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## End of an Error: Replacing Manifest Disregard with a New Framework for Reviewing Arbitration Awards, The

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# THE END OF AN ERROR: REPLACING “MANIFEST DISREGARD” WITH A NEW FRAMEWORK FOR REVIEWING ARBITRATION AWARDS

KENNETH R. DAVIS\*

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## I. INTRODUCTION

Anyone who has walked into a courthouse knows that litigation carries a heavy price tag. Lawsuits take a lot of time and cost a lot of money. Rights that abound in litigation not only protect parties but also burden them. The American judicial system is replete with discovery, motion practice, and appeals that can prolong cases for years and result in astronomical attorneys' fees.<sup>1</sup> Arbitration is a way out of the courthouse. It is a voluntary method of alternative dispute resolution that enables the parties to a conflict to avoid the wasteful complexities of the judicial system.<sup>2</sup> There is a price tag here too: sacrificing procedural and substantive rights.

Passed in 1925, the Federal Arbitration Act ("FAA")<sup>3</sup> repudiated a history of judicial hostility toward arbitration and made arbitration agreements enforceable.<sup>4</sup> This pro-arbitration statute sought to afford merchants and businesspersons such as the buyers and sellers of textiles, produce, and raw materials an efficient alternative to litigation.<sup>5</sup> No one could have imagined that arbitration would evolve into a forum where the submission of securities law claims and civil rights claims would become commonplace. The trend of arbitrating federal statutory claims caused a battle of conflicting policies. The policies advanced in securities law, civil rights law, and other federal statutes argued for significant court involvement in the arbitral process. One of the fundamental policies of the FAA—promoting efficiency in arbitration—argued for limited court participation.

Virtually everyone agreed that the courts had to have some role in reviewing awards for procedural improprieties. No one could seriously quarrel with empowering courts to vacate awards issued by corrupt arbitrators or arbitrators who

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<sup>1</sup> See Kenneth R. Davis, *A Model for Arbitration: Autonomy, Cooperation and Curtailment of State Power*, 26 *FORDHAM URB. L.J.* 167, 167-68 (1999) [hereinafter "*A Model for Arbitration*"] (pointing out abusive litigation tactics that raise fees and consume time); Jethro K. Lieberman & James F. Henry, *Lessons from the Alternative Dispute Resolution Movement*, 53 *U. CHI. L. REV.* 424, 427 (1986) (remarking that discovery can delay cases for years); Arthur R. Miller, *The Adversary System: Dinosaur or Phoenix*, 69 *MINN. L. REV.* 1, 9 (1984) (lambasting attorneys for abusing discovery to delay lawsuits).

<sup>2</sup> Edward Brunet & Jennifer J. Johnson, *Substantive Fairness in Securities Arbitration*, 76 *U. CIN. L. REV.* 459, 462 (2008) (describing arbitration as an informal and private adjudicatory process "involving reasoned presentations of proof to one or more expert arbitrators.").

<sup>3</sup> 9 U.S.C. § 1-16 (2006).

<sup>4</sup> See Part IV.A *infra* (discussing the ouster-of-jurisdiction doctrine).

<sup>5</sup> See Part IV.C *infra* (discussing the role of arbitration at the time the FAA was enacted).

denied parties fair hearings.<sup>6</sup> Disagreement focused on the scope of judicial review for errors of law committed by arbitrators. Some commentators have argued that because arbitration is a substitute for litigation, the courts should exercise at least some review of substantive errors of law.<sup>7</sup> Others have countered that the policy of efficiency, which animates arbitration, forecloses judges from meddling with arbitration awards.<sup>8</sup>

Decided in 1953, *Wilko v. Swan*<sup>9</sup> was the first case to address this conflict. In *Wilko*, the United States Supreme Court refused to allow the arbitration of federal securities fraud claims brought under § 12(2) of the Securities Act of 1933.<sup>10</sup> Defending its holding that public policy forbade arbitrators to decide such claims, the Court observed in dicta that the narrow scope of judicial review of arbitration awards was too meager to ensure that the rights provided in § 12(2) would protect victims of securities fraud.<sup>11</sup> The *Wilko* opinion suggested that a court could not vacate an award for errors “in the interpretations of the law by arbitrators” unless the errors showed “manifest disregard” of the law.<sup>12</sup> Although the Court’s nebulous comment offered scant guidance on what it meant by “manifest disregard,” this puzzling phrase so impressed the federal courts that one by one they adopted manifest disregard of the law as a narrow standard of review for errors of law in arbitration awards.<sup>13</sup> The most common view of the doctrine was that an arbitrator

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<sup>6</sup> See Federal Arbitration Act (FAA), 9 U.S.C. § 10(3) (2006). Section 10 of the FAA provides that a district court, upon motion, may vacate an award:

- (1) where the award was procured by corruption, fraud, or undue means;
- (2) where there was evident partiality or corruption in arbitrators, or either of them;
- (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or
- (4) where the arbitrators exceeded their powers, or so imperfectly executed them so that a mutual, final, and definite award upon the subject matter submitted was not made.

9 U.S.C. § 10 (2006).

<sup>7</sup> See Part IV.C, D & E *infra* (arguing that plenary review for errors of law should apply to cases where awards decide claims asserting federal statutory rights).

<sup>8</sup> *Id.*

<sup>9</sup> *Wilko v. Swan*, 346 U.S. 427 (1953), *overruled on other grounds by* *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 484 (1989).

<sup>10</sup> *Wilko*, 346 U.S. at 438.

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 436-37.

<sup>13</sup> See *Coffee Beanery, Ltd. v. WW, L.L.C.*, 300 F. App’x 415, 421 (2008) (listing circuit court cases that adopted the manifest disregard standard); Michael A. Scodro, *Deterrence and Implied Limits on Arbitral Power*, 55 DUKE L.J. 547, 567 (2005) (reporting that all the federal circuits adopted the manifest disregard standard).

manifestly disregarded the law when the arbitrator knew controlling law and intentionally flouted it.<sup>14</sup>

Applied to all awards, this blanket standard of review is inappropriate for protecting federal statutory rights such as those afforded in securities law and civil rights law. The standard has also proven unworkable. Arbitrators ordinarily do not provide written explanations for their awards, so courts are left to speculate on whether arbitrators intentionally flouted the law or merely misunderstood it.<sup>15</sup> Even if an arbitrator writes a decision, he or she will conceal having intentionally disregarded the law, for such an admission would bring judicial rebuke and the outcome that all arbitrators dread—vacatur of the award.

Over succeeding decades arbitration became more and more prevalent. *Wilko*'s legacy of prohibiting the arbitration of federal statutory claims became an anachronism. Supporting this change, the Supreme Court held in *Shearson v. McMahon*<sup>16</sup> that securities fraud claims brought under § 10(b) could be arbitrated.<sup>17</sup> To justify its holding, the Court needed to refute the very point it had relied on in *Wilko*—that the scope of review of arbitration awards does not safeguard the rights of victims of securities fraud. Seeming to repudiate the manifest disregard standard, the *McMahon* Court declared that the scope of review is sufficient to ensure that the requirements of the Act are enforced.<sup>18</sup> Nevertheless, the federal judiciary, with few exceptions, continued to apply the manifest disregard standard as if the high Court had never decided *McMahon*.

Years later, in *Hall Street Assocs., L.L.C. v. Mattel, Inc.*,<sup>19</sup> the Supreme Court held that the FAA provides the exclusive grounds for judicial review of arbitration awards.<sup>20</sup> Therefore, an arbitration agreement could not expand the grounds for

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<sup>14</sup> See, e.g., *B.L. Harbert Int'l, LLC v. Hercules Steel Co.*, 441 F.3d 905, 910 (11th Cir. 2006) (stating that the manifest disregard standard permits vacatur where there is "clear evidence that the arbitrator was 'conscious of the law and deliberately ignore[d] it.'"); *Flexible Mfg. Sys. Pty. Ltd. v. Super Prods. Corp.*, 86 F.3d 96, 100 (7th Cir. 1996) (requiring a deliberate error of law to justify vacatur); *Mich. Mut. Ins. Co. v. Unigard Sec. Ins. Co.*, 44 F.3d 826, 832 (9th Cir. 1995) (stating that a court may vacate an award under the manifest disregard standard where the arbitrator "recognized the applicable law and then ignored it."); *Merrill Lynch, Pierce Fenner & Smith v. Bobker*, 808 F.2d 930, 933 (2d Cir. 1986) (interpreting manifest disregard to mean that the arbitrator knew the law and intentionally ignored it); Stephen L. Hayford, *Law in Disarray: Judicial Standards for Vacatur of Commercial Arbitration Awards*, 30 GA. L. REV. 731, 816-17 (1996) (describing the manifest disregard standard as requiring an intentional error of the arbitrator).

<sup>15</sup> See Scodro, *supra* note 13, at 604 (noting that "a written award [is] a rarity in commercial arbitration"); Paul F. Kirgis, *Judicial Review and the Limits of Arbitral Authority: Lessons from the Law of Contract*, 81 ST. JOHN'S L. REV. 99, 119-20 (2007) (proposing that arbitrators be required to write opinions explaining their awards, which would be a change from the customary practice); Frances T. Freeman Jalet, *The Judicial Attitude*, 45 CORNELL L.Q. 519, 522 (1960) (stating that ordinarily arbitrators do not provide written opinions to explain the reasoning they employed in deciding the issues presented to them).

<sup>16</sup> *Shearson v. McMahon*, 482 U.S. 220 (1987).

<sup>17</sup> *Id.* at 242.

<sup>18</sup> *Id.* at 232.

<sup>19</sup> *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576, 577 (2008).

<sup>20</sup> *Id.* at 578.

judicial review prescribed in the FAA. This decision brought into question whether the *Hall Street* Court, by implication, abolished the manifest disregard standard. The Court, however, did not decide this issue, but rather confused the bar with alternative interpretations of the ambiguous dicta in *Wilko*, scrambling words like eggs in a skillet.<sup>21</sup> This confusion has led to conflicting judicial decisions, some courts holding that the manifest disregard standard survived *Hall Street*, others holding that *Hall Street* signaled the death of the manifest disregard standard.<sup>22</sup>

In *Stolt-Nielsen v. AnimalFeeds Int'l Corp.*,<sup>23</sup> the Court lapsed into self-contradiction. Although the court declined to decide whether the manifest disregard standard survived *Hall Street*, it professed to apply the standard *arguendo*.<sup>24</sup> The Court, however, did not apply the manifest disregard standard, but rather applied the broadest standard of plenary review. While engaging in this more searching review, the *Stolt-Nielsen* Court compounded the confusion by citing *Hall Street* for the proposition that the FAA permits only limited review for errors of law.<sup>25</sup> Most recently, in *AT&T Mobility LLC v. Concepcion*,<sup>26</sup> the Court suggested that the FAA does not permit any review for errors of law in arbitration awards, though once again unclear dicta assured continued uncertainty.

Indecision and self-contradiction have served as the dubious guideposts in this befuddling area of law. Nevertheless, some points are clear. First, *Concepcion* suggests that the Supreme Court views the manifest disregard standard with disfavor. Second, this disfavor foreshadows the end of substantive review of arbitration awards. Third, by moving in this direction, the Supreme Court has strayed from sound policy by rejecting the *McMahon* dicta.

Guided by the purposes of the FAA, its legislative history, and the role of commercial arbitration in modern society, this Article proposes a new framework for the judicial review of arbitration awards. Awards deciding federal statutory rights such as those conferred by securities law and civil rights law should be reviewed for errors of law. As recognized in *Wilko* and *McMahon*, federal rights deserve protection, even in arbitration. There is one other type of award that requires judicial correction. Despite the statements in *Hall Street* and *Concepcion* that the FAA provides the exclusive grounds for vacatur, the courts must correct awards that violate well-defined federal public policy, particularly those that endanger public health, safety, or welfare, or condone unlawful acts. All other awards should not be reviewed, on the federal level, for errors of law. Where an award does not decide a federal right or violate federal public policy, the FAA policy favoring efficiency in arbitration trumps any need of judicial review for errors of law.

Part II of this Article discusses *Wilko* and *First Options of Chicago, Inc. v. Kaplan*,<sup>27</sup> the Supreme Court decisions, which, perhaps unwittingly, led to the

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<sup>21</sup> *Id.* at 585.

<sup>22</sup> *See infra* Part III.B (cataloguing and analyzing cases interpreting *Hall Street*).

<sup>23</sup> *Stolt-Nielsen v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758, 1761 (2010).

<sup>24</sup> *Id.* at 1768 n.3.

<sup>25</sup> *Id.* at 1776.

<sup>26</sup> *AT&T Mobility v. Concepcion*, 131 S. Ct. 1740 (2011).

<sup>27</sup> *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 942 (1995).

establishment and confirmation of the manifest disregard standard. This Part also examines the reaction of the lower federal courts to this dubious standard of review.

Part III analyzes *Hall Street*, a perplexing decision which provided alternative interpretations of what “manifest disregard” might mean. The unfortunate result of *Hall Street* is that some courts have declared the manifest disregard standard dead while others have held that it is still viable.

Part IV explores the *McMahon* and *Gilmer v. Interstate/Johnson Lane Corp.*,<sup>28</sup> decisions in which the Supreme Court contradicted its dicta in *Wilko* and stated that errors of law in cases involving federal statutory rights were reviewable. Part IV shows that such review finds support in both the legislative history of the FAA and the evolution of arbitration since passage of the Act.

Part V begins with a discussion of *Stolt-Nielsen*, observing that the Supreme Court, though asserting that it was applying the manifest disregard standard *arguendo*, applied *de novo* review to nullify a partial award that would have violated FAA policy. *Stolt-Nielsen* therefore suggested that the Court might be receptive to an expanded scope of review under the proper circumstances. In *Concepcion*, however, the Court seemed to reject this possibility. Despite *Concepcion*, Part V advocates that awards violating well-defined federal public policy be subject to judicial correction at the federal level. This Part goes on to propose that there should be no federal judicial review for awards not determining federal statutory rights or violating well-defined federal public policy. Finally, this Part addresses the potential objection that the framework proposed in this Article would reduce the efficiency of arbitration.

The Article concludes with Part VI, which emphasizes the need to balance the policies of the FAA to promote the efficiency of arbitration with the policies of other federal laws. The approach proposed in this Article achieves a suitable balance. The Supreme Court has floundered on this issue for nearly sixty years. The jurisprudence of arbitration cannot withstand another sixty. It is time for Congress to set things right.

## II. MANIFEST DISREGARD: EMERGENCE AND CONFIRMATION

The Supreme Court, on numerous occasions, has addressed the standard that a court should apply when reviewing errors of law made in arbitration awards. The first such case was *Wilko v. Swan*.<sup>29</sup> It is regrettable that the *Wilko* decision resorted to ambiguous dicta, which has spawned confusion persisting to this very day.

### A. *Wilko v. Swan: The Confusion Begins*

Ironically, *Wilko* did not directly concern the scope of judicial review of arbitration awards. Rather, the issue presented in *Wilko* was whether anti-fraud claims brought under § 12(2) of the Securities Act of 1933 could be arbitrated, or whether public policy required that such claims be litigated in state or federal court.<sup>30</sup> The facts of *Wilko* were straightforward. A customer claimed that a broker-dealer induced him to purchase stock by making material misrepresentations and

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<sup>28</sup> *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 32 n.4 (1991)

<sup>29</sup> *Wilko v. Swan*, 346 U.S. 427 (1953).

<sup>30</sup> *Id.* at 430.

omitting material information.<sup>31</sup> When the customer commenced a federal lawsuit, under § 12(2), the broker-dealer moved to stay the action on the grounds that the parties had entered into an arbitration agreement.<sup>32</sup>

In *Wilko*, the policies of the Securities Act—to protect investors from securities fraud—clashed with the policy of the FAA—to create an environment hospitable to arbitration agreements.<sup>33</sup> The Supreme Court held that arbitration, though favored in other circumstances, was not a suitable means to resolve a § 12(2) fraud claim.<sup>34</sup> Bolstering its decision, the Court noted that arbitrators, who may not be knowledgeable on the intricacies of securities law, do not ordinarily write decisions or keep transcripts of hearings.<sup>35</sup> These practices prevented courts from effectively reviewing arbitration awards.<sup>36</sup> To protect investors from securities fraud, stronger procedural safeguards were required than those embedded in arbitration's informal approach to dispute resolution.<sup>37</sup>

The Supreme Court, therefore, reversed the order of the Second Circuit, which held the arbitration agreement enforceable.<sup>38</sup> The Second Circuit, as part of its rationale for holding § 12(2) claims arbitratable, observed that “arbitrators are bound to decide in accordance with the provisions of section 12(2).”<sup>39</sup> If arbitrators committed errors in interpreting the securities laws, such errors would “constitute

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<sup>31</sup> *Id.* at 428-29.

<sup>32</sup> *Id.* at 429. The broker-dealer moved under § 3 of the FAA, which provides: “If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration, the court . . . shall upon application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement . . . .” 9 U.S.C. § 3 (2006).

<sup>33</sup> *Wilko v. Swan*, 346 U.S. 427, 438 (1953).

<sup>34</sup> *Id.* In addition to questioning the adequacy of arbitration to resolve § 12(2) disputes, the Court relied on the interrelationship of two sections of the Securities Act. Section 14 provides that “[a]ny condition, stipulation, or provision . . . of this subchapter or of the rules and regulations of the Commission shall be void.” Section 22(a) provides that “[t]he district courts of the United States . . . shall have jurisdiction . . . concurrent with State and Territorial courts . . . of all suits in equity and actions at law brought to enforce any liability or duty created by this subchapter.” The Court concluded that an arbitration agreement constitutes an impermissible § 14 waiver of the § 22(a) right to sue in a state or federal district court. *Id.* at 434-35. The Second Circuit had rejected this reasoning, noting that if a party may settle a § 12(2) claim without violating the § 14 no-waiver provision, the party should be allowed to arbitrate such a claim. *U.S. v. Marachowsky*, 201 F.2d 5, 11 (7th Cir. 1953). Years later, the Supreme Court, in *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), overruled *Wilko* and reversed its position on the waiver argument, observing that “[b]y agreeing to arbitrate a statutory claim, a party does not forego the substantive rights of the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.” *Rodriguez*, 490 U.S. at 481 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985)).

<sup>35</sup> *Wilko v. Swan*, 346 U.S. 427 (1953).

<sup>36</sup> *Id.*

<sup>37</sup> *Id.* at 437.

<sup>38</sup> *Id.* at 438.

<sup>39</sup> *Wilko v. Swan*, 201 F.2d 440, 445 (2d Cir. 1953).



grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act.”<sup>40</sup> The Supreme Court, in reversing the Second Circuit, could not leave this point unanswered. If, as the Second Circuit stated, section 12(2) arbitration awards were subject to plenary judicial review for errors of law, the Supreme Court’s holding – that arbitration inadequately protects the statutory rights of victimized investors – would be undermined. The Supreme Court’s refutation of the Second Circuit’s observation on the scope of judicial review began as follows:

While it may be true, as the Court of Appeals thought, that a failure of the arbitrators to decide in accordance with the provisions of the Securities Act would “constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act,” that failure would need to be made clearly to appear.<sup>41</sup>

Unfortunately, the Supreme Court then lapsed into muddled dicta, which has cast the issue of the scope of judicial review of arbitration awards into uncertainty for over half a century. The Court stated: “In unrestricted submissions, such as the present margin agreements envisage, the interpretations of the law by the arbitrators in contrast to manifest disregard are not subject, in the federal courts, to judicial review for error in interpretation.”<sup>42</sup>

This statement perplexed the federal courts. As noted by the Fifth Circuit, “it is not surprising that the lower courts initially grappled with the uncertain implications of this clause.”<sup>43</sup> In *San Martine Compania De Navegacion v. Saguenay Terminals LTD*,<sup>44</sup> the Ninth Circuit expressed its dismay more forcefully:

Frankly, the Supreme Court’s use of the words “manifest disregard” has caused us trouble here. Conceivably the words may have been used to indicate that whether an award may be set aside for errors of law would be a question of degree. Thus if the award was based upon a mistaken view of the law, but in their assumption of what the law was, the arbitrators had not gone too far afield, then, the award would stand; but if the error is an egregious one, such as no sensible layman would be guilty of, then the award could be set aside. Such a “degree of error” test would, we think, be most difficult to apply. Results would likely vary from judge to judge. We believe this is not what the court had in mind when it spoke of “manifest disregard.”<sup>45</sup>

Despite the vagueness of the *Wilko* dicta, the circuit courts, one by one, recognized the manifest disregard standard.<sup>46</sup> For example, the Second Circuit, in *T.Co Metals*

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<sup>40</sup> *Id.*

<sup>41</sup> *Wilko v. Swan*, 346 U.S. 427 (1953) (citation omitted).

<sup>42</sup> *Id.*

<sup>43</sup> *Citigroup Global Mkts. Inc. v. Bacon*, 562 F.3d 349, 354 (5th Cir. 2009).

<sup>44</sup> *San Marine Compania De Navegacion v. Saguenay Terminals Ltd.*, 293 F.2d 796 (9th Cir. 1961).

<sup>45</sup> *Id.* at 801 n.4.

<sup>46</sup> *See, e.g., Halim v. Great Gatsby’s Auction Gallery, Inc.*, 516 F.3d 557, 563 (7th Cir. 2008) (stating that “factual or legal error, no matter how gross, is insufficient to support

*LLC v. Dempsey Pipe and Supply, Inc.*,<sup>47</sup> noted that the manifest disregard of the law standard is not met when the arbitrator makes a simple legal error.<sup>48</sup> The doctrine applies only when three elements are met.<sup>49</sup> First, the law applicable to the issue under decision must be clear.<sup>50</sup> Second, the arbitrator must have improperly applied the law and the error must have affected the outcome of the case.<sup>51</sup> Third, the arbitrator must have known the applicable law and intentionally ignored it.<sup>52</sup> Focusing on the third element of the Second Circuit's definition, the Tenth Circuit defined "manifest disregard" more succinctly. The doctrine applies when the arbitrators "knew the law and explicitly disregarded it."<sup>53</sup> This is the predominant definition of the manifest disregard standard.<sup>54</sup>

overturning an arbitration award."); *Collins v. D.R. Horton, Inc.*, 505 F.3d 874, 879 (9th Cir. 2007) (quoting *San Martine De Navegacion* for the proposition that a court may vacate an award under the manifest disregard standard only when the arbitrator knew the law and intentionally ignored it); *Three S Delaware Inc. v. DataQuick Info. Sys., Inc.*, 492 F.3d 520, 527 (4th Cir. 2007) (confirming that the Fourth Circuit recognizes the manifest disregard standard as arising from "common law"); *McCarthy v. Citigroup Global Mkts., Inc.*, 463 F.3d 87, 93 (1st Cir. 2006) (asserting that the manifest disregard standard requires that the arbitrator "willfully" decided not to apply governing law); *Dominion Video Satellite, Inc. v. Echostar Satellite L.L.C.*, 430 F.3d 1269, 1275 (10th Cir. 2005) (defining "manifest disregard" to mean more than an error of law but rather an error resulting from an arbitrator's "explicit" refusal to apply controlling law); *Manion v. Nagin*, 392 F.3d 294, 298 (8th Cir. 2004) (stating that to manifestly disregard the law the arbitrator must "clearly identify" governing law and ignore it); *Hoefl v. MVL Group, Inc.*, 343 F.3d 57, 65 (2d Cir. 2003) (characterizing the manifest disregard standard as a product of "common law"); *Dluhos v. Strasberg*, 321 F.3d 365, 370 (3d Cir. 2003) (noting that the result of judicial application of the "exceedingly narrow" manifest disregard standard "is generally to affirm easily the arbitration award"); *Prestige Ford v. Ford Dealer Computer Servs., Inc.*, 324 F.3d 391, 395-96 (5th Cir. 2003) (describing "manifest disregard" as "willfull inattentiveness to governing law"); *Scott v. Prudential Sec., Inc.*, 141 F.3d 1007, 1017 (11th Cir. 1998) (characterizing the manifest disregard standard as a nonstatutory ground of review); *Cole v. Burns Int'l Sec. Servs.*, 105 F.3d 1465, 1487 (D.C. Cir. 1997) (recognizing that the manifest disregard standard must adapt to varying circumstances, the scope of the standard increasing from limited review to plenary review for errors of law when the arbitrators decide claims alleging the denial of rights conferred by federal statutes); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Jaros*, 70 F.3d 418, 421 (6th Cir. 1995) (holding that an arbitrator manifestly disregards the law where an award lacks "any line of argument that is legally plausible").

<sup>47</sup> *T.Co Metals LLC v. Dempsey Pipe and Supply, Inc.*, 592 F.3d 329 (2d Cir. 2010).

<sup>48</sup> *Id.* at 339.

<sup>49</sup> *Id.*

<sup>50</sup> *Id.*

<sup>51</sup> *Id.*

<sup>52</sup> *Id.*

<sup>53</sup> *Hicks v. Cadle Co.*, 355 F. App'x. 186, 197 (10th Cir. 2009) (quoting *Hollern v. Wachovia Secs., Inc.*, 458 F.3d 1169, 1176 (10th Cir. 2006)). See also *Frazier v. CitiFinancial Corp.*, 604 F.3d 1313, 1322 (11th Cir. 2010) (noting that manifest disregard of the law means that the arbitrator deliberately ignored controlling law).

<sup>54</sup> See *supra* note 46 and accompanying text (setting forth the prevalent definition of the manifest disregard standard).

Because of the vagueness of the phrase “manifest disregard of the law,” not all circuits have defined the term identically. In *Merrill Lynch, Pierce Fenner & Smith v. Jaros*,<sup>55</sup> for example, the Sixth Circuit stated, “If a court can find any line of argument that is legally plausible and supports the award then it must be confirmed. Only where no judge or groups of judges could conceivably come to the same determination as the arbitrators must the award be set aside.”<sup>56</sup> Unlike the Second Circuit’s standard, which requires deliberate disregard of controlling law, the Sixth Circuit in *Jaros* seems to adopt a less deferential “clearly erroneous” standard.

In *Citigroup Global Markets, Inc. v. Bacon*,<sup>57</sup> the Fifth Circuit expressed a third variation of what “manifest disregard” might mean. The Fifth Circuit held that for a legal error to rise to the level of manifest disregard of the law it “must have been obvious and capable of being readily and instantly perceived by the average person qualified to serve as an arbitrator.”<sup>58</sup> This standard is even more confounding than the ones adopted by the Second and Sixth Circuits. There is no GRE for arbitrators. Some are lawyers who understand the legal principles governing the matter presented for arbitration. Others are chosen as arbitrators because they have experience with and expertise in the trade practices relevant to the case. Still others are not conversant or even familiar with the applicable law or with relevant trade practices. One can only guess at how a judge might determine the acumen of the “average” person qualified to serve as an arbitrator. One can only puzzle at why a standard of judicial review should depend on what such a hypothetical person can “instantly perceive.”

#### B. First Option v. Kaplan: *Dubious Confirmation*

It was not until 1995, in *First Options of Chicago, Inc. v. Kaplan*,<sup>59</sup> that the Supreme Court again mentioned the manifest disregard standard. Manuel and Carol Kaplan and their wholly-owned investment company, MKI Investments, incurred losses in the stock market crash of 1987 and later in 1989.<sup>60</sup> Their clearing firm, First Options of Chicago (“First Options”), liquidated certain MKI assets and demanded that the Kaplans pay the deficiency.<sup>61</sup> When the Kaplans refused, First Options initiated an arbitration proceeding under the auspices of the Philadelphia Stock Exchange.<sup>62</sup> MKI accepted the propriety of arbitration, but the Kaplans, who had not personally signed an arbitration agreement, denied the authority of the arbitration panel to hear their case.<sup>63</sup> The panel decided that it had such authority

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<sup>55</sup> *Merrill Lynch, Pierce Fenner & Smith, Inc. v. Jaros*, 70 F.3d 418 (6th Cir. 1995).

<sup>56</sup> *Id.* at 421.

<sup>57</sup> *Citigroup Global Markets, Inc. v. Bacon*, 562 F.3d 349 (5th Cir. 2009).

<sup>58</sup> *Id.* at 354.

<sup>59</sup> *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995).

<sup>60</sup> *Id.* at 940.

<sup>61</sup> *Id.*

<sup>62</sup> *Id.*

<sup>63</sup> *Id.* at 941.

and ultimately ruled in favor of First Options on the merits of the dispute.<sup>64</sup> The district court confirmed the award, but the Third Circuit vacated it, holding that the dispute was not arbitrable.<sup>65</sup>

The issue presented to the Supreme Court was whether the courts or the arbitrators had the authority to determine the arbitrability of the dispute between First Options and the Kaplans.<sup>66</sup> In explaining the practical importance of the issue, the Court commented on the narrow scope of judicial review of arbitration awards. If the arbitrators had the authority to decide arbitrability, their decision would be nearly immune to judicial oversight.<sup>67</sup> To prove its point, the Court cited *Wilko*, noting parenthetically and without elaboration that “parties [are] bound by arbitrator’s decision not in ‘manifest disregard’ of the law.”<sup>68</sup> This casual reference to *Wilko* did nothing to clarify the meaning of “manifest disregard” of the law. It did, however, confirm that the Supreme Court viewed manifest disregard of the law as a viable standard.

### III. HALL STREET V. MATTEL: CONFUSION CONFIRMED

In *Hall Street Assocs. L.L.C. v. Mattel, Inc.*,<sup>69</sup> the Supreme Court discussed the ambiguities in *Wilko*’s comments on the scope of judicial review of arbitration awards. As if baffled by a parchment of ancient hieroglyphics, the Court could not decipher what the curious dicta in *Wilko* meant.

#### A. The Hall Street Case

*Hall Street* involved a landlord-tenant dispute. Hall Street leased a property to Mattel, which agreed, in a written lease, to indemnify Hall Street for costs arising from violations of environmental laws committed by Mattel or its predecessor-tenants.<sup>70</sup> After the discovery of pollutants discharged at the site by Mattel’s predecessors, Mattel signed a consent order to clean up the site, and it terminated the lease.<sup>71</sup> Hall Street asserted its right to indemnification, a claim which Mattel

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<sup>64</sup> *Id.*

<sup>65</sup> *Id.*

<sup>66</sup> Emphasizing that arbitration is “simply a matter of contract,” Justice Breyer, writing for a unanimous Court, stated that the agreement itself will determine the resolution of the arbitrability issue. *Id.* at 943. Justice Breyer cautioned, however, that arbitrators may determine the issue of arbitrability only if the evidence of such an agreement is clear and unmistakable. *Id.* at 944. Because First Options could not meet this standard, Justice Breyer concluded that the issue of arbitrability in this case was for the court, rather than the arbitrators, to decide. *Id.* at 947.

<sup>67</sup> *Id.* at 942.

<sup>68</sup> *Id.* The court also noted that, under § 10 of the FAA, a court may vacate an award procured by corruption, fraud, or undue means or if the arbitrator exceeded his powers. *Id.*

<sup>69</sup> *Hall Street Assocs. L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008).

<sup>70</sup> *Id.* at 579.

<sup>71</sup> *Id.* Tests of the property’s well water, conducted in 1998, indicated high levels of trichloroethylene. After the Oregon Department of Environmental Quality found additional contamination, Mattel stopped using the well, and, along with one of its predecessors, signed the consent decree in which it undertook to clean up the site. *Id.*

contested.<sup>72</sup> The parties entered into an agreement to submit this dispute to arbitration.<sup>73</sup> The arbitration agreement provided: “The [District] Court shall vacate, modify or correct any award: (i) where the arbitrator’s findings of fact are not supported by substantial evidence, or (ii) where the arbitrator’s conclusions of law are erroneous.”<sup>74</sup>

The arbitrator decided for Mattel, ruling the indemnification provision inapplicable to the violation committed by Mattel’s predecessors.<sup>75</sup> The district court granted Hall Street’s motion to vacate the award,<sup>76</sup> invoking the parties’ agreement ostensibly authorizing the court to vacate an award based on an erroneous conclusion of law.<sup>77</sup> On appeal, the Ninth Circuit reversed the district court’s ruling, on the ground that the arbitration agreement’s judicial review provision was unenforceable.<sup>78</sup> Accordingly, the Ninth Circuit remanded the case, instructing the district court to confirm the original arbitration award.<sup>79</sup>

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<sup>72</sup> *Id.* Hall Street filed a summons and complaint in federal district court, disputing Mattel’s right to terminate the lease and seeking to enforce the indemnification clause. Mattel prevailed on the termination issue. The parties then attempted to mediate the indemnification claim, but after their efforts at mediation proved unsuccessful, they agreed to submit the dispute to arbitration. The court approved the arbitration agreement and entered an order accordingly. *Id.*

<sup>73</sup> *Id.*

<sup>74</sup> *Id.*

<sup>75</sup> *Id.* at 580. The arbitrator noted that the lease provision required Mattel to indemnify Hall Street for violations of federal, state, and local environmental law. The pollutants found on the leased premises violated the Oregon Drinking Water Quality Act. Characterizing this Act as a health law, rather than an environmental law, the arbitrator found the indemnification provision inapplicable. *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.* The district court held that the Oregon Drinking Water Quality Act was an environmental law and remanded the matter to the arbitrator. On remand, the arbitrator decided for Hall Street. Both parties moved in the district court to modify the arbitrator’s decision. The district court, again applying a plenary standard of review as stipulated by the parties, corrected the arbitrator’s calculation of interest and otherwise confirmed. *Id.*

<sup>78</sup> *Id.* at 581. The district court granted Hall Street’s motion to vacate upholding the parties contract to expand the scope of judicial review to include errors of law, relying on *LaPine Tech. Corp. v. Kyocera Corp.*, 130 F.3d 884, 889 (9th Cir. 1997). The Ninth Circuit reversed the judgment of the district court in favor of Mattel holding that according to Kyocera, the Ninth Circuit’s recent en banc decision, “the terms of the arbitration agreement controlling the mode of judicial review are unenforceable and severable.” *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 113 Fed. Appx. 272, 272-73 (2004) (quoting *Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987, 1000 (9th Cir. 2008) (en banc); see also *Bowen v. Amoco Pipeline Co.*, 254 F.3d 925, 936 (10th Cir. 2001) (holding that parties may not contractually expand the scope of judicial review of arbitration awards); cf. *Syncor Int’l Corp. v. McLeland*, 120 F.3d 262 (4th Cir. 1997), 1997 WL 45245 \*6 (reaching the same conclusion in an unpublished opinion). But see *Puerto Rico Tel. Co. v. U.S. Phone Mfg. Corp.*, 427 F.3d 21, 31 (1st Cir. 2005) (upholding contractual expansion of arbitrator’s scope of review); *Jacada (Europe), Ltd. v. Int’l Mktg. Strategies, Inc.*, 401 F.3d 701, 710 (6th Cir. 2005); *Roadway Package Sys., Inc. v. Kayser*, 257 F.3d 287, 288 (3d Cir. 2001); *Gateway Techs., Inc. v. MCI Telecomms. Corp.*, 64 F.3d 993, 997 (5th Cir. 1995); cf. *UHC Mgt. Co. v.*

## 1. The Supreme Court Decision: Obfuscation

The Supreme Court granted certiorari.<sup>80</sup> The issue before the Court in *Hall Street* was whether the parties to an arbitration agreement could validly agree to expand the grounds prescribed in § 10 and § 11 of the FAA for vacating or correcting an arbitration award.<sup>81</sup> Hall Street argued that the agreement to expand judicial review was valid, relying on the proposition that the FAA is “motivated, first and foremost, by a congressional desire to enforce agreements into which parties ha[ve] entered.”<sup>82</sup> According to Hall Street, the policy favoring the enforcement of arbitration agreements implied that courts should enforce arbitration agreements to expand judicial review.<sup>83</sup> The Court rejected this argument.<sup>84</sup> While conceding that the FAA grants the parties wide latitude in the selection of arbitrators, choice of law, and other features of the process, the Court read the text of the statute to limit the scope of review.<sup>85</sup> The Court relied on two textual arguments. First, it noted that all the grounds for vacatur prescribed in the FAA such as “corruption,” “fraud,” and “evident partiality,” address “egregious” arbitral improprieties different in kind from mere errors of law.<sup>86</sup> Second, the Court cited § 9 of the FAA, which provides that a court “must” confirm an award “unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title.”<sup>87</sup> The mandatory wording of § 9 left no room for disagreement: the statutory grounds enumerated in § 10 and § 11 of the FAA are exclusive.<sup>88</sup>

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Computer Sciences Corp., 148 F.3d 992, 997-98 (8th Cir. 1998) (expressing in dicta that parties may contractually expand the scope of review).

<sup>79</sup> Hall Street Assocs., L.L.C. v. Mattel, Inc., 552 U.S. 576, 581 (2008). The district court again held in favor of Hall Street and the Ninth Circuit again reversed on appeal. *Id.*

<sup>80</sup> *Id.*

<sup>81</sup> *Id.* at 578.

<sup>82</sup> *Id.* at 585 (quoting Dean Witter Reynolds Inc. v. Byrd, 470 U.S. 213, 220 (1985)).

<sup>83</sup> *Id.*

<sup>84</sup> *Id.* at 586. See Eric S. Chafetz, *An Opportunity Lost: The Supreme Court's Failure to Recognize the Implications of Its Holding in Hall Street Associates, L.L.C. v. Mattel, Inc.*, at 14 (March 2009), available at [http://bepress.com/eric\\_chafetz/2](http://bepress.com/eric_chafetz/2) (stating that, although *Hall Street* may have been correctly decided on the grounds of statutory interpretation, the Supreme Court underplayed the role of party intent).

<sup>85</sup> *Hall Street*, 552 U.S. at 586.

<sup>86</sup> *Id.*

<sup>87</sup> *Id.* at 587.

<sup>88</sup> *Id.* at 586. The *Hall Street* Court did not expressly rule whether parties to an arbitration agreement could expand review by limiting the decisional powers of the arbitrators rather than on expanding the review powers of the courts. Thus, the parties might seek to expand the scope of review by agreeing that the arbitrators must correctly apply a particular law or the law of a particular state and that the arbitrators exceed their powers by failing to apply such law correctly. This strategic rewording of an arbitration clause would arguably reposition legal errors of arbitrators within the range of § 10(a)(4) of the FAA, which provides review when the arbitrators exceeded their powers. However, the chance that the Supreme Court, or other courts following *Hall Street*, would uphold clauses using this backdoor strategy seems

remote. Preliminarily, it should be noted that in *Hall Street*, the parties arbitrated the application of an indemnification clause to the costs of cleaning up toxic waste. Neither party asked the arbitrators to decide its rights under federal statutes such as the federal securities laws or the federal civil rights laws. If the Court were presented with such a federal rights issue, the analysis might proceed differently because of the exigencies of public policies expressed in federal law. In the context of *Hall Street*, however, the Court emphasized that the FAA does not allow “general review for an arbitrator’s legal errors.” *Id.* at 585. It would seem that any contractual attempt to override this limitation would conflict with the Supreme Court’s view of FAA policy. Although the *Hall Street* Court did not decide the enforceability of such clauses, one could argue persuasively that directing the courts to correct all legal errors, as *Hall Street Associates* and *Mattel* attempted to do, is functionally and therefore legally equivalent to providing contractually that any legal error by the arbitrators exceeds their authority and incidentally triggers judicial review. Such a deft turn of phrase is likely to invoke charges of putting form over substance and it is unlikely to win the blessing of the Supreme Court. Furthermore, *Hall Street* mentioned circumstances, including state statutory and common law and the authority of federal courts to manage pending cases, where an award might be subject to review broader than that permitted under the FAA. *See id.* at 576, 590-92. It is telling that the Supreme Court did not list among these circumstances any contractual maneuvers that might achieve the same result. Several scholars have considered the issue as to whether wording arbitration clauses to place legal errors beyond the powers of the arbitrators would circumvent *Hall Street*. Professor Stipanowich doubts whether the Supreme Court would uphold such clauses. He states:

Although *Hall Street* came down strongly against extra-statutory bases for vacatur, might what the Second Circuit terms “judicial gloss” permit parties to give form and content to the boundaries of arbitrators’ authority and what constitutes “exceeding their powers” under § 10(a)(4)? Might, for example parties trigger judicial review of errors of law by describing a failure to faithfully observe and apply particular law as “in excess of the arbitrator’s powers.” While it is highly doubtful that the *Stolt-Nielsen* majority actively contemplated, or relishes, the prospect, there is no doubt that hopeful attorneys will seize on the wisp of a possibility of wedging a foot in the door of vacatur.

Thomas Stipanowich, *Revelations and Reaction: The Struggle to Shape American Arbitration*, Pepperdine University School of Law Legal Studies Research Paper Studies Series, Paper No. 2011/11, at 15 (Apr. 2011), available at <http://ssrn.com/abstract=1757258>. Professor Drahozal believes that such a clause is not an evasion of *Hall Street*, but it is rather an effective use of § 10(a)(4). He therefore concludes that such clauses should be enforceable, though he acknowledges that the weight of post-*Hall Street* judicial authority contradicts him. Christopher R. Drahozal, *The Supreme Court and Arbitration: Contracting Around Hall Street*, 14 LEWIS & CLARK L. REV. 905, 916 (2010). *See Francis v. Landstar Sys. Holdings, Inc.*, No. 3:09-cv-238-J-32JRK, 2009 WL 4350250, \*6, 7 (M.D. Fla. Nov. 25, 2009) (rejecting the argument that, where an arbitration agreement limited the arbitrator’s authority to applying controlling law correctly, an arbitrator who committed an error of law exceeded her authority and her award was therefore subject to vacatur); *Wood v. PennTex Resources, LP*, No. H-06-2198, 2008 WL 2609319, \*8 (June 27, 2008) (interpreting *Hall Street* to invalidate provision in arbitration agreement stating that any clearly erroneous factual determination by the arbitrators exceeds their powers and is therefore not subject to confirmation). *But see Cable Connection, Inc. v. DirectTV, Inc.*, 190 P.3d 586, 596 (Cal. 2008) (upholding, under the California Arbitration Act, the enforceability of an arbitration provision stating that arbitrators exceed their power by committing legal error and that the courts are empowered to review such errors). *See generally* Robert Ellis, *Imperfect Minimalism: Unanswered Questions in Hall Street Associates L.L.V. v. Mattel, Inc.*, 128 S. Ct. 1396 (2008), 32 HARV. J.L. & PUB. POL’Y 1187, 1195-96 (2009) (noting that after *Hall Street* sophisticated parties began to draft clauses that deny arbitrators the power to make errors of law and direct courts to vacate

Contesting this proposition, Hall Street relied on the *Wilko* decision. Hall Street contended that, by establishing the manifest disregard standard, *Wilko* had recognized the acceptability of expanded judicial review of arbitration awards.<sup>89</sup> The Court rejected this argument for several reasons. Refusing to confirm that *Wilko* established the manifest disregard standard, the Court stressed that, even if *Wilko* had done so, “manifest disregard” was judicially rather than contractually created.<sup>90</sup> The judicial power to expand the grounds of review did not imply an analogous contractual right.<sup>91</sup> Second, the Supreme Court observed that Hall Street was seeking to enforce a provision authorizing plenary judicial review for errors of law, whereas *Wilko* recognized, at the very most, a standard of review only for egregious errors.<sup>92</sup>

The Supreme Court also took note of the “vagueness of *Wilko*’s phrasing,” speculating about the meaning of the term “manifest disregard:”

Maybe the term “manifest disregard” was meant to name a new ground for review, but maybe it merely referred to the § 10 grounds collectively, rather than adding to them. . . . Or, as some courts have thought, “manifest disregard” may have been shorthand for § 10(a)(3) or § 10(a)(4), the paragraphs authorizing vacatur when the arbitrators were “guilty of misconduct” or “exceeded their powers.”<sup>93</sup>

Although the Supreme Court speculated that perhaps “the term ‘manifest disregard’ was meant to name a ground for review,”<sup>94</sup> the Court did not suggest what that ground might be. The Court’s omission is striking. This amorphous standard is the John Doe of judicial review. It is a term that the Supreme Court coined without definition or content, and yet it is a doctrine that the circuits invested with significance and that many circuits continue to apply.

## 2. Other Possible Interpretations of the *Wilko* Dicta

There are possibilities beyond those adopted by the circuit courts that one might reasonably extract from the ambiguous *Wilko* dicta. At this point, it might be instructive to revisit that ambiguous language. The Supreme Court stated that, to be reversible, a legal error committed by an arbitrator “would need to be made clearly to appear.”<sup>95</sup> The Court continued that “interpretations of the law by the arbitrators in contrast to manifest disregard are not subject, in the federal courts, to judicial review for error in interpretation.”<sup>96</sup> Although the term “manifest disregard” would

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awards with such errors, and suggesting that this practice complies with *Hall Street* and fits into § 10 of the FAA).

<sup>89</sup> *Hall Street*, 552 U.S. at 584.

<sup>90</sup> *Id.* at 585.

<sup>91</sup> *Id.*

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> *Wilko v. Swan*, 346 U.S. 427, 436 (1953).

<sup>96</sup> *Id.* at 436-37.



seem not to apply to an ordinary error of law, the term might mean that the arbitrator demonstrably failed to apply controlling law, whether the error was intentional or not. Under this definition, “manifest” would mean “demonstrable.” Many errors made by arbitrators are not demonstrable because arbitrators do not ordinarily provide written opinions to support their awards.<sup>97</sup> This lack of transparency was prevalent when the Supreme Court decided *Wilko*,<sup>98</sup> so it is quite possible that the *Wilko* Court meant “demonstrable” when it used the word “manifest.” Defining “manifest” in this way also jibes with the Court’s statement that errors must “be made clearly to appear.”<sup>99</sup> A judge should not guess at the grounds for an arbitrator’s decision and vacate that decision without a clear indication of its legal basis. “Disregard of the law,” under this definition, would mean a failure to apply the law rather than a mistake in applying it. Such a failure might well be described as “disregard.”

There is yet another and less restrictive interpretation that would provide a reasonable solution to the linguistic mystery. Perhaps an arbitrator manifestly disregards the law when he or she demonstrably (again defining “manifestly” as “demonstrably”) commits an error of law on a point not subject to interpretation, that is, on a point of well-settled law. This definition of manifest disregard of the law fits the Supreme Court’s directive in *Wilko* that “interpretations of the law” “are not subject, in the federal court, to judicial review . . . .”<sup>100</sup>

Defining “manifest disregard” is a pin-the-tail-on-the-donkey exercise. It is unfortunate that controversy surrounds both the meaning and viability of such an important legal doctrine.<sup>101</sup> Perhaps when the Supreme Court introduced the term, it did not contemplate that the circuit courts would elevate dicta to law, let alone to the principal doctrine used to decide motions to vacate arbitration awards. The time is long overdue when the high Court should announce whether manifest disregard is a living doctrine or a mere fancy of the judicial imagination. In *Hall Street*, the Court chose to keep the doctrine dangling on a tightrope, by holding that, although the FAA provides the exclusive grounds for review, § 10 might imply the manifest disregard standard. The Court’s equivocation has instigated another round of confusion among the federal courts.

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<sup>97</sup> See *supra* note 15 and accompanying text (noting that arbitrators do not ordinarily provide written explanations for their decisions).

<sup>98</sup> In a dissenting opinion to the Second Circuit’s decision in *Wilko*, Judge Clark wrote: “[T]he arbitrators will act according to their business background and there will be no way – unless they volunteer foolish explanations in their decision – of checking what they do.” *Wilko v. Swan*, 201 F.2d 439, 446 (1953) (Clark, J., dissenting).

<sup>99</sup> *Wilko*, 346 U.S. at 436.

<sup>100</sup> *Id.* at 436-37.

<sup>101</sup> See *Zachary L. Gould, Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 548 F.3d 85 (2d Cir. 2008), 25 OHIO ST. J. ON DISP. RESOL. 1109, 1109 (2010) (noting that, after *Hall Street*, the federal circuit courts disagree “not only on the manifest disregard doctrine’s scope but also on its very existence.”).

*B. The Divided Reaction to Hall Street*

The circuit courts are divided on whether *Hall Street* abolished the manifest disregard standard.<sup>102</sup> A circuit's response to *Hall Street* has often depended on

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<sup>102</sup> Some circuit courts, in the wake of *Hall Street*, continue to recognize the manifest disregard standard as a valid ground for vacating awards. See, e.g., *Johnson v. Wells Fargo Home Mortg., Inc.*, 635 F.3d 401, 415 n.11 (9th Cir. 2011) (reading the Supreme Court's decision in *Stolt-Nielsen* as expressing "some doubt" on whether the manifest disregard standard survived *Hall Street*, but concluding that, in light of the Ninth Circuit's decision in *Comedy Club*, "in this Circuit the 'manifest disregard' standard has survived *Hall Street* intact, and so we are bound to apply it") (citing *Comedy Club, Inc. v. Improv West Assocs.*, 553 F.3d 1277, 1290-91 (9th Cir. 2010)); *T.Co Metals, LLC v. Dempsey Pipe & Supply, Inc.*, 592 F.3d 329, 339 (2d Cir. 2010) (reaffirming the Second Circuit's holding in *Stolt-Nielsen* that the manifest disregard standard is a judicial gloss on the grounds for vacatur specified in § 10 of the FAA, and that the manifest disregard standard therefore survives *Hall Street*) (citing *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 548 F.3d 85, 94-95 (2d Cir. 2008)); *Comedy Club*, 553 F.3d at 1291 (adhering to the manifest disregard standard post-*Hall Street* because the standard "is a shorthand for a statutory ground under the FAA, specifically 9 U.S.C. § 10(a)(4), which states that the court may vacate where the arbitrators exceeded their powers") (internal quotation marks omitted); *Coffee Beanery, Ltd. v. WW, LLC*, 300 Fed. App'x 415, 419 (6th Cir. 2008) (holding, in an unpublished decision, that the manifest disregard standard, as a "judicially-invoked" ground for vacatur, continues to be viable after *Hall Street* because the Supreme Court only rejected contractual expansion of the grounds in §§ 10 and 11 of the FAA and did not address judicial expansion of those grounds). Other circuit courts have held that *Hall Street's* statutory interpretation that the grounds for vacatur in the FAA are exclusive abolished the manifest disregard standard. See *Medicine Shoppe Int'l, Inc., Turner*, 614 F.3d 485, 489 (8th Cir. 2010) (citing *Hall Street* for the proposition that the grounds for vacatur prescribed in § 10 are exclusive, and holding that "[a]ppellants' claims, including the claim that the arbitrator disregarded the law, are not included among those specifically enumerated in § 10 and are therefore not cognizable"); *Frazier v. Citifinancial Corp., LLC*, 604 F.3d 1313, 1324 (11th Cir. 2010) (holding that, since the manifest disregard standard was judicially created, *Hall Street* abolished it by ruling that the grounds for vacatur enumerated in §§ 10 and 11 of the FAA are exclusive); *Citigroup Global Mkts. Inc. v. Bacon*, 562 F.3d 349, 358 (5th Cir. 2009) ("In the light of the Supreme Court's clear language that, under the FAA, the statutory provisions are the exclusive grounds for vacatur, manifest disregard of the law as an independent ground for setting aside an award must be abandoned and rejected."). Still other circuit courts have commented on the issue without deciding whether *Hall Street* invalidated the manifest disregard standard. See *Hicks v. The Cadle Co.*, 355 Fed. App'x 186, 197 (10th Cir. 2009) (viewing the manifest disregard standard as judicially created, but declining to decide whether *Hall Street* abolished it because the defendants failed to meet the manifest disregard standard in their motion to vacate the award); *Ramos-Santiago v. United Parcel Serv.*, 524 F.3d 120, 124 (1st Cir. 2008) (acknowledging that *Hall Street* invalidated the manifest disregard standard, but declining to follow it because the case was brought under Puerto Rican law, not the FAA); *UMass Mem'l Med. Ctr., Inc. v. United Food and Commercial Workers Union*, 527 F.3d 1, 6 (1st Cir. 2008) (stating that courts have inherent powers, outside of § 10, to vacate awards). In *Grain v. Trinity Health, Mercy Health Servs. Inc.*, the Sixth Circuit noted that it had previously characterized the manifest disregard standard as "judicially created." 551 F.3d 374, 379-80 (6th Cir. 2008) (citing *Merrill Lynch, Pierce, Fenner & Smith v. Jaros Inc.*, 70 F.3d 418, 421 (6th Cir. 1995)), cert. denied, 130 S. Ct. 96 (2009). Although it declined to rule on the continued viability of the manifest disregard standard, it recognized, contrary to its previous decision in *Coffee Beanery*, that "*Hall Street's* reference to the 'exclusive' statutory grounds for obtaining relief casts some doubt on the continuing vitality of that theory." *Grain*, 551 F.3d at 380.

whether the circuit viewed the manifest disregard standard as statutory or nonstatutory.<sup>103</sup> As shown below, there have been three positions taken among those circuits that have reached definitive decisions.

### 1. Manifest Disregard as a Nonstatutory Ground of Review

In *Citigroup Global Markets Inc. v. Bacon*,<sup>104</sup> the Fifth Circuit held that *Hall Street* abolished the manifest disregard standard.<sup>105</sup> Although the Fifth Circuit, prior to the *Bacon* case, had adopted the manifest disregard standard as a nonstatutory ground of review, it recognized the dubious origins of the doctrine:

Our circuit did not accept manifest disregard of the law as a nonstatutory ground for vacatur with immediate confidence and certainty. . . . Indeed, manifest disregard of the law does not have a compelling origin as a ground for vacatur. Its modest debut occurs in a vague phrase found in *Wilko v. Swan* . . . .<sup>106</sup>

The Fifth Circuit noted that *Hall Street* held that the grounds for vacatur prescribed in the FAA are exclusive.<sup>107</sup> Because the Fifth Circuit had classified manifest disregard as a *nonstatutory* ground, it concluded that manifest disregard of the law was no longer a basis to vacate arbitration awards.<sup>108</sup>

*Coffee Beanery Ltd. v. WW L.L.C.*,<sup>109</sup> an unpublished decision of the Sixth Circuit, conflicts with *Bacon*.<sup>110</sup> Although conceding that *Hall Street* “significantly reduced” the viability of the nonstatutory grounds for vacatur of arbitration, the Sixth Circuit concluded nonetheless that *Hall Street* did not eliminate them.<sup>111</sup> To exempt the manifest disregard standard from *Hall Street*’s pronouncement that the grounds for vacatur in the FAA are exclusive, the Sixth Circuit stressed that *Hall Street* rejected contractual rather than judicial expansion of the scope of review.<sup>112</sup>

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<sup>103</sup> Compare *Johnson*, 635 F.3d at 401, 415 n. 11 (confirming the Ninth Circuit’s recognition of the manifest disregard standard after *Hall Street* and *Stolt-Nielsen* because manifest disregard is a “shorthand” for § 10(a)(4) of the FAA) and *T.Co Metals*, 592 F.3d at 339 (reaffirming the Second Circuit’s position that the manifest disregard standard is a “judicial gloss” on the grounds for vacatur specified in § 10 of the FAA) with *Medicine Shoppe*, 614 F.3d at 489 (holding that *Hall Street* abolished manifest disregard, which was a nonstatutory ground for vacatur) and *Frazier*, 604 F.3d at 1324 (ruling that, since the manifest disregard standard was judicially created, *Hall Street* abolished it).

<sup>104</sup> *Citigroup Global Markets Inc. v. Bacon*, 562 F.3d 349 (5th Cir. 2009).

<sup>105</sup> *Id.* at 358.

<sup>106</sup> *Id.* at 354. See *Williams v. Cigna Fin. Advisors, Inc.*, 197 F.3d 752, 759 (5th Cir. 1999) (recognizing the manifest disregard standard as a nonstatutory ground of review in light of the *First Options* decision).

<sup>107</sup> *Citigroup*, 562 F.3d at 355.

<sup>108</sup> *Id.*

<sup>109</sup> *Coffee Beanery, Ltd. v. WW, LLC*, 300 F. App’x 415 (6th Cir. 2008).

<sup>110</sup> *Id.* at 418-19.

<sup>111</sup> *Id.*

<sup>112</sup> *Id.*

Furthermore, the Sixth Circuit observed that “manifest disregard”—a narrow standard of review—comported with *Hall Street’s* disapproval of general review for arbitration awards.<sup>113</sup> The Sixth Circuit seized upon *Hall Street’s* suggestion that the vague language in *Wilko* might have “meant to name a new ground for review” outside the grounds expressed in §§ 10 and 11 of the FAA.<sup>114</sup> Given that all the circuits had adopted the manifest disregard standard before the *Hall Street* decision, the Sixth Circuit concluded that “it would be imprudent to cease employing such a universally recognized principle.”<sup>115</sup>

## 2. Manifest Disregard as a Statutory Ground of Review

In *Comedy Club, Inc. v. Improv West Associates*,<sup>116</sup> the Ninth Circuit considered whether the manifest disregard standard, which it had long recognized as a statutory ground for review, survived *Hall Street*.<sup>117</sup> The court noted that it had held previously that the manifest disregard standard is a “shorthand” for § 10(a)(4) of the FAA, the subsection authorizing the vacatur for awards “where the arbitrators exceeded their powers.”<sup>118</sup> The *Hall Street* decision, the Ninth Circuit observed, had not decided whether § 10(a)(4) of the FAA implied the manifest disregard standard of review.<sup>119</sup> Nevertheless, *Hall Street* had listed this possibility among several viable interpretations of *Wilko’s* seminal language, which gave birth to the standard.

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<sup>113</sup> *Id.*

<sup>114</sup> *Id.* at 419 (quoting *Hall Street Assocs., LLC v. Mattel, Inc.*, 552 U.S. 576, 585 (2008)). The Sixth Circuit’s interpretation of *Hall Street* is implausible. The court’s principal point was that *Hall Street* speculated that *Wilko* might have meant the term “‘manifest disregard’ to name a new ground for review.” *Coffee Beanery*, 300 Fed. App’x at 419 (6th Cir. 2008). The Supreme Court’s speculation about what *Wilko* might have meant does not imply that the Court would agree with *Wilko* if *Wilko* intended to create a ground for review not prescribed in the FAA. *Hall Street* was unequivocal that the grounds specified in §§ 10 and 11 are exclusive. If dicta in *Wilko* meant to suggest that manifest disregard of the law was a creature of judicial invention rather than one of statutory construction, the dicta in *Wilko* would violate the holding of *Hall Street*. The *Wilko* dicta would therefore not be entitled to any weight.

<sup>115</sup> *Coffee Beanery*, 300 Fed.Appx. at 419.

<sup>116</sup> *Comedy Club, Inc. v. Improv West Associates*, 553 F.3d 1277 (9th Cir. 2009).

<sup>117</sup> *Id.* at 1290; *see also* *Johnson v. Wells Fargo Home Mortgage, Inc.*, 635 F.3d 401, 415 n. 11 (9th Cir. 2011) (reaffirming that in the Ninth Circuit the manifest disregard standard has survived *Hall Street*).

<sup>118</sup> *Comedy Club*, 553 F.3d at 1290 (citing *Kyocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987, 997 (9th Cir 2003) (en banc) (holding that arbitrators exceed their powers when their decisions are completely irrational or when the arbitrators manifestly disregard the law)). *Accord* *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 548 F.2d 85, 95 (2d Cir. 2008) (holding that FAA § 10(a)(4) implies the manifest disregard standard because it includes, as a ground for judicial review of arbitration awards, a finding that the arbitrators “exceeded their powers”).

<sup>119</sup> *Comedy Club*, 553 F.3d at 1290.

Since established Ninth Circuit precedent was not “clearly irreconcilable”<sup>120</sup> with *Hall Street*, the Ninth Circuit held the manifest disregard standard viable.<sup>121</sup>

#### IV. THE SUPREME COURT’S LAPSE INTO SELF-CONTRADICTION

It is stunning that between *Wilko*, a 1953 decision arguably establishing the manifest disregard standard, and *First Options*, a 1995 decision arguably confirming the viability of that standard, the Supreme Court issued two opinions declaring that certain arbitral awards are subject to plenary review for errors of law. The decisions recognizing plenary review cannot be reconciled with the manifest disregard standard. The clash between the two standards is—manifest. To understand why the Supreme Court lapsed into self-contradiction, one must trace the evolution of arbitration policy.

##### A. Judicial Hostility Toward Arbitration Agreements

Before passage of the FAA, the widespread perception among businesspersons and legislators was that American common law courts, as a rule, refused to enforce arbitration agreements.<sup>122</sup> Though perhaps exaggerated,<sup>123</sup> the perception of judicial hostility toward arbitration had support in case law.<sup>124</sup> The courts’ rationale for this

<sup>120</sup> *Id.* at 1290 (citing *Miller v. Gammie*, 335 F.3d 889, 900 (9th Cir. 2003) (en banc) (holding that Ninth Circuit precedent will stand unless “clearly irreconcilable” with a Supreme Court ruling)).

<sup>121</sup> *Id.* at 1290; accord *Johnson v. Wells Fargo Home Mortgage, Inc.*, 635 F.3d 401, 415 n. 11 (9th Cir. 2011) (reaffirming that in the Ninth Circuit the manifest disregard standard has survived *Hall Street*).

<sup>122</sup> H.R. REP. NO. 68-96, *To Validate Certain Agreements for Arbitration*, at 1-2 (1924) (hereinafter “*House Report 1924*”) (“The need for the new law arises from an anachronism of our American law. Some centuries ago, because of the jealousy of the English courts for their jurisdiction, they refused to enforce specific agreements to arbitrate upon the ground that the courts were thereby ousted from their jurisdiction. This jealousy survived so long a period that the principle became firmly embedded in the English common law and was adopted with it by the American courts.”); *Arbitration of Interstate Commercial Disputes: Hearings on H.R. 646 and S. 1005 before the Joint Committee of Subcommittees on the Judiciary*, 68th Cong., at 14 (1924) (hereinafter “*Hearings 1924*”) (statement of Julius Henry Cohen) (“The difficulty is that men do enter into such [arbitration] agreements and then afterwards repudiate the agreement, and the difficulty has been that for over 300 years...the courts have said that that kind of an agreement was one that was revocable at any time. You go in and watch the expression on the face of your arbitrator and you have a ‘hunch’ that he is against you, and you withdraw and say, ‘I don’t believe in arbitration anymore.’”)

<sup>123</sup> See Michael H. LeRoy, *Crowning the New King: The Statutory Arbitrator and the Demise of Judicial Review*, 2009 J. DISP. RESOL. 1, 17 (2009) (commenting that, although some English courts invoked the ouster-of-jurisdiction doctrine to thwart arbitration, English courts generally enforced arbitration agreements); Paul L. Sayre, *The Development of Commercial Arbitration Law*, 37 YALE L.J. 595, 603-04 (1928) (expressing doubt that English courts were hostile to arbitration, since the prevalent practice was to secure damages for breach of the arbitration agreement through a bond); see, e.g., *Vynior’s Case*, 77 Eng. Rep. 597 (1609) (requiring a party who had posted a bond to pay damages for breaching an arbitration agreement).

<sup>124</sup> See, e.g., *Ins. Co. v. Morse*, 87 U.S. 445, 451 (1874) (declaring that “[a] man may not barter away his life or his freedom, or his substantial rights,” and that “agreements in advance

hostility – the ouster of jurisdiction doctrine – originated in eighteenth century English common law.<sup>125</sup> Protective of their power to decide cases, English courts sometimes voiced suspicion about the adequacy of the arbitral process to protect the rights of parties.<sup>126</sup> In *Scott v. Avery*,<sup>127</sup> for example, Baron Martin commented that “[u]pon the award being made, unless the arbitrators have been guilty of fraud, the courts have no power to inquire whether the arbitrators have awarded rightly or wrongly, according to law or against it.”<sup>128</sup> The ouster-of-jurisdiction doctrine migrated to the United States where many criticized the doctrine for thwarting arbitration.<sup>129</sup>

Congress passed the FAA to end the judiciary’s resistance to enforcing arbitration agreements.<sup>130</sup> Section § 2 of the FAA achieves this goal by providing that arbitration agreements are “valid, enforceable, and irrevocable.”<sup>131</sup> Yet, after passage of the FAA, *Wilko* refused to allow the arbitration of § 12(2) securities fraud claims.<sup>132</sup> The Supreme Court’s distrust of arbitration was reminiscent of the hostility expressed by English courts when invoking the ouster-of-jurisdiction doctrine.

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to oust the courts of the jurisdiction conferred by law are illegal and void.”); Leo Kanowitz, *Alternative Dispute Resolution and the Public Interest: The Arbitration Experience*, 38 HASTINGS L.J. 239, 252 (1987) (“In the past, although courts generally enforced arbitrators’ awards, they refused to grant specific performance of executory agreements to arbitrate future disputes.”).

<sup>125</sup> See, e.g., *Kill v. Hollister*, 1 Wils. 129 (1746) (holding that “the agreement of the parties cannot oust this court”). See generally Kenneth R. Davis, *The Arbitration Claws: Unconscionability in the Securities Industry*, 78 B.U.L. REV. 255, 261-63 (providing a history and analysis of English cases espousing the ouster-of-jurisdiction doctrine).

<sup>126</sup> *Scott v. Avery*, 10 Eng. Rep. 1121, 5 S.C.(H.L.) 811, 841 (1856) (opinion by Coleridge, J.) (“The courts will not enforce or sanction an agreement which deprives the subject of that recourse to their jurisdiction, which has been considered a right inalienable even by the concurrent will of the parties.”)

<sup>127</sup> *Id.*

<sup>128</sup> *Id.* at 829 (opinion of Martin, J.).

<sup>129</sup> See *Volt Info. Sciences, Inc. v. Leland Stanford Junior Univ.*, 489 U.S. 468, 474 (1989) (remarking that Congress enacted the FAA to overcome the judiciary’s refusal to enforce arbitration agreements) (citing *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 219-220 (1985)); *Kulukundis Shipping Co. v. Amtorg Trading Corp.*, 126 F.2d 978, 982-84 (2d Cir. 1942) (mocking the “hypnotic effect” of the ouster-of-jurisdiction doctrine); *United States Asphalt Ref. Co. v. Trinidad Lake Petrol. Co.*, 222 F. 1006, 1009 (S.D.N.Y. 1915) (criticizing the courts for applying the ouster-of-jurisdiction doctrine); House Report 1924, *supra* note 122, at 2 (“If one party is recalcitrant he can no longer escape his agreement, [and] [a]t the same time the party willing to perform his contract for arbitration is not subject to the delay and cost of litigation”).

<sup>130</sup> See, e.g., *Allied Bruce Terminix, Inc. v. Dobson*, 513 U.S. 265, 271 (1995) (noting that the purpose of the FAA is to put arbitration agreements “upon the same footing as other contracts”) (quoting *Volt*, 489 U.S. at 474).

<sup>131</sup> 9 U.S.C. § 2 (2000).

<sup>132</sup> *Wilko v. Swan*, 346 U.S. 427, 438 (1953).

### B. A Change of Policy

After *Wilko*, the Supreme Court began to rethink its distrust of arbitration until the Court changed its viewpoint and arbitration had the Court's unqualified support. In *Moses H. Cone v. Mercury Constr. Corp.*<sup>133</sup> the Court announced that "[s]ection 2 is a congressional declaration of a liberal federal policy favoring arbitration agreements."<sup>134</sup> Recognizing this policy, the Court in *Dean Witter Reynolds, Inc. v. Byrd*<sup>135</sup> observed that "[t]he prominent concern of Congress in passing the Act was to enforce private arbitration agreements . . . [which] requires that we rigorously enforce agreements to arbitrate."<sup>136</sup> Confirming this policy shift, a series of decisions declared virtually all federal statutory claims arbitrable. The Court applied its pro-arbitration policy to allow the arbitration of federal claims brought under anti-trust law, securities law, anti-racketeering law, and civil rights law.<sup>137</sup>

These decisions required the Court to address the standard of judicial review of awards because *Wilko*'s refusal to allow the arbitration of § 12(2) rested largely on the Court's concern over inadequate review.<sup>138</sup> The Supreme Court had two choices. It could either renounce its concern that arbitrators might commit legal error that would not be subject to judicial correction, or it could adopt a broader standard of judicial review to safeguard the rights of those submitting federal claims to arbitrators. The Court followed the second alternative, but only by resorting to more dicta, which regrettably has not supplanted the entrenched dicta of *Wilko*.<sup>139</sup>

#### 1. *McMahon* and *Gilmer*: The Shift Toward Expanded Review

The Supreme Court decided *Shearson/American Express Inc. v. McMahon*<sup>140</sup> in 1987, over three decades after *Wilko*. The McMahons had a brokerage account at Shearson, which contained a standard arbitration agreement.<sup>141</sup> Alleging securities fraud under § 10(b) of the Securities Exchange Act, the McMahons sued Shearson

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<sup>133</sup> *Moses H. Cone v. Mercury Constr. Corp.*, 460 U.S. 1, 25 (1982).

<sup>134</sup> *Id.* at 24.

<sup>135</sup> *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985).

<sup>136</sup> *Id.* at 221. See Maureen A. Weston, *The Supreme Court and Arbitration: The Other Avenues of Hall Street and Prospects for Judicial Review of Arbitral Awards*, 14 LEWIS & CLARK L. REV. 929, 930 (2010) (commenting that the Supreme Court, over the past 30 years, has adopted a pro-arbitration policy and supports upholding party intent expressed in arbitration agreements).

<sup>137</sup> See Part IV.B.1 (discussing Supreme Court cases that expanded the arbitrability of federal statutory claims).

<sup>138</sup> *Wilko v. Swan*, 346 U.S. 427, 437 (1953).

<sup>139</sup> See Part IV.B.1 (discussing decisions permitting the arbitration of a variety of federal claims).

<sup>140</sup> *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220 (1987).

<sup>141</sup> *Id.* at 222-23.

and their account representative in federal court.<sup>142</sup> The defendants moved to compel arbitration.<sup>143</sup>

The Court was dismissive of *Wilko*'s distrust of arbitration.<sup>144</sup> It had already upheld the arbitrability of antitrust claims<sup>145</sup> and § 10(b) securities fraud claim in an international context,<sup>146</sup> and it seemed eager to extend this rule to § 10(b) claims generally.<sup>147</sup> The Court, however, was obliged to reconcile the arbitrability of § 10(b) securities fraud claims with *Wilko*'s objection to that the scope of judicial review is insufficient to protect the rights of victims of securities fraud.<sup>148</sup> Upholding arbitrability while reaffirming ineffectual judicial review would have been untenable. The Court resolved this problem by issuing bold dicta that contradicted its notorious dicta in *Wilko*. The Court declared: "[W]e have indicated that there is no reason to assume at the outset that arbitrators will not follow the law; although judicial scrutiny of arbitration awards necessarily is limited, such review is sufficient to ensure that arbitrators comply with the requirements of the statute."<sup>149</sup> Reviewing awards for errors of law is far broader than the standard expressed in *Wilko*, which forecloses review for an arbitrator's "error in interpretation."<sup>150</sup>

Four years after *McMahon*, in *Gilmer v. Interstate/Johnson Lane Corp.*,<sup>151</sup> the Court held claims brought under the Age Discrimination in Employment Act arbitrable.<sup>152</sup> *Gilmer*, age 62, was a manager of financial services for Interstate/Johnson Lane.<sup>153</sup> As a condition of his employment, he signed an arbitration agreement.<sup>154</sup> When Interstate terminated his employment, he brought an action in federal district court, alleging age discrimination.<sup>155</sup> Interstate moved to compel arbitration.<sup>156</sup> *Gilmer* argued that "judicial review of arbitration decisions is

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<sup>142</sup> *Id.*

<sup>143</sup> *Id.*

<sup>144</sup> *Id.* at 233.

<sup>145</sup> *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 515-20 (1974) (holding arbitrable a securities claim brought by a Delaware corporation against a German national).

<sup>146</sup> *Mitsubishi Motors Corp. v. Soler-Chrysler Plymouth, Inc.*, 473 U.S. 614, 638 (1985) (holding that a Sherman Act antitrust claim alleged by a Puerto Rico corporation against a Japanese and a Swiss corporation was arbitrable).

<sup>147</sup> *Shearson/American Express Inc v. McMahon*, 482 U.S. at 220, 232-33 (1987).

<sup>148</sup> *See Wilko v. Swan*, 346 U.S. 427, 436 (1953).

<sup>149</sup> *Shearson/American Express Inc.*, 482 U.S. at 232.

<sup>150</sup> *Wilko*, 346 U.S. 427, 436-37.

<sup>151</sup> *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991).

<sup>152</sup> *Id.* at 23.

<sup>153</sup> *Id.*

<sup>154</sup> *Id.*

<sup>155</sup> *Id.* at 23-24.

<sup>156</sup> *Id.* at 24.



too limited” to protect victimized older workers from erroneous arbitral decisions.<sup>157</sup> Suggesting that it had resolved this concern in *McMahon*, the Court relegated this point to a footnote, quoting *McMahon*’s assurance that reviewing courts will enforce the requirements of the statute.<sup>158</sup> No further comment was needed.

## 2. Expedience over Principle

The *First Options* case was decided in 1995, after both *McMahon* and *Gilmer*.<sup>159</sup> It might seem odd that the Court, having endorsed expanded review in *McMahon* and *Gilmer*, reverted to the manifest disregard standard in *First Options*.<sup>160</sup> The reason for the Supreme Court’s fickleness might simply be explained by the cynical observation that, in each case from *Wilko* to *First Options*, the Court espoused the standard of review that provided the handiest justification for its ruling. In *Wilko*, the Court ruled against allowing the arbitration of § 12(2) securities fraud claims.<sup>161</sup> The absence of meaningful substantive review supported the decision.<sup>162</sup> *McMahon* and *Gilmer* conflicted with *Wilko* by allowing the arbitration of § 10(b) claims, RICO claims, and ADEA claims.<sup>163</sup> Part of the Court’s rationale for allowing the arbitration of these federal statutory claims was the availability of plenary court review for errors of law.<sup>164</sup> In *First Options*, the Court held that, under the facts of the case, the question of arbitrability was for the court to decide.<sup>165</sup> To assign the question of arbitrability to the arbitrator, the Court ruled, required clear and unmistakable evidence of party intent.<sup>166</sup> The Supreme Court justified this holding by noting the narrowness of the scope of judicial review. Like any issue submitted for arbitration, once the question of arbitrability is submitted to an arbitrator “the court will set [the arbitrator’s] decision aside only in very unusual circumstances.”<sup>167</sup>

## 3. Synthesis

Though expedience apparently influenced the Court, a valid policy concern unifies all four decisions. *Wilko*, *McMahon*, *Gilmer* and *First Options* all agree that a narrow scope of judicial review of awards deciding federal statutory rights is inadequate. Where federal statutory rights are arbitrated, whether they arise under

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<sup>157</sup> *Id.* at 32, n.4.

<sup>158</sup> *Id.*

<sup>159</sup> *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995).

<sup>160</sup> *Id.* at 942 (referring with approval to the manifest disregard standard).

<sup>161</sup> *Wilko v. Swan*, 346 U.S. 427, 438 (1953).

<sup>162</sup> *Id.* at 436.

<sup>163</sup> *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 35 (1991) (approving the arbitrability of ADEA claims); *Shearson American Express Inc. v. McMahon*, 482 U.S. 220, 238 (1987) (approving the arbitrability of Securities Exchange Act § 10(b) claims); *McMahon*, 482 U.S. at 242 (approving the arbitrability of RICO claims).

<sup>164</sup> *McMahon*, 482 U.S. at 232; *Gilmer*, 500 U.S. at 32 n.4.

<sup>165</sup> *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 944 (1995).

<sup>166</sup> *Id.* at 944.

<sup>167</sup> *Id.* at 942.

the securities laws, civil rights law, or other federal statutes, courts need to apply a rigorous standard of review to ensure that those rights are protected. Thus, in *Wilko* and *First Options*, where the Court directed the cases to the judicial system, the Court justified its decisions by stating that limited judicial review would be inadequate to protect the statutory rights at stake. In *McMahon* and *Gilmer*, where the Court directed the cases to arbitration, the Court insisted the level of scrutiny sufficient to protect the parties' statutory rights. The Court's concern for ensuring the enforcement of federal rights animates its pronouncements on the scope of review.

#### 4. Reactions of the Lower Courts

Many federal court decisions have reflected the concern to protect federal rights, either openly employing the broad standard of review espoused in *McMahon* and *Gilmer*, or refusing implicitly to apply the narrow manifest disregard standard.<sup>168</sup> The D.C. Circuit, for example, has applied the broad standard of judicial review adopted in *McMahon* and confirmed in *Gilmer* to awards resolving Title VII claims. In *Cole v. Burns International Security Service*,<sup>169</sup> Cole was a security guard working at Union Station in Washington, D.C. for LaSalle and Partners.<sup>170</sup> Burns Security took over the Union Station contract and required all La Salle employees, including Cole, to sign an arbitration agreement covering discrimination claims.<sup>171</sup> When Burns Security fired Cole two years later, he sued the company in federal court for racial discrimination. Burns Security moved to compel arbitration.<sup>172</sup>

Cole argued that the arbitration agreement was unenforceable because the scope of judicial review provided by the manifest disregard test was too lax to safeguard his Title VII rights.<sup>173</sup> The court disagreed, holding that, when arbitrators resolve civil rights claims, courts should review awards for errors of law.<sup>174</sup> In so holding, the D.C. Circuit relied on *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,<sup>175</sup> a Supreme Court case which held that Sherman Act antitrust cases, in an international context, are arbitrable.<sup>176</sup> The *Cole* court found the following passage from *Mitsubishi* persuasive: "By agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits to their

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<sup>168</sup> See *infra* notes 169-93 and accompanying text (discussing how some federal courts have balked at applying the manifest disregard standard).

<sup>169</sup> *Cole v. Burns Int'l Sec. Serv.*, 105 F.3d 1465 (D.C. Cir. 1997).

<sup>170</sup> *Id.* at 1469.

<sup>171</sup> *Id.*

<sup>172</sup> *Id.* at 1470.

<sup>173</sup> *Id.* at 1486.

<sup>174</sup> *Id.* at 1487.

<sup>175</sup> *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985). See also *Rodrigues de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 486 (1989) (noting that "resort to the arbitration process does not inherently undermine any of the substantive rights afforded to the petitioners under the Securities Act.").

<sup>176</sup> *Id.* at 640.

resolution in an arbitral, rather than a judicial, forum.”<sup>177</sup> Standing alone, this quote from *Mitsubishi* does not necessarily imply a plenary standard of review. The quote might simply mean that arbitrators should follow applicable statutory provisions, even though awards are not reviewable. The D.C. Circuit eliminated this possibility by quoting *McMahon’s* assurance that judicial review “is sufficient to ensure that arbitrators comply with the requirements of the statute.”<sup>178</sup> Merging *Wilko* and *McMahon*, the D.C. Circuit held that, in Title VII cases, the manifest disregard standard means unrestricted substantive review.<sup>179</sup>

The D.C. Circuit was right to rely on *McMahon*. It had no reason, however, to practice verbal alchemy, transforming “manifest disregard,” which, according to *Wilko*, forecloses review for an “error in interpretation,”<sup>180</sup> into judicial review for errors of law. The D.C. Circuit should simply have stated that manifest disregard is not the correct standard to apply to Title VII cases.

Other courts have strayed from *Wilko*, stretching the meaning of “manifest disregard” to encompass unintentional errors.<sup>181</sup> These courts, though claiming adherence to the manifest disregard standard, seem to apply a “knew or should have known” test for reviewing arbitral errors.<sup>182</sup> The explanation for this subterfuge is probably that some judges wince at the prospect of confirming a decision that would deprive a plaintiff of a federal right, whether arising out of civil rights law, securities law, or another federal statute. They simply must intervene. Murmurs of rebellion

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<sup>177</sup> *Id.* at 628.

<sup>178</sup> *Cole v. Burns Int’l Sec. Serv.*, 105 F.3d 1465 (D.C. Cir. 1997) (quoting *Shearson American Express, Inc. v. McMahon*, 482 U.S. 220, 232 (1987)).

<sup>179</sup> *Cole*, 105 F.3d at 1487; *contra DiRussa v. Dean Witter Reynolds Inc.*, 121 F.3d 818, 821-22 (1997) (rejecting *Cole’s* position that plenary judicial review should apply to arbitration awards construing federal statutory rights).

<sup>180</sup> *Wilko v. Swan*, 346 U.S. 427, 436-37 (1953).

<sup>181</sup> *See, e.g., Comedy Club, Inc. v. Improv West Assoc.*, 553 F.3d 1277, 1293 (9th Cir. 2009) (vacating arbitrator’s award for misconstruing controlling precedent limiting the scope of in-term non-compete covenants); *Coffee Beanery, Ltd. v. WW, L.L.C.*, 300 Fed. Appx. 415, 420 (6th Cir. 2008) (vacating arbitrator’s award because it improperly failed to find that the non-disclosure of a felony conviction violated the Maryland Franchise Act.); *DiRussa v. Dean Witter Reynolds, Inc.*, 121 F.3d 818, 822-23 (2d Cir. 1997), *cert. denied*, 118 S. Ct. 695 (1998) (denying motion to vacate because “at no point did DiRussa communicate . . . to the arbitrators that the ADEA mandated such an award [of attorneys’ fees] to a prevailing party.”); *Merrill Lynch, Pierce, Fenner & Smith v. Jaros*, 70 F.3d 418, 421 (6th Cir. 1995) (holding that arbitrators manifestly disregard the law when they adopt a line of legal reasoning that no judge could reasonably defend); *DeGaetano v. Smith Barney, Inc.*, 983 F. Supp. 459 (S.D.N.Y. 1997) (vacating arbitration panel’s award because the panel erroneously denied attorney’s fees to a prevailing complainant in a Title VII sexual harassment case). In *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197, 204 (2d Cir. 1998), the Second Circuit went even further by vacating an arbitration award that denied a federal age discrimination claim because the arbitrators ignored “the law or the evidence or both.”

<sup>182</sup> *See, e.g., DiRussa*, 121 F.3d at 822-23 (2d Cir. 1997) (suggesting that if plaintiff had either explained to the arbitration panel that the ADEA mandates the award of attorney’s fees to a prevailing party or quoted the relevant ADEA section, the panel’s denial of an award of attorney’s fees to plaintiff would have manifestly disregarded the law).

against the manifest disregard standard have been heard for years in some quarters of the federal judiciary.

For example, in *DeGaetano v. Smith Barney, Inc.*,<sup>183</sup> DeGaetano commenced arbitration before the New York Stock Exchange, alleging sexual harassment against Smith Barney, her former employer, and against her former supervisor.<sup>184</sup> She submitted a memorandum of law to the arbitration panel in which she asserted that, if she prevailed on her sexual harassment claim, the panel was obligated to award her attorneys' fees.<sup>185</sup> The panel awarded DeGaetano over \$90,000 in damages and interest, but it denied her attorneys' fees.<sup>186</sup> The panel stated that it did "not find that the conduct of the Respondents rose to the level contemplated by Title VII and therefore [the panel] den[ied] the requests for punitive damages and attorney's fees."<sup>187</sup>

Ruling on DeGaetano's motion to vacate that part of the award denying her attorneys' fees, Judge Cote faithfully recited the definition of the manifest disregard test and then abandoned it.<sup>188</sup> Judge Cote observed that DeGaetano was incorrect when she instructed the panel that, under Title VII, a prevailing party is entitled to attorney's fees, because awarding attorney's fees is discretionary, not mandatory.<sup>189</sup> Nevertheless, Judge Cote noted that plaintiffs in Title VII cases "ordinarily" recover attorneys' fees "unless special circumstances would render such an award unjust."<sup>190</sup> Judge Cote concluded that there were no special circumstances justifying the panel's denial of DeGaetano's request for attorney's fees.<sup>191</sup> The panel, according to her, confused the generous standard for awarding attorneys' fees with the more stringent standard for awarding punitive damages.<sup>192</sup> Judge Cote therefore held that this error amounted to manifest disregard of the law.<sup>193</sup>

This decision is hard to reconcile with the traditional manifest disregard standard. DeGaetano had misinformed the panel that she was entitled as a matter of law to attorneys' fees. Perhaps the panel felt that her misstatement of the law constituted "special circumstances" to deny such an award. Alternatively, if the panel did confuse the standard for awarding attorneys' fees with the standard for awarding punitive damages, as Judge Cote concluded, the panel did not intentionally ignore the law. Judge Cote may have claimed fidelity to the manifest disregard standard, but she applied a "knew or should have known" test, which came perilously close to plenary review for errors of law.

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<sup>183</sup> *DeGaetano*, 983 F. Supp. 459.

<sup>184</sup> *Id.* at 460.

<sup>185</sup> *Id.* at 461.

<sup>186</sup> *Id.*

<sup>187</sup> *Id.*

<sup>188</sup> *Id.* at 461-62.

<sup>189</sup> *Id.*

<sup>190</sup> *Id.* (quoting *Hensley v. Eckerhart*, 461 U.S. 424, 429 (1983)).

<sup>191</sup> *Id.* at 462.

<sup>192</sup> *Id.* at 463-64.

<sup>193</sup> *Id.*

Judge Cote, however, deserves no criticism. Tacit rejections of the manifest disregard standard are welcome. The evolution of arbitration since the passage of the FAA demands broadening the role of judicial oversight.

### C. *The Purpose of the FAA*

Before the passage of the FAA in 1925, arbitration was, for the most part, a process to resolve contract disputes between merchants.<sup>194</sup> The principal architect of the FAA, Julius Henry Cohen described the FAA as a “great tonic” for those engaged “in the field of commercial activity.”<sup>195</sup> The primary purpose of the FAA was to provide a method of dispute resolution for merchants and businessmen that would be less costly and less time-consuming than litigation. Urging passage of the FAA, Charles Bernheimer, chairman of the committee on arbitration of the New York State Chamber of commerce, testified, “The most unprofitable thing the merchant and business man, or anyone engaged in buying and selling, can have confront him is that of litigation.”<sup>196</sup>

The trend away from the courthouse and toward arbitration gained momentum in the early twentieth century. Arbitration met the needs of those involved in trade disputes, since customs, known to arbitrators with experience in the relevant industry, often provided the preferred rule of decision.<sup>197</sup> It is not surprising that by 1920 “trade associations . . . [frequently] . . . require[d] their members to submit their disputes to arbitration . . . .”<sup>198</sup>

Because customs replaced law and industry experts replaced judges, the need to review arbitration awards for substantive legal error was minimal.<sup>199</sup> The framers of the FAA, however, could not have foreseen the widespread use of arbitration to resolve federal statutory claims. While limited judicial review is appropriate for

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<sup>194</sup> See, e.g., *E. Gerli & Co. v. Oscar Heineman Corp.*, 258 N.Y. 484, 485-86 (1932) (confirming award that quality of silk delivered to merchant buyer was sub-standard); *Red Cross Line v. United Fruit Co.*, 264 U.S. 109 (1924) (alleging that a steamship operator breached a charter party by unreasonably delaying performance); *Itoh & Co. v. Boyer Oil Co.*, 191 N.Y. Supp. 290 (1921) (refusing to vacate award finding that the quality of hemp seed shipped to buyer was acceptable); Philip G. Phillips, *Legislation and Administration*, 1 U. CHI. L. REV. 424, 429 (1934) [hereinafter “*Legislation and Administration*”]; Philip G. Phillips, *Rules of Law or Laissez-Faire in Commercial Arbitration*, 47 HARV. L. REV. 590, 596-603 (1934) [hereinafter “*Rules of Law*”] (listing categories of business claims arbitrated before passage of the FAA); *Arbitration of Interstate Commercial Disputes: Joint Hearing on S. 1005 and H.R. 646 Before the Subcomm. of the Comm. on the Judiciary*, 68<sup>th</sup> Cong. 10 (1924) (statement of W.H.H. Piatt testifying, “Men have found that if they must arbitrate at once they proceed to carry out their contracts.”).

<sup>195</sup> *Arbitration of Interstate Commercial Disputes: Joint Hearing on S. 1005 and H.R. 646 Before the Subcomm. of the Comm. on the Judiciary*, 68<sup>th</sup> Cong. 16 (1924) (testimony of Julius Henry Cohen).

<sup>196</sup> *Arbitration of Interstate Commercial Disputes: Joint Hearing on S. 1005 and H.R. 646 Before the Subcomm. of the Comm. on the Judiciary*, 68<sup>th</sup> Cong. 6 (1924) (testimony of Charles L. Bernheimer).

<sup>197</sup> See *Legislation and Administration*, *supra* note 194, at 426-27.

<sup>198</sup> *Rules of Law*, *supra* note 194, at 590.

<sup>199</sup> *Id.*

contract claims, the adequacy of limited review for federal statutory claims is dubious. As Justice Clark observed, “Commercial arbitration has been highly successful in bringing a businessman’s adjudication to business questions. But it would be vastly unfortunate if it became usable as a device to blunt or break social legislation.”<sup>200</sup>

When Congress passed the FAA, it could not have imagined the type, the range, and the volume of federal statutory claims that would, as a matter of common practice, find their way to arbitration. In 1925, Congress had not yet passed any federal securities law. Neither the Securities Act of 1933,<sup>201</sup> nor the Securities Exchange Act of 1934<sup>202</sup> existed, and there was no Financial Industry Regulatory Authority (FINRA) to administer the thousands of securities arbitrations that are heard every year in its hearing rooms.<sup>203</sup> There was no 1964 Civil Rights Act,<sup>204</sup> no Age Discrimination in Employment Act,<sup>205</sup> and no Americans with Disabilities Act.<sup>206</sup> RICO, the anti-racketeering law, was still 45 years away.<sup>207</sup>

One policy of the FAA was to provide an efficient method of dispute resolution for business.<sup>208</sup> Efficiency meant distancing the courts from the process. To achieve this separation, the FAA established a narrow scope of judicial review, which prescribed nullification of awards for “fraud or other corruption or undue influence, or [for] some evident mistake not affecting the merits . . . .”<sup>209</sup> But the decision to limit the scope of review to issues of gross procedural unfairness was based on the understanding that arbitration was an economical method to resolve disputes involving merchants belonging to trade associations, and between others in the business of buying and selling goods and services. Congress could not have contemplated that the FAA would govern the arbitration of women harassed by the

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<sup>200</sup> Wilko v. Swan, 201 F.2d 439, 445 (2d. Cir. 1953) (Clark, J., dissenting).

<sup>201</sup> Securities Act of 1933, 15 U.S.C. §§ 77a-77bbbb (2006).

<sup>202</sup> Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78pp (2006).

<sup>203</sup> The Financial Industry Regulatory Authority, Inc. (“FINRA”), the only self-regulatory organization for the securities industry, operates the largest dispute resolution forum providing mediation and arbitration services for claims between and among investors, securities firms, and registered representatives. See FINRA, ARBITRATION & MEDIATION (2012), <http://www.finra.org/ArbitrationAndMediation/index.htm>.

There were 7,137 arbitration cases filed with FINRA in 2009. FINRA, *FINRA Dispute Resolution*, ARBITRATION & MEDIATION (Jan. 27, 2011), [http://www.finra.org/ArbitrationAndMediation/FINRA\\_Dispute\\_Resolution/AdditionalResources/Statistics/](http://www.finra.org/ArbitrationAndMediation/FINRA_Dispute_Resolution/AdditionalResources/Statistics/). In 2010, there were 5,680 filings. *Id.* As of December 2011, there were 4,729 filings. *Id.*

<sup>204</sup> Title VII of the Civil Rights Act of 1964, 42 U.S.C. §§ 2000e-2000h-6 (2006).

<sup>205</sup> Age Discrimination in Employment Act, 29 U.S.C. §§ 621-634 (2006).

<sup>206</sup> Americans with Disabilities Act, 42 U.S.C. §§ 12101-12213 (2006).

<sup>207</sup> Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (2006).

<sup>208</sup> See *supra* note 196 and accompanying text (discussing the FAA policy to promote efficiency).

<sup>209</sup> H.R. REP. NO. 68-96, 2 (1924) (report of Congressman Graham from the Committee on the Judiciary).

sexual conduct of their supervisors, or of retirees wiped out by unscrupulous stockbrokers who gambled funds in Ponzi schemes. One must question whether a civil rights claim of a black worker, fired because of his race, should be unreviewable if the arbitrator denied the claim because he erroneously applied the *McDonnell Douglas*<sup>210</sup> framework to the exclusion of the more plaintiff-friendly motivating factor test approved in *Costa* for all individual disparate treatment cases.<sup>211</sup> One must question whether an erroneous award denying a § 10(b) securities fraud claim should stand because a shrewd lawyer convinced a panel of arbitrators that the statute of limitations in § 804 of Sarbanes-Oxley did not apply to claims brought under the Securities Exchange Act.<sup>212</sup>

#### D. Policy Considerations

Applying plenary review for errors of law when a federally protected right is asserted reconciles the pro-arbitration policy of the FAA and the policies of federal statutes that protect substantive rights. This approach permits the arbitration of claims asserting such rights, while protecting those rights with adequate review. In addition, the approach taken in *McMahon* and *Gilmer* advances the FAA policy of honoring party intent. When parties agree to arbitrate a federal statutory right, they reasonably expect that right to be protected. The federal courts should honor that expectation.

Efficiency is also a hallmark of arbitration.<sup>213</sup> This policy, however, sometimes conflicts with the policy promoting party intent. An expansive level of judicial review for awards deciding federal claims would, to some extent, decrease efficiency. In *Dean Witter Reynolds Inc. v. Byrd*,<sup>214</sup> the Supreme Court seemed to resolve this conflict of policies in favor of party intent. The Supreme Court emphasized in *Byrd*: “We therefore reject the suggestion that the overriding goal of the Arbitration Act was to promote the expeditious resolution of claims.”<sup>215</sup> The

<sup>210</sup> *McDonnell Douglas Corp. v. Green*, 411 U.S. 792, 802-05 (1973) (establishing the three-step burden-shifting framework for deciding individual disparate treatment cases).

<sup>211</sup> *Desert Palace, Inc. v. Costa*, 539 U.S. 90, 98-99 (2003) (holding that the mixed-motive analysis prescribed in 42 U.S.C. § 2000e-2(m) applies to cases based on circumstantial evidence). Suppose, for example, that an arbitrator believes that he or she must choose between the *McDonnell Douglas* framework and the mixed-motive framework to determine the validity of a claim. The arbitrator applies the *McDonnell Douglas* framework because the plaintiff focused primarily on disproving the defendant’s non-discriminatory explanation. Finding that the plaintiff has failed to disprove the defendant’s non-discriminatory explanation, the arbitrator rules against the plaintiff, although there is strong evidence that the plaintiff could have met the motivating-factor test based on flagrantly racist statements that his supervisor made after firing him.

<sup>212</sup> 28 U.S.C. § 1658(b) (2006) (providing that securities fraud claims may be brought within five years of the violation but no longer than two years after discovery). Before the passage of Sarbanes-Oxley, federal securities law claims had to be brought within three years of the violation but no longer than one year after discovery. 15 U.S.C. § 78i(f). See *Lampf v. Gilbertson*, 501 U.S. 350, 364 n.9 (1991).

<sup>213</sup> See *supra* note 196 and accompanying text (discussing the FAA policy to promote efficiency).

<sup>214</sup> *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985).

<sup>215</sup> *Id.* at 219.

Court went on to declare, “the Act was motivated, first and foremost, by a congressional desire to enforce agreements into which parties had entered, and we must not overlook this principal objective when construing the statute, or allow the fortuitous impact of the Act on efficient dispute resolution of overshadow the underlying motivation.”<sup>216</sup> In *AT&T Mobility LLC v. Concepcion*,<sup>217</sup> however, the Court retreated from its statement in *Byrd*, declaring that it is “greatly misleading” to argue that *Byrd* recognized party intent as the primary policy of the FAA.<sup>218</sup> Once again the Supreme Court contradicted itself.

Even if the policy favoring efficiency is placed on a par with the policy favoring party intent, the two policies may be reconciled. The diminution in efficiency occasioned by implementing the standard of review suggested in *McMahon* and *Gilmer* is not a serious one. Efficiency arises from numerous other features of arbitration such as relaxed pleading requirements and evidentiary rules, limited discovery and motion practice, and an expedited hearing schedule. Other features of arbitration such as the parties’ contractual control over the proceedings, privacy, confidentiality, and arbitrator expertise—which are all reasons that motivate parties to arbitrate—are untouched by expanded review.<sup>219</sup> It should be noted too that, while applying the manifest disregard standard, courts routinely analyze the principles of controlling law and sometimes delve into the hearing record to determine whether the arbitrator committed an error justifying vacatur. If awards deciding federal statutory claims were subjected to plenary review for errors of law, the augmented role of the judiciary would not be as daunting as some might fear.<sup>220</sup>

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<sup>216</sup> *Id.* at 220.

<sup>217</sup> *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011).

<sup>218</sup> *Id.* at 1749. The Supreme Court in *Hall Street* also minimized *Byrd*’s unequivocal endorsement of party intent as the FAA’s dominant policy. The Court stated, “Despite the [*Byrd*] opinion’s language ‘reject[ing] the suggestion that the overriding goal of the [FAA] was to promote the expeditious resolution of claims’ the holding mandated immediate enforcement of an arbitration agreement; the Court was merely trying to explain that the inefficiency and difficulty of conducting simultaneous arbitration and federal-court litigation was not a good enough reason to defer the arbitration.” *Hall Street Assocs., LLC v. Mattel, Inc.*, 552 U.S. 576, 588 (2008). The Court’s protestations amount to judicial hocus pocus. Even while attempting to diffuse the policy statement in *Byrd*, the *Hall Street* Court strengthened it. As the *Hall Street* Court conceded, the rationale for “conducting simultaneous arbitration and federal-court litigation” was the primacy of the policy of honoring party intent rather than the policy of promoting efficiency.

<sup>219</sup> Professor Tom Ginsburg believes that “[p]arties will always be unwilling to arbitrate under a regime of *de novo* review, because it confers no advantages over going directly to court.” Tom Ginsburg, *The Arbitrator as Agent: Why Deferential Review Is Not Always Pro-Arbitration*, 77 U. CHI. L. REV. 1013, 1025 (2010). He does agree, however, that parties “will also be reluctant to arbitrate if the arbitrator is unlikely to resolve their dispute according to the agreed-upon law.” *Id.*

<sup>220</sup> Scholars, while generally critical of the manifest disregards standard, have debated whether the scope of judicial review of arbitration awards should be expanded or contracted. Professors Brunet and Johnson argue persuasively for expanded review of awards issued under the aegis of the NASD (now FINRA). They state: “Unlike traditional arbitration involving contractual disputes, SRO [self-regulatory organization] arbitrations adjudicate nonwaivable statutory rights. In legitimizing mandatory SRO arbitration, the Supreme Court presumed that arbitration was only a procedural choice, not a substantive choice . . . The Court



*E. Statutory Rationale*

The statutory rationale for plenary review for errors of federal statutory law appears in § 10(a)(4) of the FAA, the subsection requiring vacatur when the arbitrators exceeded their authority.<sup>221</sup> When parties arbitrate federally protected rights, they implicitly instruct the arbitrators to uphold their rights. No sensible person would arbitrate a securities fraud claim or a racial discrimination claim if he or she thought the process provided no safeguards to ensure that the law would be applied correctly. As noted above, a basic precept of arbitration policy is to respect the intent of the parties to an arbitration agreement.<sup>222</sup> By erring, arbitrators breach the intent of the parties to ensure the application of statutory rights and therefore exceed their authority. Moreover, the public policies vindicated in the statutes granting such rights do not permit the arbitrators to deny claimants such rights, intentionally or unintentionally. Under § 10(a)(4), correction of such errors falls to the courts.<sup>223</sup>

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also assumed that judicial review, although limited, would be ‘sufficient to ensure that the arbitrators comply with the requirements of the statute.’ As explained elsewhere, however, there is no meaningful judicial review of SRO arbitration awards.” Brunet and Johnson, *supra* note 2, at 489-90. See also Leroy, *supra* note 123, at 24 (contending that “Gilmer’s theory of forum substitution means that federal courts should vacate arbitration awards and court judgments [deciding federal statutory claims] at equal rates.”). But see Richard C. Reuben, *Building the Civilization of Arbitration: Personal Autonomy and Vacatur After Hall Street*, 113 PENN. ST. L. REV. 1103, 1127-28 (2009) (arguing for the abandonment of the manifest disregard standard and against any substantive review because “from the perspective of the courts, it is hard to imagine a move more detrimental to judicial efficiency than permitting expanded judicial review.”); Hayford, *supra* note 14, at 841 (advocating limited judicial review such that “[u]nless the commercial arbitration award is flawed by the types of party, advocate, or arbitrator misconduct defined in section 10(a) of the FAA, or compels the violation of a well defined and dominant public policy, the parties to a commercial arbitration agreement are stuck with the result the arbitration proceeding produces.”).

<sup>221</sup> See 9 U.S.C. § 10(a)(4) (2006).

<sup>222</sup> Professor Stipanowich has expressed the case for the primacy of party intent persuasively. He has stated: “[T]he central and primary value of arbitration is not speed, or economy, or privacy, or neutral expertise, but rather the ability of users to make key process choices to suit their particular needs . . . Choice is what sets arbitration apart from litigation. If parties truly desire an expedited procedure in which speed and economy are the preeminent goals, it is possible to structure and implement a ‘lean program’ to achieve those ends at the cost of various procedural bells and whistles. Expedited arbitration may also be utilized to strike a balance between the need for final adjudication and the maintenance of an ongoing commercial relationship. If, on the other hand, cost-savings and a quick result are much less important than controlled ‘quasi-litigation’—extensive legal due process with a tribunal comprised of three grand old ships-of-the-line that results in a highly ‘authoritative’ decision—that too is an option.” Thomas J. Stipanowich, *Arbitration: The New Litigation*, 2010 U. ILL. L. REV. 1, 51-52 (2010).

<sup>223</sup> Numerous courts have held that a violation of a well-defined and dominant public policy is a judicially created ground for vacatur, rather than a ground for vacatur under § 10(a)(4). See, e.g., *Lewis v. Circuit City Stores, Inc.*, 500 F.3d 1140, 1150-51 (10th Cir. 2007) (stating that the public policy exception is a “common law” ground of review); *Greenburg v. Bear, Stearns & Co.*, 220 F.3d 22, 27 (2d Cir. 2000) (noting that the public policy exception is a ground of review additional to those prescribed in § 10 of the FAA); *Seymour v. Blue Cross/Blue Shield*, 988 F.2d 1020, 1023 (10th Cir. 1993) (confirming that

One might argue that by invoking the intent of the parties to liberalize the scope of judicial review, expanded review conflicts with *Hall Street*'s holding that parties cannot contractually broaden the scope of review of arbitration awards.<sup>224</sup> There is no such conflict. First, the argument for expanded review applies only to awards denying claims of federal rights. *Hall Street* did not assert such a claim, but rather sought to enforce its contractual right of indemnification against Mattel.<sup>225</sup> Second, the argument for expanded review proposes that the courts interpret § 10(a)(4) to permit such review. Although drawing on the policy to uphold party intent, the argument for expanded review is statutory.

Since *Hall Street* and *Concepcion*,<sup>226</sup> the survival of the manifest disregard standard has become dubious. If the Supreme Court rejects the narrow manifest disregard standard, it will surely reject a broader standard of review for errors of law. The only alternative is for Congress to intervene. It should consider the state of arbitration today rather than the state of arbitration in 1925. If it views the FAA, not as a static law but as a dynamic one, it should fashion the FAA into a modern arbitration statute in a climate where virtually any federal claim is arbitrable and thousands of such claims are arbitrated every year.

#### F. Review of Awards Not Deciding Federal Statutory Rights

Thousands of claims, not asserting federal statutory rights, also go to arbitration. Until *Hall Street*, the entire federal judiciary, following *Wilko*'s dicta, applied the manifest disregard standard indiscriminately to all arbitration awards. It is absurd to apply the same standard of review to arbitrations resolving claims for breach of contract and to arbitrations resolving claims for racial discrimination. The mechanical application of this flawed, single standard of review is like forcing everyone to fit into the same pair of worn out shoes.

#### V. *STOLT-NIELSEN V. ANIMALFEEDS AND BEYOND*

This Part will begin with an analysis of *Stolt-Nielsen S.A. v. AnimalFeeds International Corp.*,<sup>227</sup> in which the Supreme Court applied *de novo* review to a

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the public policy exception is a "judicially-created ground for vacating an arbitration award."). If courts do not consider the "public policy exception" to fall within § 10(a)(4) of the FAA, it is unlikely that, without a directive from the Supreme Court, they would hold that § 10(a)(4) covers violations of federal statutory rights. Professor Mercantel believes that the courts should reconsider this position and hold that when arbitrators issue awards that offend a dominant public policy they have exceeded their authority. See Jonathan A. Mercantel, *The Crumbled Difference Between Legal and Illegal Arbitration Awards: Hall Street Associates and the Waning Public Policy Exception*, 14 FORDHAM J. CORP. & FIN. L. 597, 634 (2009) (arguing that "while section 10(a)(4) has not been interpreted as including the public policy exception in the past, nothing would preclude the courts from simply expanding their interpretation of section 10(a)(4) to include the public policy exception.").

<sup>224</sup> *Hall Street Assocs., LLC. v. Mattel, Inc.*, 552 U.S. 576, 586 (2008) (holding that the grounds for vacatur prescribed in the FAA are exclusive).

<sup>225</sup> *Id.* at 579-81.

<sup>226</sup> See *infra* note 268 and accompanying text (declaring that the grounds for vacatur in the FAA focus on misconduct rather than mistake).

<sup>227</sup> *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 130 S. Ct. 1758 (2010).

partial arbitration award. By doing so, the Court hinted that it might entertain broadening the standard of review under appropriate circumstances. This possibility was extinguished in *AT&T Mobility LLC v. Concepcion*.<sup>228</sup> This Part will also discuss the public policy exception, which directs courts to correct errors in awards that violate well-defined federal public policy. After approving of the public policy exception, this Part will discuss the appropriate standard of review for awards that do not decide federal statutory rights or violate well-established public policy. It will conclude that federal courts should not review such awards for errors of law, even if those errors are manifest. Finally, this Part will refute the argument that the proposal in this Article would defeat the efficiency of arbitration.

#### A. *The Stolt-Nielsen Decision: A Glimmer of Hope*

The *Stolt-Nielsen* decision is both provocative and curious because the Court's rhetoric did not match its analysis. The Court concluded that the manifest disregard standard was met, although there was no showing whatsoever that the arbitration panel intentionally flouted of the law. Rather, the Court merely found that the arbitration panel had made ordinary legal and factual errors.

##### 1. Facts and Procedural Background

A supplier of liquid ingredients to producers of animal feed, AnimalFeeds entered into contracts, known as Vegoilvoy charter parties, to ship products to its customers.<sup>229</sup> An arbitration clause was a standard provision included in these charter parties.<sup>230</sup> When, in 2003, AnimalFeeds learned that a Department of Justice investigation had revealed illegal price-fixing activities by shipping companies, AnimalFeeds brought a putative class action against a number of such companies, including Stolt-Nielsen, alleging antitrust violations.<sup>231</sup> In 2005, AnimalFeeds served a demand for class arbitration on the defendant shipping companies.<sup>232</sup>

The parties agreed to submit to a panel of three arbitrators the issue whether the class action was arbitrable.<sup>233</sup> After conducting hearings, the arbitrators ruled that the arbitration clause permitted class arbitration.<sup>234</sup> The shipping companies moved to vacate the partial award, and the district court granted the motion on the ground

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<sup>228</sup> *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1752 (2011).

<sup>229</sup> *Stolt-Nielsen S.A.*, 130 S. Ct. at 1754 (2010).

<sup>230</sup> *Id.* at 1765. The arbitration clause provided: "Any dispute arising from the making, performance or termination of this Charter Party shall be settled in New York, Owner and Charterer each appointing an arbitrator, who shall be a merchant, broker or individual experienced in the shipping business; the two thus chosen, if they cannot agree, shall nominate a third arbitrator who shall be an Admiralty lawyer. Such arbitration shall be conducted in conformity with the provisions and procedures of the United States Arbitration Act [the FAA], and a judgment of the Court shall be entered upon any award made by said arbitrator."

<sup>231</sup> *Id.*

<sup>232</sup> *Id.*

<sup>233</sup> *Id.* The panel was to follow the rules of the American Arbitration Association's Supplemental Rules for Class Arbitrations. *Id.*

<sup>234</sup> *Id.* at 1766.

that the arbitrators had manifestly disregarded the law.<sup>235</sup> The district court found that the arbitrators failed to make any meaningful choice-of-law analysis.<sup>236</sup> Clear cut choice-of-law rules, the court reasoned, pointed to the applicability of maritime law, which, under industry custom and practice, showed that the arbitration clauses in question foreclosed class arbitration.<sup>237</sup> The Second Circuit reversed, noting, “Had the district court been charged with reviewing the arbitration panel’s decision *de novo*, we might well find its analysis persuasive. But the errors it identified do not, in our view, rise to the level of manifest disregard of the law.”<sup>238</sup>

## 2. The Supreme Court’s Distortion of “Manifest Disregard”

The Supreme Court analyzed the case under FAA § 10(a)(4), which provides that a court may vacate an award when the arbitrators “exceeded their authority.”<sup>239</sup> Since *Stolt-Nielsen* also argued that the Second Circuit erred in holding that the arbitrators had not manifestly disregarded the law, the Supreme Court commented on whether the manifest disregard standard survived *Hall Street*. The Court stated: “We do not decide whether ‘manifest disregard’ survives our decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. 576, 585 (2008), as an independent ground for review or as a judicial gloss on the enumerated grounds for vacatur set forth in 9 U. S. C. § 10.”<sup>240</sup> Nevertheless, in addition to analyzing the case under the exceeded-their-authority test, the Court analyzed the case under the manifest

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<sup>235</sup> *Id.*

<sup>236</sup> *Id.*

<sup>237</sup> *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 435 F. Supp. 2d 382, 384-86 (S. D. N. Y. 2006).

<sup>238</sup> *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 548 F.3d 85, 96 (2d Cir. 2008). As a preliminary matter, the Second Circuit held that the manifest disregard standard survived *Hall Street* as a judicial gloss on the exceeding-their-authority ground for vacatur prescribed in § 10(a)(4) of the FAA. *Id.* at 95. Applying the standard, the Second Circuit showed that, contrary to the conclusion reached by the district court, the arbitrators did not manifestly disregard choice-of-law principles by failing to undertake a choice-of-law analysis. *Id.* at 96-97. First, *Stolt-Nielsen*’s brief to the arbitrators referred to choice-of-law in a single footnote without supporting authority. *Id.* at 96. More importantly, *Stolt-Nielsen* conceded in the footnote that the arbitrators “need not decide this [choice-of-law] issue, however, because the analysis is the same under either [New York law or maritime law].” *Id.* Furthermore, the arbitrators did consider the choice-of-law issue. Their award stated that they “must look to the language of the parties’ agreement to ascertain the parties’ intention whether they intended to permit or to preclude class action. This is . . . consistent with New York State law . . . and federal maritime law,” which, the Second Circuit explained, merely provide guidelines rather than fixed rules of decision. *See id.* at 97-99.

<sup>239</sup> *Stolt-Nielsen*, 130 S. Ct. 1758, 1767-68 (2010). The majority found that the panel had exceeded its authority. *Id.* at 1767-68. Justice Ginsburg disagreed. She noted that *Stolt-Nielsen* asserted only one statutory ground for vacatur. *Stolt-Nielsen* argued that the panel had exceeded its authority. She pointed out that by “referring the class-arbitration issue to an arbitration panel,” the parties had “undoubtedly empowered the arbitrators to render their clause-construction decision. That scarcely debatable point should resolve this case.” *Id.* at 1780 (Ginsburg, J., dissenting).

<sup>240</sup> *Id.* at 1768 n.3 (internal citations omitted).

disregard standard, adopting AnimalFeeds' definition *arguendo*.<sup>241</sup> This definition stated that arbitrators have manifestly disregarded the law when they "knew of the relevant [legal] principle, appreciated that this principle controlled the outcome of the disputed issue, and nonetheless willfully flouted the governing law by refusing to apply it."<sup>242</sup> The Court concluded that, under the circumstances presented on appeal, this standard was satisfied.<sup>243</sup>

Scrutinizing the Supreme Court's analysis reveals, however, that the Court applied a more exacting test than that permitted by the manifest disregard standard: It engaged in *de novo* review. In analyzing the award, the Court speculated that the panel impermissibly disregarded the parties' agreement against class arbitration and imposed on the parties the panel's view of public policy.<sup>244</sup> However, the Court's criticism of the panel centered on the weight the panel gave to certain factual submissions – an approach not permitted by the manifest disregard standard – and on the legal conclusions the panel made when endeavoring to resolve a complex question of unsettled law that might have vexed experienced judges.<sup>245</sup>

It is striking that the Court faulted the arbitrators' findings of fact. The Court criticized the arbitrators for giving insufficient weight to evidence that the Vegoilvoy Charter Party had never provided the basis for class arbitration.<sup>246</sup> It also chided the arbitrators for not being persuaded by expert speculation that sophisticated multinational commercial parties would never intend the arbitration clauses in question to authorize class arbitration.<sup>247</sup>

To the extent that the Court relied on the panel's "mistaken" factual findings to conclude that the panel manifestly disregarded the law, the Court misapplied the manifest disregard standard. Any judicial review of the factual basis for an award, let alone scrutiny at such a microscopic level, clashes with the precept of limited judicial review. In *Wallace v. Buttar*,<sup>248</sup> the Second Circuit stated a fundamental principle of arbitration, noting that "[a] federal court may not conduct a reassessment of the evidentiary record."<sup>249</sup> The standard of review is restricted to manifest

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<sup>241</sup> *Id.* at 1768 n.3.

<sup>242</sup> *Id.*

<sup>243</sup> *Id.*

<sup>244</sup> *Id.* at 1768.

<sup>245</sup> See *infra* notes 245-263 and accompanying text (discussing the reasoning of the Supreme Court majority in the *Stolt-Nielsen* opinion).

<sup>246</sup> *Stolt-Nielsen*, 130 S. Ct. at 1769. Justice Ginsburg countered with the panel's suggestion that, if a class were certified, only parties willing to participate would opt in and those unwilling to participate would be excluded from the class. *Id.* at 1781 (Ginsburg, J., dissenting).

<sup>247</sup> *Id.* at 1769.

<sup>248</sup> *Wallace v. Buttar*, 378 F.3d 182 (2d Cir. 2004).

<sup>249</sup> *Id.* at 193; see also *Electro Sci. Indus., Inc. v. Dooley*, No. 10CV1564AC, 2011 WL 1883850 (D. Ore. May 17, 2011) (refusing to vacate award because the court has no authority to re-weigh evidence offered at the arbitration hearing); *Coutee v. Barington Capital Grp., L.P.*, 336 F.3d 1128, 1133 (9th Cir. 2003) (noting that "[m]anifest disregard of the facts is not an independent ground for vacatur in this circuit."); *French v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 784 F.2d 902, 906 (9th Cir. 1986) (stating that a court will not confirm an award with

disregard of the law, not the evidence.<sup>250</sup> By sifting through the record in *Stolt-Nielsen* and weighing the evidence, the Supreme Court ignored this fundamental principle. Of course, the Supreme Court may establish any standard of review it wishes, but it is remarkable that, while professing fidelity to the manifest disregard standard, the Court breached the narrow confines of that standard.

The Supreme Court's criticisms of the panel's legal analysis also failed to meet the manifest disregard standard. The Court faulted the panel for not following "court cases denying the consolidation of arbitrations,"<sup>251</sup> though, as the Court itself emphasized, the issue presented in the *Stolt-Nielsen* case was unsettled.<sup>252</sup> The issue had been presented in *Green Tree Financial Corp. v. Bazzle*,<sup>253</sup> but, the *Stolt-Nielsen* Court pointed out that only a plurality of the *Bazzle* Court reached a consensus on that issue.<sup>254</sup> The Court chided the panel for concluding incorrectly that *Bazzle* "controlled" the "resolution" of the question whether the Vegoilvoy charter party "permit[s] this arbitration to proceed on behalf of a class."<sup>255</sup>

Though the *Stolt-Nielsen* Court was right in pointing out that *Bazzle* was merely a plurality decision and therefore not binding precedent,<sup>256</sup> the panel's reading of *Bazzle* was essentially correct. The *Bazzle* plurality stated that, when an agreement is silent on the issue of class arbitration, the issue is for the arbitrator, not the courts, to decide.<sup>257</sup> It was understandable, if not appropriate, for the panel to have relied on the *Bazzle* plurality decision, because *Bazzle* was the most authoritative statement on the issue. Nevertheless, the *Stolt-Nielsen* Court lamented that "both the parties and the arbitration panel seem to have misunderstood *Bazzle*, [believing] that it established the standard to be applied by a decision maker in determining whether a contract may permissibly be interpreted to allow class arbitration."<sup>258</sup>

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"erroneous findings of fact"); *Success Sys., Inc. v. Maddy Petroleum Equip., Inc.*, 316 F. Supp. 2d 93, 94 (D. Conn. 2004) (observing that "the Second Circuit does not recognize manifest disregard of the evidence as a proper ground for vacating an arbitrator's award."). *But see* *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197, 204 (2d Cir. 1998) (vacating award based on "manifest disregard" of the evidence). *Halligan*, however, contradicts the view followed overwhelmingly by the federal judiciary. *See* Norman S. Poser, *Judicial Review of Arbitration Award: Manifest Disregard of the Law*, 64 BROOKLYN L. REV. 471, 503 (1998) (calling the *Halligan* decision a "radical departure from existing arbitration law").

<sup>250</sup> *Wallace*, 378 F.3d at 193.

<sup>251</sup> *Stolt-Nielsen S.A. v. AnimalFeeds International Corp.*, 130 S. Ct. 1758, 1769 (2010).

<sup>252</sup> *Id.* at 1772.

<sup>253</sup> *Id.* at 1770. *See* *Green Tree Fin. Corp. v. Bazzle*, 539 U.S. 444 (2003).

<sup>254</sup> *Stolt-Nielsen*, 130 S. Ct. at 1772.

<sup>255</sup> *Id.* at 1770.

<sup>256</sup> *Green Tree Fin. Corp.*, 539 U.S. at 447.

<sup>257</sup> *Id.* at 453. The plurality stated: "The question here—whether the contracts forbid class arbitration—does not fall within this narrow exception [gateway matters that are for the court to decide]. . . . It concerns contract interpretation and arbitration procedure. Arbitrators are well situated to answer that question. Given these considerations, along with the arbitration contracts' sweeping language concerning the scope of the questions committed to arbitration, this matter of contract interpretation should be for the arbitrator, not the courts, to decide." *Id.*

<sup>258</sup> *Stolt-Nielsen*, 130 S. Ct. at 1772.

The Court then proceeded to resolve the issue whether the parties had agreed to class arbitration. Its resolution conflicted with the position of the *Bazzle* plurality. Emphasizing the FAA's policy to honor party intent, the Court believed that "the differences between bilateral and class-action arbitration are too great for arbitrators to presume, consistent with their limited powers under the FAA, that the parties' mere silence on the issue of class-action arbitration constitutes consent to resolve their disputes in class proceedings."<sup>259</sup> The Court stressed that the parties' stipulation that there was "no agreement" to proceed as a class foreclosed any possibility of an agreement for class arbitration.<sup>260</sup>

Joined by Justices Stevens and Breyer, Justice Ginsburg wrote a dissenting opinion,<sup>261</sup> aptly accusing the majority of "indulging in *de novo* review."<sup>262</sup> The majority had not found that the panel had flouted the law. At most, the panel had failed to anticipate the Court's new rule restricting class arbitration.<sup>263</sup> Although the Court claimed to apply the manifest disregard standard, it applied the broadest form of review.<sup>264</sup>

#### B. AT&T Mobility LLC v. Concepcion: *All Hope Lost?*

The *Stolt-Nielsen* decision might have been read as an indication of the Court's willingness to consider expanding the scope of judicial review under appropriate circumstances. Such a reading, however, became untenable with *AT&T Mobility LLC v. Concepcion*.<sup>265</sup> In *Concepcion*, the Supreme Court held that the FAA

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<sup>259</sup> *Id.* at 1776.

<sup>260</sup> *Id.* See also *id.* at 1766. The majority made much of what they construed as a concession by AnimalFeeds' counsel who said to the arbitration panel, "All the parties agree that when a contract is silent on the issue there's been no agreement that has been reached on [that] issue . . ." *Id.* Justice Ginsburg quoted the remainder of the sentence, which the majority had conveniently omitted. "[T]herefore there has been *no agreement to bar class arbitrations.*" Then, as Justice Ginsburg noted, counsel clarified his statement by adding, "It's also undisputed that the arbitration clause here contains broad language and this language should be interpreted to permit class arbitrations." *Id.* at 1781 (Ginsburg, J., dissenting).

<sup>261</sup> *Id.* at 1777 (Ginsburg, J., dissenting). Justice Ginsburg argued that the case was not ripe for review by the Supreme Court because the panel's decision was "abstract and highly interlocutory." *Id.* at 1778. All the panel had ruled, she noted, was that the charter party permitted class arbitration. The panel had not decided whether AnimalFeeds' claims were suitable for class arbitration or who might be eligible for inclusion if such a class were certified. *Id.*

<sup>262</sup> *Id.* (Ginsburg, J., dissenting). Justice Ginsburg criticized the majority for "substitut[ing] its judgment for that of the decisionmakers chosen by the parties." *Id.* It is curious that while applying a rigorous standard of review the Court insisted that the scope of review for arbitral awards is limited. *Id.* at 1776.

<sup>263</sup> *Id.* at 1775-76.

<sup>264</sup> But see S.I. Strong, *Does Class Arbitration "Change the Nature" of Arbitration?* *Stolt-Nielsen, AT&T and a Return to First Principles*, 17 HARV. NEGOT. L. REV. at 52. (forthcoming 2012) available at <http://ssrn.com/abstract=1791928> (fearing that *Stolt-Nielsen* may foreshadow that "courts would not only permit review of partial final awards, but would use a less deferential standard such as review for a mistake of law.").

<sup>265</sup> *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740 (2011).

preempts a California judicial rule prohibiting class arbitration waivers in consumer contracts of adhesion.<sup>266</sup> To support its holding, the Court contrasted the scope of review of a court decision with the scope of review of an arbitration award. After noting that a lower court decision is reviewed *de novo* for errors of law, the *Concepcion* Court highlighted the narrow scope of review under § 10 of the FAA. The Court stated:

Section 10 “allows a court to vacate an arbitral award *only* where the award” ‘was procured by corruption, fraud, or undue means’; ‘there was evident partiality or corruption in the arbitrators’; ‘the arbitrators were guilty of misconduct in refusing to postpone the hearing...or in refusing to hear evidence pertinent and material to the controversy[,] or of any other misbehavior by which the rights of any party have been prejudiced’; or if the arbitrators ‘exceeded their powers or so imperfectly executed them that a mutual, final, and definite award ... was not made.’<sup>267</sup>

This statement confirmed *Hall Street*’s holding that the FAA provides the exclusive grounds for vacatur. The *Concepcion* Court, however, added that “review under § 10 focuses on misconduct rather than mistake.”<sup>268</sup> This conception of review—foreclosing the correction of errors of law—dispels any thoughts that *Stolt-Nielsen* signaled the Court’s receptivity to any form of expanded review. There is, however, one ground of substantive review that will likely survive *Hall Street* and *Concepcion*.

### C. The Public Policy Exception

Federal courts have long vacated awards that offend “well accepted and deep rooted public policy.”<sup>269</sup> Courts have applied the public policy exception to prevent

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<sup>266</sup> *Id.* at 1753.

<sup>267</sup> *Id.* at 1752.

<sup>268</sup> *Id.*

<sup>269</sup> *Diapulse Corp. of America v. Carba, Ltd.*, 626 F.3d 1108, 1110 (2d Cir. 1980). In *W.R. Grace & Co. v. Local 259, Int’l Union of United Rubber Workers*, 461 U.S. 757 (1983), the Supreme Court stated that such a public policy must be “well defined and dominant, and . . . ascertained ‘by reference to the laws and legal precedents and not from general considerations of supposed public interests.’” (quoting *Muschany v. United States*, 324 U.S. 49, 66 (1945)). In *United Paperworkers Int’l Union v. Misco, Inc.*, 484 U.S. 29 (1987), the Supreme Court followed this strict definition of public policy. Cooper, a Misco employee, operated heavy equipment. After he was twice reprimanded for operating the equipment negligently, the company discovered that he was a marijuana user and fired him. Cooper filed for arbitration under his collective bargaining agreement. *Id.* at 33. The arbitrator ordered Cooper’s reinstatement and the circuit court vacated the award. The Supreme Court reversed the order of the circuit court, *id.* at 44, holding, that, although sensible, the public policy proclaimed by the circuit court was not based on settled doctrine. *Id.* at 35. Although *W.R. Grace* and *Misco* are cases arising under the Labor Management Relations Act, the federal courts have accepted a similar public policy standard in commercial arbitration cases arising under the FAA. *See, e.g., Cole v. Burns Int’l Sec. Services*, 105 F.3d 1465, 1486 (D.C. Cir. 1997) (quoting *Misco* with approval and stating that awards resulting from the mandatory arbitration of federal statutory claims are subject to at least the same rigor of review that applies to awards resulting from labor arbitration); *Bd. of Cnty. Comm’rs of Lawrence Cnty. v. L. Robert Kimball & Associates.*, 860 F.2d 683, 686 (6th Cir. 1988) (stating that public policy review of



the enforcement of awards that would endanger public health or safety, or order the performance of illegal acts.<sup>270</sup> For example, in *Diapulse Corp. of America v. Carba, Ltd.*,<sup>271</sup> Diapulse manufactured the “Diapulse Machine,” a medical device designed to promote healing.<sup>272</sup> Diapulse entered into a distributorship agreement with Carba engaging Carba as its exclusive sales representative in Germany and Switzerland.<sup>273</sup> When Carba began marketing its new “lonar” device in competition with the Diapulse Machine, Diapulse initiated arbitration seeking to enforce a non-competition clause in the distributorship agreement.<sup>274</sup> The arbitrator issued an award, which, without specifying any geographical boundary or time limitation, barred Carba from selling devices “similar” to the Diapulse Machine.<sup>275</sup> The district court held that the award, which was both vague and overbroad, constituted an unreasonable restraint of trade violating federal public policy. Accordingly, the court modified the award.<sup>276</sup>

Although *Hall Street* and *Concepcion*, taken together, show that the Supreme Court, at least for the present, rejects expanded review, the public policy exception will likely survive.<sup>277</sup> One can hardly contemplate that the Court would countenance

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commercial arbitration awards is at least as rigorous as public policy review of labor arbitration awards).

<sup>270</sup> See Kenneth R. Davis, *When Ignorance of the Law is No Excuse: Judicial Review of Arbitration Awards*, 45 BUFF. L. REV. 49, 109 (1997) (noting that the courts will not confirm commercial arbitration awards that endanger public health or safety, or order specific enforcement of illegal contracts).

<sup>271</sup> *Diapulse*, 626 F.3d at 1108.

<sup>272</sup> *Id.* at 1009.

<sup>273</sup> *Id.*

<sup>274</sup> *Id.*

<sup>275</sup> *Id.* at 1110.

<sup>276</sup> *Id.* The Second Circuit held that the district court overstepped its authority, under § 10 and § 11 of the FAA, by modifying the award. *Id.* Addressing the public policy issue, the Second Circuit vacated the award as “indefinite” under §10(d) of the FAA. *Id.* at 1111. The Second Circuit instructed the district court to refer the matter back to the arbitrator for clarification of the award. *Id.*

<sup>277</sup> *Stolt-Nielsen*, 130 S. Ct. at 1776 (2010). One author is concerned that *Hall Street* has abolished the public policy exception for reviewing arbitration awards. He reasons as follows: “*Hall Street* held that the grounds for vacatur enumerated in the FAA are exclusive. Since the public policy exception is nonstatutory, *Hall Street* has abolished it.” Mercantel, *supra* note 223, at 624-25. Another scholar is more optimistic. He states, “The public policy exception is well-grounded and well-established, and nothing in the *Hall Street* opinion evinces an intent to eliminate it. It seems likely that courts will [continue to] recognize a public policy exception . . . at least for illegal arbitration awards . . . . Less certain is whether courts will extend that exception to include the broader class of ‘well defined and dominant’ policies recognized in *Misco*.”). Reuben, *supra* note 220, at 1143. Professor Reuben is probably closer to the truth. It is inconceivable that courts will confirm awards threatening public health or safety, or ordering the performance of illegal acts. See *Globe Newspaper Co. v. Int’l Ass’n of Machinists*, 648 F. Supp. 2d 193, 194 (D. Mass. 2009) (supporting the vitality of the public policy exception post-*Hall Street*); MyLinda K. Sims & Richard A. Bales, *Much Ado About Nothing: The Future of Manifest Disregard After Hall Street*, 62 S.C. L. REV. 407, 433 (2010)

an award that endangered public health or safety. The Court would seem compelled to invalidate dangerous and illegal awards. It is inconceivable that the Court would confirm an award that blessed the unlawful monopolization of the high tech industry, or the dangerous operation of a nuclear facility. To justify the continued viability of the public policy exception, one might reason that neither *Hall Street* nor *Concepcion* considered or decided the propriety of the public policy exception. Furthermore, *Concepcion*'s pronouncement on the narrow scope of review was merely dicta. The *Hall Street* Court's use of the word "exclusive" must be read within the context of the facts presented in the case and the Court's ruling, which merely rejected the right of the parties to expand the scope of review in an arbitration agreement.

#### D. All Other Cases

This Article proposes that federal courts apply plenary review for errors of law when either federal statutory rights or federal public policy is at stake. These two circumstances, however, do not apply to a sizeable number of arbitrations. Any comprehensive framework should propose a standard of judicial review that would apply to the cases that do not fit the *McMahon* or public policy mold.

When parties submit an issue for arbitration to a trade association or an arbitration organization, they often do not specify the law that will control. In such cases, there should be no review for errors of law under the FAA. The reason for this deferential standard is that, without instructions to the contrary, arbitrators are free to decide matters before them according to their own sense of justice. One scholar has commented, "Arbitrators are not compelled to apply rules of substantive law. The weight of authority permits an arbitrator to 'do justice as he sees it' and fashion an award that embodies the individual justice required by a given set of facts."<sup>278</sup> Given that arbitrators are generally not bound to apply substantive law, courts have no basis to review awards for legal error. In *Lentine v. Fundaro*,<sup>279</sup> the New York Court of Appeals upheld an arbitration award distributing the assets of a partnership in liquidation.<sup>280</sup> Writing for the court, Judge Breitel explained that the court would not invalidate an arbitration award on the ground that the arbitrator committed an error of law.<sup>281</sup> He noted, "Absent provision to the contrary in the

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(suggesting that the public policy exception survived *Hall Street*, and concluding that *Hall Street*'s statement that the grounds for vacatur in the FAA are exclusive must refer only to contractual expansion of the scope of review and not to judicially-created grounds because "[i]t is illogical to 'cherry pick' the [judicially-created] grounds that survive post-*Hall Street*."); Codie Henderson, *The Hall Street Hangover: Recovering and Rediscovering Avenues for Review of Arbitration Awards*; *Hall Street Assocs. v. Mattel Inc.*, 128 S. Ct. 1396 (2008), 10 WYO. L. REV. 299, 314 (2010) (suggesting that the public policy exception will survive *Hall Street* because review for violations of public policy does not require a review into the merits of the award and also because "public policy has an established history in the law and would be difficult to supplant.").

<sup>278</sup> See Edward Brunet, *Arbitration and Constitutional Rights*, 71 N.C. L. REV. 81, 85 (1996).

<sup>279</sup> *Lentine v. Fundaro*, 278 N.E.2d 633 (N.Y. App. Div. 1972).

<sup>280</sup> *Id.* at 636.

<sup>281</sup> *Id.* at 635-36.

arbitration agreement, arbitrators are not bound by principles of substantive law . . .

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In the absence of a directive from the parties to apply particular law, the policy of the FAA to promote efficiency in arbitration dovetails with the primary policy of the FAA, which is to honor party intent. Any level of substantive review would conflict with the policy promoting efficiency since review injects cost and delay into the dispute resolution process. Similarly, substantive review would conflict with party intent by imposing a legal regime on the parties against their wishes as expressed in their arbitration agreement.

Parties often include a choice-of-law clause in their arbitrate agreements.<sup>283</sup> Although such a clause binds the arbitrator, it creates no obligation for a federal court to review an award for errors of law. The *Hall Street* decision, which holds that the FAA forbids parties from contractually expanding judicial review to correct errors of law, is consistent with this principle.<sup>284</sup>

State law policy may be implicated if an arbitrator misapplies state law, but, absent unusual circumstances, federal policy is not. Long before enactment of the FAA, parties to arbitration agreements sometimes chose to be governed by state law, and the courts then, as now, honored such contractual provisions.<sup>285</sup> Section 9 of the

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<sup>282</sup> *Id.* at 385, 635. See also *Shearson/American Express Inc. v. McMahon*, 482 U.S. 220, 259 (1987) (Blackmun, J., concurring in part and dissenting in part) (noting that “arbitrators are not bound by precedent”); *Liggett v. Torrington Bldg. Co.*, 158 A. 917, 919 (Conn. 1932) (noting that “[a]rbitrators, being customarily chosen by the parties because of special knowledge or skill in connection with the matter to be decided, are not bound to follow strict rules of law, unless it be made a condition of the submission, but are expected to determine the questions presented to them in light of their own special skill and knowledge.”); *Mayberry v. Mayberry*, 28 S.E. 349, 350 (1897) (commenting that “[a]rbitrators are a law unto themselves and may decide according to their views of justice”); *Soia Mentschikoff, Commercial Arbitration*, 61 COLUM. L. REV. 846, 867 (1961) (stating that arbitrators for trade associations have the task of “selecting the most relevant or appropriate norms”).

<sup>283</sup> See *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 64 (1995) (holding that a New York choice-of-law provision in a standard securities account agreement did not prevent arbitrators from awarding punitive damages); *Volt Info. Sciences, Inc. v. Bd. of Trustees of Leland Stanford Junior University*, 489 U.S. 468, 491 (1989) (Brennan, J., dissenting) (commenting that “[m]ost commercial contracts written in this country contain choice-of-law clauses”); Thomas A. Diamond, *Choice of Law Clauses and Their Preemptive Effect upon the Federal Arbitration Act: Reconciling the Supreme Court with Itself*, 39 ARIZ. L. REV. 35, 35 (1997) (noting that parties often agree to both an arbitration clause and a choice-of-law clause).

<sup>284</sup> *Hall Street Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576, 579 (2008) (holding that the FAA does not permit the parties to an arbitration agreement to require the courts to correct awards “where the arbitrator’s conclusions of law are erroneous”).

<sup>285</sup> *In re of Wilkins*, 62 N.E. 575, 576 (N.Y. App. Div. 1902) the New York Court of Appeals stated: “Where the merits of a controversy are referred to an arbitrator selected by the parties, his determination, either as to the law or the facts, is final and conclusive, and a court will not open an award unless perverse misconstruction or positive misconduct upon the part of the arbitrator is plainly established, or there is some provision in the agreement of submission authorizing it.” (emphasis added); see also *Lentine v. Fundaro*, 278 N.E. 2d 633, 635 (1972) (citing pre-1925 cases for the proposition that arbitrators must follow the law when the arbitration agreement so provides); cf. *Leete v. Griswold Post No. 79, American Legion*, 158 A. 919 (1932) (noting that arbitrators are bound by the law if the parties’

FAA provides that an award must be confirmed unless one of the grounds enumerated in § 10 or § 11 requires its nullification.<sup>286</sup> Congress elected not to include errors of law as an enumerated ground for vacatur. Although Congress did not contemplate that this exclusion would apply to awards deciding federal statutory rights, Congress surely intended that this exclusion would apply to cases where the parties chose to be governed by state law. It appears therefore that Congress, when passing the FAA, did not intend for federal courts to review arbitration awards for errors of state law.

By denying substantive review in such cases, the courts are promoting efficiency in arbitration by minimizing federal court involvement. State court involvement is another matter. If an arbitrator reaches an erroneous decision on a matter of state law, the appropriate remedy is to seek vacatur under state arbitration law, not under the FAA.

#### *E. Reduced Efficiency*

Opponents of the proposal in this Article will undoubtedly argue that, if implemented, the proposal would reduce the efficiency of arbitration. Review for errors of law in awards resolving claims asserting federal statutory rights would arguably increase the role of the courts in the process. For those who value the simplicity and economy of arbitration, such a development would be anathema.<sup>287</sup> This fear, however, is unfounded. The prevailing narrow scope of review has not deterred lawyers from seeking vacatur of awards. Courts have therefore been obliged to analyze the legal grounds allegedly supporting vacatur. Judicial decisions plumbng arbitral awards for manifest disregard of the law frequently inhabit the case-law reporters.<sup>288</sup> Implementing the approach proposed in the Article would probably not increase the judicial caseload materially.

The expenditure of judicial energy needed to determine whether an arbitrator manifestly disregarded the law would not differ substantially to if at all, from the time and effort required to determine if an award failed to uphold a federal right. The approach advocated in this Article might even reduce the burden on the

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submission directs them to follow the law.) New York statutory law and decisional law were particularly central to the shaping of federal arbitration policy and passage of the FAA. In 1920, New York State passed the first pro-arbitration statute in the United States, and the FAA was modeled after the New York statute. *See* Joint Hearings before the Sub Committee of the Committees on the Judiciary, *supra* note 122 (Statement by Julius Henry Cohen to Subcommittees on the Judiciary noting that the FAA was patterned after the New York State arbitration statute, which in 1920 became the first pro-arbitration statute in the country); *see* also Brian T. Burns, 78 *FORD. L. REV.* 1813, 1818 (2010) (reporting that Congress patterned the FAA after the New York state arbitration statute and sometimes looked to decisions of the New York Court of Appeals for guidance on how to characterize arbitration).

<sup>286</sup> *See* 9 U.S.C.A. § 9 (West 2011).

<sup>287</sup> *See* Reuben, *supra* note 220, at 1127 (arguing that “from the perspective of the courts, it is hard to imagine a move more detrimental to judicial efficiency than permitting expanded judicial review.”).

<sup>288</sup> *See* Ashby Jones, *Arbitration: Increasingly, It’s Not over Until the Vacatur Motion Fails* (Feb. 2010), <http://blogs.wsj.com/law/2011/02/14/arbitration-increasingly-it-s-not-over-until-the-vacatur-motion-fail/> (reporting that in 2010 federal and states courts issued 208 written decisions on motions to vacate arbitration awards).

judiciary compared to the burden imposed by the manifest disregard standard. In all cases where a party moves to vacate an award, the court must identify controlling law and determine if the arbitrator committed error. The manifest disregard standard adds the step of determining whether the arbitrator knew the law and deliberately flouted it. The scrutiny that the Supreme Court exercised in *Stolt-Nielsen* is an extreme example of the depths of analysis to which a court may resort when searching for manifest disregard of the law.

If the proposal in this Article were adopted, a reduction in the judicial workload would result from awards not deciding federal rights or violating federal public policy. Awards deciding state-law claims would receive no substantive review. Equally important, the approach proposed in this Article reconciles conflicts between FAA policy and policies of federal substantive law. The manifest disregard standard fails to reach a sensible or workable reconciliation of these policies. Having no review for awards deciding federal statutory rights is even less acceptable than the manifest disregard standard.

Some might prefer a single standard of review to the standard proposed in this Article. A single-standard approach, however, lacks the sensitivity to evaluate awards appropriately. The relative strength of competing policies must set the agenda for a more finely calibrated system of judicial review. Furthermore, the current state of the law recognizes a hodgepodge of nonstatutory standards of review, all of which could be discarded if the approach proposed in this Article were adopted.<sup>289</sup> This approach would promote simplicity by eliminating three current standards of review for arbitration awards: the “irrational” test, the “completely irrational” test, and the “arbitrary and capricious” test.<sup>290</sup> Courts would review awards for erroneously denying federal rights and violating federal public policies. In such cases, courts would not have to consider questions of irrationality or capriciousness. In all other cases, the courts would provide no level of review at all. The task of reviewing such awards would fall to state arbitration law and state court judges.

## VI. CONCLUSION

Since the Supreme Court decided *Wilko* in 1953, the scope of substantive review for arbitration awards has bred uncertainty among the courts and dismay among litigants unable to predict what level of review the courts will apply or how they will apply it. The *Hall Street* Court speculated about what “manifest disregard” means and whether it is even a viable doctrine, but the Court gave no answers. Confused by the Supreme Court’s indecision, the circuit courts are divided on whether the

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<sup>289</sup> See, e.g., Davis, *A Model for Arbitration*, *supra* note 1, at 167-208 (discussing the mélange of non-statutory grounds of review for arbitration awards).

<sup>290</sup> See, e.g., *Kyocera Corp. v. Prudential-Bache Servs.*, 341 F.3d 987, 997 (9th Cir. 2003) (holding that a court may vacate a “completely irrational” award); *Ainsworth v. Skurnick*, 960 F.2d 939, 941 (11th Cir. 1992) (vacating arbitrary and capricious award); *Swift Indus., Inc. v. Botany Indus., Inc.*, 466 F.2d 1125, 1135 (3d Cir. 1972) (vacating completely irrational award); *Rivera v. Thomas*, 316 F. Supp. 2d 256, 262 (D. Md. 2004) (vacating an irrational arbitration award); *Prudential-Bache Sec., Inc. v. Corporale*, 664 F. Supp. 72, 75 (S.D.N.Y. 1987) (confirming award because it was rational); *Sargent v. Paine Webber, Jackson & Curtis, Inc.*, 674 F. Supp. 920, 922 (D.D.C. 1987) (stating that an award must be vacated where the “arbitrator reveals *no support whatever for his determinations*”) (quoting *NF & M Corp. v. United Steelworkers of America*, 524 F.2d 756, 760 (3d Cir. 1975)).

manifest disregard standard survived *Hall Street*. Some courts apply the standard to all awards, whether the awards resolve claims of flagrant sexual harassment or claims of minor breach of contract. They should not. The manifest disregard standard is too blunt an instrument to handle such wide-ranging issues. Other courts have dispensed with the manifest disregard standard. These courts apply no substantive review at all to awards deciding federal claims, confirming troublesome awards that deny claimants their rights under the securities laws and civil rights laws. This trend is likely to grow after *Concepcion*.

Arbitration law needs a framework for reviewing arbitration awards that is both workable and sensible. This Article proposes that awards deciding federal statutory rights should be subject to review for errors of law. Similarly, awards violating federal public policy must be corrected. All other awards should receive no substantive review in the federal courts.

The Supreme Court has a disappointing record on establishing a sensible or even a comprehensible framework. *Wilko* did not supply the answer. Its ill-conceived pronouncement invoking the phrase “manifest disregard” has contaminated arbitration law long enough. *Hall Street*’s wordplay with the phrase “manifest disregard” turned the law into a puzzle. *Concepcion* has transformed *McMahon*’s assurance of expanded review into a supreme fib, and the gap between the rhetoric and analysis in *Stolt-Nielsen* is as daunting as Zeno’s paradox. The Supreme Court has had 60 years to set things right. That’s longer than Moses wandered in the wilderness. Maybe it’s time for Congress to act.