The Curious Case of Manifest Disregard [of the Law]

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Even casual observers of American arbitration law will have encountered the "manifest disregard of the law" doctrine. It has been invoked for decades by litigants seeking to set aside (vacate) an award under the Federal Arbitration Act (FAA). The doctrine is just one example of why the regime affecting commercial arbitration in the United States is often difficult to penetrate for non-American lawyers. Nowhere explicated in the FAA provision governing vacatur, the doctrine originates in a scrap of dictum found in a 1953 U.S. Supreme Court decision. The significance in 1953 of the relevant passage in Wilko v. Swan (346 U.S. 427 [1953]) might not have been readily apparent to many American lawyers, let alone foreign observers. After all, discretionary review had not been granted to address vacatur grounds, but rather to resolve whether a pre-dispute arbitration agreement required arbitration of claims arising under the 1933 Securities Act.

Nevertheless, in reaching the conclusion that judicial handling of such claims was essential, the Court was influenced by the limited review to which arbitral awards could be subjected. The Court wrote: "[T]he interpretations of the law by arbitrators in contrast to manifest disregard are not subject, in federal courts, to judicial review for error in interpretation" (346 U.S. at 436-437). Not surprisingly, at least initially, courts—including the Supreme Court itself— would take that passage as support for the notion that awards cannot be disturbed for errors of fact or law. (See Bernhardt v. Polygraphic Co. of America, 350 U.S. 198, 203-204(1956); Dembitzer v. Gutchen, 3 A.D. 2d. 211 (1957)).

At least by 1960, however, the important Second Circuit would guardedly concede that the Court's Wilko dictum acknowledged manifest disregard of the law as a theory of vacatur, presumably derived from the FAA vactur ground listed Section 10(a)(4) (exceeding of arbitral powers). Thereafter, most lawyers seeking vactur felt obliged to argue that the arbitrators had manifestly disregarded the law; typically these arguments were thinly veiled (and unsuccessful) attempts to attain merits review.

Over twenty years ago, Wilko was overruled. (Rodriguez de Quijas v. Shearson /American Express, Inc.490 U.S. 477 (1989). Yet, as of 2010, the manifest disregard genie has not been put back in the proverbial bottle.

What can account for the doctrine's durability? That it survived Wilko's demise , while ironic, can be explained by its origin in dictum; just as the cryptic fragment was not necessary to Wilko's subject matter arbitrability ruling concerning the 1933 Act, so was it not the reason the decision case was eventually overruled. Beyond that, the doctrine's longevity certainly cannot be explained by its utility as a restraint on arbitrator misadventure (awards are not often vacated for manifest disregard). Nor has the doctrine earned the support of commentators (they generally are critical of it). And, certainly

among courts it has not always been warmly received. Judge Posner wrote, for instance:

> A number of courts, including our own, have said that they can set aside arbitral awards if the arbitrators exhibited a "manifest disregard of the law." ….The formula is dictum… [and] was created ex nihilo ….[It] reflects precisely that mistrust of arbitration for which the Court in [later decisions] criticized Wilko. We can understand neither the need for the formula nor the role that it plays in judicial review of arbitration (we suspect none—that it is just words). If it is meant to smuggle review for clear error in by the back door, it is inconsistent with the entire modern law of arbitration. If it is intended to be synonymous with the statutory formula that it most nearly resembles—whether the arbitrators "exceeded their powers"—it is superfluous and confusing. (Baravati v. Josephthal, Lyon & Ross, Inc.,28 F.3d 704, 706 (7th Cir. 1994)).

As has been much discussed, last year in Hall Street Associates v. Mattel, Inc, 552 U.S. 576 (2008) the Court had an opportunity to confirm Judge Posner's suspicions, that the formula is "just words".

The Court was asked to determine whether the parties could expand by appropriate language in an arbitration agreement the grounds for vacatur, such as by stipulating that an award would be reviewable for errors of law. The Court concluded that under the FAA they may not add grounds to Section 10.

One making a quick read of Hall Street might be forgiven for concluding that manifest disregard was dead. The Court, after all, was quite clear in holding that that "§§10 and 11 respectively provide the FAA's exclusive grounds for expedited vacatur and modification and that "the FAA confines its expedited judicial review to the grounds listed in 9 U. S. C. §§10 and 11." (552 U.S. at 584, 592)

A closer look would engender more doubt, as, strictly speaking, the Court only opined that the language of Wilko did not support the thesis that disputants could add to the Section 10 grounds. Nevertheless, at minimum, would it not follow from the Court's language of exclusivity that manifest disregard of the law could not exist as a freestanding ground for vacatur; that at most it was a subcategory subsumed under one or more of Section 10's explicit grounds? Perhaps, but the Court failed to say so.

What the Court did do was to remark on the opacity of the Wilko dictum and that the Wilko Court's intentions were subject to debate (the Court observed: "maybe the term' 'manifest disregard' was "meant" to [accomplish x], but maybe it merely referred to [y],… [or it] may have been a shorthand for [z]" (552 U.S. at 585). It also implied that its position as a Court on the Wilko language should be distinguished from what individual Justices may have said about it. (See, e.g., Justice Stevens' dissent in Mitshibishi , 473 U.S 614, 656, 'manifest disregard' a collective reference to the Section 10 grounds).

Manifest disregard of the law is a poorly rooted oak tree born of a modest acorn that nevertheless to this minute generates bemusement. Lest one doubt that, there are new data over which to become perplexed. I have in mind last month's opinion in Stolt-Nielsen, SA v. Animal Feeds International Corp., 2010 WL 1655826 (U.S.). It was a maritime case in which the arbitrators' partial award decided that the arbitration clause, which was silent on the question of class arbitration, allowed such arbitration. The arbitrators had been influenced by the plurality opinion in Greentree Financial v. Bazzle (539 U.S. 444(2003)), but the district court ruled that in failing to perform a choice of law analysis that would have led to maritime usage, the arbitrators had manifestly disregarded the law. The Second Circuit reversed, reasoning that although the manifest disregard doctrine survived Hall Street as a

component of FAA Section 10(a)(4)(excess of powers), vacatur required that there be a rule known to the arbitrators that they then willfully repudiated. No rule prohibiting class treatment had been demonstrated by the resisting party under federal maritime or New York state law.

With manifest disregard so squarely involved in the case, the granting of certiorari surely meant that the 56 year old enigma might finally be demystified by the Court. The Supreme Court ruled in a 5:3 decision that the arbitral tribunal exceeded its powers within the meaning of FAA Section 10 by “imposing its own view of sound policy [favoring] class arbitration” instead of merely interpreting and enforcing the contract (2010 WL 1655826 (U.S.). *10).

In a footnote, the majority expressly declined to determine whether manifest disregard survived Hall Street. Nevertheless, it adopted, arguendo, the three -part test for manifest disregard identified by the Respondent and opined (without transparently applying each step) that “ [a]ssuming …such a standard applies, we find it satisfied….” (2010 WL 1655826 (U.S.) ftnt 3).

Having decided to not address the doctrine, it would seem to have sufficed to apply FAA Section 10(a)(4) alone, thus aiding in an understanding of one the FAA’s express grounds, without the distraction of the Wilko dictum. Presumably the same analysis as that offered by the Court would obtain. Now, however, we are left to wonder what limits on the doctrine remain. Can it really be manifest disregard when arbitrators prefer a plurality opinion arguably shedding the most light on the case before them (Bazzle), to a competing view more in line with the dissent in the same case? What is then left of the three part test accepted arguendo by the Court—had the arbitrators really willfully refused to apply a legal principle known by them to be controlling (to paraphrase the test)?

No doubt, the Court’s most recent dictum on manifest disregard will need some careful recasting lest the manifold restraints carefully placed on the doctrine over its lifespan dissolve, to no good end.