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# Arbitration Intoxication: Alternatives to Arbitrating Securities (and Other) Disputes

By: John S. Worden & Matthew P. Broccolo

Arbitration has many advantages. The purpose of this article is *not* to discourage participation in the arbitration process in general. Indeed, one of the authors is the chair of the San Francisco Bar Association's Arbitration Section, and both authors have arbitrated many cases in many different states, usually with success. Nonetheless, in certain cases, arbitration can present more challenges and pitfalls than a jury trial, despite our clients' belief otherwise.

Arbitration is perfect for some kinds of disputes. It is a problematic process for others. And, contrary to popular nomenclature before Congress, arbitration is not always plaintiff-hostile and defendant-friendly. Although there are many instances where a corporate defendant would be well served by the arbitration process, often they would receive a faster, cheaper and more judicious resolution of their claims in the jury system. Nonetheless, too often corporate clients refuse to consider the jury system even when it will be most advantageous for them to do so, and nowhere does this dichotomy exist more than in the FINRA/Securities Arbitration area. The purpose of this article is to shed light on instances where our corporate clients' interests are disserved by rigid adherence to a pro-arbitration mantra.

## The Evolution of Securities Arbitration

The Supreme Court has consistently bolstered arbitration as a binding alternative to litigation. Two cases in the 1980s, *Shearson/American Express Inc. v. McMahon*[1] and *Rodriguez de Quijas v. Shearson/American Express Inc.*[2] ensured that courts would enforce agreements arising out of securities disputes.[3] Since then, brokerage firms have been all in on arbitration and almost universally included mandatory arbitration clauses in their customers' contracts. The Financial Institution Regulatory Authority (FINRA) now operates the largest securities dispute resolution forum in the country.[4]

In the late 1980s, requiring arbitration made sense for brokerage firms. The claims made were basic, and the amounts sought by claimants were small. That is no longer the case. What was once thought of as a streamlined process to resolve minor disputes has become a forum where seven, eight, or nine-figure disputes are also resolved with less predictability than in the courts. These high-value cases, which contain numerous, complex, and often-unsubstantiated claims, frequently languish for years. The amount in controversy can be as much as in a major commercial battle, with some claimants asserting seven, eight, and even nine-figure claims. And all of this is managed by a much-less-regulated system than the courts.

Yet, despite these challenges for businesses, arbitration is frequently cited as actually favoring businesses over consumers. Senator Sherrod Brown introduced the Arbitration Fairness for Consumers Act early in 2019, which would prohibit binding arbitration clauses in consumer contracts.[5] Congressman Hank Johnson introduced other legislation that targeted consumer arbitration, the Forced Arbitration Injustice Repeal (FAIR) Act earlier that year.[6] Publicly, plaintiffs' bars such as the Public Investors Arbitration Bar Association (PIABA), the claimants' bar for brokerage customer disputes, is supportive of these changes, noting that they are "supportive of investor choice."[7]

With an election around the corner and the FAIR Act bill now through the House, arbitration clauses in consumer contracts, including with brokerage customers, may be a thing of the past. Yet, this may ultimately benefit brokerage firms and businesses generally. Representative Johnson's "Fact Sheet" on the FAIR Act characterizes arbitration as a forum where arbitrators "apply different rules than a courtroom setting and render a secret, unappealable decision."[8] He goes on to decry arbitration clauses as destructive to the 7th Amendment right to a trial by jury for consumers, preventative of class actions, requiring a setting that has different evidentiary and discovery standards than court, and giving businesses an unfair advantage in choice of arbitrator and forum.[9] Yet, it is far from clear that customers would benefit more than businesses from the option of going to court versus arbitration. More importantly, Representative Johnson unintentionally brings into focus a couple of the key problems with the consumer arbitration process that *frustrate businesses*.[10] The issues with the process that he outlines, which we explore in greater detail below, often create frustration for all parties involved.

# Discovery

An oft-cited reason for engaging in arbitration over trial is the streamlined discovery process. The lack of depositions, contention interrogatories, and supposedly more-limited document discovery process are all supposed to make the parties' and attorneys' lives easier in resolving a dispute. While parties forfeit useful investigative tools like depositions, the streamlined process ostensibly moves everything toward resolution more efficiently. The FINRA arbitration rules even codify the lofty notion that parties must cooperate in discovery.[11] This all makes sense in the context of simpler disputes with low dollar amounts, a few documents, and straightforward claims. In those circumstances, the time and expense involved in depositions and multiple discovery conferences are gladly avoided. And sometimes even larger disputes are best resolved through arbitration. But sometimes, especially when the dollar amounts are large and the documents correspondingly voluminous, the arbitration process breaks down.

Despite the goal of streamlined discovery, arbitrations still take a long time to resolve.[12] Capital Forensics, Inc. (CFI)[13] has found that the average lifespan of FINRA customer arbitration cases since 2009 that do not settle (or are dismissed) is approximately 15 months. Additionally, cases that go to hearing more often than not last well beyond the one year mark between claim-filing and resolution. In fact, many last far longer than that. For example, of the customer cases with awards rendered that were filed in 2014, over 13% were closed after the two-year mark, with 4% being resolved after three years. Compared with courtroom litigation, this data is not supportive of arbitration.

Of all cases filed in the federal district courts, the median resolution time for all cases that go to trial has hovered right around 27 months for the past six years.[14] If all cases that settle or are otherwise disposed of are included, that number dwindles to between 8 and 11 months depending on the year between 2014 and 2019. Examining these numbers, the question becomes: What is taking so long if securities arbitrations do not usually involve things like depositions? While there are probably a number of answers to that question, document discovery in high-value cases is certainly one.

Document discovery in arbitration can be just as time-consuming and resource-intensive as in a large commercial courtroom litigation. The authors have been involved in multiple customer arbitrations in which their clients were required to produce hundreds of thousands of pages of documents – a volume often not found in major commercial litigation.

Beyond production volume, parties must spend substantial time and resources obtaining proper disclosure from the opposition. Whereas courts have strict deadlines for documents discovery, frequent check-ins at status conferences, and other ways of keeping the parties in line, arbitrations generally allow the parties to create the discovery schedule and keep each other accountable. While this might sound nice in theory, it leaves the discovery process ripe for abuse and neglect. Parties must often file multiple motions to obtain the documents they need to prepare their cases. Additionally, the process informality frequently results in the parties engaging in last-minute, full-throttle discovery battles in the weeks leading up to the hearing.

Third-party discovery is also extremely difficult to obtain in arbitration. Third-party document discovery often ends up being necessary for respondents because the opposing customer has produced little to no probative documents, often simply because the customer possesses very little. Yet, subpoenas are frowned upon in arbitration and difficult to enforce. For example, FINRA discourages the use of subpoenas on third parties unless absolutely necessary.[15] Sometimes, even when absolutely necessary, the panel will simply deny respondents permission to serve these subpoenas without sufficient explanation. Even when third-party document subpoenas are approved by the arbitration panels, they are largely unenforceable. Courts do not enforce document subpoenas in an arbitration unless they direct the recipient of the subpoena to appear at the arbitration hearing with the documents.[16] So, if a subpoena recipient refuses to cooperate, the only options for the propounding party are to give up or gamble that forcing the recipient's appearance with the documents at the hearing will turn out well. Neither option is ideal.

Given that the discovery process can be this frustrating, the loss of depositions and contention interrogatories seems almost too high a cost to choose arbitration for many high-value or otherwise complex cases. In a case moving to trial, the defense can focus the issues through contention interrogatories that force the plaintiff to substantiate their allegations with supporting evidence, which the defense can then obtain through discovery. Armed with that evidence, the defense is able to narrow its focus on the claims and evidence actually at issue in the case. In arbitrations, the lack of contention interrogatories allows the claimants to avoid providing this evidence and makes hearings less predictable. Similarly, the lack of depositions also makes respondents' jobs harder and the witness examinations by both parties less focused. Depositions button down testimony and create a record that adverse witnesses at trial must stick to or face impeachment. At arbitration hearings, instead of conducting efficient examinations with the backdrop of prior sworn testimony, parties must spend time inefficiently wading through lines of questioning that may end up bearing no relevance to their case.

## Dispositive Motions

Motions to dismiss and motions for summary judgment are a core pillar of the practice of law in state and federal court. They are essential to quickly disposing of meritless lawsuits and saving defense attorneys' clients time and resources. For example, after their clients are served with a complaint, federal defense litigators frequently file motions to dismiss for failure to state a claim under which relief can be granted instead of answering.[17] In court, plaintiffs must file complaints containing "more than an unadorned, the-defendant-unlawfully-harmed-me accusation."[18] Unlike in arbitration, "a formulaic recitation of the elements of a cause of action will not do."[19] If defendants in a court case receive a complaint that fails this standard, they may file a motion to dismiss the complaint before discovery even begins. Likewise, if it becomes apparent after discovery that the case is meritless (or if it is clear that the plaintiff should prevail), either party can make a motion for summary judgment asking the judge to issue a final ruling based on the facts developed in the record. If granted, the judge disposes of the case at that stage and trial is avoided.

For low-dollar-value cases, it may be in neither party's interest to expend time and resources on these motions and chance an unfavorable result. In those cases, parties may prefer the leaner discovery process and informal hearing structure in arbitrations to taking chances on such motions.

However, for high-dollar-value cases, these motions can be vital tools of defendants. Both motions to dismiss and motions for summary judgment dispose of the case much quicker and less expensively than a trial. Motions to dismiss save the moving parties the enormous time and expense that the discovery process requires. Motions for summary judgment avoid the long billable hours spent briefing motions *in limine*, preparing witnesses, creating exhibits, and preparing for and executing all of the many facets of appearing in front of a jury.

Yet, the equivalents of *motions to dismiss and motions for summary judgment in arbitration are almost never granted*. Claimants often file threadbare statements of claim in arbitrations, yet arbitrators generally allow the case to proceed. The same is true when discovery is complete and shows a claimant's case to be deficient; arbitrators are still loathe to dispose of the case without a hearing. Indeed, many panels are likely uncomfortable dismissing a case before hearing evidence, given one of the few grounds for overturning an arbitration award is the denial of an opportunity to hear material evidence. In their view, the merits of a case will come forth during a hearing, so it is best to err on the side of caution and give both parties their "day in court." Unfortunately for respondents, most of the time this means that the only viable way to get out of an arbitration is to settle or take it to an unappealable hearing.

## Statutes of Limitations & Statutes of Repose

Defendants lose another key weapon in battling meritless claims when they choose arbitration: proper enforcement of statutes of limitations and statutes of repose. Both are present in every court venue in the country, and they help prevent stale claims from wasting the courts' resources and forcing defendants to battle ancient allegations. Besides enforcing the common-sense notion that claims with merit would have been brought well within the limitations period (with very few exceptions not relevant to most arbitrations), these statutes also safeguard against the enormous disadvantage at which stale claims put defendants. To defend against such claims, defendants must do the virtually impossible task of tracking down ancient documents and obtaining reliable testimony from witnesses about events they probably do not remember accurately. In court, defendants may make motions to dismiss the claims based on a statute-of-limitations defense right out of the gate if it is clear that all of the claims are stale. Or, if the record developed in discovery brings the stale nature of plaintiff's claims to light, defendants can move for summary judgment at that point. *In arbitration, these motions are almost never filed, because they are almost never granted.*

Often, the best that a respondent can hope for is that the panel addresses the issue at the hearing. Even then, panels have often allowed evidence related to stale claims to be brought in with a throw-away assurance that they will carefully consider the applicability of any statute of limitations or repose when making their ultimate determination. This fails to prevent the panel from hearing irrelevant and potentially prejudicial evidence of conduct that happened years ago. Most discouraging is that even where arbitration forums have codified their own statutes of limitation or repose, arbitration panels have not consistently applied them. FINRA Customer Arbitration Rule 12206(a) states "no claim shall be eligible for submission to arbitration under the code where six years have elapsed from the occurrence or event giving rise to the claim." Despite this rule, claimants are frequently allowed to bring in evidence concerning events that happened seven or more years before the statement of claim was filed. With respect to state or federal statutes with much shorter limitations periods (e.g.

three years for fraud or negligence, four years for breach of contract, etc.), panels almost never apply them. In practice, out-of-time claims almost always reach a ruling on the merits in arbitration.

Thankfully, things may be changing (a little) with respect to respondents' ability to bring these motions in FINRA arbitrations. CFI gathered data of awards rendered over the past decade, and the percentage of cases getting dismissed under the eligibility rule appears to be slowly crawling upwards. Additionally, recent Supreme Court precedent has given a boost to respondents defending against claims based on purchases or sales of securities prior to the limitations period. In *CALPERS. v. ANZ Sec., Inc.*,[20] the Supreme Court found that Section 11 of the Securities Act, a statute with very similar language to FINRA Rule 12206, was a "statute of repose," meaning it runs "from the defendant's last culpable act" and not from whenever the plaintiff discovered the actionable conduct. In other words, the Court held that this statute barred plaintiffs from making out-of-time claims simply because they did not discover the conduct in time. For FINRA respondents, this case theoretically means that claims against them based on purchases or sales of securities occurring more than six years prior to when the claim was filed should be dismissed. However, it remains to be seen whether recent case law will finally turn the tide and motivate arbitrators to reliably dismiss out-of-time claims. Motions to dismiss, even based on eligibility concerns, are still rarely successful in the arbitration context.

# The Trial

Large-value arbitration hearings can be lengthy affairs. On the surface, one would think that a hearing with more relaxed rules of evidence and less discovery to wade through would make things run more efficiently. This is true when there are not many documents and the disputed issues are straightforward, but not so in complex, high-value cases. In fact, trying a securities arbitration can be just as inefficient, if not occasionally more inefficient, than trying cases in federal and state court.

Arbitration hearings can be unwieldy from the start. Claimants in high-value arbitrations often throw the proverbial "kitchen sink" of claims at the respondent without having to substantiate any until the hearing, forcing the respondent's counsel to prepare for a huge universe of claims, most of which will prove baseless. In fact, claimants sometimes succeed in bringing in claims absent from their pleadings until their attorney's opening statement. In state and federal jury trials, litigants can limit the amount of unsupportable claims and evidence introduced at trial through motion practice leading up to trial and throughout the matter. As noted above, participants in arbitration cannot. Because of this, respondents must spend extensive time preparing for various eventualities in the claimants' presentation of their case that they would have eliminated through motions were they in court. Failing to do so leaves respondents open to being blindsided with no recourse. And if something unexpected arises from that testimony, parties have to quickly and nimbly adapt their case strategy. Finally, all of this is done with the nagging worry in the back of the attorney's mind that they will almost certainly be unable to appeal an adverse ruling.

# Evidence and Panelist Experience

In court, the rules of evidence are geared toward jurors to prevent irrelevant and unreliable evidence from being admitted. Relevance, in particular, is codified in the Federal Rules of Evidence and by every state evidence code.[21] Further restrictions prevent the admission of even relevant evidence in a number of circumstances, including, for example, if it based upon hearsay[22] and speculation.[23] Furthermore, relevant evidence not deemed inadmissible by other restrictive rules will still not be admitted if "its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, or by considerations of undue delay, waste of time, or needless presentation of cumulative evidence."[24]

In contrast, the introduction of evidence in arbitration is virtually unregulated. For example, the ONLY rule governing the introduction of evidence at FINRA arbitration hearings is FINRA Customer Arbitration Rule 12604(a), which simply states, "The panel will decide what evidence to admit. The panel is not required to follow state or federal rules of evidence." In other words, panels can choose whether to review, consider, and rely upon any evidence at all without respect to its relevance, speculative nature, or seriously prejudicial effect on the parties. Put simply, the admissibility of evidence is wide open at arbitration.

Compounding this issue is the fact that arbitrators, who make complex evidentiary determinations throughout the hearing, are not required to have a background in law, much less have courtroom trial experience. This is a potential nightmare scenario for attorneys, as some arbitrators charged with conducting nuanced legal analysis have little to no training in evidence law. This is not just a one-in-a thousand occurrence, either. CFI discovered that out of 4,566 three-panelist customer arbitration awards for which they had data between 2009 and 2019, 6% of these panels had not one arbitrator with a law degree. And while that number may appear low, panels with no one possessing litigation or trial experience are *significantly* higher.

Even if the parties select a fully qualified panel, they cannot prevent the arbitrators from being "tainted" by inadmissible evidence. In jury trials, jurors do not hear when pre-admission offers of proof are being argued and ruled upon by the judge. The reason for this is simple: The court does not expect jurors to ignore and forget persuasive information they see or hear simply because they are told. Jurors cannot be counted on to prevent such information from impacting their judgment, consciously or otherwise. Yet, in arbitration, panelists act as both triers of fact and evidentiary gatekeepers. They hear and see all potential evidence that is being offered by a party before it is admitted. Thus, they are not insulated from clearly inadmissible and prejudicial evidence that taints their view of a witness or the case, whether consciously or subconsciously. When it comes time to render a final decision, arbitrators face the extraordinarily difficult challenge of separating out what they should be considering as triers of fact considering from what they heard or saw as evidentiary gatekeepers.

Recently, certain attorneys have been taking advantage of the loose rules of evidence and dropping a "closing binder" into panelists' laps during their closing argument. Closing argument is *not* the time to be offering additional evidence or legal authority. Yet frequently, the binder contains excerpted cases, rules, documents, and even press clippings that the offering party never provided to the opposition. Despite the fact that this would never fly in a courtroom, panels often allow this material to be presented after making statements to the effect of: "we will carefully consider what weight, if any, to give this material." But by the time the closing argument has ended, the damage has likely been done. The offering attorney is able to refer to and twist whatever is in that binder, free of any objection from the other side. In fact, if the material is offered by the claimant, the respondent will likely be afforded no opportunity to orally rebut this evidence. In a strange quirk of the arbitration process in certain forums, claimants can "defer" all of their closing argument until after respondent has delivered theirs, depriving the respondent of the ability to rebut the argument. If claimants offered otherwise-inadmissible evidence into the record during their closing, respondent will likely have no recourse to object to it.

It bears repeating that in cases with only a few documents and lower dollar amounts at issue, these concerns mostly disappear. There, the informality of the introduction of evidence in arbitration could be a blessing. It ensures that parties do not get bogged down in the unnecessary tedium of offers of proof, motions *in limine*, and objections in cases where the evidence and issues are straightforward. But with larger and more complex cases, this informality can present serious issues. In these cases, with thousands of documents and numerous complex issues, the admission of evidence can turn into an unpredictable free-for-all.

## The Triers of Fact

Runaway juries are frequently cited as the biggest concern for defendants going to trial. Juries have a reputation for being swayed by emotion, favoring the little guy over large businesses, ignoring key evidence, awarding unjustifiably large damages, and otherwise creating misery for defendants. Worst of all, they are characterized as wildly unpredictable, creating anxiety for anyone whose job relies upon projections of litigation results for corporate defendants. Many think that juries are the antithesis of predictability.

The same concerns ostensibly do not apply to arbitrators. They are viewed as educated, professional, reasonable, and experienced people who will objectively and diligently examine the evidence and correctly apply the law to their findings. Moreover, they may believe that most arbitrators on their panel will have substantial legal experience.

In truth, the quality of an arbitration panel can vary wildly. Sometimes, the attorney may get three diligent and reasonable arbitrators who are well-versed in the law and subject matter at issue in the case. Other times, attorneys find themselves in front of arbitrators that have experience deficits, biases, short attention spans, and other issues that deeply impact the proceedings. In fact, on occasion you may find that an arbitrator is sleeping or (often) reading his or her phone during the presentation of your case.[25] And as was discussed earlier in this article, FINRA panels are not required to include a lawyer that can help guide them through thorny legal issues.

The unique problem with a bad panel versus a bad jury is that arbitrators are not only the triers of fact, but, in the context of the arbitration, the judges as well. There is no one present to excuse the arbitrators during offers of proof or otherwise provide a check against their conduct. The buck starts and stops with the arbitration panel.

Further, unlike jurors who are subjected to voir dire, arbitrators must only disclose certain information relating to bias that is required by the arbitration forum. In FINRA arbitrations, this information comes in the form of a yes and no questionnaire regarding the arbitrators' affiliations and relationship to the parties with the occasional brief description where required. Attorneys cannot question arbitrators to illuminate their internal biases, which often remain unknown throughout the hearing. Further, arbitrators may accidentally omit key information from the questionnaire until the hearing. At that point, the handicapped party's attorney has to decide whether to fight it or go forward with the hearing that their client has likely waited on for over a year.

The parties are able to do some digging into the selection of arbitrators before the panel is constituted. FINRA provides a list of ten chairpersons, ten public arbitrators, and ten non-public arbitrators for each matter. Each party can strike four names from each of the first two lists and anyone from the non-public list. Additionally, each party may rank the arbitrators they did not strike from each list in order of preference. Diligent parties will look into the arbitrators' professional background, their questionnaire, and their prior decisions with an eye towards spotting potential predispositions or biases when making these decisions. Yet, each party's choices are often very limited and do not cure the serious problem of undisclosed biases and conflicts.

Moreover, this process cannot address systemic issues with the FINRA arbitrator pool. For example, in October 2006, members of PIABA openly discussed their efforts to recruit public FINRA arbitrators at their annual meeting in Tucson.[26]

## Appeals (or Lack Thereof)

Appealing an arbitration award is an uphill, if not impossible, battle. Strangely, results produced by a less formal and revealing process than courtroom litigation are also exponentially harder to overturn. Within the vast majority of arbitration forums, appeals do not exist.[27] Instead, the only potential avenue to appeal an award is to file a motion to vacate the award under the Federal Arbitration Act in court. Those motions, which are rarely granted, can only be made under four limited circumstances: (1) where corruption, fraud, or undue means were used in obtaining the award; (2) where an arbitrator was partial or corrupted; (3) where there was misconduct by the panel in refusing to postpone the hearing, refusing to hear material evidence, or in any other form that prejudiced a party; or (4) where there was misuse of power by an arbitrator.[28] Certain courts also review awards that they deem "arbitrary and capricious" or "contrary to public policy."[29] In practice, even where one of these unusual circumstances may have occurred, courts routinely deny motions to vacate, except in the most egregious of circumstances. In fact, arbitrators do not even need to get the law close to correct to avoid worrying about being overturned. Courts have held that an "erroneous application of the law" alone is not enough to overturn an arbitration award.[30]

Complicating matters further, arbitrators are not required to tell parties why they decided the way they did. The FINRA rules only require that "the award may contain a rationale underlying the award" if the panel chooses. The parties may request an "explained decision," but such a decision need only be "a fact-based award stating the general reason(s) for the arbitrators' decision. Inclusion of legal authorities and damage calculations is not required."[31] In other words, even when required to explain their decision under the rules, arbitrators need not provide what is usually the most crucial information in any appeal: how the panel applied the law. Aggrieved parties are left with the difficult task of appealing without any written record of the arbitrators' legal reasoning in arriving at their decision. In the context of a minor dispute, the lack of an appellate process has a minimal impact. There, the parties would not likely spend the time or resources appealing an unfavorable result unless something truly egregious happened, in which case there are certain avenues to try and overturn the award. But in a major arbitration, this means that parties might get stuck with highly unfavorable, detrimental, and unfair results that will not be reviewed.[32]

# The Award

The final issue may be the most interesting to those on the respondents' end of consumer arbitrations: damages. When firms first chose arbitration over the courts, they likely thought they were avoiding runaway juries who would award customers outlandish and baseless awards. Fears of massive punitive damage awards based on sympathy for the little guy drove firms towards what they thought would be a fairer process. With respect to high value cases, things have not worked out as planned.

Generally, punitive damages are intended to be used as a deterrent and a punishment for outrageous conduct that occurs "because of the defendant's evil motive or his reckless indifference to the rights of others."[33] In California, for example, punitive damages cannot be awarded against employers who are only found liable on a theory of "*respondeat superior*," which is often the only reason brokerage firms are roped into customer arbitrations.[34] Punitive damages will not be assessed unless the employer "had advance knowledge of the unfitness of the employee and employed him or her with a conscious disregard of the rights and safety of others or authorized or ratified the wrongful conduct for which the damages are awarded or was personally guilty of oppression, fraud or malice."[35] In the context of securities arbitrations at least, this is a very high bar to meet. If this standard were properly applied in the securities arbitration context, punitive damages would be very rare.

Yet, arbitration panels award punitive damages with unsettling frequency. For example, in 2018, 5% of all cases that made it to the award stage were awarded punitive damages.[36] To be clear, that is not the percentage of cases where claimants succeeded – it is 5% of *all* cases that went through to an award, including the 60% that resulted in the denial of all of claimants' claims.[37] That means that if a respondent went the distance and was provided a decision in 2018, there was a one-in-twenty chance that the Panel awarded punitive damages. According to FINRA's statistics, claimants were awarded damages in 40% of the cases that were decided in 2018. Taken together with CFI's findings, that means that claimants who were awarded damages had a nearly 12% chance of obtaining punitive damages in 2018. By contrast, a 2005 study of all state civil trials across the country found that punitive damages were awarded in only 5% of cases *where plaintiffs prevailed.****[38]*** While current data on punitive damages is lacking, these statistics nonetheless should give one pause. Brokerage firms should seriously question the notion that arbitrations avoid irrational awards more than trials. The numbers are even more discouraging when one considers that these inexplicable awards would be appealable after trial, but rarely at arbitration.

# Conclusion

If we have seemed overly critical of arbitration, that was not our intent. We end this article where we started, by confirming our belief that in many cases arbitration is faster, cheaper, more predictable and thus preferable to the jury system. However, as discussed above, there are many circumstances where this would not be the case. For example, a defendant in a dispute over claims that are time-barred or legally unsound would be far better off in the court system where motions to dismiss and motions for summary judgment are often granted to eliminate such claims from going forward, to name just a couple of examples.

Because brokerage customer disputes invariably are litigated in FINRA Dispute Resolution, we have no countervailing examples of what would happen were they to be litigated in court today. That imbalance of information may unfairly taint arbitration when litigation would no doubt present its own challenges. Arbitration does have its merits, and can yield fair and favorable results. The vast majority of the arbitrations in which the authors have been involved resulted in favorable outcomes for our clients. Nevertheless, it is clear that arbitration has fallen miles short of its lofty promises of speedy results, cost-efficiency, and fair results, especially in the context of complex and high-value cases.

The purposes for which arbitration was designed have simply not been achieved in that context. Arbitration discovery omits depositions and contention interrogatories for the sake of expediency, but discovery often ends up eating up just as much time and money as a court case. The record is then left less clear than it would be had the process involved depositions, contention interrogatories, and court conferences. At the hearing, respondents are forced to prepare to defend against every possible claim, and do so even if the claims are meritless. And whether prejudicial or not, evidence will likely come into the record at the hearing due to a lack of evidentiary standards.

The panel itself might be experienced and diligent, or they may be biased and inattentive. Regardless of their diligence or objectivity, there is no guarantee that any arbitrator on the panel will have legal experience. When damages are awarded, respondents are at risk for runaway awards just as they would be in front of juries. And if they get an irrational result, respondents are essentially without recourse to appeal it.

John Worden is a partner in Venable LLP's San Francisco office and chair of the San Francisco Bar Association's ADR/Arbitration Section. Matt Broccolo is a senior associate in Schiff Hardin's New York office. Both authors have arbitrated many cases in many different states, usually with success.

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[1] *Shearson/Am. Exp., Inc. v. McMahon*, 482 U.S. 220 (U.S. 1987).

[2] *Rodriguez de Quijas v. Shearson/Am. Exp., Inc.*, 490 U.S. 477 (U.S. 1989).

[3] *McMahon* provided that agreements to arbitrate under the Securities Exchange Act of 1934 were enforceable while *Rodriguez* provided that agreements to arbitrate under the Securities Act of 1933 securities act were enforceable. *See McMahon*, 482 U.S. at 238*; Rodriguez*, 490 U.S. at 485–86.

[4] Jill I. Gross, *The End of Mandatory Securities Arbitration*, 30 Pace L. Rev. 1174, 1177 (2010).

[5] Mark Schoeff Jr., *Bills would end mandatory arbitration in adviser, broker contracts*, Investment News (May 4, 2019, 2:01 pm) https://www.investmentnews.com/article/20190304/FREE/190309977/bills-would-end-mandatory-arbitration-in-adviser-broker-contracts.

[6] *See Id.* One bill was introduced by Senator Blumenthal in the Senate, the other by Representative Johnson in the House. *See* H.R. 1423, 116th Cong. (as introduced in House, February 28, 2019); *see also* S. 610, 116th Cong. (2019).

[7] Schoeff, *supra* note 5.

[8] Press Release, *FAIR Act: The Forced Arbitration Injustice Repeal Act*, Hank Johnson Media Center (Sept. 20, 2019). https://hankjohnson.house.gov/sites/hankjohnson.house.gov/files/documents/The%20FAIR%20Act%20One%20Pager%20.pdf

[9] *Id.*

[10] While prior bills calling for an end to mandatory arbitration in brokerage customer disputes seem to languish and die, Representative Johnson's FAIR Act bill has gained some momentum. It passed the Democratic-majority House on September 20, 2019, and is now in the Senate just over a year before the 2020 election. *See* H.R. 1423, 116th Cong. (as passed by House September 20, 2019). Should the Senate and Presidency swing to the Democrats in 2020, arbitration clauses in consumer contracts may become a thing of the past.

[11] FINRA Customer Arbitration Rule 12505 ("The parties must cooperate to the fullest extent practicable in the exchange of documents and information to expedite the arbitration.").

[12] We have examined securities arbitrations here because there is data available to analyze, unlike in other types of arbitrations.

[13] CFI is an entity specializing in arbitration data analytics (among other things).

[14] United States District Courts – National Judicial Caseload Profile (June 30, 2019) https://www.uscourts.gov/sites/default/files/data_tables/fcms_na_distprofile0630.2019.pdf.

[15] *See* FINRA Customer Arbitration Rule 12512 ("Unless circumstances dictate the need for a subpoena, arbitrators shall not issue subpoenas to non-party FINRA members and/or employees or associated persons of non-party FINRA members at the request of FINRA members and/or employees or associated persons of FINRA members.").

[16] *See, e.g.*, *Hay Grp., Inc. v. E.B.S. Acquisition Corp.*, 360 F.3d 404, 407 (3d Cir. 2004) (noting that "the only power conferred on arbitrators with respect to the production of documents by a non-party is the power to summon a non-party 'to attend before them or any of them as a witness and in a proper case to bring with him or them any book, record, document or paper which may be deemed material as evidence in the case'") (citation omitted).

[17] *See, e.g.,* Fed. R. Civ. P. 12(b)(6); Cal. Civ. Proc. § 430.10(e).

[18] *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (U.S. 2009), citing *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (U.S. 2007).

[19] *Twombly*, 550 U.S. at 555.

[20] 137 S. Ct. 2042, 2049 (U.S. 2017).

[21] FED. R. EVID. 402 ("Irrelevant evidence is not admissible."); *See, e.g.*, Cal. Evid. Code § 350 ("No evidence is admissible except relevant evidence.").

[22] FED. R. EVID. 802. ("Hearsay is not admissible unless any of the following provides otherwise: a federal statute; these rules; or other rules prescribed by the Supreme Court.").

[23] FED. R. EVID. 602 ("A witness may testify to a matter only if evidence is introduced sufficient to support a finding that the witness has personal knowledge of the matter.").

[24] FED. R. EVID. 403.

[25] We are not joking.

[26] Karen Donovan, *Fix Arbitration Now*, Wealth Management, (Jan 1, 2007). https://www.wealthmanagement.com/archive/fix-arbitration-now.

[27] *See, e.g.*, FINRA Customer Arbitration Rule 12904(b) ("Unless applicable law directs otherwise, all awards rendered under the Code are final and are not subject to review or appeal."); *but see* Rule 34 of JAMS Comprehensive Arbitration Rules & Procedures ("The Parties may agree at any time to the JAMS Optional Arbitration Appeal Procedure.").

[28] 9 U.S.C. § 10 (2002).

[29] *See, e.g., Brown v. Rauscher Pierce Refsnes, Inc.*, 994 F.2d 775, 779 (11th Cir. 1993).

[30] *See, e.g., Local 863 Int'l Bhd. of Teamsters, Chauffeurs, Warehousemen & Helpers of Am. v. Jersey Coast Egg Producers, Inc.*, 773 F.2d 530, 533 (3d Cir. 1985) (stating that "a court [may not] disturb an arbitrator's award because it finds an error of law," instead requiring a finding that the "arbitrator's decision evidences manifest disregard for the law rather than erroneous interpretation of the law").

[31] FINRA Customer Arbitration Rule 12904(g).

[32] Parties may sometimes agree to an appeal process laid out by the arbitration clause in their contract. This adds a layer of protection against unfair or unreasonable awards that would otherwise not be appealable. However, this is available as an option in every forum. Notably, FINRA provides no right of appeal or ability to provide for an appeal mechanism in contracts.

[33] Restatement (Second) of Torts § 908 (1979).

[34] Cal. Civ. Code § 3294(b) (1992).

[35] *See id.* Additionally, the statute provides that the behavior triggering punitive damages on the part of a corporate employer must be on the part of an officer, director, or managing agent of the corporation.

[36] These statistics were taken from data collected by CFI.

[37] Dispute Resolution Statistics, FINRA, (September 2019) https://www.finra.org/arbitration-mediation/dispute-resolution-statistics.

[38] Thomas H. Cohen & Kyle Harbeck, *Punitive Damage Awards in State Courts, 2005*, U.S. Department of Justice Office of Justice Programs, Bureau of Justice Statistics (March 2011), https://bjs.gov/content/pub/pdf/pdasc05.pdf.