Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
October 2013 Issue

Herb Fox

The Reversible Arbitration Award: A hybrid already here

The rules of judicial review have changed in California – and not a moment too soon!

One of the hallmarks of contractual binding arbitration has long been the absence of full judicial review. Arbitrators could apply incorrect law, foreign law, or no law at all in adjudicating disputes, and there was no remedy for errors of law or legal reasoning. Judicial review was limited to the narrow statutory factors set forth in Code of Civil Procedure sections 1986.2 and 1986.6 (see sidebar article on Next Page).

As the state Supreme Court pronounced in 1992, arbitrators were free to render an award "reached by paths neither marked nor traceable and not subject to judicial review" (*Moncharsh v. Heily & Blaze* (1992) 3 Cal.4th 1 ("*Moncharsh*"). This limitation was justified on the questionable hypothesis that parties to an arbitration agreement voluntarily traded their right to an adjudication based on accepted legal principles, for the speed, privacy and efficiency of arbitration.

For many, however, the limited judicial oversight of arbitration awards was the Achilles' heel of the entire mechanism. Without the predictability and fairness offered by applying procedural and substantive law, arbitration was little more than a game of roulette where the numbers were stripped from the table and the croupier could stop the wheel at will.

But in California, the rules of the game have now changed.

Sixteen years after *Moncharsh*, the Supreme Court corrected course and has carved out an exception to the limited scope of review that is potentially large enough to swallow the entire concept of "binding" arbitration.

In 2008, our Supreme Court held that parties to an arbitration agreement can stipulate to allow full judicial review of the merits of the award (*Cable Connection Inc. v. DirectTV Inc.* (2008) 44 Cal.4th 1334). The Supreme Court held that if the parties so agreed, arbitration awards governed by the California Arbitration Act can now be reviewed, and reversed, for legal errors or erroneous reasoning. We have now entered the hybrid world of the reversible arbitration award.

And this sea change in California law could not have come at a more opportune time. Not long after *Cable Connection*, our court system tumbled into the abyss of layoffs, court closures and consolidations, turning an already overwhelmed civil justice system into one marked by chaos and inexorable delays.

The availability of a reversible arbitration award is one path out of these Dickensian times.

The Supreme Court explained it best:

> Enforcing contract provisions for review of awards on the merits relieves pressure on congested trial court dockets. [Citations Omitted] Courts are spared not only the burden of conducting a trial, but also the complications of discovery disputes and other pretrial proceedings. Incorporating traditional judicial review by express agreement preserves the utility of arbitration as a way to obtain expert factual determinations without delay, while allowing the parties to protect themselves from perhaps the weakest aspect of the arbitral process, its handling of disputed rules of law.

(*Id.*at 1364.)

While the exercise of the right to judicial review will delay the finality of an arbitration award, that review will take place on the Superior Court's law and motion calendar, thereby shaving years off the time it would have taken to get to trial and through post-trial proceedings. Even adding the time required for appellate court review, a reviewable arbitration proceeding can move from the initial arbitration demand to a fully reviewed final judgment in three years or less – much less than the four to six years now required for a full trial and appellate review in the state courts.

Parties who agree to arbitrate but who stipulate to full judicial review under *Cable Connection*, can enjoy the best of two worlds: the relative speed, efficiency and convenience of arbitration, combined with a judicial safety net that helps assure that the award is consistent with California law and is supported by substantial evidence.

Indeed, a clause providing for full judicial review of arbitration awards is likely to become a standard-of-care issue in drafting agreements or stipulating to arbitration. Now that such review is an option, attorneys who do not recommend such terms to their clients may be hard pressed to explain later, after an arbitration loss based on legal error, that the client waived the right to seek judicial review.

Practitioners should note one major caveat to this option. The right to stipulate to full judicial review of arbitration awards, as now recognized in *Cable Connection*, applies *only* to arbitration agreements governed by the California Arbitration Act ("CAA"). [Code Civ. Proc., § 1280 et. seq.] In arbitrations governed by the Federal Arbitration Act ("FAA). [9 USC §1 et seq.], parties may *not* stipulate to expanded judicial review, a limitation imposed by the U.S. Supreme Court in

See Fox, Next Page

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
October 2013 Issue

The myth of the "non-appealable" arbitration award

In fact, opportunities abound for setting aside standard "binding" arbitration awards

How many times have you been told that a binding arbitration award is "not appealable"?

If it's been once, it's been too many times, because it's a myth. Arbitration awards can be challenged in the trial courts and Courts of Appeal, and often enough those challenges are successful – even where the parties did not stipulate to full judicial review pursuant to *Cable Connection v. DirectTV.*

The statutory grounds for vacating or correcting arbitration awards are set forth in sections 1286.2 and 1286.4 of the Code of Civil Procedure. (For analogous standards under the Federal Arbitration Act, see 9 USC §§10, 11.) While often described as "narrow," these statutory grounds are broader than many practitioners realize. The fact is that opportunities abound for setting aside standard "binding" arbitration awards, as seen by the sample of recent state court cases cited below.

- **Failure to admit material evidence**: An arbitrator's exclusion of evidence was held reversible error in *Burlage v. Superior Court* (2009) 178 Cal.App.4th 524. Section 1286.2(5) of the Code of Civil Procedure provides that a court "shall" vacate an award when a party's rights "were substantially prejudiced ... by the refusal of the arbitrator [ ] to hear evidence material to the controversy...."
- **Merits review where arbitrator violates non-waivable statutory claims**: In *Pearson Dental Supplies v. Superior Court* (2010) 48 Cal.4th 665, the Supreme Court reversed an arbitrator's award that found an employee's FEHA claim was time-barred. The Court held that in the context of contractual arbitration of non-waivable statutory claims, courts may review the legal merits of arbitrator's rulings that bar those claims.
- **Vacature of award after trial court improperly removed first arbitrator**: In *Bosworth v. Whitmore* (2006) 135 Cal.App.4th 536, an arbitration award was vacated where the trial court had improperly removed the first arbitrator and appointed a successor.
- **Violation of public policy as exceeding authority:** In *California Department of Human Resources v. Service Employees Int'l Union, Local 1000* (2012) 209 Cal.App.4th 1420, an arbitration award was partially vacated where the arbitrator exceeded his powers by awarding public employees a pay increase where matter was subject to legislative approval.
- **Restricting party's right to representation:** An arbitration award was vacated where the arbitrator excluded from the proceeding a corporate party's attorney and representative (*Hoso Foods, Inc. v. Columbus Club, Inc.* (2010) 190 Cal.App.4th 881*)*.
- **Improper ex parte communications between arbitrators**: In *Maaso v. Signer* (2012) 203 Cal.App.4th 362, the Court of Appeal affirmed an order vacating a medical malpractice arbitration award that was procured by "undue means," where there was ex parte contact between the doctor's party arbitrator and the neutral arbitrator while the award was pending.
- **Failure to disclose conflict:** In *Gray v. Chiu* (2013) 212 Cal.App.4th 1355, a Court of Appeal vacated a medical malpractice arbitration award where the doctor's attorney failed to disclose to plaintiff's counsel that he belonged to the same arbitration provider firm as the arbitrator.
- **Erroneous determination that proceeding was binding**: A Mandatory Fee Dispute arbitrator's erroneous determination that award was binding resulted in vacating award (*Glaser, Weil, Fink, Jacobs & Shapiro, LLP v. Goff* (2011) 1940 Cal.App.4th 423.)
- **Improper impaneling of arbitrators:** An award rendered by a single arbitrator was vacated where parties' agreement called for a panel of three arbitrators (*Parker v. McCaw* (2005) 125 Cal.App.4th 1494).

These and other cases (published and non-published, state and 9th Circuit) demonstrate that "binding" arbitration awards are not sacrosanct. Counsel facing the losing end of a "binding arbitration" are well advised to deeply investigate the prospect of judicially vacating the award before advising the client that the decision is final and "non appealable." It just might not be the case!

— Herb Fox

Hall Street Associates, L.L.C. v. Mattel, Inc. (2008) 552 U.S. 576. Whether an arbitration agreement is governed by the CAA or the FAA can be a gnarly legal issue that itself is often the subject of appellate court determination (see, e.g., *Valencia v. Smyth* (2010) 185 Cal.App.4th 153 for a mind-numbing example of the twists and turns of the choice of law analysis).

Thus counsel who intend to stipulate to judicial review must be very careful to draft the arbitration agreement so that it is clearly governed by the CAA.

Pre-arbitration: Drafting the *Cable Connection* mantra

The premise of *Cable Connection* is that if the parties expressly stipulate, an arbitrator who commits legal error is acting in excess of his or her power. Such an excess of authority, in turn, constitutes statutory grounds to vacate or correct the arbitration award (see Code Civ.Proc., §§1986.2(a)(4) and 1986.6(b)).

Cable Connection and its progeny make clear, however, that it is not sufficient for the parties to simply agree that the arbitrator must apply California law (See, e.g., *Gravillis v. Coldwell Banker Residential Brokerage Co.* (2010) 182 Cal.App.4th 503.) The agreement should expressly state that the failure to follow California law would be an excess of authority, *and* that the issue of legal error is subject to judicial review. (*Cable Connection* at p. 1361).

The clause at issue in *Cable Connection* reads as follows, and good drafting practice dictates adopting this language verbatim:

> The 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.

During the arbitration: Creating and preserving the record

One result of a *Cable Connection* agreement for judicial review will be a higher degree of formality in the arbitration

See Fox, Next Page

Journal of Consumer Attorneys Associations for Southern California
ADVOCATE
October 2013 Issue

proceeding itself. Although the arbitration will still likely take place in a conference room with the arbitrator, parties and counsel sitting around a table, the possibility of judicial review requires the creation and preservation of an adequate record to allow for that review. In that sense, the arbitration proceeding will begin to more closely resemble a bench trial.

Here are some tips for creating and preserving that record.

First, there should be a certified court reporter in attendance so that there will be a reporter's transcript of the arbitration hearing.

Next, the parties should carefully prepare arbitration briefs and, if appropriate, closing briefs that set up the issues and the applicable law. Not only will these serve as a resource for the arbitrator, they may later serve as a roadmap for appellate counsel and the reviewing court(s).

Further, the parties should clearly stipulate *on the record* that the rules of evidence shall apply and that evidentiary objections can be made during the proceeding. This will modify the usual arbitral forum rules regarding evidence (see, e.g., AAA Commercial Arbitration Rule R-31 and JAMS Comprehensive Arbitration Rule 22(d)). Keep in mind, however, that a wrongful exclusion of relevant evidence is already one of the statutory bases for vacating an award (Code Civ. Proc., §1286.2(a)(5); see sidebar article).

Further, the parties should require that the arbitrator prepare a "reasoned decision," akin to a Statement of Decision, setting forth the arbitrator's findings of fact and conclusions of law. For obvious reasons, a one sentence award ("The arbitrator finds in favor of the claimant") will be of little use to a reviewing court later. If the parties are submitting to the rules of an established ADR provider, counsel should carefully check those rules as to timing of such a stipulation. For example, AAA rules require that a stipulation for a "reasoned award" must be made *before* the appointment of the arbitrator (see, e.g., AAA Commercial Arbitration Rule R-42(b)).

Finally, the arbitrator should be apprised of the fact of the *Cable Connection* stipulation. That the parties have agreed that the arbitrator may not make errors of law or legal reasoning will necessarily affect the arbitrator's conduct and standard of care in adjudicating the case (and perhaps thereby avoid the need for judicial review!)

Post-award proceedings

An arbitration award that is subject to full judicial review is challenged by the same statutory procedure as any other arbitration award. A Petition to Vacate or Correct the award must be filed in the Superior Court within 100 days after a signed copy is served on the parties. (Code Civ. Proc., § 1288.)

The basis for that petition would be that by committing an error of law or legal reasoning, in light of the parties' stipulation, the arbitrator has "exceeded his or her powers" and the award therefore must be vacated or corrected. (Code Civ. Proc., §§ 1286.2(4)); 1286.6(b).)

That petition should be treated much as an appeal, with a full record of the arbitration proceedings lodged as exhibits, including a reporter's transcript; a copy of the briefs and other pleadings; a full set of exhibits offered at the arbitration hearing; and, of course, a copy of the arbitrator's reasoned decision.

Moving on up, any Superior Court order vacating the arbitration award (unless remanded for a rehearing), or any judgment confirming the award as rendered or as corrected, is immediately appealable to a Court of Appeal. (Code Civ. Proc., §1294.)

Both the Superior Court and the Court of Appeal will likely apply the normal appellate standards of review to the arbitration proceeding, although the extent to which the parties might stipulate to a modified standard of review (e.g., de novo review of the weight of the evidence) was left unanswered in *Cable Connection*.

Alternatives to a *Cable Connection* agreement

Finally, counsel should not overlook alternatives to a *Cable Connection* agreement for full judicial review of arbitration awards.

One such alternative is a true "arbitration appeal." Where the parties have entered into an arbitration agreement and would like the protection afforded by judicial review but still want to maintain privacy and/or the relative speed of arbitration, they may be able to invoke a true "arbitration appeal." (See, e.g., *Cummings v. Future Nissan* (2005) 128 Cal.App.4th 321, approving a procedure where the agreement allowed review of the award by a second arbitrator, applying normal appellate procedures and standards, with the power to vacate the award.) At least one major provider, JAMS, already offers an "arbitration appeal" as an option.

Another alternative, outside of an arbitration proceeding, is for the parties to stipulate to the appointment of a "private judge" or referee to conduct a trial. (Code Civ. Proc., § 638; Rules of Court, rules 2.830 and 3.900 et seq.) The referee's decision, once reduced to a judgment by the court, is reviewable on appeal as any other final judgment. (Code Civ. Proc., § 645.)

Herb Fox is a Certified Appellate Law Specialist handling civil appeals and writs throughout California. He was appellate counsel in Harris v. Sandro *(2002) 96 Cal.App.4th 1310 and* Parker v. McCaw *(2005) 125 Cal.App.4th 1495, decisions vacating arbitration awards. He can be contacted at hfox@foxappeals.com.*