ORIGINAL

# OFFICIAL TRANSCRIPT
# PROCEEDINGS BEFORE

# THE SUPREME COURT
# OF THE
# UNITED STATES

**CAPTION:** OFELIA RODRIGUEZ de QUIJAS, ET AL., Petitioners
V. SHEARSON/AMERICAN EXPRESS, INC., ETC.

**CASE NO:** 88-385

**PLACE:** WASHINGTON, D.C.

**DATE:** March 27, 1989

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IN THE SUPREME COURT OF THE UNITED STATES

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OFELIA RODRIGUEZ de QUIJAS, ET AL., Petitioners, v. SHEARSON/AMERICAN EXPRESS, INC., ETC. : No. 88-385

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Washington, D.C.

Monday, March 27, 1989

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 10:02 o'clock a.m.

APPEARANCES:

DENIS A. DOWNEY, ESQ., Brownsville, Texas; on behalf of the Petitioners.

THEODORE A. KREBSBACH, ESQ., New York, New York; on behalf of the Respondents.

C O N T E N T S

P R O C E E D I N G S

(10:03 a.m.)

CHIEF JUSTICE REHNQUIST: We'll hear argument first this morning in No. 88-385, Ofelia Rodriguez de Quijas, et al., versus Shearson/American Express.

ORAL ARGUMENT OF DENIS A. DOWNEY, ESQ.,

ON BEHALF OF THE PETITIONERS

MR. DOWNEY: Mr. Chief Justice and may it please the Court:

These cases arise from complaints filed in the Southern District of Texas, Brownsville Division, which allege violations of state common law, including sexual assault, state statutory securities provisions, and federal securities provisions.

Pursuant to the order of the district court, all these issues were ordered submitted to arbitration, with the exception of the 12(2) Securities Act claims. That order was appealed to the Fifth Circuit Court of Appeals, who in effect held that this Court's decision in McMahon had overruled the Wilko decision, and the Fifth Circuit ordered the 12(2) claims be in fact arbitrated.

And it's on the writ of certiorari to the Fifth Circuit in fact that we are here before you today.

These facts basically are similar. They involve a number of plaintiffs. The basic allegation is fraudulent trades in the accounts of these individuals. While a brief review of the facts indicates that they are sad facts, the remarkable thing about these cases are in fact that these cases are all too common.

The reality of America is that women outlive men, and the result is that at some point in a woman's life she finds herself with insurance proceeds or with liquidation of business proceeds, frequently lacking in business experience, and with a fear for future financial security. These cases are about in fact all of us.

As we see this case, the critical issue here is whether or not this Court is going to overrule its decision rendered in Wilko 36 years ago. The standard analysis that's been applied to all this Court's cases would appear to be that we look at the purposes, the legislative history, and the text of the Acts in question. And of course, we're dealing here with the Federal Arbitration Act of 1925 and the Federal Securities Act of 1933.

In the Petitioners' view, the Federal Arbitration Act has been read much too broadly. It would appear that the text of the Federal Arbitration

Act expresses the intent to place arbitration contracts on exactly the same footing as other contracts.

And that is also what the legislative history would seem to indicate. The key phrase here throughout the court cases that have reviewed the legislative history of that Act is that the intent was to place these contracts on the same footing as other contracts.

We do not see an elevated federal policy in the Federal Arbitration Act.

QUESTION: Certainly we would have to reconsider some of our recent cases to adopt that view, wouldn't we, Mr. Downey?

MR. DOWNEY: Yes, that's unquestionably, unquestionably true.

Our purpose here is, rather than in the absolute sense, to try to create a better comparative balance between the Federal Arbitration Act and the 1933 Securities Act. We see the Federal Arbitration Act as involving federal policies of considerably less importance than that of the 1933 Securities Act.

QUESTION: Mr. Downey, is there any evidence that Congress meant to treat claims under Section 12(2) differently than claims under Section 10(b)? Do we have anything in the legislative history to indicate that Congress intended them to be treated differently, even

though they were not enacted at the same time?

MR. DOWNEY: Well, I would say that, first of all, the fact that the 10(b) action, the civil part of it, is an implied cause of action. Although I understand there's a sensitivity that we shouldn't treat implied actions differently than express actions, I think there are some contexts where that fact would be true.

In this instance, this may well have been an instance where Congress intended that the area be left to the courts for general development.

I would also point out that there is a difference in 10(b) and 12(2) in the sense that 12(2) addresses -- purports to protect purchasers of securities, whereas the 10(b) action is both purchasers and sellers. So perhaps Congress felt less inclined to protect in fact brokers under Section 10, who would be sellers.

I think the legislative history of the '33 Securities Act shows -- and also I would add to that that obviously the difference of the jurisdictional provisions tells us something. There must be a reason why the jurisdictional provisions are not the same. There must be some sort of a logical explanation for that.

The '33 Securities Act --

QUESTION: Perhaps there is, but is it an explanation that has anything to do with the difference between the two sections for present purposes?

MR. DOWNEY: I'm not sure I understand that question.

QUESTION: Well, you say that the jurisdictional provisions are different. Well, that may be true. They may use different words as well. But why does that have anything to do whether -- with the question whether for purposes of the question before us today you should treat 10(b) and 12(2) any differently?

MR. DOWNEY: Well, I would say because perhaps Congress was less inclined to protect the sellers of securities under the '34 Act, as opposed to the '33 Act, which protects the purchaser; that perhaps Congress was less sympathetic.

QUESTION: Well, no, you have to say less inclined to protect sellers and purchasers than to protect purchasers alone. Is that your point?

MR. DOWNEY: Yes, but in kind of a subtractive sense. And I understand your question. It's well taken, obviously.

What we see in the 1933 Securities Act is that Congress -- one of the problems with the securities

field after the crash and before was that the state legislation that existed was a patchwork, and one of the substantive reasons that the '33 Securities Act was passed in fact was to create a situation where the issuers of securities could not run and hide in a convenient state.

And so that concept would seem to connect with Section 22, which appears to give the purchaser of securities the right in fact to place issuers in the court of their choice and in the venue selection of their choice.

We think it's also significant that the '33 Securities Act adopted the Brandeis thesis of fiduciary duty, which we think is highly relevant to these cases.

The legislative history of the '33 Act shows a discussion of the fine print in prospectuses, indicates that there was a need to protect the old and the unsophisticated, which is certainly before this Court today; and also indicated there had been an historical ineffectiveness of enforcement of criminal sanctions of wire and mail fraud statutes. In fact, the '33 legislative history would seem to show that Congress realized that it was important that private enforcement would be used to effectuate the goals.

QUESTION: Mr. Downey, did you raise the

adhesion argument below?

MR. DOWNEY: We have made the argument consistently through the district court that in fact these are adhesion contracts and that there is overreaching.

QUESTION: Was that ever addressed below?

MR. DOWNEY: It's never been addressed, no.

QUESTION: You make another argument, don't you, that regardless of what this Court does, if we were to disagree with you about the validity today of Wilko and were to reject that now, I take it you argue that in any event it shouldn't be applied to your clients?

MR. DOWNEY: Yes, that's correct, Justice.

QUESTION: You think it would not be retroactive under a Chevron analysis?

MR. DOWNEY: Well, I think that goes -- I think the key issue on the retroactivity goes to the question of whether or not there would be manifest or substantial injustice to apply this case retroactively, and we think that that's a question that --

QUESTION: These agreements were signed before McMahon was decided?

MR. DOWNEY: These agreements were signed in 1982 and 1983, and owing to the criminal docket of the Southern District little progress has been made.

QUESTION: Mr. Downey, could I come back to the adhesion contract point for a moment. What did the lower courts say about that?

MR. DOWNEY: The lower courts really didn't address the question.

QUESTION: Well, they had to address it, didn't they? I mean, even if you lose on the arbitrability point, surely it would be trumped by the fact that it's not a valid contract anyway, wouldn't it?

How could they not have addressed it?

MR. DOWNEY: Okay. They could not have addressed it -- and that's a major problem in this whole arbitration area. They did not address it because of the existing principle that one may not address these issues unless there is an allegation of fraud in the inducement of the specific arbitration term.

So district courts aren't looking at these, at these terms, at the basic contract itself, unless you can come forward and show --

QUESTION: Well, but that's applying a doctrine of adhesion. What they're saying is it is not an adhesion contract unless there's --

MR. DOWNEY: Well, what they're saying is we will address only one question, whether or not there is

fraud in the inducement of this specifically in the arbitration provision; we will ignore any other contractual issue.

And so that if the broker holds a gun --

QUESTION: How can they possibly do that? I mean, you can say there's no contract. They've really been doing that? You say there's no contract and the court below says, well, maybe there was and maybe there wasn't, but we're only going to look at the meaning of this particular contractual term? And you jumped up and said, but there's no contract at all, and the court says, well, maybe there was and maybe there wasn't?

MR. DOWNEY: That's right.

QUESTION: I can't believe they did that.

MR. DOWNEY: Right, and the argument I made to the Fifth Circuit in fact was that if the broker held a gun up to the client's head and said, sign the contract, under the way that they've interpreted that we can't do anything about that, that has to go to arbitration, because he didn't hold a gun up and say, sign the arbitration term.

So it's created a situation where district courts really don't get to review these things until after arbitration.

QUESTION: Oh, I see. You're saying that they

defer that question and leave the question of adhesion to the arbitrator.

MR. DOWNEY: Correct.

QUESTION: Well, what's the matter with that?

MR. DOWNEY: Well, in the egregious case where there is obvious overreaching, that means we go through the arbitration process, entertain that question, and go back, you know, to district court again. It takes a lot of time, and that's obviously an inefficient way to utilize judicial resources.

I think if there's a fundamental claim like that, the district court ought to decide it up front.

QUESTION: But by hypothesis there was no overreaching or at least no fraud in the agreement to arbitrate.

MR. DOWNEY: Right. The overreaching -- well, there's overreaching in the sense and adhesiveness in the sense that virtually all of these margin contracts require that term.

QUESTION: Well, but didn't the lower courts here at least find that the agreement to arbitrate was an agreement, a valid agreement?

MR. DOWNEY: Well, in essence they -- it's an interesting question. Presumably that's what they found, although I don't believe there's a specific

finding to that effect.

In all of these cases, these investors had absolutely no idea what they were signing. This document was face down, it was fine print. These people were not sophisticated. These people were, you know, neophyte investors who had no concept at all what it was they were being asked to sign.

They didn't even receive copies of these documents so they could later review them and change their mind and take their money out of the market. That never happened.

The issue for us, of course, is what Wilko decided, and we think it's very clear, based on 36 years of what legal commentators said and based on every decision of this Court with the exception of McMahon, that Wilko said that the waiver of the choices in Section 22 amounted to an attempted waiver of the provision.

And we think that that's very clearly what Wilko decided, even though the Wilko court gratuitously went on to note that, perhaps 12(2) claims a special right, the reverse burden of proof could not be properly vindicated in anything but a judicial forum, and also buttressed that argument by adopting the Securities Exchange Commission argument that in fact that burden in

12(2) was effectively reversed again against the purchaser of the security through the lack of appeal. In fact, because Section 10 of the Arbitration Act is so restrictive, it becomes virtually impossible for someone who loses an arbitration to effectively appeal that decision.

We think that Wilko was very clearly decided on the choices lost under 22(a). And what we are saying basically what Wilko held is exactly what Shearson/American Express told you here two years ago, and really we're not saying anything more than that. They did add to our argument the fact that 10(b) was an implied cause of action.

QUESTION: The Fifth Circuit, Mr. Downey, in its opinion says that you didn't contest the arbitrability of your Exchange Act claims following McMahon. Now, you didn't make an adhesion argument with respect to the Exchange Act claims?

MR. DOWNEY: Well, of course our expectation is that at some point these will be held to be adhesion contracts. Presumably if this Court returns this case to the district court for trial on that issue, on the 12(2) issue, that will happen there.

QUESTION: But it sounds at least from the Fifth Circuit's opinion as if you didn't make any claim

that there simply wasn't any contract under the Exchange Act claim.

MR. DOWNEY: Well, the claim, that claim, is made in the complaint, but that was not a matter that was appealed to the Fifth Circuit. The Fifth Circuit strictly was on the question of 12(2).

Our position is that Wilko should not be overruled. Over and above the broad jurisprudential issues in question, we think, first of all, this is not a constitutional case. The Court has not put Congress in the situation where it can't do anything. This is not one of those cases where Congress has left the development of law to the Court.

This is a very specific, narrow, carefully drawn statute. Congress has acquiesced in this decision for 36 years. As this Court noted in Huddleston, also the fact that when it made its amendments in '75 to the securities laws, plural, there was no change made in the coexistence of Section 11 causes of action and 10(b) causes of action, and we think that argument applies here.

In 1975 Congress, when it changed the arbitration provisions, did not in fact make any changes to the Securities Act. In fact, in '75 in the conference report they specifically endorsed Wilko. And

however pejorative a view one takes as to what that might be, what that might have meant with respect to 10(b)(5), we think it's very clear and express that we adopted -- that Congress adopted Wilko.

And that's exactly what Shearson said to this Court two years ago in McMahon.

We would also point out that recent attempts to make modifications in this area by Congress -- H.R. 4960 attempted to address only the jurisdictional provision of the 1934 Act. No attempt was made to change the '33 Act.

We think that the quality of arbitration is at issue because of the arguments on retroactive application of any change that this Court might make to Wilko, because I think that Respondent will pretty much agree that the key issue here on retroactivity would be whether or not there was a manifest injustice which would be occasioned by retroactive application.

And that would seem to turn on whether or not the arbitration forms can fairly vindicate 12(2) claims. We don't think they can.

What we have said basically more than anything is that there's a lot of things wrong inherently with arbitration. There's nothing that the Securities and Exchange Commission can do to give us an Article III

judge choice, nor to give us a jury.

Our basic position is also that this is the worst possible choice we're being given. We're being given a choice between home court A and home court B. There is an inherent self-interest in those forums. It's Shearson/American Express that gets to pick them. So obviously, if those forums don't give the results that Shearson/American Express wants, they're not going to appear in their form document.

We also think that people who are designated as arbitrators in this case are going to be hired by the exchanges and obviously are self-interested.

The challenge that we threw out to the industries, the securities industry and the arbitration industry, in our McMahon amicus brief was to show us that, notwithstanding obvious inequalities in the procedures of arbitration, that in fact the results were fair.

That challenge has not been answered. What we have in response to that challenge in fact is a three-month study that the industry -- an accountant, an accounting firm, did for the industry, which allowed selected members of that industry to pick their favorite three months to provide a result.

And we think that that's not the -- that's not

the level of proof, for example, that was utilized in overturning Plessy v. Ferguson. That to us is not a serious jurisprudential insight.

As far as the -- a comment needs to be made on the Securities and Exchange oversight. This Court obviously considered that to be of some significance in the McMahon case. We have a problem with that because we wouldn't be here in the first place if the Securities and Exchange Commission had enforced their 15c2-2 rule in the first place.

We find that the Securities and Exchange Commission has been very variable in its protection of investors. One will recall that they appeared against arbitrability in Wilko, they appeared for it in McMahon, and that they have not appeared to take any position in this case whatsoever.

We also have a serious question about whether or not really the Securities and Exchange Commission has authority to change these arbitration rules. It seems to us that the argument that's being made by Respondents is that the '33 Act is not specific enough to override this wide, this virtually unfettered power that parties have under the Arbitration Act to make contracts for arbitration.

And it seems to me that the changes made in

1975 lack that same specificity in giving to the Securities and Exchange Commission the power to generally control SRO's.

We also feel that the Court should give some consideration to protecting the unsophisticated investor. How that could be done is a difficult question, but it may be that perhaps 12(2) claims are less suitable to arbitration where the investors, as here, are really unsophisticated.

We would also like to make the observation that in a sense this case comments upon the relative merits of adjudication and arbitration, and it seems to Petitioners it's somewhat ironic that, after what can only be described as the great history of this Court that has given us one man, one vote, and ended segregation, the principle of judicial review, that there are no true amicus who come before this Court to in fact defend the role of this Court, and really that that defense falls to a somewhat sad group of investors from Brownsville, Texas, whose greatest expectation in all of this is to simply recover their life savings.

Thank you.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Downey.

Mr. Krebsbach.

ORAL ARGUMENT OF THEODORE A. KREBSBACH, ESQ.

ON BEHALF OF RESPONDENTS

MR. KREBSBACH: Thank you, Mr. Chief Justice. May it please the Court:

Petitioners' 12(2) claims can be vindicated in this case at the same self-regulatory organization arbitration forums under the oversight jurisdiction of the Securities and Exchange Commission that this Court found in McMahon were adequate to vindicate claimant's rights under Section 10(b).

QUESTION: Or not vindicated, as the case may be. Or not vindicated, as the case may be. Your point is that it's no better and no worse.

MR. KREBSBACH: Exactly. We believe that there is no reason to distinguish Section 12 and Section 10(b) for purposes of arbitrability, since the Securities Act of 1933 and the Exchange Act of 1934 constitute interrelated components of the federal regulatory scheme governing transactions in securities.

The Securities Exchange Commission agrees that the McMahon holding applies equally to Section 12(2) claims under the Securities Act as it does to Section 10(b) claims under the Exchange Act for SRO forums under the Commission's jurisdiction.

This conclusion is also reached by applying

the Court's traditional analysis which it applied in McMahon for determining the arbitrability of a statutory claim. That is, that the Federal Arbitration Act applies to statutory claims the burden on the party opposing arbitration to show a contrary Congressional intent expressed in the statute, its legislative history, or a conflict between arbitration and the statute.

QUESTION: Has the SEC formally suggested that Wilko be overruled?

MR. KREBSBACH: In their amicus brief, Your Honor, in the McMahon case.

QUESTION: In McMahon.

MR. KREBSBACH: Yes.

QUESTION: They thought that Wilko should be overruled?

MR. KREBSBACH: They did, and they took the position that their oversight jurisdiction would cause 12(2) claims to be arbitrated as well as 10(b) claims.

QUESTION: The Petitioner takes the view, Mr. Krebsbach, that even if it is overruled that it shouldn't apply retroactively to these Petitioners.

MR. KREBSBACH: We disagree, Your Honor, for the same --

QUESTION: But this was signed, these

agreements were signed, before McMahon was decided, were they not?

MR. KREBSBACH: That is true, Your Honor. However, at the time, for example, that the McMahon decision was decided in 1987, the lower courts had extended Wilko's rationale to 10(b). Notwithstanding that, the courts have uniformly retroactively applied the McMahon decisions to pending cases. We feel that under Chevron --

QUESTION: Well, that's a little hard to justify under Chevron, isn't it?

MR. KREBSBACH: Well, under the Chevron test which Your Honor mentioned, we feel that the key test is whether or not there is any prejudice to the plaintiffs. And in light of the fact that this Court --

QUESTION: Let me ask you this. Under the predispute arbitration agreements in this case, would the arbitration have to take place in New York or Texas?

MR. KREBSBACH: It would take place usually in the venue closest to where the plaintiff resides. This venue would be in Texas.

QUESTION: You would concede that it could occur under these agreements in Texas, notwithstanding

the provisions of the agreement?

MR. KREBSBACH: Yes. Not only would we concede that, Your Honor; that has been the practice for as long as I can recall. The arbitration itself will always take place where the claimant resides.

Just to follow up on my prior point as far as whether or not there is any substantive prejudice to the plaintiff, we believe that the Court has articulated time and time again over the past 15 years that a plaintiff does not waive substantive rights in arbitration.

It's not a situation where the Court would be changing a prior decision with respect to a substantive right under the statute. It will simply be changing the forum where the plaintiff's rights will be adjudicated, and all the substantive rights that the plaintiff in this case will have in court they will have in the arbitration forum.

Examining the statute itself, there is nothing in the Securities Act of 1933, any more than there is in the Exchange Act of 1934, which expresses a Congressional intent to prohibit arbitration of Securities Act claims.

The only arguable evidence of such intent was the anti-waiver provision, and this Court in McMahon

ruled that the anti-waiver provision only bars arbitration of Securities Act claims when arbitration is inadequate to protect statutory rights.

Also, with respect to the legislative history, there is nothing in the legislative history, again either in the Securities Act or the Exchange Act, indicating a Congressional intent in 1933 or 1934 to prohibit arbitration of Federal Securities Act claims.

Petitioners' argument is incorrect that Congress expressed such an intent in amendments to Section 28(b) in 1975 in a single sentence in a conferee report which pertained to 28(b), which was an amendment which gave SRO rights, jurisdictional rights, over member-member arbitrations and did not even address the issue of investor-member arbitration.

The single sentence was as follows, that: "It was the clear understanding of the conferees that this amendment did not change existing law as articulated in Wilko v. Swan" with respect to the applicability and enforceability of arbitration agreements between customers and member firms, as opposed to member-members.

It's Petitioners' position that this sentence indicated that Congress in 1975 wished to prohibit arbitration of Securities Act claims. This same

argument was made to the Court in McMahon and was considered and analyzed and rejected by the Court in McMahon, which held that at best Congress indicated in 1975 an intent to leave the Wilko issue to the courts.

Congress never said in this single sentence in 1975 what it thought that the Wilko law was. McMahon has told us that Wilko only bars arbitration of Securities Act disputes when arbitration is inadequate. The arbitration forums before the Court today have been expressly found to be adequate by the Court in McMahon.

A single ambiguous sentence with respect to legislation pertaining to member-member arbitration cannot logically overcome the clear Congressional intent expressed in the Federal Arbitration Act and the Securities Act.

Furthermore, Congress could have simply prohibited arbitration of these disputes very simply in 1985 by including plain language in the amendment to that effect.

And it is also instructive to look at events since the McMahon case was decided in 1987. In 1988 the Congress passed very significant amendments in the Securities Act area. However, although they considered amendments with respect to securities arbitration, they did not enact any such legislation, although they were

aware at the time that lower courts had extended the Court's holding in McMahon to Wilko v. Swan and prohibited -- and allowed arbitration of Section 12(2) claims. Notwithstanding that, no legislation was enacted by the Congress in 1988.

Finally, with respect to the third prong of the test, there is no conflict between arbitration and Section 12(2) and the purposes of that statute, any more than there is with respect to Section 10(b) claims. There would of course be a conflict if arbitration could not effectively carry out the purposes of Section 12(2).

However, the McMahon Court has already ruled that SRO arbitration forums with SEC oversight jurisdiction are adequate.

Since McMahon, it is significant to note that there have been significant changes in the arbitration rules which are designed to improve the process which was approved by the Court in McMahon and further protect investors' rights.

These rules have been adopted by the Security Industry Conference on Arbitration, which is composed of industry and public members, have also been approved by the SRO's themselves, and are pending right now before the SEC, which is holding public hearings. We

anticipate that within the next month these rules will be adopted as they stand or with slight revisions.

The first of these rules has to do with disclosure of the clause itself and would require all the arbitration clauses to be in plain English and specify the procedural rights an investor is waiving by going to arbitration.

Secondly, to address some of the concerns raised by the dissenting opinion in McMahon with respect to a perception of possible bias at SRO forums, a number of rule changes have been proposed. These rules -- these rule changes are in the context of a point made in the dissenting opinion in McMahon that, since the SRO's in effect run these forums, there may be a perception, although unfounded by, unsupported by empirical data, that perhaps the SRO's favor members and there is a bias against investors at these forums.

QUESTION: Does the arbitration clause at issue meet all the requirements of the new rule?

MR. KREBSBACH: The arbitration clause at issue in this case?

QUESTION: Yes.

MR. KREBSBACH: No, Your Honor, it does not. The arbitration clause at issue in this case is the identical arbitration clause that the Court examined in

McMahon.

QUESTION: So it does not conform with the requirements that the SEC is about to adopt in the rules you were just indicating?

MR. KREBSBACH: No, it does not. And in fact, the SEC has not in any way attempted to indicate that any arbitration forms used in the past were not adequate contracts. It's simply in effect, we believe, bending over backwards to address these perception concerns.

QUESTION: So its rules will be prospective?

MR. KREBSBACH: They will apply just to future contracts.

Fundamentally, the issue here is not where the arbitration is held, but whether the arbitrators themselves who decide these cases are fair and whether they're chosen in a fair and impartial manner. And what a number of people have looked at, including the dissenters in McMahon, is whether or not people described as public arbitrators at SRO forums in fact have perhaps contacts with the industry and should be labeled as securities arbitrators.

So what these rules have done is addressed situations perhaps where a spouse of an industry person may have been an arbitrator, and they have ruled those people cannot serve as a public arbitrator, they have to

be labeled as a securities arbitrator. People that are retired, but had recent affiliations with the industry, are no longer labeled under the new rule as a public arbitrator.

Nor do people that have industry ties, such as attorneys representing brokerage firms and other similar situations, are no longer able to be listed as public arbitrators.

In addition, arbitrators must publish previous ten-year biographies, so that people are adequately aware of the background of these arbitrators. And this, combined with the fact that the majority of the arbitrators at SRO forums are always from the public and that the investor has a preremptory challenge and unlimited challenges for cause, we believe, together with the SEC oversight over these rules, ensures that the process will be fair and will be perceived as fair.

QUESTION: Mr. Krebsbach, what does "SRO" stand for? Securities regulatory organization?

MR. KREBSBACH: Exactly, Your Honor. The SRO forums are simply the exchange forums, whether it's the New York Stock Exchange, the NASD, and I believe there are about twelve other exchanges that have arbitration forums.

Shearson, as a member of probably all of these

exchanges, is required to arbitrate at any of those at the selection and choice of the investor in the first instance.

Another perception problem with respect to the arbitration process itself has to do with what is perceived as a limited record for appeal, and it was noted in the dissenting opinion in McMahon that there is no requirement of a transcript at the SRO forums. That has now been changed. A transcript is going to be required under these new rules.

QUESTION: Well, why should we overrule a statutory construction case? Why shouldn't we leave it to Congress? You think just because it's wrong? Because if we go back to overrule all the cases that we now think are wrong, that would be quite an undertaking.

MR. KREBSBACH: We agree, Your Honor. We think that it goes beyond that. There has been a line of cases by this Court during the past 15 years -- Mitsubishi, Scherk, Moses Cone, Southland v. Keating, Byrd, up to and including McMahon, which have addressed this issue of arbitration in a consistent and uniform manner and have articulated an approach to the arbitration of statutory disputes which we feel is inconsistent with that --

QUESTION: Well, we must have thought that Wilko was different. In McMahon we must have thought that 12(2) is different, because we didn't overrule Wilko.

MR. KREBSBACH: It's unclear, Your Honor, because the 12(2) issue --

QUESTION: Well, we didn't overrule Wilko, did we?

MR. KREBSBACH: Well, the 12(2) issue was not before the Court in Wilko, Your Honor.

QUESTION: Well, I know, but if they were the same issues we would have overruled Wilko.

MR. KREBSBACH: Well, it appears --

QUESTION: You say there is no difference.

MR. KREBSBACH: Based on the rationale that the Court used in McMahon, we feel there is no difference, because if you look at the adequacy of the forum to resolve the dispute we feel that an SRO forum with SEC oversight jurisdiction is just as adequate to resolve a dispute under the Securities Act as the Exchange Act.

And it's true, Your Honor, you did not overrule Wilko in McMahon. We believe it was because it was not before the Court.

QUESTION: What if we didn't treat the two the

same? Would one govern, govern the practice? In other words, would the effect of not overruling Wilko be to simply deprive McMahon of all practical effect?

MR. KREBSBACH: No, I think the effect of not overruling Wilko, to the extent that McMahon also stays intact, would be that agreements under the Securities Act would not be arbitrated and agreements under the Exchange Act would.

I don't know if this would be a good policy or would be consistent with Congressional intent. I think it would also cause a lot of confusion with respect to the arbitration of other statutory disputes.

Wilko really stands alone with respect to this Court's arbitration jurisprudence, in that it's really the only case where it in the first instance presumed that the arbitration forum was inadequate.

QUESTION: But it stood alone a long time.

MR. KREBSBACH: Until this Court's decision in McMahon.

QUESTION: And Congress didn't act.

MR. KREBSBACH: Well, what the Court said in McMahon was that Wilko meant that an anti-waiver provision will bar arbitration of disputes under the federal securities laws if arbitration is inadequate. And I believe that the Court in McMahon also said that

Congress has left this issue to the courts because they believe in the first instance it would make no sense for Congress to have to conduct an inquiry on each occasion whether a particular arbitration forum was inadequate.

I think it makes good sense that this issue was left to the courts, and I think Congress has done so.

QUESTION: Why do you think Congress hasn't acted, in view of what you just said?

MR. KREBSBACH: Why they have not acted? I believe subsequent to McMahon it made very good sense for the Congress to leave this issue to the courts, and I believe that they think that the SRO arbitration system is adequate.

It's under the jurisdiction of the Securities and Exchange Commission, which is the Congressional agency which is empowered to protect investors' rights under the Securities Act. I think Congress feels confident that the SEC can do the job in this area.

QUESTION: Going back to the baseball cases, Congress didn't act and we chose not to. Why should we do any different here?

MR. KREBSBACH: Well, if you look at the whole notion of Congressional action by silence, clearly the cases go both ways. I think there have been a lot of

cases where the Court has re-examined precedent and overturned it notwithstanding the fact that Congress has done nothing in the intervening years.

QUESTION: Really, your argument is that the arbitration process is now a process of integrity, and that we should recognize that fact and incidentally take a burden off the federal courts, isn't it?

MR. KREBSBACH: That would be the result. It's not necessarily the reason, but that would be one of the results.

And to answer your question, yes, I think the SRO process is an arbitration process --

QUESTION: Maybe that's the real reason.

MR. KREBSBACH: That it would take away a burden from the courts? I think --

QUESTION: You can't be too proud of some of the things that have happened in the Street in the past decade, can you?

MR. KREBSBACH: There has been a lot of bad publicity during the past five years, there's no doubt about it. However, I should point out again that arbitration proceedings, although they are officially public, that has not prevented investors in the past from going to the press with the results of their arbitration if it was to their benefit.

But more significantly, I think that the Court must rely on the fact that there is SEC oversight in this area and trust the SEC to do the job, and I believe they have.

Going back to the issue of the transcripts, we believe that the fact that there now will be a transcript of these cases and under the new rules the arbitrators must list the issues decided and the damages awarded, and that together with the documents would give an appellate court if necessary a complete evidentiary record to review on a motion to vacate.

The fourth and last issue which is addressed by these new rules is the issue of the adequacy of discovery in arbitration. Now, as everyone knows, one of the positive points about arbitration is that you don't have the unlimited, unfettered discovery of the type that you have in federal court, which oftentimes is abused and which oftentimes results in a lot of the delay and cost of litigation.

Now, the Uniform Code provides certain discovery guidelines which have been approved by the SEC. Practically speaking, an investor can receive any documents from any member firm across the country, whether the firm is a party or not. And the arbitrators have the power to refer for disciplinary proceedings any

member who does not comply with their directives.

As a practical result, if the investor makes an informal demand for documents, if they are not produced they go to the arbitrators, and if the documents are relevant they will direct the parties, the member firms, to produce them.

In addition, the rules now provide for a prehearing conference where any prehearing discovery disputes can be resolved. And in addition, the attorneys have the same subpoena power that they would have under law.

Finally, with respect to depositions, the arbitrators will now have the power to direct depositions in cases where they feel they are appropriate.

As McMahon correctly held, there is no conflict between the Arbitration Act and the purposes of the securities laws. We as Respondents would argue that the combination of the arbitrator expertise at SRO forums combined with the control by the arbitrators of the oftentimes abused discovery process will in many cases make arbitration a preferred means of dispute resolution for investors.

While the Court does not have to expressly overrule Wilko to find in favor of Respondents in this

case -- it can hold simply that it will follow the McMahon rationale with respect to SRO arbitrations which are adequate -- Respondents believe that the stare decisis doctrine is best served by the Court ruling that McMahon is no longer good law.

If Wilko is overruled, there will be a consistent interpretation and application by this Court of the Federal Arbitration Act in numerous decisions over the past 15 years. This will allow individuals to predict outcomes in similar cases.

In addition, the stare decisis objective of preventing constant relitigation of similar issues with respect to other statutory claims will also be served.

QUESTION: Well, that depends on what other kinds of arbitration there can be. Are there any other kinds of arbitration that could possibly be written into an agreement that would come under the Acts?

MR. KREBSBACH: Yes, conceivably a document could list virtually any arbitration forum whatsoever.

QUESTION: So what do we do with those? With respect to those, all these nice arguments you've been making to us about how good the SRO arbitration is would be irrelevant, wouldn't they?

MR. KREBSBACH: They would, you're absolutely right.

QUESTION: So how predictable would that case be?

MR. KREBSBACH: I think what the Court should do to address that situation is in the first instance assume that the forum will be adequate. I think there are sufficient statutory safeguards in place to address the adequacy --

QUESTION: You want us to interpret the statute so that only good arbitration is exempted from it, bad arbitration is not exempted from it?

MR. KREBSBACH: I wouldn't use the terms "good" and "bad," but arbitration that's adequate to protect statutory rights should be allowed and arbitration that isn't should not be allowed.

QUESTION: Well, I think any arbitration that would pass muster in judicial review as being rudimentarily fair and not being set aside by judicial review is good enough arbitration, I would presume. I mean, I can't see reading the statute -- you read the statute to say arbitration is part of the rights that you can't waive or it isn't.

We can't possibly pick and choose among various types of arbitration, can we?

MR. KREBSBACH: I do agree with you, Your Honor. I think that there should be a presumption that

arbitration is adequate and that there are adequate statutory safeguards, in those cases where during the course of the hearing itself it is demonstrated not to be the case, to then make a motion to vacate and have the award overturned.

I don't think it makes sense for the court to have to examine in the first instance the adequacy of the forum prior to having an arbitration hearing. I think that goes against the Congressional intent behind the Arbitration Act in enforcing the parties' contracts to have a swift resolution of their dispute.

If Wilko is overruled, the Court will create uniformity in its interpretation of the Federal Arbitration Act and also reject an outdated precedent in light of its cases over the past 15 years.

In conclusion, Respondents ask this Court to affirm the unanimous decision of the Fifth Circuit Court of Appeals enforcing the parties' agreement to arbitrate their Section 12(2) dispute.

This will also avoid the result in this case where the Petitioners' 12(2) claims will proceed in federal court while their other claims under RICO, Section 10(b) of the Exchange Act, and common law claims will proceed in arbitration. Such a result we feel makes for bad policy and thwarts the Congressional

intent in the Federal Arbitration Act, as would any ruling that distinguishes between different sections of the Securities Act and/or the Exchange Act for purposes of arbitrability.

Unless the Court has questions, I have nothing further.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Krebsbach.

Mr. Downey, do you have rebuttal?

REBUTTAL ARGUMENT OF DENIS A. DOWNEY, ESQ.,
ON BEHALF OF PETITIONERS

MR. DOWNEY: Yes, Mr. Chief Justice.

Some comments have been made about the changes that have been proposed by the Securities and Exchange Commission. First of all, we're two years post-McMahon and we haven't had those.

But there are two things that those changes do not address that are critical. The one is they're not going to require arbiters, arbitrators, to give legal reasons for their decisions, and that's going to make it very difficult to effectively appeal those decisions.

The second and most critical thing it doesn't address is the selection of the panels for arbitration. The truth is that we think the industry cheats. The industry says they have 500 people that can hear these

cases, but in fact they have pre-selected a group who, based on the history of prior arbitrations, are going to give the result that they want.

So when we go to arbitration we have a choice in fact between 15 people who are going -- who have a bias against us, a proven bias. And it's not a question of public or non-public arbitrator; it's a question of what their track record is, that only the NASD knows or only the NYSE knows.

In response to Justice O'Connor's question, the venue in these cases on arbitration is Dallas, which is a distance of some 500 miles from where these people live.

The other thing that I think is significant is that, in relation to what Congress said in 1975, this Respondent said to this Court at page 17 of the McMahon brief: "The plain meaning of this language expresses Congressional intent that the 1975 amendments not change the Wilko holding that claims arising under Section 12(2) of the Securities Act are non-arbitrable."

It seems that the securities industry is here selling this Court arbitration once again. In fact, they will say anything that suits their purposes.

We don't trust securities arbitration. If Mr. Krebsbach were to go outside in the hall and offer to

enter into an agreement to arbitrate that wasn't an SRO arbitration, we'd be much more inclined to do so. We think that the worst possible option for investors is to be thrown into SRO arbitration.

And also, it's true that really, that these are just part of the problems that are affecting this whole industry. And as the Court has noted, there are other problems in the commodities field, and they are sooner or later going to have to be addressed here as well.

We think that the intent of Congress is clear and, though it may be inconvenient to split the claims, if we are true to what the cases have said, we look at each individual statute and we decide what in fact the Congressional intent was. That decision was made in 1953 by the Wilko Court and this Court should adhere to that decision.

Thank you.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Downey. The case is submitted.

(Whereupon, at 10:50 a.m., oral argument in the above-entitled case was submitted.)

CERTIFICATION

Alderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of The United States in the Matter of:

No. 88-385 - OFELIA RODRIGUEZ de QUIJAS, ET AL., Petitioner V. SHEARSON/ AMERICAN EXPRESS, INC., ETC.

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BY Judy Freilicher

(REPORTER)