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The Application of Due Process to Arbitration Awards of Punitive Damages—Where is the State Action?

Charles Smith* 

"[The] due process challenge to the arbitration panel's award of punitive damages must fail. To decide otherwise would constitutionalize private arbitration proceedings and diminish both the effectiveness and the appeal of the arbitral forum as an alternative means for resolving disputes."1

I. INTRODUCTION

Arbitration is a private process that is similar to a court trial. It is often used to gain a final decision as to a contested matter in a way that is generally less expensive and time consuming than litigating the same dispute in the court system. Arbitration statutes such as the Federal Arbitration Act2 (FAA) allow judicial review of arbitration awards on very limited grounds.

State action is a requirement that a claim made pursuant to the Due Process Clause of the Fourteenth Amendment of the United States Constitution must be grounded in conduct by a state actor, such as a government employee or agency, instead of a private actor. However, under specific circumstances, the conduct of a private actor can be categorized as state action.

Therefore, at first blush, it would seem that arbitration and state action exist in two separate areas of the law. However, in recent years, a number of cases and commentators have addressed the issue of whether a court should confirm an arbitration award when the award violates the Due Process Clause of the Fourteenth Amendment. This would seemingly invoke the state action requirement in the sense that any court is a state actor. The typical Due Process challenge to an arbitration award features an award that includes punitive damages in excess of the limits imposed by the United States Supreme Court. In other words, the losing party in arbitration challenges the arbitrator’s award as if it were a jury verdict.

However, the cases have uniformly declined to hold that a court is a state actor in this situation, and thus arbitration awards of punitive damages that would otherwise violate Due Process should be confirmed. On the other hand, the commentators are more open to the position that a court’s confirmation of an arbitra-

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tion award is state action, and thus the award must be evaluated according to the strictures of Due Process.

Part II of this article will discuss the process of arbitration, including what constitutes arbitration, the limited judicial review of arbitration awards, the policy of finality of arbitration, and the contractual nature of arbitration. Part III will analyze the concept of state action in the context of a recent United States Supreme Court case as well as an older case holding that a court was a state actor.

Part IV of this article will discuss United States Supreme Court cases dealing with Due Process challenges to jury verdicts of punitive damages. Specifically, these challenges are to the amount of punitive damages, which are currently limited by the United States Supreme Court's Due Process jurisprudence to no more than a single-digit ratio between punitive and compensatory damages. Part V will analyze the availability of punitive damages in arbitration.

Part VI of this article will talk about the cases and articles that have considered whether there is state action when a party requests that a court confirm an arbitration award as a judgment. As stated above, this issue is generally raised with respect to an arbitration award that contains punitive damages in excess of the limits imposed by the United States Supreme Court pursuant to Due Process.

In particular, this article will analyze why the position of the courts—no state action—is correct. Specifically, this article will take the position that the policy of finality traditionally found in arbitration law must trump any constitutional inquiries. This is because arbitration is ultimately based on the parties' agreement, which inevitably recites that the arbitrator's decision shall be final and, in any event, this finality is generally implied.

To permit another avenue for judicial review of an arbitral award would further chip away at both the policy of finality and the efficacy of arbitration itself. A recent Eleventh Circuit case—B.L. Harbert Int'l, LLC v. Hercules Steel Co.—put it well when it stated:

In litigating this case without good basis through the district court and now through this Court, Harbert has deprived Hercules and the judicial system itself of the principal benefits of arbitration. Instead of costing less, the resolution of this dispute has cost more than it would have had there been no arbitration agreement. Instead of being decided sooner, it has taken longer than it would have to decide the matter without arbitration. Instead of being resolved outside the courts, this dispute has required the time and effort of the district court and this Court.

When a party who loses an arbitration award assumes a never-say-die attitude and drags the dispute through the court system without an objectively reasonable belief it will prevail, the promise of arbitration is broken. Arbitration's allure is dependent upon the arbitrator being the last decision maker in all but the most unusual cases. The more cases there

3. 441 F.3d 905 (11th Cir. 2006). The B.L. Harbert case featured a challenge to an arbitration award solely on the grounds that the award reflected a "manifest disregard of the law." Id. at 910. The manifest disregard exception, which is not one of the Federal Arbitration Act's limited grounds for judicial review, has been accepted by every federal circuit as well as a number of state courts. See infra note 53.
are, like this one, in which the arbitrator is only the first stop along the way, the less arbitration there will be. If arbitration is to be a meaningful alternative to litigation, the parties must be able to trust that the arbitrator's decision will be honored sooner rather than later.4

Arbitration is a private process to which the parties have agreed, and the courts' only obligation is to uphold that agreement pursuant to established arbitration and contract law. It follows that, in order to preserve the arbitration system itself, judicial review based on Due Process cannot be allowed. Therefore, a court's confirmation of an arbitration award cannot be state action.

II. ARBITRATION DEFINED

There are almost as many definitions of "arbitration" as there are courts and commentators willing to define the process. The issue is complicated somewhat by the failure of many arbitration statutes, including the FAA, to provide a definition. Set forth below are some guidelines pertaining to the procedure of arbitration, the limited judicial review of an arbitrator's award, the policy of finality inherent in arbitration, and the contractual nature of arbitration.

A. Arbitration Procedure

The procedure for an arbitration proceeding is informed by one or both of two sources: (1) any guidelines provided by the courts, and (2) the parties' arbitration agreement. More fundamentally, there can be no arbitration without the parties' agreement thereto.5 Some courts define arbitration by setting forth a fairly precise list of elements,6 while other courts view the situation in a more philosophical manner.7 The courts have determined that arbitration has taken place in a number of diverse circumstances as shown by the following cases.

4. 441 F.3d at 913 (emphasis added).
5. An arbitration agreement is generally a written contract executed by all parties, though an arbitration agreement can also be created by way of an unsigned writing or ratification by the parties' conduct. Examples of enforcement of an arbitration agreement based on an unsigned writing include: Genesco, Inc. v. T. Kakuuchi & Co., 815 F.2d 840, 846 (2d Cir. 1987) ("[W]hile the [FAA] requires a writing, it does not require that the writing be signed by the parties."); Valero Ref., Inc. v. M/T Lau-berhorn, 813 F.2d 60, 64 (5th Cir. 1987) (same conclusion). Examples of the parties' conduct forming an arbitration agreement by ratification include: Nghiem v. NEC Elec., Inc., 25 F.3d 1437, 1440 (9th Cir. 1994) ("[A]n agreement to arbitrate an issue need not be express; . . . it may be implied from the conduct of the parties." (quoting Fortune, Alsweet & Eldridge, Inc. v. Daniel, 724 F.2d 1355, 1356 (9th Cir. 1983))); Law Offices of Ian Herzog v. Law Offices of Joseph M. Fredrics, 71 Cal. Rptr. 2d 771, 774 (Cal. Ct. App. 1998) ("While the [California arbitration] statutes permit the courts to specifically enforce only written agreements to arbitrate, once the parties have arbitrated and a written award is made, the courts can enforce the award even if the underlying agreement to arbitrate were oral.") (citation omitted).
7. See, e.g., Bowles Fin. Group, Inc. v. Stifel, Nicolaus & Co., 22 F.3d 1010, 1011 (10th Cir. 1994):
The case of *FIT Tech, Inc. v. Bally Total Fitness Holding Corp.* showed that an arbitration in everything but name is, in fact, an arbitration. The *FIT* case arose out of an Asset Purchase Agreement under which the plaintiffs (primarily Laird and Baker) sold eight health and fitness centers to the defendant (Bally). The Asset Purchase Agreement contained provisions which provided for reference of any dispute regarding the calculation of what was basically the final purchase price "to the Accountants [designated as PriceWaterhouseCoopers elsewhere in the contract] for final determination . . . which determination shall be final and binding on all of the parties hereto."10

Disputes developed between the parties and the plaintiffs filed an action for breach of contract and other claims against the defendant alleging various accounting and operating violations which purportedly reduced the amount of the purchase price.11 The defendant moved to dismiss the complaint on the grounds that the claims therein were required to be submitted to the accountants under the Asset Purchase Agreement, but while the district court concluded that certain factual allegations were within the purview of the accountants, the court decided that most allegations were to be decided by the court.12 The defendant appealed, arguing that all of the plaintiffs' claims should be submitted to the accountants or, alternatively, all such claims were subject to the pending arbitration as to the Employment Agreement.13

Initially, the court of appeals held that "arbitration" would be defined by federal law, not state law.14 The *FIT* court then decided the question of "[w]hether the accounting remedy is "arbitration" under the federal statute" in the affirmative because "[t]he answer does not depend on the nomenclature used in the agreement [citation omitted]; rather, the question is how closely the specified procedure resembles classic arbitration and whether treating the procedure as arbitration serves the intended purposes of Congress."15

The *FIT* court noted that the Asset Purchase Agreement "makes the Price Waterhouse remedy 'final' . . . and other common incidents of arbitration of a contractual dispute are present: an independent adjudicator, substantive standards

Arbitration is a creature born of a contract between parties who are desirous of avoiding litigation in a court of law. Arbitration requires the parties agree to rules of arbitration. Frequently, rules of arbitration specifically exclude the application of judicial rules of evidence and, instead, the arbitrators determine the materiality and relevance of all evidence offered. Arbitrators are not judges of a court nor are they subject to the general superintending power of a court. Arbitration provides neither the procedural protections nor the assurance of the proper application of substantive law offered by the judicial system. Those who choose to resolve a dispute by arbitration can expect no more than they have agreed. One choosing arbitration should not expect the full panoply of procedural and substantive protection offered by a court of law. In short, "by agreeing to arbitrate, a party 'trades the procedures and opportunity for review of the courtroom for the [perceived] simplicity, informality, and expedition of arbitration.'"

8. 374 F.3d 1 (1st Cir. 2004).
9. *Id.* at 2-3.
10. *Id.* at 3.
11. *Id.* at 4.
12. *Id.* The defendant's motion for reconsideration, which was based on the assertion that the plaintiffs had elected to submit all claims to arbitration due to the pendency of an arbitration commenced under the provision in the Employment Agreement, was denied. *Id.* at 4-5.
13. *Id.* at 5.
14. *Id.* at 6.
15. *Id.* at 7.
(the contractual terms of the pay-out), and an opportunity for each side to present its case."\textsuperscript{16} The court of appeals held that "the accounting remedy departs from a common feature of many arbitrations" in that the reference to the accountants would resolve only part of the disputes between the parties.\textsuperscript{17} However, the court stated that "arbitrations sometimes do cover only a part of the overall dispute between the parties."\textsuperscript{18}

The finding that the "accounting remedy" in the Asset Purchase Agreement featured in the FIT case evidences that special words such as "arbitration" or "arbitrator"—or even any reference to an Alternative Dispute Resolution (ADR) provider and its procedures—are not necessary in order for a process to be deemed an arbitration. This is consistent with the FAA's policy of encouraging arbitration.\textsuperscript{19}

The case of Kabia v. Koch\textsuperscript{20} showed that even The People's Court's proceedings can constitute arbitration. The dispute in Kabia v. Koch was based on allegedly defamatory statements made during a televised episode of The People's Court by the defendant, "Arbitrator" Edward I. Koch, that the plaintiff was a "kidnapper."\textsuperscript{21} The plaintiff's underlying action for damages against his son had originally been filed in small claims court, but the plaintiff and his son accepted the opportunity to instead have their dispute resolved on The People's Court.\textsuperscript{22} They signed an agreement to arbitrate which provided that the show's producer (not the losing party) would pay any award or, in the event of no award (such as a defense judgment), all litigants would be paid $250.00 each by The People's Court.\textsuperscript{23} Plaintiff's also granted a release of the defendant and others pertaining to "statements during ... the arbitration which plaintiff and/or defendant [in the underlying dispute] ... feel rightly or wrongly to be derogatory, defamatory or in some other way injurious to themselves."\textsuperscript{24}

In the plaintiff's defamation action, the court ruled that the proceeding over which the defendant presided on The People's Court was an arbitration, and thus the defendant was immune from liability by first reasoning that arbitration is defined by the Black's Law Dictionary as "[a] process of dispute resolution in which a neutral third party (arbitrator) renders a decision after a hearing at which both parties have an opportunity to be heard."\textsuperscript{25} In addition, the plaintiff and his son both agreed, in their underlying small claims action, "to arbitrate their dispute

\begin{itemize}
  \item[16.] Id.
  \item[17.] Id.
  \item[18.] Id.
  \item[19.] See, e.g., Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 24-25 (1991) (the purpose of the FAA "was to reverse the longstanding judicial hostility to arbitration agreements that had existed at English common law and had been adopted by American courts, and to place arbitration agreements upon the same footing as other contracts. ... [The FAA's] provisions manifest a 'liberal federal policy favoring arbitration agreements.'"); Discover Bank v. Super. Ct., 113 P.3d 1100, 1110 (Cal. 2005) ("California law, like federal law, favors enforcement of valid arbitration agreements. ... Thus, under both federal and California law, arbitration agreements are valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.") (Citation omitted).
  \item[21.] Id. at 251-52.
  \item[22.] Id.
  \item[23.] Id. at 252.
  \item[24.] Id. (quoting BLACK'S LAW DICTIONARY 105 (6th ed. 1990)).
  \item[25.] Id. at 254.
\end{itemize}
before an agreed-upon arbitrator [the defendant]."26 Finally, the court noted the limits on judicial review of any arbitration but stated that "[s]uch limits are the essence of arbitration and allow for its economical and expeditious resolution of disputes."27

The Kabia v. Koch case took a situation that had the proper terminology in the arbitration agreement and clarified that the "show business" aspects of the process—in particular, the fact that the show's producer, not the losing party, would pay any award or, if no award, each party would receive $250.00 from the producer—did not remove the dispute from the arbitration arena.

B. The Arbitration Process is Dictated by the Parties' Contract

The above discussion displays the courts' involvement in arbitration. However, at its core, arbitration is still a private proceeding subject to the parties' arbitration agreement.28 To this end, the FAA states:

A written provision ... to settle by arbitration a controversy thereafter arising ... or ... to submit to arbitration an existing controversy ... shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.29

Additionally, the parties to an arbitration agreement have considerable leeway in crafting the process for their arbitration. These issues can include but are not limited to (1) alteration of the statutory judicial review standards, (2) designation of the substantive law to be applied, and (3) selection of the arbitrator(s).

The courts are split as to whether the parties to an arbitration agreement can agree to expand the scope of judicial review of the arbitral award beyond the statutory grounds.30 The case of Gateway Techs., Inc. v. MCI Commc'ns Corp.31 provides an example of where an arbitration agreement that expanded judicial review was enforced. In Gateway, the arbitration agreement allowed for de novo judicial review based on errors of law.32 The Fifth Circuit emphasized the FAA's policy of enforcing arbitration agreements, stating that "federal arbitration policy

26. Id.
27. Id. at 255.
28. Action Box Co. v. Panel Prints, Inc., 130 S.W.3d 249, 252 (Tex. App. 2004) ("The authority of an arbitrator derives from the arbitration agreement and is limited to a decision of the matters submitted therein.").
31. 64 F.3d 993 (5th Cir. 1995).
32. Id. at 995.
demands that the court conduct its review according to the terms of the arbitration contract.\textsuperscript{33}

On the other hand, many jurisdictions have declined to enforce arbitration agreements which expand judicial review. For instance, in \textit{Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.},\textsuperscript{34} the Ninth Circuit acknowledged the federal policy of following arbitration but still refused to enforce a provision of the parties' contract that provided for expanded judicial review of the arbitrator's award, reasoning:

\begin{quote}
[P]arties have complete freedom to contractually modify the arbitration process by designing whatever procedures and systems they think will best meet their needs . . . Once a case reaches the federal courts, however, the private arbitration process is complete, and because Congress has specified standards for confirming an arbitration award, federal courts must act pursuant to those standards and no others.\textsuperscript{35}
\end{quote}

On a related issue, a few courts have dealt with the issue of whether an arbitration agreement will be enforced if it deprives the court of the ability to review on grounds permitted by law.\textsuperscript{36} Also, arbitration agreements which provide for "appellate" review of an arbitration award by another arbitration tribunal are enforceable.\textsuperscript{37}

In arbitration, the parties are free to designate by way of a choice of law clause the applicable substantive and procedural law. In \textit{Volt Information Sciences, Inc. v. Bd. of Trustees of Leland Stanford Jr. Univ.},\textsuperscript{38} the United States Supreme Court recognized the parties' right to include a choice of law clause in their arbitration agreement, reasoning that "[w]here, as here, the parties have agreed to abide by state rules of arbitration, enforcing those rules according to the terms of the agreement is fully consistent with the goals of the FAA, even if the result is that arbitration is stayed where the Act would otherwise permit it to go forward."\textsuperscript{39}

\textsuperscript{33} \textit{Id.} at 997.
\textsuperscript{34} 341 F.3d 987 (9th Cir. 2003).
\textsuperscript{35} \textit{Id.} at 1000.
\textsuperscript{36} Compare Bowen v. Amoco Pipeline Co., 254 F.3d 925, 931 (10th Cir. 2001) (limitation allowed if clear and specific) with Hoef v. MVL Group, Inc., 343 F.3d 57, 64 (2d Cir. 2003) ("Arbitration agreements are private contracts, but at the end of the process the successful party may obtain a judgment affording resort to the potent public legal remedies available to judgment creditors. . . . Congress impressed limited, but critical, safeguards onto this process, ones that respected the importance and flexibility of private dispute resolution mechanisms, but at the same time barred federal courts from confirming awards tainted by partiality, a lack of elementary procedural fairness, corruption, or similar misconduct.").
\textsuperscript{37} Cummings v. Future Nissan, 27 Cal. Rptr. 3d 10, 11, 12 & n.3, 17 (Cal. Ct. App. 2005) (arbitration agreement providing for second arbitrator's review of first arbitrator's award "according to the law and procedures applicable to appellate review by the California Court of Appeal of a civil judgment following [a] court trial" was enforceable; the second arbitrator's reversal of the first arbitrator's award was judicially reviewable). Some private ADR providers have created "appellate arbitration" procedures as part of the services they offer. \textit{E.g.}, J.A.M.S. \textit{OPTIONAL ARBITRATION APPEAL PROCEDURE} (2003), \textit{available at} http://www.jamsadr.com/rules/optional.asp.
\textsuperscript{38} 489 U.S. 468 (1989).
\textsuperscript{39} \textit{Id.} at 479.
In *Sovak v. Chugai Pharmaceutical Co.*, the Ninth Circuit held the FAA, not Illinois law, governed the arbitration procedures, holding:

Parties may agree to state law rules for arbitration even if such rules are inconsistent with those set forth in the Federal Arbitration Act . . . However, parties must clearly evidence their intent to be bound by such rules. . . . In other words, the strong default presumption is that the FAA, not state law, supplies the rules for arbitration.  

In *Sovak*, the court stated that "a general choice-of-law clause within an arbitration provision does not trump the presumption that the FAA supplies the rules for arbitration" in support of its holding that the general choice-of-law clause in the parties' agreement applied to Illinois substantive law only.  

Therefore, while the parties may be free to choose their own arbitration procedures by contract, they should be careful to specify the governing law in the arbitration clause and not simply rely on a choice-of-law provision purporting to pertain to the entire contract. Moreover, the parties should expressly designate whether their choice-of-law clause applies to substantive law only, procedural law only, or both.  

Finally, "[o]ne of the main advantages of contractual arbitration is that it allows the parties to designate a single arbitrator or a panel and to specify the qualifications the arbitrator(s) must possess." This seemingly broad discretion in picking an arbitrator or panel of arbitrators can be impacted by, *inter alia*, requirements that the arbitrator must be impartial and this impartiality requirement holds true even in the situation of a "party arbitrator."  

However, there is no requirement that the ADR provider selected by the parties proffer a panel of potential arbitrators that features gender, racial, or ethnic diversity as would be mandated for a jury panel in court. In addition, the parties can agree that the arbitrator(s) shall have special expertise with respect to the subject matter of the dispute or the process itself (e.g., complex litigation).

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40. 280 F.3d 1266 (9th Cir. 2002).
41. *Id.* at 1269.
42. *Id.* at 1270. Ordinarily, the FAA applies in both federal and state courts. A *LITIGATOR'S GUIDE TO EFFECTIVE USE OF ADR IN CALIFORNIA* 387, § 9.35 (2006). However, not everyone agrees with this interpretation. *E.g.*, Green Tree Fin. Corp. v. Bazzle, 539 U.S. 444, 460 (2003) (Thomas, J., dissenting) (citing other cases in which he has dissented on the same point).
44. *See infra* notes 45.
45. Traditionally, party arbitrators were assumed to not be neutral. *E.g.*, Sunkist Soft Drinks, Inc. v. Sunkist Growers, Inc., 10 F.3d 753, 758-60 (11th Cir. 1993). However, the current trend is that all arbitrators, "party" or not, shall be impartial. *See AAA COMMERCIAL RULES AND MEDIATION PROCEDURES*, R. R-17(a)(iii) (2007).
46. Smith v. Am. Arbitration Ass'n, 233 F.3d 502, 504-07 (7th Cir. 2000). This case is analyzed *infra* Part VI.A.2.
C. Arbitration's Policy of Finality

Perhaps the main characteristic of arbitration is that, except for very limited circumstances, the arbitrator's award is not subject to review by the courts as to errors of law or fact. For instance, a recent United States Supreme Court case stated, "When an arbitrator resolves disputes regarding the application of a contract, and no dishonesty is alleged, the arbitrator's 'improvident, even silly, fact-finding' does not provide a basis for a reviewing court to refuse to enforce the award."49

Furthermore, while many arbitration agreements specify that the arbitral award shall be final and binding, this policy of finality is implied in arbitration even if the arbitration agreement is silent on the point. As the California Supreme Court put it:

Even had there been no such expression of intent [that the award be final], however, it is the general rule that parties to a private arbitration impliedly agree that the arbitrator's decision will be both binding and final. Indeed, "The very essence of the term 'arbitration' [in this context] connotes a binding award." In the early years of this state, this court opined that, "When parties agree to leave their dispute to an arbitrator, they are presumed to know that his award will be final and conclusive... ." One commentator explains, "Even in the absence of an explicit agreement, conclusiveness is expected; the essence of the arbitration process is that an arbitral award shall put the dispute to rest."50

In accordance with these policies, statutes governing judicial review of an arbitration award specify only limited conditions under which an award can be vacated. For example, the FAA provides grounds for vacatur based on procedural improprieties such as corruption, fraud, or arbitrators who exceed their powers.51

48. Major League Baseball Players Ass'n v. Garvey, 532 U.S. 504, 509 (2001). See IBEW Local No. 573 v. Steen Elec., Inc., 232 F. Supp. 2d 797, 802 (N.D. Ohio 2002) ("It is the arbitrator's construction [of the parties' contract] which was bargained for; and so far as the arbitrator's decision concerns construction of the contract, the courts have no business overruling him because their interpretation of the contract is different from his."). City of Coffeyville v. IBEW, Local No. 1523, 14 P.3d 1, 9 (Kan. 2000) ("The court has a very limited scope of review when considering whether to set aside an arbitrator's decision.").

49. Garvey, 532 U.S. at 509. The Second Circuit case of Wallace v. Buttar provided this illuminating observation:
This case raises questions regarding the scope of federal court review of a decision issued by an arbitral panel. . . . Federal district judges are, of course, highly skilled in matters of weighing evidence. As illustrated by the result we reach here [reversal of the vacatur of the arbitration award and remand for the purpose of entering an order confirming the award], however, district judges must put these skills aside when faced with the question of whether a decision issued by an arbitral panel should be confirmed.


51. 9 U.S.C. §10(a) (2000). These limited avenues for judicial review of arbitration awards are typically repeated in state arbitration statutes. E.g., ALASKA STAT. § 09.43.120 (2006). Alaska is one of the thirty-four states that have adopted the Uniform Arbitration Act. 27 AM. JUR. 3D Proof of Facts 103 § 2 & n.9 (2005). However, even states which have not adopted the UAA have very similar sta-
A host of cases recite that the statutory grounds are the sole grounds for judicial review in accordance with the general rule of arbitral finality. However, many federal and state courts also permit some non-statutory grounds for vacating an arbitration award, such as manifest disregard of law, violation of public policy, or the parties’ agreement to expand the grounds of judicial review beyond the statutory grounds.

D. Closing Remarks as to Arbitration

In reviewing the cases cited above, it appears that any attempt to define arbitration could easily be summarized in the famous words of Justice Potter Stewart: “I know it when I see it.” However, the cases reveal a few important characteristics: arbitration is a private procedure intended to result in a final decision rendered by a neutral tribunal with no appeal due to an error of law or fact, with an emphasis on the finality of the arbitral decision.
III. "STATE ACTION" DEFINED

The concept of "state action" is vital to the question of whether a violation of the United States Constitution has occurred. This is because a cause of action based on a violation of the Constitution must be a result of state action in order for the claim to be valid due to the "essential dichotomy set forth in the Fourteenth Amendment between deprivation by the State, subject to scrutiny under its provisions, and private conduct, 'however discriminatory or wrongful,' against which the Fourteenth Amendment offers no shield."58

The state action doctrine has been subject to a number of different interpretations over the years.59 The discussion of the following United States Supreme Court cases will show how troublesome this area of the law can be.60

A. Tarkanian v. NCAA—The NCAA is Not a State Actor and Thus it is Not Subject to Due Process Restrictions

The Tarkanian case featured disciplinary action taken by the National Collegiate Athletic Association (NCAA) against a state university, the University of Nevada, Las Vegas ("UNLV"), as well as its coach, Jerry Tarkanian61, based on numerous violations of the NCAA's rules. In particular, the NCAA put UNLV's basketball team on probation and ordered the school to show why further penalties should not be imposed, unless it severed all ties between its athletic program and Tarkanian during the probationary period.62 When UNLV accordingly notified Tarkanian that it planned to suspend him, Tarkanian filed suit in Nevada state court, alleging deprivation of his Fourteenth Amendment Due Process rights in violation of 42 U.S.C. § 1983.63

56. 57. Or, for that matter, a claim pursuant to 42 U.S.C. § 1983 (2000). Lugar v. Edmondson Oil Co., 457 U.S. 922, 928-29 (1982) ("In cases under § 1983, 'under color' of law has consistently been treated as the same action as 'state action' required under the Fourteenth Amendment.").
58. 59. Jackson v. Metro. Edison Co., 419 U.S. 345, 349 (1974). While Jackson dealt with an alleged Due Process violation, it should be noted that cases involving violations of other Constitutional provisions, such as Equal Protection, also invoke the state action requirement. B.E. WITKIN ET AL., 8 SUMMARY OF CALIFORNIA LAW, "CONSTITUTIONAL LAW," 70, § 697 (10th ed. 2005) ("Like the Due Process Clause, the Equal Protection Clause applies only to state action, and not to private discrimination.").
60. 61. Sarah Rudolph Cole, Fairness in Securities Arbitration: A Constitutional Mandate?, 26 Pace L. Rev. 73, 84-85 (2005) (providing brief descriptions of the four standards used for determining whether there is state action).
62. 63. See Jackson, 419 U.S. at 349-50 ("[T]he question whether particular conduct is 'private,' on the one hand, or 'state action,' on the other, frequently admits of no easy answer."); Rudolph Cole, supra note 59, at 84 ("While the theory underlying state action is well-understood, determining whether an individual is a state actor when she allegedly violates constitutional rights is not easily predictable.").
61. 62. Tarkanian won 729 games as a Division I college coach (including 509 victories at UNLV), and on August 8, 2005, UNLV announced that it was naming the basketball court at the school's arena, Thomas & Mack Center, in honor of Tarkanian. UNLV to Honor Coach Jerry Tarkanian, http://unlvrebels.collegesports.com/sports/m-baskbl/spec-rel/080805aab.html (last visited March 8, 2006).
Tarkanian prevailed in the state courts, obtaining injunctive relief and an award of attorney’s fees against both UNLV and the NCAA on the grounds that Tarkanian’s suspension was state action that was prohibited by the Fourteenth Amendment and therefore in violation of § 1983. The United States Supreme Court granted certiorari to review the state action holding as to the NCAA and ruled that the NCAA was not a state actor.

Litigation to enjoin Tarkanian’s suspension on Due Process grounds proceeded through the Nevada state court system, and the Nevada Supreme Court ultimately affirmed the trial court’s decision that the NCAA’s conduct constituted state action for the purposes of Tarkanian’s Due Process allegations.

Tarkanian argued that the NCAA was a state actor due to its misuse of power possessed by virtue of state law, alleging that UNLV delegated its functions to the NCAA. The United States Supreme Court rejected that argument.

The Tarkanian court dubbed the situation a “mirror image” of the typical state action case and stated the question as “whether UNLV’s actions in compliance with the NCAA rules and recommendations turned the NCAA’s conduct into state action.” The Court first pointed out that UNLV was just one of many institutions that belonged to the NCAA and, since the vast majority of those institutions were located outside of the State of Nevada, these institutions “did not act under color of Nevada law.” Therefore, the source of the NCAA’s rules “is not Nevada but the collective membership, speaking through an organization that is independent of any particular State.”

The Supreme Court conceded that state action could result if UNLV transformed the NCAA’s rules into state rules and the NCAA into a state actor.

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64. Tarkanian, 488 U.S. at 181-82.
65. Id. at 182. The question of whether the NCAA could be a state actor had been decided by a number of lower courts, with more recent cases holding that the NCAA was not a state actor. Id. at n. 5 (collecting cases); but see Brentwood Acad. v. Tenn. Secondary Sch. Athletic Ass’n, 531 U.S. 288, 294 n.1 (2001) (citing recent cases ruling that private organizations in charge of state high school athletics were state actors). There was no dispute that UNLV, as a public university, was a state actor that engaged in state action when it suspended Tarkanian. Tarkanian, 488 U.S. at 183; see also id. at 199 (White, J., dissenting) (“All agree that UNLV, a public university, is a state actor, and that the suspension of Jerry Tarkanian, a public employee, was state action. The question here is whether the NCAA acted jointly with UNLV in suspending Tarkanian and thereby also became a state actor.”).
66. Tarkanian, 488 U.S. at 189. The Nevada Supreme Court further affirmed the trial court’s holding that Tarkanian’s Due Process rights had been violated by the NCAA, reduced the award of attorney’s fees awarded by the trial court, and later awarded additional fees based on the appeal. Id. at 188-89 & n.10. UNLV, which was also a defendant, did not appeal from the trial court’s order that it pay 10% of the attorney’s fees awarded to Tarkanian by the trial court. Id. at 189.
67. Id. at 191-92. Specifically, Tarkanian claimed that this delegation by UNLV “cloth[e]d the [NCAA] with authority both to adopt rules governing UNLV’s athletic programs and to enforce those rules on behalf of UNLV.” and the Nevada Supreme Court reasoned that UNLV and the NCAA “acted jointly to deprive Tarkanian of liberty and property interests, making the NCAA as well as UNLV a state actor.” Id. at 192.
68. Id.
69. Id. at 192-93.
70. Id. at 193-94.
71. Id. In what could be considered a prophecy of the Court’s holding in the Brentwood Academy case fifteen years later, the Tarkanian Court stated in a footnote that “[t]he situation of course would be different if the membership consisted entirely of institutions located within the same State, many of them public institutions created by the same sovereign.” Id. at 194 n.13.
72. Id. at 194.
However, the Court then noted that "[n]either UNLV's decision to adopt the NCAA's standards nor its minor role in their formulation is a sufficient reason for concluding that the NCAA was acting under color of Nevada law when it promulgated standards governing athlete recruitment, eligibility, and academic performance."\(^{73}\)

The Court declined to adopt Tarkanian's assertion that there was state action by the NCAA due to delegation of power by UNLV, noting that the school had not given the NCAA any power to do anything regarding Tarkanian (or any other employee); instead, "[t]he commitment by UNLV to adhere to NCAA enforcement procedures was enforceable only by sanctions that the NCAA might impose on UNLV itself."\(^{74}\)

Likewise, the Court rejected Tarkanian's argument that UNLV's promise to cooperate in the NCAA's enforcement proceedings created a partnership or transfer of certain university powers to the NCAA, noting that "the NCAA and UNLV acted much more like adversaries than like partners" as UNLV sought to retain its highly successful basketball coach.\(^{75}\) Moreover, the NCAA had no traditional prosecutorial powers—such as the ability to subpoena witnesses or impose contempt sanctions—in pursuing its enforcement action against UNLV; rather, "[i]t's greatest authority was to threaten sanctions against UNLV."\(^{76}\) In particular, the NCAA could not, and did not, directly discipline Tarkanian since its "show cause" order gave UNLV options other than suspending the coach.\(^{77}\)

The Supreme Court dealt with Tarkanian's last contention as follows:

Finally, Tarkanian argues that the power of the NCAA is so great that the UNLV had no practical alternative to compliance with its demands. We are not at all sure this is true, but even if we assume that a private monopolist can impose its will on a state agency by a threatened refusal to deal with it, it does not follow that such a private party is therefore acting under color of state law.\(^{78}\)

In a final note, the majority opinion cited the irony that would occur if the NCAA's sanctions against UNLV—which were contested by UNLV and its counsel, including the Nevada state attorney general—were attributed to the State of Nevada.\(^{79}\)

\(^{73}\) *Id.* at 195.

\(^{74}\) *Id.* at 195-96.

\(^{75}\) *Id.* at 196.

\(^{76}\) *Id.* at 197.

\(^{77}\) *Id.* at 197-98.

\(^{78}\) *Id.* at 198-99 (footnote omitted). This attractive argument was acknowledged by the Court when it said that "[UNLV]'s desire to remain a powerhouse among the Nation's college basketball teams is understandable, and nonmembership in the NCAA obviously would thwart that goal." *Id.* at 198 n.19.

\(^{79}\) *Id.* at 199. In dissent, Justice White wrote that the NCAA was a state actor since it acted jointly with UNLV, which was undisputedly a state actor. *Id.* (White, J., dissenting). The dissent concluded: Had UNLV refused to suspend Tarkanian, and the NCAA responded by imposing sanctions against UNLV, it would be hard indeed to find any state action that harmed Tarkanian. But that is not this case. Here, UNLV did suspend Tarkanian, and it did so because it embraced the NCAA rules governing conduct of its athletic program and adopted the results of the hearings conducted by the NCAA concerning Tarkanian, as it had agreed that it would. Under these facts, I would find that the NCAA acted jointly with UNLV and therefore is a state actor.
The Court's opinion was well reasoned but it did not recognize the reality that the NCAA's control over intercollegiate athletics is overwhelming. Simply put, the vast majority of all top athletes go to colleges and universities with leading sports programs, and these schools are NCAA members. Therefore, the NCAA has a monopoly over the college sports scene. This monopoly, coupled with the prevalent membership of state universities, creates at least the appearance that the NCAA is some sort of public agency instead of a purely private enterprise.

B. Shelley v. Kraemer—A Court is a State Actor in a Fourteenth Amendment Case Involving Race Discrimination

In Shelley v. Kraemer, the United States Supreme Court was presented with the question of whether court enforcement of private restrictive covenants as to real property which discriminated on the basis of race or color infringed on their Fourteenth Amendment rights. The Court observed that the restrictive covenants were private agreements and the "[p]articipation of the State consists in the enforcement of the restrictions so defined." In other words, there would be no state action if there were voluntary compliance with the restrictive covenants. The issue then became whether the cases before the Court—all of which involved scenarios where the purposes of the restrictive covenants were secured only by judicial enforcement—involved state action.

The Supreme Court began its analysis by stating it has long been established that judicial action was state action for the purposes of the Fourteenth Amendment. The Court then held that judicial enforcement of the restrictive covenants was state action for three reasons. First, except for "the active intervention of the state courts," the plaintiffs could have occupied the properties otherwise subject to the restrictive covenants. Second, the "full coercive power of government" was made available by the states to individuals to deny others, based on race or color, the enjoyment of property rights. Third, the Court stated:

The enforcement of the restrictive agreements by the state courts in these cases was directed pursuant to the common-law policy of the States as formulated by those courts in earlier decisions. . . . The judicial action in each case bears the clear and unmistakable imprimatur of the State. . . .

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Id. at 203 (White, J., dissenting).
80. 334 U.S. 1 (1948).
81. Id. at 8. The restrictive covenants in question were agreements signed by most or all residents of a certain section of a street by which they agreed not to sell to or permit occupation by other than "those of the Caucasian race." Id. at 6. Therefore, if an owner of land subject to one of these restrictive covenants attempted to sell his or her property to a non-White person, one or more of the other parties to the covenant could file suit to enjoin the buyer from taking possession and to divest the buyer of title and revest title in the seller or another person directed by the court, which is what happened in the cases that gave rise to Shelley v. Kraemer. Id. at 6-8.
82. Id. at 13.
83. Id.
84. Id. at 13-14.
85. Id. at 14.
86. Id. at 19.
87. Id.
Nor is the Amendment ineffective simply because the particular pattern of discrimination, which the State has enforced, was defined initially by the terms of a private agreement. State action, as that phrase is understood for the purposes of the Fourteenth Amendment, refers to exertions of state power in all forms.\footnote{Id. at 19-20 (footnotes omitted).}

In Shelley v. Kraemer, the subject contracts were all private agreements that could have been performed without any state involvement. The state entered the picture only when parties to the restrictive covenants filed suit to enjoin the buyers from taking possession of the properties that had ostensibly been sold to them.

On its face, this scenario is very similar to a situation where, pursuant to an arbitration agreement, arbitration takes place and the arbitrator renders an award of punitive damages, and then one of the parties challenges the award in court by arguing that the award is invalid under the Fourteenth Amendment.

\section*{C. Closing Remarks as to State Action}

The Tarkanian case is illustrative of the typical dispute over the existence of state action—i.e., action by a private actor that could be interpreted to be a public function. In Tarkanian, the party bringing the Due Process challenges tried to emphasize the relationship—as memorialized by contract between the state and private actors—in order to show that the private actor’s conduct constituted state action.

On the other hand, Shelley v. Kraemer featured private agreements—the restrictive covenants—that had nothing to do with the state until one of the contracting parties wished to force compliance by another contracting party who was transferring the property to a non-White person. When this forced compliance was required, it was undertaken by filing suit in a state court. According to Shelley v. Kraemer, the court’s enforcement of the restrictive covenant was state action, which permitted application of Due Process strictures. Therefore, the analytical structure set forth in Shelley v. Kraemer would indicate that any private contract, including an arbitration agreement, could involve state action whenever judicial intervention is requested with respect to the contract.

However, the analysis is not that simple. This is because the holding of Shelley v. Kraemer has been limited to race discrimination cases. For instance, the case of Davis v. Prudential Securities, Inc.\footnote{59 F.3d 1186 (11th Cir. 1995).} disregarded the impact of Shelley v. Kraemer, stating on the grounds that “[t]he holding of Shelley, however, has not been extended beyond the context of race discrimination.”\footnote{Id. at 1191. A recent law review article expanded on this criticism of Shelley v. Kraemer, noting: Many commentators worried about Shelley’s possible implications. According to some, Shelley could be interpreted to create state action in any contract dispute that resulted in court involvement. Concerns over Shelley’s implications never materialized, however. The Court, perhaps concerned about the loss of the critical dichotomy between public and private law and the constitutionalization of contract law, has rejected the invitation to extend Shelley. Since Shelley, no other case has found state action solely on the basis that the court enforced an otherwise private arrangement. \cite{1191} Commentators have, however, exaggerated Shelley’s influence. If the contract did not involve issues of race, it was treated as private.}
Thus, the availability of *Shelley v. Kraemer* as precedent in support of the argument that judicial confirmation of an arbitral award is state action is, at best, weak and, at worst, nonexistent.

**IV. DUE PROCESS LIMITS ON AWARDS OF PUNITIVE DAMAGES**

**A. The United States Supreme Court's Jurisprudence as to Constitutional Limits on Punitive Damages**

The United States Supreme Court’s recent jurisprudence as to the issue of excessive punitive damages has involved constitutional challenges to verdicts including punitive damages on the grounds that such verdicts violated the Excessive Fines Clause of the Eighth Amendment and, more currently, the Fourteenth Amendment’s Due Process Clause.

The Court addressed the Eighth Amendment issue in the case of *Browning-Ferris Industries of Vermont v. Kelco Disposal, Inc.*, in which the trial court awarded approximately four hundred thousand dollars in compensatory and treble damages, attorney’s fees and costs, and just over six million dollars in punitive damages. The Court’s opinion was pertinent for two reasons.

First, the Court held that the Eighth Amendment did not apply to punitive damages, reasoning that the Excessive Fines Clause pertains only to criminal matters prosecuted by the government and does not “serve] as a check on the power of a jury to award damages in a civil case” between private parties. Second, the Court declined to reach the Due Process issue raised by the defendants on the grounds that they had not raised it before the District Court or Court of Appeals, nor did they raise it in their petition for writ of certiorari. However, the Court did acknowledge:

There is some authority in our opinions for the view that the Due Process Clause places outer limits on the size of a civil damages award made pursuant to a statutory scheme [citation omitted], but we have never addressed the precise question presented here: whether due process acts as

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the Court enforced in *Shelley* had not been racially restrictive on its face, the argument that applying *Shelley* in subsequent cases would constitutionalize contracts might be viable. Moreover, *Shelley* is an unusual case that will not likely be repeated. The Court’s decision turned on the fact that the lower court had to look at the color of *Shelley*’s skin in order to determine whether to enforce the contract. Without race as a factor, the enforcement of a facially neutral covenant would not have been state action. *The Court's refusal to extend Shelley has resulted in reluctance to find state action, even in comparable situations where race discrimination is a consequence of the private litigants' behavior.*


This article is discussed *infra* Part VI.B.1.

92. *Id.* at 262.
93. *Id.* at 259-60.
94. *Id.* at 277.
a check on undue jury discretion to award punitive damages in the absence of any express statutory limit.\textsuperscript{95}

Therefore, the Court declined to permit an Eighth Amendment attack on a punitive damages award in a civil case because the Eighth Amendment applied to criminal matters only. However, it left the door open for a Due Process attack, and that invitation was quickly accepted, as shown by the following cases.

In \textit{Pacific Mutual Life Ins. Co. v. Haslip},\textsuperscript{96} the Court took up the issue that the \textit{Browning-Ferris} case declined to address—i.e., whether an award of punitive damages could violate Due Process. In \textit{Pacific Mutual}, the verdict was in the amount of $1,040,000, with "a punitive damages component of not less than $840,000.00."\textsuperscript{97} The Court affirmed the punitive damages award by first approving the jury instruction given at trial based on "deterrence and retribution, the state policy concerns sought to be advanced."\textsuperscript{98} Next, the Court recognized the efficacy of the post-trial review procedure.\textsuperscript{99} Finally, the state supreme court provided an additional check by undertaking a comparative analysis as well as evaluating punitive damages under a detailed seven-part standard.\textsuperscript{100}

Based on the variety of checks under which the punitive damages award was reviewed by the lower courts in \textit{Pacific Mutual}, the Court held that no "constitutional impropriety" occurred and thus the Due Process challenge was rejected.\textsuperscript{101} However, the Court did not establish any mathematical criteria by which to measure punitive damages.\textsuperscript{102}

In \textit{Honda Motor Co., Ltd. v. Oberg},\textsuperscript{103} the plaintiff won a jury verdict in an Oregon state court for compensatory damages of $735,512.31 and punitive dam-

\textsuperscript{95} \textit{Id.} at 276-77. Justice Brennan, in a concurring opinion, underscored the efficacy of a Due Process attack on a punitive damages award, noting "that punitive damages are imposed by juries guided by little more than an admonition to do what they think is best." \textit{Id.} at 281 (Brennan, J., concurring). Two other justices sued the "skyrocketing" awards of punitive damages. \textit{Id.} at 282 (O'Connor, J., concurring and dissenting).

\textsuperscript{96} 499 U.S. 1 (1991).

\textsuperscript{97} \textit{Id.} at 6-7 & n.2. The Court observed that the punitive damage award is "more than 4 times the amount of compensatory damages, is more than 200 times the out-of-pocket expenses . . . and, of course, is much in excess of the fine that could be imposed for insurance fraud. . . . Imprisonment, however, could also be required of an individual in the criminal context." \textit{Id.} at 23.

\textsuperscript{98} \textit{Id.} at 19. The text of the jury instruction is set forth in a lengthy footnote. \textit{Id.} at 6 & n.1.

\textsuperscript{99} The trial court was obligated to consider several matters when reviewing an award of punitive damages including but not limited to the "culpability of the defendant's conduct," the "desirability of discouraging others from similar conduct," the 'impact upon the parties,' and 'other factors, such as the impact on third parties.'" \textit{Id.} at 20.

\textsuperscript{100} \textit{Id.} at 21-22.

\textsuperscript{101} \textit{Id.} at 23-24. In an extended discussion, Justice Scalia averred that the "traditional practice of American courts" was to leave the amount of punitive damages to the jury's discretion and therefore he would not inquire into the "fairness" or "reasonableness" of the procedure for determining the amount of punitive damages. \textit{Id.} at 24-25 (Scalia, J., concurring). Justice Kennedy, while writing separately, relied heavily on the concept that "[j]ury determination of punitive damages has . . . [a] long and principled recognition as a central part of our system. . . .' \textit{Id.} at 40 (Kennedy, J., concurring). The dissent lamented that the jury was provided with discretion without direction in setting the amount of punitive damages; the jury instructions regarding punitive damages "are so fraught with uncertainty that they defy rational implementation." \textit{Id.} at 43 (O'Connor, J., dissenting).

\textsuperscript{102} \textit{Id.} at 18 ("We need not, and indeed we cannot, draw a mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable that would fit every case.").

\textsuperscript{103} 512 U.S. 415 (1994).
ages of $5,000,000.00.\textsuperscript{104} The defendant appealed through the state court system, unsuccessfully asserting that the amount of punitive damages was excessive, and the Oregon Constitution prohibited judicial review of a jury verdict as to the amount of punitive damages.\textsuperscript{105} The United States Supreme Court granted certiorari "to consider whether Oregon's limited judicial review of the size of punitive damages awards is consistent with our decision in Haslip."\textsuperscript{106}

The Court noted that the Oregon procedure permitted a new trial to be granted as to whether there was any evidentiary support for punitive damages but that no judicial review existed if the amount of punitive damages were the only issue.\textsuperscript{107} The defendant unconvincingly argued that the Oregon courts did have the power to reduce the amount of an award of punitive damages on the grounds that the jury was influenced by "passion and prejudice" since "[n]o Oregon court for more than half a century has inferred passion and prejudice from the size of a [punitive] damages award, and no court in more than a decade has even hinted that courts might possess the power to do so."\textsuperscript{108}

The Supreme Court held that judicial review of punitive damages provided a protection against arbitrary awards and that Oregon's deprivation of any such judicial review violated Due Process.\textsuperscript{109} Thus, the Supreme Court imposed a procedural limitation—i.e., the availability of judicial review of the amount of the punitive damages—in Honda. However, the Court did not create a substantive limitation on punitive damages.

Eventually, in State Farm Mutual Automobile Ins. Co. v. Campbell,\textsuperscript{110} the United States Supreme Court created a mathematical formula for limiting punitive damages. The State Farm case involved a matter in which the jury rendered a verdict of $1 million in compensatory damages and $145 million in punitive damages.\textsuperscript{111} The Court held that the jury's $145 million punitive damages award violated Due Process.\textsuperscript{112} The following analysis will concentrate on the part of the Court's analysis regarding the disparity—or ratio—between the plaintiff's actual or potential harm and the amount of punitive damages.

The Court rejected the imposition of a "bright-line ratio" for placing a limit on the amount of punitive damages,\textsuperscript{113} but it endorsed a single-digit ratio between punitive and compensatory damages, stating:

\textsuperscript{104} Id. at 418.
\textsuperscript{105} Id. Specifically, the Oregon Constitution prohibited judicial review of such a jury verdict "unless the court can affirmatively say there is no evidence to support the verdict." Id. at 418.
\textsuperscript{106} Id. at 420.
\textsuperscript{107} Id. at 426-27. Moreover, "[e]very other State in the Union affords postverdict judicial review of the amount of a punitive damages award." Id. at 427-28.
\textsuperscript{108} Id. at 428.
\textsuperscript{109} Id. at 432.
\textsuperscript{110} 538 U.S. 408 (2003).
\textsuperscript{111} Id. at 412. The determination of the amount of the verdict took an interesting path that need not be recounted here in detail. Suffice it to say that (1) the jury's verdict was $2.6 million in compensatory damages and $145 million in punitive damages, (2) the trial judge reduced the verdict to $1 million in compensatory damages and $25 million in punitive damages, and (3) the Utah Supreme Court reinstated the punitive damages award of $145 million. Id. at 415.
\textsuperscript{112} Id. at 418.
\textsuperscript{113} Id. at 425.
Our jurisprudence and the principles it has now established demonstrate, however, that, in practice, few awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process. In Haslip, in upholding a punitive damages award, we concluded that an award of more than four times the amount of compensatory damages might be close to the line of constitutional impropriety. 499 U.S., at 23-24. We cited that 4-to-1 ratio again in Gore. 517 U.S., at 581. The Court further referenced a long legislative history, dating back over 700 years and going forward to today, providing for sanctions of double, treble, or quadruple damages to deter and punish. Id., at 581, and n. 33. While these ratios are not binding, they are instructive. They demonstrate what should be obvious: Single-digit multipliers are more likely to comport with due process, while still achieving the State's goals of deterrence and retribution, than awards with ratios in range of 500 to 1, id., at 582, or, in this case, of 145 to 1. 114

The Court opined that, in this case, the presumption was against a verdict featuring punitive damages that were 145 times greater than the compensatory damages. 115 The Court provided a number of reasons in support of this presumption including, the substantial nature of the award of compensatory damages, the purely economic nature of the case (with no physical injuries), the inclusion of emotional distress damages in the award of compensatory damages that should not be duplicated in the award of punitive damages, the irrelevance of a $100 million punitive damages award in another state in a dissimilar case, and the notion that the defendant's wealth could not justify an otherwise unconstitutional award of punitive damages. 116

Therefore, according to the State Farm case, the amount of punitive damages should be less than ten times the amount of compensatory damages.

B. Closing Remarks as to the Determination of the Amount of Punitive Damages

The United States Supreme Court has addressed an important issue: how to determine the amount of punitive damages in a way that provides some certainty but still gives lower courts the discretion to award punitive damages in an amount greater than the single-digit ratio scheme approved in State Farm. The bottom line is that this judicially established ratio still affords plaintiffs the possibility of obtaining substantial monies in addition to their being fully compensated for all tangible and intangible losses.

114. Id. (emphasis added).
115. Id. at 426.
116. Id. at 426-28.
V. WHEN PUNITIVE DAMAGES ARE AVAILABLE IN ARBITRATION

In Mastrobuono v. Shearson Lehman Hutton, Inc., the United States Supreme Court ruled that arbitrators can award punitive damages when the parties' arbitration agreement provides for them. In accordance with the holding of Mastrobuono specifically as well as the FAA's general policy of the enforceability of arbitration agreements, the courts have often construed arbitration agreements so as to allow arbitral awards of punitive damages.

A. Mastrobuono v. Shearson Lehman Hutton, Inc.—An Arbitral Award Can Include Punitive Damages if Permitted by the Parties' Arbitration Agreement

In Mastrobuono, the parties proceeded to arbitration before the National Association of Securities Dealers (NASD) pursuant to a contract that included an arbitration agreement as well as a choice of law clause providing that the contract "shall be governed by the laws of the State of New York." The arbitration award contained compensatory and punitive damages in favor of the petitioners. The respondents, who claimed at the arbitration that arbitrators could not award punitive damages under New York law, paid the compensatory damages but made a motion to vacate the award as to the punitive damages. The district court granted the motion to vacate and the Seventh Circuit affirmed, relying on the choice of law clause and a decision by the New York Court of Appeals barring arbitrators from awarding punitive damages. The United States Supreme Court granted certiorari due to a split in the federal circuits "on whether a contractual choice-of-law provision may preclude an arbitral award of punitive damages that otherwise would be proper" and reversed the lower courts' decisions.

The Mastrobuono Court first held that punitive damages could be available in arbitration so long as the parties' arbitration agreement provided therefor, concluding:

[W]e think our decisions in Allied-Bruce, Southland, and Perry make clear that if contracting parties agree to include claims for punitive damages within the issues to be arbitrated, the FAA ensures that their agreement will be enforced according to its terms even if a rule of state law would otherwise exclude such claims from arbitration. Thus, the case before us comes down to what the contract has to say about the arbitrability of petitioners' claim for punitive damages.

The Court then needed to reconcile two apparently conflicting contractual provisions: first, a general choice-of-law clause designating New York law as

118. Id. at 53-54.
119. Id. at 54.
120. Id.
121. Id. at 54-55 (citing Garrity v. Lyle Stuart, Inc., 386 N.Y.S.2d 831 (1976)).
122. Id. at 55.
123. Id. at 58.
governing the contract; second, an agreement to arbitrate "in accordance with the rules then in effect, of the National Association of Securities Dealers, Inc. or the Boards of Directors of the New York Stock Exchange, Inc. and/or the American Stock Exchange Inc. as [the petitioners] may elect."\textsuperscript{124}

The Court held that choice-of-law clause was "reasonably [to] be read as merely a substitute for the conflict-of-laws analysis that otherwise would determine what law to apply to disputes arising out of the contractual relationship."\textsuperscript{125} Moreover, the choice-of-law clause could even be read to allow punitive damages in that it "might include only New York’s substantive rights and obligations, and not the State’s allocation of power between alternative tribunals."\textsuperscript{126}

If anything, the arbitration agreement weighed more in favor of permitting an arbitral award of punitive damages since the arbitration agreement authorized proceeding under NASD rules, which allowed arbitrators to award "damages and other relief."\textsuperscript{127} In fact, a manual provided to NASD arbitrators stated in pertinent part that "[p]arties to arbitration are informed that arbitrators can consider punitive damages as a remedy."\textsuperscript{128}

The Court rejected the argument that, read together, the choice-of-law clause and the arbitration agreement expressed intent to preclude punitive damages by noting that the choice-of-law clause created an ambiguity as to whether the arbitration agreement would otherwise allow punitive damages.\textsuperscript{129} Instead, the Court asserted that "ambiguities as to the scope of the arbitration clause itself [must be] resolved in favor of arbitration."\textsuperscript{130}

Finally, the Supreme Court relied on two established rules of contract interpretation in support of its ruling that punitive damages were available under the subject contract. First, the Court reasoned that any ambiguity had to be interpreted against the drafting party. Second, "a document should be read to give effect to all its provisions and to render them consistent with each other."\textsuperscript{131} The Court stated:

We think the best way to harmonize the choice-of-law provision with the arbitration provision is to read "the laws of the State of New York" to encompass substantive principles that New York courts would apply, but not to include special rules limiting the authority of arbitrators. \textit{Thus, the choice-of-law provision covers the rights and duties of the parties, while the arbitration clause covers arbitration; neither sentence intrudes upon the other}. In contrast, respondents’ reading sets up the two clauses in

\begin{itemize}
\item \textsuperscript{124} \textit{Id.} at 58-59 & n.2.
\item \textsuperscript{125} \textit{Id.} at 59.
\item \textsuperscript{126} \textit{Id.} at 60.
\item \textsuperscript{127} \textit{Id.} at 60-61.
\item \textsuperscript{128} \textit{Id.} at 61.
\item \textsuperscript{129} \textit{Id.} at 62.
\item \textsuperscript{130} \textit{Id.}
\item \textsuperscript{131} \textit{Id.} at 63.
\end{itemize}
conflict with one another: one foreclosing punitive damages, the other allowing them. This interpretation is untenable.132

It follows that the Mastrobuono case simply complied with the line of United States Supreme Court authorities which have declared that "the central purpose of the FAA [is] to ensure 'that private agreements to arbitrate are enforced according to their terms.'"133 Furthermore, the Court could have further supported its ruling based on the maxim of jurisprudence that says "[p]articular expressions qualify those which are general"134 in coming to the same conclusion in that the particular designation of NASD rules permitting punitive damages in the arbitration agreement would control in the face of the more general choice-of-law clause purporting to govern the entire contract.135

B. Post-Mastrobuono Jurisprudence Relating to Arbitration Awards of Punitive and Other Extra-Compensatory Damages

Cases decided after Mastrobuono have reflected the courts’ willingness to permit arbitral awards to include punitive damages. A leading reason justifying confirmation of an arbitration award of punitive damages is that the parties’ arbitration agreement designates a certain state’s law as governing the proceeding and that state’s law allows punitive damages for the matter that is the subject of the arbitration.

For instance, the contract in the case of Stark v. Sandberg, Phoenix & von Gontard, P.C.136 featured a provision stating: "To the extent allowed by applicable law, any Claim . . . shall be resolved by binding arbitration in accordance with [the FAA, AAA rules and] . . . this Agreement."137 The contract further provided

132. Id. at 63-64 (emphasis added). The dissent disagreed with the majority’s conclusions that (1) a choice-of-law clause governing the entire contract did not impact the arbitration agreement contained therein; and (2) NASD rules permitted punitive damages. Id. at 64-72 (Thomas, J., dissenting).
133. Id. at 53-54 (citing Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Junior Univ., 489 U.S. 468, 479 (1989)).
134. CAL. CIVIL CODE § 3534 (West 1997).
135. One commentator expressed concerns about arbitral awards of punitive damages in the context of NAFTA arbitration due to the extremely limited opportunity for review, stating: Chapter 11 review also tends to be less accountable because Chapter 11 tribunals are themselves more insulated from review. Whether a Mississippi punitive damages award is excessive is determined in the first instance by the trial judge and ultimately by the Mississippi Supreme Court. Indeed, the U.S. Supreme Court has held that the Due Process Clause requires appellate review of punitive damages awards and that such review must be de novo. The decisions of the Mississippi Supreme Court are in turn reviewable by the U.S. Supreme Court to ensure compliance with the substantive requirements of the Due Process Clause discussed above. Although review by the U.S. Supreme Court itself is rare, the possibility of such review exerts a restraining influence on state courts. Review of NAFTA Chapter 11 decisions is far more limited. A court reviewing a Chapter 11 award may not set it aside if the tribunal misinterpreted the law or misapplied it to the facts but only if the tribunal was improperly constituted or decided matters beyond the scope of the arbitration. This more limited review of Chapter 11 tribunals increases the chances that review by such tribunals will result in errors.
136. 381 F.3d 793 (8th Cir. 2004).
137. Id. at 800.
that Missouri law would be the applicable law.\textsuperscript{138} The Eighth Circuit found that Missouri law did not permit a waiver of punitive damages and, therefore, the district court’s confirmation of the arbitral award of punitive damages was affirmed on appeal.\textsuperscript{139}

The Montana Supreme Court case of Wallace v. Hayes\textsuperscript{140} also purported to follow state law when it held that the arbitral award properly included punitive damages.\textsuperscript{141} However, the Wallace court then indicated that an arbitration award of punitive damages was still reviewable by the court pursuant to any grounds provided by the state statute governing punitive damages since any arbitration award can be vacated if the arbitrator exceeds his or her power.\textsuperscript{142} But, this sort of reasoning runs contrary to the usual jurisprudence pertaining to the “exceeding arbitral powers” standard because an error of law does not mean that the arbitrator exceeded his or her powers.\textsuperscript{143}

Finally, to show that the courts will look to sources other than the parties’ arbitration agreement to support an arbitration award of punitive damages, the case of Rosati v. Bekhor\textsuperscript{144} held that, even in the absence of a formal arbitration agreement, an arbitral award of punitive damages can still be confirmed by the court if both sides to the proceeding request punitive damages.\textsuperscript{145} Thus, it is clear that an arbitration award of punitive damages is proper and will be confirmed by the court so long as the award is justified by the law applicable to the arbitration proceeding.

An interesting twist on the question of whether an arbitrator can award punitive damages occurs when the arbitration agreement expressly prohibits punitive damages but the claimant is requesting an award of some other type of extra-compensatory damages such as treble damages. This was addressed by the United States Supreme Court in the case of PacifiCare Health Systems, Inc. v. Book.\textsuperscript{146}

In PacifiCare, the claimants were physicians (collectively “the physicians”) who had contracted with managed-health-care organizations (collectively “PacifiCare”) to provide health care services to PacifiCare’s insureds.\textsuperscript{147} The physicians alleged violations of the Racketeer Influenced and Corrupt Organizations Act (RICO).\textsuperscript{148} PacifiCare moved to compel arbitration under the subject contracts, and the physicians opposed on the grounds that “because the arbitration provisions

\textsuperscript{138} Id.
\textsuperscript{139} Id. at 800-01.
\textsuperscript{140} 124 P.3d 110 (Mont. 2005).
\textsuperscript{141} Id. at 111, 116.
\textsuperscript{142} Id. at 116.
\textsuperscript{143} E.g., DiRussa v. Dean Witter Reynolds, Inc., 121 F.3d 818, 824 (2d Cir. 1997) (the proper inquiry is the scope of the arbitrator’s power, not whether the arbitrator made the correct decision); Moshonov v. Walsh, 996 P.2d 699, 702 (Cal. 2000) (“[A]rbitrators do not ‘exceed[] their powers’ . . . merely by rendering an erroneous decision on a legal or factual issue, so long as the issue was within the scope of the controversy submitted to the arbitrators.”); In re United Fed’n of Teachers v. Bd. of Educ. of the City Sch. Dist. of the City of N.Y., 801 N.E.2d 827, 834-35 (N.Y. 2003) (arbitral award based on contract interpretation confirmed “even in circumstances where an arbitrator makes errors of law or fact” (emphasis removed)).
\textsuperscript{144} 167 F. Supp. 2d 1340 (M.D. Fla. 2001).
\textsuperscript{145} Id. at 1347.
\textsuperscript{146} 538 U.S. 401 (2003).
\textsuperscript{147} Id. at 402.
\textsuperscript{148} Id.
prohibit an award of punitive damages . . . respondents could not obtain ‘meaningful relief’ in arbitration for their claims under the RICO statute, which authorizes treble damages.\textsuperscript{149} The district court denied the motion to compel arbitration and the Eleventh Circuit affirmed based on the grounds stated by the physicians.\textsuperscript{150}

Upon grant of certiorari, the Supreme Court first determined that the issue of arbitrability was to be decided by the court and not the arbitrator.\textsuperscript{151} The \textit{PacifiCare} Court then cited several precedents which indicated that treble damages were more compensatory or remedial than punitive in nature.\textsuperscript{152} The Court concluded:

In light of our case law’s treatment of statutory treble damages, and given the uncertainty surrounding the parties’ intent with respect to the contractual term “punitive,” the application of the disputed language to respondents’ RICO claims is, to say the least, in doubt. And \textit{Vimar} instructs that we should not, on the basis of “mere speculation” that an arbitrator might interpret these ambiguous agreements in a manner that casts their enforceability into doubt, take upon ourselves the authority to decide the antecedent question of how the ambiguity is to be resolved. In short, since we do not know how the arbitrator will construe the remedial limitations, the questions whether they render the parties’ agreements unenforceable and whether it is for courts or arbitrators to decide enforceability in the first instance are unusually abstract. As in \textit{Vimar}, the proper course is to compel arbitration.\textsuperscript{153}

\textit{PacifiCare} provides a good example of giving the parties what they contracted for—i.e., arbitration according to agreed-upon rules. This is consistent with “the federal policy of favoring arbitration.”\textsuperscript{154} However, the \textit{PacifiCare} Court went further than simply following this policy when it narrowly interpreted the arbitration agreement’s ban on punitive damages so as to allow the physicians to seek the extra-contractual remedy of treble damages. This holding serves notice on parties who include arbitration clauses in their contracts, if they wish to prohibit a particular type of remedy, to specify that remedy as one that the arbitrator may not award. For that matter, parties should be free to permit punitive damages in their arbitration agreements but place limits on the amount thereof.\textsuperscript{155}

\begin{footnotes}
\item[149.] \textit{Id.} at 403.
\item[150.] \textit{Id.}
\item[151.] \textit{Id.} at 404-05. On the other hand, the Court recently held that “a challenge to the validity of the contract as a whole, and not specifically to the arbitration clause, must go the arbitrator.” Buckeye Check Cashing v. Cardegna, Inc., 546 U.S. 440, 449 (2006).
\item[152.] \textit{PacifiCare}, 538 U.S. at 405-06.
\item[153.] \textit{Id.} at 406-07 (footnotes and citation omitted).
\item[155.] See KNIGHT, \textit{supra} note 43, at 8-36, § 8:154 (“mini/max” or “high/low” clauses acceptable in arbitration agreements).
\end{footnotes}
C. Closing Remarks as to the Availability of Punitive Damages in Arbitration

The Mastrobuono case and its progeny make it clear that an arbitrator can award punitive damages so long as the parties’ arbitration agreement so provides. The cases also make it clear that, in the absence of a contract provision expressly barring punitive damages, an arbitral award of punitive damages is proper. Therefore, parties who wish to negate the possibility of punitive damages in arbitration should include a specific prohibition thereof in their arbitration agreement.

VI. WHETHER A COURT’S CONFIRMATION OF AN ARBITRATION AWARD CONSTITUTES STATE ACTION FOR DUE PROCESS PURPOSES

While Mastrobuono made it clear that an arbitral award can include punitive damages if permitted by the parties’ arbitration agreement, there can still be an issue as to whether punitive damages awarded in arbitration are subject to Due Process limitations. However, for Due Process to be applicable, there must be state action.

The courts have uniformly declined—with two exceptions in dicta only—to accept this Due Process argument on the grounds that there is no state action. On the other hand, the commentators have generally reached the opposite conclusion. The following discussion will analyze some of the cases and articles that have dealt with the issue of whether a court’s confirmation of an arbitrator’s award is the state action required for a claim based on Due Process.

A. Cases on Whether a Court’s Confirmation of an Arbitration Award is State Action for Due Process Purposes

1. Davis v. Prudential Securities, Inc.156—No State Action Due to the Finality of Arbitration and the Inapplicability of Shelley v. Kraemer

In Davis, the parties (Davis and PSI) agreed to have their dispute arbitrated by the American Arbitration Association.157 The arbitration panel rendered an award in favor of Davis for compensatory damages of $483,684 and punitive damages of $300,000, and this award was confirmed by the district court.158

On appeal, PSI asserted that confirmation of the punitive damages award violated Due Process, alleging that “arbitration lacks the procedural protections and meaningful judicial review required for the imposition of punitive damages as required by the United States Supreme Court in the Haslip and Honda cases.”159

The Davis court began its examination of the state action issue by stating that “it is axiomatic that constitutional due process protections ‘do not extend to ‘private conduct abridging individual rights.’”160 The court agreed with the many

156. 59 F.3d 1186 (11th Cir. 1995).
157. Id. at 1187.
158. Id. at 1187-88.
159. Id. at 1188, 1190; see the discussion of these cases supra Part IV.A.
160. Id. at 1190.
courts that have held that Due Process does not apply to private arbitration cases because of the lack of state action, finding that "the arbitration was a private proceeding arranged by a voluntary contractual agreement of the parties . . . [that] did not constitute state action."\(^{161}\)

The Eleventh Circuit then rejected the applicability of *Shelley v. Kraemer* on the grounds that its holding had not been extended to situations other than race discrimination, and the concept of state action had been further limited by the United States Supreme Court.\(^{162}\)

The *Davis* court returned to basic principles of arbitration law in distinguishing the *Honda* case, reasoning that *Honda* involved circumstances in which a jury was given unreviewable discretion to determine punitive damages and that the problems associated with a jury—e.g., bias against a large corporation without a local presence—would not obtain in the case where an arbitrator determined punitive damages.\(^{163}\)

The court also noted the deference given by Congress to arbitrators' expertise as well as the ""federal policy [established by the FAA] favoring arbitration . . . requiring that [courts] rigorously enforce agreements to arbitrate.""\(^{164}\) *Davis* even noted the commentators' prediction that the problem of runaway punitive damages verdicts would be diminished in the arbitral forum.\(^{165}\)

*Davis* also discussed how the United States Supreme Court has upheld the arbitrability of RICO claims which include treble damages\(^ {166}\) and that the Court did not broach the Due Process question in *Mastrobuono* which featured an arbitration award of punitive damages greater than the award in the instant case.\(^ {167}\)

The *Davis* court concluded:

> Finally, we find it significant that PSI was a voluntary participant in the arbitration procedure. As the Supreme Court has stated, ""arbitration under the [Federal Arbitration] Act is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit."" Thus, an agreement to arbitrate is equivalent to voluntarily entering into a contract, the terms of which the parties are free to specify. . . . In this case, we agree that PSI may not require customers to arbitrate under the terms of an account agreement that PSI drafted and later complain about the adequacy of the procedures afforded by the forum of its own choosing.

*In sum, we are persuaded that PSI's due process challenge to the arbitration panel's award of punitive damages must fail. To decide otherwise would constitutionalize private arbitration proceedings and diminish*

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161. *Id.* at 1191.
162. *Id.* at 1191-92.
163. *Id.* at 1192.
164. *Id.* (quoting Shearson/Am. Express, Inc. v. McMahon, 482 U.S. 220, 226 (1987)).
165. *Id.* (citing Stephen J. Ware, Punitive Damages in Arbitration: Contracting Out of Government's Role in Punishment and Federal Preemption of State Law, 63 FORDHAM L. REV. 529, 570 (1994)).
166. *Id.* at 1193 (citing McMahon, 482 U.S. at 240-42).
167. *Id.* (citing Mastrobuono, 514 U.S. 52, 54 (1995)).
both the effectiveness and the appeal of the arbitral forum as an alternative means for resolving disputes.\textsuperscript{168}

Davis provided a thorough analysis of the issues presented in the context of a Due Process challenge to an arbitration award of punitive damages. The court cited the general concepts of arbitration law highlighting the policy of finality. The court also discussed the inefficacy of Shelley v. Kraemer since it has been narrowly applied to race discrimination cases only. In sum, Davis gives us an excellent template of arguments to make in opposing a Due Process challenge to an arbitration award of punitive damages.

2. Smith v. American Arbitration Ass'n\textsuperscript{169}—No State Action to Support an Equal Protection Claim Based on a Private ADR Company's Allegedly Providing a Pool of Arbitrators With Insufficient Gender Diversity

In Smith, the situation was a little different in that the plaintiff challenged the arbitration procedure on the grounds of lack of gender diversity as to the arbitration panel\textsuperscript{170} Specifically, the plaintiff's request for an injunction was denied by the district court, which dismissed the lawsuit for failure to state a claim\textsuperscript{171} The arbitration proceeded and, according to the appellate court, "the arbitrators announced that they would issue their decision shortly."\textsuperscript{172} The Seventh Circuit rebuffed the plaintiff's contention that the Equal Protection Clause of the Fifth Amendment required gender diversity for an arbitration panel, reasoning:

Arbitration is a private self-help remedy. The American Arbitration Association is a private organization selling a private service to private parties who are under no legal obligation to agree to arbitrate their disputes or, if they decide to use arbitration to resolve disputes, to use the services of the Association, which is not the only provider of such services. [Citation omitted.] When arbitrators issue awards, they do so pursuant to the disputants' contract—in fact the award is a supplemental contract obligating the losing party to pay the winner. The fact that the courts enforce these contracts, just as they enforce other contracts, does not convert the contracts into state or federal action and so bring the equal protection clause into play.\textsuperscript{173}

The Smith case showed that the strictures of Equal Protection—whether it is based on an allegation of gender, racial, or some other illicit discrimination—do not apply to arbitration proceedings administered and decided by private parties. This is analogous to the finding of no state action in private party discipline proceedings such as the circumstances in the Tarkanian case analyzed above.

\textsuperscript{168} Davis, 59 F.3d at 1193-94 (citations and footnotes omitted; emphasis added).
\textsuperscript{169} 233 F.3d 502 (7th Cir. 2000).
\textsuperscript{170} Id. at 504 (the panel, drawn from a pool of fourteen men and only one woman provided by defendant American Arbitration Association, was all male).
\textsuperscript{171} Id.
\textsuperscript{172} Id.
\textsuperscript{173} Id. at 507 (emphasis partially added).
However, there was a curious point which was briefly discussed by the Smith court but not necessary to its decision: what would happen if a party to an arbitration agreement challenged a provision therein requiring a certain gender composition of the arbitration panel? The Seventh Circuit commented about this issue:

But we do not suppose that there is anything in the law that would forbid private parties to stipulate to a mode of private dispute resolution that specified a particular gender composition of the tribunal, assuming the arbitrators are not employees of the American Arbitration Association or of some other dispute-resolution agency conducting the arbitration, which might bring Title VII into play.  

This sort of analysis seems to take the fundamentally contractual nature of arbitration to the extreme. In other words, according to Smith, an arbitration service provider is under no obligation to follow any laws—except to avoid vacatur pursuant to the grounds under federal and state law—so long as that provider follows the contractual limitations dictated by the parties. While the parties’ arbitration agreement should be respected, this raises the potential for a court to be in the position of confirming an arbitration award achieved through unusual methods.  


In MedValUSA, the arbitrator awarded the plaintiff no compensatory damages and five million dollars in punitive damages. Finding no state action, the Connecticut Supreme Court rejected the defendant’s contention that the trial court’s confirmation of the arbitration award violated its Due Process rights.  

Because the defendant argued that the award would be unenforceable except for the judicial action, the MedValUSA court devoted most of its analysis to the question of “whether the judicial confirmation of the arbitration award constituted an incident of government authority that uniquely aggravated the defendant’s claimed injury” pursuant to Shelley v. Kramer. The court allowed that “[a]t first glance, judicial confirmation of an arbitration award fits the Shelley pattern perfectly.” After all, without the judicial enforcement of the arbitral award, it would have no effect; “[t]herefore, the same ‘but for’ reasoning that guided the

174. Id. at 504-05.
175. At least the arbitration agreement in Smith did not call for the decision to be made “by flipping a coin or studying the entrails of a dead fowl.” See LaPine Tech. Corp. v. Kyocera Corp., 130 F.3d 884, 891 (9th Cir. 1997) (Kozinski, J., concurring), vacated, Kyocera Corp. v. Prudential-Bache Trade Servs., 341 F.3d 987 (9th Cir. 2003).
177. Id. at 426.
178. Id.
179. Id. at 430.
180. This case is discussed supra Part III.B-III.C.
181. MedValUSA, 872 A.2d at 430.
analysis of the Supreme Court in *Shelley* would seem to compel the conclusion that the judicial confirmation of an arbitration award constitutes state action.”\(^{182}\)

However, the *MedValUSA* court quickly noted that *Shelley v. Kraemer* was “the subject of much controversy and criticism” and its holding “has been effectively confined to its facts.”\(^{183}\) For instance, critics of *Shelley v. Kraemer* have expressed misgivings about what would happen if its reasoning were extended since, at least theoretically, all private contracts would be subject to constitutional standards.\(^{184}\) Moreover, the United States Supreme Court itself has placed “minimal reliance” on *Shelley v. Kraemer* as precedent, and extensive discussions of the case usually appear in concurring rather than majority opinions of the Court.\(^{185}\)

In addition, *MedValUSA* relied on many federal and state courts that “have concluded that judicial confirmation of an arbitration award is not sufficient to convert the action of an arbitrator into state action.”\(^{186}\) In citing these cases, the *MedValUSA* court referred to “arbitration [as] a ‘private self-help remedy.’”\(^{187}\) *MedValUSA* further noted that the holding of *Shelley v. Kraemer* had been limited to race discrimination cases.\(^{188}\) Also, if participation in arbitration is voluntary, “there is no state action involved, not even in the judicial confirmation of the punitive damage award.”\(^{189}\)

Finally, the cases cited in support of the court-confirmation-as-state-action position were distinguished by the *MedValUSA* court. For example, the court distinguished the cases of *New York Times v. Sullivan*\(^{190}\) and *Cohen v. Cowles Media Co.*\(^{191}\) by noting that, in both cases, “the court did not address whether the conduct of a private actor was converted into state action by the actions of the court—the only question was whether the action of the court itself constituted state action.”\(^{192}\)

In *MedValUSA*, the Connecticut Supreme Court concentrated its analysis on identifying and defining state action and showing its inapplicability to a situation where judicial confirmation of an arbitration award is sought. The court did not discuss at all the strong concept of finality inherent in arbitration. However, *MedValUSA*’s distinguishing of United States Supreme Court cases such as *Shel-

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182. *Id.*
183. *Id.* at 431.
184. *Id.* at n. 10.
185. *Id.* at 432. In fact, only one majority opinion by the United States Supreme Court—Evans v. Abney, 396 U.S. 435 (1970)—has discussed *Shelley* at any length. *MedValUSA*, 872 A.2d at 433.
187. *Id.* (quoting Smith v. Am. Arbitration Ass’n, Inc., 233 F.3d 502, 507 (2000)). The *MedValUSA* case cited to several cases in support of this proposition, including the *Davis* and *Smith* cases discussed *supra* Part VI.A.1-VI.A.2. *MedValUSA*, 872 A.2d at 434-35. *MedValUSA* also cited a number of cases—including *Birmingham News v. Horn*, analyzed *infra* Part VI.A.6—that have distinguished and criticized the “no state action” holding of the prevailing judicial view on this question. *MedValUSA*, 872 A.2d at 435.
188. *MedValUSA*, 872 A.2d at 434 (citing *Davis v. Prudential Sec., Inc.*, 59 F.3d 1186, 1192 (11th Cir. 1995)).
ley v. Kraemer carried the day as to the state action issue without the necessity of delving specifically into arbitration law. 193

4. Sawtelle v. Waddell & Reed, Inc. 194—Court Acknowledges There is no State Action but Uses Due Process Limits on Punitive Damages to Support Vacatur Based on the Award’s “Irrationality”

The Sawtelle case featured an arbitral award of approximately two million dollars in compensatory damages and twenty-five million dollars in punitive damages. 195 The trial court reduced the compensatory damages to slightly more than one million dollars but confirmed the award as to the punitive damages. 196 In particular, the trial court rejected the defendants’ assertion that the amount of punitive damages was governed by the standards set forth by the United States Supreme Court since those standards “dealt purely with due process concerns not relevant in arbitration proceedings.” 197 The trial court also held that, even if those standards obtained, the award of punitive damages was not “irrational as grossly excessive.” 198

The appellate court agreed that Due Process did not apply to the award of punitive damages, reasoning:

[T]here is ample authority for the proposition that a private arbitration does not implicate due process concerns since, where the parties have vo-

193. The MedValUSA court did not neglect the finality of arbitration completely. In response to a challenge to the arbitral award on the grounds that it violates public policy, the court stated:

We have been wary about vacating arbitral awards on public policy grounds because ‘implicit in the stringent and narrow confines of this exception to the rule of deference to arbitrators’ determinations, is the notion that the exception must not be interpreted so broadly as to swallow the rule.’

Id. at 438 (citation omitted).

Interestingly, the dissent in MedValUSA uses the public policy favoring arbitration to support its contention that the amount of an arbitration award of punitive damages should be reviewable by the courts, reasoning:

I also find it troubling that the majority’s ill-conceived reasoning is not confined to this case, but extends to any punitive damage award issued by an arbitrator no matter how large that award may be. Under its rationale, a $50 million punitive damage award or even a $5 billion award would not violate public policy and, therefore, would be immune from judicial review. It does not take much foresight to predict that the majority’s decision will cause parties to shun arbitration as a preferred method of dispute resolution because it will expose them to virtually unlimited punitive damage awards without any meaningful recourse from the courts. I therefore submit that the majority opinion, in addition to violating the state’s public policy disfavoring excessive punitive damages, also undermines the well established public policy favoring arbitration. Even the majority implicitly concedes that this latter policy is dominant, well-defined and expressly stated.

Id. at 449-51 (Zarella, J. dissenting) (footnotes omitted; emphasis added); see Hadelman v. DeLuca, 876 A.2d 1136, 1139 (Conn. 2005) (Zarella, J., concurring) (“[T]he assessment of punitive damages when there has been no award of compensatory damages violates the public policy of this state to foster dispute resolution through arbitration.”).

195. Id. at 267.
196. Id. at 269.
197. Id.
198. Id.
luntarily participated in the arbitration process, there is no state action involved, not even in the judicial confirmation of the punitive damage award. 199

However, the Sawtelle court then skirted the state action rule by stating that the Supreme Court’s Due Process standards for punitive damages could “provide a guide for determining whether such an award is irrational.” 200 In fact, after an extensive discussion, the appellate court in Sawtelle stated as to the “irrationality” claim:

[T]he $25 million punitive damages awarded here bears no rational relationship to the amount of compensatory damages sustained by Sawtelle or to the severity or extent of Waddell’s misconduct, and is totally out of proportion to the statutory penalty provided and damages awarded in prior comparable cases and cannot stand. 201

Moreover, following a similar line of thinking, Sawtelle further justified vacatur of the punitive damages award on “manifest disregard” grounds. 202 Therefore, the Sawtelle case accepted precedent regarding the state action issue. However, it employed the Due Process analysis as to punitive damages under the guise of applying the non-statutory vacatur grounds of irrationality and manifest disregard. This type of analysis almost makes the state action requirement superfluous because state action is not part of the irrationality or manifest disregard standards. It seems unfair to be able to circumvent the state action requirement by using other non-statutory grounds for vacatur as a tool for what is, in reality, a Due Process challenge.


In Commonwealth, the defendant attacked the arbitration award of forty-five thousand dollars in punitive damages on Due Process grounds. 204 The district court declined to accept the defendant’s argument. 205 However, in a footnote, the district court criticized the usual rule of no state action, stating that “[w]hile the procedures utilized in private arbitration do not constitute state action [citation omitted], the application of the coercive power of a court to confirm and enforce an arbitration award arguably is another matter.” 206

The court in Commonwealth came to the correct result for one good reason—i.e., the securities industry’s inherent acceptance of the limited judicial review of

199. Id. at 271 (citations omitted).
200. Id.
201. Id. at 273.
202. Id. at 274.
204. Id. at 172.
205. Id. at 177.
206. Id. at 177 n.37 (citation omitted).
arbitral awards apparently waived any non-statutory challenge such as Due Process\textsuperscript{207}—but seemingly declined to accept another good reason—i.e., no state action to support a Due Process challenge.\textsuperscript{208} Stockbroker-customer contracts invariably include arbitration agreements, and judicial review of arbitration awards is always very limited in all jurisdictions.\textsuperscript{209}

6. \textit{Birmingham News Co. v. Horn}\textsuperscript{210}—Again, a "Finding" of State Action to Support the Due Process Contention is Merely a Step in a Manifest Disregard Analysis

In \textit{Birmingham News}, the Alabama Supreme Court appeared to be critical of precedents for the no state action rule, stating with respect to the \textit{Davis} case that "there was no court involvement [in \textit{Davis}] until after the award was made. In these cases, but for the court action, there would have been no arbitration at all. These appeals are appeals from the circuit court judgments of confirmation, not from the underlying awards."\textsuperscript{211} However, in ostensibly finding state action, the Alabama Supreme Court then noted that its true purpose was to examine the matter under the manifest disregard exception.\textsuperscript{212}

Like \textit{Commonwealth}, the \textit{Birmingham News} case has not been cited with approval as to its state action analysis.\textsuperscript{213} Moreover, a court which does not review the arbitration award for a Due Process violation does not need to make a finding of state action. For example, in a manifest disregard situation, the court could just acknowledge the established law—whether based on the Due Process Clause or any other source of law—and then analyze whether the arbitrator manifestly disregarded that established law in determining whether to vacate the arbitral award.

\textsuperscript{207} Id. at 177.
\textsuperscript{208} Id. at 66-67. The manifest disregard exception refers to a situation where a court may vacate an arbitral award if the arbitrator knew of applicable law yet refused to apply it and was "well defined, explicit, and clearly applicable to the case." \textit{Id.} at 50 (quoting Halligan v. Piper Jaffray, Inc., 148 F.3d 197, 202 (2d Cir. 1998)).
\textsuperscript{210} 210. 901 So.2d 27 (Ala. 2004).
\textsuperscript{211} Id. at 66.
\textsuperscript{212} Id. at 66-67.
\textsuperscript{213} See, e.g., MedValUSA, 872 A.2d at 435.
B. Articles Addressing the Issue of Whether a Court's Confirmation of an Arbitration Award is State Action for Due Process Purposes

Recent articles by two commentators, Sarah Rudolph Cole and Carole J. Buckner, provide substantial analyses of the state action issue with regard to arbitration. Professor Cole's article provides a detailed analysis of the state action jurisprudence of the United States Supreme Court and applies it to various types of arbitration. Professor Buckner's article discusses the specific question of the applicability of Due Process to class arbitration.

1. Professor Cole—"State Action is Easier to See in Some Forms of Arbitration Than in Others"214

Professor Cole divides arbitration into three types: court-ordered arbitration, arbitration that is required by an agency (such as the NASD), and contractual arbitration.215 She concludes that state action is present in court-ordered and agency-initiated arbitration but there is no state action with regard to contractual arbitration.216

Professor Cole first discussed the state action aspect of court-ordered arbitration, which "provides for compulsory, nonbinding arbitration in smaller federal civil actions, typically when damages claimed are less than $150,000."217 The fact that the parties are required by the court to go through the arbitration process satisfies the state action element.218 The nonbinding aspect of court-ordered arbitration avoids infringement of constitutional rights such as the right to a jury trial.219

Professor Cole next analyzed agency-initiated arbitration in the context of securities arbitration, stating that "[a] more nuanced and complicated question is whether agency-initiated arbitration involves state action."220 She reasoned that, because of the significant involvement of the Securities Exchange Commission in

215. Id. at 2-3. This article has extensively addressed contractual arbitration, because in my mind, that is "true" arbitration because of the finality of the process. See the analysis of the policy of finality supra Part IV.A-IV.B, V.A. On the other hand, this article has not dealt with court-ordered arbitration since it is nonbinding. See generally Rudolph Cole, supra note 214, at 23-26. As for agency-required arbitration, I consider it to be a subset of contractual arbitration because there is an arbitration agreement as a condition of employment. See id. at 30; but see Armendariz v. Found. Health Psychcare Servs., Inc., 6 P.3d 669, 674 (Cal. 2000) (arbitration agreement must provide "essential fairness" to the employee, including but not limited to a neutral arbitrator, adequate discovery, and limitations on the cost of arbitration).
217. Id. State courts offer court-ordered nonbinding arbitration as well. See, e.g., CAL. R. CT. 3.810 et seq. (2007) (California court rule which refers to the procedure as "judicial arbitration").
219. Id. at 27.
220. Id. at 25. This is the topic of a more recent article by Professor Cole. See Rudolph Cole, Fairness in Securities Arbitration, supra note 59.
regulating and encouraging the ostensibly private organizations like the NASD to use arbitration, "state action is present in securities arbitration."\textsuperscript{221}

Professor Cole embraced the "entanglement" test for showing state action in the context of securities arbitration, reasoning:

Prior to the 1998 NASD rule change exempting statutory discrimination claims from arbitration, however, several member employees attempted to convince courts that the SEC-SRO relationship transformed the SRO into a state actor, at least when it mandated arbitration of discrimination claims. \textit{While the employees failed to convince the courts that SROs are state actors, the arguments they advanced support a finding that, at least since 1993, when the SEC began mandating that brokers register with an SRO, SROs are state actors when they require employees and customers to participate in arbitration.}

To establish state action in these discrimination cases, member employees relied principally on the excessive entanglement argument articulated in \textit{Lugar}. That is, the member employee claims that an SRO becomes excessively entangled with the government when the SEC moves from simply approving an SRO's decision to require members to arbitrate to encouraging or endorsing that action. According to claimants, the encouragement comes from the SEC's ability to approve, reject, or abrogate existing SRO rules.\textsuperscript{223}

Professor Cole then discussed contractual arbitration, which she characterized as "traditionally a private party arrangement."\textsuperscript{224} The only court involvement, if any, occurs prior to the start of and after the completion of arbitration.\textsuperscript{225}

After analyzing United States Supreme Court cases regarding state action, Professor Cole concluded that contractual arbitration does not implicate state action, reasoning:

\textit{Applying current Supreme Court jurisprudence, private party use of a private dispute resolution system does not create state action. Nor is state action present when one arbitral party seeks to enforce an arbitra-}

\textsuperscript{221}This type of organization is called a "self-regulatory organization" or SRO. Rudolph Cole, \textit{supra}, note 214, at 28. The relationship between the federal government and SROs is described as follows:

Although SROs are responsible for protecting investors from wrongful acts their members commit, they are not federal agencies. No statute mandated the creation of these SROs, and the government does not appoint SRO board members. Nor do government employees serve on any NASD or NYSE board or committee. Nevertheless, SROs maintain significant government connections. For example, the Securities Exchange Commission (SEC) is responsible for providing oversight of the SROs. The SEC reviews existing SRO rules and may approve or disapprove proposed new rules. Moreover, it can alter or abrogate existing rules and may proceed against a SRO if the SRO does not enforce its own rules.

\textit{Id.} at 30.

\textsuperscript{222}Id. at 29.

\textsuperscript{223}Id. at 30-31 (emphasis added; footnotes omitted).

\textsuperscript{224}Id. at 41. Contractual arbitration is extensively described \textit{supra} Part II.

\textsuperscript{225}Id.
tion agreement or award. The FAA, which provides the mechanism by which such enforcement actions proceed, is a neutral regulatory scheme. . . . [J]udicial enforcement of neutral laws is not state action even when the result disadvantages protected groups.226

Professor Cole's conclusions regarding court-ordered and contractual arbitration are well-taken. Court-ordered arbitration implicates state action since the parties are forced by the court to participate. Contractual arbitration, as shown by ample case authority, does not implicate state action. However, Professor Cole's analysis finding of state action with respect to securities arbitration is misplaced since securities arbitration is merely a subset of contractual arbitration. Securities arbitration, even if it is standard in the industry, is still something to which the parties have agreed.227 After all, the standard arbitration provision is not so overwhelming that it bars anyone from opting out of working or trading in the securities industry.228

2. Professor Buckner—Is There State Action in Class Arbitration?

Professor Buckner's article provides a detailed discussion of state action jurisprudence and its application to non-class and class arbitrations.229 Given the specialized nature of her article, the following examination of it will touch on the class arbitration setting only.

Professor Buckner divided her analysis of state action in class arbitrations into two parts. First, she discussed "hybrid" class arbitration, which was described as follows:

[U]nder the hybrid system of class arbitration, courts maintain "discretion" to determine whether a particular case is appropriate for class arbitration. Although arguably discretion violates the spirit of the Supreme Court's plurality opinion in Bazzle, courts operating under the hybrid model continue to assert that they (rather than the arbitrator) have discretion to determine which cases are appropriate for class arbitration treatment.230

226. Id. at 49 (emphasis added).
227. Marion, supra note 209, at 402.
228. Please note that "[s]ome analysts, however, have historically regarded the NASD [which handles 90% of all securities arbitrations] as an expensive and unfriendly venue for investors." Id. at 422-23. This could support a challenge to a petition to compel arbitration on the grounds that the standard securities arbitration agreement is unconscionable. 9 U.S.C. § 2 (2000); Circuit City Stores, Inc. v. Adams, 279 F.3d 889, 893-94 (9th Cir.) (an arbitration provision in an employment contract was procedurally and substantively unconscionable since the arbitration provision was included in a standard-form contract prepared by the party with superior bargaining power, it gave the employee no option but to sign or reject the contract, it required the employee to arbitrate but gave the employee the option of arbitration or litigation, and the employee was limited to injunctive relief and front and back pay only with no emotional distress or punitive damages as provided by state law).
230. Id. at 226-27 (footnotes omitted). In Green Tree Fin. Corp. v. Bazzle, 539 U.S. 444 (2003), a plurality of the United States Supreme Court held that whether the subject arbitration agreements could
Professor Buckner concluded that the hybrid model implicates state action for two reasons. First, there is "entanglement" between a state actor—the court—and a private actor—the arbitrator. She made a particularly apt analogy to court-ordered arbitration to support this entanglement argument. Second, she contended that state action exists because "the state has 'traditionally' and 'exclusively' controlled class action litigation." Professor Buckner then analyzed the state action standard as to models of class arbitration created by private ADR providers such as the American Arbitration Association (AAA) and JAMS. She concluded that state action could obtain under the entanglement test due to the possibility that judicial involvement would be greater in the class arbitration context rather than the non-class arbitration context.

Applying the public function test, Professor Buckner contended that the level of judicial involvement would determine whether there was state action, reasoning:

To the extent that a private arbitrator accepts a judicial delegation as authorized by the AAA Rules, the delegation element of the public function arm of the state action doctrine continues to be satisfied. However, private parties may make their way to arbitration providers for class arbitration without judicial involvement. After the Bazzle decision, it is more likely that courts will simply compel the arbitrator to decide whether class arbitration is proper or not, deferring all decisions from that point onward to the arbitrator. Under such a scenario, discretionary judicial delegation of an arbitral matter to class arbitration is absent. The involvement of the courts is much like the court's involvement in non-class arbitration in that it is not the state actor, but rather private parties who delegate the power to the arbitrator or arbitration provider. Private provider models operating without delegation involve no state action and re-

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be interpreted to forbid class arbitration was an issue of contract interpretation to be decided by the arbitrator. Id. at 453-54.

231. Buckner, supra note 229, at 233-34.

232. Id. at 233 ("Much as judicially annexed arbitration involves state action, the hybrid system involves state action.") (footnote omitted).

233. Id. at 234. In addition, Professor Buckner criticizes the hybrid model; since these criticisms pertain to "doctrinal and practical issues," and not state action issues, her commentary will not be discussed herein. See id. at 236-40.

234. These private ADR providers have created rules for class arbitrations that are "loosely patterned on Federal Rule of Civil Procedure 23." Id. at 239.

235. Id. at 239, 245-46. Professor Buckner further noted:

Once the scene of the potential constitutional deprivation shifts from the arbitral forum to the courtroom, whether for an initial determination of class certification (under the hybrid model) or a review of an arbitrator's determination (under provider models), judicial participation places the court's imprimatur upon the proceeding. Just as in the peremptory challenge cases, where the court, in essence, "reviews" the constitutionality of the private actors' jury selections, a court's review of the private arbitration providers' certification determinations involves state action.

Id. at 245-46 (footnote omitted).
quire no due process under the public function prong of the state action
doctrine.236

Professor Buckner's analysis is apt given the unique scenario of class arbitra-
tions. The level of judicial involvement in class arbitrations appears to be much
higher than that found in non-class arbitrations. However, Professor Buckner did
not discuss the contractual nature of all arbitrations, whether class or not.

C. Closing Remarks as to Whether a Court's Confirmation of an Arbitra-
tion Award is State Action for Due Process Purposes

The cases are uniform in holding that court confirmation of an arbitral award
is not state action. Therefore, the losing party in an arbitration cannot count on
using the Due Process limits on punitive damages to challenge an award of puni-
tive damages when a court is presented with a motion to confirm the award as a
judgment. Once again, if the parties wish to exclude punitive damages from the
arbitration award, they should do so in their arbitration agreement because, once
the arbitrator rules, the award is final unless it can be challenged pursuant to the
limited grounds stated in arbitration statutes such as the FAA. However, Profes-
sor Buckner makes a good point with respect to class arbitrations, that there could
be state action since the court is generally more involved in the matter. This is not
true in the situation of the typical commercial arbitration in that the court's in-
volve ment is restricted to deciding whether to confirm or vacate the arbitration
award.

VII. CONCLUSION

In recent years, a number of cases and commentators have addressed the issue
of whether a court should confirm an arbitration award of punitive damages when
it violates the Due Process Clause of the Fourteenth Amendment. This would
seemingly invoke the state action requirement in the sense that any court is a state
actor.

The uniform position of the courts—no state action—is correct. Specifically,
the policy of finality traditionally found in arbitration law must trump any constitu-
tional inquiries. This is because arbitration is ultimately based on the parties' 
agreement, which inevitably will recite that the arbitrator's decision shall be final.
In any event, this finality is generally implied under established arbitration law.

The bottom line is that arbitration is a private process to which the parties
have agreed, and the courts' only obligation is to uphold that agreement pursuant
to established arbitration and contract law. It follows that Due Process challenges
to arbitration awards of punitive damages cannot be allowed. Therefore, a court's
confirmation of an arbitration award cannot be construed to be state action.

236. Id. at 248-49 (footnotes omitted). The public function test means that "state action [is] present in
the exercise by a private entity of powers traditionally exclusively reserved to the State." Jackson v.
Metro. Edison Co., 419 U.S. 345, 352 (1974). This standard requires more than extensive government
regulation or a monopoly granted by the government. Id. at 351-52; Kruger v. Wells Fargo Bank, 521
P.2d 441, 449 (Cal. 1974).