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# ARBITRATION UNBOUND?: THE LEGACY OF McMAHON\*

Bruce M. Selya<sup>†</sup>

## INTRODUCTION

In Shelley's rendition of the Prometheus legend, the Greek god passes a torch of fire to Mankind in order to free humanity from the failed rule of a pantheon of spiteful deities.<sup>1</sup> Acting in what appears to have been a kindred spirit, the Supreme Court, in *Shearson/American Express, Inc. v. McMahon*,<sup>2</sup> authorized the securities industry to substitute the free-form liteness of arbitration for the weary rituals of adjudication, thereby carving out an escape route from Law's Dominion. While it was not love at first sight,<sup>3</sup> the securities industry came to embrace the concept. The industry's ardor for arbitral solutions has not since waned—romances have a tendency to last despite increased awareness of a loved one's flaws—but it is fair to say that the perceived advantages of arbitration over adjudication have diminished. Thus, as *McMahon*'s tenth anniversary approaches, it is appropriate to ask if the securities industry's marriage to legal privatization is headed for the rocks.

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<sup>1</sup> PERCY BYSSHE SHELLEY, *PROMETHEUS UNBOUND* (1819).

<sup>2</sup> 482 U.S. 220, *reh'g denied*, 483 U.S. 1056 (1987).

<sup>3</sup> See, e.g., George H. Friedman, *Changes in Rules on Securities Cases*, N.Y. L.J., Aug. 5, 1993, at 3, 28 (crediting *McMahon* with fanning the flames of affection for arbitration within the securities industry, though not producing instant enthusiasm for it).

Part I of this Article chronicles the Supreme Court's pilgrimage from atheism to evangelism with respect to securities arbitration and posits that *McMahon* inaugurated a new era in the handling of securities disputes. Part II considers the extent to which the passing of the torch to securities arbitrators has succeeded in liberating investors and brokerage houses from the shackles of civil litigation. It begins by investigating the conditions that spawned the push for arbitration and then concludes that the new freedom, securities arbitration, is coming to resemble the old tyranny, conventional adjudication. Part II also explores some of the possible systemic reasons for this development. Part III posits that we should become increasingly worried about the future of securities arbitration, as too many of the reforms that have been proposed for the industry threaten to push arbitration further toward the litigation model. Part IV discusses the consequences of these trends, suggesting that securities arbitration, in its current evolution, faces a substantial threat to its continued independence: it may become so similar to litigation as to cease to be a viable alternative to the courts. If this happens, the courts' own alternative dispute resolution ("ADR") systems may expand to fill the space that the arbitrators have abandoned.

Finally, Part V suggests the following: that privately sponsored securities arbitration is a desirable alternative to adjudication, and that society benefits from having multiple options available. To avoid undermining this duality, however, securities arbitration must return to its mission as an efficient alternative dispute resolving mechanism rather than recasting itself as a cheap copy of the courts.

## I. THE PROMETHEAN GESTURE

An historic perspective on the case law lays bare the framework of the debate. The acceptability vel non of securities arbitration as an alternative to the courts has closely followed the zeitgeist of the era in which the question arose. When the Supreme Court first addressed the matter in *Wilko v. Swan*,<sup>4</sup> public confidence in our principal social institutions, including

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<sup>4</sup> 346 U.S. 427 (1953), *overruled* by *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989).

the courts, was relatively high, and post-Depression suspicion of the private sector continued to ferment. In hindsight, we see the *Wilko* Court, flush with memories of the multifarious abuses perpetrated by the securities industry in the Roaring Twenties, struggling to reconcile the New Deal investor protections contained in the Securities Act of 1933 with the policy choices of the earlier laissez faire Congress that enacted the Federal Arbitration Act of 1925 (the "FAA").

In *Wilko*, an investor signed a margin agreement in which he consented to forgo the opportunity to sue in the event a dispute arose, agreeing instead to submit any claims against the broker to binding arbitration.<sup>5</sup> The Court faced an apparent conflict: In the Securities Act, Congress created a right of action for investors to sue brokerage houses that engaged in deceptive sales practices, and, in the bargain, it resolutely declared that waivers of the Act's protections would be impuissant;<sup>6</sup> earlier, however, Congress had enacted the FAA to permit parties to settle their disputes rapidly and cheaply in an arbitral forum.

In attempting to reconcile the competing centrifugal and centripetal forces that pushed and pulled these statutory schemes, the Court expressed its deep mistrust of industry-sponsored arbitration, notwithstanding the evident purpose of the FAA. While acknowledging that Congress had placed its imprimatur on private arbitration as an acceptable alternative to the "complications of litigation,"<sup>7</sup> the Court refused to pay blind obeisance to that seal of approval. It concluded instead that the policies of the FAA should be subrogated to those of the Securities Act and that the protections of the latter would be "lessened in arbitration as compared to judicial proceedings."<sup>8</sup>

The *Wilko* Court proffered several reasons for its jaundiced view of arbitral venues. First, the Justices remarked on the securities industry's sordid past and noted that, unlike commercial arbitration—which typically pitted parties of relatively equal bargaining power against each other before an industry

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<sup>5</sup> *Id.* at 435.

<sup>6</sup> *Id.* at 428-30.

<sup>7</sup> *Id.* at 431.

<sup>8</sup> *Id.* at 435.

arbitrator—securities arbitration (not a new phenomenon when the *Wilko* Court studied the question) usually involved a battle between small investors and large corporate entities in a forum controlled by the industry.<sup>9</sup> Relatedly, the Court observed that securities arbitration differed from commercial arbitration in that the former often required findings on the state of mind of an alleged wrongdoer whereas the latter usually needed nothing more subtle than a determination of the amount of money due under a contract or the quality of a commodity.<sup>10</sup>

Second, the Court noted the widespread practice of arbitrators to announce results unaccompanied by written opinions.<sup>11</sup> This praxis, the Court mused, made it likely that the law would cease to grow in the securities area, creating a substantial probability that arbitrators would apply inconsistent standards to different cases. Finally, the Court pointed out the difficulty of performing meaningful appellate review of an arbitral decision given the absence of either a written opinion or a developed record.<sup>12</sup> The *Wilko* Court feared that, if securities arbitration became the norm, congressional intent would be thwarted as no rule of law would limit the avarice of the securities industry. Accordingly, the Court found the preservation of the choice of a judicial forum essential to vindicating rights under the Securities Act. In other words, the industry-specific policies of the Securities Act trumped the FAA's more broadly focused policies favoring private agreements to arbitrate disputes. Therefore, the Court held that predispute arbitration agreements comprised invalid waivers of the protections conferred by the Securities Act.

Lower federal courts extended the *Wilko* principle over the next three decades to encompass various other claims arising under not only the Securities Act but also the Securities Exchange Act of 1934, which contains a similar nonwaiver provi-

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<sup>9</sup> *Wilko*, 346 U.S. at 435.

<sup>10</sup> *Id.* at 435-36.

<sup>11</sup> *Id.* at 436. Justice Jackson noted in his concurrence that presumably agreements to submit disputes to arbitrators *after* a dispute arose would be enforceable. See *id.* at 438. Subsequent courts so held. See C. Edward Fletcher III, *Privatizing Securities Disputes Through the Enforcement of Arbitration Agreements*, 71 MINN. L. REV. 393, 420 n.193 (1987) (collecting cases). Today, the overwhelming majority of disputes proceed to arbitration under the guise of a predispute arbitration agreement.

<sup>12</sup> *Wilko*, 346 U.S. at 436.

sion<sup>13</sup> and the Age Discrimination in Employment Act ("ADEA").<sup>14</sup> Employing somewhat different reasoning, but relying to a certain degree on *Wilko's* wary attitude toward arbitration, federal courts also refused to allow arbitrators to decide Title VII,<sup>15</sup> ERISA,<sup>16</sup> and antitrust claims.<sup>17</sup>

The Supreme Court revisited the issue of arbitration in the securities context in *Scherk v. Alberto-Culver Co.*<sup>18</sup> There, the Court permitted a claim under the Exchange Act to proceed to arbitration. The *Scherk* Court distinguished *Wilko* on the ground that the dispute sub judice involved an international securities transaction raising conflict-of-law problems not associated with domestic securities transactions.<sup>19</sup> The *Scherk* Court classified the arbitration clause as a "specialized kind of forum selection clause that posits not only the situs of suit but also the procedure to be used in resolving the dispute."<sup>20</sup> To permit a party to "repudiate its solemn promise" to adhere to such a forum selection clause would "reflect a 'parochial concept that all disputes must be resolved *under our laws and in our courts* . . . ."<sup>21</sup> *Scherk*, fairly read, is a harbinger of changing attitudes.

A pair of cases heard during the 1984-85 Term furnished an occasion for further reflection on the value of arbitration in the securities context. In *Dean Witter Reynolds, Inc. v. Byrd*,<sup>22</sup> the Supreme Court held that a securities dealer could compel a customer to submit pendent state law claims (not themselves subject to a statutory nonwaiver prohibition) to arbitration

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<sup>13</sup> See, e.g., *Smoky Greenhaw Cotton Co. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 720 F.2d 1446, 1448 (5th Cir. 1983), cert. denied, 482 U.S. 928 (1987); *Stockwell v. Reynolds & Co.*, 252 F. Supp. 215, 220 (S.D.N.Y. 1965); see also Jeffrey W. Stempel, *Pitfalls of Public Policy: The Case of Arbitration Agreements*, 22 ST. MARY'S L.J. 259, 286 (1990).

<sup>14</sup> See, e.g., *Nicholson v. CPC Int'l, Inc.*, 877 F.2d 221, 230 (3d Cir. 1989).

<sup>15</sup> See, e.g., *Alexander v. Gardener-Denver Co.*, 415 U.S. 36, 44-45 (1974).

<sup>16</sup> See, e.g., *Lewis v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 431 F. Supp. 271, 275-78 (E.D. Pa. 1977).

<sup>17</sup> See, e.g., *American Safety Equip. Corp. v. J.P. Maguire & Co.*, 391 F.2d 821, 826-28 (2d Cir. 1968).

<sup>18</sup> 417 U.S. 506, reh'g denied, 419 U.S. 885 (1974).

<sup>19</sup> *Id.* at 515-18.

<sup>20</sup> *Id.* at 519.

<sup>21</sup> *Id.* (quoting *Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 9 (1972) (emphasis supplied)).

<sup>22</sup> 470 U.S. 213 (1985).

even though the related federal law claims had to proceed to adjudication. Ironically, the Court premised this ruling on its conclusion that upholding the arbitration clause in this manner served to advance the FAA's central policy of enforcing private agreements to arbitrate legal claims,<sup>23</sup> a thought process that blithely overlooked the creation of parallel (and essentially duplicative) litigation in contravention of the very policies of efficiency and economy that the FAA was designed to promote. On somewhat similar grounds, the Court in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,<sup>24</sup> upheld the validity of an agreement to arbitrate antitrust disputes arising under the Sherman Act, proclaiming that "we are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration as an alternative means of dispute resolution."<sup>25</sup> These decisions reveal that the Justices were achieving a greater comfort level with arbitral solutions. The handwriting was on the wall.

Two years later, the *McMahon* Court drove a stake through the heart of *Wilko*, holding that all claims under the Exchange Act—the statute under which the bulk of claims against brokers are brought<sup>26</sup>—are subject to mandatory arbitration if customer-dealer agreements so provide. By the time the decision was tendered, America bore little resemblance to the nation in which the *Wilko* Justices lived. Public institutions still reeled from the damage of Vietnam and Watergate, the President identified government as the principal enemy of the people, and faith in the unchecked private sector rose in tandem with stock prices. *McMahon* symbolized these changing times and reflected the fact that, by the mid-1980s, the *Wilko* Court's distrust of arbitration, if ever justifiable or supportable, had become old hat. Over and beyond that symbolism, the *McMahon* Court's reasoning is significant for its evangelical expression of a newfound faith in the techniques of ADR.

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<sup>23</sup> *Id.* at 219-20.

<sup>24</sup> 473 U.S. 614 (1985).

<sup>25</sup> *Id.* at 626-27.

<sup>26</sup> *See, e.g.*, Constantine N. Katsoris, *Should McMahon Be Revisited?*, 59 BROOK. L. REV. 1113, 1115 (1993).

Writing for the majority, Justice O'Connor scrapped the *Wilko* Court's approach and began instead from the premise that the FAA mandated judicial enforcement of all arbitration agreements on par with other contractual provisions, and this mandate controlled in the absence of a clearly expressed contrary legislative intent.<sup>27</sup> The Court then moved to the Exchange Act's nonwaiver provision and determined that it prohibited only waivers of compliance with the Act's substantive protections, not waivers of jurisdictional provisions. To justify this departure from precedent, the Court reduced *Wilko* to the proposition that predispute arbitration agreements were unenforceable then because "arbitration [in 1953] was judged inadequate to enforce [Securities Act] rights."<sup>28</sup>

Now, however, contemporary securities arbitration had matured, and modern improvements in the arbitration process made many of *Wilko*'s reservations obsolete. In espousing this rationale and finding arbitration sufficiently capable of protecting Exchange Act rights, the Court emphasized the emerging role of the SEC—which appeared as an amicus on behalf of the securities industry after years of opposing predispute arbitration agreements—in reviewing the arbitration procedures of the industry's self-regulatory organizations ("SROs"). In the end, the Court concluded that SRO sponsored arbitration provided investors with adequate protection.<sup>29</sup>

After *McMahon*, *Wilko* lived on only as a ghost of its former self, haunting the securities bar until the Court finally exorcised it from the body of American jurisprudence in *Rodriguez de Quijas v. Shearson/American Express, Inc.*<sup>30</sup> After that decision, which overruled *Wilko* and held squarely that disputes under the Securities Act were arbitrable, securities dealers were free to enforce predispute arbitration agreements arising under both the Securities Act and the Exchange Act.

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<sup>27</sup> *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 229 (1987).

<sup>28</sup> *Id.* at 228-29.

<sup>29</sup> Noting that the Racketeer Influenced and Corrupt Organizations Act ("RICO") did not contain a nonwaiver provision, the *McMahon* Court unanimously held that RICO claims could be subjected to compulsory arbitration. *Id.* at 238-42. Congress had the last word: It revised the statute to delete securities fraud from the list of predicate acts that could animate a RICO claim. See Private Securities Litigation Reform Act of 1995, 18 U.S.C. § 1964 (Supp. 1996).

<sup>30</sup> 490 U.S. 477 (1989).



The *Rodriguez* Court made little effort to defend the *Wilko* Court's rationale. Instead, the Court wrote off *Wilko* as a relic contaminated by the "old judicial hostility to arbitration."<sup>31</sup> Citing *McMahon*, the *Rodriguez* Court viewed subsequent improvements to the arbitration process as revealing the inadequacies of *Wilko*'s analysis and statutory interpretation.<sup>32</sup>

Although the *Wilko* Court undoubtedly possessed the prejudices that the *McMahon* Court attributed to it, the argument that the changed nature of arbitration in itself suffices to carry the day seems unconvincing. The cornerstone of the *McMahon* Court's distinction is that, since *Wilko* was handed down, Congress granted the SEC explicit statutory authority to oversee SROs' arbitration procedures. Apparently, the Commission had only limited authority over SROs' arbitration procedures in the 1950s. This cornerstone is set in sand rather than cement: as Justice Blackmun noted in his dissent, the Commission's new-found authority extended only to reviewing the procedures adopted by the SROs and not to reviewing specific arbitration cases.<sup>33</sup> Indeed, SROs still carry out their activities with a great deal of independence from Commission oversight.<sup>34</sup> In short, the *McMahon* Court may have overestimated the SEC's ability to protect the quality of arbitral proceedings.

None of this is to say that the situation remained static over the more than three decades that separated *Wilko* and *McMahon*; in the interim SROs substantially upgraded their arbitration procedures, most notably by the promulgation and adoption of a Uniform Code of Arbitration.<sup>35</sup> The Uniform Code provided much-needed guidance to arbitrators and brought a far greater degree of predictability to arbitral pro-

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<sup>31</sup> *Id.* at 480 (quoting *Kulukundis Shipping Co. v. Amtorg Trading Corp.*, 126 F.2d 978, 985 (2d Cir. 1942)).

<sup>32</sup> *Id.* at 483.

<sup>33</sup> *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 265 (1987) (Blackmun, J., dissenting).

<sup>34</sup> Even with the SEC looking on, the NASD has faced in recent years a substantial antitrust investigation by the Department of Justice and a lawsuit by the SEC itself for alleged industry-wide manipulative pricing practices. See Jeffrey Taylor & Deborah Lohse, *SEC Seeks Settlement with NASD*, WALL ST. J., June 18, 1996, at C1.

<sup>35</sup> See, e.g., Katsoris, *supra* note 26, at 1117-19 (citing SECURITIES INDUSTRY CONFERENCE ON ARBITRATION, SECOND REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION TO THE SECURITIES AND EXCHANGE COMMISSION: PROPOSAL FOR A UNIFORM CODE OF ARBITRATION (1978)).

ceedings. Without diminishing the industry's accomplishments, however, it is fair to say that most of the shortcomings which concerned the *Wilko* Court remain unchanged: arbitrators customarily do not generate written opinions; their decisions are not given precedential weight in subsequent arbitrations; there is usually no developed record available for review (save, perhaps, for a transcript of the hearing itself); and judicial review of arbitral awards is so narrowly circumscribed as to be virtually useless.<sup>36</sup> Simply put, the explicit grant of powers to the SEC has not altered the bone structure of arbitration.

Furthermore, nothing in the text of the FAA even empowers a court to review the procedural format of an arbitration mechanism selected by the parties (beyond what is in essence review for abuse of process).<sup>37</sup> The choice of arbitration procedures is left entirely to the agreement of the contracting parties.<sup>38</sup> Thus, to the extent that the nonwaiver provisions in the Securities Act and the Exchange Act prohibit only waivers of the organic statutes' substantive provisions, the Court's general analysis of arbitration procedures in *McMahon* is beside any relevant point.

Once one realizes the doubtful validity of depicting the evolution of securities arbitration toward a higher form of existence, it becomes apparent that, whatever the *McMahon* Court said, the driving force behind its approach lay in a pragmatic policy choice: a choice to elevate the FAA's goal of promoting the enforcement of arbitration agreements to permit speedy and inexpensive dispute resolution over the more traditional, but also more cumbersome, mechanism of adjudication. The relative emphasis on one policy choice over the other is the essence of the disagreement between the *McMahon* and *Wilko* Courts. A fair reading of *McMahon* is that the Justices believed securities arbitration always had been up to the task of resolving disputes between investors and brokerage houses, and that *Wilko* was a frolic and an aberration. In *McMahon*,

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<sup>36</sup> See, e.g., *Advest, Inc. v. McCarthy*, 914 F.2d 6 (1st Cir. 1990).

<sup>37</sup> See *id.* at 8-9.

<sup>38</sup> One federal court recently went so far as to say that parties may even alter the grounds on which an arbitrator's decision may be reviewed. See *PaineWebber, Inc. v. Elahi*, 87 F.3d 589, 599 (1st Cir. 1996).

the Court belatedly gave effect to Congress' ancient wish to experiment with the arbitrator's conference room as a viable alternative to the courthouse.

This brings us full circle: The laissez-faire era of the 1920s which gave birth to the FAA<sup>39</sup>—and against which the post-Depression *Wilko* Court rebelled—is similar to the virulently free-market era that produced *McMahon*. The securities arbitration line of cases depicts, like few others, the Court's ongoing struggle to reconcile the codification of the New Deal's free-market sobriety with statutory memorials to this country's abiding faith in Adam Smith's invisible hand.

Since *McMahon*, the roster of claims that parties may agree to send to arbitration has lengthened dramatically. The securities field is emblematic of this expansion. Arbitrators operating under the SROs' auspices now are resolving employment disputes under Title VII,<sup>40</sup> the ADEA,<sup>41</sup> and the ERISA statute<sup>42</sup>—areas far removed from the heralded competence of securities arbitrators. Several courts—perhaps recognizing that the *McMahon* Court's emphasis on administrative oversight of

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<sup>39</sup> Another interesting parallel is that the FAA was enacted at a time when observers of the courts believed there was a litigation crisis. See Stempel, *supra* note 13, at 277, 355 n.66 (noting that the "proponents of the [FAA], and probably the Congress that passed it, viewed arbitration as a substantial means of docket reduction and saw themselves as living in the midst of a litigation explosion"). Similarly, during the 1980s the courts have once again become mired in a confidence crisis. See *infra* Part II.

<sup>40</sup> See, e.g., *Bender v. A.G. Edwards & Sons, Inc.*, 971 F.2d 698, 699 (11th Cir. 1992) (upholding agreement to arbitrate employment disputes where plaintiff raised Title VII and common law claims); *Alford v. Dean Witter Reynolds, Inc.*, 939 F.2d 229, 229 (5th Cir. 1991) (upholding compulsory arbitration of Title VII claims), *dismissed*, 975 F.2d 1161 (5th Cir. 1992); see generally Stuart H. Bompey & Michael P. Pappas, *Is There a Better Way? Compulsory Arbitration of Employment Discrimination Claims After Gilmer*, 19 EMPLOYEE REL. L.J. 197, 197 (1993-94) (observing that federal and state courts have upheld predispute arbitration clauses in the context of civil rights disputes both within and without the securities industry); Megan L. Dunphy, Comment, *Mandatory Arbitration: Stripping Securities Industry Employees of Their Civil Rights*, 44 CATH. U. L. REV. 1169, 1204 (1995) (mourning the willingness of federal courts to send civil rights claims to compulsory arbitration).

<sup>41</sup> See, e.g., *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 23, 26 (1991) (holding that predispute arbitration agreement between registered representative and stock exchange mandated arbitration of claims arising under the ADEA of 1967, 29 U.S.C. §§ 621-631 (1994)).

<sup>42</sup> See, e.g., *Bird v. Shearson Lehman/American Express, Inc.*, 926 F.2d 116, 117 (2d Cir.), *cert. denied*, 501 U.S. 1251 (1991) (upholding compulsory arbitration of ERISA claims against employer).

arbitration procedures was superfluous—have gone further and permitted arbitration of statutory civil rights claims outside the securities context where there is no administrative oversight of arbitration procedures.<sup>43</sup> Whether or not intended that way by the Court, *McMahon* has been widely perceived as a Promethean gesture, freeing the private sector from the burdensome chains of a clogged, tired and unresponsive judicial system.<sup>44</sup>

## II. PROMETHEUS BOUND

Looking backward at *McMahon*, one wonders whether the Promethean gesture merely exchanged one set of chains for another. The answer to that question depends in large part upon the extent to which arbitration has fulfilled its promise. After all, the debate between proponents and opponents of securities arbitration has been waged under the assumption that arbitration brings something special to the table—swifter, cheaper, more convenient dispute resolution. To the extent that this assumption is flawed, the arbitration alternative itself becomes suspect—for even the most partisan adherents of arbitration must confess that judicial resolution offers advantages that arbitration lacks: e.g., more sophisticated truth-seeking devices, a body of precedent and the availability of meaningful appellate review. Arbitration is arguably a better choice only if these advantages are counterbalanced by expedition and inexpensiveness. But are they?

An analysis of the current state of securities arbitration would be incomplete without first considering the conditions that created the need for securities arbitration. For this, we must return to the symbolic—and potentially radical—implications of the *McMahon* decision for judicial dispute resolution.

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<sup>43</sup> See Bompey & Pappas, *supra* note 40, at 197 (observing that federal and state courts are upholding agreements to arbitrate discrimination claims both inside and outside the securities industry).

<sup>44</sup> See, e.g., Shearson/American Express, Inc. v. McMahon, 482 U.S. 220, 243 (1987) (Blackmun, J., dissenting) (lambasting the Court for approving the “abandonment of the judiciary’s role in the resolution of claims under the Exchange Act”).

In the last decade, courts have been under siege. Attacks have emanated from the left, the right and the center—attacks that are fueled by what many observers label as a “litigation crisis.”<sup>45</sup> Some observers have suggested that the courts’ adversarial model itself is to blame for exploding caseloads and burgeoning dockets. In their view, judicial proceedings lead parties to polarize their legal positions, stifling incentives for reaching negotiated—and therefore potentially superior—settlements of private conflicts.<sup>46</sup> Critics also claim that litigation places a premium on rule based conflict resolution at the expense of practical solutions informed by a more flexible set of (nonlegal) principles, unwritten norms and community values.<sup>47</sup> Moreover, detractors muse, the marriage between increasingly intricate processes of adjudication and time based compensation for practicing lawyers is an open invitation to prolong cases beyond all reason.<sup>48</sup> In fine, there is a widespread perception that the adjudicatory model, like the dance of the toreadors, emphasizes stylized conflict over common-

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<sup>45</sup> See, e.g., RICHARD A. POSNER, *THE FEDERAL COURTS: CRISIS AND REFORM* 76 (1985) (describing litigation crisis and refuting claims that no such situation exists); Warren G. Burger, *Isn't There a Better Way?*, 18 A.B.A. J. 274, 275 (1982) (arguing that courts are in the midst of a litigation crisis); Harry T. Edwards, *Alternative Dispute Resolution: Panacea or Anathema*, 99 HARV. L. REV. 668, 669 (1986) (discussing potency of the ADR debate at a time in which the “cost of litigation has substantially increased and the number of cases filed in state and federal courts has mushroomed.”); Susan A. Fitzgibbon, *The Judicial Itch*, 34 ST. LOUIS U. L.J. 485, 550 n.1 (1990) (noting that congested court dockets have contributed to the popularity of ADR methods). *But see generally* Marc S. 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. (1983) (examining historical data and debunking the supposed litigation crisis).

<sup>46</sup> See, e.g., Joseph F. Weis, Jr., *Are Courts Obsolete?*, 67 NOTRE DAME L. REV. 1385, 1396 (1992) (mulling inability of law to give jury freedom to award compromise verdicts).

<sup>47</sup> See, e.g., JEROLD AUERBACH, *JUSTICE WITHOUT LAW?* 138-47 (1983) (heralding community based dispute resolution informed by local values in place of adjudication); Judith M. Keegan, *The Peacemakers: Biblical Conflict Resolution and Reconciliation as a Model Alternative to Litigation*, 1987 MO. J. DISP. RESOL. 11 (arguing for dispute resolution based on community values, built upon biblical paradigm, and noting genesis of mediation and arbitration in biblical times).

<sup>48</sup> See, e.g., NATIONAL ASSOCIATION OF SECURITIES DEALERS, *SECURITIES ARBITRATION REFORM: REPORT OF THE ARBITRATION TASK FORCE 7* (1996) [hereinafter *TASK FORCE REPORT*].

sense cooperation—and, to make matters worse, looks down its aristocratic nose at more creative solutions to obvious problems.

Capitalizing on (and contributing to) public discontent with the courts, the ADR movement has made significant inroads in the past decade. Proponents sing a siren's song: as contrasted to litigation, they croon, arbitration is cheaper, speedier, more private, and more informal.<sup>49</sup> In addition, arbitrators are said to have greater expertise than judges (most of whom are avowed generalists, and damn proud of it) and jurors; they are also freer to do justice, this thesis runs, because they are not swaddled in the straitjacket of *stare decisis*. In a nutshell, the ADR industry has prospered based on its widely credited claim that it is less "legalistic" than the arthritic judicial system. The sales pitch is working because different constituencies, weary of the protracted delays and inordinate expense that all too often accompany adjudication, are ready converts.

This, in brief, is the dream of securities arbitration: a less expensive, less formal, more efficient method for resolving disputes that would otherwise become bogged down in the court system. It is one thing, however, to dream the magnificent dream; it is quite another to evaluate the reality of events in the cold light of day.

A careful examination of the recent experience in securities arbitration yields surprising results. Securities arbitration appears atavistically to have acquired some of the most frequently calumnized aspects of civil litigation.<sup>50</sup> Discovery requests are in vogue,<sup>51</sup> and prehearing motion practice relating

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<sup>49</sup> See, e.g., Fletcher, *supra* note 11, at 394 ("arbitration is an increasingly popular alternative"); Dunphy, *supra* note 40, at 1172-73 nn.16-17.

<sup>50</sup> See, e.g., TASK FORCE REPORT, *supra* note 48, at 7 (reporting widespread concern that securities arbitration is "moving away from a model of informal, expeditious, and inexpensive dispute resolution" due to incorporation of "too many characteristics of civil litigation"); Norman S. Poser, *When ADR Eclipses Litigation: The Brave New World of Securities Arbitration*, 59 BROOK. L. REV. 1095, 1105-06 (1993) (noting that adoption of civil litigation methods is contributing to an "emerging compromise between [arbitration's advantages of speed, economy, privacy, and finality] and the protections afforded by judicial procedures").

<sup>51</sup> See TASK FORCE REPORT, *supra* note 48, at 7 (citing extensive discovery requests, stonewalling in response, and dilatory tactics as prime examples of a "lawyering" approach to arbitration); *New York Stock Exchange, Inc. Symposium on Arbitration in the Securities Industry*, 63 FORDHAM L. REV. 1499, 1559 (1995)

to a myriad of subjects, such as the arbitrability of claims, the availability of discovery, and the applicability of statutes of limitations, is commonplace.<sup>52</sup> Even the hearings themselves look more and more like conventional trials; the duration has increased, as has the average time between the filing of a claim and the emergence of a dispositive ruling.<sup>53</sup> Increasingly formalized procedural and evidentiary standards abound. More and more, investors find that they need to retain paid advocates (either lawyers or professional nonlawyer paladins) to offset the well funded representation typically furnished to broker-dealers.<sup>54</sup>

And as the arbitration environment becomes increasingly litigious, the expense of a typical securities arbitration proceeding mounts, threatening to overtake the cost of a comparable case in litigation. Data collected for 1989-90 from five federal district courts indicates that, on average, arbitral decisions based on a paper record took 279 days to resolve; decisions emanating from live hearings before arbitral panels on average consumed 449 days.<sup>55</sup> By comparison, the overwhelming majority of civil actions between individual investors and broker-dealers filed in these courts settled or were otherwise disposed of prior to trial on the merits within 510 days, with the median time to achieve settlement being 365 days.<sup>56</sup> Of the litigated disputes that proceeded to trial (fourteen percent), time to final judgment ran 744 days, with a median time of 594 days.<sup>57</sup> More recent evidence indicates that the margin between arbitrated cases and litigated cases is shrinking, and there is every reason to believe that the cost differential is narrowing commensurately.<sup>58</sup> The short of it is that the time-and-money dif-

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[hereinafter *NYSE Symposium*] (grousing that securities arbitration discovery phase has the "smell, the touch, [and] the feel of litigation") (remarks of Michael Stone).

<sup>52</sup> See TASK FORCE REPORT, *supra* note 48, at 7.

<sup>53</sup> See TASK FORCE REPORT, *supra* note 48, at 7.

<sup>54</sup> See TASK FORCE REPORT, *supra* note 48, at 7.

<sup>55</sup> See GENERAL ACCOUNTING OFFICE, SECURITIES ARBITRATION: HOW INVESTORS FARE 45 (GAO/GGD-92-74) (May 1992) [hereinafter GAO REPORT].

<sup>56</sup> See *id.* at 49.

<sup>57</sup> See *id.*

<sup>58</sup> See TASK FORCE REPORT, *supra* note 48, at 7 (reporting that "SRO arbitration has incorporated too many characteristics of civil litigation, thereby undermining . . . the essential advantages of arbitration—speed and low cost"); Katsoris, *supra* note 26, at 1119 & n.43 (warning that securities arbitrations have generally increased both in duration and cost since the *McMahon* decision).

ferences between arbitration and litigation are not nearly as great as one might expect. As the gap closes, the widely advertised advantages of arbitration over litigation recede.

The rebirth of the litigation model in the securities arbitration context is a worrisome development. Among other things, it challenges the bedrock assumption that the private sector is able to manage conflict better and more cheaply than the courts. Recognizing that this trend undermines the foundation on which the securities industry built the arbitral alternative,<sup>59</sup> the National Association of Securities Dealers ("NASD") assembled a blue-ribbon task force to look into matters. The Task Force quickly verified the existence of the problem. It determined that the "increasingly litigious nature of securities arbitration has gradually eroded the advantages of SRO arbitration" and that all parties in interest—brokerage houses and investors alike—perceived securities arbitration to be "moving away from a model of informal, expeditious, and inexpensive dispute resolution."<sup>60</sup>

Where does this leave us? Securities arbitration may have been fraught with difficulties from the start, but the concept had undeniable advantages. To the extent that the arbitration model recreates itself in the image of the litigation model, these advantages erode. This metamorphosis gives rise to a bizarre paradox: A dispute resolving technique bred as an escape from the excesses of litigation seems bent on transmogrifying itself into that which it despised. Those arbitration advocates who once hurried out of courthouses to seek their own fortune are now, like so many of today's children, pining for their old rooms.

It is difficult to isolate a specific explanation for this *volte face*. Part of the problem is that it is hard to tell the symptoms from the causes. Another difficulty is the myriad of possible explanations, including the growing litigiousness of society, the essentially standardless nature of arbitration, and the increasing participation of lawyers in the arbitral process. Despite

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<sup>59</sup> See Lynn Katzler, Comment, *Should Mandatory Written Opinions Be Required in All Securities Arbitrations?: The Practical and Legal Implications to the Securities Industry*, 45 AM. U. L. REV. 151, 163-64 (1995) (noting the objective of the Task Force: to discern causes for the increasing ineffectiveness, inefficiency and cost of securities arbitration).

<sup>60</sup> TASK FORCE REPORT, *supra* note 48, at 7.



this uncertainty, it seems fairly clear that broader systemic forces have had a hand in molding the securities arbitration process. One such force is the longstanding jurisdictional rivalry between the courts and privately sponsored alternatives (such as securities arbitration) that are designed to oust the courts' jurisdiction over classes of disputes. Some scholars suggest that competitive interaction between courts and ADR firms is desirable because it will lead to more efficient dispute resolution.<sup>61</sup> This chanty has a pleasing melody, but the lyrics do not fit.

One of the by-products of market competition is a rough kind of averaging: In striving to maximize market share, competitors tend to imitate each other and, thus, competing products—say, political parties or religions—become less distinct over time. This middling tendency—known to economists as the Hotelling Paradox<sup>62</sup>—undermines any assurance that competitors will innovate or make better products. All it ensures is that a competitor which sets out to differentiate its products probably will produce a good or service that, over time, becomes more and more similar to the good or service offered by the market leader. Moreover, because this is a dynamic process, the market leader often will adjust by pirating some of the product differentiating aspects of the second entrant.

The Hotelling Paradox appears to be at work here. In their attempt to "compete" for the courts' business, the SROs increasingly have adopted certain features of litigation. Like some competitors, the courts have responded by offering versions of ADR services (in addition to an increasing emphasis on their ancient ADR mechanism: settlement). As the two systems compete, distinctions blur, and we are left with one dish that, while edible, retains none of the spices which distinguished its two predecessors. The Hotelling Paradox, if allowed to continue unchecked, risks leaving parties with no option but the same thin gruel.

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<sup>61</sup> See, e.g., Edward Brunet, *Questioning the Quality of Alternative Dispute Resolution*, 62 TUL. L. REV. 1, 7 (1987) (arguing that "[c]ompetition and the values underlying competition should play a major role in shaping future dispute resolution mechanisms").

<sup>62</sup> See generally HEINZ KOHLER, *INTERMEDIATE MICROECONOMICS: THEORY AND APPLICATIONS* 256-60 (2d ed. 1986).

### III. THE FLICKERING TORCH

The current state of affairs in securities arbitration might not be as much of a concern were it not for the fact that the future looks even more problematic. The principal cause for unease lies in the recommendations assembled by the prestigious NASD Task Force. While accurately noting the emerging problems, the Task Force has suggested some reforms that run the risk of making arbitration look even more like civil litigation.

Take, for example, the Task Force's recommendation that the NASD formalize its discovery procedures. The Task Force found that the process has been marred by both overreaching (broadcast discovery requests) and by stonewalling (refusing to respond fully to discovery demands).<sup>63</sup> Its solution to this set of problems consists of a general overhaul of the entire discovery mechanism. This would entail adopting rules requiring the automatic production of "essential documents" early in an arbitral proceeding.<sup>64</sup> While this proposal has some promise, it is difficult to say how effective it might be. Certainly, the endless proliferation of elaborate discovery requests has not been eliminated in civil litigation despite the inauguration of an automatic production rule.<sup>65</sup> Perhaps securities cases are different,<sup>66</sup> but the fear remains that they are not. This fear seems particularly well founded because, under the Task Force's proposal, parties would continue to be able to request other items not listed in the automatic discovery rule upon a showing that the desired discovery is reasonably likely to be

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<sup>63</sup> See TASK FORCE REPORT, *supra* note 48, at 78-79.

<sup>64</sup> See TASK FORCE REPORT, *supra* note 48, at 82. The prototype for this proposal is the mandatory early disclosure provision familiar to civil litigants, which provides that a party must "without awaiting a discovery request" furnish a standardized list of data to his adversary. FED. R. CIV. P. 26(a).

<sup>65</sup> See Griffin B. Bell et al., *Automatic Disclosure in Discovery—The Rush to Reform*, 27 GA. L. REV. 1 (1992).

<sup>66</sup> According to the Task Force, automatic document production is especially useful in securities arbitration because, "[u]nlike civil litigation generally, securities arbitration claims routinely present recurring issues that require the same types of evidence." TASK FORCE REPORT, *supra* note 48, at 82.

relevant and important to a disputed issue.<sup>67</sup> This language is not much of a deterrent to a securities bar that has prospered by churning out papers.

Another Task Force suggestion that may have unfortunate consequences is the recommendation that arbitrators be appointed much earlier in the process so that, among other functions, they can play a greater role in the discovery phase. Along with providing for earlier appointment, the Task Force also recommends enhancing the role of arbitrators, tutoring them in how to perform that role, and hiking their compensation.<sup>68</sup> These are profound changes and, while they sound pleasing, if adopted they will almost certainly lead to a professionalization of the arbitral pool (and, concomitantly, a formalization of the arbitration process). Indeed, the Task Force frankly acknowledges that

[w]ith the changes in securities arbitration . . . the traditional model of arbitration has become difficult to sustain. The demands upon securities arbitrators in terms of training, expertise, responsibilities, and time commitment have grown dramatically. Many believe that the inevitable result will be a cadre of professional, full time arbitrators, *not unlike the judiciary*.<sup>69</sup>

This fits hand-in-glove with the jurisdictional sprawl that has trailed in *McMahon's* wake. Because arbitrators must now decide a much more diversified array of cases—ranging from Title VII to ERISA—they will have to become jacks-of-all-trades, or, in other words, generalists (much like judges). Just as formalization of the process undercuts one principal advantage of arbitration—flexibility—so, too, professionalization of the decisionmaking function undercuts another principal advantage of arbitration—decisionmaking by persons who have expertise in a technical field. In the bargain, increased professionalization also threatens to shrink the pool of qualified individuals who are willing to serve as arbitrators.<sup>70</sup> These dangers are all the more ominous because some observers have already voiced qualms that arbitrators are ill-

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<sup>67</sup> See TASK FORCE REPORT, *supra* note 48, at 84.

<sup>68</sup> See TASK FORCE REPORT, *supra* note 48, at 86-88.

<sup>69</sup> TASK FORCE REPORT, *supra* note 48, at 88-89 (emphasis supplied).

<sup>70</sup> The Task Force Report notes that increasing the role of arbitrators is also likely to dissuade qualified individuals—who usually lead busy “outside” lives—from service. See TASK FORCE REPORT, *supra* note 48, at 89.

equipped to handle the large and complex securities disputes that formerly fell within the province of judges and the courts.<sup>71</sup>

Other Task Force recommendations, if implemented, would move securities arbitration even closer to the litigation model. For instance, the Task Force suggests that arbitrators provide written explanations of any decision to grant or reject a motion to dismiss on the basis of a statute of limitations.<sup>72</sup> This proposal brings to the table a feature that has slowed the progress of cases through the courts, but since the arbitrators' written explanations presumably would not have precedential value,<sup>73</sup> the proposal denies the benefit that ordinarily would accrue.

Finally, in what is perhaps the most revealing window on the state of securities arbitration, the Task Force recommends that the NASD initiate and expand voluntary mediation and Early Neutral Evaluation ("ENE") programs as an alternative to an arbitration process that has become "too adversarial, too costly, and too time[-]consuming."<sup>74</sup> Whether intended or not, the irony in this comment is palpable, and the statement shows just how far contemporary securities arbitration has strayed from its historic homeland.

#### IV. THE CIRCLING VULTURES

As our parents and teachers always have been fond of reminding us, actions have consequences. If the concept of arbitrating customer-broker disputes in the securities field is a sound one—and most observers, aware that the judicial system is poorly equipped to deal expeditiously with the small-dollar disputes that typify the genre, think that it is<sup>75</sup>—then the current trend in securities arbitration seems to invite unfortunate results. The principal threat to the continued sustain-

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<sup>71</sup> See TASK FORCE REPORT, *supra* note 48, at 11.

<sup>72</sup> See TASK FORCE REPORT, *supra* note 48, at 30. Others have gone further and argued that arbitrators should hand down written opinions in all cases. See WRITTEN OPINIONS, *supra* note 59, at 157 (opining that arbitral rules should be amended "to require a statement of the underlying reasons for the award because, as currently written, the rule fails to protect investors as intended by Congress").

<sup>73</sup> See Katsoris, *supra* note 26, at 1133; Katzler, *supra* note 59, at 151, 175, 196.

<sup>74</sup> TASK FORCE REPORT, *supra* note 48, at 47.

<sup>75</sup> See, e.g., Fletcher, *supra* note 11, at 458.

ability of securities arbitration is that it may come to resemble litigation so closely that it, too, will become muscle-bound and thus unable to deal expeditiously with the mine-run of customer-broker controversies. Put bluntly, a private dispute resolving system that models itself on the courts will have less and less legitimacy as an alternative to litigation. If it walks like a duck and squawks like a duck, many people will think either that it is a duck or that it is so similar a creature as to make any difference inconsequential.

This thought is hardly new or original. Commentators have foreseen since the time of the *McMahon* decision that such a scenario would not bode well for the continued relevance of securities arbitration.<sup>76</sup> Of course, securities arbitration, even under a litigation model, would continue to lighten the courts' caseloads. This is a current priority of policymakers,<sup>77</sup> but it strains credulity that this benefit, standing alone, will prove to be enough to ensure the viability of the arbitration alternative. The courts are far from perfect, but the hard truth is that neither securities arbitration nor any other private dispute resolution mechanism has ever been properly equipped to beat the courts at their own game. Insofar as securities arbitration is concerned, the lack of an organic body of precedent and the narrow scope permitted for judicial review bear witness to this verity. They are only two of several shortcomings that typically burden alternatives to conventional adjudication. The mills of the courts grind slowly, and the cost of the grinding is steep—but courts possess all the trappings of fairness (e.g., openness to public scrutiny, impartial decisionmakers, reasoned decisionmaking, meaningful appellate review) that private alternatives cannot readily offer.

It is, therefore, reasonable to assume that if parties begin to feel that arbitration is merely a marginally more efficient method of dispute resolution, saddled with an increasing num-

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<sup>76</sup> See C. Edward Fletcher III, *Learning to Live with the Federal Arbitration Act—Securities Arbitration in a Post-McMahon World*, 37 EMORY L.J. 99, 133-37 (1988) (warning that law's acceptance of securities arbitration as an alternative to the courts poses the risk that it may "become co-opted by the law and eventually become so formalized that it takes on the characteristics of other legal institutions").

<sup>77</sup> See, e.g., FEDERAL JUDICIAL CENTER, *STALKING THE INCREASE IN THE RATE OF FEDERAL CIVIL APPEALS* 1 (1995).

ber of the procedural accoutrements that bog down conventional litigation while driving up its cost, then there will be mounting pressure to stay with the real McCoy and keep disputes within the judicial system. If a litigation model will prevail in all available fora, then there is a huge incentive for parties to choose the forum that has the most stability and the greatest experience in adjudicating disputes.

Some might demur on the ground that the labor arbitration experience indicates otherwise. Private labor arbitration grew out of the need to provide alternatives to the dislocations caused by strikes and lockouts.<sup>78</sup> Thanks largely to Congress, various administrative agencies, and the courts, the relative freewheeling of labor arbitration has given way to a litigation model complete with a home grown concept of *stare decisis*, a corpus of written opinions, and a widening scope of judicial review.<sup>79</sup> Yet, despite these embellishments labor arbitration has flourished. Though this might suggest at first blush that an increasingly judicialized arbitral forum can remain viable even in the absence of demonstrable efficiency gains, the suggestion will not wash. Labor arbitration is waged between relative equals and offers unions and management a singular benefit not present in the securities context: It replaces the general strike and the lockout as the principal means for resolving industrial disputes. In contrast, securities arbitration accomplishes no such overriding objective; it is supposed to be a cheaper, quicker, more private and more efficacious alternative to the courts—nothing more. If the arbitration model squanders these advantages, there is little to suggest that people will choose it as an alternative to litigation.

Another, closely related danger exists. If arbitration continues to abandon those features of dispute resolution that make it attractive, then the courts can be expected to move into the resultant vacuum. Courts already face legislative pressure to create their own ADR systems.<sup>80</sup> Such pressure reflects the fear that the litigation model has become so rule bound that it cannot, without external prodding, adapt to the flexible, practical methods of dispute resolution that contempo-

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<sup>78</sup> See Fitzgibbon, *supra* note 45, at 488.

<sup>79</sup> Edwards, *supra* note 45, at 680.

<sup>80</sup> See, e.g., Civil Justice Reform Act of 1990, 28 U.S.C. §§ 471-482 (1994).

rary society demands.<sup>81</sup> If securities arbitration remains so intent on judicialization that it neglects the brave new world of ADR, then one suspects that legislative initiative and an innate sense of self-preservation will combine to push the courts in that direction.

## V. PROMETHEUS UNBOUND

This, then, is the challenge faced by contemporary securities arbitration: that, in its struggle for respectability, it will become an increasingly irrelevant, warmed-over variant of conventional adjudication. Such a development would be a step backward. In an ever more complex civilization, it is socially useful—and wise—to have separate kinds of dispute resolution mechanisms. The courts are in a fair amount of trouble,<sup>82</sup> but they are not candidates for the endangered species list. And they are for the foreseeable future likely to remain rule bound, procedure oriented institutions. This is neither a grave disappointment nor, in itself, a bad thing; a certain procedural emphasis is necessary if the judiciary is to perform its essential function. But there is clearly room and reason for other options. The existence of a specialized, privately operated forum, tailored to handle problems that arise repetitively within a delineated industry and in which procedural safeguards are relaxed in the service of speedier, more private, less expensive dispute resolution, seems highly desirable. These options, operating in parallel, give disputants the luxury of choice—and the very fact that two systems exist will exacuate both of them.

To achieve this objective, however, securities arbitration must return to its first principles. That means, of course, that securities arbitration must jettison some of the flotsam of litigation that it has accumulated and avoid the further clutter that it has been eyeing. Securities arbitration is a desirable alternative to the courts only if it provides tangible benefits that adjudication cannot easily replicate. Thus, to prosper in the future, arbitration must relearn the lessons of the past.

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<sup>81</sup> Chronicled *supra* Part II.

<sup>82</sup> The courts' difficulties have been more fully chronicled elsewhere. See, e.g., Bruce M. Selya, *The Confidence Game*, 30 NEW ENG. L. REV. 909 (1996).

Along the way, the securities industry must break out of the mold of the Hotelling Paradox. While the industry must strive to make securities arbitration fair and efficient, it must not dissipate the advantages inherent in the arbitral forum. In this market, product differentiation is critical: the purpose of securities arbitration is not to provide a cheaper imitation of adjudication but, rather, to permit investors and brokerage houses to resolve their disputes swiftly and inexpensively. This is precisely why Congress and the courts sanctioned securities arbitration in the first place.

An automobile analogy may help illustrate the point. The majordomos of securities arbitration have begun to act like a Ford dealer who bedecks a base model with fancy gewgaws and then attempts to compete with a nearby Mercedes dealer. That strategy is doomed to failure; longtime Ford owners will probably think that the unnecessary accoutrements are not worth the added cost, while longtime Mercedes owners will almost certainly prefer the genuine article. The way to sell a Ford is as an alternative means of transportation—a vehicle which is serviceable, less conspicuous, and far less pricey.

A decision to return securities arbitration to its home soil requires a certain boldness. The industry has a stake in the Task Force—a group composed of distinguished persons knowledgeable in the field—and a change in direction would entail rejecting many of the Task Force recommendations chronicled in Part III of this Article. But taking this route will permit us to retain the baby while draining the bath water. To cite one example, the Task Force correctly notes the problems that attend the current discovery process in securities arbitration, but formalizing the procedure, as the Task Force proposes, will simply accelerate the movement toward the contemporary litigation model. Allowing the arbitrator *more* flexibility to shape discovery according to the needs of the specific situation would seem to hold more promise than making arbitral discovery increasingly rule based.

At the same time, we must not unduly burden arbitrators. They must remain free to decide their cases in an informal, efficient, and flexible manner. Any effort to force exegetic written opinions or mandatory statements of the rationales underlying decisions should be strongly resisted.



Proponents claim that these recommended innovations, while cumbersome, will make securities arbitration fairer. At the risk of sounding heretical, I assert that improved fairness should not be the main objective. In striving to keep securities arbitration as close to the Ford "base model" as possible, we must recognize that arbitration will not always yield the same outcomes as would occur in adjudication. Streamlined arbitration procedures risk producing somewhat less accurate results than full-fledged trials, but the savings in time and money that arbitration affords can compensate for some lessened degree of accuracy. As with the test limned by the Supreme Court for detecting violations of procedural due process,<sup>83</sup> we must balance the risk of an incorrect result in an arbitral proceeding against the public interest in having a more efficient, less formal alternative to conventional adjudication. Just as the *Mathews* Court found that the strictest procedural safeguards were not required in less formal administrative contexts,<sup>84</sup> we should permit the relaxation of litigation based standards in securities arbitration.

This state of affairs is all the more tolerable because little probative evidence exists to support a conclusion that the relative informality of securities arbitration is *systematically* unfair in any way. Although some commentators decry the dangers of industry control over the rites of securities arbitration,<sup>85</sup> the General Accounting Office has found that investors win sixty percent of the cases brought in securities arbitration and that arbitrators typically award sixty percent of the amount investors claim as losses in their complaints. This compares favorably with conventional adjudication, in which investors prevail roughly forty percent of the time.<sup>86</sup>

In the end, the best alternative is to have alternatives. A healthy judicial system and a vibrant private arbitration mechanism, coexisting in parallel, constitute an effective guarantee that parties will be able to take their disputes to that forum which can best resolve them.<sup>87</sup> We must remember Shake-

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<sup>83</sup> See *Mathews v. Eldridge*, 424 U.S. 319, 335 (1976).

<sup>84</sup> See *id.* at 348-49.

<sup>85</sup> See, e.g., Lydia A. Hervatin, Note, *Predispute Arbitration Agreements in Securities Disputes: Rodriguez De Quijas v. Shearson/American Express, Inc.—Speedy Justice or Just Speed?*, 24 LOY. L.A. L. REV. 757 (1991).

<sup>86</sup> See GAO REPORT, *supra* note 55, at 31.

<sup>87</sup> In this regard, securities arbitration should also recognize its own limitations

speare's admonition that "the world is broad and wide,"<sup>83</sup> and our society has both the space and the need for distinctive methods of dispute resolution, not merely a forthright method of court run adjudication and a pale pastiche of it. Preserving healthy adjudicatory *and* arbitral options is the objective toward which we, as judges, academics, industry leaders and lawyers, should strive.

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and confine its scope to those areas in which it can operate most efficiently and do the greatest good. Voluntary agreements to arbitrate have a place in the securities context where the outcome of a typical dispute often depends on documentation. The use of mandatory arbitration to resolve ERISA and Title VII claims is much harder to justify as such claims typically depend more upon the credibility of witnesses and other elements better suited to the truth seeking devices of traditional adjudication. In addition, forcing arbitrators to handle cases outside their specific area of expertise will have the unfortunate effect, chronicled *supra* Part III, of requiring them to become generalists (i.e., more like public-sector judges) and thereby destroying the current advantage that attends decisionmaking by individuals with technical proficiency in the securities field.

<sup>83</sup> WILLIAM SHAKESPEARE, *ROMEO AND JULIET* act 3, sc. 3, l. 56 (1595).

