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Manifest Disregard After Hall Street

Gary B. Born (Wilmer Cutler Pickering Hale and Dorr LLP) · Monday, March 9th, 2009 · WilmerHale

The U.S. Supreme Court's recent decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1369 (2008) has provoked substantial commentary – as with many Supreme Court decisions regarding arbitration. The *Hall Street* decision held that the Federal Arbitration Act ("FAA") did not permit parties contractually to expand the grounds for vacating or modifying an arbitral award. In so doing, the Court adopted a sweeping, and arguably radical, interpretation of the FAA that raised uncertainties about a number of issues under the FAA, including the continuing viability of the "manifest disregard of law" ground for vacating arbitral awards and the authority of parties contractually to reduce the statutory grounds for vacating arbitral awards.

A recent Court of Appeals decision confirms the uncertainty produced by *Hall Street*. The decision, by the Fifth Circuit in *Citigroup Global Markets, Inc. v. Bacon*, 2009 WL 542780, held that manifest disregard of law was not a ground for vacating an arbitral award under the FAA in the United States. In so doing, the Court rejected a lengthy line of U.S. appellate decisions, as well as Supreme Court dicta, which recognized a non-statutory basis for vacating arbitral awards where the arbitrators acted in "manifest disregard of the law." The Fifth Circuit's decision furthers a split among the circuit courts regarding the interpretation of the *Hall Street* decision and the viability of "manifest disregard" as a basis for vacating arbitral awards. The resulting uncertainties ill-serve either the purposes of the FAA or the role of arbitration generally in efficient resolution of business disputes.

The Fifth Circuit began its analysis in *Citigroup Global Markets, Inc. v. Bacon* by underscoring the fact that, historically, U.S. courts have enjoyed only very limited powers to set arbitral awards aside. Beginning with an analysis of decisions prior to the 1925 enactment of the United States Arbitration Act, upon which the FAA (enacted in 1945) was based, the court discussed the historical trend of affirming awards even when the awards were "based upon error in law or fact." According to the Fifth Circuit, "strictly confining the perimeter of federal court review of arbitration awards is a widely accepted practice that runs throughout arbitration jurisprudence – from its early common law and equity days to the present." The Court's analysis was, in this regard, historically accurate and in keeping with developments in other jurisdictions around the world over the past several decades.

With this basic premise, the Fifth Circuit next reviewed the statutory grounds for setting aside or vacating an award under Section 10 of the FAA and the *Hall Street* decision. Although the issue presented in *Hall Street* did not deal directly with manifest disregard of the law as a grounds for

vacating an award, the Fifth Circuit interpreted the *Hall Street* decision as holding that Sections 10 and 11 of the FAA provided the *sole and exclusive* grounds for vacating or modifying an award under the FAA. Noting that the Supreme Court had reached its decision in *Hall Street* by focusing on the language of the FAA – which provides that an order "must" be confirmed unless one of the grounds in Section 10 or 11 apply – the Fifth Circuit concluded that only specifically-identified statutory grounds are available as grounds for challenging an arbitral award brought under the FAA.

The Fifth Circuit also noted that, while the standard of manifest disregard of law was not directly at issue in *Hall Street*, the Supreme Court rejected manifest disregard as an independent grounds for challenging an arbitration award. According to the Court of Appeals, the *Hall Street* decision reflected a "clearly and repeatedly stated holding . . . that §§ 10 and 11 provide the exclusive bases for vacatur and modification of an arbitration agreement under the FAA." At the same time, the Court of Appeals observed that application of the manifest disregard standard had been difficult for the courts and produced uncertain and conflicting results.

The Fifth Circuit noted the existence of divergent decisions by other appellate courts following the *Hall Street* decision. In particular, four other appellate decisions following *Hall Street* have considered whether manifest disregard of the law is still a valid basis for vacating an arbitral award under the FAA. The First Circuit stated in dicta that *Hall Street* abolished manifest disregard as a ground for vacatur (*see Ramos-Santiago v. United Parcel Service*, 524 F.3d 120, 124 n.3 (1st Cir. 2008)). The Sixth Circuit, Second Circuit and Ninth Circuit have continued to review arbitral awards for manifest disregard of the law, although they have adopted somewhat different approaches to the *Hall Street* decision and the ground of manifest disregard.

For example, the Sixth Circuit applied the manifest disregard standard by "narrowly construing the holding in *Hall Street* to apply only to contractual expansions of the grounds for review," and deciding that the Supreme Court had in fact hesitated in rejecting the manifest disregard standard. *See Coffee Beanery, Ltd. v. WW. L.L.C.*, 2008 WL 4899478, at *4 (6th Cir. Nov. 14, 2008). The Fifth Circuit disagreed with the Sixth Circuit's decision by noting that the opinion ignored "*Hall Street*'s express holding that the grounds for vacatur found in § 10 are exclusive;" the Fifth Circuit also found that the Supreme Court, in fact, had not hesitated from rejecting manifest disregard of the law as a grounds for vacating an award.

The Second and Ninth Circuits have also continued to review arbitral awards for manifest disregard of the law, but they have done so by recasting the standard as a shorthand for Section 10(a)(4) of the FAA, which allows a court to vacate an award "where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made." For example, in *Stolt-Nielsen SA v. AnimalFeeds Int'l Corp.*, 548 F.3d 85 (2d Cir. 2008), the Second Circuit recognized that *Hall Street* established that the exclusive grounds for vacating an arbitration award were provided for in the FAA. However, the Second Circuit continued to apply the grounds for vacating an award by "reconceptualiz[ing] [the standard] as a judicial gloss on the specific grounds for vacatur enumerated in section 10 of the FAA." Similarly, the Ninth Circuit also decided that manifest disregard was best understood as a shorthand for Section 10(a)(4), a position that the Ninth Circuit had taken even prior to the *Hall Street* decision. *See Comedy Club Inc. v. Improv West Assocs.*, 2009 WL 205046 (9th Cir. Jan. 29, 2009).

Without completely rejecting the Second and Ninth Circuit's reconceptualization of the standard as

part of Section 10(a)(4), the Fifth Circuit held that the Supreme Court's *Hall Street* decision had conclusively rejected manifest disregard as an independent, nonstatutory ground for disturbing an arbitration award. The Fifth Circuit added that "the term itself, as a term of legal art, is no longer useful in actions to vacate arbitration awards." Expressly overturning any prior Fifth Circuit precedent that held that "nonstatutory grounds may support the vacatur of an arbitration award," the court reversed the district court's decision vacating the arbitral award, and remanded the case to the district court for consideration of whether the award was subject to vacatur under any of the statutory grounds in the FAA.

The Fifth Circuit's decision compounds the uncertainties produced by *Hall Street* and its interpretational approach to the FAA. The Supreme Court's attention to the FAA is welcome, and has the potential to contribute to the development of U.S. arbitration law. The Court's decision in *Hall Street*, however, has not provided sufficient guidance to the courts or to parties who elect to arbitrate their disputes. In light of the split among the circuit courts in interpreting and applying *Hall Street*, the Court will very likely be asked to return to these issues in the near future.

When the Court does so, it would best honor the FAA and the strong US public policies favoring arbitration by endorsing the analysis of the Second, Fifth, and Ninth Circuits that the statutory grounds in the FAA are the exclusive grounds for vacating arbitral awards, that "manifest disregard of the law" does not exist as an independent, non-statutory basis for vacating arbitral awards, and that an arbitrator's disregard of the law can be a basis for vacating an arbitral award under §10(a)(4) of the FAA for excess of the arbitrator's authority only where "the arbitrator is fully aware of the controlling principle of law and yet does not apply it."

In revisiting its analysis in *Hall Street*, the Court can further honor the FAA and the strong US public policies favoring arbitration by giving broader effect to the parties' autonomy – the foundation of the arbitral process – to shape their arbitration, including the scope of judicial review of their arbitral award. That was a consideration that was not fully addressed in *Hall Street* and without which any interpretation of the FAA, or other national arbitration legislation, lacks viability.

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