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60-Second Memo

April 16, 2008

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Judicial Review of Arbitration Awards: What's the Scope?

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Employers who use employment agreements or who find themselves dealing with disgruntled employees often look to arbitration as a cost-effective and expeditious means of resolving disputes. Arbitration can be particularly attractive in employment cases where the matters often involve smaller sums of money. However, a United States Supreme Court decision issued last month may cause employers to reconsider the circumstances under which they choose to arbitrate.

In *Hall Street Associates, L.L.C. v. Mattel, Inc.*, decided on March 25, 2008, the United States Supreme Court held that parties who avail themselves of arbitration under the Federal Arbitration Act (FAA) cannot, by private agreement, expand the grounds for judicial review of an arbitrator's award. Thus, parties arbitrating under the FAA may only vacate an arbitration award in the event of fraud, corruption, misconduct or where arbitrators exceed the scope of their authority and rules on an issue not

submitted to them.

Hall Street v. Mattel began as a lease dispute between a landlord, Hall Street, and its tenant, Mattel. Mattel had used the property for many years as a manufacturing site. The lease provided that Mattel would indemnify Hall Street for any costs resulting from Mattel's and its predecessors' failure to abide by environmental laws in its use of the leased premises.

In 1998, tests of the property's well water showed high levels of a hazardous chemical compound. The Oregon Department of Environmental Quality (DEQ) discovered even more pollutants, and Mattel, along with one of its predecessors, signed a consent order providing for cleanup of the area.

Thereafter, Mattel gave notice that it intended to terminate the lease. Hall Street filed a lawsuit, contesting Mattel's right to vacate the lease and claiming that the lease obliged Mattel to indemnify Hall Street for costs spent in the clean-up.

At the district court level, Mattel won on the lease termination issue. After the parties unsuccessfully tried to mediate the indemnification issue, they agreed to arbitrate that claim pursuant to the FAA. The parties drew up an arbitration agreement, which the district court approved and entered as an order. The arbitration agreement provided that the district court could enter judgment upon any arbitration award by confirming, modifying or correcting the award. The parties also agreed that the court would vacate, modify or correct any award in which "the arbitrator's findings of facts are not supported by substantial evidence" or "where the arbitrator's conclusions of law are erroneous."

The arbitrator decided in Mattel's favor. In particular, the arbitrator held that Mattel need not indemnify Hall Street because the Oregon Drinking Water Quality Act ("Oregon Act") was not an environmental law, with which Mattel was obligated to comply under the lease, but rather one dealing with human health. Hall Street filed a motion with the district court vacating the arbitration award on the grounds that the arbitrator committed legal error in failing to find that the Oregon Act was an applicable environmental law under the lease. The district court agreed and vacated the award, invoking the

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standard of review chosen by the parties in the arbitration agreement.

After Mattel won a reversal on appeal to the Ninth Circuit, Hall Street sought review by the United States Supreme Court. The issue was whether the parties could, by agreement, expand the scope of judicial review of an arbitration award.

The federal circuits had been split as to whether the parties themselves could agree to greater oversight by the courts under the FAA. Some circuits had held that the provision of the FAA were the exclusive grounds under which an award may be vacated, whereas other circuits had held that they were mere threshold provisions, open to expansion by agreement by the parties.

The Supreme Court held that the FAA sets forth the exclusive grounds for modification or vacation of an arbitration award. Therefore, parties arbitrating under the FAA may not supplement by contract additional grounds under which a court may vacate an arbitration award, even for legal error.

The Supreme Court took a very literal interpretation of §9, which provides that a court "must" confirm an award "unless" it is vacated, modified, or corrected "as prescribed" in §§ 10 and 11. The Supreme Court found that an arbitrator's commission of a legal error is not an enumerated ground for vacation of an arbitration award. The Court further held that, even if it assumed that §§ 10 and 11 could be supplemented, it would "stretch basic interpretive principles to expand the stated grounds to the point of evidentiary and legal review generally." Sections 10 and 11 address what the Supreme Court termed as "egregious departures" from the parties' agreed-upon arbitration: corruption, fraud, evident partiality, misconduct, misbehavior, exceeding the scope of powers, evident material miscalculation, evident material mistake, awards upon a matter not submitted. The Court drew on the legal principle of *ejusdem generis*, whereby, when a statute sets out a series of specific items ending with a general term, that general term is confined to covering subjects comparable to the specifics it follows. As it went on to note, "'fraud' and a mistake of law are not cut from the same cloth."

The Supreme Court noted that its decision was limited to the question of the scope of judicial review available under the FAA. It made certain to point out that parties wanting broader review of awards could contemplate enforcement under state statutory or common law.

Employers who use arbitration agreements should review those agreements in light of this new decision. Arbitration agreements that provide for judicial review on different grounds than those provided by the FAA may prove problematic to employers seeking to vacate unfavorable arbitration awards.

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