

# Judicial Review in Arbitration

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ntil last year it was virtually impossible to obtain judicial review of an arbitrator's decision. The governing statute largely restricts any reversal to extreme cases, such as when the arbitrator is guilty of fraud, corruption, or other misconduct. (See Cal. Code Civ. Proc., § 1282.6 (a).) And prior appellate decisions held that a court could not intervene even when the arbitrator made an error of law that prejudiced a party. (See *Moncharsh v. Heily & Blase*, 3 Cal. 4th 1 (1992).)

However, the ground shifted in August with *Cable Connection, Inc. v. DIRECTV, Inc.* (44 Cal. 4th 1334 (2008)), which opened the door to expanded judicial review in arbitration. To appreciate this change, it is important to review *Moncharsh* as well as the pros and cons of arbitration itself. Armed with that background, counsel can determine how best to customize an arbitration clause so parties can enjoy both the efficiency of arbitration and the opportunity for meaningful judicial review.

## THE MONCHARSH RULE

In *Moncharsh*, the California Supreme Court

observed the general rule that an arbitrator's decision cannot be reviewed for errors of fact or law. The risk of mistake is acceptable, said the court, because "by voluntarily submitting to arbitration, the parties have agreed to bear that risk in return for a quick, inexpensive, and conclusive resolution to their dispute." In words that reverberated throughout the state, the court declared that "[t]he arbitrator's decision should be the end, not the beginning, of the dispute." (3 Cal. 4th at 10, 12.)

In declining to allow review for legal error, the *Moncharsh* court explained that "the Legislature has set forth grounds for vacation ... and correction ... of an arbitration award and '[a]n error of law is not one of the grounds.'" (*Moncharsh*, 3 Cal. 4th at 14; Cal. Code Civ. Proc. § 1286.2(a), 1286.6.)

## THE CABLE CONNECTION CLAUSE

The arbitration clause at issue in *Cable Connection*, however, stated that "[t]he arbitrators shall not have the power to commit errors of law or legal reasoning, and the award

may be vacated or corrected on appeal to a court of competent jurisdiction for any such error." (*Cable Connection*, 44 Cal. 4th at 1340.) In upholding this provision, the court relied on both the principle of freedom to contract (the right of the parties to establish their own arbitration procedure) and on section 1286.2(a)(4) of the Code of Civil Procedure, which allows an arbitration award to be vacated if the arbitrators "exceeded their powers."

However, the language of the contract in that case was crucial. The opinion in *Cable Connection* noted two provisions of the controlling clause: (1) it limited the arbitrator's power, and (2) it expressly allowed for judicial review. The court then observed that "[w]e do not decide here whether one or the other of these clauses alone, or some different formulation, would be sufficient to confer an expanded scope of review." (44 Cal. 4th at 1361.)

The court underscored the need for specificity in the governing contract. "[W]e emphasize that parties seeking to allow judicial review ... and to avoid an additional dispute over the scope of review, would be well advised to provide for that review explicitly and unambiguously." (44 Cal. 4th at 1361.)

Although the *Cable Connection* ruling blazes a new trail for arbitration in California, it also leaves open several questions. For example, can the parties contract for judicial review of mixed questions of law and fact? Can parties agree to judicial review for the purpose of ascertaining whether the award is based on substantial evidence? The answers are not altogether clear.

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The court majority in *Cable Connection* relied on language from *Moncharsh* that “in the absence of some limiting clause in the arbitration agreement, the merits of the award, either on questions of fact or law, may not be reviewed except as provided in the statute.” (44 Cal. 4th at 1357.) This reasoning produced the core message of *Cable Connection*: “The California rule is that the parties may obtain judicial review of the merits by express agreement.” (44 Cal. 4th at 1340.) Arguably, parties can contract for review of any error.

But Justice Carlos R. Moreno’s concurring and dissenting opinion (in which Chief Justice Ronald M. George concurred) left the question open. “Nor is it clear,” he wrote, “that this refashioning will stop at reviewing for legal error—will parties be able to bind courts to review mixed questions of law and fact, or whether the arbitration award is based on substantial evidence?” (44 Cal. 4th at 1375.)

## STATE VS. FEDERAL COURT

The *Cable Connection* ruling applies in California courts. The Federal Arbitration Act (FAA) (9 U.S.C. §§ 1–307), which covers cases filed in federal court, does not permit the parties to expand the scope of review by agreement (*Hall Associates, L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1396, 1402–06 (2008)). Although the FAA generally applies to contracts that affect interstate commerce (*Southland Corp. v. Keating*, 465 U.S. 1, 10–11 (1984); 9 U.S.C. § 2), the state Supreme Court ruled in *Cable Connection*, consistent with *Hall Street*, that the FAA does not prevent a California court from allowing judicial review under the state’s arbitration law (44 Cal. 4th at 1348–54). Even though the federal standards are different and do not apply in a California courtroom, counsel should keep in mind that even in federal cases an arbitrator’s award may be reviewed for “manifest disregard of law.” (See *Comedy Club, Inc. v. Improv West Associates*, 553 F.3d 1277, 2009 WL 205046 (9th Cir. 2009).)

Judicial review may not be desirable in every case. To make an informed

decision about whether to have a judge review an arbitrator’s decision, it is helpful to analyze the advantages and disadvantages of arbitration itself.

## ADVANTAGES OF ARBITRATION

**More-predictable awards.** Jury verdicts tend to be erratic and generally larger than arbitration awards—or at least that is the standard assumption. But because arbitration awards are private, it is impossible to conduct a detailed comparison.

**Speed.** This factor may be less compelling since the advent of “fast track” court procedures. Nevertheless, arbitration does tend to be faster and more efficient than traditional court litigation.

**Cost savings.** Though generally true, this point has limits. In arbitration, counsel can reduce or eliminate discovery expenses, but that savings must be weighed against the accompanying inability to quickly dispose of a case by demurrer or summary judgment and the risk of a surprise at the hearing. Moreover, counsel should keep in mind that parties, when faced with the expense of litigation and trial in the courts, tend to become more realistic regarding settlement than they would be at arbitration.

**Choice of a decision maker.** In court, the litigants sometimes draw a judge who has little or no experience with the subject matter of the case. An arbitration agreement can mandate selection of an arbitrator who has extensive experience in the particular area involved.

**Confidentiality.** For those favoring arbitration, a major factor is the ability to keep the proceedings private. But counsel should not be too smug in thinking that an arbitrated case will remain behind the curtain forever. If a party asks the court to confirm, correct, or vacate the award, the arbitrator’s decision must be filed with the court and, of necessity, is exposed to public view. (Section 1285.4(c) of the Code of Civil Procedure requires that an arbitrator’s award be attached to any court petition to confirm, correct, or vacate.)

## DISADVANTAGES OF ARBITRATION

**No appeal.** Binding arbitration elimi-

nates the right to appeal on the merits. Until *Cable Connection*, this was perhaps the single most important disadvantage of arbitration. The loss of appellate rights is particularly important if the arbitrator is both free to ignore the law and empowered to decide the case based on his or her perception of fairness. The California Supreme Court has held that arbitrators, unless specifically restricted by the agreement to abide by legal rules, “may base their decision upon broad principles of justice and equity. ... [A]rbitrators are not bound to award on principles of dry law, but may decide on principles of equity and good conscience.” (*Advanced Micro Devices, Inc., v. Intel Corporation* (9 Cal. 4th 363, 374–5, 387 (1994)).)

**Inadequate record.** Many an arbitration goes unreported. Without a stenographic record and a meaningful appellate transcript, a case may not be susceptible to judicial review, even in a case where review is available.

**Informal rules of evidence.** Unless the parties agree otherwise, the rules of evidence do not apply to an arbitration (for example, “hearsay” evidence is permitted). Thus, a party might lose a case in arbitration that would have been won in court.

**Limited discovery.** In many arbitrations discovery is limited. For this reason, a lawyer in arbitration may not have the same tools that are available in a court proceeding to properly evaluate the case for settlement and trial.

**No guarantee of experts.** Arbitrators are not required to allow expert testimony. Their job is to use their own special skill and knowledge, notwithstanding the absence of direct evidence from experts. Therefore, including a clause that affirms the use of experts is particularly important, especially if the dispute is one that will turn on expert testimony, such as a malpractice case.

**No malicious prosecution.** If the defendant prevails in arbitration, counsel cannot file a suit for malicious prosecution. (See *Brennan v. Tremco*, 25 Cal. 4th 310 (2001).)

## CUSTOMIZING THE AGREEMENT

If you decide to proceed with ADR rather than litigate in court, the best way to handle these concerns is to customize the arbitration agreement. Although adding lots of bells and whistles to a standard arbitration agreement may appear cumbersome, a creative lawyer can tailor the process to meet a client's needs.

Every case is unique, and the drafting attorney must determine which provisions to include and which to eliminate. Keep in mind that the *Cable Connection* decision does not establish that every innovative contractual provision will receive a judicial blessing. Accordingly, be sure to include a "severance" clause.

Here's some sample contract language to consider:

- **Governing Law.** This arbitration shall be governed by the California Arbitration Act, sections 1280 through 1294.2 of the Code of Civil Procedure (the "Act"). If a conflict exists between the provisions of the Act and this Agreement, the language of this Agreement shall control.

- **ADR Service Provider.** The arbitration shall be administered by [name of arbitration service provider].

- **Selection of Arbitrator.** The arbitrator shall be an attorney or retired judge having at least [number] years prosecuting, defending, arbitrating, mediating, and/or judging disputes regarding [area(s) of law].

- **Demand for Arbitration.** Any party to this agreement may serve a Demand for Arbitration ("Demand") setting forth the allegations against another party, and the party served shall serve a Response to Demand for Arbitration ("Response") setting forth a response to such allegations, including affirmative defenses, if any. Any party may serve a Cross-Demand for Arbitration. These pleadings shall be, in all respects, as required under California law for a Complaint, an Answer, and a Cross-Complaint, respectively.

- **Court Reporter.** A certified court reporter shall report the proceedings at all hearings and, at the request of

a party, prepare a certified Reporter's Transcript. The arbitrator shall maintain all documents normally provided to a court in a Clerk's Transcript and, upon request, shall prepare an Arbitrator's Transcript containing all documents that would normally be in a Clerk's Transcript. All reviewing courts shall treat the Arbitrator's Transcript as if it were a Clerk's Transcript.

- **Demurrers and Motions for Summary Judgment.** The parties shall be permitted to file, and the arbitrator shall hear and rule upon, demurrers and motions for summary judgment.

- **Evidence and Expert Testimony.** The California Evidence Code shall govern the arbitration. Expert testimony shall be permitted according to the same standard as allowed in a court of law.

- **Discovery.** The parties may conduct any discovery permitted under the California Discovery Act. The arbitrator shall adjudicate any disputes with regard to discovery.

- **Limit on Arbitrator's Power and Right to Judicial Review.** The arbitrator shall not have the power to commit (a) errors of law or legal reasoning, (b) errors of fact, (c) errors with regard to mixed questions of law and fact. In addition, the arbitrator shall not have the power to render an award (d) not based on substantial evidence, (e) based on evidence not presented at the hearing, or (f) not in conformity with the substantive and procedural law of the state of California. If the arbitrator exceeds any of the foregoing specific powers, the award may be vacated or corrected by filing a petition pursuant to the Act in the Superior Court in and for the county of [name]. In reviewing the award, the Superior Court shall sit as if it were an appellate court, in all respects, including but not limited to the scope of review. The decision of the Superior Court is, itself, subject to review by the California appellate courts.

- **Reasoned Award.** The arbitrator shall hear and determine the matter,

and shall execute and acknowledge the award in writing and cause a copy thereof to be delivered to each of the parties. The award shall include factual findings, conclusions of law, and the reasons on which the decision is based. The decision of the arbitrator shall be final, binding, and conclusive, except to the extent the decision may be submitted for judicial review as provided herein. The award of the arbitrator may be confirmed by the Superior Court in [name] County, and such Court may vacate, modify, or correct the award in accordance with the prevailing sections of the Act and in accordance with the terms and conditions herein.

- **Malicious Prosecution.** A favorable termination in this arbitration shall be deemed to be a favorable termination for purposes of a malicious prosecution action. Any such malicious prosecution action shall be submitted to arbitration under the terms of this agreement.

*If you decide to proceed with ADR, it's best to customize the arbitration agreement.*

- **Severance Clause.** In the event that any provision (or any portion thereof) of this agreement to arbitrate is held to be void, voidable, or unenforceable, the remaining portions shall remain in full force and effect.

When it comes to ADR, one size does not fit all. Consider these sample clauses as a menu to choose from rather than the elements of a meal to be consumed in one sitting.

Although judicial review may not be appropriate in every case you agree to arbitrate, the *Cable Connection* decision at least makes it an option to weigh. ☛

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## Judicial Review in Arbitration

- 1 Prior to *Cable Connection, Inc. v. DITECTV, Inc.*, it was difficult to obtain judicial review of an arbitrator's award.  
 True  False
- 2 Under *Cable Connection*, a court can always review mixed questions of law and fact in an arbitrator's award.  
 True  False
- 3 The parties should have a court reporter at all hearings to ensure later meaningful judicial review of an arbitration award.  
 True  False
- 4 One advantage of arbitration is that the decision will always remain private.  
 True  False
- 5 It is wise to include a severance clause in every arbitration agreement.  
 True  False
- 6 Formal rules of evidence apply to all arbitrations.  
 True  False
- 7 Attorneys should draft arbitration provisions to fit the needs of their particular clients.  
 True  False
- 8 A defendant who prevails in arbitration may always bring a court action for malicious prosecution.  
 True  False
- 9 In California, parties may obtain judicial review of an arbitration award by express agreement.  
 True  False
- 10 For parties to obtain judicial review, the arbitration agreement must clearly provide for it.  
 True  False
- 11 One advantage of arbitration is the ability to select a decision maker who has expertise in the subject matter.  
 True  False
- 12 Arbitrators are not required to allow expert testimony.  
 True  False
- 13 To ensure meaningful judicial review, the arbitrator should be required to prepare a record analogous to a clerk's transcript in a court trial.  
 True  False
- 14 Providing for judicial review of an arbitration award is always desirable.  
 True  False
- 15 Unless an agreement provides otherwise, arbitrators may ignore the law and base their decisions on principles of equity and fairness.  
 True  False
- 16 The law automatically allows an arbitrator to decide demurrers and motions for summary judgment.  
 True  False
- 17 Parties to arbitration are always entitled to conduct any discovery permitted under the California Discovery Act.  
 True  False
- 18 Prior to *Cable Connection*, a court could not provide relief when an arbitrator made an error of law that prejudiced a party.  
 True  False
- 19 If a case in state court affects interstate commerce, the Federal Arbitration Act prevents judicial review of any arbitration award.  
 True  False
- 20 If the parties clearly agree in writing, cases governed by the Federal Arbitration Act may be subject to judicial review.  
 True  False

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