

1999

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### Recommended Citation

Christina S. Young, *NASD Applications Require Arbitration of Employment Disputes - Mouton v. Metropolitan Life Insurance Co.*, 1999 J. Disp. Resol. (1999)

Available at: <https://scholarship.law.missouri.edu/jdr/vol1999/iss1/10>

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# NASD Applications Require Arbitration of Employment Disputes

*Mouton v. Metropolitan Life Insurance Co.*<sup>1</sup>

## I. INTRODUCTION

Under the Federal Arbitration Act's (FAA) mandate favoring arbitration, numerous statutory claims are subjected to arbitration.<sup>2</sup> For employment disputes falling under Title VII, competing approaches based on whether the employment agreement was a union or a non-union agreement, have been adopted.<sup>3</sup> Union agreements to arbitrate employment disputes are generally not compelled to arbitrate. Conversely, in a non-union employment agreement, broad arbitration clauses are interpreted to require arbitration of Title VII claims. These inconsistent rules have been applied to the detriment of non-union employees.

## II. FACTS AND HOLDING

Andre Mouton was employed by Metropolitan Life Insurance Company as a sales agent.<sup>4</sup> Metropolitan is a member of the National Association of Securities Dealers (NASD), which required Mouton to be licensed by NASD.<sup>5</sup> In 1989, Mouton completed the Uniform Application of Securities Industry Regulation<sup>6</sup> to become licensed.<sup>7</sup> By signing the application, Mouton agreed to "arbitrate any dispute, claim or controversy that may arise between [him] and [his] firm, or a customer, or any other person, that is required to be arbitrated under the rules, constitutions or by-laws of the [NASD] as may be amended from time to time".<sup>8</sup> In

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1. 147 F.3d 453 (5th Cir. 1998).

2. Norris Case, *Arbitration of Workplace Discrimination Claims: Federal Law and Compulsory Arbitration*, 14 *TOURO L. REV.* 839, 847 (1998).

3. *Id.* at 851.

4. *Mouton*, 147 F.3d at 454.

5. *Id.*

6. The Uniform Application of Securities Industry Regulation is also known as a U-4 Registration. *Id.*

7. *Id.*

8. At the time of signing the NASD in 1989 the Code section 1 provided arbitration was required for: [A]ny dispute, claim or controversy arising out of or in connection with the business of any member of the Association, with the exception of disputes involving the insurance business of any member which is also an insurance company: (2) between or among members and public customers, or others.

*Id.*

1993, amendments were made to NASD rules,<sup>9</sup> but Mouton never filed a new U-4 registration after the amendments were made.<sup>10</sup>

In 1995, Mouton was on disability leave,<sup>11</sup> but he testified for a co-worker in a Title VII sexual harassment action brought against Metropolitan.<sup>12</sup> After testifying and upon his return to work, Mouton was subjected to unlawful employment actions which resulted in his termination and the granting of a right to sue letter by the EEOC.<sup>13</sup>

Mouton filed a Title VII complaint in December 1996.<sup>14</sup> Based on the NASD agreement signed by Mouton, Metropolitan asked for a summary judgment.<sup>15</sup> The district court denied the motion because a genuine issue of material fact existed as to whether Mouton was required to arbitrate his Title VII claim under the 1989 version of the agreement; however, the district court did grant a stay of further proceedings until an appeal of the summary judgment was complete.<sup>16</sup>

The Fifth Circuit Court of Appeals reversed the district court's denial of Metropolitan's summary judgment motion, stating that under the NASD rules Title VII actions require arbitration even for pre-amendment disputes.<sup>17</sup>

### III. LEGAL BACKGROUND

Two opposing rules have developed with respect to compulsory arbitration of employment discrimination claims based on whether the workplace is union or non-union.<sup>18</sup> Union workers are not compelled to arbitrate employment discrimination claims under collective bargaining agreements, but non-union employees must arbitrate claims when an arbitration clause exists in the employment contract.<sup>19</sup>

In *Alexander v. Gardner-Denver*,<sup>20</sup> the Supreme Court held that an employee is not barred from a judicial determination in an employment discrimination claim if arbitration proceedings occurred under a collective bargaining agreement.<sup>21</sup> An employee who exercises her collectively bargained rights does not waive her individual rights under Title VII.<sup>22</sup> Because Title VII rights are individual rights, a

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9. The amended rules state:

[T]he arbitration of any dispute, claim or controversy arising out of or in connection with the business of any member of the [NASD] or arising out of the employment or termination of employment of associated person(s) with any member, with the exception of disputes involving the insurance business of any member which is also an insurance company.

*Id.* at 455.

10. *Id.*

11. Mouton was on leave because of a work-related accident that occurred in 1994. *Id.*

12. *Id.*

13. *Id.*

14. *Id.*

15. *Id.*

16. *Id.*

17. *Id.*

18. Case, *supra* note 2, at 839.

19. *Id.*

20. 415 U.S. 36 (1974).

21. Case, *supra* note 2, at 840.

22. *Id.*

collective bargaining agreement made by a group cannot act as a waiver of the individual's right.<sup>23</sup>

In 1991, the Supreme Court again reviewed mandatory arbitration agreements in employment contracts.<sup>24</sup> In *Gilmer v. Interstate/Johnson Lane Corp.*, the plaintiff was required to register with the New York Stock Exchange (NYSE), which subjected him to regulations requiring arbitration of "[a] controversy between a registered representative and any member or member organization arising out of the employment or termination of employment of such registered representative."<sup>25</sup> *Gilmer* subsequently brought an age discrimination claim against his employer.<sup>26</sup> Relying on the Supreme Court's ruling in *Alexander*, the district court denied a motion to compel arbitration.<sup>27</sup> This ruling was later reversed by the Fourth Circuit Court of Appeals.<sup>28</sup>

In reviewing the issue, the Supreme Court highlighted the Federal Arbitration Act's mandate favoring arbitration of disputes, and held that arbitration can be used to resolve statutory claims unless the legislature specifically addresses a preclusion.<sup>29</sup> Since the ADEA does not specifically preclude arbitration, *Gilmer* allows arbitration of such disputes.<sup>30</sup>

Even though the result reached in *Gilmer* was different than the earlier decision in *Alexander*, *Alexander* was not overruled.<sup>31</sup> Under *Gilmer*, a distinction was made between contractual rights under a collective bargaining agreement and an individual's statutory rights.<sup>32</sup>

Since *Gilmer*, courts have generally enforced compulsory arbitration of employment disputes arising in non-union contracts.<sup>33</sup> A few courts, however, have avoided compulsory arbitration by applying *Alexander* and distinguishing *Gilmer*.<sup>34</sup> The Ninth Circuit used public policy in *Prudential Insurance Co. of America v. Lai*<sup>35</sup> arguing that victims of harassment could not knowingly agree to submit disputes to arbitration by registering with NASD.<sup>36</sup> In *Prudential*, for example, the employees signed the U-4 form, but were not given an opportunity to read the form and were told they were applying to take a required test.<sup>37</sup> Arbitration was never mentioned to the employees and they were never given a NASD Manual that contained the arbitration terms.<sup>38</sup> The court determined there was no valid agreement to arbitrate because they did not "knowingly contract to forego their statutory remedies in favor

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23. *Id.* at 843-44.

24. *Id.* at 845.

25. *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 23 (1991).

26. *Id.*

27. *Id.* at 24.

28. *Gilmer v. Interstate/Johnson Lane Corp.*, 895 F.2d 195, 196 (4th Cir. 1990).

29. *Gilmer*, 500 U.S. at 26.

30. *Id.*

31. *Case, supra note 2*, at 851.

32. *Id.*

33. *Id.* at 854.

34. *Id.*

35. 42 F.3d 1299 (9th Cir. 1994).

36. *Case, supra note 2*, at 854.

37. *Prudential*, 42 F.3d at 1301.

38. *Id.*

of arbitration.”<sup>39</sup> Similarly, in a Seventh Circuit case, *Farrand v. Lutheran Brotherhood*,<sup>40</sup> the court found that an employer could not compel arbitration because the NASD arbitration clause, unlike the NYSE rules in *Gilmer*, did not specifically require arbitration of employment disputes.<sup>41</sup>

Conflicting decisions based on union and non-union contracts as well as differing results in circuit courts for non-union contracts leaves confusion in deciding if compulsory arbitration clauses will be enforced in employment disputes.

#### IV. INSTANT DECISION

In the instant case, the court first addressed whether the NASD code, prior to its 1993 amendments, requires the employment dispute brought by Mouton to be arbitrated.<sup>42</sup> If the pre-1993 NASD Code required arbitration by the broad language in the arbitration clause, then the court did not need to decide the effect of the 1993 amendments, which included language requiring arbitration of disputes “arising out of [the] employment or termination of employment.”<sup>43</sup> The court had three primary reasons for following the majority of other circuits upholding such mandatory arbitration agreements.<sup>44</sup>

First, the court noted that in 1987 NASD had made it clear that the arbitration provisions included “employment disputes between its members and their registered representatives, such as securities dealers.”<sup>45</sup> The court also pointed to an explanation of the 1993 amendments that stated that the new language was not meant to broaden any category subject to arbitration, but only to “clarify that employer-employee dispute[s] indeed fell within the ambit of the Code’s arbitration provisions.”<sup>46</sup>

Second, the court looked at public policy issues that favor arbitration of such disputes.<sup>47</sup> The primary focus was the Federal Arbitration Act’s policy that “any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.”<sup>48</sup> The court stated that there was no doubt employment-related claims were subject to arbitration under the pre-1993 Code, but even if the provisions were ambiguous the ambiguity would be resolved in favor of arbitration.<sup>49</sup>

39. *Id.* at 1305.

40. 993 F.2d 1253 (7th Cir. 1993).

41. Case, *supra* note 2, at 856.

42. *Mouton*, 147 F.3d at 455.

43. *Id.*

44. *Id.*

45. *Id.* (citing Proposed Rule Change by National Association of Securities Dealers Relating to Amendments to Code of Arbitration Procedure, 52 Fed. Reg. 9232 (1987)).

46. *Id.* (citing Filing of Proposed Rule Change by National Association of Securities Dealers, Inc., Relating to Enforcement of Arbitrators’ Orders Under the NASD Code of Arbitration Procedure, 58 Fed. Reg. 39070, 39071 (1993)).

47. *Id.* at 456.

48. *Id.* (quoting *Moses H. Cone Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24-25 (1983)).

49. *Id.*

Finally, the court looked at a prior case involving a Title VII claim, *Rojas v. TK Communications, Inc.*,<sup>50</sup> in which the court stated that the arbitration clause need not explicitly refer to employment-related disputes in order to mandate arbitration.<sup>51</sup> Language in an arbitration clause, including “other disputes,” was broad enough to encompass Title VII claims.<sup>52</sup> The court concluded that the clause where Mouton “agreed to arbitrate ‘any dispute, claim or controversy that may arise between [himself] and [Metropolitan]’” was broad enough to encompass a Title VII claim.<sup>53</sup>

Next, the court addressed whether Mouton’s claim fell under the exception to arbitration for “disputes involving the insurance business of any member which is also an insurance company.”<sup>54</sup> The court followed two circuits in rejecting this argument.<sup>55</sup> In the Third Circuit, the case of *In re Prudential Insurance Co. of America Sales Practice Litigation*<sup>56</sup> held that under the NASD Code the intent was to require arbitration of employment disputes but not insurance claims, and, since a retaliation claim is unrelated to the insurance business, it was subject to arbitration.<sup>57</sup> The Tenth Circuit has also addressed the issue in *Armijo v. Prudential Insurance Co. of America*,<sup>58</sup> stating “there is nothing unique about these discrimination claims by plaintiffs that involve the insurance business of prudential.”<sup>59</sup> Mouton’s claim likewise involved only Metropolitan’s obligation as an employer, not as an insurer.<sup>60</sup> Any other decision would render meaningless arbitration agreements where companies are involved in the insurance business and have NASD-licensed employers.<sup>61</sup>

Lastly, Mouton argued that “he did not knowingly and voluntarily waive his access to a judicial forum.”<sup>62</sup> Applying the decision in *Rojas* that the arbitration clause need not explicitly refer to employment disputes, the court held Mouton agreed to arbitrate “any dispute, claim or controversy.”<sup>63</sup>

Based on the broad scope of the NASD arbitration provision, the public policy concerns favoring arbitration, and the fact that the claim did not fall under the insurance exception, the court concluded that Mouton was required to arbitrate his Title VII claim.<sup>64</sup>

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50. 87 F.3d 745 (5th Cir. 1996).

51. *Mouton*, 147 F.3d at 456.

52. *Id.*

53. *Id.*

54. *Id.*

55. *Id.*

56. 133 F.3d 225 (3d Cir. 1998).

57. *Mouton*, 147 F.3d at 456 (citing *In re Prudential Ins. Co.*, 133 F.3d at 234).

58. 72 F.3d 793 (10th Cir. 1995).

59. *Mouton*, 147 F.3d at 457 (quoting *Armijo v. Prudential Ins. Co. of Am.*, 72 F.3d 793, 800 (10th Cir. 1995)).

60. *Id.*

61. *Id.*

62. *Id.*

63. *Id.*

64. *Id.*

## V. COMMENT

Under the court's decision in *Mouton*, the Fifth Circuit Court of Appeals joined the majority of other circuits who generally favor compulsory arbitration.<sup>65</sup> The Ninth and Seventh Circuits have avoided compulsory arbitration of employment disputes, still relying in part on the decision reached in *Alexander*.<sup>66</sup> As a majority of Circuit Courts of Appeals adopt the approach of compulsory arbitration of employment disputes for non-union employees, two contrasting rules for resolution of employment disputes are left. As a result, confusion has developed in the employment contracting setting.

Union employees cannot collectively bargain away or waive an individual right.<sup>67</sup> In *Alexander*, the court noted the importance of the individual's right to bring a discrimination action.<sup>68</sup> In light of the importance of this right, a non-union employee should not waive this right without knowingly entering into such an agreement. The decision in *Gilmer* on which the majority of courts now rely, drew a distinction between union and non-union employees due to the fact that the union's collective bargaining agreements acted to destroy an individual right.<sup>69</sup> This majority in the Court of Appeals fail to appreciate the similarities between collective bargaining agreements and the mandatory registration with NASD for securities dealers.

Securities dealers such as *Mouton* are required to complete the U-4 application in order to register with NASD. Included in the application and registration is a broad mandatory arbitration clause. The individual's rights waived by such an application and registration form are especially significant in the employment dispute context.

First, as argued in *Gilmer*, employers have significant bargaining power over employees.<sup>70</sup> When an employer is required to arbitrate as a condition of employment, concern develops over the involuntary waiver of access to the judicial forum. The right to adjudication is an individual right that should not be waived by a mandatory registration requirement. A forum needs to exist for bargaining between the employer and employee over the waiver of access to the judicial forum and mandatory arbitration.

Second, many employees may sign the registration forms without knowing they are waiving a right. For example, when an employee signs the U-4 form which subjects her to a broad arbitration clause she must also realize that the arbitration clause includes portions of the NASD code. The employee must look to a separate document than those signed to understand the full reach of the arbitration clause. In *Prudential*, the Ninth Circuit Court of Appeals refused to enforce an arbitration clause contained in the NASD rules because the appellant was never given copies of

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65. Case, *supra* note 2, at 857.

66. See Case, *supra* note 2, at 854.

67. *Alexander*, 415 U.S. at 51-52.

68. *Id.*

69. *Gilmer*, 500 U.S. at 34-35.

70. *Id.* at 32-33.

the NASD manual.<sup>71</sup> A requirement of knowingly agreeing to arbitrate under the U-4 registration should at least be required for non-union employees.

Finally, even though the general rule under the FAA is to allow arbitration in the employment dispute setting, the employer is at an advantage. The bias toward employers stems from their routine contact with arbitrators and procedures. *Gilmer* addressed this concern by pointing out that significant procedural mechanisms were in place by the New York Stock Exchange (NYSE) in agreements made by those required to register with NYSE.<sup>72</sup> The advantage enjoyed by employers can be cured by procedural safeguards used to protect employees.

The FAA mandate favoring arbitration changed the attitude of courts toward arbitration, but this policy created conflicting rules that gave greater rights to union employees. Applying an inconsistent policy toward non-union employees has a tremendous impact on employee rights under Title VII. If a union employee does not waive her right by signing a collective bargaining agreement, it follows that a non-union employee should not be able waive her right by registering with NASD. Certain factors should specifically be addressed when applying the NASD arbitration clause to employment disputes, such as (1) if a registration is mandatory, (2) if the clause was knowingly agreed to, and (3) if procedures exist to ensure fairness in the arbitration proceedings.

Mandatory registration with associations such as NASD leaves the employee with no meaningful choice about arbitration. To keep her job, an employee must sign the form and agree to arbitrate. This lack of choice is comparable to union employees who cannot waive their individual right to bring suit by belonging to the union. The distinction between union and non-union employees unfairly allows enforcement of mandatory arbitration clauses in registration contracts, but disallows such enforcement in the collective bargaining context.

When mandatory registration is required, special attention should focus on the employee "knowing" that employment disputes will be subjected to arbitration. As the court in *Prudential* highlighted, the employee should "knowingly contract to forego their statutory remedies."<sup>73</sup> The form should focus attention on the arbitration clause by placing it in bold or capitol letters in the text and the NASD Manual should be provided to employees and posted in the workplace.

Lastly, as noted by the *Gilmer* court, procedures should exist to ensure fairness in the arbitration proceedings.<sup>74</sup> The *Gilmer* court offered several meaningful suggestions to eliminate the bias toward the employer, including: information about the arbitrator's employment history and background, and an offering the employee the ability to make a peremptory challenge of the arbitrator chosen by the employer.<sup>75</sup> It is argued that these factors would help to ensure fairness once arbitration is compelled.

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71. *Prudential*, 42 F.3d at 1304.

72. *Gilmer*, 500 U.S. at 30-32.

73. *Prudential*, 42 F.3d at 1305.

74. *Gilmer*, 500 U.S. at 30-32.

75. *Id.* at 30; see Case, *supra* note 2, at 849.

If a distinction is made between union and non-union employment contracts, safeguards should be considered to make sure non-union employees are also not “forego[ing] their statutory remedies” without knowledge that they are doing so.<sup>76</sup>

## VI. CONCLUSION

Employment contracts containing arbitration clauses are increasingly being applied to Title VII claims brought by employers.<sup>77</sup> These agreements have been upheld by a majority of circuits following the decision in *Gilmer*.<sup>78</sup> The Fifth Circuit Court of Appeals joined the majority of circuits favoring this policy without fully appreciating the fact that few distinctions actually exist between signing a collective bargaining agreement and signing NASD registration forms.

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76. *Prudential*, 42 F.3d at 1305.

77. Case, *supra* note 2, at 854-57.

78. *Id.* at 862.