An Argument Against the Availability of Punitive Damages in Commercial Arbitration

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NOTE

AN ARGUMENT AGAINST THE AVAILABILITY OF PUNITIVE DAMAGES IN COMMERCIAL ARBITRATION

Arbitration provides an economical and expeditious method for litigants to resolve disputes outside of the judiciary.\(^1\) Despite

\(^1\) See Judicial Review of Arbitration: The Role of Public Policy, 58 N.W.U. L. Rev. 545 (1964) ("arbitration has emerged as inexpensive, speedy and favored way to settle disputes without resorting to the courtroom". . .); see also Goldstein, Alternatives for Resolving Business Transaction Disputes, 58 St. John's L. Rev. 69, 78 (1983) (arbitration offers more privacy and convenience while reducing formality); Raymos, Punitive Damage Awards in Maritime Arbitration: A Legitimate Part of the Arbitrator's Arsenal?, 10 MAR. LAW. 251, 253 (1985) (arbitration compared favorably to judicial procedures because of economy and speed).

Unlike professional lawyers and judges, arbitrators are not "steeped in the rules of procedure and evidence." Id. at 253. One scholar has called the arbitrator "a peculiar breed," not limited at all to any one method of decision making, even entitled to follow the divine word should he or she so choose. Fowks, The Arbitrator: As a Punisher and As a Professional, 47 Kan. B.A. J. 7, 10-11 (1978).


The objective of maintaining inexpensive and time-saving arbitral procedures manifests itself throughout the Commercial Arbitration Rules of the American Arbitration Association ("AAA"). See, e.g., Com. Arb. Rules § 14 (1977) (seven-day time limit for appointment of neutral arbitrator); id. § 17 (generally only one arbitrator employed to hear dispute). The average duration of an arbitration procedure under the AAA rules is four to five months. Meyerowitz, The Arbitration Alternative, 71 A.B.A. J., Feb. 1985, at 78, 80. Furthermore, it is usually unnecessary for a successful complainant to have a court confirm the award, clearly a significant expense, since it is well-recognized that arbitrators have the final word and courts will generally not overturn an arbitrator's award. See Robbins, Securities Arbitration: Preparation and Presentation, 42 Arb. J., June 1987, at 3, 14; see also infra note 5 (discussing grounds for modifying or vacating arbitrator's award).
initial concern that arbitrators with varied legal abilities would encroach upon judges "rightful" control over American legal affairs, modern state and federal courts now look favorably upon arbitration\(^2\) and substantial latitude has been afforded arbitrators in fashioning remedies.\(^3\) Hence, commercial arbitration has burgeoned as

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Notably, arbitrators often have no legal background or training, nor do they necessarily possess any particular expertise in the matter of the arbitration. F. Elkouri & E. Elkouri, How Arbitration Works 120 (4th ed. 1985). Rather, the most important quality for an arbitrator has proven to be that of impartiality. Id. at 119. In some disputes, however, a specific expertise is considered essential. Id. This is especially true in cases involving medical or engineering issues. See generally Ranner, The Dynamics of the Arbitration Process, 39 Ann. J., June 1984, at 57, 57 (high degree of quality in labor arbitration is necessitated due to ongoing contractual relationship in post-arbitral period); Note, Awarding Punitive Damages in Medical Malpractice Arbitration, 20 Cal. W.L. Rev. 312, 315 n.26 (1984) (medical malpractice arbitrators are "highly sophisticated and competent" fact finders unlike emotionally susceptible jurors).


Among favorable federal court decisions are: Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 24-25 (1983); Foster v. Turley, 808 F.2d 38, 42 (10th Cir. 1986); Pierson v. Dean, Witter, Reynolds, Inc., 742 F.2d 334, 338 (7th Cir. 1984); Weissbuch v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 558 F.2d 831, 833 (7th Cir. 1977).

\(^3\) See, e.g., South East Atlantic Shipping Ltd. v. Garnac Grain Co., 356 F.2d 189, 192 (2d Cir. 1966) (arbitrator found to have acted properly in assessing party's "business morality" prior to determining award); School City, 422 N.E.2d at 662 (arbitrators, in granting relief, not bound by principles of substantive law). Arbitrators' power to grant "extraordinary remedies" was recognized as far back as the late 1920's. See Hoellering, Remedies in Arbitration, 20 Forum 516, 517 (1985).

Attorney's fees may become part of the award if expressly provided for in the arbitration clause itself. See, e.g., Stermer v. Modiano Constr. Co., 44 Cal. App. 3d 264, 272-73, 118 Cal. Rptr. 303, 314-15 (1975) (agreement may provide payment of attorney's fees to winning party in breach of contract dispute); see generally M. Domke, Domke on Commercial Arbitration § 43.01, at 536 (rev. ed. 1987) (discussing importance of parties' agreement in awarding attorney's fees). A minority view among courts allows the arbitrator to award attorney's fees even if the parties' arbitration agreement did not provide for such. See J.R. Snyder Co. v. Soble, 57 Mich. App. 485, 226 N.W.2d 276 (1975). In Snyder, the arbitrator's award included a provision for "reasonable attorney's fees," although there was no mention of this in the arbitration agreement, and the trial court affirmed a $4,000 attorney's fee. Id. at 485-87, 226 N.W.2d at 277, 279. In affirming the expansive view of arbitrators' powers taken by the lower court, the appellate court sustained the award and noted that "[e]ven if the question were properly before us we would not be disposed to disallow the fee." Id. at 491, 226 N.W.2d at 279.

In addition, "as between court and arbitrator, the U.S. Supreme Court has stated that when a court has determined that the subject matter of a dispute is arbitrable, procedural questions 'which grow out of the dispute and bear on its final disposition should be left to the arbitrator.'" F. Elkouri & E. Elkouri, supra note 1, at 223 (quoting John Wiley & Sons v. Livingston, 376 U.S. 543, 557 (1964)).
a means of settling breach of contract and tort actions when the parties have agreed to forego the more traditional judicial setting. The arbitral award now enjoys the protection of statutes defining those circumstances under which the award may or may not be overturned or altered by a court. These statutory provisions have often been construed in a light most favorable to sustainment of the arbitrator’s ruling. Indeed, because neither procedural nor

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4 See F. Elkouri & E. Elkouri, supra note 1, at 39. Nearly 40,000 arbitration cases were filed in 1984 alone. Meyerowitz, supra note 1, at 79. As a result of the increase in arbitrated claims, courts have been forced to devote significant time to enforcing and vacating clauses and awards. See, e.g., Southland Corp. v. Keating, 465 U.S. 1, 17 (1984) (award affirmed); Compania Espanola de Petroleos, S.A. v. Nereus Shipping, S.A., 527 F.2d 966, 975 (2d Cir. 1975) (clause altered in effort to have it "fit . . . new situation"), cert. denied, 426 U.S. 936 (1976).

5 See Arbitration Act § 10, 9 U.S.C. § 10 (1982). This section of the Federal Arbitration Act provides the only statutory grounds upon which an award may be vacated. See id. Section 10 provides in pertinent part:

- In either of the following cases the United States court . . . may make an order vacating the award upon the application of any party to the arbitration—
  - Where the award was procured by corruption, fraud, or undue means.
  - Where there was evident partiality or corruption in the arbitrators, or either of them.
  - Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, . . . or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.
  - Where the arbitrators exceeded their powers, or so imperfectly executed them that a . . . definite award . . . was not made.


Furthermore, modification of an arbitrator’s award is statutorily provided for in the Federal Arbitration Act when the arbitrator has made a material mistake or miscalculation, decided a matter not within his or her authority, or failed to grant the award in proper form. See 9 U.S.C. § 11 (1982).

6 See Baker v. Sadick, 162 Cal. App. 3d 618, 623-24, 208 Cal. Rptr. 676, 679 (1984). In Baker, a patient and her doctor entered into an agreement whereby “any dispute as to medical malpractice [was to be] determined by submission to arbitration.” Id. at 622-23, 208 Cal. Rptr. at 679. The patient’s claim for medical malpractice in performing breast reduction surgery was taken to arbitration pursuant to the contract. Id. at 622, 208 Cal. Rptr. at 678. As one part of her prayer for relief, the patient sought punitive damages. Id. The appellant argued that the California Civil Code did not allow for punitive damages in “professional negligence claims.” Id. at 623, 208 Cal. Rptr. at 679. Notwithstanding the statute, however, the judge upheld the arbitrator’s award of punitive damages, finding that: “An agreement to arbitrate is a contract . . . Although awards may be vacated if the arbitrator has exceeded his power, any ambiguities in the scope of arbitration are resolved in favor of coverage.” Id. (citations omitted); see also North Cent. Util., Inc. v. East Columbia Water Dist., 480 So. 2d 901, 905-06 (La. Ct. App. 1985) (burden shifts to defendant to set forth factual basis for vacating award), cert. denied, 481 So. 2d 1329 (La. 1986). See generally D. Siegel, Handbook of New York Practice 828 (1978) (only “complete irrationality” will bring about judicial in-
substantive law governs most of their decisions, arbitrators often grant rather unconventional decrees.\footnote{See Coast Trading Co. v. Pacific Molasses Co., 681 F.2d 1195, 1198 (9th Cir. 1982) (absent compelling reasons, labor arbitration awards will be upheld).}
Notwithstanding the enormous latitude given arbitrators, some courts have drawn the line at punitive damages awards, reasoning that the inherently penal nature of exemplary damages warrants a certain degree of judicial oversight and control. As a matter of policy, it is argued, such punishment is best administered exclusively by the courts. In the leading case of Garrity v. Lyle

its failure to adhere to Trade Rules of American Dry Pea & Lentil Association).

See supra note 3 and accompanying text.


In Cochetti v. Desmond, 572 F.2d 102 (3d Cir. 1978), the Third Circuit expressed the quintessential nature of punitive damages:

Punitive damages are not a favorite of the law. Usually assessed both as an example and as a warning against particularly egregious conduct, such damages serve both punitive and deterrent functions. Such awards may be particularly appropriate as a means of vindicating the public interest in preventing violations of civil rights by state officials. The availability of punitive damages as a deterrent may be more significant than ever today, in view of the apparent trend of decisions curtailing the powers of [the] federal courts to impose equitable remedies to terminate such violations.

Id. at 105-06.


One commentator has noted that in the context of stockbroker-customer disputes, “[o]ne of the primary reasons customers' lawyers have traditionally avoided arbitration in which the broker engaged in fraudulent conduct has been the belief that punitive damages are unavailable in arbitration.” Smiley, supra note 7, at 199. Another author has suggested that “because arbitration decisions are rarely published, a punitive damage award from a private arbitral forum may fail to warn potential wrongdoers of the penalty imposed for the conduct. Note, Punitive Damage Awards in International Arbitration: Does the “Safety Valve” of Public Policy Render them Unenforceable in Foreign States?, 20 Loy. L.A.L. Rev. 455, 480 (1987).

While Garrity held that an arbitrator may never award punitive damages, 40 N.Y.2d at 356, 353 N.E.2d at 794, 386 N.Y.S.2d at 832, not all courts have followed this rule. See, e.g., Willis v. Shearson/American Express, Inc., 569 F. Supp. 821, 824 (M.D.N.C. 1983) (arbitrator may award punitive damages when parties' contract so provides). In Willis, the court interpreted a broad arbitration clause within a brokerage agreement as entitling "any arbitrator who may hear this matter to award punitive damages." Id. The court refused to follow Garrity even though the contract provided that New York law would govern, id. at 823-
Stuart, Inc., for example, the New York Court of Appeals held that it is against public policy to award punitive damages in arbitration proceedings brought pursuant to an arbitration provision in the parties’ contract. The court ruled that such awards could not be enforced even when parties had previously authorized an arbitrator to grant punitive damages at his or her discretion. Punitive damages, the court reasoned, are shaped by attitudinal philosophies about correction and reform and are therefore a matter best left exclusively to the state’s consideration.

The United States Supreme Court, in Shearson/American Express, reasoning that “federal law governs the categories of claims subject to arbitration.” Id. Furthermore, the court explained that “[t]he Court perceives no public policy reason persuasive enough to justify prohibiting arbitrators from resolving issues of punitive damages submitted by the parties.” Id. at 824; see also Penna, Punitive Damages and Public Policy, N.Y.L.J., Jan. 14, 1986, at 1, col. 1 (discussing alignment among courts with respect to availability of punitive damages in arbitration).

24, reasoning that “federal law governs the categories of claims subject to arbitration.” Id. Furthermore, the court explained that “[t]he Court perceives no public policy reason persuasive enough to justify prohibiting arbitrators from resolving issues of punitive damages submitted by the parties.” Id. at 824; see also Penna, Punitive Damages and Public Policy, N.Y.L.J., Jan. 14, 1986, at 1, col. 1 (discussing alignment among courts with respect to availability of punitive damages in arbitration).

13 Id. at 356, 353 N.E.2d 794, 386 N.Y.S.2d at 832. In Garrity, the plaintiff-author instituted a court action to confirm an arbitration award of both compensatory and punitive damages against the defendant-publisher, based upon the arbitrator’s finding that the publisher had engaged in “malicious” harassment of the plaintiff and “gross[ly]” underpaid the royalties owed her. Id.
14 Id. Although the court conceded that an arbitrator has authority to “fashion” a remedy according to the wrong done, the majority restricted the scope of such remedy exclusively to compensatory damages. See id. at 357, 353 N.E.2d at 794, 386 N.Y.S.2d at 832. “[A]rbitrators are not . . . empowered to ride roughshod over strong policies in the law which control coercive private conduct.” Id. at 357, 353 N.E.2d at 795, 386 N.Y.S.2d at 832. Hence, punitive measures were “confine[d] to the State and its courts.” Id.
15 Id. at 359, 353 N.E.2d at 796, 386 N.Y.S.2d at 834. Since punitive damages are either available or not available as a matter of law, some jurisdictions have developed tests so that judges may determine the fairness of allowing punitive damages on a more uniform basis. See, e.g., Miley v. Oppenheimer & Co., 637 F.2d 318, 331 (5th Cir. 1981). Miley rejected the four-part Texas test of fairness of punitive awards preferring, instead, “a formula of punitive damages equal to three times compensatory damages.” Id. Such a formula is consistent with statutory law. See, e.g., Sherman Act, 15 U.S.C. § 1 (1982) (antitrust treble damages); Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (1982) (securities fraud treble damages); see also Northern v. McGraw-Edison Co., 542 F.2d 1336, 1350 (9th Cir. 1976) (punitive damages approximated three times compensatory damages), cert. denied, 429 U.S. 1037 (1977); Palmer Coal & Rock Co. v. Gulf Oil Co., 524 F.2d 884, 887 (10th Cir. 1975) (same formula used in fraud case), cert. denied, 424 U.S. 969 (1976).

The Sixth Circuit uses a different standard for determining the propriety of punitive liability: (1) punitive damages may only be awarded in particular cases, such as those involving fraud or gross misrepresentation; and (2) there must have been actual damage suffered by plaintiff. Edwards v. Travelers Ins., 563 F.2d 105, 118 (6th Cir. 1977); see also Note, Punitive Damages in Arbitration: The Search for a Workable Rule, 63 Cornell L. Rev. 272, 295 (1978) (setting forth a model for testing fairness of noncompensatory arbitral awards).
press, Inc. v. McMahon, has arguably left the door open on this issue. In McMahon, the plaintiff-customer brought a civil RICO claim against the defendant-brokerage firm alleging misrepresentation and churning of plaintiff's accounts. The defendant sought to compel arbitration based on a standard arbitration clause provided in the customer agreement that the plaintiff had signed. The plaintiff argued, however, that fraud claims under RICO were nonarbitrable because of the statute's treble damages provision. Emphasizing the civil nature of the RICO claims, the Supreme Court concluded that such claims were arbitrable. The Court stated that the treble damages provision was intended to play primarily a remedial role. State courts may thus find themselves re-evaluating their own policies with regard to the permissibility of punitive damages in arbitration awards.


11. McMahon, 107 S. Ct. at 2235-36. The standard form “Customer Agreement” provided:

Unless unenforceable due to federal or state law, any controversy arising out of or relating to my accounts... shall be settled by arbitration in accordance with the rules... of the National Association of Securities Dealers, Inc. ... and/or the American Stock Exchange, Inc. as I may elect.


13. McMahon, 107 S. Ct. at 2344. They contended that because racketeering is essentially a criminal misdeed, RICO actions must be heard by the courts regardless of any prior agreement to arbitrate, due to the “public interest in [its] enforcement.” Id. The district court ordered arbitration of the common law tort and Securities Exchange Act claims, but not the RICO claims. McMahon v. Shearson/American Express, Inc., 618 F. Supp. 384, 389 (S.D.N.Y. 1985). On appeal, the Second Circuit reversed as to the Exchange Act claims, finding both claims to be non-arbitrable. See McMahon, 788 F.2d at 96-98.

14. McMahon, 107 S. Ct. at 2344-46. The Court reaffirmed a previous holding, emphasizing that “the fact that conduct can result in both criminal liability and treble damages does not mean that there is not a bona fide civil action.” Id. at 2344 (quoting Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 492 (1985)).

15. Id. at 2345.

16. If punitive damages are deemed to include statutory treble damages, state courts may find that the Supreme Court ruling mandates that they now permit the issue of punitive damages to be settled by arbitration. See generally Flanagan v. Prudential-Bache Sec., Inc., 67 N.Y.2d 500, 506, 495 N.E.2d 345, 348, 504 N.Y.S.2d 82, 85 (enforcement of Federal Arbitration Act requires state courts to apply Supreme Court decisions, if available, or those of lower federal courts if in agreement), cert. denied, 107 S. Ct. 402 (1986); Associated Gen. Contractors v. Savin Bros., 45 App. Div. 2d 136, 145, 356 N.Y.S.2d 374, 382 (3d Dep't 1974), aff'd per curiam, 36 N.Y.2d 957, 335 N.E.2d 859, 375 N.Y.S.2d 555 (1975) (court of appeals upholds arbitration award of three times liquidated damages).
Currently, three theories exist regarding the availability of punitive damages to arbitrating plaintiffs. Proponents of the first view favor strict adherence to the Garrity court's holding and contend that punitive damages should never be awarded in arbitration proceedings. Proponents of the second theory, in contrast, would allow the arbitrator to award punitive damages if both parties had provided for them in their arbitration agreement. The final approach would permit arbitrators to grant punitive damages whenever deemed appropriate under the circumstances. This more liberal view was adopted by the California Supreme Court in the seminal case of Baker v. Sadick. The ruling of the New York Court of Appeals in Garrity prompted considerable debate as to whether one has a "right" to punitive damages if clearly warranted under the circumstances. Since courts themselves have struggled with the applicability and assessment of punitive liability, they have consequently been reluctant to sanction arbitration awards of punitive damages. The proponents of Garrity argue that punitive damages should never

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23 See infra notes 26-33 and accompanying text.
24 See infra notes 35-36 and accompanying text.
28 162 Cal. App. 3d 618, 208 Cal. Rptr. 676 (1984); see infra notes 40-45 and accompanying text; supra note 6.
27 See, e.g., Raymos, supra note 1, at 258-59 (supporting use of punitive damages in arbitration awards); Note, supra note 11, at 470-72 (broad sweep of Garrity holding impugns previous case law).

Plaintiffs seeking to preempt a defendant's motion to compel arbitration on the ground that arbitration forecloses them from their "right" to recover punitive damages have met with little success. See, e.g., Sweater Bee By Banff, Ltd. v. Manhattan Indus., Inc., 754 F.2d 457, 463 (2d Cir.) ("[n]or are we persuaded ... that arbitration would be prejudicial because an award of punitive damages would be foreclosed that might otherwise be forthcoming from the district court"), cert. denied, 474 U.S. 819 (1985); Baselski v. Paine, Webber, Jackson & Curtis, Inc., 514 F. Supp. 535, 543 (N.D. Ill. 1981) (arbitration would not result in "forfeiture" of "right" of plaintiff to pursue punitive damages).

29 See supra note 11 and accompanying text.
be awarded by any adjudicator other than a court of law, regardless of the existence of a prior agreement to the contrary. While this reasoning can be supported by both public policy and due process arguments, the Garrity court focused solely on the public policy rationale, asserting that a punitive damages award by an arbitrator would contravene New York's policy of prohibiting the "uncontrolled use of coercive economic sanctions in private arrangements."  

Although courts adopting a strict Garrity approach find that arbitrators may never award punitive damages as a remedy in commercial disputes, other jurisdictions have permitted punitive damages to be granted at the arbitrator's discretion if the parties expressly allowed for such awards in their arbitration agreement.

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31 See infra notes 46-53 and accompanying text.

32 See infra notes 62-75 and accompanying text.


The court will vacate an award enforcing an illegal agreement or one violative of public policy. Since enforcement of an award of punitive damages as a purely private remedy would violate public policy, an arbitrator's award which imposes punitive damages, even though agreed upon by the parties, should be vacated . . . .

If arbitrators were allowed to impose punitive damages, the usefulness of arbitration would be destroyed. It would become a trap for the unwary given the eminently desirable freedom from judicial overview of law and facts . . . . It would lead to a Shylock principle of doing business without a Portia-like escape from the vise of a logic foreign to arbitration law.

*Id.* at 357-59, 353 N.E.2d at 795-96, 386 N.Y.S.2d at 832-34 (citations omitted).

In arriving at its decision, the court distinguished prior case law in which treble damages had been permitted, implicitly asserting that public policy considerations need not be accounted for when applying statutorily mandated remedies. See *id.* at 357-58, 353 N.E.2d at 795, 386 N.Y.S.2d at 833. *But see id.* at 363-64, 353 N.E.2d at 799, 386 N.Y.S.2d at 837 (Gabrielli, J., dissenting) (public policy may be manifested through statutes).

34 See supra notes 26-33.

35 See, e.g., Willis v. Shearson/American Express, Inc., 569 F. Supp. 821, 824 (M.D.N.C. 1983). In Willis, plaintiff had invested funds in an account managed by the defendant corporation which he claimed were fraudulently invested by the defendant. Their contract provided that "any controversy arising out of or relating to [the] accounts . . . shall be settled by arbitration in accordance with the rules then in effect of the National Association of Securities Dealers, Inc. or . . . the New York Stock Exchange . . . or the American Stock
While an argument can be made that this second method brings into play the best of both worlds—parties enjoying the right to receive what they bargained for, and states maintaining their police powers to punish malevolent parties in all other circumstances—it can be argued that the public's interest is not duly served when arbitrators are permitted to award punitive damages.\(^{36}\) Indeed, it is submitted that the state's power to punish is one that is not readily transferrable to a panel of arbitrators because to do so transgresses important state interests.

The third view that has been advanced would advocate extending arbitrators' powers beyond the express authority granted to them in the parties' predispute agreement.\(^{37}\) Courts following this line of reasoning perceive broad arbitration clauses as bestowing great discretion upon the arbitrator in fashioning a remedy.\(^{38}\) Under this rationale, even if a contract has been entered into because of fraud, the arbitration clause may be severable, and thus enforceable.\(^{39}\) *Baker v. Sadick*\(^ {40}\) is the leading case supporting this proposition.\(^ {41}\) *Baker* involved a medical malpractice dispute which had been sent to arbitration by way of a contract provision be-

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Exchange." *Id.* at 822-23. Because of this broad arbitration agreement, the district court found that the "provision includes claims for punitive damages." *Id.* at 824. The court stated, "Hence, the parties by their contract have authorized any arbitrator who may hear this matter to award punitive damages." *Id.* (emphasis added).

The Seventh Circuit has interpreted the *Garrett* ruling itself as espousing this view. See Pierson v. Dean, Witter, Reynolds, Inc., 742 F.2d 334, 337 (7th Cir. 1984) (only where punitive damages are specifically mentioned in the contract may an arbitrator award them). Arbitration awards under collective bargaining agreements have generally been subjected to the same interpretation. See, e.g., Baltimore Regional Joint Bd. v. Webster Clothes, Inc., 596 F.2d 95, 98 (4th Cir. 1979) (where bargaining agreement does not contemplate punitive damages they must be excluded from arbitral award).

\(^{36}\) See Penna, *supra* note 11, at 1-2.


\(^{38}\) See *supra* note 8 and accompanying text (discussing lack of procedural and substantive restrictions on arbitrators).

\(^{39}\) See Robert Lawrence Co. v. Devonshire Fabrics, Inc., 271 F.2d 492, 411 (2d Cir. 1959). Where an arbitration contract is sufficiently broad to cover a fraud claim, exchanged promises to arbitrate may permit the separation of the arbitration clause from the contract and permit the parties to proceed to arbitration. *Id.*


tween the defending surgeon and his patient.\textsuperscript{42} The California Court of Appeals upheld the arbitrator's award of exemplary damages.\textsuperscript{43} The Baker court distinguished Garrity as based solely on a contract action, holding that tortious misconduct is an acceptable basis for punitive liability even in the context of an arbitration proceeding.\textsuperscript{44} The court's ruling was broad, concluding that any matter voluntarily submitted to arbitration is a potential source of punitive liability.\textsuperscript{45}

It is submitted that while the strict approach of Garrity will provide the most favorable results, it also implicitly raises more questions than it answers,\textsuperscript{46} including the question of what constitutes "public policy."\textsuperscript{47} This is an important consideration because many jurisdictions have utilized the public policy rationale to restrict the scope of authority an arbitrator may lawfully exercise.\textsuperscript{48}

\begin{itemize}
  \item \textsuperscript{42} Baker, 162 Cal. App. 3d at 621-22, 208 Cal. Rptr. at 678. Liability for tort claims generally will not be arbitrated since the parties rarely foresee tort actions in advance of injury and, therefore, will not have agreed to arbitrate. However, if the tort issue arises in connection with a contract, as in Baker, the courts will redress the breach of contract by allowing the parties to proceed to arbitration. See Kilgore Mfg. Co. v. New Hampshire Fire Ins. Co., 280 App. Div. 332, 335, 113 N.Y.S.2d 554, 557 (1952), aff'd, 305 N.Y. 815, 113 N.E.2d 558 (1953). If the tort claim is not directly related to the contract, generally it cannot be arbitrated. See generally Old Dutch Farms, Inc. v. Milk Drivers & Dairy Employees Local Union, 359 F.2d 598, 603 (2d Cir.) (absent express contract provision granting arbitrator the power to hear tort claim, employer did not forego his statutory right to judicial determination), cert. denied, 385 U.S. 832 (1966).
  \item \textsuperscript{43} Baker, 162 Cal. App. 3d at 631, 208 Cal. Rptr. at 684.
  \item \textsuperscript{44} Id. at 630, 208 Cal. Rptr. at 684. In refusing to follow Garrity, the California Court of Appeals commented that since punitive damages are normally recoverable in medical malpractice actions, "[i]t strains legal imagination to conclude an agreement to substitute arbitration for litigation results ipso facto in forbearance of a claim which would support an award of punitive damages." Id.
  \item \textsuperscript{45} Id.
  \item \textsuperscript{46} Compare Garrity, 40 N.Y.2d at 357-58, 353 N.E.2d at 795, 386 N.Y.S.2d at 833 (prohibition against arbitrator awarding punitive damages based on "strong public policy") with id. at 363, 353 N.E.2d at 799, 386 N.Y.S.2d at 837 (Gabrielli, J., dissenting) ("public policy against punitive damages is not so commanding that the Legislature has found it necessary to embody that policy into law").
  \item \textsuperscript{47} See Safeway Stores, Inc. v. Retail Clerks Int'l Ass'n, 41 Cal. 2d 567, 571, 261 P.2d 721, 726 (1953) (term "public policy" inherently not subject to precise definition).
  \item \textsuperscript{48} See supra note 33. Parties wishing to attack the arbitral award on public policy grounds must do so in the early stages of the proceedings to ensure favorable results. M. Domke, supra note 3, § 33:03, at 469-71; see also Sweater Bee By Banff, Ltd. v. Manhattan Indus., Inc., 754 F.2d 457, 460-64 (2d Cir. 1985) (discussion of policy arguments in favor of and opposed to waiving arbitration when not asserted at earliest stage), cert. denied, 474 U.S. 819 (1985).
\end{itemize}

To restrict the arbitral award, parties are advised to do so at the outset in the predispute arbitration agreement. See Note, Arbitrability of Disputes Under the Federal Arbitration Act, 71 Iowa L. Rev. 1137, 1144-46 (1986).
While not lending itself to any precise definition,9 "public policy" is generally associated with the "social, moral, and physical condition of the community."50 Its boundaries may best be ascertained in state constitutions, legislation,51 and case law.52 It is suggested that public policy is a matter most fairly adjudged by the government and one not to be left in private hands, since the private sphere is too susceptible to its own biases and not sufficiently concerned with the interest of the public at large.53

PUNITIVE DAMAGE AWARDS UNAFFECTED BY THE McMAHON DECISION

In Shearson/American Express, Inc. v. McMahon,54 the Supreme Court determined that arbitrators may lawfully arbitrate disputes in which the plaintiffs, if successful, are to be recom-

In Sprinzen v. Nomberg, 46 N.Y.2d 623, 389 N.E.2d 456, 415 N.Y.S.2d 974 (1979), the New York Court of Appeals recognized that only a few matters were "so intertwined with overriding public policy considerations" as to merit judicial intervention, including: (1) awards containing punitive damages; (2) matters regarding liquidation of insolvent insurance companies when there exists a statute granting exclusive subject matter jurisdiction to the state. Id. at 630, 389 N.E.2d at 459, 415 N.Y.S.2d at 977; see also Gross, Labor Relations Law, 32 Syracuse L. Rev. 389, 405 (1981) (New York Court of Appeals viewed as narrowing bounds of arbitration by reviewing public policy considerations in public sector disputes).


52 In re Adoption of MM, 652 P.2d 974, 978 (Wyo. 1982). "When the constitution and statutes have not spoken on a subject, public policy refers to a principle of law that holds no one can lawfully do that which has a tendency to be injurious to the public." Id.


pensed with statutory treble damages. It is submitted that the holding of McMahon, though seemingly bestowing upon the arbitrator the authority to grant punitive awards, does not in fact extend that far, and that a restrictive interpretation of McMahon is warranted because statutory treble damages, by nature, differ from punitive damages in several significant respects. While it is conceded that both punitive damages and statutory treble damages serve similar functions—to deter future misconduct and punish wrongdoers—it is only when imposing punitive damages that a judge must ascertain the relevant public policy issues. In addition, treble damages require a finding of actual damages, whereas punitive liability will often be imposed even when only nominal

55 Id. at 2343, 2346; see supra notes 17-20 and accompanying text.
57 See, e.g., International Bhd. of Elec. Workers v. Foust, 442 U.S. 42, 48 (1978) (purpose of imposing punitive liability is to punish reprehensible conduct); In re Air Crash Disaster, 644 F.2d 594, 610 (7th Cir.) (punitive damages punish misconduct), cert. denied, 454 U.S. 878 (1981); Conchetti v. Desmond, 572 F.2d 102, 105 (3d Cir. 1978) (assessment of punitive damages is usually to set an example and serve as a warning). Punitive damages have been defined by one commentator as "any penalty, in money or property, exacted from the defendant by a civil judgment primarily to deter him or others from engaging in similar conduct or to punish him for engaging in such activity." See Wheeler, supra note 53, at 273.
58 This is so because treble damages awards are made pursuant to statute. Omnibus Housing Act, ch. 403, §§ 9, 51, as amd’y [1983] N.Y. Laws 732-741 (subtenant "entitled to damages of three times the overcharge" of rent by original tenant); see Kolbert v. Clayton, 127 Misc. 2d 1036, 1037, 487 N.Y.S.2d 985, 995 (N.Y.C. Civ. Ct. N.Y. County 1985) ("fair reading" of Omnibus Housing Act mandates granting of treble damages when violated); see also Royal Business Mach., Inc. v. Lorraine Corp., 633 F.2d 34, 49 (7th Cir. 1980) (prerequisite to punitive damages recovery is that public interest be served thereby); Glissman, 175 Ind. App. at 496, 372 N.E.2d at 1190 (punitive damages "awarded in furtherance of public policy"); Davis v. Williams, 92 Misc. 2d 1051, 1055, 402 N.Y.S.2d 92, 95 (N.Y.C. Civ. Ct. Kings County 1977) (punitive damages serve policy of enforcing housing standards). One federal court's public policy justification for exacting a punitive damages award against a corporate defendant was the desire to bring "home" to those in positions of authority the dire implications of their wrongdoings. Aldrich v. Thomson McKinnon Sec., Inc., 756 F.2d 243, 247 (2d Cir. 1985).
59 See, e.g., Stoner v. Houston, 265 Ark. 928, 933, 582 S.W.2d 28, 31 (1979) (court reversed treble damages recovery in action for injury to property because actual damages of one dollar did not support such a remedy).
Recognizing these differences, courts will often employ disparate standards in applying the two types of damages.\textsuperscript{61}

**The Constitutionality of Punitive Damages in Arbitral Awards**

The bifurcated purpose in exacting punitive damages from a defendant is both punishment and deterrence.\textsuperscript{62} While awarded solely in civil actions, punitive damages generally impose a hardship severe enough to justify characterizing them as "quasi-criminal."\textsuperscript{63} In other contexts, the Supreme Court has noted that certain sanctions may legitimately be treated as criminal in nature, though not technically classified as such,\textsuperscript{64} thereby entitling the defendant to numerous constitutional safeguards.\textsuperscript{65}

The demands of procedural due process render uncertain the constitutional validity of punitive damages, particularly in light of the fact that punitive damages have often been criticized as being rendered in an arbitrary and capricious fashion by overly sympathetic juries.\textsuperscript{66} The issues raised thereby become even more com-
pelling when punitive liability is assessed in the context of an arbitrated dispute.\textsuperscript{67} The "fundamental fairness" requirement of fourteenth amendment due process, for instance, is not safeguarded by arbitral procedures as generally employed.\textsuperscript{68} Moreover, a "heavy-handed" punitive damages award may bear such a disturbing resemblance to criminal sanctions as to implicate both the eighth amendment\textsuperscript{69} and the civil litigant's right of appeal.\textsuperscript{70} When punitive damages are imposed by an arbitrator, there are a limited number of instances in which a judge will possess jurisdiction to ensure that such rights are not being violated.\textsuperscript{71}

Of critical concern is protecting the civil defendant's seventh amendment right to a jury trial.\textsuperscript{72} Although defendants charged with serious federal crimes may waive their right to a trial by jury,\textsuperscript{73} courts are reluctant, out of concern for the defendant, to allow a waiver of a jury trial where the circumstances would otherwise clearly warrant one.\textsuperscript{74} It is submitted that because they clearly resemble criminal sanctions, punitive damages must not be permitted outside the protective eye of the judiciary.\textsuperscript{75}

**CONCLUSION**

Courts have come a long way from the time when they considered arbitration a usurpation of their jurisdictional power over via-

\textsuperscript{67} See Saunders, The Quest for Balance: Public Policy and Due Process in Medical Malpractice Arbitration Agreements, 23 Harv. J. on LEGIS. 267, 272-280 (1986).


\textsuperscript{69} U.S. Const. amend. VIII. "Excessive bail shall not be required, nor excessive fines imposed, nor cruel and unusual punishment inflicted." Id.

\textsuperscript{70} See Raymos, supra note 1, at 256. "Congress, by statute, has indicated a reluctance to upset arbitration awards by allowing only narrow grounds for review of arbitration awards." Id.; see also 9 U.S.C. § 10-11 (1982 & Supp. 1986).


\textsuperscript{72} U.S. Const. amend. VII. The seventh amendment provides: "In Suits at common law, . . . the right of trial by jury shall be preserved, and no fact tried by jury, shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law." Id.

\textsuperscript{73} Singer v. United States, 380 U.S. 24, 34 (1965).

\textsuperscript{74} See id. Waiver will only be allowed when the defendant expressly and intelligently consents to the waiver and the Government and a responsible trial judge acquiesce. Id. at 24.

\textsuperscript{75} See supra note 63 and accompanying text.
ble disputes. Today, parties can usually be confident that their contractual arrangements to arbitrate claims will be enforced by the courts. Nonetheless, parties must not confuse their own right to undergo extra-judicial dispute resolution with the state's exclusive authority to dispense punishment. Whereas the former is a function of contract law, the latter is derived from public policy and due process principles. Hence, notwithstanding the parties' prior agreement, arbitrators must be prevented from granting punitive damages in commercial arbitration awards.

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