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The Arbitration of Employment Disputes in the Securities Industry: A Study of FINRA Awards, 1986-2008

Abstract

[Excerpt] This article reports on the results of our recent study of 3,200 arbitration awards issued in employment cases administered under the auspices of FINRA, its predecessor the National Association of Securities Dealers (NASD), and the New York Stock Exchange (NYSE). It responds to Colvin's call for more empirical research while providing some data on the debate over the fairness of mandatory employment arbitration agreements in the securities industry.

After disclosing the limitations of our study and presenting our findings with regard to the FINRA cases, we consider how these findings bear on the debate about mandatory arbitration, specifically whether or not our findings show a repeat player effect in the FINRA employment cases, or show that employees fared better under FINRA's voluntary arbitration than under mandatory arbitration, or that FINRA employment arbitration does not protect employee civil rights.

Keywords

arbitration, awards, Financial Industry Regulatory Authority, FINRA, securities industry, employment disputes

Disciplines

Dispute Resolution and Arbitration | Finance and Financial Management | Labor and Employment Law | Labor Relations

Comments

Suggested Citation

Lipsky, D. B., Seeber, R. L., & Lamare, J. R. (2010). The arbitration of employment disputes in the securities industry: A study of FINRA awards, 1986-2008 [Electronic version]. *Dispute Resolution Journal*, 65(1), 54-61.

Required Publisher's Statement

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The Arbitration of Employment Disputes in the Securities Industry:

A Study of FINRA Awards, 1986-2008

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We are grateful to Alex Colvin for his comments on an earlier version of this paper.

We also want to thank Abhishek Gupta, Caralyn Olie, and Missy Herrington for their invaluable assistance in the preparation of this article. The authors are solely responsible for any errors of fact or interpretation contained in the article.

The arbitration of employment disputes has been the subject of intense interest in recent years. On the one hand, proponents of the process maintain that arbitration provides a faster and cheaper means of resolving employment disputes than litigation. On the other hand, despite numerous supportive decisions on arbitration by the U.S. Supreme Court,¹ opponents argue that arbitration is not an adequate substitute for a judicial forum because it does not provide a level playing field. They maintain that employers experienced in arbitration enjoy an advantage in arbitration over inexperienced employees (the so-called “repeat player effect”).² They also express concerns that mandatory arbitration “undermines the development of public law for civil rights and consumer rights, because there is no meaningful judicial review of arbitrators’ decisions.” They contend that voluntary arbitration is more advantageous to employees. In addition, they say that employees have a better chance of winning in post-dispute voluntary arbitration than they do under mandatory arbitration, and that “arbitrators enjoy near complete freedom to ignore the law and even their own rulings because they know that their rulings will not be seriously examined by a court applying current law.”³

Several of these criticisms of mandatory and consumer arbitration are

stated in the findings section of a bill that Congress is currently considering, called the Arbitration Fairness Act (AFA).⁴ This bill would amend the Federal Arbitration Act (FAA) to ban the use of mandatory pre-dispute arbitration agreements in employment, consumer, franchise, and civil rights disputes.⁵

However, the issues raised by the AFA “findings” have yet to be fully examined using systematic, comprehensive empirical data. Only within the last decade or so have researchers begun to do serious statistical analyses of critical issues in arbitration. In the August-October 2009 issue of this journal, our Cornell colleague, Alexander Colvin, explained that the research gap is due in part to “the dearth of publicly available data on which to conduct empirical research that would help evaluate the arguments of both sides of the employment arbitration debate.”⁶ He noted that what little research exists “is based on data made available to individual researchers by arbitration service providers,” such as the American Arbitration Association (AAA) and the Financial Industry Regulatory Authority (FINRA), which adminis-

ters employment and consumer arbitration for the securities industry. After reviewing some of the principal empirical studies of employment arbitration and discussing his own research, Colvin ultimately concluded that the picture is still not complete. “[W]e are still trying to answer basic questions about the general characteristics of [the employment arbitration] dispute resolution system,” he wrote.⁷

This article reports on the results of our recent study of 3,200 arbitration awards issued in employment cases administered under the auspices of FINRA, its predecessor the National Association of Securities Dealers (NASD), and the New York Stock Exchange (NYSE).⁸ It responds to Colvin’s call for more empirical research while providing some data on the debate over the fairness of mandatory employment arbitration agreements in the securities industry.

After disclosing the limitations of our study and presenting our findings with regard to the FINRA cases, we consider how these findings bear on the debate about mandatory arbitration, specifically whether or not our

(Continued on page 54)



The Arbitration of Employment Disputes in the Securities Industry: A Study of FINRA Awards, 1986-2008

(Continued from page 12)

findings show a repeat player effect in the FINRA employment cases, or show that employees fared better under FINRA's voluntary arbitration than under mandatory arbitration, or that FINRA employment arbitration does not protect employee civil rights.

Importance of Securities Cases

Although an analysis of the securities customer-broker cases would clearly be valuable (since there are so many more of them⁹), our professional interest in employment relations led us to focus only on the employment awards. In any event, it is clear that the securities industry is an important focus for the study of consumer and employment arbitration because our contemporary arbitration system can, in large part, be traced to practices that had their origins in that industry. Several of the U.S. Supreme Court's most important decisions regarding arbitration originated in the securities industry. For example, *Shearson/American Express v. McMahon*,¹⁰ held that an investor who signed a pre-dispute arbitration agreement with a brokerage firm could be compelled to arbitrate claims arising under the Securities and Exchange Act. In *Rodriguez de Quijas v. Shearson/American Express, Inc.*,¹¹ the Court overturned *Wilco v. Swan*,¹² which held that claims arising under the Securities Act could not be compelled to arbitration by means of a contract.

Most critically for employment relations, the Supreme Court's seminal decision in *Gilmer v. Interstate/Johnson Lane, Corp.*,¹³ held that a broker-employee who had signed a registration form (Form U4) with the SEC requiring the use of arbitration to resolve statutory claims had waived his right to take an age discrimination claim to the federal courts. The *Gilmer* case is widely credited with ushering in the widespread use of mandatory pre-dispute arbitration agreements in employment relations.¹⁴

Overview of FINRA's Arbitration Program

The securities employment arbitration program began in 1986. Between 1986 and 2008, about 3,200 employment awards were issued. The NASD was the principal administrator but the NYSE also administered cases. This changed in 2007, when FINRA was established. FINRA assumed the NASD's enforcement and regulatory functions and the NYSE and NASD dispute resolution programs were consolidated under FINRA's authority.¹⁵

According to the FINRA Web site, FINRA is "the largest independent regulator for all securities firms doing business in the United States," overseeing nearly 4,768 brokerage firms and 634,000 registered securities representatives. FINRA also administers "the largest dispute resolution forum for investors in registered firms."¹⁶ It also administers the employment arbitration program for the securities industry under the Code of Arbitration Procedure for Industry Disputes (Industry Code). Rule 13200 of the Industry Code requires a dispute to be arbitrated if it arises out of the business activities of a "member" or an "associated person" and is between or among members, associated persons, or members and associated persons. Members are brokers and dealers and associated persons are people associated with them (i.e., employees). The employees in FINRA employment cases are brokers registered with the SEC and authorized to recommend and execute buy-sell orders, known as registered representatives.

(These cases make up about 23% of all FINRA filings.¹⁷) It is estimated that about one-third of the employees in the securities industry are registered representatives.¹⁸ We use the term "employee" in this article to refer only to registered representatives.

Limitations of the FINRA Experience

We must acknowledge some limitations in our analysis of the FINRA employment cases. Although it is one of the largest mandatory arbi-

The securities industry is an important focus for the study of arbitration because our contemporary arbitration system can, in large part, be traced to practices that had their origins in that industry.

tration programs in the country, it probably constitutes a relatively small proportion of the total number of employment claims that are arbitrated under mandatory arbitration procedures.¹⁹ Also, not all the cases were arbitrated under mandatory procedures. The reason is that while the securities industry used mandatory arbitration to resolve all employment claims from 1986-1999, in 1999 the SEC approved the industry's request to make arbitration of employment discrimination claims voluntary under Rule 13201 of the Code of Arbitration Procedure.²⁰ That rule became effective Jan. 1, 2000. However, other types of employment claims remain subject to mandatory arbitration under Rule 13200.

Simultaneously with the change to voluntary arbitration of employment discrimination claims in 2000, the SEC also approved other changes to the rules governing discrimination claims. After 1999, arbitrators hearing discrimination claims had to have a law degree, membership in a bar association, substantial familiarity with the law, 10 or more years of experience in law practice, law teaching, or government enforcement of equal employment opportunities statutes, or experience as a judge, arbitrator or mediator, or in-house counsel with such matters. In addition, the chair of a panel or a single arbitrator in a discrimination case may not have represented primarily the views of employers or of employees within the previous five years.²¹

Some Findings of Our Study

Our study examined four variables: the types of claims involved in FINRA awards, the average size of the awards, the amounts awarded and the time it took to render the awards. Each will be examined in turn.

Types of Claims. Figure 1 shows the types of claims made by employees. Out of 3,200 FINRA cases analyzed:

- in 28%, employees claimed the employer denied them compensation allegedly owed;
- in 27.4%, employees claimed the employer had defamed them in some fashion (e.g., by alleging they had “churned” a customer’s account);
- in 13.5%, employees claimed they were wrongfully terminated; and
- in 8.4%, employees claimed their employer breached the contract.

Cases involving a claim of statutory discrimination constituted 17.1% of the total.

In every case, the employee (and counsel) presented the arbitrator with a monetary figure representing the damages associated with the claim.

This figure usually included the claimant’s demand for back pay and often included a claim for punitive damages. In each case, the employer denied that the employee’s claims had merit (and sometimes filed counterclaims). The employer’s position in each case was that the arbitrator should not award the employee any money at all.

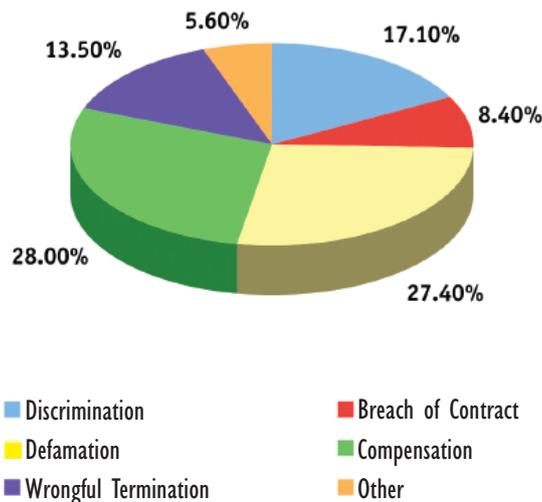
The Size of the Monetary Awards. In 61% of the cases, the arbitrator found sufficient merit in the employee’s claim to award the employee an amount of money greater than zero. The total sum awarded to employees over the life of the program exceeds \$467 million.

The average (or mean) award across all cases is about \$146,000 [\$467 million divided by 3,200]. However, the average award is elevated because of a handful of very large awards. The 10 largest awards, for example, accounted for 22% (over \$101 million) of the total, and the 20 largest cases accounted for nearly 30% (about \$138 million).

The single largest award was \$27.6 million (of which \$25 million was for punitive damages) in a case called *Sawtelle v. Waddell & Reed*.²² One commentator called this a landmark case, saying it “will go down in Wall Street history as the longest arbitration and the largest punitive damage award ever given to a financial advisor.”²³

From filing through arbitration to appeals and settlement, *Sawtelle* took 12 years. In 2001, a three-person arbitration panel found that Waddell had “orchestrated a campaign of deception” against Sawtelle and implied to clients that he had mishandled their accounts, was untrustworthy, had left the business, and was even “in

Figure 1.
Percentage of Employment Cases by Type



some way involved with the embezzling of client funds.”

In addition to the \$25 million in punitive damages, the panel awarded Sawtelle \$1.8 million in compensatory damages (plus compound post-judgment interest), and \$747,000 in attorney fees. The panel also ordered that the defamatory information Waddell and Reed had placed in Sawtelle’s SEC file be expunged.

Waddell sought to vacate the award, but the New York trial court modified the award only slightly. On further appeal, the New York Appellate Division vacated the punitive damages award and “remanded to the original panel of arbitrators for reconsideration of the issue of punitive damages.”²⁴ On remand, the same arbitrators again held the respondents liable for \$25 million in punitive damages. Once again the Appellate Division vacated the punitive damages award and remanded the matter back to arbitration.²⁵ Sawtelle appealed the Appellate Division’s decision to the New York Court of Appeals, New York’s highest court, but the court declined to take the case. To avoid further litigation, the parties negotiated a settlement that resulted in Sawtelle receiving about \$10 million.²⁶

The *Sawtelle* case is clearly the exception to the norm in FINRA employment arbitration. In fact, the median amount claimed in these cases was \$375,000, while the median amount awarded was only \$1,000—a mere quarter of a percent of the amount claimed.

Economists analogize outcomes of the type we found here to a sports tournament: for example, in a tennis or a golf tournament, a small number of entrants are top prize winners and therefore receive very large purses, but the vast majority of entrants in the tournament receive very little or nothing.²⁷

A tournament has a distribution of outcomes that statisticians would term “skewed.” In a skewed distribution the mean (or simple average) of the distribution is either higher or lower than the median (which is the value of the observation exactly at the mid-point of the distribution; i.e., 50% of the observations in the distribution are higher than the median and 50% are lower). Only in a normal distribution (which has the

familiar bell-shaped curve) are the mean and median values of the distribution equal.

It is not unusual to find skewed distributions in other areas of life. Economists have noted that many labor markets seem to resemble tournaments; for example, in the performing arts, a relatively small number of actors receive extremely high levels of compensation (some actors receive \$20 million or more to appear in a single motion picture), whereas the vast majority of actors earn very little.²⁸ There are two fundamental approaches to judging whether a market, an organization, or a dispute resolution process is fair and

equitable: “Distributive justice” calls for a judgment about whether the outcomes are just or fair; “procedural justice” calls for a judgment about whether the procedures followed during the process are just or fair.²⁹ Some people judge fairness on the basis of outcomes. They believe that any process that produces extremely high salary for actors and baseball players, and very large bonuses for Wall Street bankers, must be inherently unfair.

We are reluctant to make such judgments based only on the size and distribution of FINRA awards. In our view, standards of procedural justice should be used to evaluate the fairness of an arbitration program: Thus, the rules and procedures that govern in these

cases—the inputs, rather than the outputs—must be examined.

Employee Win Rates. Researchers frequently use “win rates” to evaluate arbitration outcomes, but the term “win” is obviously sensitive to precisely how it is defined. For instance, a “win” might be defined to mean that the arbitrator awarded some amount of money to the claimant, regardless of how little the award or the relationship of the award to the amount claimed. (For example, a \$1,000 award to an employee who claimed \$10 million in damages.) Even though the employee receiving this amount probably would not think of this as a win, most empirical researchers would, since they consider any award of money to an employee to be a victory for the employee because the arbitrator found liability on the part of the employer.³⁰ If we use this definition, then the employee win rate in the FINRA cases we studied is 61%, while the employer win rate is 39%.

Our study examined four variables in the FINRA awards: the types of claims involved, the average size of the awards, the amounts awarded and the time it took to render the awards.

Suppose we redefine a win to mean any case in which the award is greater than 50% of the amount claimed. Using this definition of a win, the employee win rate drops to about 20% and the employer win rate jumps to 80%.

There is wide variation in the findings of previous research on win rates in employment arbitration cases.³¹ In the majority of these studies, a win is defined as any award in which the employee receives any amount of money.³² The win rates in these studies range from a low of 20% to a high of 74%.³³ The employee win rate in our study of the FINRA cases sits firmly within the range of employee win rates found by other researchers.

Swiftness of the Proceedings. To gauge the swiftness of the proceedings in FINRA cases, we examined three different time-related variables:

We also considered how our findings relate to several controversial issues, including, for example, the repeat player phenomenon, and the ability of arbitration to vindicate civil rights.

(1) the time between the filing of the demand and the issuance of the award; (2) the time between the final hearing session and the issuance of the award; and (3) the number of hearing sessions in each case. (FINRA defines a hearing session as half a day.)

The mean elapsed time between filing of a complaint and issuance of an award was 513 days, or about 17 months. The mean elapsed time between the final hearing session and the issuance of an award was 110 days, or a little less than four months. The mean number of hearing sessions was 7.4 (i.e., 3.7 days).

Once again the distribution of hearing sessions across all cases was highly skewed. The median number of hearing sessions was 4.0 (i.e., 2 days). The three longest cases had 201, 145, and 108 sessions, but excluding those cases from the calculation of the mean had almost no effect: it reduced that statistic from 7.4 to 7.23 sessions.

Our findings regarding the speed of FINRA employment arbitration compares favorably with employment arbitration in other fora. For example, Theodore Eisenberg and Elizabeth Hill reported that the mean time between filing to disposition of an employment discrimination claim in federal court was 709 days, or nearly 2 years.³⁴

Michael Delikat and Morris Kleiner examined

over 3,000 employment discrimination cases filed in federal court in New York during the period 1997-2001; they found only 125 cases (3.8%) resulted in a trial to conclusion and a median time from filing to verdict of 25 months. They also examined 186 NASD cases conducted during the same period; they found a median time of 16 months from filing to the issuance of the award.³⁵ This was 33% sooner than in the federal court cases.

More recently Colvin examined 849 AAA employment arbitration cases, finding a mean time from filing to decision of 332 days—about 11 months.³⁶

We tentatively conclude that 17 months between filing a FINRA case and issuance of the award compares favorably to the 25-month period for litigating discrimination cases in federal court, but not as favorably to AAA employment

arbitration that did not involve employment discrimination claims.

How Our Findings Relate to the Debate Over Employment Arbitration

Our analysis of the FINRA awards casts light on three major issues raised by critics of mandatory employment arbitration. First, do repeat employers have an advantage over one-shot employees? Second, is voluntary arbitration more advantageous for employees than mandatory arbitration? Third, does employment arbitration provide adequate protection of employees' civil rights?

The Repeat Player Effect. Some scholars believe that employers are repeat players in arbitration and therefore have an advantage over employees who are first-time players in employment arbitration. They contend that employers are likely to have more arbitration experience and better representation in arbitration than employees.³⁷

Empirical researcher Lisa Bingham uncovered the repeat player effect in several empirical studies of employment arbitration.³⁸ For example, in a study of 244 employment arbitration cases, Bingham found an employee win rate of 29% when the case involved a repeat employer and a win rate of 62% when there was no repeat

employer. Bingham replicated her results in follow-up studies.³⁹

In our examination of the possible existence of a repeat player effect in FINRA employment arbitrations, we came to realize that the concept is not as clear as one might think. Previous researchers would have counted an employer as a repeat player in employment arbitration if they found the employer’s name repeated in additional cases. But there are factors that weigh against this method of counting repeat players. Should a firm that has been involved in a merger, acquisition, or restructuring be considered the same firm? Suppose there are long gaps between a firm’s involvement in one FINRA arbitration case and its involvement in another (for example, one in 1998 and another 10 years later). Suppose a firm has been involved in several FINRA cases, but the cases have been conducted at different locations. What if the attorney representing the firm is different in each case? Previous researchers have not made these distinctions.

An examination of the FINRA employment cases reveals that the attorneys representing a single securities firm changed from case to case. Should the firm be considered a repeat player only if it is represented by the same attorney? If the attorneys change from one arbitration case to another, then perhaps the firm should be considered a repeat player only if it has an “institutional memory.” By this we mean that a firm passes on its experience in previous employment arbitration cases to the new attorneys.

It also should not be assumed that only firms are repeat players. Even if an employee has never previously been involved in an employment arbitration, the employee’s attorney may have represented multiple employees in the past. In the FINRA cases, we found some law firms that had repeatedly represented different employees.⁴⁰ If the employee is represented by a highly experienced, successful attorney, then the disadvantage the employee is alleged to have by virtue of being a one-shot player is certainly diminished, if not eliminated.

We also need to consider whether the experience of the parties and their attorneys in other fora (such as in employment cases administered by the AAA) could make all of them repeat players. This experience is undoubtedly relevant to the skills the attorneys are able to exercise in FINRA cases.

We have not yet explored all the possible dimensions of the repeat player phenomenon in the FINRA cases. However, using the conventional definition of a repeat player, we have analyzed who the repeat players are in the FINRA

employment arbitration cases. Table 1 shows that some major securities firms had scores of arbitration cases during the existence of the FINRA arbitration program. Over 19% of all FINRA awards involved the same five firms, about 30% involved the same 10 firms. On average, one of these firms was the respondent in 88 cases.

The average number of cases in which the other firms were involved was 2.6. We performed various statistical tests to determine whether the win rates of the firms that were major users of the FINRA arbitration program were higher than the win rates of firms that had been involved in only one or two cases. For example, we compared the win rate of the top five firms with the win rate of all other firms; we also compared the win rate of the top ten firms with the win rate of all other firms.

Table 1: Number of Awards in Cases Involving the Top Five Users of the FINRA Employment Arbitration Program

Company Name	Number of Awards	Percent of Total Awards
Prudential	213	6.7
Merrill Lynch	168	5.3
Citigroup	80	2.5
A.G. Edwards	74	2.3
PriceWaterhouseCoopers	73	2.3
<i>Total</i>	<i>608</i>	<i>19.1</i>

For these tests we considered an employer win to be any case in which the arbitrator awarded nothing to the employee. Under this definition the firms as a group won about 39% of the cases. The top ten firms had a win rate of 46.7%, while the top five had a win rate of 50.2%. The win rate for all other firms was 35.%.

These differences are statistically significant.⁴¹ However, when we conducted a multivariate regression analysis, using the size of the award (corrected for inflation) as the dependent variable and a repeat player variable as one of several explanatory variables, we found that the repeat player variable had no significant effect on the size of the award. This finding suggests that other factors (such as the size of the claim, the nature of the charge, etc.) may have more influence than their experience in arbitration on the size of the awards of the top five or ten firms. Put another way, despite the higher win rates of the repeat players with the most experience in FINRA arbitration, there may not be a causal

relationship between that experience and the size of the firms' awards.⁴²

Mandatory versus Voluntary Arbitration. Critics of mandatory arbitration maintain that the distinction between mandatory and voluntary arbitration has a significant effect on arbitration outcomes: employees, they argue, are at a disadvantage under mandatory arrangements and are likely to receive lower awards than they would if they had the option of voluntarily using arbitration after a dispute arises. FINRA's changes in the handling of arbitration of employment discrimination cases after 1999 has provided an opportunity to compare two distinct arbitration regimes: a mandatory regime with somewhat looser procedures and a voluntary regime with more stringent procedures.

One effect we found was a dramatic decline in the number of discrimination awards after 1999. From 1986 through 1999, there were 288, an average of 22 a year. From 2000 through 2008, there were only 50 discrimination awards, an average of six awards a year.

Because we only studied FINRA employment cases that went to an award, we cannot determine whether there was a drop in discrimination case filings. Nevertheless, we think it reasonable to postulate that after 1999, when employees in the securities industry were no longer compelled to arbitrate discrimination claims, most chose litigation.

We also found that after 1999 the mean and median awards in discrimination cases significantly increased. From the inception of the employment program through 1999, the mean was \$66,405 and the median was \$225. After 1999, the mean award was \$183,728 and the median was \$578.

These differences are statistically significant. Once again we used multiple regression analysis to control for other factors that might influence the size of the awards in discrimination cases. We found that, when other factors influencing awards were controlled, the awards in discrimination cases were about \$11,500 higher after 1999 than they had been before 1999, representing about an 8% increase in the size of discrimination awards.⁴³

Our analysis of the FINRA data strongly suggests that there is no other factor that can explain the drop in the number of discrimination awards

and the increase in the size of awards in those cases after 1999, other than the change from mandatory to stricter voluntary procedures. This provides some support to the critics of mandatory arbitration, although additional evidence is required before firm conclusions can be drawn.

The Protection of Civil Rights

Regarding the protection of civil rights, we have not uncovered any evidence that mandatory arbitration in the securities industry undermined civil rights because of a lack of "meaningful judicial review" of arbitration awards. Readers of the *Dispute Resolution Journal* understand that courts give great deference to arbitral decisions and in

general are reluctant to vacate them.⁴⁴ However, they have shown greater willingness to scrutinize awards when consumers and employees with statutory claims challenge the arbitration process on the ground of unconscionability.⁴⁵ These decisions have provided important guidance to arbitration providers and arbitrators as to what constitutes a fair arbitration procedure.

We have not found any court decisions dealing with unconscionability that arise out of a FINRA or NASD employment arbitration case. FINRA and NASD rules were designed to be fair and avoid the taint of unconscionability. Whenever critics have pointed to weaknesses in the

rules (as in the case of discrimination claims), FINRA has generally tried to correct those weaknesses.

With the help of several graduate students, we read a large sample of the employment arbitration awards, searching for cases in which the arbitrator or panel failed to give due regard to claims of employment discrimination. Our examination did not reveal any FINRA cases in which the arbitrators, in our judgment, failed to adequately weigh employee claims of discrimination. We found this to be true under both mandatory and voluntary arbitration regimes.

Critics of mandatory arbitration might argue that our examination was insufficient, but we believe it is a first step in making a judgment on this important question, if only in the context of a single industry.

A related question we considered is whether arbitrators who decide workplace disputes have the skills, experience, and qualifications to decide

The employee win rate in the FINRA employment cases fell within the range of employee win rates found by other researchers.

statutory employment discrimination claims. The NASD and its successor FINRA have both shown great concern about the qualifications of arbitrators to hear statutory complaints. This was a major reason why the NASD introduced stricter qualification requirements for arbitrators hearing discrimination cases in 1999. Today, FINRA requires all arbitrators newly admitted to its roster to undergo training and standardized testing.⁴⁶ It also requires all arbitrators on its roster to be trained in new and revised rules of procedure, as well as in special topics, such as motions to dismiss and expungement.

In sum we have not uncovered any evidence that the FINRA arbitration program has failed to protect the civil rights of claimants.

Conclusions

Our study of FINRA's employment arbitration program had the purpose of providing an overview of the FINRA experience and determining whether that experience exhibited deficiencies of the type described by critics of mandatory employment arbitration. Although our analysis is admittedly limited, it does allow us to draw two tentative conclusions. First, employment arbitration under FINRA does not appear to be substantially different from employment arbitration administered by other providers.

Second, the switch from mandatory to voluntary procedures produced mixed results: it reduced the number of discrimination awards (and possibly the number of discrimination claims moving to arbitration), but it increased the size of the awards in such cases.

We also found evidence of a correlation between the win rate and the experience of the brokerage firms that most often use FINRA arbitration cases. Although this suggests a repeat player effect, more sophisticated analysis suggests that other factors are more important in predicting the size of the awards than previous experience in FINRA arbitration.

Our analysis does not deal with other criticisms of mandatory arbitration. We believe that research still needs to be undertaken into many aspects of employment arbitration, including, for example, access to the arbitration process, the criteria used to decide arbitral issues, the relationship between the type of claim and the outcome, and the nature of non-monetary claims, counterclaims and awards.

In the meantime, we hope our study sheds additional light on the FINRA employment arbitration process and the validity of criticisms of mandatory arbitration. We plan to continue to analyze the FINRA cases and hope to have additional results to report in the future. ■

ENDNOTES

¹ Most notably, *Gilmer v. Interstate/Johnson Lane, Corp.*, 500 U.S. 20 (1991) and *Circuit City Stores v. Saint Clair Adams*, 532 U.S. 105 (2001).

² The repeat player effect is based on the belief that sophisticated employers, by virtue of their knowledge and experience of the arbitration process, are likely to have an edge over employees involved in employment disputes, who are much less likely to have had any previous experience in arbitration. For a discussion of the repeat player effect, see, Ronald L. Seeber & David B. Lipsky, "The Ascendancy of Employment Arbitrators in U.S. Employment Relations: A New Actor in the American System?" 44(4) *British J. of Indus. Rel.*, 729-35 (Dec. 2006).

³ The quoted language is contained in both H.R. 1020 and S. 931. H.R. 1020 and S. 931 were introduced in the House and the Senate, respectively, in 2009. The AFA is actually a series of amendments to the Federal Arbitration Act.

⁴ See *supra* n.3.

⁵ A pre-dispute employment arbitration agreement results when an employer requires its employees to sign an

agreement waiving the right to resolve future employment disputes in court and instead requiring such disputes to be submitted to arbitration.

⁶ Alexander J. S. Colvin, "Employment Arbitration: Empirical Findings and Research Needs," 64 (3) *Disp. Resol. J.*, 6 (2009).

⁷ *Id.* at 11.

⁸ FINRA, the NASD and the NYSE were all classified as self-regulatory organizations (SROs). The Securities and Exchange Commission (SEC), the major federal regulatory agency for the securities industry, delegates to the SROs responsibility for enforcing certain industry standards and requirements related to brokerage and trading activities.

⁹ Between 1994-2008, over 90,000 investor claims were filed. Compare this with the employment data: Between 1986 and 1993 there were about 600 employment arbitration awards. There was only one employment claim filed in 1986, and only seven filed in 1987. However, in 1988 56 employment claims were filed; by 1994 the number of claims had reached 201 (according to records made available to the authors by FINRA).

¹⁰ 482 U.S. 220 (1987).

¹¹ 490 U.S. 477 (1989).

¹² 346 U.S. 427 (1953).

¹³ 500 US 20 (1991).

¹⁴ For a discussion of the significance of *Gilmer*, see David B. Lipsky *et al.*, *Emerging Systems for Managing Workplace Conflict: Lessons from American Corporations for Managers and Dispute Resolution Professionals* 198-212 (Jossey-Bass 2003).

¹⁵ All FINRA/NASD/NYSE securities industry rules must be approved by the SEC.

¹⁶ www.finra.org/AboutFINRA/index.htm.

¹⁷ Rule 13000 *et seq.*, Code of Arbitration Procedure for Industry Disputes, in the FINRA Manual.

⁷ For information about FINRA dispute resolution programs and arbitration rules, see www.finra.org/index.htm; Other sources include Janice Kwon, "Securities Industry Arbitration: Overview of the Industry and the Debate Over Self-Regulatory Organizations," unpublished paper prepared for the Association for Conflict Resolution Task Force charged with examining the Arbitration Fairness Act of 2009; *Invest-*

tor's Guide to Securities Industry Disputes: How to Prevent and Resolve Disputes with Your Broker (Jill Gross & Alice Oshins, eds., Pace Law School and FINRA Investor Education Foundation, n.d.) Very little legal or empirical research has been conducted on arbitration in the securities industry. For some recent papers see, Symposium, "The Current State of Securities Arbitration," 76 *U. Cin. L. Rev.* 459 (2007-08).

¹⁸ "Employment Discrimination: How Registered Representatives Fare in Discrimination Disputes" (U.S. GAO, March 1994).

¹⁹ The AAA has reported to us that it administers over 4,000 employment arbitration programs that have been judged to comply with the "Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of the Employment Relationship." For discussion of this protocol, see John T. Dunlop & Arnold M. Zack, *Mediation and Arbitration of Employment Disputes* (Jossey-Bass 1997). Colvin is currently conducting research on the arbitration cases that have arisen under these programs; he believes the vast majority call for mandatory arbitration.

²⁰ Effective Jan. 1, 1999 "the NASD removed from the Code of Arbitration Procedure ... the requirement for registered persons to arbitrate claims of statutory employment discrimination," NASD "Employment Arbitration Rules: SEC Approves New Arbitration Disclosure Rule and Procedures for Employment Arbitration," NASD Notice to Members 99-96, Dec. 1999, p. 735. The NASD noted that the "rule change did not affect private arbitration agreements that might exist between employees and member firms," p. 738. For a report dealing with the arbitration of discrimination claims in the securities industry, see GAO report, *supra* n. 18.

²¹ Rule 13802, FINRA Code of Arbitration Procedure, adopted 1999.

²² *Sawtelle v. Waddell & Reed, Inc.*, (Docket No. 97-03642, award issued Aug. 7, 2001; 2001 NASD Arb. Lexis 820).

²³ Paul Glen Neuman, "Stephen B. Sawtelle, the \$27 Million Man," *J. for Managers and Principals of Fin. Serv. Firms*, found at www.brokerdealer-magazine.com/?p=333.

²⁴ *Sawtelle v. Waddell & Reed*, 304 A.D. 2d 103, 754 N.Y.S. 2d 264 (2003).

²⁵ *Sawtelle v. Waddell & Reed, Inc.*, 21 A.D. 3d 820, 801 N.Y.S. 2d 286 (2005).

²⁶ "Stephen B. Sawtelle v. Waddell & Reed," at www.zoominfo.com/people/Sawtelle_Stephen_98771757.aspx.

²⁷ For example, see Sheldon Rosen, "Prizes and Incentives in Elimination Tournaments," 76 (4) *Am. Econ. Rev.* 701-15 (1986); Ronald G. Ehrenberg & Michael L. Bognanno, "Do Tournaments Have Incentive Effects?" 98(61) *J. of Pol. Econ.* 1307-324 (1990); Ronald G. Ehrenberg & Michael L. Bognanno, "The Incentive Effects of Tournaments Revisited: Evidence from the European PGA Tour," 43 *Indus. & Lab. Rel. Rev.* 74-88. (Supp 1990).

²⁸ Will Smith was reportedly paid \$80 million for his motion picture work in 2009; Johnny Depp received \$72 million, reported at http://www.forbes.com/lists/2008/53/celebrities08_The-Celebrity-100_EarningsPrevYear.html on April 5, See also, Under the Stars: Essays on Labor Relations in Arts and Entertainment. (L.S. Gray & R.L. Seeber, eds., ILR Press 1996). Seeber noted that in a typical year the median compensation of a member of the Screen Actors Guild for film work is zero; that is, a majority of SAG members do not obtain roles in a movie in a typical year.

²⁹ These terms are associated with the work by John Rawls, *A Theory of Justice* (OUP, rev. ed. 1999). See also, Lawrence B. Solum, "Procedural Justice," 78 *So. Calif. L. Rev.* 181 (2004).

³⁰ An excellent summary of this research is contained in Mark D. Gough, Empirical Analysis of Employment Arbitration Decisions, Master of Science Thesis, Pa. State Univ., College of Liberal Arts, May 2009.

³¹ Virtually all of this research is based on cases administered by the AAA.

³² See Gough, *supra* n. 31. In a conversation with Gough, Colvin confirmed our view that the definition of a win used by most researchers is when any money is awarded to the claimant.

³³ Gough, *supra* n. 30.

³⁴ Theodore Eisenberg & Elizabeth Hill, "Arbitration and Litigation of Employment Claims: An Empirical Comparison," 58(4) *Disp. Resol. J.* 44-54 (2003).

³⁵ Michael Delikat & Morris M. Kleiner, "An Empirical Study of Dispute Resolution Mechanisms: Where Do Plaintiffs Better Vindicate Their Rights?" 58(4) *Disp. Resol. J.* 56 (Nov. 2003-Jan. 2004).

³⁶ Alexander J.S. Colvin, "Empirical Research on Employment Arbitration: Clarity Amidst the Sound and Fury?" 11(2) *Employee Rights & Employment Pol'y J.*, 405-47 (2008).

³⁷ Marc Galanter introduced the concept of a repeat player in "Why the

'Haves' Come Out Ahead: Speculations on the Limits of Legal Change," 9(1) *L. & Soc'y Rev.*, 95-160 (1974).

³⁸ Lisa B. Bingham & Shimon Sarraf, "Employment Arbitrations Before and After the Due Process Protocol for Mediation and Arbitration of Statutory Disputes Arising Out of Employment: Preliminary Evidence that Self-Regulation Makes a Difference," in *Alternative Dispute Resolution in the Employment Arena* 303-29 (S. Estreicher & D. Sherwyn, eds., Kluwer Law Int'l 2004).

³⁹ See, e.g., Lisa B. Bingham, "On Repeat Players, Adhesive Contracts, and the Use of Statistics," in "Judicial Review of Arbitration Awards," 29(2) *McGeorge L. Rev.*, 223-60 (1998).

⁴⁰ Liddle & Robinson, L.L.P., counsel to the claimant in the *Sawtelle* case, has represented numerous other claimants in FINRA cases.

⁴¹ We used a series of independent t-tests and found that the differences in means were significant at the .01 level.

⁴² Please contact us if you would like to receive a copy of our repeat player regression results.

⁴³ See our invitation in n. 42.

⁴⁴ The foundation for the judicial policy of deferral to arbitration in labor arbitration was laid most clearly in the "Steelworkers Trilogy"; see *Steelworkers v. American Mfg. Co.*, 363 U.S. 564 (1960); *Steelworkers v. Warrior & Gulf Navig. Co.*, 363 U.S. 574 (1960); and *Steelworkers v. Enterprise Wheel & Car Corp.*, 363 U.S. 593 (1960). Most recently the Supreme Court reaffirmed its faith in the arbitration process in *14 Penn Plaza v. Pyett*, 556 U.S. ___ (2009). For one account of the evolution of the policy of judicial deferral in labor and employment cases, see Lipsky *et al.*, *supra* n. 15 at 183-224.

⁴⁵ For examples of court decisions dealing with unconscionability, see *Hooters of Am. v. Phillips*, 173 F.3d 933 (1999); *Stirlen v. Supercuts*, 51 Cal. App. 4th 1519 (1997); *Ting v. AT&T*, 319 F.3d 1126 (2003); *Ingel v. Circuit City Stores*, 328 F.3d 1165 (2003); and *Armendariz v. Foundation Health Psych-care*, 6 P. 3d 669 (Calif. 2000).

⁴⁶ We thank George Friedman, executive vice president and director of dispute resolution for FINRA, for providing us with information about FINRA's training programs. The qualifications of labor arbitrators who decide statutory claims are examined in Michel Picher *et al.*, *The Arbitration Profession in Transition: A Survey of the National Academy of Arbitrators* (Cornell/PERC Institute on Conflict Resolution 2000).

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