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PREDISPUTE ARBITRATION AGREEMENTS BETWEEN BROKERS AND INVESTORS: THE EXTENSION OF WILKO TO SECTION 10(b) CLAIMS

I. INTRODUCTION

A broker and an investor sign a customer agreement. The agreement includes a clause requiring arbitration in the event the investor should have any dispute with the broker. A dispute does in fact arise, and the investor seeks to bring an antifraud action against the broker in federal court under section 10(b) of the Securities Exchange Act of 1934 (Exchange Act or 1934 Act). The broker moves for a stay and an order to compel arbitration under the Federal Arbitration Act. The investor responds that the Exchange Act provides a right to a judicial forum that cannot be waived by any stipulation and that this precludes enforcement of the arbitration agreement. The Supreme Court has recently granted certiorari to decide this conflict.

In Wilko v. Swan the Court held that predispute arbitration agreements were unenforceable when an investor brought a claim under section 12(2) of the Securities Act of 1933 (Securities Act or

2. Id. at §§ 78a-78kk.
4. Id. at § 4.
5. Id. at §§ 1-14.
7. Id. at § 78cc(a).
8. McMahon v. Shearson/American Express, Inc., 788 F.2d 94 (2d Cir.), cert. granted, 107 S. Ct. 60 (1986). The case also raises the issue of the arbitrability of RICO claims. This comment does not address that question.
10. Section 12 (b) provides:
Any person who:
(2) offers or sells a security . . . by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,
The Court found that the Act's provision of a judicial forum was subject to the protection of the Act's nonwaiver provision. The Court's analysis focused on Congress' intent to protect investors through a process involving judicial expertise and review, along with the provision of certain procedural advantages. Subsequently, federal courts read Wilko to preclude arbitration when claims were brought under section 10(b) of the Exchange Act. The courts based this extension on the common policy of the two securities acts and the identity of their nonwaiver provisions.

In recent years, two arguments have been raised against the application of Wilko to section 10(b) claims. First, Justice Stewart, writing for the majority in Scherk v. Alberto-Culver Co., stated in dictum that a "colorable argument" could be made against extending Wilko because of differences between the jurisdictional and the protective provisions of the two acts. The argument was uniformly rejected by the federal appellate courts. Recently, however, Justice White, in his concurrence in Dean Witter Reynolds, Inc. v. Byrd, revived this argument. Though the courts have generally rejected it again, the argument was adopted by the Eighth Circuit. The second argument against extending Wilko asserts that improvements in the quality of the arbitration process, together with a renewed emphasis in recent Supreme Court decisions favoring arbitration, make the arbitral a satisfactory forum for resolving securities law disputes. If accepted, this second argument would not merely preclude extension of the Wilko holding to Exchange Act claims, but overrule Wilko altogether.

This comment will examine the Wilko case in detail and determine whether its premises and reasoning apply with equal force to the protective and jurisdictional provisions of both securities acts.

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction . . . .
The argument raised by Justices Stewart and White will be read in light of Wilko, judicial and legislative history, and the standards of language analysis that the Court applied in previous decisions involving the Exchange Act. Finally, there will be a reevaluation of the arbitration process through the lens of recent Court instruction on reading the Arbitration Act.

II. PREDISPUTE ARBITRATION AGREEMENTS AND THE 1933 AND 1934 SECURITIES ACTS: Wilko and Scherk

A. Overview of the Securities and Federal Arbitration Acts

1. The Securities Acts.—In direct response to the market crash of 1929 Congress passed the Securities Act of 1933 and the Securities Exchange Act of 1934. Congress had recognized the hazards of an unequal bargaining position between those in the industry and investors. Through full and fair disclosure requirements and the threat of civil and criminal liability, the Securities Act, aimed principally at the issuance of securities, manifested the congressional intent to rectify this dangerous imbalance. The 1934 Act, as an extension of the 1933 Act, promoted the same policy of investor protection by requiring disclosure and providing penalties for non-disclosure to those dealing in secondary markets, exchanges, and over-the-counter markets.

2. Federal Arbitration Act.—In the face of historic judicial antipathy to arbitration Congress passed the Federal Arbitration Act in 1925. This Act “established a new policy declaring the validity, irrevocability and enforceability of any contractual agreement submitting future disputes to arbitration.” This “new policy” reaffirmed an underlying policy of controlling the expense and complexity of dispute resolution. The Act provided that a party to an arbitration agreement could seek a stay of federal court action pending arbitration as well as an order to compel arbitration.

21. See S. REP. No. 47, 73d Cong., 1st Sess. 1 (1933). See also infra Section V.
23. Id.
24. Id. at 528-29 & n.25.
28. 9 U.S.C. at § 3.
29. Id. at § 4.
B. Wilko v. Swan: A Judicial Forum Cannot Be Waived Under the 1933 Act

1. Overview.—In 1953 the Supreme Court in Wilko v. Swan faced the issue of whether an arbitration clause in a margin account agreement between an investor and a broker was enforceable under section 2 of the Federal Arbitration Act. The investor brought the underlying claim under section 12(2) of the Securities Act, one of the Act’s antifraud provisions. He signed the agreement prior to any alleged violation and before any dispute had arisen. The investor asserted that the broker had induced him to buy shares of a certain stock based on false representations of an upcoming merger. The plaintiff was lead to believe the value of the stock would rise $6.00 a share. Two weeks later the stock was sold at a loss. The district court denied the broker’s motion for a stay pending arbitration; the court of appeals reversed.

The issue in Wilko was whether section 14 of the 1933 Act, the

31. The arbitration clause read as follows: “Any controversy arising between us under this contract shall be determined by arbitration pursuant to the Arbitration Law of the State of New York, and under the rules of either the Arbitration Committee of the Chamber of Commerce of the State of New York or of the American Arbitration Association, or of the Arbitration Committee of the New York Stock Exchange or such other Exchange as may have jurisdiction over the matter in dispute ....” Id. at 432 n.15.

33. For the text of § 12(2), see supra note 10; Wilko, 346 U.S. at 428-29.
34. Wilko, 346 U.S. at 435. The Court considered this fact essential. This comment discusses only arbitration clauses entered into prior to any alleged violation.
35. Id. at 428-29.
36. Id. at 429.
37. Id.
38. Id. at 430.
39. Id.
40. 15 U.S.C. § 77n (1982). This section reads as follows: “Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this title or of the rules and regulations of the Commission shall be void.”
Act's nonwaiver provision, precluded enforcement of the arbitration agreement. Section 14 voids "any stipulation" waiving compliance with "any provision" of the Securities Act. The arbitration agreement at issue here was a stipulation. The crux of the case centered on construction of the "any provision" language and on determining whether Congress intended the Act's provision of a judicial forum to be nonwaivable under section 14.41

Strictly speaking, the provision at issue in Wilko was not the protective provision, section 12(2). The Court, however, made clear that section 12(2)'s standards would govern whether the matter would be addressed in an arbitral or a judicial forum.42 The provision in question was section 22(a)43 of the 1933 Act, the jurisdictional provision, that creates concurrent federal and state jurisdiction for all 1933 Act claims. The Court held that the right to have a section 12(2) Securities Act claim heard in a judicial forum was the kind of right Congress intended section 14 to protect.44

Justice Reed, speaking for the majority, began his analysis by addressing the origins of and the purposes behind the Securities Act.45 In response to the market crash of 1929, Congress had responded with a legislative scheme designed to protect investors through a policy of full and fair disclosure.46 Section 12(2) of the Act was created by Congress "to effectuate this policy."47 The Court stated that section 12(2) created a "special right" for the investor because the seller is made to assume the burden of proving

41. Wilko, 346 U.S. at 430.
42. "We agree that in so far as the award in arbitration may be affected by legal requirements, statutes or common law, rather than by considerations of fairness, the provisions of the Securities Act control." Id. at 433-34.
43. 15 U.S.C. § 77v(a) (1982). This section reads as follows:
   The district courts of the United States, and the United States courts of any Territory, . . . shall have jurisdiction of offenses and violations under this subchapter and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the offer or sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. . . . No case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States . . . .
44. Wilko, 346 U.S. at 435.
45. Id. at 430-31.
46. Id. at 431.
47. Id.
lack of *scienter*.\textsuperscript{48} This right was special because it shifted the burden of proof as usually found at common law.\textsuperscript{49} The Court then tied effectuation of this special right to the procedural guarantees of section 22(a). First, the right was enforceable in a state or federal forum, with removal from the state forum forbidden. Second, when a federal court is chosen, the plaintiff had a wide choice of venue and nationwide service of process, and was not subject to the usual diversity and jurisdictional amount requirements.\textsuperscript{50}

Next, the Court looked briefly to the congressional policy behind the Federal Arbitration Act.\textsuperscript{51} Congress saw arbitration as a desirable alternative to complex litigation. It avoided delay and expense.\textsuperscript{52} Moreover, it was intended to apply to controversies based on both statutes and standards otherwise created.\textsuperscript{53} However, “[t]his hospitable attitude [of Congress] . . . toward arbitration [did] not solve [the Court’s] question as to the validity of [the] stipulation . . . to submit [the securities claim] to arbitration . . . .”\textsuperscript{54}

2. The Court’s Analysis.—The Wilko Court held that “an arrangement to arbitrate [was] a [section 14] ‘stipulation’ and [that] the right to select the judicial forum [under section 22(a) was] the kind of ‘provision’ that [could not] be waived under § 14 of the Securities Act.”\textsuperscript{55} This holding had two cornerstones: first, an analysis of policy and statute; second, an analysis of the difference between adjudication and arbitration.

The Court accepted the investor’s argument that Congress intended the nonwaiver provision of section 14 “to assure that sellers could not maneuver buyers into a position that might weaken their ability to recover under the Securities Act.”\textsuperscript{56}

[T]he Securities Act was drafted with an eye to the disadvantages under which buyers labor. Issuers of and dealers in securities have better opportunities to investigate and appraise the prospective earnings and business plans affecting securities than buyers. It is therefore reasonable

\begin{itemize}
  \item \textsuperscript{48} Id.
  \item \textsuperscript{49} Id.
  \item \textsuperscript{50} Id.
  \item \textsuperscript{51} Id. at 431-32. It is interesting to note the order in which the two acts are addressed. In Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974), it is the policy behind the Arbitration Act that is first addressed.
  \item \textsuperscript{52} Wilko, 346 U.S. at 431-32.
  \item \textsuperscript{53} Id.
  \item \textsuperscript{54} Id. at 432.
  \item \textsuperscript{55} Id. at 434-35.
  \item \textsuperscript{56} Id. at 432.
\end{itemize}
for Congress to put buyers of securities covered by that Act on a different basis from other purchasers.\textsuperscript{57}

This "different basis" prevented securities purchasers from being subject to arbitration clauses. Such arbitration clauses, when signed "prior to any violation of the Securities Act," represented the kind of maneuvering that Congress created section 14 to prevent. The investor who signed an arbitration agreement gave up the protective rights that Congress provided—for example, the wide choice of courts and venue. Further, the investor gave up these rights "at a time [prior to the violation,] when he [was] less able to judge the weight of the handicap the Securities Act place[d] upon his adversary."\textsuperscript{58}

Equally significant was the Court's acceptance of the investor's argument that "arbitration lacks the certainty of a suit at law under the Act to enforce [an investor's] rights."\textsuperscript{59} Arbitration could not apply the securities laws as effectively as a judicial proceeding.\textsuperscript{60} The Court indicated by example\textsuperscript{61} that arbitration was more suited to issues that were objectively measurable. The Court had serious doubts about the viability of arbitration when a "case require[d] subjective findings on the purpose and knowledge of an alleged violator of the [Securities] Act."\textsuperscript{62}

The Court then raised a series of objections to the suitability of the arbitration process for resolving claims under the securities laws. Initially, the Court found that arbitrators may make legal determinations and apply them "without judicial instruction on the law."\textsuperscript{63} Further, an arbitration "award may be made without explanation of [the arbitrators'] reasons and without a complete record of their proceedings, [or] the arbitrators' conception of the legal meaning of [the specially designed] statutory requirements."\textsuperscript{64} Most importantly, there is no judicial review for error in interpreting the law.\textsuperscript{65} In addition, the "[p]ower to vacate an award is lim-

\begin{itemize}
\item \textsuperscript{57} Id. at 435.
\item \textsuperscript{58} Id.
\item \textsuperscript{59} Id. at 432.
\item \textsuperscript{60} Id. at 435.
\item \textsuperscript{61} The issues to be decided were not like determining the "quality of a commodity or the amount of money due under a contract . . . ." Id.
\item \textsuperscript{62} Id. at 435-36.
\item \textsuperscript{63} Id. at 436.
\item \textsuperscript{64} Id. An arbitrator or self-regulatory organization (SRO), in light of the Uniform Arbitration Code, may choose to create "some sort of record." See Katsoris, The Arbitration of a Public Securities Dispute, 53 Fordham L. Rev. 279, 286 n.47 (1984).
\item \textsuperscript{65} Wilko, 346 U.S. at 436.
\end{itemize}
"lited" to egregious circumstances. Without a record to determine any such abuses, it will be impossible to vacate an award for failure to decide "in accordance with the provisions of the Securities Act." The Court concluded: "As the protective provisions of the Securities Act require the exercise of judicial discretion to fairly assure their effectiveness, it seems to us that Congress must have intended § 14 . . . to apply to waiver of judicial trial and review."68

Thus, the Court found that the right to choose a judicial forum was necessary to maintain and effect the rights that Congress provided in the protective provisions of the Act. As such, the right to a judicial forum was an independent right of substantive significance. Though such a conclusion was not easily reconcilable with the policy behind the Federal Arbitration Act, "the intention of Congress concerning the sale of securities [was] better carried out by holding invalid such an agreement for arbitration of [predispute violations] arising under the Act."70

C. Scherk v. Alberto-Culver Co.: The "Colorable Argument"

1. Overview.—After Wilko, federal courts generally accepted the view that Wilko's logic was equally applicable to claims brought under section 10(b) of the 1934 Act. However, in Scherk v. Alberto-Culver Co. a majority of the Supreme Court raised a doubt about this applicability in what appeared an obvious parallel between the policies of the two acts and the relevant provisions at issue.

Scherk centered around a business transaction between an American corporate purchaser and a German seller. The transaction involved the sale of three enterprises, organized under the laws of Germany and Liechtenstein, along with the purchase of certain

66. Id.
67. Id.
68. Id. at 437.
69. Id. at 437-38 (citing Boyd v. Grand Trunk Western R.R. Co., 338 U.S. 263 (1949), in which forum selection was considered a "'substantial right'").
70. Id. at 438.
71. See, e.g., Greater Continental Corp. v. Schechter, 422 F.2d 1100, 1103 (2d Cir. 1970) (citing Wilko): This type of question concerning . . . the meaning of Rule 10b-5 is properly litigated in the courts where a complete record is kept of the proceedings and findings and conclusions are made. It was for that reason that in both the 1933 and 1934 securities acts Congress provided that questions arising under those acts were not to be determined in arbitration proceedings (but rather in the courts) even if the contract between the parties contained an arbitration provision.
trademarks. The issue of fraud centered on whether or not the trademarks were encumbered. The contract was negotiated in the United States, England, and Germany, signed in Austria, and closed in Switzerland. The contract included an agreement to refer any controversy or claim to arbitration before the International Chamber of Commerce in Paris under the law of Illinois.

The American plaintiff brought suit in a United States district court under section 10(b) of the 1934 Act. The district and appellate courts, following Wilko, denied Scherk's motion to stay litigation pending arbitration. The Supreme Court reversed and held the agreement arbitrable.

The Court based its holding entirely on the "truly international" nature of the agreement. The Court viewed the arbitration agreement in the contract as a problem of "international conflict-of-laws" rather than domestic securities law. The arbitration clause was taken as a "specialized kind of forum selection" that permitted an orderly choice of situs and procedures to resolve the dispute. The Court found such a choice essential to avoid chaos and provide the predictability required by the international business community. Thus, Wilko was distinguished since it involved a completely domestic dispute. In essence, the Court refused to take a "parochial" attitude towards international business transactions.

2. The Colorable Argument.—The holding in Scherk was based entirely on the international nature of the transaction. However, in

73. Id. at 508.
74. Id.
75. Id. at 508-09.
76. Id. at 508.
77. Id. at 509.
78. Id. at 510.
79. The majority may have simply found it unthinkable to bring an action of such international dimension into federal court after Alberto-Culver had agreed to arbitration before the international community. Cf. Gruenbaum, Avoiding the Protection of the Federal Securities Laws: The Antiwaiver Provisions, 20 SANTA CLARA L. REV. 49, 58 n.48 (1980) (arguing that the Court doubted from the outset that section 10(b) even applied).
80. Scherk, 417 U.S. at 515.
81. Id. at 516.
82. Id. at 519.
83. Id. at 516.
84. Id. at 515.
85. Id. at 516-17, 519. Wilko was further distinguished on the ground that the loss of the Securities Act's procedural advantages, central in the wholly domestic context of Wilko, was "chimerical" in the context of an international transaction, since the defendant could quickly resort to a foreign court to block access to the American courts. Id. at 518.
dictum, Justice Stewart stated that "a colorable argument could be made that even the semantic reasoning of the Wilko opinion does not control the case before us." 86 This argument consisted of a number of subparts:

1. There was no express statutory counterpart to section 12(2) in the 1934 Act. 87
2. "[N]either § 10(b) nor rule 10(b)-5 speaks of a private remedy to redress violations of the kind alleged here." 88
3. Though courts had recognized a section 10(b) private right of action, "the [Exchange Act] itself does not establish the 'special right' that the Court in Wilko found significant." 89
4. The jurisdictional provision of the 1933 Act, section 22(a), provided for concurrent state and federal forums, whereas the parallel section of the 1934 Act, section 27, provided for exclusive federal jurisdiction. 90 Justice Stewart stated that this contrast demonstrated a more restricted jurisdiction. 91

3. Positions Rejecting the Colorable Argument After Scherk.—The colorable argument was uniformly rejected by post-Scherk federal appellate courts deciding the issue of the arbitrability of section 10(b) claims. 92 First, some of these courts recognized the argument as mere dictum. They focused on the fact that the Scherk Court’s hold-

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86. Id. at 513. At the time, "colorable" was defined as "seemingly valid, genuine; plausible; having an appearance of truth, right, or justice; also, counterfeit or feigned. Syn: See SPECIOUS." WEBSTER’S NEW INTERNATIONAL DICTIONARY 529 (2d ed. 1959).
87. Scherk, 417 U.S. at 513.
88. Id. Rule 10b-5 is codified at 17 C.F.R. § 240.10b-5 (1986).
89. Scherk, 417 U.S. at 514.
90. 15 U.S.C. § 78aa (1982). This section reads as follows:
   The district courts of the United States, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder . . . . Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder . . . may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found . . . .
91. Scherk, 417 U.S. at 513.
ing made the international aspects of that case entirely dispositive.\textsuperscript{93} Thus, \textit{Scherk} itself was not considered applicable in a wholly domestic context.\textsuperscript{94}

Second, courts rejected the argument on its merits. Most significant in their analysis was the fundamental consideration given to the policy behind both securities acts. For instance, in \textit{Weissbuch v. Merrill Lynch, Pierce, Fenner \& Smith, Inc.}\textsuperscript{95} the Seventh Circuit held that “policy considerations mandate the application of \textit{Wilko} to Rule 10b-5 situations absent the presence of international concerns.”\textsuperscript{96} That court found \textit{Wilko’s} analysis wholly adaptable to section 10(b) claims because of the “overriding concern for the protection of investors.”\textsuperscript{97}

This policy of investor protection is the common source of both the Securities Act and the Exchange Act.\textsuperscript{98} In \textit{Wilko} the Court understood the Securities Act to manifest this policy through an interactive system of provisions. The Securities Act gives investors remedies through its protective provisions, and also gives the procedural means, such as a judicial forum, to adequately effect those remedies.\textsuperscript{99} The basic design of the Exchange Act is no different. Thus, when comparing section 12(2) of the 1933 Act and section 10(b) of the 1934 Act, the Tenth Circuit found “it is necessary to recognize that the policy considerations in the two instances with respect to the two remedies [section 12(2) and section 10(b)] are not different.”\textsuperscript{100} That court found that the purpose of rule 10(b)-5 was to protect the vulnerable purchaser from the more sophisticated seller.\textsuperscript{101} Further, the court added that “the parallel considerations of the two Acts make it impossible to draw . . . a distinction.”\textsuperscript{102} Inexplicably, the \textit{Scherk} majority never addressed the issue of investor protection in its “colorable argument.”

In turn, the federal courts did not directly address the specific distinctions between section 12(2) and section 10(b) put forward by Justice Stewart. The questions of whether section 10(b) is a “special

\textsuperscript{93.} See, e.g., \textit{Weissbuch}, 558 F.2d at 835-36.
\textsuperscript{94.} See, e.g., \textit{Moore}, 590 F.2d at 827-28 (finding considerations and policies in \textit{Scherk} significantly different from those found controlling in \textit{Wilko}).
\textsuperscript{95.} 558 F.2d 831 (7th Cir. 1977).
\textsuperscript{96.} \textit{Id.} at 835.
\textsuperscript{97.} \textit{Id.} at 836.
\textsuperscript{100.} \textit{Merrill Lynch, Pierce, Fenner \& Smith, Inc. v. Moore}, 590 F.2d 823, 827 (10th Cir. 1978).
\textsuperscript{101.} \textit{Id.}
\textsuperscript{102.} \textit{Id.} at 826.
The parallels and distinctions between the jurisdictional provisions were addressed more thoroughly in other opinions, notably by Justice Douglas in his Scherk dissent. Just as with a section 12(2) action brought in an arbitral, there would be "'subjective findings on the purpose and knowledge' of the defendant, questions ill-determined by arbitrators without judicial instruction on the law."105 There would be no development of a record, nor any judicial review.106 Moreover, "[t]he extensive pretrial discovery provided by the Federal Rules of Civil Procedure . . . would not be available . . . [Nor would] the wide choice of venue provided by [section 27]."107 Justice Douglas concluded that the "loss of the proper judicial forum carries with it the loss of substantial rights."108 Thus, the loss of an exclusive federal forum would be the loss of a "substantial right," as the loss of concurrent jurisdiction was held to be in Wilko.109


104. See infra Sections III and IV.


106. Id.

107. Id. The Ninth Circuit adduced other lost advantages: the right to a federal forum without a need to meet diversity or jurisdictional amount requirements; nationwide service of process provided by section 27 of the 1934 Act; and the venue provisions of section 27, which in fact provide the plaintiff with a wider choice than the venue provisions of section 22(a) of the 1933 Act. Conover v. Dean Witter Reynolds Inc., 794 F.2d 520, 526-27 (9th Cir. 1986).


109. "These are the policy considerations which underlay Wilko and which apply to the instant case as well." Scherk, 417 U.S. at 532 n.11 (Douglas, J., dissenting). See Wilko v. Swan, 346 U.S. 427, 437 (1953) (citing Boyd v. Grand Trunk Western R.R. Co., 338
The "colorable argument" raised no question about the practical identity of the two acts' nonwaiver provisions. As the appellate court decisions made clear, section 29(a) of the 1934 Act and section 14 of the 1933 Act were virtually identical. In some post-Scherk decisions this particular equivalence, combined with policy considerations, was virtually dispositive.

In addition to the federal courts' agreement that Wilko should be extended to section 10(b) claims, the Third Circuit, in Ayres v. Merrill Lynch, Pierce, Fenner & Smith, Inc., asserted that Congress had apparently accepted this position as well. In 1975, Congress made significant revisions in the securities laws.

Section 28(b) was developed to permit an exception to the rule of nonwaiver of a judicial forum by participants in self-regulatory organizations who enter arbitration agreements among themselves. The conference committee report on this amendment stated that "[i]t was the clear understanding of the conferees that this amendment did not change existing law as articulated in Wilko . . . concerning the effect of arbitration proceeding provisions of agreements entered into by [nonindustry] persons dealing with members and participants of

U.S. 263 (1949), which indicated that loss of a right to select a judicial forum was a loss of a substantial right).


Section 14 states:

Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.


Section 29(a) states:

Any condition, stipulation, or provision binding any person to waive compliance with any provision of this chapter or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void.


111. See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Moore, 590 F.2d 823, 827-29 (10th Cir. 1978); Weissbuch, 558 F.2d at 835-36.


113. Id. at 536-37.


self-regulatory organizations.\textsuperscript{116}

The \textit{Ayres} court inferred that Congress would not have asserted the continuing vitality of \textit{Wilko} in a revision of the 1934 Act unless it applied to Exchange Act claims.\textsuperscript{117} The Seventh Circuit adopted the \textit{Ayres} court analysis.\textsuperscript{118}

The Securities and Exchange Commission (SEC) had also taken a stand in favor of extending \textit{Wilko} to section 10(b) claims.\textsuperscript{119} In adopting rule 15c2-2\textsuperscript{120} the SEC recognized that the \textit{Wilko} doctrine applied to all the federal securities laws.\textsuperscript{121} Rule 15c2-2 prohibits

\begin{itemize}
  \item 118. Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 558 F.2d 831, 836 (7th Cir. 1977).
  \item 119. The SEC recently reversed its position and now contends that arbitration agreements that refer to the rules of securities associations or exchanges, subject to SEC oversight, are enforceable. \textit{See generally} SEC Brief, supra note 31.
  \item 120. Rule 15c2-2 provides:
  \begin{quote}
    It shall be a fraudulent, manipulative or deceptive act or practice for a broker or dealer to enter into an agreement with any public customer which purports to bind the customer to the arbitration of future disputes between them arising under the Federal securities laws, or to have in effect such an agreement, pursuant to which it effects transactions with or for a customer.
  \end{quote}
  \item 17 Upon being "informed that the Commission had submitted an \textit{amicus curiae} brief on the side of the securities industry rather than investors," Rep. Dingell, as Chairman of the Subcommittee on Oversight and Investigation of the Committee on Energy and Commerce, requested that the SEC provide the Subcommittee with documentation relating to the SEC's previous position against arbitration and its recent change in favor of arbitration. Letter from John D. Dingell, supra note 31, at 2. The tone of the letter indicates that the Subcommittee will require a well-founded basis for the SEC's dramatic reversal. Chairman Dingell specifically reminded Chairman Shad that "time and time again, the Commission has advised the Committee of serious \textit{limitations} on your authority and in the arbitration process itself," \textit{id.} at 3 (emphasis in original), \textit{e.g.}, in an August 1986 Commission report issued only three months before the Commission's reversal in \textit{McMahon}, \textit{id.}
  \item Most significantly, the letter also suggests that Congress intends to look into "legislative or regulatory changes . . . appropriate to improve the arbitration process and [SEC] oversight thereof." \textit{Id.} This evidences a general concern that the congressional purpose behind the securities laws, investor protection, is the continuing preeminent concern of Congress. In light of the critical importance of congressional intent in deciding the arbitrability issue, and congressional doubts concerning SEC oversight and the arbitration process itself, \textit{id.} at 3, action in favor of the arbitrability of § 10(b) claims or in overturning \textit{Wilko} remains highly questionable.
brokers from using predispute arbitration clauses in agreements with customers that purport to bind investors to arbitration when "Federal securities law" claims are at issue.\(^\text{122}\) The Commission, in its discussion of rule 15c2-2's final adoption, made clear that "Federal securities law" included the 1934 Act and section 10(b).\(^\text{123}\) Quoting the Sixth Circuit as exemplary, the Commission stated "[c]ourts have consistently held that Wilko's [sic] holding and rationale [under the Securities Act of 1933] are equally applicable to cases arising under the 1934 Act."\(^\text{124}\) The Commission, responding to industry criticism, noted that there was no authoritative "basis upon which the Commission [could] determine that the Wilko analysis [did] not hold equally true for other federal securities acts, which contain[ed] substantially identical anti-waiver provisions."\(^\text{125}\)

The parallel policy needs and purposes of the two acts, apparent congressional and clear SEC extension of Wilko, and the superficial distinctions made by the "colorable argument" should have finished that argument. However, the Court's continuing focus on limiting its analysis of congressional intent primarily to statutory language ("semantic reasoning," as Justice Stewart called it), and the Court's recent endorsement of the policy behind the Arbitration Act, have recalled the colorable argument from the brink. Justice White took the step of resurrecting the argument,\(^\text{126}\) and the First and Eighth Circuits have given it the force of precedent.\(^\text{127}\) As long as Wilko remains the law, however, this argument cannot stand.

\(^\text{122. See supra note 120.}\)
\(^\text{123. 48 Fed. Reg. 53,404 (1983).}\)
\(^\text{124. Id. (quoting First Heritage Corp. v. Prescott, Ball & Turben, 710 F.2d 1205, 1207 (6th Cir. 1983)).}\)
\(^\text{125. 48 Fed. Reg. 53,404 n.6 (1983).}\)
\(^\text{127. In Page v. Moseley, Hallgarten, Estabrook & Weedan, Inc., 806 F.2d 291 (1st Cir. 1986), the First Circuit held predispute arbitration agreements enforceable when plaintiffs raise section 10(b) claims. The Page court was "persuaded by the result reached by the Eighth Circuit, although for somewhat different reasons . . . ." Id. at 295. The court made only limited use of the colorable argument, id. at 296, focusing primarily on recent Supreme Court instruction concerning the Arbitration Act, id. at 296-98. By contrast, the Eighth Circuit wholly adopted the colorable argument, see Phillips v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 795 F.2d 1993, 1395-98 (8th Cir.), petition for cert. filed, 55 U.S.L.W. 3096 (U.S. Oct. 7, 1986) (No. 86-578), and included only brief, general statements on the policy favoring arbitration, id. at 1395, 1398.}\)
III. JUSTICE WHITE AND A RE-EXAMINATION OF THE COLORABLE ARGUMENT

This section will review Justice White's restatement of the colorable argument and its adoption by the Eighth Circuit panel in Phillips. It will then address each objection to the nonarbitrability of section 10(b) claims. Included in the overall analysis will be certain analyses of the Second, Third, Ninth, and Eleventh Circuits in recent opinions upholding the application of Wilko to the 1934 Act. In the end, the only legitimate question remaining will be whether arbitration procedures, the quality of the arbitrators, and the overall fairness of the arbitration process have improved sufficiently in the last thirty-three years to remove a need for the "judicial direction" that the Wilko Court understood as necessary for giving full effect to the protective provisions of the securities acts created by Congress.

A. Restatement of the Colorable Argument

In Dean Witter Reynolds, Inc. v. Byrd the Supreme Court, in a footnote, portrayed the state of the colorable argument. It noted that Scherk raised doubts about the extension of Wilko to section 10(b) claims. It further noted, however, that the Scherk Court did not hold that Wilko would not apply in the section 10(b) context. The Byrd majority expressly recognized that numerous federal courts have applied Wilko to section 10(b) claims and that agreements to arbitrate such claims are unenforceable in these courts. The Court chose not to resolve the issue since it was not properly before the Court.

In a concurring opinion, Justice White, who had dissented in Scherk, essentially restated the Scherk majority's colorable argument. First, he noted that the Wilko analysis centered around the intercon-

132. See infra Section V.
134. Id. at 215 n.1.
connection of sections 12(2), 14, and 22(a) of the 1933 Act. He then stated that the reasoning that upheld nonwaiver in *Wilko* could not be "mechanically transplanted to the 1934 Act." The extent of actual analysis is as follows:

(1) Justice White recognized that section 29(a) and section 14, the nonwaiver provisions, were equivalent. He did not consider this equivalence sufficient to counterbalance the lack of similarity he found between sections 12(2) and 22(a) of the 1933 Act and sections 10(b) and 27 of the 1934 Act.

(2) The jurisdictional provisions of the two acts were distinguishable. Section 27 of the 1934 Act provided for exclusive jurisdiction in the federal courts, whereas section 22(a) of the 1933 Act provided for concurrent state and federal jurisdiction. The *Scherk* Court called this a significant restriction. Justice White again characterized section 27 as "narrow."

(3) "More importantly," the section 10(b) and rule 10b-5 claims were implied rather than express private causes of action. Justice White drew two conclusions from this premise. First, "[t]he phrase 'waive compliance with any provision of this chapter', [§ 29(a),] is . . . literally inapplicable." Second, "Wilko's [sic] solicitude for the federal cause of action—the 'special right' established by Congress . . . is not necessarily appropriate where the cause of action is judicially implied and not so different from the common law action." Supplementing Justice White's position, the Eighth Circuit recalled that it was the shift in the burden of proof to the defendant that made section 12(2) special and distinguished it from the common-law remedy.

(4) The *Phillips* court went one step beyond the colorable argument and added that it was the difference between the two acts in conjunction with "the strong federal policy favoring enforcement of arbitration agreements" that prohibited an extension of *Wilko* to the

137. *Id.*
138. *Id.*
139. See supra note 90.
140. See supra note 43.
143. *Id.* at 224-25 (citing *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983)).
144. The logical steps between premise and conclusion are absent.
146. *Id.*
B. Analysis of the Colorable Argument

1. The Parallels Between Section 29(a) of the 1934 Act and Section 14 of the 1933 Act: The Policy of Investor Protection.—Even the Eighth Circuit, ruling against nonwaiver, found the two nonwaiver sections virtually identical. Yet it failed to look at the importance of this parallel. This failure is difficult to understand in light of the pre-Byrd decisions that found the similarity between the two sections a strong ground for extending Wilko.

As stated in Wilko, the nonwaiver provision “assure[d] that sellers could not maneuver buyers into a position that might weaken their ability to recover under the Securities Act.” Thus, section 14 of the 1933 Act manifested Congress’ policy of investor protection. This protection was especially important, in the broker-investor context, against those in the securities industry with superior

148. Id. at 1398. See infra Section IV.
149. As noted in Phillips, since Byrd a majority of the federal district courts addressing the issue of arbitrality of section 10(b) claims have ruled in favor of arbitrality. Phillips, 795 F.2d at 1396 n.8. Moreover, as one district court has noted, almost all of the district court rulings for nonarbitrability have been based on a “finding that binding pre-Byrd precedent on this issue exists in their circuit . . . .” Shotto v. Laub, 632 F. Supp. 516, 525 (D. Md. 1986). Since that time two circuit courts have reconsidered the extension of Wilko, independent of precedent, and in thoroughgoing analyses have ruled in favor of extension. Wolfe v. E.F. Hutton & Co., Inc. 800 F.2d 1032 (11th Cir. 1986) (en banc); Conover v. Dean Witter Reynolds, Inc., 794 F.2d 520 (9th Cir.), petition for cert. filed, 55 U.S.L.W. 3159 (U.S. Aug. 29, 1986) (No. 86-321). As demonstrated by Shotto’s mechanical recitation of the colorable argument, district courts ruling in favor of arbitrability are acting no differently from the courts that mechanically rely on precedent, i.e., they are expressly holding that the colorable argument is correct without any searching analysis as to why. See, e.g., Bob Ladd, Inc. v. Adcock, 633 F. Supp. 241, 242-43 (E.D. Ark. 1986); Brener v. Becker Paribas, Inc., 628 F. Supp. 442, 447 (S.D.N.Y. 1985); West v. Drexel Burnham Lambert, Inc., 623 F. Supp. 26, 27-28 (W.D. Wash. 1985); Dees v. Distenfield, 618 F. Supp. 123, 125-26 (C.D. Cal. 1985).

These cases are not based solely on the White concurrence. They also rely equally, as does Phillips, on the view that federal arbitration policy, in light of the improved quality of arbitration procedures, overrides the federal securities law policy. The differences adduced by Justice White merely act as a wedge to hold the door open for this policy favoring arbitration. See, e.g., Brener, 628 F. Supp. at 448 (focusing on the quality of arbitration procedures that now exist); Dees, 618 F. Supp. at 126 (focusing on policy favoring arbitration and absence of indication from Congress that rule 10b-5 claims should not be arbitrated). The policy logic on which these cases hinge would not only deny extension of Wilko, but reverse it altogether. See infra Section IV.

150. Phillips, 795 F.2d at 1397.
151. This argument has recently been re-emphasized. See Conover, 794 F.2d at 523; McMahon v. Shearson/American Express, Inc., 788 F.2d 94, 98 (2d Cir.), cert. granted, 107 S. Ct. 60 (1986).
152. Wilko, 346 U.S. at 432.
access to information.\textsuperscript{153} This same policy and the same concerns are at the heart of the 1934 Act.\textsuperscript{154} The virtual identity of section 29(a) of the 1934 Act and section 14 of the 1933 Act assuredly manifests an equal design to protect investors.

As the central provisions at issue in the arbitration cases, sections 29(a) and 14 set the boundaries for discussing the other issues. The courts must confront the congressional purpose of investor protection. Yet neither the Phillips panel nor Justice White addresses the policy of the Exchange Act in their arguments. They subtly displace this policy by pointing to the difference between sections 12(2) and 10(b) and sections 22(a) and 27. This disregard of the central policy in the securities acts, so highly respected in Wilko,\textsuperscript{155} defies reason\textsuperscript{156} and recent instruction of the Court itself.\textsuperscript{157}

2. Implied Remedy v. Express Remedy.—Justice White offers the argument that since the private right of action under section 10(b) is not expressly in the language of the statute, it "literally" is not a provision of the 1934 Act—at least for purposes of the protection offered by section 29(a).\textsuperscript{158} This conclusion is the result of an overly strict application of the Court's approach to statutory language analysis.

\textsuperscript{153} Id. at 435.

\textsuperscript{154} "The Securities Act of 1933 was designed to provide investors with full disclosure . . . . The 1934 Act was intended principally to protect investors . . . ." Ernst & Ernst v. Hochfelder, 425 U.S. 185, 195 (1976). "The 1933 and 1934 Acts constitute interrelated components of the federal regulatory scheme governing transactions in securities." Id. at 206. Section 10(b) itself states that "the Commission may prescribe [rules and regulations] necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78j(a) (1982) (emphasis added).

\textsuperscript{155} As powerfully stated in the last sentence of Wilko: "Recognizing the advantages that prior agreements for arbitration may provide for the solution of commercial controversies, we decide that the intention of Congress concerning the sale of securities is better carried out by holding invalid such an agreement for arbitration of issues arising under the Act." 346 U.S. at 438.

\textsuperscript{156} In Scherk, the policy of investor protection was overcome by sufficient countervailing grounds. In that case, the international dimension of the transactions, the choice of law problem, and the need for predictability in the international business community took that particular transaction and the agreement tied to it completely out of the "parochial" sphere of American securities laws. In fact, Justice Stewart's developed analysis of the crucial international elements stands in marked contrast to the "colorable argument."

\textsuperscript{157} See infra Section V.

\textsuperscript{158} The First Circuit agrees with this aspect of Justice White's argument. See Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 291, 296 (1st Cir. 1986). See also supra note 127.
In his concurrence in *Blue Chip Stamps v. Manor Drug Stores*\(^\text{159}\) Justice Powell stated that "[t]he starting point in every case involving construction of a statute is the language itself."\(^\text{160}\) In *Ernst & Ernst v. Hochfelder*\(^\text{161}\) Justice Powell, now writing for the majority, reiterated this approach, and stated further that ascertainment of congressional intent rested primarily on statutory language in the case of both implied and express remedies.\(^\text{162}\) Shortly thereafter, in *Santa Fe Industries v. Green*\(^\text{163}\) Justice White, speaking for the majority, followed both of the above-stated precepts and essentially held that the meaning of the language on the face of the statute set the limits of its protections when no legislative history supported a departure from that language.\(^\text{164}\)

In the above cases, the language logically read as the Court interpreted it. In *Hochfelder* the Court had to ascertain the standard of liability under section 10(b). The relevant statutory language forbade the use of "any manipulative or deceptive device or contrivance . . . ."\(^\text{165}\) Justice Powell began his analysis of this language by stating that "[t]he words 'manipulative or deceptive' used in conjunction with 'device or contrivance' strongly suggest that § 10(b) was intended to proscribe knowing or intentional conduct."\(^\text{166}\) He rejected the SEC's argument for a negligence standard because it "simply ignore[d] the use of the words 'manipulative,' 'deceptive,'

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160. Id. at 756.
162. Id. at 200.
163. 430 U.S. 462 (1977) (holding that section 10(b) requires deception or misrepresentation and that a breach of fiduciary duty alone is not subject to section 10(b)'s protections).
164. Id. at 473. Justice White added that even if the language of the statute was not "'sufficiently clear in its context,'" additional considerations would weigh heavily. Thus, the Court also looked (1) to the usefulness of the remedy sought in light of congressional policy, and (2) to the interrelation of state and federal law. Id. at 477-79.
165. Section 10(b) states:

> [It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—]
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

166. *Hochfelder*, 425 U.S. at 197 (citing, e.g., Loss, *Summary Remarks*, 30 Bus. Law 163, 165 (Mar. 1975) ("Since when is negligent conduct 'manipulative' or 'deceptive'? We are dealing, after all, with the English language.")).
and 'contrivance' . . . .'

Justice Powell noted the dictionary definition of these terms in showing an "unmistakable . . . congressional intent to proscribe a type of conduct quite different from negligence." He looked additionally to the specialized application of the term "manipulative" which "was virtually a term of art when used in connection with securities markets." The statutory language "connote[d] intentional or willful conduct" in light of its common and industry usage. Thus, the Court found that "the language of a statute controls when sufficiently clear in its context." The Court did turn to the legislative history of section 10(b) to find any possible support for a contrary position. That history was not explicit as to congressional intent. In fact, the Court found that the relevant portions of that history supported the Court's language analysis.

In Santa Fe the issue was whether a breach of fiduciary duty, standing alone, fell within the language of section 10(b). This case came soon after Hochfelder, and Justice White followed Justice Powell's mode of analysis. He looked first to the language of the statute. He found that the meaning of the terms "manipulative," "deceptive," and "contrivance" derived from their common use in the securities market and in the 1934 Act itself. It was clear in its context that the use of these terms required some sort of deception or misrepresentation. Thus, unless such practices accompanied a breach of fiduciary duty, there could be no violation of section 10(b). The Court so held, as it found no legislative history to the contrary.

Though the Court's primary focus was the statutory language,
the meaning of that language (the way the words in the statute are used) necessarily required reference to some other source—for example, use of the term in the securities markets or in common English. Looking solely at the language of section 10(b), without any reference beyond a dictionary, one would not find a private right of action. However, it defies the method of analysis found in Hochfelder and Santa Fe to discern congressional intent in such a vacuum. As Justice White stated, the Supreme Court itself has recognized a private right of action under section 10(b) and rule 10b-5. The words in section 10(b) must be read in that context. The Court has used these words in finding a private remedy, and, therefore, in judicial practice the words of the statute mean that there is a private cause of action.

This argument cannot be avoided by labeling this private right "merely a judicially created action." The Court did not create the private right; the Court only recognized it. It was Congress that intended such an action to exist.

Therefore one cannot argue that the implied private right of action under section 10(b) is not literally a provision of the Exchange Act. The Supreme Court has recognized that Congress has provided this right. That right is now contained within the words of section 10(b). It is part of their meaning.

This position is supported by the line of Supreme Court cases ruling that "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change . . . ." As the Court recognized, in 1975 Congress made the "most substantial

177. Katsoris, supra note 64, at 301.
   To say that a private cause of action is implied is to say that Congress intended such an action to exist. See, e.g., Merrill Lynch, Pierce, Fenner & Smith v. Curran, 456 U.S. 353, 377-78 (1982); Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11, 15-16. It is as if Congress explicitly provided for the cause of action. (parallel citations omitted).
180. Further, the sweeping language of the 1934 Act's jurisdictional provision, section 27, which gives the federal courts exclusive jurisdiction over violations of the Exchange Act and all suits brought to enforce any liability or duty created thereunder, "applies to all actions . . . including implied actions . . . ." Wolfe, 800 F.2d at 1036.
and significant revision of this country's federal securities laws since the passage of the Securities Exchange Act in 1934.' "182 Prior to this congressional action the "federal courts had consistently and routinely permitted a [private] plaintiff to proceed under § 10(b) . . . ."183 Therefore, "the fact that a comprehensive reexamination and significant amendment of the [federal securities laws] left intact the statutory provisions under which the federal courts had implied a [private] cause of action is itself evidence that Congress affirmatively intended to preserve that remedy."184

This examination of Justice White's language analysis elucidates two points. First, section 10(b), containing a private cause of action, is a provision of the Act; and as a protective provision it is the kind of substantial right encompassed by the nonwaiver section. Second, there are serious flaws in making an overly strict language analysis the sole means of discerning congressional intent in every action. It must be congressional intention and usage that determine the context and meaning of statutory language. In addition, as the Court has made clear, attention must be paid to express decisions of the Court, acceptance of such decisions by Congress, or pertinent legislative history.185 Thus, once given full context, the analysis of statutory language can look to the actual usage of the specific words that Congress chose.186

The above argument against extension is a subset of the general argument that an implied remedy is somehow inferior to an express remedy. To reiterate the contrary in the present context:

(1) The private right of action under section 10(b) is established "beyond peradventure" in the eyes of the Supreme Court.187

(2) In 1975 Congress made major revisions in the Exchange Act.188 Section 10(b) and rule 10b-5 were left intact. Congress was surely aware that federal courts had been implying private rights of

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183. Id. at 385.
185. Cf. Kohn v. American Metal Climax, Inc., 458 F.2d 255, 280 (3d Cir. 1972) (Adams, J., concurring and dissenting) (contending that courts should look to legislative and administrative history in determining the meaning of language in § 10(b)).
186. Statutory analysis should consist of: (1) a study of the text of the statute; (2) an examination of legislative and judicial history of the statute; (3) due regard for the purposes underlying the acts. Conover v. Dean Witter Reynolds, Inc., 794 F.2d 520, 523 (9th Cir.), petition for cert. filed, 55 U.S.L.W. 3159 (U.S. Aug. 29, 1986) (No. 86-321).
188. Id. at 384-85.
action under section 10(b) and rule 10b-5. By leaving them intact Congress has recognized the private right.189

(3) The 1975 amendment included a revision of section 28(b) of the Exchange Act.190 The committee conference report recognized that this change would not affect the application of the Wilko doctrine.191 By making this affirmation in an amendment to the 1934 Act, it can be argued that Wilko was meant to extend to the provisions of that Act, including section 10(b).

(4) The SEC, in adopting rule 15c2-2, recognized the Wilko doctrine’s applicability to all federal securities laws.192

3. Wilko’s “Solicitude” for Section 12(2): The Special Right?—The Wilko Court found section 12(2) to provide a “special right” because it shifted the burden of proof normally found at common law.193 A significant parallel is found in Herman & MacClean v. Huddleston.194 In that case the Court held that the preponderance-of-evidence standard and not the clear-and-convincing-evidence standard was the standard of proof in a section 10(b) action.195 The Court expressly rejected the lower court’s rationale that “the traditional use of a higher burden of proof in civil fraud actions at common law” required a higher burden in a section 10(b) action.196 Thus, if “special right” is defined by a change from the common-law standard of proof in favor of the plaintiff, then section 10(b) provides a special right.

The Huddleston Court further stated that “[r]eference to common law practices can be misleading . . . since the historical considerations underlying the imposition of a higher standard of proof

189. Conover, 794 F.2d at 524.
191. See supra note 116.
192. See supra notes 120-24 and accompanying text. The SEC now contends that a change in circumstances has rendered securities industry arbitration procedures adequate. The Commission argues that the expansion of its oversight powers under § 19 of the Securities Exchange Act, 15 U.S.C. § 78(s) (1982), ensures such adequacy. The Commission points out that such oversight and assumed safeguards did not exist at the time Wilko was decided. See SEC Brief, supra note 31, at 13-21. However, industry arbitration procedures, even under SEC oversight, remain inadequate when viewed against the congressional standards for protecting investors, as identified in Wilko. See infra text accompanying note 276.

The Commission strongly agrees with the position that the “colorable argument” should be rejected. SEC Brief, supra note 31, at 21-26.
195. Id. at 390.
196. Id. at 388.
have questionable pertinence here.”

This is so because the securities acts go beyond the common law. As the Huddleston Court stated of the securities acts’ antifraud provisions: “Moreover, the antifraud provisions of the securities laws are not coextensive with common-law doctrines of fraud. Indeed, an important purpose of the federal securities statutes was to rectify perceived deficiencies in the available common-law protections by establishing higher standards of conduct in the securities industry.”

Thus, it seems fair to say that all the provisions of the securities acts are special in that these provisions differ from the common law. If they did not differ, there would have been no need for Congress to create them.

The view that each protective provision of the securities acts is a special right can be supported by a careful reading of Wilko and its discussion of section 12(2). First, the Wilko Court’s holding does not include the special rights language. The issue was whether the Act’s nonwaiver provision, section 14, encompassed the right to select a judicial forum under section 22(a). The burden of proof provided in section 12(2) would not have been waived since its standards would have also controlled the arbitration. What in essence was waived was the right to have the section 12(2) claim heard in a judicial forum.

Further, the “special right” language was prefatory to the Court’s holding. The term was mentioned only twice, in consecutive sentences of a single paragraph. This paragraph began the Court’s analysis of the issue it had just raised. The paragraph represents, in encapsulated form, the entire history and expanse of the Securities Act: the genesis of the securities laws, their policy, a particular section, and fine procedural details.

The first sentence recalls President Roosevelt’s message to Congress that sellers of securities must beware of their actions (in light of the market crash). Congress then passed the Securities

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197. Id.
198. Id. at 388-89.
199. Under such a reading, Wilko’s “solicitude” for section 12(2) would be no different from its “solicitude” for any other congressionally-created right in the securities acts.
203. This language is five paragraphs removed from the beginning of the Court’s central argument. All of these paragraphs can fairly be called prefatory.
204. Wilko, 346 U.S. at 431.
205. Id. at 430.
Act to protect investors through a policy of full and fair disclosure.\textsuperscript{206} The next line reads, "to effectuate this policy, § 12(2) created a special right . . . ."\textsuperscript{207}

It is clear that the whole course of events leading to the enactment of the Securities Act did not reach its culminating point in section 12(2). In other words, section 12(2) is not the only way "to effectuate this policy," though the Court's language literally reads so. Rather, section 12(2) is one aspect of a statutory scheme that effectuates the policy of investor protection. Section 12(2) is only exemplary, chosen because it was the protective provision underlying the \textit{Wilko} plaintiff's claims.

As stated in \textit{Huddleston}, all the securities acts' remedial provisions are special in the sense that they were newly-created remedies different from then-available common-law remedies. \textit{Wilko} said nothing different. At the end of his central analysis of section 22(a) and arbitration procedures, Justice Reed wrote: "As the protective provisions of the Securities Act require the exercise of judicial direction to fairly assure their effectiveness, it seems to us that Congress must have intended § 14 . . . to apply to the waiver of judicial trial and review."\textsuperscript{208} It is the "protective provisions" of the Securities Act, and not only section 12(2), that "require" a judicial forum. The protective provisions of the 1934 Act require no less in light of the above discussions and policy.

4. Exclusive v. Concurrent Jurisdiction.—Finally, the differences between the jurisdictional statutes, section 22(a) of the Securities Act and section 27 of the Exchange Act, will be considered. The chief distinction raised in the colorable argument was the exclusivity of federal jurisdiction. Why the narrowing of jurisdiction was considered so important that it permits waiver of the federal forum has never been adequately explained. The loss of a judicial forum to an arbitral, which the \textit{Wilko} Court considered insufficient to effectuate the protective provisions, occurs in both circumstances.

The only apparent argument for exclusive jurisdiction's making waiver more appropriate is that the "narrowing" of the forum manifests less of a congressional intent to effectuate the protective provisions of the 1934 Act. This is highly unlikely.\textsuperscript{209} In fact a contrary reading seems at least equally appropriate. The Ninth Circuit

\begin{figure}
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206. \textit{Id.} at 431.

207. \textit{Id.}

208. \textit{Id.} at 437.

209. \textit{See supra} note 154.
\end{flushleft}
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found the distinction between concurrent and exclusive jurisdiction "an even more forceful indication of Congress' intent that federal courts oversee the interpretation and application of the 1934 Act." Additionally, one commentator has suggested "that the exclusive jurisdiction granted to the federal courts by section 27 of the Exchange Act amounts to the creation of a 'special right' which is at least as important as the special right referred to in Wilko." Both statements emphasize the position that Congress intended its grant of exclusive federal jurisdiction to provide greater protection than concurrent jurisdiction provided.

It may be further argued that Congress provided exclusive jurisdiction to create a uniquely federal right. Such rights are best suited to development and interpretation in federal courts in which the judiciary has a greater expertise in the substantive area of the law. Further, the need for uniformity and predictability in application of the statutes is best met by allowing development of this case law solely in the federal forum. This is especially true when, as with the securities acts, the language of the statute is expansive and the latitude for judicial interpretation is wide.

210. Conover v. Dean Witter Reynolds, Inc., 794 F.2d 520, 527 (9th Cir.), petition for cert. filed, 55 U.S.L.W. 3159 (U.S. Aug. 29, 1986) (No. 86-321). The Eleventh Circuit in Wolfe v. E.F. Hutton & Co., 800 F.2d 1032, 1036-37 (11th Cir. 1986) (en banc) considered the loss of the exclusive forum as a concern of "nearly equal force" to the loss of both state and federal forums. This was so because the 1934 Act "permit[s] a plaintiff to obtain a federal forum without having to meet the requirements of diversity jurisdiction—something which, for one reason or another, plaintiffs often find advantageous."

211. Gruenbaum, supra note 79, at 59 (emphasis in original). The author states that "[i]ndeed, Congress' vesting exclusive jurisdiction over Exchange Act claims in the federal courts would seem to make the right created thereby more 'special' than the right created by the concurrent state and federal court jurisdiction provided for in the Securities Act."

212. The First Circuit has argued that because Congress did not expressly create a private section 10(b) action, private plaintiffs are not covered by the 1934 Act's jurisdictional provisions. Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 291, 297 (1st Cir. 1986). The court contended that "[h]ad Congress regarded an exclusive federal court forum as so critical, it would have been simple for Congress to provide, as it did in the 1933 Act, that individuals be able to bring a cause of action in that forum." However, this argument would be no different from contending that there should be no private right of action under section 10(b) because if Congress had intended such a right, "it would have been simple enough for Congress to provide it." The Supreme Court has taken a different approach to ascertaining congressional intent. See supra Section III.B.2.


214. Id. at 331.

215. Id.
Thus, it is not self-evident that exclusive jurisdiction is a restricting factor. Without an explanation as to why section 27 is restrictive with regard to investors' rights, there is no principled reason to use Congress' provision of exclusive jurisdiction as a rationale for minimizing the right to a judicial forum.

In sum, the distinctions between the two securities acts do not provide an analytic basis to ignore their bond of common policy. In light of Wilko, the private remedial provisions of both acts are worthy of the protections provided by their identical nonwaiver sections. However, the Wilko rationale itself has been brought into question by those who contend that arbitration is a sufficient and practical way to protect investors. Before addressing the strength of this argument, the matter of equal bargaining position will be faced.

IV. DISPUTES BETWEEN BROKERS AND INSTITUTIONAL INVESTORS OR SOPHISTICATED INVESTORS

A. Overview

When the fraud claim against a broker is brought by an institutional investor or by a sophisticated individual investor, the question of equal bargaining position becomes relevant. The Wilko Court stated that Congress' purpose in enacting the antiwaiver provisions was to assure that sellers could not maneuver buyers in such a way as to weaken the protections afforded buyers under the Securities Act. 216 Furthermore, Justice Reed found that "[w]hile a buyer and seller of securities, under some circumstances, may deal at arm's length on equal terms, it is clear that the Securities Act was drafted with an eye to the disadvantages under which buyers labor." 217 Such disadvantages occurred because "dealers in securities have better opportunities to investigate and appraise the prospective earnings and business plans affecting securities than the buyer." 218

In Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, Inc. 219 the Seventh Circuit found the bargaining posture of the parties to be a consideration "at play" in Wilko and Scherk. 220 Earlier in its opinion, the court stated that "[i]t is clear that the Securities Acts were

217. Id. at 435.
218. Id.
219. 558 F.2d 831 (7th Cir. 1977).
passed with an eye to the disadvantages confronting the small investor in [the] area." Further developing this position, the court adopted Justice, then Judge, Stevens' analysis of Wilko (taken from his dissent in the circuit court's Scherk decision) that Wilko's protections were aimed only at "the relatively uninformed individual investor." Thus, the Weissbuch court found that "where both parties possessed formidable financial interests and where their arbitration agreement emerged from a period of prolonged and extensive negotiations . . . [t]he waiver of a statutory remedy in the courts could be realistically perceived as the product of a bargain." This position has been accepted by a number of commentators, and was most recently adopted in the Ninth Circuit.

The central position of the Weissbuch argument, that the securities acts were created only to protect small investors as such, was strenuously rejected by Justice Douglas in his Scherk dissent. He stated that the Securities Act "does not speak in terms of 'sophisticated' as opposed to 'unsophisticated' people dealing in securities. The rules when the giants play are the same as when the pygmies enter the market."

In Justice Douglas' analysis, the giants receive the same protections as the small investors not for themselves, but because the acts of the giants have immediate impact on their individual small investors. Thus, in Scherk Alberto-Culver was not the victim of the alleged fraud: "the thousands of investors who are the security

the "disparity of bargaining power" question, the Weissbuch decision gives the disparity issue new life).

221. Weissbuch, 558 F.2d at 834.
222. Id. at 835 (quoting Alberto-Culver v. Scherk, 484 F.2d 611, 617 (7th Cir. 1973) (Stevens, J., dissenting), rev'd on other grounds, 417 U.S. 506 (1974)).
223. Id.
224. Katsoris, supra note 64, at 295 n.115; Krause, Securities Litigation: The Unsolved Problem of Predispute Arbitration Agreements for Pendent Claims, 29 DePaul L. Rev. 693, 703 n.58 (1980); Note, supra note 22, at 539-40. These commentators tend to cite a few decisions by the lower federal courts as well as decisions involving transactions between members of the securities industry. These later cases are now governed by § 28(b) of the 1934 Act. The analogy to transactions between industry insiders and outsiders may falter when the kind of knowledge attributable to insiders has to be assumed of investors.
227. Id. at 526. "To decide issues of law on the size of the person who gets advantage or claims disadvantage is treacherous." Gruenbaum, supra note 79, at 62 (quoting Bruce's Juices v. American Can Co., 330 U.S. 743, 753 (1947)). This argument is not effective if, as Weissbuch contends, the law does not initially apply to large investors.
holders in Alberto-Culver" were the victims of that fraud. Justice Douglas argued that institutional investors "cannot waive those statutory [protections], for our corporate giants are not principalities of power but guardians of a host of wards unable to care for themselves. It is these wards that the 1934 Act tries to protect."

Justice Douglas' dissent rests on the same premise as Justice Stevens' dissent—that Congress passed the 1934 Act to protect the small investor. However, in Justice Douglas' view this requires that large institutional investors receive all of the Act's protections, since these investors are merely embodiments of the thousands of smaller investors entitled to such protection. This should be so whether the institutional investor likes it or not. Read in any light, Justice Douglas' analysis does not explain why large or sophisticated individual investors, acting solely on their own account, should receive the same protections as small or institutional investors.

B. Application of the Securities Acts to All Investors

The Supreme Court, in granting certiorari to hear McMahon v. Shearson/American Express, Inc., may choose to face the questions presented by both the sophisticated individual investor and the institutional investor. Assuming for purposes of argument that the McMahons were sophisticated investors, there may yet be a rea-
son for the Court to provide them the full protection of the securities acts. Such a rationale is based on the premise that the securities acts protect investors not only directly, but also through protecting the integrity of the marketplace. As the Court recently made clear in *Randall v. Loftsgaarden*, the 1934 Act is "not confined solely to compensating defrauded investors. . . . Congress [also] intended to deter fraud and manipulative practices in the securities markets, and to ensure full disclosure of information material to investment decisions."

The Exchange Act, as an extension to the 1933 Act, was aimed at transactions conducted on the securities exchanges and over-the-counter markets. Congress enacted the 1934 Act to deal with "transactions in securities [that] . . . are affected with a national public interest." These regulations were designed to, "[among other things], perfect the mechanisms of a national market system for securities . . . in order to protect interstate commerce, the national credit, the Federal taxing power . . . and to insure the maintenance of fair and honest markets in such transactions . . . ." Thus, if the antiwaiver provisions of the securities acts are necessary in all cases to assure the maintenance of "fair and honest markets," neither the sophisticated individual investor nor the large institutional investor should be permitted to ignore those provisions.

Accredited when that investor's net worth exceeds $1,000,000 at the time of the purchase, or when the investor's income has been greater than $200,000 in the two years prior to the purchase and greater than $200,000 in the year of purchase. 17 C.F.R. § 290.215 (1986). These rules for accredited investors are especially important in determining the disclosure requirements for securities issues in limited offerings. T. Hazen, *The Law of Securities Regulation* §§ 4.13-4.20 (Lawyer's ed. 1985). However, in light of the strong policy statements made in *Wilko*, and the heavy responsibilities placed on brokers to deal fairly, *id.* at § 10.6, it would be incongruous to call the McMahons sophisticated for present purposes.

234. 106 S. Ct. 3143, 3154 (1986).
235. *Id.* (citing Affiliated Ute Citizens v. United States, 406 U.S. 128, 151 (1972)).
238. *Id.* (emphasis added).
239. The *Wilko* Court stated that "[w]hile a buyer and seller of securities, under some circumstances, may deal at arm's length on equal terms, it is clear that the Securities Act was drafted with an eye to the disadvantages under which buyers labor." *Wilko* v. *Swan*, 346 U.S. 427, 435 (1953). The Court did not draw any express conclusions about how "arm's length [transactions] on equal terms" were to be dealt with. It is possible to read this statement as standing for the proposition that all buyer-seller transactions in securities will be subject to the Act's protections because of a general overriding concern for investor protection.

This author's view is that all transactions should be protected only if such protections secure the integrity of the marketplace. In this way the full protection necessary for the small investor, and the nation's economic health, would be assured.
Under this view, the integrity of the market may be threatened if the larger disputes are no longer subject to the scrutiny of the federal judiciary. Without the fear of the remedies available in federal court and the stigma attached to being brought into court, brokers and dealers may fail to restrain their actions with sufficient rigor.\textsuperscript{240} Such an attitude in relation to large investors would affect the market as a whole and reach all investors. Thus, no investor, even if personally sophisticated, can be allowed to bargain away the protections afforded to other investors.

V. Do Changes in Arbitration Practices and Quality Mandate the Recession of Wilko?

Changes in the arbitration procedures within the securities industry, improvement in the quality of arbitrators, and a recent group of Supreme Court cases renewing the emphasis placed on the Federal Arbitration Act\textsuperscript{241} are the basis for industry\textsuperscript{242} and commentator\textsuperscript{243} assertions that the \textit{Wilko} doctrine may no longer be viable.\textsuperscript{244} The argument appears to be twofold: (1) improved

\textsuperscript{240} Though there may be a price to pay in arbitration, and some stigma from losing an award, the effect of an arbitral is not the same as that of an adjudication. The brokers argue that they seek arbitration not because it favors them, but because it is a fair and efficient process for all concerned. The independence, thoroughness, and efficiency of the securities industry's arbitration procedures, however, remain in question. \textit{See, e.g.}, Katsoris, supra note 64, at 309-14; Note, \textit{Federal and State Securities Claims: Litigation or Arbitration?—Dean Witter Reynolds, Inc. v. Byrd, 105 S. Ct. 1238 (1985)}, 61 WASH. L. REV. 245, 259-61 (1986). \textit{See also infra note 270}.


\textsuperscript{243} \textit{See, e.g.}, Katsoris, supra note 64, at 298-301; Krause, \textit{supra} note 224, at 720-21.

\textsuperscript{244} The First and Eighth Circuits take the position that the passage of the Arbitration Act, along with recent Supreme Court decisions permitting arbitration of certain kinds of claims, create a presumption that arbitration is procedurally adequate. Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 291, 297 (1st Cir. 1986) ("[W]e reject the proposition that, after \textit{Mitsubishi}, courts can consider the alleged ineffectiveness of the arbitral forum in deciding the arbitrability of a federal statutory right."); Phillips v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 795 F.2d 1393, 1398 n.16 (8th Cir.), \textit{petition for cert. filed}, 55 U.S.L.W. 3296 (U.S. Oct. 7, 1986) (No. 86-578) ("Congress, through the Arbitration Act, as well as the Supreme Court have expressed increased approval for the use of arbitration rather than adjudication."). To say that competent arbitrators fairly apply an arbitral's procedural rules, however, is not equivalent to saying that those procedures meet the protective standards demanded by the securities acts. The congressional provisions for investor protection and the \textit{Wilko} rule that developed out of Congress' mandate have never been set aside by either Congress or the Court. These circuit courts are simply wrong to presume such a change.
arbitration procedures increase investor protection, thus decreasing
the policy concerns behind the securities acts, which (2) permits
greater attention to be paid to the policy behind the arbitration acts,
at a time when that policy is being actively promoted by the Court.

A. Nonwaiver Provisions Are Not Subject to Policy Balancing

In Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc.245 the
Court, speaking through Justice Blackmun, gave instruction on in-
terpreting the Federal Arbitration Act:

Just as it is the congressional policy manifested in the Fed-
eral Arbitration Act that requires courts liberally to con-
strue the scope of arbitration agreements covered by that
Act, it is the congressional intention expressed in some other statute
on which the courts must rely to identify any category of claims as to
which agreements to arbitrate will be held unenforceable.246

Thus, the courts' inquiries regarding the enforceability of arbitra-
tion agreements must center on the issue of whether "Congress in-
tended the substantive protection afforded by a given statute [other
than the Arbitration Act] to include protection against waiver of the
right to a judicial forum . . . . [T]hat intention will be deducible
from text or legislative history" of the other statute.247

This is not a balancing test. The Court "must rely" on the con-
gressional intent and policy behind the statutes that prohibit waiver
of a judicial forum.248 The policies underlying arbitration only be-
come relevant insofar as the policy behind the federal statute at is-
structure here, the Securities Act or the Exchange Act—recognizes that
arbitration policy.249

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246. Id. at 3355 (emphasis added).
247. Id. (citing Wilko v. Swan, 346 U.S. 427 (1953)).
Third Circuit also stated that "Wilko did not involve interpretations of arbitration agree-
ments; rather [it] involved interpretations of federal statutes that prohibit the applica-
tion of forum-selection clauses." Id.
249. Some courts contend that Mitsubishi requires that the policies behind the Arbitra-
tion Act be weighed equally with those of other federal statutes (e.g., the securities laws).
See, e.g., Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 291, 297 (1st
Cir. 1986) (Arbitration Act should receive equal deference). Mitsubishi never stated such
a rule. The Mitsubishi Court only instructed courts to look at the congressional intent in
the statute at issue to determine if Congress permitted waiver of a judicial forum. Mit-
subishi, 105 S. Ct. at 3355. As the Court understood, two statutes are not wholly equal
simply because Congress created them both.

This point is plainly made by comparing the history and policy of the Arbitration
Act with that of the securities acts. In 1925, the Arbitration Act was passed to ease the
The Mitsubishi Court cited Wilko as an example of how courts should carry out this inquiry.\(^{250}\) In Wilko itself, the Court began its concluding paragraph by stating that "[t]wo policies, not easily reconcilable, are involved in this case."\(^{251}\) At first glance it appears that the Court engaged in a balancing of the two policies. However, a review of the Court's preceding analysis demonstrates the contrary.

In stating the issue, the Wilko Court had asked whether an "agreement to arbitrate a future controversy [was] a 'condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision' of the Securities Act which § 14 declares 'void.' "\(^{252}\) This framing of the issue subordinated arbitration to the question of nonwaiver. Further, Justice Reed gave only a paragraph of prefatory discussion to the general purposes of the Arbitration Act.\(^{253}\) All of the Court's hard analysis centered around the requirements of the Securities Act.\(^{254}\) And the Court's decision rests wholly on that analysis.

Justice Reed removed any doubts about policy balancing in the final sentence of his opinion:

burdens of time and expense on parties and the courts. See supra Section II.A.2. (Arguably, it provides brokers and dealers with other advantages as well. See infra note 270.) After the great market crash of 1929, Congress passed the securities acts to protect investors against unfair practices. See supra Section II.A.1. But the two securities acts were not only designed to protect investors. By attempting to guarantee a fair marketplace, Congress was working to repair the fallen economic health and security of the nation. See supra Section IV.B. Thus, while the absence of arbitration in certain situations may add a burden of time and expense to investors, brokers, and the courts, the failure to arbitrate securities claims will neither bring down the federal courts nor bankrupt investors. In sharp contrast, the absence of the securities laws' protections would pose a threat to millions of individual investors and to the nation's economy as a whole.

This threat to investors and the nation is real. "The cases litigated number in the thousands every year." Katsoris, The Securities Arbitrators' Nightmare, 14 Fordham Urb. L.J. 3 (1986) (footnote omitted). Churning, insider trading, and the entire range of securities violations still exist, and unfortunately on no small scale (as, e.g., the Winans, Levine, and Boesky cases highlight). Thus, the protection of the securities acts remains a necessity. If arbitration can meet the congressional standards of protection required by the securities acts, it should be considered. Otherwise, the policy behind arbitration cannot be allowed to dilute those standards.

The good life of the "Roaring Twenties" had to give way to the necessities of the crash. Equally, the Arbitration Act of 1925, with its desire for speed and inexpensive solutions, must give way to policies that are aimed at conserving the fundamental economic well-being of the nation. See infra note 280 and accompanying text.

\(^{250}\) Mitsubishi, 105 S. Ct. at 3355.
\(^{251}\) Wilko, 346 U.S. at 438.
\(^{252}\) Id. at 430.
\(^{253}\) Id. at 431-32.
\(^{254}\) Id. at 434-38. See supra Section II.B.
Recognizing the advantages that prior agreements for arbitration may provide for the solution of commercial controversies, we decide that the intention of Congress concerning the sale of securities is better carried out by holding invalid such an agreement for arbitration of issues arising under the Act.\textsuperscript{255}

It is this concern with the underlying policy of the Securities Act that is the definitive consideration. Under both Mitsubishi and Wilko the same deference must be given to the Exchange Act. Since the considerations for prohibiting waiver of the judicial forum are fundamentally identical in both acts, arbitration agreements are best held invalid when an investor brings a section 10(b) claim.

\textbf{B. Changes in the Procedure, Quality of Arbitrators, and Fairness}

In Wilko the Court held that Congress intended to protect investors through the provision of a judicial forum. The intention of Congress cannot have changed. The policy behind the Arbitration Act cannot be used to counterbalance this intent to provide a judicial forum. However, it may be possible to restate in functional terms Congress' intention to provide a judicial forum. Thus, the proposition that arbitration is functionally equivalent to adjudication in a judicial forum becomes the only viable argument against application of the nonwaiver provision.

\textit{The Uniform Code of Arbitration}.—In 1976 the SEC solicited comment regarding development of a uniform system of dispute resolution procedures for small claims.\textsuperscript{256} This initiated a dialogue that ultimately lead to a number of self-regulatory organizations (SROs) forming the Securities Industry Conference of Arbitration (SICA).\textsuperscript{257} SICA "developed [the] comprehensive Uniform Code of Arbitration . . . for the securities industry."\textsuperscript{258} The Code was adopted by participating SROs in 1979 and 1980.\textsuperscript{259} The Code's procedures apply uniformly to all claims, with some exceptions for small claims under $2,500.\textsuperscript{260}

\begin{itemize}
\item \textsuperscript{255} Wilko, 346 U.S. at 438 (emphasis added).
\item \textsuperscript{256} Settling Disputes Between Customers and Registered Brokers and Dealers, Securities Exchange Act Release No. 12,528 (June 9, 1976), reprint\textsuperscript{ed} in 9 S.E.C. Docket 833-35 (Mar.-July 1976).
\item \textsuperscript{257} Katsoris, supra note 64, at 283.
\item \textsuperscript{258} Id. at 284.
\item \textsuperscript{259} Id.
\item \textsuperscript{260} Id. at 285, 289. The Uniform Code of Arbitration (Securities Industry Conference on Arbitration 1979) was adopted without change by the National Association of Securities Dealers (NASD) in 1979. This Code embodies the following rules (citations are to NASD Code of Arbitration Procedure, N.A.S.D. Manual (CCH) ¶¶ 3701-3743):
\end{itemize}
The Code provides that a majority of the arbitration panel must not be part of the securities industry. No clear guidance is given in the Code as to who qualifies to be "public arbitrators," that is, those arbitrators who are to constitute a majority of the panel. Nor, for that matter, is there quality guidance for industry arbitrators. One court has stated that "the arbitrators available to consider disputes are generally knowledgeable individuals who have had experience working with the federal securities laws." However, even if these persons are as qualified as federal judges, questions of impar-

(1) There is a six-year time period from the occurrence of the event at issue to raise the claim. ¶ 3715.
(2) The SRO appoints a panel of three to five impartial arbitrators—a majority of whom cannot be from the securities industry (though the public customer may request such a majority). ¶ 3719.
(3) The Director of Arbitration of the SRO determines who serves on the panel, and who acts as chairperson. ¶ 3720.
(4) The parties must be informed of the affiliations of the panel before a hearing date is fixed. ¶ 3723.
(5) Each party gets one peremptory challenge and unlimited challenges for cause. ¶ 3722.
(6) The arbitrators have a duty to disclose any ground that may prevent objectivity. ¶ 3723.
(7) Wide latitude is given as to materiality, relevance, and admissibility of evidence. ¶ 3734.
(8) Parties have a right at any time to representation by counsel. ¶ 3727.
(9) Subpoena power exists as provided by law, but parties are encouraged to cooperate and produce requested data without resort to subpoena. ¶ 3732.
(10) Arbitrators can compel members of the SRO to appear and produce records. ¶ 3733.
(11) Parties shall cooperate voluntarily in exchanging records. ¶ 3732(b).
(12) The Code sets out provisions for pleadings requiring— (a) a "Statement of Claim" specifying relevant facts and remedies sought, ¶ 3713(b); (b) twenty days to answer, ¶ 3713(d); (c) that the answer be specific in setting forth all available defenses, ¶ 3713(d).

261. See supra note 260.
262. Katsoris, supra note 64, at 310.
263. There has historically been a problem with the individual investor's view of the arbitral as inherently unfair because those who sit on the panel are either in the industry or closely affiliated. Id. at 309-12. The Code has added rules to guard against those who are essentially industry members being classified as public arbitrators. Id. However, to investors who consider themselves members of the "public," the Code's use of the term "public" may seem narrow, and questions of inherent bias may arise. See, e.g., Note, supra note 240, at 260 (remarking that attorneys who represent securities brokers are often selected as "public" arbitrators).

264. Brener v. Becker Paribus, Inc., 628 F. Supp. 442, 448 (S.D.N.Y. 1985). The court also noted that "[t]he American Arbitration Association maintains a list of arbitrators who have been selected for their knowledge and expertise." Id. at 448 n.9. Most SROs presently keep their own list of arbitrators. Katsoris, supra note 64, at 312 n.258.
Arbitrability of Section 10(B) Claims

...tiality and meaningful public participation still remain. Assum..."265

Assuming that the Code is an improvement and arbitrators are qualified and "generally knowledgeable," the important procedural differences between arbitration and adjudication adduced in Wilko remain. Accountability of the arbitral through a formal record and review is still not required.266 The SROs often choose to keep "some sort of record,"267 but there seems to be no system of opinions. The scope of judicial review and vacation of award is still limited to egregious behavior.268 Thus, as long as there is a full and fair hearing and the arbitrators are honest, there will be no substantive review.269 A SICA proposal to broaden the scope of review was "rejected as inimical to the simplicity and brevity of arbitration procedures."270 Without a record or review there is no way to assure that the protective provisions crafted by Congress are being properly applied.271

Other procedural disadvantages for investors assigned to arbitrals remain. The wide choice of venue provisions remains lost in arbitration.272 Investors can choose which SRO to arbitrate before, but they are subject to that SRO's choice of locale for arbitration.273 Nor is the extensive pretrial discovery provided by the courts available in arbitration.274 "This is true 'even though the lack of discovery may be fatal to a party's case.' "275

Thus, Congress' guarantee of investor protection still cannot be assured to the extent the Wilko Court envisioned. There are no appellate arbitrators (competent or not) to review interpretations of

266. Id. at 286.
267. Id. at 286 n.47.
268. Id. at 290-91.
269. Id. at 290 (citing Burchell v. Marsh, 58 U.S. 344, 349 (1854)).
270. Id. at 291. It is also noteworthy that the investor gives up the right to a jury trial in a federal forum by submitting claims to arbitration. Note, supra note 240, at 255. Further, brokers may seek arbitration to avoid more liberal jury awards. Note, supra note 22, at 551 n.180.
271. In Wilko the Court found that the provisions of the Securities Act would control arbitration even if the agreement to arbitrate did not require that the arbitrators follow that law. 346 U.S. 427, 434 (1953). Cf. Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 105 S. Ct. 3346, 3353-55 (1985) (arbitration clause need not expressly mention statute for statutory rights to be arbitrated, with arbitral applying substantive rights afforded by the statute at issue).
273. Note, supra note 240, at 255.
274. Katsoris, supra note 64, at 287 & n.52.
275. Id. at 287 n.52 (quoting G. Goldberg, A LAWYER'S GUIDE TO COMMERCIAL ARBITRATION 40 (2d ed. 1983)).
law. Moreover, the absence of wide-ranging venue and discovery procedures makes the arbitral less advantageous to the investor. The SEC's oversight of industry arbitration procedures has not cured these fundamental flaws adduced in Wilko.276

The arbitration process as it now exists simply does not meet the standards of the type of forum intended by Congress to assure the effectiveness of the securities acts' remedial provisions.277 Thirty-three years ago the Wilko Court specifically brought out that English law did provide for "judicial determination of legal issues" decided in an arbitral.278 It may be that the Court was indicating that a sufficient arbitration process, which would include a thorough review, might meet the requirements of investor protection under the Securities Act's jurisdictional provisions. Yet the securities industry rejected the SICA proposals to broaden the scope of review as inimical to the arbitration process.279

If the securities industry truly wants the repeal of Wilko, it will have to provide the assurances of investor protection that Congress requires under the jurisdictional provisions of the securities acts. That the provision of such assurances runs counter to the efficiency policy behind the Arbitration Act is irrelevant. Mitsubishi requires only that when determining the arbitrability of securities law claims, the courts look to Congress' intent in creating the securities statutes.

The securities laws are demanding. They do create inconvenience. Yet they have a weighty purpose, born of the need to protect the financial health of millions of individuals and the nation. Cries of inefficiency and inconvenience, or assertions that the arbitration process is close enough or fair enough, should not induce courts to give up the principles Congress established in the securities acts. It is the securities industry that must live up to those principles and develop suitable procedures. It was the failure of the securities industry that originally led to the creation of the securities acts. As the Wilko Court reiterated, "let the seller also beware"—and be responsible.280

276. See SEC Brief, supra note 31.
278. Id. at 437.
279. Katsoris, supra note 64, at 291.
280. Wilko, 346 U.S. at 430 (quoting H.R. REP. No. 85, 73d Cong. 1st Sess. 2 (1933)).

After four years of warnings about the unrestricted use of arbitration clauses, the SEC, in May of 1983, issued a notice of proposed rulemaking calling for broker-dealers to provide information on the judicial alternatives under the federal securities laws. "The securities industry severely criticized the proposed rule" and raised the charge that the
VI. Conclusion

A careful reading of Wilko, coupled with a thorough analysis of the relevant provisions of the two securities acts, requires that the Wilko doctrine be extended to section 10(b) claims. Moreover, a re-examination of the arbitration process in light of Wilko and Mitsubishi reveals that the arbitration process has not changed sufficiently to meet the demands of investor protection. Thus, the Court should expressly recognize that the Wilko rationale encompasses section 10(b) claims. Any policy re-evaluation that would overturn Wilko must be left to Congress.

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