California Supreme Court Expands Judicial Review in Arbitration Cases
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Awards rendered by arbitrators are ordinarily subject to limited judicial review and may be overturned only in narrow circumstances. In particular, an award is not subject to attack in court merely because it contains errors of law. In an important decision that may encourage broader use of arbitration, however, the California Supreme Court has ruled that the parties to an arbitration proceeding may, by their agreement, subject the arbitration award to more expansive judicial review. *Cable Connection, Inc. v. DIRECTV, Inc.,* 2008 WL 3891556 (August 25, 2008).

The *Cable Connection* case was not the first occasion on which the California Supreme Court has addressed the issue of the scope of judicial review of arbitration awards. In a 1992 decision, the Court enunciated the general rule that an arbitrator’s award is not subject to review for errors of law, even if the arbitrator’s error resulted in substantial prejudice to a party. *Moncharsh v. Heily & Blase, Inc.,* 3 Cal. 4th 1 (1992). To quote the Court: “This expectation of finality strongly informs the parties’ choice of an arbitral forum over a judicial one. The arbitrator’s decision should be the end, not the beginning, of the dispute.” 3 Cal.4th at 10.

And going even further, the *Moncharsh* Court noted: “Thus, it is the general rule that, with narrow exceptions, an arbitrator’s decision cannot be reviewed for errors of fact or law. In reaffirming this general rule, we recognize there is a risk that the arbitrator will make a mistake. That risk, however, is acceptable for two reasons. First, 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.” 3 Cal. 4th at 11.

The general rule of limited review of arbitration awards is embodied in a California statute, Code of Civil Procedure § 1286.2, which provides that the only basis to vacate an award is if it was obtained through “corruption, fraud or other undue means.” Another stated basis for modification or outright vacation of an award is if the arbitrators “exceeded their powers.” An error of law, on the other hand, is not a ground for vacation or modification of the award.

In the wake of *Moncharsh,* parties have grappled with whether they can, by contract, limit an arbitrator’s power and thereby allow for more expansive judicial review of the arbitrator’s decision. For example, if the arbitration clause says the arbitrator is limited to deciding the case pursuant to California law and has no power to go beyond that, can a court – in light of the *Moncharsh* decision – review the arbitration award for legal error? The theory is that the arbitrator “exceeded his power” by not correctly applying the law.
This was the question presented in the Supreme Court’s recent *Cable Connection* case. The case arose out of a substantial dispute between DIRECTV and its dealers in four states who claimed that the company had wrongfully withheld commissions and assessed improper charges. The matter proceeded to arbitration administered by the American Arbitration Association, which appointed a panel of three arbitrators.

The parties’ agreement stated that “Any dispute or claim arising out of the interpretation, performance, or breach of this Agreement… shall be resolved only by binding arbitration, at the request of either party, in accordance with the rules of the American Arbitration Association…. The arbitrators shall apply California substantive law to the proceeding, except to the extent Federal substantive law would apply to any claim.” The arbitration clause further specified: “This Section and any arbitration conducted hereunder shall be governed by the United States Arbitration Act (9 U.S.C. Section 1, et seq.).”

After the arbitrators rendered a decision, DIRECTV petitioned the court to vacate the award, arguing that it reflected errors of law and that it therefore was beyond the scope of the arbitrators’ powers.

The trial court vacated the award, but an intermediate court of appeal reversed, ruling that a contract purporting to inject judicial review into the arbitration process is unenforceable. The appellate court held that under the governing arbitration statutes, the only basis to vacate an arbitration award is if the petitioner shows the award was obtained through “corruption, fraud or other undue means.” An error of law, said the court, could not be a ground for vacation of an arbitration award under Code of Civil Procedure § 1286.2.

The state Supreme Court reversed the court of appeal and in so doing marked a major shift in California arbitration law. The court recognized that under the Federal Arbitration Act the result would be different, as the U.S. Supreme Court has ruled in *Hall Street Associates, LLC v. Mattel, Inc.*, 128 S. Ct. 1396 (2008), that the FAA does not allow parties to alter via contract provisions the statutory standard of limited judicial review.

Under the California Arbitration Act, however, the parties are free to do so. In the *Cable Connection* case, the Court analyzed its prior *Moncharsh* ruling in great detail. It paid due deference to *Moncharsh*’s holding that the general rule is that “an arbitrator’s decision is not ordinarily reviewable for error by either the trial or appellate courts.” 3 Cal. 4th at 13. The Court also observed, however, that the scope of arbitration is a matter of agreement between the parties and that the powers of an arbitrator may be limited and circumscribed by the agreement to arbitrate or in the parties’ stipulation of the issue to be decided by the arbitrator.
In the *Cable Connection* case, the Court said that the key is the parties' agreement. If the agreement properly limits the arbitrator's authority by requiring that the award follow the law, judicial review of the merits is possible. To quote the court: “[t]he scope of arbitration is… a matter of agreement between the parties’ . . . and . . . [t]he powers of an arbitrator are limited and circumscribed by the agreement or stipulation of submission.”

To be sure, future California cases will turn on the precise wording of the arbitration clause as well as the submission agreement that places the matter before a neutral arbitrator. Parties who utilize arbitration as an alternate dispute resolution tool should therefore review and reassess the arbitration clauses used in their agreements in the wake of this important decision. While it remains to be seen whether the *Cable Connection* case will have an impact elsewhere, it definitely alters the arbitration landscape in California.