plaintiffs in litigated cases enhance the regulatory function of the Federal Trade Commission by acting as private attorneys general. *See id.* at 1073-74. *But see* John R. Allison, *Arbitration Agreements and Antitrust Claims: The Need for Enhanced Accommodation of Conflicting Public Policies*, 64 N.C. L. REV. 219, 252-253 (1986) (arguing that antitrust claims should be arbitrable, and pointing out that arbitrating antitrust claims harms the public no more than settling antitrust claims).

86. Section 29(a) of the Exchange Act, for example, provides for exclusive federal court jurisdiction over claims arising under the Act. 15 U.S.C. § 78aa (1994). Additionally, the Clayton Act, the Sherman Act, the Civil Rights Act of 1964, and the Americans with Disabilities Act ("ADA") provide for exclusive jurisdiction in federal court. *See* 15 U.S.C. § 9 (1994) (Clayton Act); 15 U.S.C. § 4 (1994) (Sherman Act); 42 U.S.C. § 1983 (1994) (Civil Rights Act of 1964); 42 U.S.C. § 2000e (1994) (Title VII); 42 U.S.C. § 12101(b) (1994) (ADA).

Act. After rendering several decisions undermining *Wilko*,<sup>87</sup> the Court ultimately arrived at this conclusion in *Shearson/American Express Inc. v. McMahon*,<sup>88</sup> in which the Court held enforceable a pre-dispute agreement to arbitrate claims arising under Section 10 of the Securities Exchange Act of 1934 (Exchange Act).<sup>89</sup> Although the Exchange Act has an anti-waiver provision<sup>90</sup> and a jurisdictional provision,<sup>91</sup> both nearly identical to the provisions determinative in *Wilko*, the Court held that the waiver provision in the Exchange Act referred to substantive rather than procedural rights, such as the right of access to federal courts.<sup>92</sup> Inimical to the reasoning in *McMahon*, *Wilko* survived merely because of the Supreme Court's institutional loyalty to its prior decisions.<sup>93</sup> A vestige of the time when courts viewed arbitration with suspicion, *Wilko* contradicted the Court's shift to a policy favoring arbitration, and the Court, therefore, could not tolerate *Wilko* in the post-*McMahon* era.<sup>94</sup> In *Rodriguez de Quijas v. Shearson/American Ex-*

---

87. See *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 509 (1974) (enforcing an agreement to arbitrate a transnational dispute involving claims arising under Section 10(b) of the Exchange Act because the policies that necessitated the *Wilko* holding were inapplicable in the arena of international trade); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 638-40 (1985) (enforcing an agreement to arbitrate a transnational dispute involving Sherman Act antitrust claims).

88. 482 U.S. 220 (1987).

89. See *id.* at 237-38.

90. See *id.* at 227. Section 29(a) of the Exchange Act declares void "[a]ny condition, stipulation, or provision binding any person to waive compliance with any provision of [the Exchange Act] . . ." 15 U.S.C. § 78cc(a).

91. See *McMahon*, 482 U.S. at 227. Section 27 of the Exchange Act provides in relevant part: "The district courts of the United States . . . shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder." 15 U.S.C. § 78aa.

92. See *McMahon*, 482 U.S. at 227-29. The Court reasoned, in spite of *Wilko*, that Section 29(a) forbids agreements to waive "compliance" with the provisions of the Exchange Act. See *id.* Section 27, the jurisdictional provision, however, imposed no statutory duties requiring "compliance." Hence the waiver provision did not refer to the jurisdictional provision. See *id.* at 228.

93. Determined to reconcile *Wilko* with *McMahon*, the Court suggested that Section 12(2) rights are "special" in comparison to Section 10(b) rights because Section 12(2) provides a form of strict liability eliminating elements such as due diligence and causation. See *McMahon*, 482 U.S. at 228-29. This rationale is unpersuasive, however, since both sections protect investors from securities fraud, and since Section 12(2) applies only to sellers whereas Section 10(b) applies more broadly to certain nonsellers.

94. See *id.* at 256-57 (Blackmun, J., dissenting) (discerning no meaningful distinction between the statutory scheme of the Securities Act on which *Wilko* ruled and the statutory scheme of the Exchange Act on which *McMahon* ruled). Justice Stevens noted that *Wilko* had stood for thirty-two years, a longevity which created a presumption of congressional approval. See *id.* at 268-69 (Stevens, J., concurring in part and

*press, Inc.*,<sup>95</sup> the Court abandoned the charade that *Wilko* and *McMahon* could be reconciled and held Section 12(2) claims arbitrable.<sup>96</sup>

*Wilko* seems today an anachronism, an arbitrary obstacle to freedom of contract and self-government. Nevertheless, *Wilko* identified a serious shortcoming of arbitration, not easily dismissed. However confusingly, *Wilko* suggested correctly that the narrow scope of judicial review would perpetuate legal error in arbitration awards.<sup>97</sup> *McMahon* scorned this concern, comforting us with the

---

dissenting in part). Abandoning the doctrine, therefore, should have been left to Congress. *See id.* at 269. (Stevens J., concurring part and dissenting in part).

95. 490 U.S. 477 (1989).

96. Since *Rodriguez de Quijas*, the public policy defense has faded into disrepute, and courts now enforce pre-dispute agreements to arbitrate virtually any federal claim. *See, e.g.,* *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991) (subjecting Age Discrimination in Employment Act claims to arbitration); *Patterson v. Tenet Healthcare, Inc.*, 113 F.3d 832, 837 (8th Cir. 1997) (stating that Title VII claims can be subject to arbitration); *Cole v. Burns Int'l Security Servs.*, 105 F.3d 1465, 1482 (D.C. Cir. 1997); *Pritzker v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 7 F.3d 1110, 1116 (3d Cir. 1993) (holding that ERISA claims can be subject to arbitration); *Mago v. Shearson Lehman Hutton, Inc.*, 956 F.2d 932 (9th Cir. 1992) (holding that the employee failed to establish that Congress, in enacting Title VII, intended to preclude arbitration of Title VII claims); *Bird v. Shearson Lehman/ American Express, Inc.*, 926 F.2d 116 (2d Cir. 1991) (concluding that Congress did not intend to preclude a waiver of a judicial forum for statutory ERISA claims and, furthermore, that the FAA requires courts to enforce agreements to arbitrate such claims); *Alford v. Dean Witter Reynolds, Inc.*, 939 F.2d 229 (5th Cir. 1991) (holding that Title VII claims can be subject to arbitration).

97. *See Wilko*, 346 U.S. at 436-37. The Court lapsed into enigmatic language when it stated:

Power to vacate an award is limited. While it may be true, as the Court of Appeals thought, that a failure of the arbitrators to decide in accordance with the provisions of the Securities Act would 'constitute grounds for vacating the award pursuant to Section 10 of the Federal Arbitration Act,' that failure would need to be made clearly to appear. In unrestricted submission, such as the present margin agreements envisage, the interpretations of the law by the arbitrators in contrast to manifest disregard are not subject, in the federal courts, to judicial review for error in interpretation.

*Id.* Justice Jackson, in a concurring opinion, questioned why the Court had drifted into this unfortunate language which unnecessarily declares that courts may not review arbitral awards for errors of law. *See id.* at 438-39 (Jackson, J., concurring). In dissent, Justice Frankfurter, joined by Justice Minton, argued that Section 10 of the FAA grants courts the authority to review arbitral awards for legal error. *See id.* at 439-40.

The judicial word salad in the majority opinion led to adoption of the manifest disregard test, and it has elicited endless criticism. Some believe the standard is too broad. *See, e.g.,* Michael P. O'Mullan, *Seeking Consistency in Judicial Review of Securities Arbitration: An Analysis of the Manifest Disregard of the Law Standard*, 64 FORDHAM L. REV. 1121, 1135 (1995) (faulting the manifest disregard standard for compromising the finality of arbitration awards); Brad A. Galbraith, *Vacatur of Commercial Arbitration Awards in Federal Court: Contemplating the Use and Utility of the*

bromide that the scope of judicial review is sufficient “to ensure that arbitrators comply with the requirements of the statute.”<sup>98</sup> Three years earlier, in *Mitsubishi v. Soler Chrysler-Plymouth, Inc.*,<sup>99</sup> the Court sought to mollify fears of arbitrating Sherman Act antitrust claims in international tribunals announcing that “it would not require intrusive [judicial] inquiry to ascertain that the tribunal took cognizance of the antitrust claims and actually decided them.”<sup>100</sup> Unfortunately, these assurances of adequate judicial oversight misstate the practice of most federal courts. The prevailing standard of review — the manifest disregard test — permits vacatur only when arbitrators intentionally disregard the law.<sup>101</sup>

---

“Manifest Disregard” of the Law Standard, 27 IND. L. REV. 241, 259 (1993) (criticizing the manifest disregard test because it encourages costly and lengthy motions and appeals); Marta B. Varela, *Arbitration and the Doctrine of Manifest Disregard*, 49 DISP. RESOL. J. 64, 67 (June 1994) (lambasting the manifest disregard standard for encouraging pointless motions and appeals which rob arbitration of finality). Others criticize the manifest disregard test because it is too narrow. See, e.g., MACNEIL ET AL., *supra* note 54, at § 40.7.2.5, 40:94 (deploring the manifest disregard test for permitting arbitrators to render awards without regard to controlling law); Richard E. Speidel, *Arbitration of Statutory Rights Under the Federal Arbitration Act: The Case for Reform*, 4 OHIO ST. J. ON DISP. RESOL. 157, 198 (1989) (opposing the manifest disregard test because it effectively precludes judicial correction of error in arbitral awards). Still others argue that the test is superfluous. See, e.g., Stephen L. Hayford, *Law in Disarray: Judicial Standards for Vacatur of Commercial Arbitration Awards*, 30 GA. L. REV. 731, 816-17 (1996) (construing the manifest disregard to overlap with Section 10(d)(3) of the FAA which provides for judicial vacatur when arbitrators to engage in improper conduct); Bret F. Randall, Comment, *The History, Application, and Policy of the Judicially Created Standards of Review for Arbitration Awards*, 1992 BYU L. REV. 759, 768 n.51 (1992) (suggesting that the manifest disregard test merely redefines error reversible under Section 10 of the FAA).

98. 482 U.S. at 232.

99. 473 U.S. 614 (1985).

100. *Id.* at 638.

101. First suggested in murky dicta in *Wilko v. Swan*, 346 U.S. 427, 436-37 (1953), the manifest disregard test has bloomed into the predominant standard of review of arbitration awards, although several versions of the test have developed. *Merrill Lynch, Pierce, Fenner & Smith v. Bobker*, 808 F.2d 930 (2d Cir. 1986) is a seminal case defining the test. *Bobker* held that the manifest disregard test is met when an arbitrator knew controlling law but nevertheless disregarded it. See *id.* at 933. The *Bobker* view of manifest disregard predominates among the circuits. *Flexible Mfg. Sys. Pty. Ltd. v. Super Prod. Corp.*, 86 F.3d 96, 100 (7th Cir. 1996) (holding that manifest disregard requires arbitrators to ignore deliberately law known to them); *Kanuth v. Prescott, Ball & Turben, Inc.*, 949 F.2d 1175, 1182 (D.C. Cir. 1991) (explaining that manifest disregard occurs when the arbitrators correctly state the law and proceed to ignore it); *Jenkins v. Prudential-Bache Sec., Inc.*, 847 F.2d 631, 634 (10th Cir. 1988) (remarking that manifest disregard “deals mainly with willful inattentiveness to the governing law”). Some courts have adopted more liberal versions of the test. In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Jaros*, 70 F.3d 418, 422 (6th Cir. 1995), the court equated the manifest disregard test with the standard of rationality. Adopting an even more liberal standard, *Cole v. Burns Int’l Sec. Serv.*, 105 F.3d 1465 (D.C. Cir.

Applying this test, courts routinely confirm legally erroneous awards.<sup>102</sup>

The solution, however, is not to deny arbitrability. Rather, the courts should broaden their scope of review. When parties agree to arbitrate federal statutory claims, or claims under any particular law, they implicitly instruct the arbitrators to apply controlling law correctly.<sup>103</sup> Parties do not expect arbitrators to misapply the law. Upon entering into an arbitration agreement, if told that a reviewing court would confirm an erroneous award, the parties would surely object, for they envision judicial review of such errors. Yet the predominant version of the manifest disregard standard ignores this expectation. By reviewing awards for errors of law, the courts would meet party expectations and preserve guaranteed rights.<sup>104</sup>

---

1997), held that all errors of statutory interpretation, whether deliberate or not, constitute manifest disregard. Yet another recent relaxation of the manifest disregard standard permits vacatur based on errors of fact as opposed to errors of law. See *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197, 204 (2d Cir. 1998). But see *Marshall v. Green Giant Co.*, 942 F.2d 539 (8th Cir. 1991) (expressing reservations about the manifest disregard test); *R.M. Perez & Associates, Inc. v. Welch*, 960 F.2d 534 (5th Cir. 1992) (rejecting the manifest disregard test in any form); *Raiford v. Merrill Lynch, Pierce, Fenner & Smith*, 903 F.2d 1410 (11th Cir. 1990) (rejecting the manifest disregard test in any form). See generally Eric P. Tuchman, *Claims Resulting From Employment Discrimination*, N.Y. L.J., Nov. 5, 1998, at 3 (discussing the impact of *Halligan* on the scope of judicial review of arbitration awards).

102. See, e.g., *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818, 822 (1997) (sustaining erroneous denial of attorneys' fees in ADA arbitration); *Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp.*, 103 F.3d 9, 14 (2d Cir. 1997) (upholding award even if based on misinterpretation of law); *Advest, Inc. v. McCarthy*, 914 F.2d 6, 10-11 (1st Cir. 1990) (confirming award that assessed wrong measure of damages); *San Martine Compania de Navagacion, S.A. v. Saguenay Terminals, Ltd.*, 293 F.2d 796, 800 (9th Cir. 1961) (confirming award although its legal accuracy was questionable).

103. See *Davis*, *Judicial Review*, *supra* note 4, at 123-126 (arguing that when parties submit a federal claim to arbitration, they reasonably expect the court to review the award for errors of law). But see *Hayford*, *supra* note 97, at 742-43 (concluding that most arbitration agreements evidence the intent of the parties to forego judicial review).

104. See Ian M. Comisky & Marvin Comisky, *Commercial Arbitration — Panacea or Nightmare?*, 47 TEMPLE L.Q. 457, 507 (1974) (advocating judicial review of arbitration awards for legal error but that such review be limited to a single instance without further appeal); Francis T. Freeman Jalet, *Judicial Review of Arbitration: The Judicial Attitude*, 45 CORNELL L.Q. 519, 556 (1960) (comparing the folly of confirming an erroneous award to the folly of affirming an erroneous judgment); C. Evan Stewart, *Securities Arbitration Appeal: An Oxymoron No Longer?*, 79 KY. L.J. 347, 368 (1990/1991) (proposing that the scope of judicial review of securities arbitration awards be expanded to ensure that arbitrators, who are often untrained to cope with complex securities law, are subject to judicial oversight); Philip G. Phillips, Note, *Rules of Law or Laissez-Faire in Commercial Arbitration*, 47 HARV. L. REV. 590, 613 (1934) (favoring expanded judicial review of arbitration awards). But see *Varelo Ref.*, *supra* note 73, at 64, 75 (opposing expanded review of arbitration awards because such review would

A small dose of governmental intervention in the form of judicial review would obviate the need to preclude arbitration and to force government-controlled adjudication on the parties. The arbitration agreement would be enforced, judicial review would accord with the intent of the parties, and governmental judicial power would be minimized.

The public policy defense barred the arbitration of statutory claims that the courts believed fell outside the competence of arbitration. Aside from the public policy defense, which was judge-made law, various state legislatures have enacted statutes placing express limitations on arbitration. Such "special" restrictions on arbitration agreements prevent parties from entering into arbitration agreements unwittingly and protect them from arbitration under circumstances where the state believes the courts would provide a more suitable forum. The motivation for such law is benign; the government shields the potential victim - the small business operator, the employee, and the consumer. When such limitations exceed the strictures of general common law, however, they contradict the autonomy of the parties to the arbitration agreement and frustrate the parties' efforts at cooperation. Special restrictions on arbitration may dislodge the dispute from the private sector, shunting the dispute to the courts. Such law violates all the social policies that arbitration serves.

### C. Special State Law Restrictions

Some legislation, like the public policy defense, forbids the arbitration of certain claims.<sup>105</sup> Other legislation provides procedures interfering with arbitration,<sup>106</sup> and a third category has conditioned the enforceability of arbitration agreements on compliance with special contractual requirements applicable only to arbitration agreements.<sup>107</sup>

The California Franchise Investment Law was an example of a state statute prohibiting the arbitration of a class of claims.<sup>108</sup> In *Southland Corp. v. Keating*,<sup>109</sup> the Supreme Court invalidated the statute. Owners of 7-Eleven convenience stores sued Southland,

---

compromise the finality of arbitration); Note, *Judicial Supervision of Commercial Arbitration*, 53 GEO. L.J. 1079, 1081 & n.3 (1965) (questioning whether the scope of judicial review of arbitration awards should be expanded).

105. See *infra* notes 108-116 and accompanying text.

106. See *infra* notes 118-129 and accompanying text.

107. See *infra* notes 134-137 and accompanying text.

108. See *Southland Corp. v. Keating*, 465 U.S. 1 (1984).

109. *Id.*

the franchisor, for breach of contract, in tort, and for violations of California's Franchise Investment Law.<sup>110</sup> Based on arbitration clauses in the franchise agreements, Southland moved to compel arbitration,<sup>111</sup> but the California Supreme Court denied the application insofar as it sought the arbitration of claims arising out of the California statute.<sup>112</sup> The California court ruled that only courts may determine such claims.<sup>113</sup> Finding that "Congress intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements,"<sup>114</sup> the United States Supreme Court held that state law bans on classes of claims violate the FAA.<sup>115</sup> The Court ruled therefore that the FAA preempted the California statute's prohibition of the arbitration of claims arising under the statute.<sup>116</sup>

*Southland* misinterpreted the FAA, which Congress intended to be a procedural statute applicable only to federal courts.<sup>117</sup> Never-

---

110. *See id.* at 4.

111. *See id.*

112. *See id.* at 5.

113. *See Keating v. Superior Court of Alameda County*, 31 Cal.3d 584, 627 (1982), *overruled by Southland Corp. v. Keating*, 465 U.S. 1 (1984). The court rejected the argument that the FAA preempts California's statutory requirement of judicial, rather than arbitral, determination of claims brought under the California Franchise Investment Law. *See id.* The court grounded its holding on the strength of California's public policy to protect investors as evidenced in a regulatory scheme, and on the similarity between California's policy to protect franchise investors and the federal policy to protect securities investors. *See id.* at 604.

114. *Southland*, 465 U.S. at 16.

115. *See id.*

116. *See id.* Justice Stevens took a more moderate view than the majority, asserting that the purpose of the FAA is to overcome judicial hostility toward arbitration agreements, not to deny the states the authority to legislate in the area of arbitration. *See id.* at 18-19 (Stevens, J., concurring in part and dissenting in part). He argued that state law limitations on the scope of arbitration agreements should not be per se unenforceable, if the limitations are based on strong public policy consistent with federal law. *See id.* at 21 (Stevens, J., concurring in part and dissenting in part).

117. Justice O'Connor, in a persuasive dissent joined by Justice Rehnquist, argued that the FAA, as enacted, was a procedural statute applicable to federal courts, and that Congress did not intend the FAA to apply to the states. *See id.* at 21-23 (O'Connor, J., dissenting). Justice O'Connor relied on the legislative history of the FAA. She cited, for example, the American Bar Association, which wrote: "[t]he statute establishes a procedure in the Federal courts for the enforcement of arbitration agreements . . . . A Federal statute providing for the enforcement of arbitration agreements does relate solely to procedure of the Federal courts." *Id.* at 26 (O'Connor, J., dissenting) (citing Committee on Commerce, Trade and Commercial Law, *The United States Arbitration Law and Its Application*, 11 A.B.A. J. 153, 154-55 (1925)). In addition, Julius Henry Cohen, who drafted the bill, informed two congressional subcommittees at a joint hearing that Congress, by enacting the FAA, was "'directing its own courts . . . . There is not disposition therefore by means of the Federal bludgeon to force an individual State into an unwilling submission to arbitration en-

theless, *Southland* advanced the policies highlighted in this Article. By prohibiting the arbitration of claims brought under the Franchise Investment Law, California law had created its own adjudicative monopoly. Annulling the statute vindicated the contractual right of parties to establish a private forum to decide such claims. *Southland* contracted the compass of state adjudicative power while expanding the scope of self-government.

The issue in *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University*<sup>118</sup> was more complex, for it concerned whether the Court would enforce a choice-of-law clause that operated to impose a stay of arbitration. In *Volt*, the parties to a construction contract entered into an arbitration agreement which included a California choice-of-law clause. When a dispute arose, Volt demanded arbitration.<sup>119</sup> In response, Stanford commenced an action in California state court against Volt, and in that action Stanford also sought indemnification from third parties that had not agreed to arbitrate their dispute with *Southland*.<sup>120</sup> Relying on the choice-of-law clause, Stanford moved to stay arbitration invoking a California statute, which permitted the court to stay arbitration pending resolution of a related, state court action involving parties not subject to arbitration.<sup>121</sup>

The Supreme Court correctly discerned no conflict between the FAA and the California statute.<sup>122</sup> The FAA preempts state law bans on arbitrating any category of claim, but it does not require adherence to particular procedural rules.<sup>123</sup> It therefore does not

---

forcement.’” *Id.* at 26-27 (O’Connor, J., dissenting) (citing Arbitration of Interstate Commercial Disputes, Joint Hearings on S. 1005 and H.R. 646 before the Subcommittees of the Committees on the Judiciary, 68th Cong., 1st Sess. 39-40 (1924)).

118. 489 U.S. 468 (1989).

119. *See id.* at 470.

120. *See id.* at 470-71.

121. *See id.* at 471. Volt petitioned the California appellate court to compel arbitration and to stay the California trial court litigation until arbitration was completed. *See id.* at 471 n.2.

122. *See id.* at 471 n.3.

123. *See id.* at 476.

There is no federal policy favoring arbitration under a certain set of procedural rules; the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate. Interpreting a choice-of-law clause to make applicable state rules governing the conduct of arbitration — rules which are manifestly designed to encourage resort to the arbitral process — simply does not offend the rule of liberal construction set forth in *Moses H. Cone*, nor does it offend any other policy embodied in the FAA.

*Id.* The Court added that the California statute furthered federal arbitration policy by providing sensible rules for multiparty contractual disputes. *See id.* at 476 n.5.

preempt state law governing arbitral procedures.<sup>124</sup> The Court recognized that the California law did not bar the arbitration of any disputes, but merely established procedural rules governing arbitration.<sup>125</sup> The parties, by incorporating a California choice-of-law clause into their contract, expressed their intent to submit to California's arbitral procedures.<sup>126</sup> Even if the result of their selection of California law was to stay arbitration, the parties' intent to follow California law determined the outcome.<sup>127</sup> The Court noted, in addition, that the California statute is consistent with the FAA because the statute provides a procedure for avoiding contradictory judgments that might arise if two parallel proceedings, one in arbitration and the other in court, proceeded simultaneously.<sup>128</sup> Such a sensible procedure might encourage arbitration.<sup>129</sup>

The California statute addressed in *Volt*, however, violates the thesis of this Article. Even if it provides a workable rule to avoid conflicting outcomes, the California statute establishes a mechanism for delaying arbitration and perhaps denying meaningful arbitration if the parallel court action decides arbitrable issues. This level of state interference potentially strips the parties of the power to create a private forum for dispute resolution. The incursion is procedural and subtle. While it does not outlaw the enforceability of a single arbitration agreement, and therefore conforms to the

---

124. See *id.* at 477 n.6. The Court distinguished *Southland v. Keating*, 465 U.S. 1, 16 n.10 (1984) on this basis. See also *Perry v. Thomas*, 482 U.S. 483, 490-91 (1987) (holding that the FAA preempts a California state statute precluding the arbitration of certain wage collection claims). The Court subsequently decided *Allied-Bruce Terminix Cos. v. Dobson*, 115 S. Ct. 834, 839 (1995) (holding that the FAA preempts an Alabama state statute invalidating all pre-dispute arbitration agreements). The *Allied-Bruce* Court also confronted the issue of whether the FAA's scope, which includes any contract evidencing a transaction "involving commerce," is co-extensive with the scope of the commerce clause which reaches transactions "affecting commerce." *Id.* The Court found the two provisions to be co-extensive. See *id.*

125. See 489 U.S. at 476-79.

126. See *id.*

127. See *id.* Joined by Justice Marshall, Justice Brennan noted that "[a]pplying the California procedural rule, which stays arbitration while litigation of the same issue goes forward, means simply that the parties' dispute will be litigated rather than arbitrated." *Id.* at 487 (Brennan, J., dissenting).

128. See *id.* at 476 n.5.

129. See *id.* (surmising that the California statute would foster arbitration because "the FAA itself contains no provision designed to deal with the special practical problems that arise in multiparty contractual disputes when some or all of the contracts at issue include agreements to arbitrate"). But see *id.* at 487 n.8 (Brennan, J., dissenting) (arguing that whether the California stay statute ultimately fosters arbitration is irrelevant, because the only pertinent issue is whether the California statute enforces arbitration agreements, as the FAA requires).

FAA, it nevertheless tends to place disputes otherwise destined for arbitration into the hands of the state.

If, however, parties to an arbitration agreement include a provision limiting the scope of arbitrable issues or remedies, or if they adopt procedures that may postpone or even foreclose arbitration, those provisions must be honored. Thus, the courts must enforce an express provision in the agreement, which, like the California statute, calls for a stay of arbitration. The arbitration agreement determines the scope of arbitration and the rules under which it is conducted. The state must enforce party intent.

Broader than current arbitration policy the arbitration policy proposed in this Article, would expressly nullify any state law restricting arbitration.<sup>130</sup> Such a policy would preempt the California law, and the parties' adoption of a choice-of-law provision therefore would not imply adoption of a California law expressly invalidated under principles of federal preemption.

More recently, in *Doctor's Associates, Inc. v. Casarotto*,<sup>131</sup> the Court concluded that special rules interfering with the enforcement of arbitration agreements violate the FAA. *Casarotto* concerned a special restriction on the form of arbitration agreements rather than a special restriction on the scope of arbitration agreements, as in *Southland*, or a special restriction on procedures applicable to arbitration, as in *Volt*. *Casarotto* purchased a Subway sandwich franchise from Doctor's Associates. The franchise agreement contained an arbitration clause.<sup>132</sup> When *Casarotto* brought suit against Doctor's Associates for breach of contract and various torts, Doctor's Associates sought to stay the proceedings pending arbitration.<sup>133</sup> *Casarotto* challenged the arbitration clause, because it failed to satisfy Montana law which required arbitration clauses to be "typed in underlined capitals on the first page of the contract."<sup>134</sup> The Supreme Court held that the FAA forbids special limitations on arbitration agreements, and that federal policy

---

130. To come within the reach of federal law, the arbitration agreement would have to affect interstate commerce. See 9 U.S.C. § 2 (1994); see also *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265 (1995) (holding that the reach of the FAA is co-extensive with the scope of the commerce clause).

131. 517 U.S. 681 (1996).

132. See *id.* at 683.

133. See *id.*

134. *Id.* The Montana statute provided more fully: "Notice that a contract is subject to arbitration . . . shall be typed in underlined capital letters on the first page of the contract; and unless such notice is displayed thereon, the contract may not be subject to arbitration." MONT. CODE ANN. § 27-5-114(4) (repealed 1997).

therefore preempted the Montana statute.<sup>135</sup> If the notice provision had applied to all contracts, it would have been enforceable, but because it applied only to arbitration agreements, it was unenforceable.<sup>136</sup>

The *Casarotto* decision relied on Section two of the FAA, which makes arbitration agreements as enforceable as other contracts.<sup>137</sup> Section 2 preserves the applicability of ordinary contract defenses to arbitration agreements, but it forbids the creation of defenses unique to arbitration. As *Casarotto* instructs, Section 2 prevents state law from disregarding the contractual intent of the parties by invalidating otherwise enforceable arbitration agreements. *Casarotto* also satisfies the thesis of this Article. If the Montana law were upheld, disputes earmarked for arbitration would be detoured to the courts, and the sphere of private adjudication would dwindle.

#### D. Threshold Issues

Even when no law blocks the arbitration of a particular claim, threshold issues of enforceability of the agreement may arise. A party may resist arbitration on the ground that assent to the agreement was fraudulently induced, coerced, or manipulated by someone in a position of trust. When a party interposes a defense assailing the validity of assent, the issue arises whether the court or the arbitrator should determine the validity of the defense.

Section 2 of the FAA provides, as it should, that arbitration agreements are subject to common law defenses.<sup>138</sup> If, for example, a party fraudulently induces another into an arbitration agreement, the aggrieved party should be permitted to present its contract defense to a court. By asserting a fraud defense, the aggrieved party has brought into question the validity of the arbitration agreement. If a party raises a threshold issue of enforceability, the arbitrator should not decide the issue, since the issue for decision impugns the very agreement that purportedly confers authority on him.

The FAA implies correctly that the court, not the arbitrator, decides threshold issues of enforceability. By stating that written ar-

---

135. See 517 U.S. at 686-88.

136. See *id.* at 686-87.

137. See Stephen J. Ware, *Arbitration and Unconscionability After Doctor's Associates, Inc. v. Casarotto*, 31 WAKE FOREST L. REV. 1001, 1012-13 (1996) (agreeing with the *Doctor's Associates* decision to affirm the "contractual approach" to enforcing arbitration agreements).

138. See *id.*

bitration agreements are enforceable “save upon such grounds as exist at law or in equity,”<sup>139</sup> Section 2 suggests that until the threshold issue of enforceability is resolved, the arbitration agreement is not enforceable. The court is therefore the proper tribunal to resolve the threshold issue. If the court finds fraud, the arbitration agreement fails; for the arbitrator never had authority to decide any issue, threshold or ultimate. If the court rejects the fraud defense, the matter proceeds to arbitration. Section 4 confirms that the court decides threshold issues.<sup>140</sup> That section provides that “[i]f the making of the agreement . . . be in issue, the court shall proceed summarily to the trial thereof.”<sup>141</sup> If, for example, a party interposes a fraud, incapacity, duress, or unconscionability defense, “the making of the agreement” is at issue, and the court, not the arbitrator, must determine the validity of the defense.

Reserving for the court the responsibility to make such rulings does not infringe on the parties’ freedom of contract. Nor does such a reservation of authority unduly expand governmental adjudicative power. If a party has an arguable contract defense to an alleged arbitration agreement, the state should not force that party to arbitrate any issues until the court has ruled the agreement valid. To compel arbitration prematurely would trample the aggrieved party’s freedom of contract.

The Supreme Court has abandoned the wisdom of the FAA, implementing misguided arbitration policy.<sup>142</sup> Thus, when fraud is an alleged defense to arbitrability (and, by analogy, when a party interposes any defense to arbitrability), the arbitrators, not the courts, decide the issue.<sup>143</sup> In *Prima Paint v. Flood & Conklin*

---

139. *Id.*

140. Section 4 of the FAA provides:

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court . . . for an order directing that such arbitration proceed in the manner provided for in such agreement . . . . The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement . . . . If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof.

9 U.S.C. § 4 (1994).

141. *Id.*

142. See *supra* note 94-96 and accompanying text (citing Supreme Court cases espousing pro-arbitration policy).

143. See *infra* notes 144-157 and accompanying text.

*Mfg.*,<sup>144</sup> *Prima Paint* and Flood & Conklin entered into a Consulting Agreement, which contained an arbitration clause.<sup>145</sup> When a dispute arose, Flood & Conklin served notice to arbitrate.<sup>146</sup> *Prima Paint* resisted arbitration asserting a fraudulent inducement defense.<sup>147</sup> The issue was whether the court or the arbitrators should decide if Flood & Conklin had fraudulently induced *Prima Paint* to sign the Consulting Agreement.<sup>148</sup> The Supreme Court held that the arbitrators should decide the issue,<sup>149</sup> adopting the "separability" doctrine.<sup>150</sup> Donning their magician's robes, a majority of Justices pretended that the fraud arguably invalidating a contract has no effect on the validity of an arbitration clause within the contract.<sup>151</sup>

The errant reasoning of *Prima Paint* applies by analogy to any contract defense.<sup>152</sup> If the defense does not apply specifically to the arbitration clause as opposed to the whole contract, the defense does not attach to the arbitration clause.<sup>153</sup> Rarely will predatory

---

144. 388 U.S. 395 (1967).

145. *Id.* at 398. The typical broad arbitration clause provided: "Any claim or controversy arising out of or relating to this Agreement, or the breach thereof, shall be settled by arbitration in the City of New York, in accordance with the rules then obtaining with the American Arbitration Association." *Id.*

146. *See id.*

147. *See id.* at 399. *Prima Paint* commenced an action in federal district court to enjoin arbitration. Flood & Conklin moved, pursuant to Section 4 of the FAA, to compel arbitration. *See id.*

148. *See id.*

149. *See id.* at 404.

150. *Id.* at 402. *See also* R.M. Perez & Assoc., Inc. v. Welch, 960 F.2d 534, 538-39 (5th Cir. 1992) (directing arbitrators to hear claims that securities client agreements and options agreements resulted from fraud where the alleged acts of fraud did not relate to the arbitration clauses per se).

151. *See* 388 U.S. at 402. The Court concluded that when a party alleges that fraud induced the contract as a whole the issue goes to the arbitrator. When, on the other hand, a party alleges that fraud attached specifically to the arbitration clause rather than the contract as a whole, the issue goes to the court. *See id.* at 402, 406-07. Justice Black dissented. He believed that the FAA makes enforceability issues subject to state law, *id.* at 412-15, and he found that under controlling New York law issues of arbitrability are for the court to decide. *See id.* at 425 (Black, J., dissenting). *See* Stephen J. Ware, *Employment Arbitration and Voluntary Consent*, HOFSTRA L. REV. 84, 131 (1996) (criticizing the *Prima Paint* decision for adopting the separability doctrine).

152. *See infra* notes 153-157 and accompanying text.

153. *See* C.B.S. Emp. Fed. Cr. Union v. Donaldson, 912 F.2d 1563, 1567 (6th Cir. 1990) ("The *Prima Paint* doctrine is not limited, however, to rescission based on fraudulent inducement, but extends to all challenges to the making of a contract." (quoting *Rhoades v. Powell*, 644 F. Supp. 645, 653 (E.D. Cal. 1986))); *Unionmutual Stock Life Ins. Co. v. Beneficial Life Ins. Co.*, 774 F.2d 524, 529 (1st Cir. 1985) ("The teaching of *Prima Paint* is that a federal court must not remove from the arbitrators consideration of a substantive challenge to a contract unless there has been an in-

conduct, such as duress or overreaching, focus specifically on an arbitration provision. Under *Prima Paint*, therefore, the determination of the validity of contract defenses enters the realm of arbitrability, even though the validity of the very agreement conferring authority on the arbitrator is at issue. In *Rojas v. TK Communications, Inc.*,<sup>154</sup> the Fifth Circuit relegated the issue of unconscionability to an arbitrator.<sup>155</sup> The plaintiff asserted a sexual harassment claim against her employer, and when the employer moved to dismiss the complaint on the ground that Rojas' employment agreement contained an arbitration clause, Rojas countered that the arbitration agreement was unconscionable.<sup>156</sup> The court ceded the unconscionability issue to the arbitrator, because Rojas challenged the entire contract, not the arbitration clause specifically.<sup>157</sup>

Despite *Prima Paint*, many courts, loathe to relinquish their authority to decide questions presented to them, simply rule on threshold issue of enforceability.<sup>158</sup> Unfortunately, most of these courts, in cases where unconscionability is interposed as a defense, uphold arbitration agreements despite distressing proof of overreaching and unfairness. Until a recent NASD rule change, courts

---

dependent challenge to the making of the arbitration clause itself. The basis of the underlying challenge to the contract does not alter the severability principle.”)

154. 87 F.3d 745 (5th Cir. 1996).

155. *See id.* at 749.

156. *See id.* at 746-47.

157. *See id.* at 749. The court noted that Rojas argued that her employer had misrepresented the terms of her employment agreement and that Rojas had alleged that her employer had had an undue bargaining advantage. *See id.* at 749 n.3. Because these arguments focused on the agreement as a whole, rather than on the arbitration clause specifically, the court referred the unconscionability issue to arbitration. *See id.* at 749. *See also* Satarino v. A.G. Edwards & Sons, Inc., 941 F. Supp. 609, 613 (N.D. Tex. 1996) (relying on *Rojas* and directing to arbitration the claim that an employment agreement of a securities firm employee was an unenforceable contract of adhesion).

158. *See, e.g.,* Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith Inc., No. 98-1246, 1998 WL 880910, \*21 (1st Cir. Dec. 22, 1998) (sustaining the mandatory arbitration of Title VII claims in securities industry); Webb v. Investacorp, Inc., 89 F.3d 252, 259 (5th Cir. 1996) (enforcing mandatory arbitration clauses in employment agreements between brokerage firm and employees because employees failed to prove fraud, duress or lack of appreciation for the consequences of arbitration clauses); Barrowclough v. Kidder Peabody, Inc., 752 F.2d 923, 937 (3d Cir. 1985) (enforcing mandatory arbitration clauses in employee agreements between brokerage firms and employees despite universal requirement of such clauses); Pierson v. Dean, Witter, Reynolds, Inc., 742 F.2d 334, 339 (7th Cir. 1984) (rejecting claim that mandatory arbitration clause in securities customer account agreement was unconscionable although accompanying choice-of-law clause implied waiver of right to punitive relief); *see* Dean, Witter, Reynolds, Inc. v. Sanchez Espada, 959 F. Supp. 73, 79 (D. Puerto Rico 1997) (stating that threshold issues of whether the parties entered into an arbitration agreement are for the courts).

routinely sustained mandatory arbitration clauses in employment contracts of securities employees, despite the requirement that securities employees had to sign contracts containing such clauses or not work in the industry.<sup>159</sup> Arbitration associations instruct arbitrators, tacitly or expressly, that they need not follow positive law,<sup>160</sup> and the prevailing standard of judicial review - the manifest disregard test - permits the court to vacate an award only if the arbitrator intentionally disregarded the law.<sup>161</sup> Forcing employees to arbitrate claims is oppressive.<sup>162</sup> Federal courts fail to apply common law defenses to arbitration agreements because the Supreme Court has distorted arbitration policy.<sup>163</sup> This failure results in the enforcement of arbitration agreements that courts should reject as unconscionable.

### E. Punitive Damages

Perhaps the most controversial issue in arbitration is whether punitive damages should be an available remedy. Although prohibi-

---

159. Mandatory arbitration of claims brought by securities employees "is an industry-wide practice, with no opportunity for individual modification." 140 CONG. REC. E1753-02 (daily ed. Aug. 17, 1994) (statement of Rep. Markey). See also NASD Code of Arb. Proc. § 1201 (CCH NASD Manual 1997, 1998) (amended by SR-NASD-97, eff. Jan. 1, 1999). But see SEC RULE 97-77 (June 22, 1998) (adopting the NASD's proposal to exempt claims of sexual or racial harassment and discrimination from mandatory arbitration); *Duffield v. Robertson Stephens & Co.*, 144 F.3d 1182, 1199 (9th Cir. 1998) (holding mandatory securities arbitration contrary to Title VII), cert. denied, 119 S. Ct. 445 (Nov. 9, 1998).

160. SROs, such as the NASD and NYSE, handle an enormous number of securities arbitrations. See Katsoris, *SICA: The First Twenty Years*, supra note 39, at 491. The Arbitrator's Manual, a handbook provided to all SRO arbitrators, says: "Arbitrators are not strictly bound by case precedent or statutory law. Rather, they are guided by their analysis, by the underlying policies of the law and are given wide latitude in their interpretation of legal concepts." THE ARBITRATOR'S MANUAL (Securities Industry Conference on Arbitration 27-28 (1996)) [hereinafter ARBITRATOR'S MANUAL].

161. See supra notes 97-103 and accompanying text (discussing and criticizing the manifest disregard test).

162. See Kenneth R. Davis, *The Arbitration Claws: Unconscionability in the Securities Industry*, 78 B.U. L. REV. 255, 259 (1998) (arguing that mandatory arbitration in the securities industry is unconscionable because arbitrators are not required to follow controlling law and courts do not correct legal error in arbitral awards). A vast body of federal case law, however, upholds mandatory arbitration agreements in the securities industry. *Schuetz v. CS First Boston Corp.*, 1997 U.S. Dist. LEXIS 11612 (S.D.N.Y. July 31, 1997) (gender discrimination); *Bender v. A.G. Edwards & Sons, Inc.*, 971 F.2d 698 (11th Cir. 1992) (sexual harassment); *Willis v. Dean, Witter, Reynolds, Inc.*, 948 F.2d 305 (6th Cir. 1991). The SEC has approved an NASD rule which eliminates the blanket requirement of mandatory arbitration of discrimination claims in the securities industry. SEC RULE 97-77 (June 22, 1998).

163. See supra notes 143-151 and accompanying text (discussing the Supreme Court's pro-arbitration policy).

tions against punitive damages are “special restrictions” on arbitration, the punitive damages issue has stirred so much interest that this Article treats the issue separately. The issue emerged in *Garrity v. Lyle Stuart, Inc.*,<sup>164</sup> in which an author alleged in arbitration that her publisher had maliciously refused to pay her royalties. Finding for the author, the arbitration panel awarded her compensatory and punitive damages.<sup>165</sup> The Court of Appeals vacated the punitive award, because the majority of the Court believed that only the state should wield the power to impose punitive remedies.<sup>166</sup> Writing for the majority, Chief Judge Breitel observed that the state, not private arbitrators, must serve as “the engine for imposing social sanction.”<sup>167</sup> Public policy, therefore, prohibited parties from delegating to arbitrators the power to punish.<sup>168</sup>

This public policy argument has enlisted support in several jurisdictions.<sup>169</sup> Its luster derives from the traditional role of the government as the agent of punishment. Criminal law is an exclusive

---

164. 40 N.Y.2d 354, 353 N.E.2d 793, 386 N.Y.S.2d 831 (1976).

165. *See id.* at 356.

166. *See id.* at 358.

167. *Id.*

168. *See id.* at 360 (Gabielli, J., dissenting). Justice Gabielli rejected the premise that arbitral awards of punitive damages violate public policy. *See id.* at 361. To support his view, he cited a recent Court of Appeals decision sustaining an arbitral award of treble liquidated damages, which he characterized as a penalty and therefore indistinguishable from punitive damages. *See id.* Because the award in *Garrity* was neither “irrational or unjust,” he would have confirmed it. *Id.* at 364.

169. *See, e.g.,* *McElroy v. Waller*, 731 S.W.2d 789, 792 (Ark. Ct. App. 1987) (applying Arkansas statute that forecloses arbitral punitive awards); *United States Fidelity & Guar. Co. v. DeFluiter*, 456 N.E.2d 429, 432 (Ind. Ct. App. 1983) (holding punitive damages unavailable in commercial arbitration); *Shaw v. Kuhnel Assoc., Inc.*, 698 P.2d 880, 882 (N.M. 1985) (following the *Garrity* rule). *But see* *Complete Interiors, Inc. v. Behan*, 558 So.2d 48 (Fla. Dist. Ct. App. 1990) (denying arbitrator the authority to award punitive damages unless the arbitration agreement expressly confers such authority); *Belko v. AVX Corp.*, 1988 Cal. LEXIS 862 (Dec. 8, 1988) (upholding implied agreement to authorize arbitral punitive awards); *but cf. Starkenstein v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 572 F. Supp. 189, 191-92 (M.D. Fla. 1983) (concluding that Florida law permits arbitrators to award punitive damages); *Baker v. Sadick*, 162 Cal. App. 3d 618 (1984) (permitting arbitrators to award punitive damages even without express authorization); *Rodgers Builders, Inc. v. McQueen*, 331 S.E.2d 726, 734 (N.C. Ct. App. 1985) (ruling that clause directing arbitration of claims arising out of contractual relationship impliedly authorized punitive awards); *Grisom v. Greener & Sumner Constr., Inc.*, 676 S.W.2d 709, 711 (Tex. Ct. App. 1984) (supporting rule that arbitrators have authority to award punitive damages unless the agreement divests them of such authority). *See generally* Kenneth R. Davis, *A Proposed Framework for Reviewing Punitive Damages Awards of Commercial Arbitrators*, 58 ALB. L. REV. 55, 62-65 (1994) (discussing *Garrity* and reviewing the different positions states have taken regarding the availability of punitive damages in commercial arbitration).

province of the state,<sup>170</sup> and although society values freedom of contract, public policy imposes limits on one's right to submit to punishment contractually. Courts will not enforce a private agreement in which a party has consented to be imprisoned or enslaved. Punitive damages, like criminal law, penalizes wrongdoers and deters misconduct.<sup>171</sup> The analogy between criminal law and punitive damages has led many to condemn punitive arbitral awards, which arguably represent a usurpation of the state's exclusive power to punish.<sup>172</sup>

*Garrity*, however, interferes with the social policies that arbitration serves. In regulating private arbitration, the state's only appropriate role is to enforce arbitration agreements according to the common law of contracts. In other words, the state must engage in the minimal amount of regulation necessary to achieve the intent of the parties to the agreement. Contract law embodies public policy limitations on agreements, such as agreements subjecting a

170. See JEROME HALL, *GENERAL PRINCIPLES OF CRIMINAL LAW* 321 (1947) (noting that only the state inflicts criminal punishment); WAYNE R. LAFAYE AND AUSTIN W. SCOTT, JR., *HANDBOOK ON CRIMINAL LAW* § 3, at 11 (1972) (remarking that "[w]ith crimes, the state itself brings criminal proceedings to protect the public interest").

171. See 1 JAMES D. GHIARDI AND JOHN J. KIRCHNER, *PUNITIVE DAMAGES, LAW AND PRACTICE*, § 2.01, at 1 (1998) (stating that punishment and deterrence are the objectives of punitive damages); 1 LINDA L. SCHLUETER AND KENNETH R. REDDEN, *PUNITIVE DAMAGES* § 2.2(A), at 28 (3d ed. 1995) (noting that the principal purposes of punitive damages are "to punish the defendant for his wrongdoing and to deter him and others from similar misconduct"); *RESTATEMENT (SECOND) OF TORTS* § 908(1) (1979) ("Punitive damages are damages, other than compensatory or nominal damages, awarded against a person to punish him for his outrageous conduct and to deter him and others like him from similar conduct in the future.").

172. See *Garrity v. Lyle Stuart, Inc.*, 40 N.Y.2d 354, 359, 353 N.E.2d 793, 796-97, 386 N.Y.S.2d 831, 834 (1976) (commenting that "[f]or centuries the power to punish has been a monopoly of the State"); *Shaw v. Kuhnelt & Assocs.*, 102 N.M. 607, 609 (Sup. Ct. 1985) (holding that the authority to award punitive damages "is reserved to the courts"); Ira P. Rothken, *Punitive Damages in Commercial Arbitration: A Due Process Analysis*, 21 *GOLDEN GATE U. L. REV.* 387, 404 (1991) (opposing punitive awards in arbitration because arbitrators are not restrained by the rigor of due process). Some even object to punitive damages in civil litigation. A vehement denunciation of punitive damages appears in a century-old New Hampshire case. "The idea [of punitive damages] is wrong. It is a monstrous heresy. It is an unsightly and unhealthy escrescence, deforming the symmetry of the body of the law." *Fay v. Parker*, 53 N.H. 342, 382 (1873). See also, *Murphy v. Hobbes*, 5 P. 119, 121 (Colo. 1884) (objecting to punitive damages because such relief obscures the distinction between criminal law and civil law and fails to afford procedural safeguards guaranteed in criminal prosecutions); Jerome Hall, *Interrelations of Criminal Law and Torts: I*, 43 *COLUM. L. REV.* 753, 757 (1943) (referring to Blackstone's distinctions between criminal law, which involves wrongs against the public, and tort law, which involves wrongs against the individual).

party to physical punishment or slavery. Moreover, contract law will not condone agreements induced by fraud, duress or other unconscionable means. Any limitation on the scope of arbitral issues beyond that point is excessive because it intrudes upon the unique benefits of the arbitration agreement: promoting autonomy and cooperation, while limiting governmental adjudicative power over civil disputes.

When analyzed under this model, the *Garrity* argument loses persuasiveness.<sup>173</sup> *Garrity* stands on the assumption that the government's monopolistic power to impose punishment strips arbitrators of the authority to award punitive damages. The ubiquitous hand of the state reaches into the arbitral hearing room and reclaims its rightful position as the exclusive agent of punishment. Any state policy to increase or even to maintain governmental power in the field of dispute resolution, however, contradicts the social policies supporting arbitration. The core of arbitral policy should be limiting, not perpetuating, governmental power.<sup>174</sup>

If awarding punitive damages in arbitration wrenched jurisdiction from the criminal courts, one might accept the *Garrity* rationale and weigh the benefits of the rule against the damage that the rule would cause to arbitration policy. Punitive damages, however, have never resided in the province of criminal law; rather, such damages have always been a civil remedy.<sup>175</sup> Though the law dif-

---

173. Commentators have criticized *Garrity* on numerous grounds. See, e.g., Thomas J. Stipanowich, *Punitive Damages in Arbitration: Garrity v. Lyle Stuart, Inc. Reconsidered*, 66 B.U. L. REV. 953, 959 (1986) (excoriating *Garrity* as "an anomaly, frustrating the goals of fairness and finality that are the essence of arbitration and undermining the valuable role that punitive damages play in deterring fraudulent or malicious conduct"); Richard P. Hackett, Note, *Punitive Damages in Arbitration: A Search for A Workable Rule*, 63 CORNELL L. REV. 272, 300 (1978) (predicting that the inflexibility of the *Garrity* rule will ultimately aggravate the inefficiencies the rule attempted to resolve).

174. One commentator suggests that the historical prevalence of arbitration, which has for centuries imposed punishment, refutes the proposition that punishment is an exclusive function of the state. See Stephen J. Ware, *Punitive Damages in Arbitration: Contracting out of Government's Role in Punishment and Federal Preemption of State Law*, 63 FORDHAM L. REV. 529, 563 (1994). Regardless of whether the state holds a monopoly over the power to punish, the question is whether the state should, for public policy reasons, wield the power to impose punitive relief to the exclusion of arbitrators. The social policy supporting arbitration rejects reserving such power to the state.

175. See *Gertz v. Robert Welch, Inc.*, 418 U.S. 323, 350 (1973) (recognizing that punitive damages "are private fines levied by civil juries"); Malcolm E. Wheeler, *The Constitutional Case for Reforming Punitive Damages Procedures*, 69 VA. L. REV. 269, 273 (1983) (defining punitive damages as penalties imposed by civil judgment to punish and deter wrongdoers).

fers from state to state, civil juries throughout the country award punitive relief in appropriate tort cases.<sup>176</sup> Some states require reckless disregard for the welfare of others, while others require willful misconduct or even malice.<sup>177</sup> Many states permit punitive awards for strict products liability torts where the defendant showed reckless disregard for the safety of customers and the public.<sup>178</sup> Nearly all the states, however, recognize punitive damages as a tort remedy.<sup>179</sup> Since arbitration substitutes for civil litigation, remedies available in court should be available to arbitrators.<sup>180</sup> Constricting the scope of arbitral remedies would cede power to the state and diminish one of the principal functions of arbitration — the limitation of governmental adjudicative power over civil disputes.

Judge Breitel supported his public policy argument against arbitral punitive awards by pointing out in *Garrity* that arbitration is “manipulatable by the party in a superior bargaining position.”<sup>181</sup> One party may force the other into the agreement, and the stronger party may corrupt the process. Such abuse undoubtedly occurs, but the proper response is to invalidate unconscionable arbitration agreements, not to impose blanket restrictions on all arbitration agreements, even those not tainted with impropriety.

Finally, the narrow standard of judicial review of arbitration awards concerned Judge Breitel.<sup>182</sup> Excessive and unsupportable awards might elude correction.<sup>183</sup> Although awards are sometimes unjust, the remedy, again, is not to deny parties their freedom of

176. See *infra* notes 176-79 and accompanying text (discussing the current state law of punitive damages).

177. See GHIARDI & KIRCHNER, *supra* note 171, § 5.01, at 3-8 (summarizing the standards in each state for the imposition of punitive damages).

178. See SCHLUETER & REDDEN, *supra* note 170, at 528 (pointing out that most states permit punitive awards in strict products liability cases for reckless or outrageous conduct, a standard which borders on intentional tort); GHIARDI & KIRCHNER, *supra*, note 171, at 6-12 to 6-13 (commenting that, although punitive damages, which are based on willful misconduct, seem inapplicable in strict products liability cases, most courts allow the imposition of punitive damages in such cases).

179. See GHIARDI & KIRCHNER, *supra* note 170, Table 4-1, at 48-52 (showing the positions that all the fifty states take on the availability of punitive damages as a civil remedy).

180. See Constantine N. Katsoris, *The Betrayal of McMahon*, 24 FORDHAM URB. L.J. 221, 229 (1997) (arguing that arbitrators should have authority to award all the relief that civil courts may grant).

181. *Garrity*, 40 N.Y.2d at 358.

182. See *id.* at 358 (fearing that if arbitrators were permitted to award punitive damages, arbitration would degenerate into “a trap for the unwary given the eminently desirable freedom from judicial overview of law and facts”).

183. See *id.*

contract, but rather to adjust the scope of review to comport with the intent of the parties.<sup>184</sup>

If an agreement implies judicial review for legal error, the court may correct such error and avoid unjust awards.<sup>185</sup> An arbitration agreement implies judicial review when the complainant brings particular statutory claims to arbitration or when the parties have included a choice-of-law clause in the agreement. In either case, they have instructed the arbitrator to apply particular substantive law, and should the arbitrator fail to do so correctly, the court may, on appropriate motion, vacate the award.

If the parties, without adopting a choice-of-law clause, arbitrate a claim ordinarily classified as a common law cause of action, the arbitrator, under customary arbitration practice, may rely on his own sense of justice. In such a case, the court may not review an award for substantive error, because the arbitrator, not bound by substantive law, has not erred by using his discretion rather than any particular legal principles. Arbitrators, however, never have license to abdicate reason. An award of one million dollars for the simple breach of a contract causing no loss whatsoever, is subject to vacatur on the ground that the award is unreasonable.<sup>186</sup> A party would not, and could not as a matter of public policy, subject itself to the caprices of renegade or irrational arbitrators. Under this approach to review, the judiciary intervenes only to the extent

---

184. See *supra* notes 97-104 and accompanying text (discussing judicial review of arbitral awards).

185. See Davis, *Judicial Review*, *supra* note 4, at 123-29 (discussing the scope of judicial review implied in arbitration agreements).

186. Many courts apply the test of rationality to review arbitration awards. See, e.g., *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1060 (9th Cir. 1991) (confirming rationally supported arbitration award); *Advest, Inc. v. McCarthy*, 914 F.2d 6, 9 n.6 (1st Cir. 1990) (applying the standard of rationality to test arbitration award); *Jenkins v. Prudential-Bache Securities, Inc.*, 847 F.2d 631, 634 (10th Cir. 1988) (following rationality test to review arbitration award); *French v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 784 F.2d 902, 906 (9th Cir. 1986) (confirming award not evidencing "complete irrationality"); *Swift Indus., Inc. v. Botany Indus., Inc.*, 466 F.2d 1125, 1134-35 (3d Cir. 1972) (vacating irrational award); *Clemons v. Dean Witter Reynolds, Inc.*, 708 F. Supp. 62, 64 (S.D.N.Y. 1989) (remanding case to arbitrators for explanation of how damages were calculated); *McLaughlin, Piven, Vogel, Inc. v. Gross*, 699 F. Supp. 55, 58 (E.D. Pa. 1988) (confirming award challenged for factual conclusions rather than for irrationality), *aff'd*, 862 F.2d 308 (3d Cir. 1988); *Sargent v. Paine Webber, Jackson & Curtis, Inc.*, 674 F. Supp. 920, 922-23 (D.D.C. 1987) (remanding case to arbitrators because award showed no support for its conclusions); *Prudential-Bache Securities, Inc. v. Caporale*, 664 F. Supp. 72, 74-75 (S.D.N.Y. 1987) (confirming award not sufficiently irrational to justify vacatur); *Lentine v. Fundaro*, 29 N.Y.2d 382, 385-86, 278 N.E.2d 633, 635, 328 N.Y.S.2d 418, 421-22 (1972) (adopting the "completely irrational" standard).

necessary to effect the contractual intent of the parties, not to substitute its judgment for that of the arbitrators.

*Garrity* conflicts with the arbitration policy proposed in this Article. *Garrity*, however, does not conflict with the FAA.<sup>187</sup> Congress passed the Act to overcome the legacy of judicial antipathy toward arbitration.<sup>188</sup> The FAA did not seek to insure that punitive remedies would be available in arbitration. The House Report on the bill destined to become the FAA declared that “the purpose of the bill is to make valid and enforceable agreements for arbitration . . . .”<sup>189</sup> As the Seventh Circuit has recognized:

We think the policy favoring arbitrability applies with less force when there are doubts concerning the availability of punitive remedies — as opposed to the scope of arbitral issues . . . . Just as the FAA does not favor or disfavor arbitration under a particular set of rules, neither does it favor or disfavor any particular type of remedy.<sup>190</sup>

In *Mastrobuono v. Shearson Lehman Hutton, Inc.*,<sup>191</sup> the Supreme Court cast doubt on the vitality of *Garrity*, though it did not hold that the FAA preempts the *Garrity* rule.<sup>192</sup> The Mas-

187. Unfortunately, the Supreme Court has frequently misinterpreted the congressional policy embodied in the FAA.

188. See *supra* note 57 and accompanying text (discussing the ouster-of-jurisdiction doctrine).

189. H.R. REP. NO. 96, 68th Cong., 1st Sess. 1 (1924). The report continues that the purpose of the bill is to place “[a]n arbitration agreement . . . on the same footing as other contracts, where it belongs.” *Id.*

190. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 20 F.3d 713, 718 (7th Cir. 1994), *rev’d*, 514 U.S. 52 (1996).

191. 514 U.S. 52 (1996). Even before the Supreme Court decided *Mastrobuono*, circuit courts had held predominantly that the FAA’s pro-arbitration policy argues in favor of interpreting arbitration agreements to vest arbitrators with the authority to award punitive damages. See, e.g., *Lee v. Chica*, 983 F.2d 883, 887-88 (8th Cir. 1993) (sustaining punitive award in securities arbitration); *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1062-63 (9th Cir. 1991) (sustaining punitive award in arbitration of fraud claim arising from breach of contract to repair cruise ship); *Raytheon Co. v. Automated Business Sys., Inc.*, 882 F.2d 6, 11-12 (1st Cir. 1989) (sustaining punitive award in arbitration of claims arising from breach of exclusive dealership agreement); *Bonar v. Dean Witter Reynolds, Inc.*, 835 F.2d 1378, 1387 (11th Cir. 1988) (sustaining punitive award in securities arbitration); *Willoughby Roofing & Supply Co. v. Kajima Int’l, Inc.*, 598 F. Supp. 353, 357 (N.D. Ala. 1984) (sustaining punitive award in arbitration of claims arising from willful breach of construction contract), *aff’d per curiam*, 776 F.2d 269 (11th Cir. 1985). *But see Barbier v. Shearson Lehman Hutton, Inc.*, 948 F.2d 117, 122 (2d Cir. 1991) (vacating punitive award in securities arbitration).

192. See *Mastrobuono*, 514 U.S. at 63-64. Universally required in retail securities account agreements, the arbitration clause in *Mastrobuono* may have been unconscionable. The Court, however did not address the issue. Even had the Court considered the issue of unconscionability, it would surely have rejected the

trobuonos, clients of Shearson, entered into a standard-form securities trading agreement, which contained an arbitration clause and a choice-of-law clause adopting the law of New York. When the Mastrobuonos filed a federal action alleging account mismanagement, Shearson moved successfully to compel arbitration before the NASD.<sup>193</sup> Shearson argued at the arbitration hearing that the *Garrity* rule applied by operation of the choice-of-law clause and that the panel therefore lacked authority to grant punitive relief.<sup>194</sup> The panel nevertheless awarded the Mastrobuonos \$400,000 in punitive damages.<sup>195</sup>

The Supreme Court had two clear alternatives. It might have held that the FAA preempts *Garrity*, although such a holding would have misconstrued the FAA, which simply makes arbitration agreements enforceable but does not require the availability of particular forms of relief such as punitive damages. The Supreme Court, on the other hand, might have correctly applied the FAA and reversed the punitive award because the arbitration agreement adopted the *Garrity* rule. Rejecting both possibilities, the Court misconstrued the agreement and upheld the award.<sup>196</sup> Although the choice-of-law clause, a term in the parties' agreement, gave effect to the *Garrity* rule, the Court would not enforce the clause.<sup>197</sup> The Court reached this dubious conclusion despite the *Volt* decision, which had affirmed a stay of arbitration resulting from the enforcement of a California choice-of-law clause.<sup>198</sup> As *Volt* held, federal arbitration policy does not require the application of any

---

unconscionability argument. Despite the policy of the FAA, the Court grants indulgences to arbitration agreements not afforded other contracts. *See supra* note 68 and accompanying text (discussing the Supreme Court's pro-arbitration policy).

193. *Mastrobuono*, 514 U.S. at 54. The Mastrobuonos also asserted claims against the person who managed their account. *See id.*

194. *See id.*

195. *See id.* The compensatory award was \$159,327. Respondents paid the compensatory award, but moved in district court to vacate the punitive award. *See id.* The district court vacated the award and the Seventh Circuit affirmed. *See id.* Both courts held that the choice-of-law clause denied the arbitration panel the authority to award punitive damages. *See id.* at 54-55.

196. *See id.* at 55.

197. In *Volt Information Sciences, Inc. v. Leland Stanford Junior Univ.*, 489 U.S. 468 (1989), the Court enforced a choice-of-law provision which resulted in the stay of arbitration. Justice Thomas argued in his dissenting opinion in *Mastrobuono* that *Volt* was indistinguishable from *Mastrobuono*. *Mastrobuono*, 514 U.S. at 64-67 (Thomas, J. dissenting).

198. 489 U.S. at 475.

particular rules (and by analogy the availability of any particular remedies) in arbitration.<sup>199</sup>

The Supreme Court in *Mastrobuono* rationalized its refusal to enforce the choice-of-law clause, not by preempting *Garrity*, but by engaging in a strained analysis of the parties' agreement. The Court seized upon an NASD rule, which merely instructs arbitrators to disclose in the arbitration award "the damages and other relief awarded," extracting from this rule a phantom authorization for arbitrators to award punitive damages.<sup>200</sup> The Court also relied upon the Arbitrator's Manual, an unofficial handbook provided to all NASD arbitrators to familiarize them with the arbitral process. The NASD does not provide the parties with a copy of the manual.<sup>201</sup> Although the manual suggests to arbitrators that they may award punitive damages, the manual was not incorporated, expressly or impliedly, into the *Mastrobuono*'s client agreement.<sup>202</sup> Yet the Court negated the effect of the choice-of-law clause and held that the parties intended to authorize the panel to award punitive damages.<sup>203</sup>

Embellished with the trappings of contract analysis, the ruling in *Mastrobuono* rested on the Court's misperception of the FAA.<sup>204</sup> The Court announced, as it had in the past, that the FAA favors

---

199. *See id.*

200. *Mastrobuono*, 514 U.S. 52 (1996). Justice Thomas, in a dissenting opinion, pointed out that this rule, rather than conferring authority on arbitrators to grant any particular form of relief, merely describes the form of the award. *See id.* at 68.

201. *See id.* at 61. The Arbitrator's Manual provides: "The issue of punitive damages may arise with great frequency in arbitrations. Parties to arbitration are informed that arbitrators can consider punitive damages as a remedy." *See* ARBITRATOR'S MANUAL 26-27 (1992).

202. *Mastrobuono*, 514 U.S. at 69 (Thomas, J., dissenting).

203. The Court invoked the rule of contract construction known as *Contra Proferentem*. *See id.* at 62. This rule states that if analysis of the entire contract in which an ambiguous term appears does not reveal the probable meaning of the ambiguous term, the term should be construed against the party that drafted it. *See* CORBIN, *supra*, note 51, at 262 (stating that *Contra Proferentem* applies only if the meaning of the ambiguous term is in doubt "[a]fter applying all of the ordinary processes of interpretation" and "admitt[ing] in evidence . . . all the relevant circumstances and communications between the parties"). The Court should not have resorted to this rule of construction, because the choice-of-law clause resolved any question as to the availability of punitive relief. *See* Kenneth R. Davis, *Protected Right or Sacred Rite: The Paradox of Federal Arbitration Policy*, 45 DEPAUL L. REV. 65, 82 (1995) (discussing the contrived contract analysis of the *Mastrobuono* Court).

204. *Mastrobuono*, 514 U.S. at 57. The Court declared that "the FAA's pro-arbitration policy does not operate without regard to the wishes of the contracting parties." *Id.* This curious formulation of arbitration policy suggests that party intent is merely a secondary concern of federal arbitration policy. Satisfying party intent, however, is the primary objective of the FAA. *See* 9 U.S.C. § 2 (1994).

the expansive interpretation of arbitration clauses, implicitly abandoning contract principles that might limit the scope of arbitrable issues.<sup>205</sup> Codified in the FAA, federal policy, however, simply enforces arbitration agreements as written.<sup>206</sup> The FAA does not favor the inclusion of particular remedies in arbitration. Though the *Mastrobuono* Court purported to apply contract principles, it distorted those principles to arrive at the desired result - confirmation of the award.<sup>207</sup>

If the FAA had adopted a broader policy favoring arbitration — the policy proposed in this Article — the *Mastrobuono* Court might have arrived at a more advantageous result and declared *Garrity* preempted. Denying parties the right to confer arbitrators with the authority to award punitive damages, as the *Garrity* rule does, forces the machinery of state adjudicative power on the parties, because such a mandatory rule confers on the state the exclusive power to award punitive relief. Such a rule interferes with self-government, one of the overarching benefits of arbitration agreements.

### Conclusion

The state hungers for power. The business of government is to get it, use it, and expand it. Contract offers a tool to carve out private spheres of control, areas beyond the reach of the state. By contracting, parties establish the rules that govern their economic relationships. The arbitration agreement is such a tool, wresting the power to adjudicate civil disputes from the state and conferring that power on the parties to the agreement. Other forms of alternative dispute resolution — negotiation, mediation, and settlement — are invaluable in resolving disputes, but none carries the unique benefits of arbitration. If negotiation fails to result in settlement,

---

205. *Mastrobuono*, 514 U.S. at 63.

206. 9 U.S.C. § 2 (1994). Since *Mastrobuono*, the vitality of the *Garrity* rule in New York has come into question. See *Mulder v. Donaldson, Lufkin & Jenrette*, 224 A.D.2d 125, 648 N.Y.S.2d 535 (N.Y. App. Div. 1996) (declaring that punitive arbitration awards are proper unless prohibited expressly in the arbitration agreement). See Dominic Bencivenga, *Securities Arbitration: 'Garrity' Rejected in Punitive Damages Ruling*, N.Y. L.J., Oct. 17, 1996, at 5 (predicting that *Garrity* will not survive *Mastrobuono*).

207. One of the Court's most dubious arguments mischaracterized the choice-of-law clause "merely as a substitute for the conflict-of-laws analysis" that would otherwise apply in the event of a contract dispute. *Mastrobuono*, 514 U.S. at 59. The Court concluded from this strained assumption that "[i]n such event, there would be nothing in the contract that could possibly constitute evidence of an intent to exclude punitive damages claims." *Id.*

the dispute goes on. Mediation does not bind the parties. When the mediator leaves the room, the dispute remains, and unless the parties settle, a compulsory solution is necessary. Settlement is desirable, but heated disagreements resist compromise.

Arbitration substitutes for litigation; it provides an alternative forum where an insoluble controversy finds binding resolution. It is, however, more than a practical alternative to litigation — a time and money saver. Parties enter pre-dispute agreements anticipating the possibility of conflict. At this early point, the contractual interests of both are in harmony and cooperation is easily achieved. After a dispute has arisen, arbitration reconciles autonomy and cooperation, though the two seem incompatible in the face of controversy. The common desire for swift and affordable justice motivates the quarreling parties to agree on a binding method for resolving their dispute — an adversarial proceeding without extensive state involvement.

The unique feature of arbitration is limited state involvement in civil adjudication. The state, however, has a substantial role in the arbitral process. The courts must enforce freely negotiated arbitration agreements, while refusing to enforce illegal and unconscionable ones. In addition, the courts must review awards to insure that arbitrators meet the expectations of the parties. Any other state involvement is too much.

Although the FAA substantially, if imperfectly, promotes these policies, the Supreme Court has strayed radically from them. As if on a see-saw, the Court intervenes too much or too little, rarely finding the proper balance. The Court once embraced the public policy defense to arbitration, frustrating the intent of parties to arbitrate claims arising under federal statute. Now the imperial guard of arbitration refuses to allow the lower courts to monitor arbitration agreements, even when court intervention is necessary to effect party intent. When the Supreme Court becomes sensitive to the social policies that arbitration serves, arbitration will assume an even more central role in balancing the power of government with the rights of the individual.