



CONSTRUCTION LAW ALERT

December 2007

www.bergersingerman.com

Contractual Expansion of Judicial Review of Arbitration Awards

by Jeffrey S. Wertman, Esq.

Arbitration has become a standard part of commercial contracts, particularly in construction contracts. Arbitration is a method of dispute resolution in which a neutral third party, an arbitrator, makes a legally binding decision which can be enforced in the same manner as a judgment obtained in a court of law. If one of the parties is dissatisfied with the arbitrator's decision, he may file an action in court to vacate the award.

Arbitration awards are difficult to overturn in court because the various arbitration statutes list only narrow grounds for appeal. For example, Section 10 of the Federal Arbitration Act ("FAA") states several grounds for vacating an arbitration award: (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; and (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.

The Issue- Whether Parties Can Expand Judicial Review of Arbitration Awards?

Given the limited standard of judicial review of arbitration awards, are the parties free to provide for a broader scope of court review by so stipulating in the arbitration contract itself?

Federal Courts Split on Issue

The federal courts of appeal are split on this issue. The Ninth and Tenth Circuit Courts of Appeal have held that the

FAA provides the exclusive standard by which a federal court can review arbitration awards, and, therefore, the parties cannot expand contractually the scope of judicial review. The First, Third, Fourth, Fifth and Sixth Circuits have held the standard of review in the FAA provides a default rule only, and the parties can modify that standard of review by agreement, and the First Circuit has indicated in *dicta* it would allowed parties to contact for expanded judicial review of awards.

The policy dimensions of this debate set those in favor of deferring to Congress's power to determine the scope of lower federal court subject matter jurisdiction, i.e., the FAA specifies the grounds for vacating an award, and the courts cannot go beyond the statute, versus those in favor of parties have freedom to decide, via contract, the procedural aspects of their arbitration.

Supreme Court to Decide Issue *Hall Street Associates v. Mattel*

The United States Supreme Court in *Hall Street Associates v. Mattel*, (No. 06-989), will hopefully resolve the split of authority among the federal courts of appeal and decide whether the parties by contract can alter the standard of judicial review under the FAA.

In *Hall Street Associates v. Mattel*, Hall Street Associates leased property to toy manufacturer Mattel and filed suit after Mattel failed to clean up contaminates from its on-site factory. The parties initially agreed to arbitrate the dispute, subject to judicial review of findings of fact and conclusions of law. The arbitration agreement between the parties in this case stated that a district court reviewing an arbitration award should vacate, modify, or correct the award “where the arbitrator’s conclusions of law are erroneous” – a more expansive scope of review than provided by the FAA.

The arbitrator ruled that

Mattel need not indemnify Hall Street. The arbitrator found that Mattel had not violated “any applicable environmental laws,” an exception to the indemnity requirement under the property lease. Hall Street moved to vacate the proceeding in district court. The court granted the motion and remanded the case to the arbitrator, deeming erroneous the arbitrator’s conclusions that the Oregon Drinking Water Quality Act was not an applicable environmental law and that the exception to indemnification applied. On remand, the arbitrator ruled in Hall Street’s favor, and the district court upheld the award.

Mattel appealed to the Ninth Circuit Court of Appeal, which reversed the district court’s decision vacating the initial arbitration award. The Ninth Circuit reasoned that the provision in the arbitration agreement providing for de novo (expanded) judicial review of the arbitrator’s decision was unenforceable. The trial court again vacated the initial arbitration decision, ruling that the arbitrator exceeded his power within the FAA with an

“implausible interpretation of the contract.” The Ninth Circuit reversed this decision, holding that “implausibility is not a valid ground for voiding an arbitration award” under the FAA.

On November 7, 2007, the United States Supreme Court heard oral arguments in the case. The Supreme Court is expected to render a decision in this case by June 2008.

Conclusion

Business have become increasingly unhappy with arbitration, which is turning out to be as expensive as litigating disputes in court. If the Supreme Court in *Hall Street Associates v. Mattel* decides that parties have the authority to expand the scope of judicial review of arbitration awards, it will make arbitration more attractive. However, if the Court decides that parties cannot expand the court’s limited review of arbitration awards, more and more businesses, including those in the construction industry, may eliminate arbitration provision in their contracts.

The information in this Construction Law Alert is of a general nature only and is not intended to be relied upon as, nor a substitute for, specific professional advice. No responsibility for the loss occasioned to any purpose acting on or refraining from action as a result of any material in this publication can be accepted.

The hiring of a lawyer is an important decision that should not be based solely on advertisements. Before you decide, ask us to send you free written information about our qualifications and experience.



Jeffrey S. Wertman

jwertman@bergersingerman.com
(954) 627-9912

Jeffrey S. Wertman is a member of Berger Singerman’s Dispute Resolution Team. Jeff focuses his practice in the areas of construction law, construction litigation, construction ADR, and general civil, corporate, commercial and complex litigation in state, federal and appellate courts.