

Arbitration Vacatur: The Supreme Court Bars One Route and Muddles the Other—Manifest Mistake Is Dead!

In my article, *The Arbitrator Blew It! Now What?*¹ I commented critically about the growing disposition of courts to vacate arbitral awards that have “manifestly” disregarded the law, even though this criterion is not specifically spelled out as a vacatur ground in the Federal Arbitration Act (FAA)² or any comparable state statute.

At the same time that courts by judicial fiat had been vacating awards that “manifestly” disregarded the law, parties themselves began contracting to expand the scope of judicial review to that akin to recognized common law precepts. Federal courts were “split over the exclusiveness of [the] statutory grounds when parties take the FAA shortcut to confirm, vacate, or modify an award, with some saying the recitations are exclusive, and others regarding them as mere threshold provisions open to expansion by agreement.”³ The Supreme Court in this case has now settled the issue: such agreements are invalid; arbitral awards may be vacated only for the reasons exclusively spelled out in Sec. 10 of the FAA. *Hall Street* also signifies very strongly (and post-*Hall* federal decisions unanimously have held) that “manifest disregard” of the law no longer is a basis for vacating arbitration awards.

In *Hall*, a bench trial had upheld the tenant’s (Mattel’s) right to terminate its lease. The parties, with the district court’s approval and order, then agreed to arbitrate the landlord’s claim for cleanup expenses, agreeing further that the resulting award could be vacated, modified, or corrected “if the arbitrator’s conclusions of law were erroneous.” An award for Mattel first was vacated, the district court applying the agreement’s legal review standard in accordance with the Ninth Circuit’s earlier ruling in *LaPine Technology Corp. v. Kyocera Corp.*⁴ On remand, the arbitrator then ruled for *Hall* (the landlord) and the award was confirmed by the district court. The Ninth Circuit reversed, this time on the strength of *Kyocera Corp. v. Prudential*,⁵ which overruled *LaPine* and held that contracts changing the mode

of judicial review were unenforceable. The Supreme Court affirmed, the six justice majority finding that the Federal Arbitration Act, 9 U.S.C. Secs 9-11, deliberately limited vacatur only to the grounds specifically provided therein. The holding is clearly mandated by the text of the statute, which, in accordance with traditional principles of statutory construction, must be strictly construed.

9 U.S.C. Sec. 10(a) lists only four bases for vacating: (1) if procured by corruption, fraud, or undue means; (2) where there was evident partiality or corruption in the arbitrators; (3) where the arbitrators were guilty of misconduct; or (4) where they exceeded their powers. Sec. 11 permits modification only where “there was an evident miscalculation of figures or evident material mistake.” Otherwise, the court “must” (not “may”) confirm! 9 U.S.C. Sec. 9 and 12 V.S.A. Secs. 5677-5678 are virtually the same.⁶ As *Hall Street* declared:

... [T]he text compels a reading of the Sections 10 and 11 categories as exclusive. To begin with, even if we assumed Sections 10 and 11 could be supplemented to some extent, it would stretch basic, interpretive principles to expand the stated grounds to the point of evidentiary and legal review generally. Sections 10 and 11, after all, address egregious departures from the parties’ agreed-upon arbitration: ‘corruption,’ ‘fraud,’ ‘evident partiality,’ ‘misconduct,’ ‘misbehavior,’ ‘evident partiality,’ ‘exceed(ing) ... powers,’ ‘evident material miscalculation,’ ‘evident material mistake,’ ‘awards upon a matter not submitted’ ... Given this emphasis on extreme arbitral conduct, the old rule of *ejusdem generis* has an implicit lesson to teach here. Under that rule, when a statute sets out a series of specific items ending with a general term, that general term is confined to covering subjects comparable to the specifics it follows. Since a general term included in the text is normally so limited, then surely a statute with no textual hook for expansion cannot authorize contracting parties to supplement

review for specific instances of outrageous conduct with review for just any legal error ... ‘Fraud’ and a mistake of law are not cut from the same cloth.⁷

Dissenting, Justice Stevens wrote: “Sections 10 and 11 are best understood as a shield meant to protect parties from hostile courts, not a sword with which to cut down parties’ valid, irrevocable and enforceable agreements to arbitrate their disputes subject to judicial review for errors of law.”⁸ The majority disagreed. For the expedient of arbitration and its more flexible procedural and evidentiary rules and speedy confirmation process, parties sacrifice among other things the traditional standard of appellate review. Expanding the scope of judicial review undercuts the basic premise of arbitration, namely “that the arbitration process may be more expeditious and less costly than ordinary litigation.”⁹ In a footnote, Justice Stevens conceded that “Congress significantly limited the grounds for judicial vacatur or modification ... in order to protect arbitration awards from hostile and meddlesome courts.”¹⁰ An opposite result, as the *Hall* majority pointed out, would “open the door to the full-bore legal and evidentiary appeals that can render informal arbitration merely a prelude to a more cumbersome and time-consuming judicial review process.”¹¹

Hall did leave a way out. “The FAA is not the only way into court for parties wanting review of arbitration awards: “[T]hey may contemplate enforcement under state statutory¹² or common law, for example, where judicial review of different scope is arguable.”¹³ But if they resort to the FAA, they are limited to the statutory bases for vacatur or modification.

Hall and “Manifest Disregard”

This non-statutory “manifest disregard” basis for vacating arbitration awards stems from unsupported dicta in *Wilko v. Swan*¹⁴ and *First Options of Chicago v. Kaplan*,¹⁵ which virtually every federal circuit court—but not

at least eight states¹⁶—had adopted as a new, non-statutory basis for vacating arbitration awards. Even our Vermont Supreme Court in *Shahi v. Ascend Financial Services*¹⁷ and *Muzzy v. Chevrolet Div.*,¹⁸ relying upon now outmoded but then prevailing Second Circuit law, seems to have ill-advisedly accepted this criterion, without taking note of its origin.

Hall argued with some logic that “expandable judicial review” beyond the statutory criteria was the law, given the virtually unanimous willingness of circuit courts to upset awards where the arbitrator had “manifestly” disregarded the law. If the courts can expand the scope of judicial review of an award for non-statutory reasons like “manifest mistake,” then, the argument went, surely parties on their own could contractually agree to do so.

The *Hall* majority, however, refused to accept as a given the proposition that *Wilko* had indeed created a new non-statutory vacatur ground. First of all, the majority pointed out, *Wilko* did not decide that “manifest disregard” was a valid basis for vacatur, although “it is true that the Court’s discussion includes some language arguably favoring *Hall Street*’s position” but “arguable is as far as it goes.”¹⁹ *Wilko*, the Court noted, hardly could be viewed as expanding the scope of judicial review since it stressed that “the power to vacate an award is limited” before going on to add that “interpretations of the law by the arbitrators in contrast to ‘manifest disregard’ (of the law) are not subject ... to judicial review.”²⁰ *Hall* “reads this statement as recognizing ‘manifest disregard of the law’ as a further ground for vacatur on top of those listed (in the FAA) and some Circuits have read it the same way ... and sees this supposed addition to Sec. 10 as the camel’s nose: if judges can add grounds to vacate ... so can contracting parties.”²¹

But, this is too much for *Wilko* to bear. Quite apart from its leap from a supposed judicial expansion by interpretation to a private expansion by contract, *Hall Street* overlooks the fact that the statement it relies on expressly rejects just what *Hall Street* ask for here, general review for an arbitrator’s legal errors. Then there is the vagueness of *Wilko*’s phrasing. Maybe the term “manifest disregard” was meant to name a new ground for review, but maybe it merely referred to the Sec. 10 grounds collectively, rather than adding to

them, ... or ... “manifest disregard” may have been shorthand for Sec. 10(a)(3) or Sec. 10(a)(4), ... authorizing vacatur when the arbitrators were “guilty of misconduct” or “exceeded their powers.” We, when speaking as a Court, have merely taken the *Wilko* language as we found it, without embellishment ... and now that its meaning is implicated, we see no reason to accord it the significance that *Hall Street* urges.²²

Although not squarely putting “manifest disregard” to bed, *Hall Street* by its emphasis on the exclusivity of the FAA Sec. 10 bases for vacating awards, surely has signaled that “manifest disregard” no longer is a valid principle for vacating arbitration awards, and post-*Hall Street* decisions unanimously have so held.

As of this writing (mid-August, 2008), a quick Lexis search uncovers over sixty federal court decisions citing *Hall Street* and denying applications to vacate arbitration awards. Not one has applied or recognized as still viable the “manifest disregard” test.

Both before²³ and after *Hall Street* some courts finessed the issue by viewing the “manifest disregard” standard [as] cabined entirely within 9 U.S.C. Sec. 10(a)(4) (arbitrators exceeded their powers).²⁴ Another district court “will view ‘manifest disregard of law’ as judicial interpretation of the Section 10 requirements, rather than as a separate standard of review.”²⁵ The Supreme Court in *Hall Street*, in the quotation above, so suggested. Even under this approach, however, it is clear that “manifest disregard” no longer is a separate basis for vacatur.

Most post-*Hall* federal courts including, importantly, the Second Circuit,²⁶ on which the Vermont Supreme Court relied in *Shahi*, have specifically rejected “manifest disregard” as a vacatur criterion, because *Hall*, although not specifically so holding, stressed so emphatically the exclusiveness of the FAA Sec. 10 vacatur remedies.²⁷

The Vermont Supreme Court in *Shahi* and *Muzzy*, found no “manifest disregard of the law,” but only after an extensive review of the record. Given *Hall Street* and the unanimous conclusions of post-*Hall* federal decisions, we should anticipate that Vermont courts no longer will scrutinize vacatur applications on this basis, but hold fast to the specific statutory criteria.

As one commentator wrote several years ago, it is time to bury “manifest

disregard” of the law as a basis for vacating an arbitral award.²⁸ Even at best it demanded a thorough judicial review of the arbitration record, as our Supreme Court in *Shahi* was required to conduct, thus defeating the arbitration desideratum of expedient resolution of controverted issues. At worst, it meant no more than what a court subjectively decided it meant.

If the term means no more than the statutory grounds—“misconduct” or “exceeding their powers”—as *Hall* and others have suggested, we do not need it. If “manifest disregard” means something else—another reason beyond those enumerated in Section 10 of the FAA—it no longer is a permitted remedy for an arbitrator’s alleged mistakes. If the parties really want to preserve a right to appeal an arbitration award on traditional grounds, they might just as well litigate.

May “manifest disregard of the law” rest in peace!

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¹ Vt. B.J., summer 2003, at 39.

² 9 U.S.C. Sec. 10(a).

³ *Hall Street Associates v. Mattel*, 128 S. Ct. 1396, 1403 (2008).

⁴ 130 F.3d 884, 889 (9th Cir. 1997).

⁵ 341 F.3d 987 (9th Cir. 2003).

⁶ See *Shahi v. Ascend Financial Services*, 179 Vt. 434, 439, 898 A.2d 116 (2006) for the minimal differences between the FAA and Vermont Arbitration Act.

⁷ 128 S.Ct. at 1404.

⁸ 128 S.Ct. at 1409.

⁹ 128 S.Ct. at 1409, n.3.

¹⁰ 128 S.Ct. at 1409.

¹¹ 128 S.Ct. at 1405.

¹² See, e.g., N.J.S. 2A: 23(B)-4(c), which permits “the parties (to expand) the scope of judicial review of an award by expressly (so) providing.” Why they would want to do so, instead of selecting ordinary litigation or alternatively ADR is another matter. C.J. Wilentz of the New Jersey Supreme Court commented: “I doubt if many will. And if they do, they should abandon arbitration and go directly to the law courts.” *Perini Corp. v. Grete Bay Hotel & Casino Inc.*, 129 N.J. 548-49, 610 A.2d 364 (1992).

¹³ *Hall*, 78 S. Ct. at 1406.

¹⁴ 346 U.S. 427, 436 (1953). *Wilko* invalidated agreements to arbitrate securities claims, a holding ironically overruled by *Rodriguez v. Shearson*, 490 U.S. 477 (1989). In a footnote dictum, the court in contrasting the very limited bases for vacating an arbitral award and the standard for reviewing a court judgment, noted: “the interpretation of the law by the arbitrators

in contrast to “manifest disregard” are not subject, in the federal courts, to judicial review” (italics added).

¹⁵ 514 U.S. 938, 948-9 (1995). In deciding if the court or the arbitrator decides whether a dispute is arbitrable, *First Option* commented how important this issue was because an arbitration award can be upset only under “unusual circumstances,” namely for the reasons set forth in Sec. 10 of the FAA and “in the event of ‘manifest disregard’” of the law, citing without further comment, *Wilko’s* observation in n. 14 *supra*. Neither *Wilko* nor *First Option* cited precedent for their *dicta*.

The New York Court of Appeals defined “manifest mistake” in its most stringent form: “‘manifest disregard’ of law ... is a ‘severely limited doctrine of last resort limited to the rare occurrences of apparent ‘egregious impropriety’ on the part of the arbitrators ...’ where none of the provisions of the FAA apply.” *Wien & Malkin v. Helmsley-Spear*, 6 N.Y.3d 471, 480, 846 N.E. 3d 1201 (2006) (italics added, citations omitted). To vacate on this ground, the court must conclude “(1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether and (2) the law ignored ... was well defined, explicit, and clearly applicable to the case.” Even if the arbitrator is arguably construing or applying the contract and acting within the scope of his authority, that a court is convinced he committed serious error does not suffice to overturn his decision.” *Wien* at 6 N.Y.3d 481 (citations omitted). See *The Arbitrator Blew It*, *supra* note 1, at 41-2 for other courts’ explanations and the attempt by the National Conference of Commissioners on Uniform State Laws to clarify “manifest disregard.”

Wien at n. 11, emphasized that in the period 1960-2003 New York had vacated only four out of forty-eight awards where “manifest disregard” had been alleged, and all but one involved decisions where the arbitrators had exceeded their powers, which, as noted in the text, is a statutory ground for vacatur. As the above quotation indicates, the Court of Appeals conceded that “‘manifest disregard’ of the law” is not a statutory ground. *Wien* is a good example of how the arbitration desideratum—quick, expeditious resolution of disputes—is thwarted when the courts start to wrestle with arbitrators’ perceived “manifest disregard” of the law. Five years elapsed between the panel’s award and the Court of Appeals decision.

¹⁶ They are chronicled in *Coors v. Cabot*, 114 P.2d 60, 63, 2004 Colo. App. LEXIS 2306 (20-04), *cert. denied*, 2005 Colo. LEXIS 507 (2005). The Colorado Court of Appeals expressed very clearly the rationale for rejecting the “manifest disregard” thesis: “[The arbitration statute] is in derogation of the common law and must be strictly construed ... [I]t is not for this court to impose an additional, non statutory ground (for vacatur) ... Conspicuously missing from this [arbitration] statute is a provision that permits a court to vacate a judicial award when the arbitration panel has exhibited a “‘manifest disregard” of the law.” 114 P.2d at 65.

Tretina Printing v. Fitzpatrick & Assocs.,

135 N.J. 349, 640 A.2d 788, 793 (N.J. 1994): “Arbitration awards may be vacated only for fraud, corruption or similar wrongdoing on the part of the arbitrators.” *Cf. Perini v. Great Bay Hotel*, 129 N.J. 479, 548-9 (1992) where Chief Justice Wilentz disagreed with the thesis supported by three majority justices and two dissenting justices that an award could be set aside if procured by “undue means.” He castigated “overly intrusive review of arbitration awards” and “the steady deterioration of the deference which should be paid to arbitration decisions.” Both *Tretina* and Chief Justice Wilentz in *Perini* felt that the parties by contract could opt for a different standard of review than those set forth in the Uniform Arbitration Act. So did the Colorado appellate court in *Coors*, 114 P.2d at 95. As the text makes plain, *Hall v. Mattel* rejects this thesis, although New Jersey and other states have by statute permit it.

¹⁷ 179 Vt. 434, 898 A.2d 116 (2006). Asked to vacate an arbitration award, the Vermont Supreme Court first admonished: “Plaintiffs must satisfy at least one of the [statutory] criteria triggering ... vacating of an arbitration award ... [We] confine our review to (1) whether there exist statutory grounds for vacating or modifying the arbitration.” 179 Vt. at 439. But belying this caveat, the Supreme Court in considering whether the arbitrator had misapplied Vermont law on compensatory damages, wrote: “A party’s mere conjecture, however, is not sufficient to demonstrate that an arbitration panel exhibited “manifest disregard” of the law” (italics added), citing the prevailing rule in the Second Circuit, *Merrill Lynch v. Bobker*, 808 F.2d 930, 933 (2d Cir. 1986). As the text notes, Second Circuit district courts agree this is no longer the law.

Shahi challenged application of the manifest mistake doctrine. If the issue is squarely presented, one would hope that our Supreme Court would reexamine its position in the light of *Hall Street*.

¹⁸ 153 Vt. 179, 184

¹⁹ 128 S.Ct. at 1403 (italics added).

²⁰ 128 S.Ct. at 1403.

²¹ *Id.* (italics added).

²² *Id.* at 1404 (italics added).

²³ See *The Arbitrator Blew It*, *supra* note 1, at 40 and n. 46.

²⁴ See *Wise v. Wachovia Sec.*, 450 F.3d 265, 268-9 (7th Cir. 2006). *Stevens & Co v. Cikanek*, 2008 U.S. Dist. LEXIS at p. 11 (N.D. Ill. 2008). At least one court in the Second Circuit has adopted this approach even after *Hall Street*. *Mastec North America v. MSE Power Systems*, 2008 U.S./ Dist. LEXIS 52205, *4-5 (N.D. N.Y. July 8, 2008).

²⁵ “The Supreme Court’s holding in *Hall Street* limits the application of ‘manifest disregard of the law’ to the Section 10 bases,” *Mastec North America*, 2008 U.S. Dist. LEXIS 52205, at *9.

²⁶ *Rosen Associates v. Webb*, 2008 U.S. Dist. LEXIS 51446, p. 8-9: “Relying on *dicta* from ... *Wilko* ... the Second Circuit has held that ‘manifest disregard’ of the law by the arbitrators provides a basis for vacatur” [citing *Merrill Lynch*, *supra* at n. 17, on which the Vermont Supreme Court relied in *Shahi*, *supra* n. 17] ... However,

the Supreme Court ... in *Hall Street* has recently held that the FAA’s additional judicial narrow statutory grounds [for] vacatur are exclusive ... As the Second Circuit’s traditional understanding of *Wilko* and Sec. 10—that *Wilko* endorsed “manifest disregard” and that Section 10’s grounds are not exclusive—is inconsistent with the basis for the holding in *Hall Street*, the Court finds that the ‘manifest disregard’ of the law standard is no longer good law.”

To the same effect: In the Matter of the Arbitration between Supreme Oil Co., et al. v. Supreme Oil Company, Inc, 2008 U.S. Dist. LEXIS 58029, p. 8 (S.D. N.Y. July 31, 2008).

²⁷ See, e.g., *Horving Ramos-Santiago v. UPS*, 524 F.3d 120, 124 (1st Cir. April 24, 2008) (“This Court has recognized a very limited exception under which we may vacate an arbitration award when ... the arbitrator acted in “manifest disregard” of the law’ [but] manifest disregard of the law is not a valid ground for vacating ... an arbitral award in cases brought under the FAA” (citing *Hall Street*)); *Peregrin v. Fassar*, 2008 U.S. Dist. LEXIS 47570, p. 5 (June 19, 2008) (“An award may be vacated only if it satisfies one of the statutory grounds set out in 9 U.S.C. Sec. 10(a)” (italics added, citing *Hall Street*)); *Wood v. Penntex Resources et al.*, 458 F. Supp. 2d 355 (S.D. Tex. June 27, 2008) at n. 4 (“*Hall Street* overrules Fifth Circuit precedent establishing ‘manifest disregard’ ... as an additional ground for vacatur distinct from the explicitly enumerated statutory grounds ... ”); *ALS & Associates v. AGM*, 8 U.S. Dist. LEXIS 42641 at 10, (citing *Horving*); *Prime Therapeutics v. Omnicare*, 555 F. Supp. 2d. 993 (D. Minn. May 21, 2008), 2008 U.S. Dist. LEXIS 41306 at 15 (Does *Hall Street* “suggest that courts can no longer vacate an arbitration award based on judicially-created grounds such as “manifest disregard” of the law? After *Hall Street* this Court believes the answer to that question is yes.”); *Wood v. Penntex Resources*, 2008 U.S. Dist. LEXIS 50071, at 21, n.4 (June 27, 2008) (“*Hall Street* overrules Fifth Circuit precedent establishing ‘manifest disregard’ of clearly applicable law as an additional ground for vacatur distinct from the explicitly enumerated statutory grounds.”); *National Resort v. Cortez*, 2008 U.S. App. LEXIS 10560, *1 (5th Cir. 2008) (“[D]istrict courts must review an arbitrator’s findings of fact and conclusions of law under the highly deferential standard set forth in 9 U.S.C. Sec. 10(a)” (followed by *National Resort v. Rachel Cortez*, 2008 U.S. Dist. LEXIS 55745, 4 and n. 2 (“The court interprets the mandate of the Fifth Circuit [in *National Resort*, *supra*] to be a directive ... to review the record ... to determine whether there should be a vacatur of the arbitrator’s awards under the standard set forth in Sec. 10(a) ... [T]he Fifth circuit’s directive on remand precludes use of [any other review standards] or the making of a decision based on public policy” (italics added)).

²⁸ *The time has come for the U.S Supreme Court to bury the misconceived doctrine of “manifest disregard” of the law*, 16 Am. REV. INT’L ARB. 211 (2005).