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THE MANIFEST DISREGARD OF LAW DOCTRINE: WHAT DOES THE FUTURE HOLD?

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The doctrine of manifest disregard of law as a basis for vacating arbitration awards traces its origins to a 1953 opinion of the United States Supreme Court, *Wilko v. Swan*, 346 U.S. 427, 436-37 (1953), in which the Supreme Court stated 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." There is not much controversy or disagreement in court opinions as to the parameters of the manifest disregard of law doctrine. Remarkably, since February 2007, eight Circuit Courts of Appeal[1] have issued fourteen opinions[2] discussing the manifest disregard of law ground for vacating arbitration awards.

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[1] Opinions dealing with this doctrine have been issued since February 2007 by the Second, Third, Fourth, Eighth, Ninth, Tenth, Eleventh and District of Columbia Circuits. Other Circuits have issued similar opinions. *See e.g., Wise v. Wachovia Securities, LLC*, 450 F.3d 265 (7th Cir. 2006).

[2] Second Circuit: *Porzig v. Dresdner, Kleinwort, Benson, North America LLC*, 497 F.3d 133 (2d Cir. 2007) (application is "appropriately rare;" two elements of the doctrine); *Appel Corp. v. Katz*, 217 Fed.Appx. 3, 2007 WL 419190 (2d Cir. Feb. 2, 2007) (unreported) (the arbitrators' explanation of their award was far more than the "barely colorable justification for the outcome" required to make the doctrine not applicable).

Third Circuit: *Sherrock Bros., Inc. v. Daimlerchrysler Motors Co, LLC*, 2008 WL 63300 (3d Cir. Jan. 7, 2008) (more than mere legal error or misunderstanding, must "fly in the face of clearly established legal precedent") (unreported); *Five Star Parking v. Union Local 723*, 246 Fed.Appx. 135, 2007 WL 2110716 (3d Cir. July 24, 2007) (manifest disregard established if contract construction is totally unsupported by principles of contract construction; serious error does not suffice) (unreported); *Sutter v. Oxford Health Plans LLC*, 227 Fed.Appx. 135, 2007 WL 625625 (3d Cir. Feb. 28, 2007) (general statement) (unreported).

Fourth Circuit: *Long John Silver's Restaurants, Inc. v. Cole*, 514 F.3d 345 (4th Cir. 2008) (statement of two elements).

Eighth Circuit: *Hall v. American General Financial Services, Inc.*, 2008 WL 222300 (8th Cir. Jan. 29, 2008) (general statement) (unpublished); *Pirooz v. MEMC Electronic Materials, Inc.*, 237 Fed.Appx. 125, 2007 WL 1881112 (8th Cir. July 2, 2007) (adopting district court's opinion without comment) (unpublished); *Hudson v. ConAgra Poultry Co.*, 484 F.3d 496 (8th Cir. 2007) (general statement).

The manifest disregard doctrine is very narrow, and is applicable only in rare circumstances. The formulation of the manifest disregard of law standard in these opinions is fairly uniform, requiring that two elements be proven:

1. the arbitrator(s) knew of a governing legal principle yet refused to apply it or ignored it; and

2. the law ignored by the arbitrator(s) was well-defined, explicit, not reasonably debatable and clearly applicable to the case.

The fact that a judge or appellate panel believes that the arbitrator(s) misapplied the law does not constitute manifest disregard of law. *Sherrock Bros., Inc.; Alred; Five Star Parking; Hicks.* There are sometimes practical problems in the implementation of this doctrine. If there is no binding precedent in the court applying the doctrine on the legal issue underlying the claim, there may not be any law that can be manifestly disregarded. *Collins v. D. R. Horton, Inc.*, 505 F.3d 874 (9th Cir. 2007). If there is no record of the arbitration proceedings, or no reasoned award, it may not be possible to prove the elements of the doctrine. *OneBeacon America Ins. Co. v. Turner*, 204 Fed.Appx. 383, 2006 WL 3102578 (5th Cir. Oct. 30, 2006) (lack of record made it impossible to establish that the arbitral panel was aware of binding law on the issue presented); *Van Pelt v. UBS Financial Services, Inc.*, 2007 WL 2997598 (W.D. N.C. Oct. 12, 2007) ("Since the panel was silent as to its reasoning for the compensatory damages, UBS cannot meet its burden of showing that the panel manifestly disregarded the law …."). The lack of a reasoned award may present a particular problem in reinsurance arbitrations, which frequently do not involve reasoned awards. This standard of review is much more difficult to sustain than the normal appellate review standard, which may result in reversal if the lower court erred in interpreting the law.

In *Hall Street Associates, LLC v. Mattel, Inc.*, No. 06-989 (Mar. 25, 2008), the United States Supreme Court made it clear that the grounds for vacating or modifying arbitration awards set out in the Federal Arbitration Act ("FAA") are the exclusive grounds upon which federal courts may modify or vacate such awards. The Supreme Court rejected the proposition that parties could, by contract, agree to different bases upon which federal courts could vacate or

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Ninth Circuit: *Collins v. D. R. Horton, Inc.*, 505 F.3d 874 (9th Cir. 2007) (statement of two elements; mere error of law insufficient); *Comedy Club, Inc. v. Improv West Associates*, 514 F.3d 833 (9th Cir. 2008) (as amended) (general statement in the context of whether the award was "completely irrational," traditionally a second judicially created basis for vacation of an award).

Tenth Circuit: *Hicks v. Bank of America, N.A.*, 218 Fed.Appx. 739, 2007 WL 521175 (10th Cir. Feb. 21, 2007) ("willful inattentiveness to the governing law;" more than error).

Eleventh Circuit: *Alred v. AVIS Rent-a-Car*, 247 Fed.Appx. 167, 2007 WL 2110720 (11th Cir. July 24, 2007) (arbitrator was "conscious of the law and deliberately ignored it;" mere misinterpretation, misstatement or misapplication is insufficient).

DC Circuit: *Lessin v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 481 F.3d 813 (DC Cir. 2007) (stating the two elements of the doctrine).

modify arbitration awards. The Court noted that section 9 of the FAA, 9 U.S.C. § 9, states that a court "must" confirm an arbitration award "unless" it is vacated, modified, or corrected "as prescribed" in sections 10 and 11.[3] The grounds for vacating an arbitration award are set out in 9 U.S.C. § 10,[4] while the grounds for modifying an arbitration award are set out in 9 U.S.C. § 11.[5]

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[3] Hall Street Associates at 5.

[4] Title 9. Arbitration,

Chapter 1. General Provisions

§ 10. Same; vacation; grounds; rehearing

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration--

(1) where the award was procured by corruption, fraud, or undue means;

(2) where there was evident partiality or corruption in the 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 that a mutual, final, and definite award upon the subject matter submitted was not made.

(b) If an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators.

(c) The United States district court for the district wherein an award was made that was issued pursuant to section 580 of title 5 may make an order vacating the award upon the application of a person, other than a party to the arbitration, who is adversely affected or aggrieved by the award, if the use of arbitration or the award is clearly inconsistent with the factors set forth in section 572 of title 5.

[5] Title 9. Arbitration

Chapter 1. General Provisions

§ 11. Same; modification or correction; grounds; order

In either of the following cases the United States court in and for the district wherein the award was made may make an order modifying or correcting the award upon the application of any party to the arbitration--

(a) Where there was an evident material miscalculation of figures or an evident material mistake in the description of any person, thing, or property referred to in the award.

(b) Where the arbitrators have awarded upon a matter not submitted to them, unless it is a matter not affecting the merits of the decision upon the matter submitted.

(c) Where the award is imperfect in matter of form not affecting the merits of the controversy.
The order may modify and correct the award, so as to effect the intent thereof and promote justice between the parties.

The Court noted that some Circuits have read *Wilko* as recognizing "manifest disregard of the law" as a further ground for vacatur of an arbitration award in addition to those listed in § 10, created by judicial decree. *Hall Street Associates* at 7. See, *e.g., McCarthy v. Citigroup Global Markets, Inc.*, 463 F.3d 87, 91 (C.A.1 2006); *Hoeft v. MVL Group, Inc.*, 343 F.3d 57, 64 (C.A.2 2003); *Prestige Ford v. Ford Dealer Computer Servs., Inc.*, 324 F.3d 391, 395-396 (C.A.5 2003); *Scott v. Prudential Securities, Inc.*, 141 F.3d 1007, 1017 (C.A.11 1998). The Court rejected the suggestion that if courts could expand the judicial review provisions of the FAA, parties could also expand judicial review of arbitration awards by contractual agreement.

> But this is too much for *Wilko* to bear. Quite apart from its leap from a supposed judicial expansion by interpretation to a private expansion by contract, Hall Street overlooks the fact that the statement it relies on expressly rejects just what Hall Street asks for here, general review for an arbitrator's legal errors. Then there is the vagueness of *Wilko*'s phrasing. Maybe the term "manifest disregard" was meant to name a new ground for review, but maybe it merely referred to the § 10 grounds collectively, rather than adding to them. See, *e.g., Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 656, 105 S.Ct. 3346, 87 L.Ed.2d 444 (1985) (STEVENS, J., dissenting) ("Arbitration awards are only reviewable for manifest disregard of the law, 9 U.S.C. §§ 10, 207"); *I/S Stavborg v. National Metal Converters, Inc.*, 500 F.2d 424, 431 (C.A.2 1974). Or, as some courts have thought, "manifest disregard" may have been shorthand for § 10(a)(3) or § 10(a)(4), the subsections authorizing vacatur when the arbitrators were "guilty of misconduct" or "exceeded their powers." See, *e.g., Kyocera, supra*, at 997. We, when speaking as a Court, have merely taken the *Wilko* language as we found it, without embellishment, see *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 942, 115 S.Ct. 1920, 131 L.Ed.2d 985 (1995), and now that its meaning is implicated, we see no reason to accord it the significance that Hall Street urges.

Hall Street Associates at 8.

Some of the recent Circuit Court opinions have expressly characterized the manifest disregard of law doctrine as being a judicially created basis for vacating arbitration awards, in addition to the grounds articulated in the FAA. In *Hudson*, the Eighth Circuit characterized the doctrine as one of the "grounds for vacating an arbitration award that [is] not expressed in the Federal Arbitration Act itself …." 484 F.3d at 504. In *Hicks*, the Tenth Circuit included the doctrine in a list of "a handful of judicially created reasons that a district [court] may rely upon to vacate an arbitration award …." 218 Fed.Appx. at 745; 2007 WL at *4. In *Aldred*, the Eleventh Circuit referred to the doctrine as one of three "non-statutory grounds … for vacating an award …." 247 Fed.Appx. at 169; 2007 WL at *2.

The Court's statement in *Hall Street Associates* that the grounds for vacating an arbitration award stated in the FAA are the "exclusive" grounds for vacating an award appears unambiguous, and would seem to exclude all judicially created, as well as all contractually created, grounds for vacating an arbitration award. If this is literally true, the manifest disregard of law doctrine, as described in *Hudson*, *Hicks* and *Aldred*, may no longer be viable.

The extended quotation from *Hall Street Associates* above, however, seems to indicate that the manifest disregard doctrine may survive under a slightly different characterization. Indeed, the opinion goes to some lengths to distinguish the judicially created manifest disregard of law doctrine from the contractual attempt to expand the basis for vacatur of arbitration awards. Although it was not presented with the issue of the viability of the manifest disregard of law doctrine, the Court stated several possible justifications for the manifest disregard of law doctrine, including one that ties the doctrine back to the FAA, suggesting that the doctrine may be an example, or a specification, of arbitrators exceeding their authority, which is stated in §10(a)(4) to be a basis for vacating an award. The Supreme Court put it this way:

> "manifest disregard" may have been shorthand for § 10(a)(3) or § 10(a)(4), the subsections authorizing vacatur when the arbitrators were "guilty of misconduct" or "exceeded their powers." See, *e.g., Kyocera, supra,* at 997.

Hall Street Associates at 8. The citation of *Kyrocera* is particularly interesting, because in *Kyrocera Corp. v. Prudential-Bache Trade Servs., Inc.*, 341 F.3d 987 (9th Cir. 2003) the Ninth Circuit held that parties may not contract for expanded judicial review of arbitration awards. Although this was a minority view of circuits which had addressed the issue at that time, the Supreme Court later came to the same conclusion in *Hall Street Associates*. In *Kyrocera*, the Ninth Circuit may have had the right position both on the appropriateness of parties contractually expanding the bases for vacating arbitration awards and on the proper justification for the manifest disregard of law doctrine.

In this light, the manifest disregard of law doctrine, with its narrow focus and rare application, remains a useful tool to ensure that arbitrators do not act in a manner that is clearly and fundamentally contrary to what our legislatures and courts have determined are clear requirements for the ordering of our affairs, which should be beyond the powers of any arbitrator.

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