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## ARTICLES

# IN SEARCH OF A STANDARD FOR JUDICIAL REVIEW OF LEGAL ERROR IN COMMERCIAL ARBITRATION AWARDS

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One of the principal characteristics supposedly distinguishing arbitration from litigation as a mode of dispute resolution is that an arbitral decision is essentially final — both as to matters of fact and also as to matters of law.<sup>1</sup>

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1. Section 1286.2 of the Code of Civil Procedure specifies the following limited grounds upon which an award may be vacated, all of which focus on the integrity of the process, not the merits:

- (a) The award was procured by corruption, fraud or other undue means;
- (b) There was corruption in any of the arbitrators;
- (c) The rights of such party were substantially prejudiced by misconduct of a neutral arbitrator;
- (d) The arbitrators exceeded their powers and the award cannot be corrected without affecting the merits of the decision upon the controversy submitted; or
- (e) The rights of such party were substantially prejudiced by the refusal of the arbitrators to postpone the hearing upon sufficient cause being shown therefor or by the refusal of the arbitrators to hear evidence material to the controversy or by other conduct of the arbitrators contrary to the provisions of

California appellate statements are legion to the effect that arbitration awards are not open to judicial review on their merits.<sup>2</sup> Since California enacted a comprehensive arbitration statute in 1927,<sup>3</sup> the California Supreme Court has adhered closely to the tenet that arbitrator decisions are not subject to judicial review for errors of law. This standard follows from the Court's assertions that an arbitrator generally is not obliged to follow the law, but instead is free to decide cases based upon "broad principles of justice and equity."<sup>4</sup>

In recent years, the Supreme Court has deviated from this path on only three isolated occasions when it reviewed and vacated arbitral awards as "against public policy."<sup>5</sup> One of these cases involved a McCarthy-era labor grievance arbitration in which the Court overturned an arbitrator's reinstatement of a Communist Party member.<sup>6</sup> In the other two cases, both of

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this title.

(West 1982).

2. California courts frequently say, "in the absence of some limiting clause in the arbitration agreement, the merits of the award, either on questions of fact or of law, may not be reviewed except as provided in the statute." *E.g.*, *Crofoot v. Blair Holdings Corp.*, 119 Cal. App. 2d 156, 186, 260 P.2d 156, 172 (1953).

3. California has had a statute relating to arbitration virtually since the state was admitted. Stats. 1851, ch. 4. However, it was not until the 1927 statute was enacted that written arbitration agreements uniformly became specifically enforceable in accordance with the provisions of what have since evolved through amendment into sections 1280 et seq. of the Code of Civil Procedure. *See Crofoot v. Blair Holdings Corp.*, *supra*, 119 Cal. App. 2d at 180-181, 260 P.2d at 169 (1953).

4. *See Grunwald-Marx, Inc. v. Los Angeles Joint Bd., Amalgamated Clothing Workers*, 52 Cal. 2d 568, 589, 343 P.2d 23, 35 (1959); *Sapp v. Barenfeld*, 34 Cal. 2d 515, 523, 212 P.2d 233, 239 (1949). Such a broad declaration of deference has prompted some lawyers to counsel clients against submitting disputes to arbitration. In other cases, parties have tailored arbitration clauses in an effort to preserve access to the courts for review of errors of law. One of the techniques for doing so relies on section 1286.2, subdivision (d) of the Code of Civil Procedure, which provides that an arbitration award may be vacated if "the arbitrators exceeded their powers." With this provision in mind, parties may draft an arbitration agreement which specifically limits the arbitrator's power to deciding cases according to the law of whatever jurisdiction is to be applicable. The recent decision in *Pacific Gas & Elec. Co. v. Superior Court*, 227 Cal. App. 3d 51, 82, 277 Cal. Rptr. 694, 712 (1991), has raised doubts about the efficacy of this technique. *See* discussion at pages 16-25, *infra*.

5. The United States Supreme Court has also endorsed the concept of refusing to enforce an arbitral award which violates some "explicit public policy." *W.R. Grace & Co. v. Local No. 759, Int'l Union of United Rubber Workers*, 461 U.S. 757, 766 (1983). That this proposition is not a broad license to review awards, however, is clear from the more recent case of *United Paperworkers Int'l Union v. Misco, Inc.*, 484 U.S. 29 (1987).

6. *See Black v. Cutter Laboratories*, 43 Cal. 2d 788, 790, 798-799, 278 P.2d 905, 911-912 (1955), *appeal dismissed*, 351 U.S. 292 (1956) (award in labor grievance arbitration

which were decided on the same day, the Court vacated awards in favor of unlicensed construction contractors.<sup>7</sup>

Notwithstanding the Supreme Court decisions, any number of court of appeal panels have felt free to review arbitral awards for errors of law<sup>8</sup> and, when courts disagreed with the law applied, awards have been vacated.<sup>9</sup>

The rationale used to justify review of an arbitral award for error of law has varied. In some instances, opinions have been tailored to the provisions of Code of Civil Procedure section 1286.2, subdivision (d).<sup>10</sup> Under this rubric, a court first asserts that the power of arbitrators is limited to deciding the law correctly and then concludes that the arbitrators have exceeded their power if they err as to the law.<sup>11</sup> Alternatively, a court which disagrees with an arbitral decision on a point of law may say that the decision was in excess of the power of the arbitrators because the issue had not been submitted to them for decision.<sup>12</sup>

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directing reinstatement of Communist Party member "against public policy, as expressed in both federal and state laws").

7. *Loving & Evans v. Blick*, 33 Cal. 2d 603, 204 P.2d 23 (1949); *Franklin v. Nat C. Goldstone Agency*, 33 Cal.2d 628, 204 P.2d 37 (1949). In *Loving & Evans*, which was a 4-3 decision, the dissenting justices argued that, by submitting to arbitration instead of objecting to it, the owner waived its defense that the contractor was unlicensed. See 33 Cal. 2d at 617, 620-625, 204 P.2d at 33-36 (dissenting opinions). The same justices dissented from *Franklin* on the same grounds. The unique power of the public policy against unlicensed contracting, as evidenced by the recent case of *Hydrotech Sys., Ltd. v. Oasis Waterpark*, 52 Cal.3d 988, 277 Cal. Rptr. 517 (1991) (unlicensed contractor denied recovery even though allegedly induced by fraud to perform work for which a license was required), undoubtedly influenced the decisions in *Loving & Evans* and *Franklin*.

8. *E.g.*, *Webb v. West Side Dist. Hosp.*, 144 Cal. App. 3d 946, 193 Cal. Rptr. 80 (1983) (confirmation of arbitral award for breach of contract affirmed, but only after the court reviewed and agreed with the merits of the arbitrator's determination that the contract did not restrain trade unlawfully).

9. *E.g.*, *Evans Prods. Co. v. Millmen's Union No. 550*, 159 Cal. App. 3d 815, 205 Cal. Rptr. 731 (1984) (award required employer to hire minor under 18 to work in violation of federal child labor law); *Retail Clerks Union, Local 334 v. Food Employers Council, Inc.*, 85 Cal. App. 3d 286, 149 Cal. Rptr. 428 (1978) (liquidated damage award invalid under Civil Code § 1670); *Allen v. Interinsurance Exch.*, 275 Cal. App. 2d 636, 80 Cal. Rptr. 247 (1969) (error as to law on contributory negligence).

10. Section 1286.2, subdivision (d) provides that an award may be vacated when "the arbitrators exceeded their powers."

11. See *Allen v. Interinsurance Exch.*, 275 Cal. App. 2d 636, 80 Cal. Rptr. 247 (1969).

12. See *Cobler v. Stanley, Barber, Southard, Brown & Assoc.*, 217 Cal. App. 3d 518, 265 Cal. Rptr. 868 (1990); *French v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 784

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In other cases, awards have been reviewed without regard to constraints like those imposed by section 1286. A "manifest disregard" of the law,<sup>13</sup> a "completely irrational" decision<sup>14</sup> or, as a recent opinion put it, an "egregious mistake"<sup>15</sup> may be grounds for vacating an award. These cases seem to be concerned with how far an arbitrator has strayed from their concept of the path of legal rectitude.<sup>16</sup>

Some courts have reviewed awards and been willing to set them aside only when the court could conclude that an error of law appeared on the face of the award.<sup>17</sup> However, the most recent case observed that it made no sense for review to depend on whether an error was apparent from the face of the award or not.<sup>18</sup>

Although the Supreme Court cases characterizing arbitral awards as not subject to review for errors of law frequently have been cited in support of decisions upholding awards, these decisions uniformly seem to have been ignored by court of appeal

F.2d 902, 908 (9th Cir. 1986).

13. This standard, which is derived from the United States Supreme Court opinion in *Wilko v. Swan*, 346 U.S. 427, 436-37 (1953), is that typically articulated in federal court cases.

14. *Lesser Towers, Inc. v. Roscoe-Ajax Constr. Co.*, 271 Cal. App. 2d 675, 699-702, 77 Cal. Rptr. 100, 115-118 (1969).

15. *Pacific Gas & Elec. Co. v. Superior Court*, 227 Cal. App. 3d 51, 84, 277 Cal. Rptr. 694, 714 (1991) (hereinafter cited as *PG&E v. Superior Court*).

16. As may be seen from the opinion in *San Martine Compania de Navegacion, S.A. v. Saguenay Terminals Ltd.*, 293 F.2d 796 (9th Cir. 1961), courts have struggled to decide how marked a departure from the judicial norm will be tolerated. In the *Saguenay Terminals* case, the Ninth Circuit considered degrees of error ranging from a mistaken view in which the arbitrators "had not gone too far afield" to an error so "egregious" that "no sensible layman would be guilty of," *id.* at 801 n.4, but concluded that more would be necessary to constitute "manifest disregard." Its formulation was arbitrators understanding the law and consciously not applying their understanding. *See id.* at 801. An award resulting from such a decision would be the equivalent of an award procured by 'undue means.' *See id.* In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930 (2d Cir. 1986), the court said both that an "arguable difference" about the law was not enough, but that the "governing law" must be "well defined, explicit and clearly applicable," *id.* at 934, and that "manifest disregard" would exist when an "arbitrator appreciates the existence of a clearly governing legal principle, but decides to ignore or pay no attention to it." *Id.* at 933. In other words, the error must be "obvious and capable of being readily and instantly perceived by the average person qualified to serve as an arbitrator." *Id.*

17. *E.g.*, *Campbell v. Farmers Ins. Exch.*, 260 Cal. App. 2d 105, 67 Cal. Rptr. 175 (1968).

18. *PG&E v. Superior Court*, 227 Cal. App. 51, 79, 82 Cal. Rptr. 694, 712 (1991).

cases in which awards have been reviewed for errors of law.<sup>19</sup>

Further, although courts regularly recite that an exception to the rule of non-reviewability arises when the parties to arbitration agree to reserve questions of law for review in the courts, it is rare to see any reasoned inquiry into the issue of whether parties have agreed to such a reservation. In one recent case, for example, after acknowledging that conventional appellate review of points of law was proper if the parties had so provided, the court leapt to the conclusion that the parties before it had not.<sup>20</sup>

This paper surveys cases under California law in which commercial arbitration awards have been reviewed for errors of law and proposes a coherent approach to judicial review of alleged errors of law in commercial arbitration awards.<sup>21</sup> Both of the following issues will be addressed:

1. When and how courts should decide whether parties to an arbitration agreement have reserved arbitrator decisions on points of law for judicial review.

2. Whether and, if so, when and by what standard courts

19. It is not clear from the opinions whether the court of appeal panels have been unaware of the decisions or whether they were viewed as not applicable.

20. See *PG&E v. Superior Court*, 227 Cal. App. 51, 66, 277 Cal. Rptr. 694, 701 (1991).

21. Because of the broad reach of Commerce Clause jurisdiction, see *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983), many arbitration agreements may be subject to enforcement under the United States Arbitration Act, 9 U.S.C.A. §§ 1 et seq. (1980) (the "Federal Act"). Judicial review of arbitral awards for errors of law under the Federal Act is outside the scope of this article. It is governed by section 10 of the Federal Act, 9 U.S.C.A. § 10 (1980), and cases thereunder. However, California law will apply when the terms of an arbitration agreement that is subject to the Federal Act provide for California law to govern the arbitration. See *Vol Information Sciences, Inc. v. Board of Trustees of the Leland Stanford Junior Univ.*, 489 U.S. 468 (1989); *Pacific Gas & Elec. Co. v. Superior Court*, 227 Cal. App. 3d 51, 65, 277 Cal. Rptr. 694, 700 (1991).

In general, this article is also not concerned with the review of awards in labor grievance arbitrations under collective bargaining agreements. As California has acknowledged, the review of such awards even in state courts is governed by section 301 of the federal Labor Management Relations Act. 29 U.S.C.A. § 185(a) (1978). See *O'Malley v. Wilshire Oil Co.*, 59 Cal. 2d 482, 486, 30 Cal. Rptr. 452, 455, 381 P.2d 188, 191 (1963); *Screen Actors Guild v. A. Shane Co.*, 225 Cal. App. 3d 260, 275 Cal. Rptr. 220 (1990); *Greenfield v. Mosley*, 201 Cal. App. 3d 735, 247 Cal. Rptr. 314 (1988); *Safeway Stores, Inc. v. Brotherhood of Teamsters, Local No. 70*, 83 Cal. App. 3d 430, 435, 147 Cal. Rptr. 835, 838 (1978).

should review arbitrator decisions on points of law when the parties have not agreed to reserve such issues for review.

1. *Determination of Reserved Right of Review*

Conceptually, an agreement whereby parties provide for submission of a dispute to arbitration, but at the same time agree to reserve arbitrator decisions on points of law or, for that matter, issues of fact for review by the courts should present no problem. As has been recognized:

The strength of arbitration is that it is not compulsory but is predicated upon the voluntary agreement of the parties to arbitrate future or existing disputes.<sup>22</sup>

If the courts are going to respect an agreement of parties to arbitrate, there is no reason they should not also respect a reservation in such an agreement of the right of judicial review of an arbitral decision. It is, accordingly, not surprising that no California case has been found in which such a reservation has been questioned.<sup>23</sup>

The question, of course, is not whether parties can enter into such an agreement, but whether they have done so. What the parties have agreed to is, thus, the first question a court should address in deciding whether to review an arbitral award for errors of law.

The issue is simple if the parties state *in haec verba* in their arbitration agreement that conclusions of law in an arbitration award shall be subject to judicial review or, even more clearly, that an arbitration award shall be subject to judicial review for errors of law.

An alternative technique which has sometimes been recommended by lawyers, including the author, is to limit the power of the arbitrator or arbitrators under the arbitration agreement to

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22. *Crofoot v. Blair Holdings Corp.*, 119 Cal. App. 2d 156, 184, 260 P.2d 156, 170-171 (1953).

23. Section 1296, which was added to the Code of Civil Procedure in 1979, provides that, if a construction contract with a public agency requires that an arbitration award be supported by law and substantial evidence, it shall be vacated if not supported by substantial evidence or if based on an error of law. What the legislature thought it was adding to the law by this provision is not clear.

deciding issues submitted to them in accordance with some specified body of law, for example, the law of California as applied to disputes arising in California between citizens of California. The thinking behind this approach is that it gives a court a “peg” on which to hang judicial review, *i.e.*, the provision in Code of Civil Procedure section 1286.2, subdivision (d) which empowers a court to vacate an arbitration award when the arbitrators have exceeded their powers.<sup>24</sup>

Suppose, however, that parties simply provide for their arbitration to be “governed by the law of California” or that disputes in arbitration must be decided “in accordance with the law of California.”

Such a provision does not necessarily mean that the parties desire to reserve arbitrator decisions about California law for review by the courts. As has been recognized recently, the issue of applicable law is distinct from the issue of judicial reviewability.<sup>25</sup>

The parties may want California law to govern the outcome of their dispute, but they may also be content to abide by arbitrator determinations of California law, regardless of whether the arbitration rulings are correct or erroneous.<sup>26</sup>

Indeed, if the agreement to arbitrate is truly consensual, who is to say that the parties are not willing to accept the risk of an arbitrator being dead wrong on the law in exchange for other benefits to be derived from arbitration — privacy, finality, etc.<sup>27</sup>

Even though a governing law provision does not necessarily imply reservation of points of law for judicial review, it also does not necessarily mean that the parties have agreed to forego such

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24. The efficacy of this technique has recently been opened to question. See *PG&E v. Superior Court*, 227 Cal. App. 3d 51, 277 Cal. Rptr. 694 (1991).

25. See *id.* at 82, 277 Cal. Rptr. at 712.

26. *Id.*, 277 Cal. Rptr. at 712.

27. If the arbitration agreement is explicit in submitting an issue of law to arbitration with knowledge of the finality of the arbitral process, the losing party cannot complain if a court refuses to review the resulting award. See *International Bhd. of Teamsters Local No. 117 v. Washington Employers, Inc.*, 557 F.2d 1345 (9th Cir. 1977) (award of punitive damages for violation of state statute upheld in collective bargaining contract arbitration, when parties submitted issue of statutory violation to arbitration).



review. As may readily be appreciated, the parties may have desired judicial review, but simply may not have expressed their agreement artfully. Alternatively, desperation may imprint one memory of the intent of an unclear arbitration agreement upon the mind of the side which loses in arbitration, while the heady haze of victory may blot out any such intent from the mind of the side which prevails.

When one side is dissatisfied with an arbitral award and claims that a right to judicial review of errors of law was reserved in the arbitration agreement, but the party supporting the award contends that the agreement reserved no such right, a court is presented with an issue as to the proper interpretation of the arbitration agreement.

There is no reason why the dispute over the right to judicial review should not be dealt with like any other dispute requiring interpretation of an arbitration agreement.<sup>28</sup> The only difference is that the matter before the court is whether to vacate an award or not instead of the preliminary issue of whether to compel arbitration or not.

In either event, a trial court should attempt to decide the question by utilizing the language of the agreement and the canons of construction to ascertain the intent of the parties.<sup>29</sup> If the language of the agreement appears susceptible of an interpretation contended for by either of the parties, the court should also consider extrinsic evidence in support of and in opposition to the alleged meaning.<sup>30</sup>

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28. The ordinary rules of contract interpretation apply to an arbitration agreement. See *Victoria v. Superior Court*, 40 Cal. 3d 734, 738-739, 222 Cal. Rptr. 1, 2-3, 710 P.2d 833, 834-835 (1988). "Courts are not at liberty to shirk the process of construction under the empire of a belief that arbitration is beneficent any more than they may shirk it if their belief happens to be to the contrary." *Marchant v. Mead-Morrison Mfg. Co.*, 252 N.Y. 284, 299-300, 169 N.E. 386, 391 (1929) (J. Cardozo).

29. *Ticor Title Ins. Co. v. Rancho Santa Fe Assn.*, 177 Cal. App. 3d 726, 730, 223 Cal. Rptr. 175, 177 (1986); *Bergin v. Van der Steen*, 107 Cal. App. 2d 8, 13, 236 P.2d 613, 617 (1951). Another line of California cases holds that the purpose of the rules of construction is to ascertain the meaning of the words used in the agreement, thus setting forth an objective approach. See, e.g., *Brant v. California Dairies*, 4 Cal. 2d 128, 133, 48 P.2d 13, 16 (1935); *Mission Valley East, Inc. v. County of Kern*, 120 Cal. App. 3d 89, 97, 174 Cal. Rptr. 300, 305 (1981).

30. *Pacific Gas & E. Co. v. G.W. Thomas Drayage etc. Co.*, 69 Cal. 2d 33, 37-40, 69 Cal. Rptr. 561, 564-566, 442 P.2d 641, 644-646 (1968); *Southern Pac. Land Co. v. Westlake Farms, Inc.*, 188 Cal. App. 3d 807, 815-816, 233 Cal. Rptr. 794, 799 (1987).

The trial court's conclusion will be subject to de novo review on appeal, unless it turns on the credibility of extrinsic evidence.<sup>31</sup> When extrinsic evidence is in conflict, any reasonable construction by the trial judge should be upheld.<sup>32</sup>

The recent case of *Pacific Gas & Electric Co. v. Superior Court*<sup>33</sup> raised just such an issue. The arbitration agreement did not refer expressly to any right of judicial review. However, as amended by a prehearing stipulation, the agreement did call for the arbitral award to be in the form of a statement of decision complying with Code of Civil Procedure section 632.<sup>34</sup> What was the intent of the parties? On the one hand, a statement of decision may have been required because the parties desired to reserve errors of law for judicial review. On the other hand, while the parties may have been willing to accept the arbitral award as final, even if wrong on the law, they may have provided for a formal statement of decision for any number of reasons, including the desire to impose a discipline on the arbitrators' decision making process.<sup>35</sup>

Instead of searching for the intent of the parties, however, when the losing side in *PG&E* sought to vacate the award, the superior court apparently jumped to the conclusion that a right to judicial review was reserved simply because the submission to arbitration set forth specific questions about the parties' legal obligations. The court fell into the trap of supposing that, if arbitrators were required to decide a dispute according to external law, they were not empowered to mistake the law and an award based upon an erroneous view of the law should, accordingly, be vacated because it exceeded their powers.<sup>36</sup>

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31. *Conejo Valley Unified School Dist. v. William Blurock & Partners, Inc.*, 111 Cal. App. 3d 983, 987, 169 Cal. Rptr. 102, 104 (1980).

32. *Parsons v. Bristol Dev. Co.*, 62 Cal. 2d 861, 866, 44 Cal. Rptr. 767, 770-771, 402 P.2d 839, 842-843 (1965); *Los Banos Gravel Co. v. Freeman*, 58 Cal. App. 3d 785, 791-792, 30 Cal. Rptr. 180, 183 (1976); *Medical Operations Management, Inc. v. National Health Laboratories, Inc.*, 176 Cal. App. 3d 886, 891, 222 Cal. Rptr. 455, 458 (1986).

33. 227 Cal. App. 3d 51, 277 Cal. Rptr. 694 (1991).

34. *Id.* at 62, 277 Cal. Rptr. at 698.

35. *See id.* at 82, 277 Cal. Rptr. at 712. As one authority put it, a provision requiring arbitrators to abide by particular rules of law in their decision may merely be "directory" and not a limitation on their powers. STURGES, *COMMERCIAL ARBITRATION & AWARDS* 794 (1930).

36. *Id.* 227 Cal. App. 3d at 62-63, 277 Cal. Rptr. at 699.

The court of appeal set out to correct the error of the superior court's ways, but fell into a trap of its own. It began by acknowledging the established principle that:

the parties to a contract may draft an arbitration provision so as to afford judicial review of questions of law.<sup>37</sup>

In the event of disagreement, as in the *PG&E* case, it follows, as previously stated, that a preliminary issue is whether the parties have so provided. The court of appeal held that the superior court erred in concluding that imposition of a requirement on arbitrators to follow external law necessarily implied a right to judicial review of the arbitrators' decision.<sup>38</sup> Parties might provide for their arbitration to be governed by external law, it reasoned, without providing for judicial review. So far so good. However, the court of appeal then jumped to a conclusion of its own, namely, that the parties had not provided for judicial review:

The question here is what judicial review should be afforded where they [the parties] have not done so [provided for judicial review].<sup>39</sup>

The court based this assumption on nothing more than the "common expectation" that, when parties agree to "binding" arbitration "in the present day world," they expect the decision of the arbitrators to be "final."<sup>40</sup> In short, the question was not dealt with, as it should have been, by remanding the case for a proper determination by the trial court.<sup>41</sup>

## 2. *Standard of Review in Absence of Reserved Right*

The *PG&E* court went on to attempt the task of formulating a standard of judicial review of arbitrator error to be applied

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37. *Id.* at 81, 277 Cal. Rptr. at 712.

38. *Id.* at 65, 277 Cal. Rptr. at 701.

39. *Id.* at 81, 277 Cal. Rptr. at 712.

40. *Id.* at 82, 277 Cal. Rptr. at 712.

41. In all fairness to the *PG&E* court, there is no suggestion in the opinion that the argument of either of the parties focused specifically on the issue of whether they intended in their arbitration agreement to reserve a right to judicial review. This may indicate that they simply did not address the issue of reviewability in negotiating the arbitration agreement. The court, thus, probably reached the correct result, but its opinion obscures the analytical framework which should have been employed.

despite the absence of any reserved right of review.<sup>42</sup> Its opinion dealt successfully with one of the principal incongruities in earlier court of appeal decisions, *i.e.*, making review available when error appeared on the face of an award, but not otherwise.<sup>43</sup> However, like many of its predecessors, it was either unaware of or ignored the logic of the governing California Supreme Court authority.<sup>44</sup>

#### a. Supreme Court Decisions

The genesis of the competing lines of authority concerning review of arbitration awards in the absence of a reserved right of review, at least so far as California is concerned, appears to lie in the early case of *Muldrow v. Norris*,<sup>45</sup> in which the Supreme Court vacated an award because the arbitrators had applied an erroneous measure of damages.

The *Muldrow* court wrote, on the one hand, that, "under a general submission," *i.e.*, one that does not limit their power so that their awards must be in accordance with external rules of law, arbitrators may decide cases "on principles of equity and good conscience."<sup>46</sup> If they do, "a mere mistake of law cannot be taken advantage of."<sup>47</sup> To avail themselves of such immunity, however, arbitrators must render a "general" award, *i.e.*, an award that says nothing more, for example, than "A shall pay B \$ X."<sup>48</sup>

On the other hand, said the court in *Muldrow*, "in all cases

42. *Id.* at 84, 277 Cal. Rptr. at 714.

43. See discussion at pages 41-51, *infra*.

44. Neither *Sapp v. Barenfeld*, 34 Cal. 2d 515, 212 P.2d 233 (1949), nor *Grunwald-Marx, Inc. v. Los Angeles Joint Bd. Amalgamated Clothing Workers*, 45 Cal. 2d 501, 289 P.2d 476, 37 A.L.R. 2d 1349 (1955), which, as discussed *infra*, appear to be controlling, is cited anywhere in the *PG&E* opinion. The court's extensive survey of the historical development of judicial review of arbitral awards in California simply skips over these cases.

45. 2 Cal. 74 (1852). *Muldrow* was decided in an era when courts were hostile to arbitration. Thus, even though the parties had agreed in their submission not to appeal from the arbitrators' award, the Supreme Court readily entertained the appeal saying, "agreements of parties cannot divest Courts of law or equity of their proper jurisdiction." 2 Cal. at 79.

46. *Id.* at 77.

47. *Id.*

48. See *id.* A general award was again held immune from review in *Peachy v. Ritchie*, 4 Cal. 205 (1854).

where the arbitrators give the reasons for their finding," i.e., what was then called a "special" award, "they are supposed to have intended to decide according to law [as opposed to general principles of fairness and equity] . . . In such cases if they mistake the law, the award must be set aside."<sup>49</sup>

Shortly thereafter, in *Carsley v. Lindsay*, the California Supreme Court reversed a trial court judgment vacating an arbitral award.<sup>50</sup> The dissatisfied arbitrant sought to uphold the trial court's decision on the ground that the award was "contrary to law and evidence."<sup>51</sup> However, the Supreme Court said that it was "not aware that an award of an arbitration can be impeached on this ground."<sup>52</sup>

Although the award in *Carsley* could have been characterized as a general award, as the term was used in *Muldrow*, the Court did not mention any distinction between a general award and a special award or between an error of law which appeared on the face of an award and one which did not.

The *Muldrow* notion that an arbitral award may be reviewed for errors of law if they appear on the face of the award was revived in the case of *In Re Connor*.<sup>53</sup> However, in *Connor* the proposition was qualified in that awards would not be vacated for "mere ordinary errors," but only those which are "gross."<sup>54</sup>

Again, in *Utah Construction Co. v. Western Pacific Ry. Co.*,<sup>55</sup> the California Supreme Court reiterated that an arbitral award "cannot be impeached on the ground that it is contrary to

49. *Id.* at 78.

50. 14 Cal. 390 (1859).

51. *Id.* at 395.

52. *Id.* *Muldrow* is not mentioned in the opinion or in the reported summary of the arguments.

53. 128 Cal. 279, 60 P. 862 (1900).

54. *Id.* at 282, 60 P. 862. This concept appears to have been drawn from Code of Civil Procedure section 1289, as it then existed, which made "gross error" a ground for vacating a statutory arbitration award.

55. 174 Cal. 156, 162 P. 631 (1916). Curiously enough the *Utah Construction Co.* case is the only California case found by the author in which the parties actually reserved a right of judicial review for errors of law. They did so, however, only as to one of the issues in the case.

law, unless the error appears on its face.”<sup>56</sup>

A second requirement in some more recent cases that the rights of a party be “substantially prejudiced” surfaced for the first time when the *Utah Construction* court added that an award would not be vacated for error appearing on its face unless the error also “causes substantial injustice.”<sup>57</sup>

The tide in the Supreme Court turned against review of arbitral awards in the wake of the 1927 enactment of a “comprehensive all-inclusive” arbitration statute which abolished common law arbitration.<sup>58</sup> An agreement to arbitrate future disputes has since been specifically enforceable, whereas before it had been regarded as “invalid and unenforceable, as constituting an attempt to oust the legally constituted courts of their jurisdiction and to set up private tribunals.”<sup>59</sup>

Enactment of the comprehensive arbitration statute reflected a significant shift in public policy, according to the Supreme Court in *Pacific Vegetable Oil Corp. v. C.S.T., Ltd.*<sup>60</sup> By providing for enforcement of all written arbitration agreements, persons were encouraged “to avoid delays by obtaining adjustment of their differences by an agency of their own choosing.”<sup>61</sup>

The *Pacific Vegetable Oil Corp.* opinion also said it was clear under the statute that “the merits of the controversy between the parties are not subject to judicial review.”<sup>62</sup> However, the *Pacific Vegetable Oil Corp.* case involved a controversy over arbitrator fact finding and fact finding procedure, not whether the arbitrators applied the law correctly.<sup>63</sup>

56. *Id.* at 160-161, 162 P. at 633.

57. *Id.*

58. See *Crofoot v. Blair Holdings Corp.*, 119 Cal. App. 2d 156, 182, 260 P.2d 156, 169 (1953).

59. *W. H. Blodgett Co. v. Bebe Co.*, 190 Cal. 665, 214 P. 38, 26 A.L.R. 1070 (1923).

60. 29 Cal. 2d 228, 174 P.2d 441 (1946).

61. *Id.* at 240, 174 P.2d at 449.

62. *Id.* at 233, 174 P.2d at 445. Under the 1927 statute, the grounds for vacating an award were specified in section 1288 of the Code of Civil Procedure. They are now in section 1286.2.

63. *Id.* Courts of appeal continued to review arbitral awards for errors of law which appeared on their face. See *Popcorn Equip. Co. v. Page*, 92 Cal. App. 2d 448, 453-454, 207 P.2d 647, 649-650 (1949); *United Farmers Assn. of California v. Klein*, 41 Cal. App. 2d 766, 769, 107 P.2d 631, 633 (1941); *In Re Frick*, 130 Cal. App. 290, 292, 19 P.2d 836,

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In 1949, in *Sapp v. Barenfeld*,<sup>64</sup> the Supreme Court reversed a trial court's order vacating an arbitration award and remanded the case for entry of an order confirming the award despite a claim that the arbitrators had wrongly decided one of the legal issues put to them, to wit, a claim by the owner of a building for damage resulting from delay in completion of construction.

The *Sapp* court held that the claimed error of law did not support vacating the award, observing that, "unless specifically required to act in conformity with rules of law," arbitrators were free to "base their decision upon broad principles of justice and equity."<sup>65</sup>

Thus, arbitrators were free to reject a claim which a party could assert successfully in a judicial action.<sup>66</sup> Moreover, they could do so either "impliedly," *i.e.*, in a general award or "expressly," *i.e.*, in an award in which they said what they were doing and why.<sup>67</sup> No mention was made in *Sapp* of any distinction between errors appearing on the face of an award and errors masked by the general nature of the award.<sup>68</sup>

The *Sapp* decision was followed in 1953 by the off-cited court of appeal decision in *Crofoot v. Blair Holdings Corp.*,<sup>69</sup> in which the late Professor George Osborne, then on the Stanford Law faculty and later at Hastings, arbitrated a complex commercial dispute.

If there had been any error in *Crofoot*, it undoubtedly would have appeared on the face of the award. Professor Osborne exposed his reasoning in detail in 215 pages of findings and opinion leading to a five-page award.<sup>70</sup>

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836-837 (1933).

64. 34 Cal. 2d 515, 212 P. 2d 233 (1949).

65. *Id.* at 523, 212 P.2d at 239.

66. *Id.*

67. *Id.*

68. *Id.* Even though an extensive list of California cases involving review of arbitration awards was cited in *PG&E v. Superior Court*, 227 Cal. App. 51, 277 Cal. Rptr. 694 (1991), that court's research, like any number of other court of appeal opinions, either ignored or failed to discover this pivotal case.

69. 119 Cal. App. 2d 156, 260 P.2d 156 (1953).

70. *Id.* at 165, 260 P.2d at 159.

The First District Court of Appeal affirmed the trial court's order and judgment confirming the award. The court read both *Pacific Vegetable Oil Corp.* and *Sapp* as rejecting the rule of *Utah Construction Co.* and concluded, accordingly, that:

in the absence of some limiting clause in the arbitration agreement, the merits of the award, either on questions of fact or of law, may not be reviewed except as provided in the statute.<sup>71</sup>

The statutory grounds of judicial review, of course, as then contained in section 1288 of the Code of Civil Procedure and now in section 1286.2, do not include an error of law, whether or not appearing on the face of an award.

The view that arbitral awards are not reviewable for errors of law was reinforced in *Griffith Co. v. San Diego College for Women*.<sup>72</sup> The Supreme Court cited both *Sapp* and *Crofoot* approvingly in *Griffith Co.*, but, strictly speaking, the discussion was only dicta, as the Court concluded that the arbitrators had not made any error of law.<sup>73</sup>

Another nail in the coffin of reviewability of legal error was driven by the Supreme Court in *O'Malley v. Petroleum Maintenance Corp.*,<sup>74</sup> where the Court again affirmed a judgment confirming an award — this time in a labor grievance arbitration — despite a contention that the arbitrators had erred on a matter of law.<sup>75</sup>

71. *Id.* at 185-186, 260 P.2d at 171-172. The statute in question was California's arbitration statute as it had been completely redrafted in 1927. The grounds for vacating an arbitration award, as then specified in section 1288 of the Code of Civil Procedure, are essentially the same as now set forth in section 1286.2. Indeed, they have remained in large part the same since as long ago as in the earliest of California's arbitration statutes. See Stats. 1851, Ch. 5, § 386. However, the significance of the 1927 legislation was that it applied to all written arbitration agreements and thereby abolished the distinction between common law arbitration, which was relatively ineffectual, and statutory arbitration, which had previously been available only in limited situations. See *Crofoot v. Blair Holdings Corp.*, 119 Cal. App. 2d 156, 180-182, 260 P.2d 156, 169 (1953). As recognized by the Supreme Court in the *Pacific Vegetable Oil Corp.* case, *supra*, the 1927 statutory reform replaced a juridical hostility to arbitration with a "strong public policy in favor of arbitration." *Id.* at 184, 260 P.2d at 170.

72. 45 Cal. 2d 501, 289 P.2d 476, 47 A.L.R. 2d 1349 (1955).

73. *Id.* at 515-516, 289 P.2d at 484, 47 A.L.R. 2d at 1357.

74. 48 Cal. 2d. 107, 308 P.2d 9 (1957).

75. The arbitrators allegedly erred in *Petroleum Maint. Co.* in determining that discharge of an employee was arbitrable. They said they were bound by a superior court order compelling arbitration of the merits of the discharge and that, if the question had



*Sapp* and *Crofoot* were cited with approval still again in *Grunwald-Marx, Inc. v. Los Angeles Joint Board, Amalgamated Clothing Workers*.<sup>76</sup> The late Justice Raymond Peters, who had written *Crofoot* while on the Court of Appeal, wrote for the Court in this case, saying that the arbitrators were correct on the law, this time in the reasons they gave for their award, just as they had been correct in *Griffith Co.*, but that, even if they had not been correct, the award was proper, because, as in *Sapp*, "arbitrators may base their decisions on broad principles of justice and equity."<sup>77</sup>

The Supreme Court reiterated its views once more in *Morris v. Zuckerman*,<sup>78</sup> both that, after a matter had been decided by arbitration, the merits of the controversy were not open to judicial review and also that, as in *Sapp*, arbitrators are not constrained by rules of law.<sup>79</sup>

Although judicial review of alleged errors of law in an arbitral award has not been before the Supreme Court in more than 20 years since *Morris v. Zuckerman*, the Court has given little indication, if any, that it would depart from the views expressed originally in *Sapp*. Indeed, in a case reserving to the courts the question of whether an insured waived arbitration of an uninsured motorist claim by failing to comply with the one-year time limitation in section 11580.2, subdivision (i) of the Insurance Code, the Supreme Court quoted *Sapp* for the freedom given to arbitrators in deciding cases, as distinguished from the control imposed upon a court, which must apply the law as it is laid

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been open, they would have concluded that the discharge was not arbitrable. 48 Cal. 2d at 113, 308 P.2d at 13 (dissenting opinion). The court majority said, in effect, that it did not care whether the reasons were correct, because it was not going to inquire into the merits of the decision. *Id.* at 111-112, 308 P.2d at 12. This is similar to the rule on appeal from a trial court decision which reaches the right result although for the wrong reasons. "[A] ruling or decision, itself correct in law, will not be disturbed on appeal merely because given for a wrong reason." *D'Amico v. Board of Medical Examiners*, 11 Cal. 3d 1, 9, 112 Cal. Rptr. 786, 799, 520 P.2d 10, 23 (1974).

76. 52 Cal. 2d 568, 589, 343 P. 2d 23, 35 (1959).

77. *Id.* at 589, 343 P.2d at 35.

78. 69 Cal. 2d 686, 72 Cal. Rptr. 880, 446 P. 2d 1000 (1968).

79. *Id.* at 691, 72 Cal. Rptr. at 884, 446 P.2d at 1004. See *Greenfield v. Mosley*, 201 Cal. App. 3d 735, 745, 247 Cal. Rptr. 314, 320 (1988) (J. Arabian). Although the *Greenfield* court reviewed an arbitration award for error of law, it actually reversed a judgment vacating the award because it concluded that no error appeared on the face of the award. *Id.* at 748, 247 Cal. Rptr. at 322.

down by the authorities.<sup>80</sup>

#### b. Court of Appeal Decisions

If the Supreme Court thought that by *Sapp* it was creating an Eden of non-reviewability, the ink was scarcely dry on its opinion before the serpent began lurking about. Thus, in *United States Plywood Co. v. Hudson Lumber Co.*,<sup>81</sup> while the court relied on both *Sapp* and *Crofoot* to uphold an award against attack by a dissatisfied arbitrator, it noted that no error appeared on the face of the award and buttressed its decision with pre-*Sapp Crofoot* authority that an arbitral award would not be reviewed for errors of law “unless the error appears on the face of the award.”<sup>82</sup>

From *United States Plywood* to *PG&E*, court of appeal panels have since vacillated in their treatment of arbitral awards. One line of cases has adhered dutifully to *Sapp* and *Crofoot*. For example, in *Interinsurance Exchange v. Bailes*,<sup>83</sup>

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80. See *Freeman v. State Farm Mut. Auto. Ins. Co.*, 14 Cal. 3d 473, 121 Cal. Rptr. 477, 535 p. 2d 341 (1975). The Court did render a tantalizing decision in *Orpustan v. State Farm Mut. Auto. Ins. Co.*, 7 Cal. 3d 988, 103 Cal. Rptr. 919, 500 P. 2d 1119 (1972). This case upheld the requirement of “physical contact” as a condition of recovery on uninsured motorist coverage, but said it was for an arbitrator, not the court, to decide whether the physical contact had occurred within the meaning of the law. What the Court did not address was how it would react to an attack on an award if it disagreed with an arbitrator’s decision. The only case in which the Court actually might be said to have wavered from its stance is *Jefferson Ins. Co. v. Superior Court*, 3 Cal. 3d 398, 90 Cal. Rptr. 608, 475 P. 2d 880 (1970), where a purported arbitral award was vacated because of an error of law on the theory that property insurance appraisers are not arbitrators and their decision is, accordingly, not entitled to the same finality as an arbitral award. However, while sitting on the court of appeal, one current Supreme Court Justice apparently subscribed to the notion that an award may be vacated for error of law, if the error appears on the face of the award. See *Greenfield v. Mosley*, 201 Cal. App. 3d 735, 745, 247 Cal. Rptr. 314, 320 (1988) (J. Arabian). Although the *Greenfield* court reviewed an arbitration award for error of law, it actually reversed a judgement vacating the award because it concluded that no error appeared on the face of the award. *Id.* at 748, 247 Cal. Rptr. at 322.

81. 124 Cal. App. 2d 527, 269 P.2d 93 (1954).

82. The *United States Plywood* court quoted both from *In re Frick*, 130 Cal. App. 290, 292, 19 P.2d 836, 836-837 (1930), which in turn cited to *Carsley* and *Utah Constr. Co.*, and also from *Popcorn Equip. Co. v. Page*, 92 Cal. App. 2d 448, 451, 207 P.2d 647 (1949), adding emphasis to the quote from *In re Frick*. Interestingly, Justice Peters, who had written *Crofoot*, concurred in the *United States Plywood* decision. See also *Sampson Motors, Inc. v. Roland*, 121 Cal. App. 2d 491, 494, 263 P.2d 445, 447 (1953), which similarly cited *Utah Constr. Co.* and *Popcorn Equip. Co.*

83. 219 Cal. App. 2d 830, 33 Cal. Rptr. 533 (1963).

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the court cited the entire chain of Supreme Court cases from *Pacific Vegetable Oil Corp.* to *Grunwald-Marx* in affirming an arbitral award.<sup>84</sup> The court concluded that the arbitrator had erred in denying res judicata effect to a previous judicial determination, but said that:

It is now the settled law of California that, except for the matters expressly provided for in section 1286.2 of the Code of Civil Procedure, a decision of an arbitrator is binding, whether or not correct in law or in fact.<sup>85</sup>

Other courts like *Durand v. Wilshire Ins. Co.*<sup>86</sup> similarly concluded that arbitrators had erred in applying the law (collateral estoppel in *Durand*), but nevertheless affirmed the awards on the ground that errors of law by an arbitrator are not subject to judicial review.<sup>87</sup>

Still other courts appeared ill at ease in going this far. Thus, while relying on *Crofoot* to reject the argument that an arbitration award should be vacated because of "manifest disregard" of the law, the court in *Lesser Towers, Inc. v. Roscoe-Ajax Construction Co.*,<sup>88</sup> suggested that the arbitrators would have exceeded their power if they had given a "completely irrational" construction to the contract at issue.

Still others simply ignored the Supreme Court. Without citing any of the pertinent Supreme Court authority, the court in *Campbell v. Farmers Insurance Exchange*<sup>89</sup> reverted to the ob-

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84. *Id.* at 835-36, 33 Cal. Rptr. at 537.

85. *Id.* at 834, 33 Cal. Rptr. at 536.

86. 270 Cal. App. 2d 58, 75 Cal. Rptr. 415 (1969).

87. *Id.* at 60-62, 75 Cal. Rptr. at 417. Numerous other decisions reiterated that, in the absence of a clause limiting an arbitrator's power, an arbitral award is not subject to review for errors of fact or law. See *Golden State Lines v. Fox*, 232 Cal. App. 2d 135, 412 Cal. Rptr. 568 (1965); *Olivera v. Modiano-Schneider*, 205 Cal. App. 2d 9, 23 Cal. Rptr. 30 (1962); *B.S.B. Constr. Co. v. Rex Constr. Co.*, 200 Cal. App. 2d 327, 19 Cal. Rptr. 167 (1962); *Goosen v. Adair*, 185 Cal. App. 2d 810, 8 Cal. Rptr. 855 (1960); *Case v. Alperson*, 181 Cal. App. 2d 757, 5 Cal. Rptr. 535 (1960); *Lauria v. Soriano*, 180 Cal. App. 2d 163, 4 Cal. Rptr. 328 (1960); *Ulene v. Millman*, 175 Cal. App. 2d 655, 346 P.2d 494 (1959); *Harris v. Havenar*, 169 Cal. App. 2d 531, 337 P.2d 832 (1959); *Strauss v. North Hollywood Hosp., Inc.*, 150 Cal. App. 2d 306, 309 P.2d 541 (1957); *Gerard v. Salter*, 146 Cal. App. 2d 840, 304 P.2d 237 (1956); *Cecil v. Bank of America*, 142 Cal. App. 2d 249, 298 P.2d 24 (1956).

88. 271 Cal. App. 2d 675, 699-702, 77 Cal. Rptr. 100, 115-118 (1969).

89. 260 Cal. App. 2d 105, 67 Cal. Rptr. 175 (1968).

solete notion that an award will be vacated for an error of law which "appears on the face of the award and causes substantial injustice."<sup>90</sup>

The court in *Allen v. Interinsurance Exchange*<sup>91</sup> injected a new issue by construing section 11580.2 of the Insurance Code, which provides for arbitration of uninsured motorist claims, to require that arbitrators abide by external law in deciding such claims.<sup>92</sup> From this premise, it concluded that the power of arbitrators was limited to applying the law correctly. This gave the *Allen* court license to review the arbitral award under Code of Civil Procedure section 1286.2, subdivision (d) and to vacate it as in excess of the arbitrator's power when it concluded that the arbitrator had erred in applying the law of contributory negligence.<sup>93</sup>

The fun really began with *Allen*. Cases like *State Farm Mut. Auto. Ins. Co. v. Guleserian*<sup>94</sup> and *Lindholm v. Galvin*<sup>95</sup> remained faithful to the *Sapp* line.<sup>96</sup> The *Guleserian* court went so far as to say that an award could not be vacated for an error of law "no matter how gross."<sup>97</sup> Another court observed that:

when parties opt for the forum of arbitration they agree to be bound by the decision of that forum knowing that arbitrators, like judges, are fallible.<sup>98</sup>

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90. *Id.* at 111-112, 67 Cal. Rptr. at 179.

91. 275 Cal. App. 2d 636, 80 Cal. Rptr. 247 (1969).

92. *Id.* at 640, 641, 80 Cal. Rptr. at 249, 250.

93. *Id.* at 640, 80 Cal. Rptr. at 250. The purity of the court's holding was diluted by the facts that the arbitrator acknowledged the error and the error appeared on the face of the award and also by the court's characterization of the error as "gross." *Id.*

94. 28 Cal. App. 3d 397, 104 Cal. Rptr. 683 (1972). The *Guleserian* court labored to distinguish *Allen* as based upon the proposition that, "to prevent injustice," an arbitrator has the power to correct error in his own award "within a reasonable but very short period." *Id.* at 403, 104 Cal. Rptr. at 687-688.

95. 95 Cal. App. 3d 443, 157 Cal. Rptr. 167 (1979).

96. See also *Herman Feil, Inc. v. Design Center*, 204 Cal. App. 3d 1406, 251 Cal. Rptr. 895 (1988); *Santa Clara-San Benito Chapter of the Nat. Elec. Contractors Assn., Inc. v. Local No. 332, International Bhd. of Elec. Workers*, 40 Cal. App. 3d 431, 114 Cal. Rptr. 909 (1974) labor grievance award confirmed, citing *Guleserian* and *Bailes*; *Hernandez v. State Farm Ins. Co.*, 272 Cal. App. 2d 255, 77 Cal. Rptr. 196 (1969).

97. *State Farm Mut. Auto. Ins. Co. v. Guleserian*, 28 Cal. App. 3d 397, 402, 104 Cal. Rptr. 683, 687 (1972).

98. *That Way Prod. Co. v. Directors Guild, Inc.*, 96 Cal. App. 3d 960, 965, 158 Cal. Rptr. 474, 477 (1979). The *That Way Prod. Co.* court ducked the *Bailes-Abbott* split by concluding that no error appeared on the face of the award before it. *Id.* at 965-66, 158

On the other hand, in *Abbott v. California State Auto. Ins.*,<sup>99</sup> the court reached the same conclusion as in *Campbell*. The rationale of the *Abbott* court was similar to that in *Allen* — an error of law on the face of the award exceeded the power of the arbitrator within the meaning of section 1286.2, subdivision (d).<sup>100</sup> The standard used by *Abbott* and *Campbell* in reviewing awards in uninsured motorist cases was later also applied to the review of awards in a real estate development joint venture,<sup>101</sup> a construction case<sup>102</sup> and a labor grievance arbitration.<sup>103</sup> Other courts reverted to the “completely irrational” standard of the *Lesser Towers* case.<sup>104</sup> In one instance, different panels in the same district even differed over the extent to which arbitral awards are subject to review for legal error. One case cited *Sapp* in upholding an award, while the other vacated an award for error on its face.<sup>105</sup>

Some courts seemed to feel that one way out of the dilemma between the two lines of cases was to say that it was not necessary to choose between them because, upon review, no error was found in the award.<sup>106</sup> At least two courts covered all the bases. In reversing the vacatur of a labor grievance award and confirming a medical malpractice award, respectively, these decisions

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Cal. Rptr. at 477-478. The court also noted that it was more restricted in reviewing a collective bargaining agreement award than otherwise. *Id.* at 966, 158 Cal. Rptr. at 478.

99. 68 Cal. App. 3d 763, 137 Cal. Rptr. 580 (1977).

100. *Id.* at 770-771, 137 Cal. Rptr. at 584.

101. *Hirsch v. Ensign*, 122 Cal. App. 3d 521, 176 Cal. Rptr. 17 (1981).

102. *Ray Wilson Co. v. Anaheim Memorial Hosp.*, 166 Cal. App. 3d 1081, 213 Cal. Rptr. 62 (1985). The court here said that, in the absence of an error of law on its face, the award would be vacated only if it was “completely irrational.” *Id.* at 1091, 213 Cal. Rptr. at 68.

103. *National Football League Players' Assn. v. National Football League Management Council*, 188 Cal. App. 3d 192, 233 Cal. Rptr. 147 (1986).

104. *Manatt, Phelps, Rothenberg & Tunney v. Lawrence*, 151 Cal. App. 3d 1165, 1171, 199 Cal. Rptr. 246, 249 (1984); *Jones v. Kvistad*, 19 Cal. App. 3d 836, 843, 97 Cal. Rptr. 100, 105 (1971).

105. *Compare Nogueiro v. Kaiser Found. Hosp.*, 203 Cal. App. 3d 1192, 250 Cal. Rptr. 478 (1988) (medical malpractice award which was ambiguous in that it may or may not have erroneously failed to apply MICRA limit on non-economic losses upheld, citing *Sapp* and others) with *National Football League Players' Assn. v. National Football League Management Council*, 188 Cal. App. 3d 192, 233 Cal. Rptr. 147 (1986) (award vacated because of substantial injustice resulting from apparent failure of arbitrators to apply mitigation of damage doctrine).

106. See *Park Plaza, Ltd. v. Pietz*, 193 Cal. App. 3d 1414, 239 Cal. Rptr. 51 (1987); *National Auto. & Cas. Ins. Co. v. Superior Court*, 184 Cal. App. 3d 948, 229 Cal. Rptr. 366 (1986).

observed first that arbitrators are not required to follow the law.<sup>107</sup> Then they stated that, if arbitrators are bound by the law, their award was nevertheless to be approved if it was not, in the words of the *Lesser Towers* case, completely irrational.<sup>108</sup> Finally, the courts concluded that, in the awards before them, the arbitrators were correct in their legal analysis.<sup>109</sup>

In one of the most recent decisions, the court in *Cobler v. Stanley, Barber, Southard, Brown & Assoc.*,<sup>110</sup> strained to find that the arbitrator's power was limited to deciding breach of contract issues<sup>111</sup> and then vacated that part of an award which awarded emotional distress damages as contrary on its face to the law in a breach of contract case and, therefore, beyond the power of the arbitrator.<sup>112</sup>

### c. The PG&E Standard of Review

As stated above, the *PG&E* court recognized the lack of logic in drawing any distinction between an error which appeared on the face of an award and one which did not. Either an arbitral award should be reviewable for errors of law or it should not.

One might argue that attempting to review awards for errors of law that do not appear on their faces would raise potentially difficult problems of proof. Granted. A party who wants to attack an award will not, for example, be able to use an arbitrator's testimony to establish a point that does not appear in the award itself.<sup>113</sup> However, other sources of proof will be available,

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107. *Hacienda Hotel v. Culinary Workers Union, Local 814*, 75 Cal. App. 3d 1127, 223 Cal. Rptr. 305 (1985); *Woodard v. Southern Cal. Permanente Medical Group*, 171 Cal. App. 3d 656, 217 Cal. Rptr. 514 (1985).

108. *Id.*

109. *Id.*

110. 217 Cal. App. 3d 518, 265 Cal. Rptr. 868 (1990).

111. The *Cobler* court relied upon a clause which provided for arbitration of any dispute "arising from" this agreement as being narrower than one which provides for arbitration of any dispute "arising out of or related to" an agreement. 217 Cal. App. 3d at 530, 265 Cal. Rptr. at 875.

112. *Id.* at 532-533, 265 Cal. Rptr. at 876-877. The court cited *Sapp* in support of its power to confirm the award in part and vacate it in part, *see id.* at 530, 265 Cal. Rptr. 875, but ignored *Sapp's* broader teaching.

113. Evidence Code section 703.5 provides that an arbitrator is not competent to give any such testimony.

such as a comparison of the award with a transcript, if one is made, or with arguments made by the parties in their arbitral briefs. The problems of proof simply suggest that, as framed, a rule permitting review of arbitral awards for error of law, but only when error appears on the face of the award, not only ignores Supreme Court authority, but subordinates justice to judicial convenience.

The *PG&E* court purported to do away with the distinction. "Ordinarily," the court said, an arbitral award should not be subject to review for errors of law, regardless of whether the alleged error appears on the face of the award or not.<sup>114</sup> However, it could not resist the temptation to retain some power of review over arbitral awards other than that granted by Code of Civil Procedure section 1286.2. Thus, it said that an award would be subject to review if arbitrators made:

such an egregious mistake that it amounts to an arbitrary remaking of the contract between the parties.<sup>115</sup>

One wonders why the *PG&E* court expounded to the extent it did to reach this limited conclusion. It appears merely to revise the vocabulary used by previous courts without altering in any substantive way the willingness to review awards for error of law. Indeed, the *PG&E* court itself acknowledged the similarity of its formulation to that of courts which were willing to review "utterly irrational" legal conclusions.<sup>116</sup>

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114. *PG&E v. Superior Court*, *supra*, 227 Cal. App. 3d at 83, 277 Cal. Rptr. at 713.

115. *Id.* at 84, 277 Cal. Rptr. at 714. Although the *PG&E* court was dealing with a contract interpretation dispute, its "egregious mistake" standard would logically have equal application to a tort or statutory claim.

116. *Id.*, 277 Cal. Rptr. at 714. Instead of even mentioning *Sapp* or *Grunwald-Marx, Inc.*, the *PG&E* court drew upon a passing observation in *Posner v. Grunwald-Marx, Inc.*, 56 Cal. 2d 169, 14 Cal. Rptr. 297, 363 P.2d 313 (1961), a labor grievance case involving the same parties as the earlier *Grunwald-Marx* decision. The *Posner* case arose out of a petition to compel arbitration and did not involve review of an award. Although the Court said it was not going to adopt the then freshly decided *Steelworkers Trilogy* in all respects, its indication that it would not allow an arbitrator to arbitrarily remake a collective bargaining agreement nevertheless tracked the opinion of the United States Supreme Court in the third of these three cases. See *United Steelworkers v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 597 (1960) (award must draw its "essence" from the agreement and will be set aside only when the "words manifest an infidelity to this obligation"). Because they normally take place in the course of an ongoing collective bargaining relationship, labor grievance arbitrations involve special concerns that the arbitrator not stray from the contract. Indeed, collective bargaining agreement arbitration clauses frequently contain language to the effect that an arbitrator's power is limited to

## d. The Proposed Standard

If a court is going to start down the road of the *PG&E* case, why not go all the way? Assuming that *Sapp*, *Griffith* and *Grunwald-Marx* are still good law, and, as set forth above, there is no reason to suppose they are not, then there is similarly no reason not to carry the logic of the *PG&E* case to its ultimate conclusion. If an arbitration provision is truly the product of agreement between parties of relatively equal bargaining power, and if the parties have not reserved points of law for judicial review, why not conclude that they were prepared to accept the arbitral decision as final—right, wrong or indifferent, even if it flouts the law as understood by the disappointed arbitrator?<sup>117</sup>

After all, if parties to consensual arbitration agreements are unwilling to accept decisions of law as final, they first of all do not have to agree to arbitrate. If they do accept arbitration, they have virtually complete control over the structure of the process. They can specify, if they desire, such matters as the number and qualification of arbitrators, the time and place of hearing, the availability of pre-hearing discovery, the applicability of rules of

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interpretation and application of the contract and that the arbitrator may not add to the contract or modify any of its provisions. See, e.g., *W.R. Grace & Co. v. Local No. 759, Int'l Union of United Rubber Workers*, 461 U.S. 757, 763 n.4 (1983). Except when commerce is not involved, as in *Posner*, labor grievance arbitration awards are governed by Section 301 of the Labor Management Relations Act, not by the state or federal arbitration statutes. See cases cited in note 20, *supra*. Although commercial arbitration precedents may be helpful in dealing with labor grievance arbitration awards, *United Paperworkers Int'l Union v. Misco, Inc.*, 484 U.S. 29, 40 n.9 (1987), the collective bargaining situation is unique. See *Dryer v. Los Angeles Rams*, 40 Cal. 3d 406, 415 n.9, 220 Cal. Rptr. 807, 813 n.9, 709 P.2d 826, 832 n.9 (1985).

117. Although it failed to follow its own logic, the *PG&E* court at least recognized that:

if the disputed issue of law has actually arisen, the positions of the disputants are staked out, the consent to arbitration is then given with no reservation of a right to judicial review, and the arbitrator accepts the legal position of one side, the loser has no fair complaint, regardless of how egregious the error of law.

227 Cal. at 83, 277 Cal. Rptr. at 713. Why should it make any difference whether the arbitration agreement covers an existing dispute or future disputes? Parties invariably must accept or allocate the risk of future changes in the law as applied by the courts, as well as unexpected disputes, whenever they enter into any agreement. They can take the same possibilities into account in judging whether to select arbitration as a dispute resolution mode and how to structure the arbitral process, including whether to forego any right to judicial review.



evidence at hearings, the standard of decision of arbitrators, the manner of expression of the decision of arbitrators in their award and, of course, whether errors of law are to be reserved for judicial review. Parties have another opportunity to guard against a "runaway" arbitrator when they exercise their power to select arbitrators. Why give them still a further bite at the apple? If the legislature really believes that arbitration is an acceptable alternative to litigation, when freely consented to and conducted by a fair process, who are the courts to sit in judgment on the outcome, no matter how repugnant it may be to the persona of the judge or judges to whom complaint of error is made? Isn't this simply an anachronous remnant of the historical hostility of courts to arbitration?<sup>118</sup>

Apart from the difficulty of applying the *PG&E* standard to a particular case, the problem it poses is that, depending on whether an award is being attacked or defended, it may afford an arbitrant continued hope or concern that, if a court can be persuaded that the award is sufficiently wide of the court's mark on the law, it will be subject to vacatur. This in turn may lead to wasteful expenditure of litigating resources.

The fact of the matter is that, regardless of the standard articulated, the efforts of disappointed arbitants to overturn awards on the basis of grounds other than those specified in Code of Civil Procedure section 1286.2 are generally fruitless. Courts which review for error of law on the face of an award and also courts which review for a completely irrational award or, as

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118. To be effective in refraining from review of arbitration awards for errors of law, courts must also resist the temptation to manipulate the scope of the submission so as to limit the arbitrator's power to decide an issue with which they disagree. In *Cobler v. Stanley, Barber, Southard, Brown & Assoc.*, 217 Cal. App. 3d 518, 265 Cal. Rptr. 868 (1990), for example, the court acknowledged that a clause which provided for arbitration of any dispute "arising from or related to" the contract would have covered claims for fraud or emotional distress, but relied on the phrase "arising from" alone to preclude the arbitrator from considering such claims and thus vacated an award of damages for emotional distress. *Id.* at 530-531, 265 Cal. Rptr. at 875-876. For a case in which the court avoided review by interpreting an arbitration clause broadly, see *Taylor v. Crane*, 24 Cal. 3d 442, 155 Cal. Rptr. 695, 595 P.2d 129 (1979). Courts must similarly refrain from relying on an error of law as evidencing bias or misconduct on the part of an arbitrator, as the court did in *San Martini Compania de Navegacion, S.A. v. Saguenay Terminals Ltd.*, 293 F.2d 796, 801 (9th Cir. 1961). In short, no matter how tempting it may be to remedy a perceived injustice resulting from application of a rule of decision at odds with what the court would apply to the same dispute, a court should stay its hand.

in the *PG&E* case, egregious error typically find none.<sup>119</sup>

### 3. *Possible Exceptions to Non-Reviewability*

Should there be any exceptions to a rule which calls for courts not to review arbitral awards for errors of law, even if they appear on the face of the award and are flagrant?

One possibility was recognized by the *PG&E* court itself — that of awards made in disputes arising out of contracts of adhesion. Another involves cases where the dispute is not submitted to arbitration voluntarily, but instead because of a statutory mandate. Still another includes disputes in which statutory claims are asserted.

#### a. *Contracts of Adhesion*

Just because an arbitration claim is contained in a contract of adhesion does not necessarily mean that it will be denied enforcement under California law.<sup>120</sup> To the contrary, in the absence of some “special element of unfair advantage,” an arbitration agreement in an adhesion contract will be enforced.<sup>121</sup> In other words, if the arbitration provision contract of adhesion is regarded as fair, it will be enforced as if it were the product of negotiated agreement.

The question arises whether the product of the arbitration process should be evaluated any differently when the process is embedded by one party in a contract of adhesion instead of resulting from the participation of both parties.

The *PG&E* court asserted that, if an adhesive arbitration

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119. The number of post-*Sapp* non-labor grievance cases in which awards have actually be vacated or remained vacated, after consideration on appeal of claimed errors of law, may be as few as five. See *Cobler v. Stanley, Barber, Southard, Brown & Assoc.*, 217 Cal. App. 3d 518, 265 Cal. Rptr. 868 (1990); *Abbott v. California State Auto. Assn.*, 68 Cal. App. 3d 763, 137 Cal. Rptr. 580 (1977); *Allen v. Interinsurance Exch.*, 275 Cal. App. 2d 636, 80 Cal. Rptr. 247 (1969); *Pacific Auto Ins. Co. v. Lang*, 265 Cal. App. 2d 837, 71 Cal. Rptr. 637 (1968); *Drake v. Stein*, 116 Cal. App. 2d 779, 254 P.2d 613 (1953).

120. *Keating v. Superior Court*, 31 Cal. 3d 584, 595, 183 Cal. Rptr. 360, 366, 645 P.2d 1192, 1198 (1982); *Graham v. Scissor-Tail, Inc.*, 28 Cal. 3d 807, 819-820, 171 Cal. Rptr. 604, 611-612, 623 P.2d 165, 172-173 (1981).

121. See *Keating v. Superior Court*, *supra*, 31 Cal. 3d at 595, 183 Cal. Rptr. at 366, 645 p. 2d at 1198.

clause is not invalidated, "then the consequences that attend arbitration, including the limited scope of review provided by law, should obtain."<sup>122</sup>

The *PG&E* court advanced two reasons for its conclusion. One was that a more rigorous standard of review would supposedly give an unfair advantage to the adhering party. It could seek review of an unfavorable award; the adhesive party could not. The second was that the benefits to society from arbitral finality would be undercut.<sup>123</sup>

The first of these arguments was made without support. Even if judicial review for errors of law were made available only to the adhering party, the court did not offer any reason why that would give the adhering party an "unfair" advantage. After all, it is the adhering party which is compelled to arbitrate without even an opportunity to participate in designing the arbitral process.

The second argument presupposes an absolute interest in the finality of arbitrations. In actuality, by providing grounds for vacatur, *i.e.*, review of arbitral awards,<sup>124</sup> the legislature has evidenced only a limited societal preference for immunizing arbitral awards from judicial review, and this only when parties to a dispute do not reserve a right of review.<sup>125</sup> The fact that society's interest in the finality of arbitral awards is limited gives rise to the next question, which is whether, in any particular case, this interest outweighs the interest of the disputants in quality of outcome.

The real issue is whether judicial review and approval of the process as fair is the functional equivalent of or an adequate surrogate for freely bargained-for consent. There are, of course, ob-

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122. 227 Cal. App. 3d at 89, 277 Cal. Rptr. at 717. The court held that either the contract was not adhesive or that any claim based on its being adhesive had been waived. *See id.* at 86-87, 277 Cal. Rptr. at 715.

123. *Id.* at 89, 277 Cal. Rptr. at 717.

124. See CAL. CODE CIV. PROC. § 1286.2 (West 1982).

125. Courts have expressed more interest in the finality of a judgment resulting from confirmation of an arbitral award than in the finality of the award itself. *See Rios v. Allstate Ins. Co.*, 68 Cal. App. 3d 811, 137 Cal. Rptr. 441 (1977) (doctrine of finality of judgments barred subsequent suit based on allegedly fraudulent presentation to arbitrator; plaintiff should have raised issues in petition to vacate award).

vious differences. Parties who bargain over an arbitration agreement have the opportunity to tailor such matters as the number and qualifications of arbitrators, the scope of the agreement, the place of the arbitration, and the arbitral procedure to their specific needs. A fairness determination is rather more "quick and dirty." It is limited to whether the parties will have an opportunity to be heard before a tribunal that is reasonably impartial.

Are these differences enough to lead to a different standard of review? Arguably they are. The Supreme Court has recognized that the policy in favor of letting arbitrants govern their own destiny is stronger when:

parties of presumptively equal bargaining power have entered into an agreement containing a commitment to arbitrate by a procedure of unchallenged fairness.<sup>126</sup>

than when an arbitration clause is part of a contract of adhesion.<sup>127</sup>

It is not unreasonable to suppose that provisions for arbitration may be included in contracts of adhesion, not only to save litigating time and expense and gain privacy, but also with a view to obtaining outcomes that are more favorable to adhesive parties than in litigation. Adhesive institutions may expect, for example, that even though arbitrators qualify as impartial and their efforts are unstained by misconduct, their views of the law will be more harmonious with those of adhesive institutions than the views of courts might be.<sup>128</sup> This line of analysis suggests that courts should review the law applied in adhesive arbitrations.

The obvious occasion for doing so is when a party objects to an award. The current combination of calendar pressure on courts and presumption in favor of enforcement of arbitration agreements makes it unlikely that objections to going forward

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126. *Erickson, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street*, 35 Cal. 3d 312, 322, 197 Cal. Rptr. 581, 587, 673 P.2d 251, 257 (1983).

127. *Id.* at 322 n.7, 197 Cal. Rptr. at 587 n.7, 673 P.2d at 257 n.7.

128. The author is aware of concern among members of the plaintiffs' personal injury bar, for example, that, as a practical matter, those who defend medical malpractice arbitrations have better access to arbitrator information than plaintiffs' counsel and, thus, are able to propose arbitrators who are intuitively defense inclined.

with arbitration is pursuant to an adhesive agreement will receive only cursory treatment. Although the usual presumption in favor of validity poses the same obstacle to an attack on the resulting award, courts at the post award stage will be faced with a smaller universe of disputes to consider — in most cases, the parties will have settled or accepted the award — and the fact that an award is final, whereas a referral to arbitration is preliminary, gives more reason for deliberate consideration.<sup>129</sup>

## b. Arbitrations Mandated by Statute

A more difficult class of cases are those in which arbitration is effectively mandated by statute, such as disputes over uninsured motorist claims,<sup>130</sup> or at least preferred, such as in medical

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129. Legislative concern about the adhesive nature of form real estate contracts and medical service contracts has prompted the enactment of statutes regulating certain aspects of the form of such agreements. See CAL. CODE CIV. PROC. §§ 1295, 1298 (West 1982); CAL. HEALTH & SAFETY CODE § 1363. Contracts between consumers and health care providers or health care service plans may or not be regarded as adhesive depending on the circumstances of their formation. Compare *Madden v. Kaiser Foundation Hosps.*, 17 Cal. 3d 699, 710-711, 131 Cal. Rptr. 882, 889, 552 P.2d 1178, 1185 (1976) (not adhesion contract because health care service plan was negotiated by representative entity which could bargain effectively on behalf of the covered individuals), with *Beynon v. Garden Grove Medical Group*, 108 Cal. App. 3d 698, 706, 707, 161 Cal. Rptr. 146, 150-151 (1980) (adhesion contract when no showing that health care service plan was bargained for by powerful representative). Even in *Madden*, the contract was said to have "some adhesive characteristics." 17 Cal. 3d, *supra*, at 710, 131 Cal. Rptr. at 889, 552 P.2d at 1185.

130. Section 11580.2 of the Insurance Code (a) requires that any policy of automobile bodily injury liability insurance offer uninsured motorist coverage which (b) provides for arbitration of any dispute between the carrier and an insured over what the insured is "legally entitled" to recover from an uninsured motorist.

Arbitration is commanded by statute in several other categories of disputes in California. One involves construction contract claims against state agencies. CAL. PUB. CONTR. CODE §§ 10240 et seq. (West 1985). Another is any dispute between an insurance carrier and an insured over fees to be paid to the insured's lawyer as so-called "cumis counsel" for defending a case when the carrier is paying for the defense under a reservation of rights. CAL. CIVIL CODE § 2860 (West 1985). Still another is attorney client fee dispute arbitrations. CAL. BUS. & PROF. CODE §§ 6200 et seq. (West 1987). In addition, suits against local public agencies on construction contract claims involving \$375,000 or less must be referred to judicial arbitration. CAL. PUB. CONTR. CODE § 20104.4, subdivision (b) (West 1985).

Except for disputes governed by section 2860 of the Civil Code, the provisions of these statutory schemes regulate the arbitrations involved so as to vitiate the need for any court-devised standard of review. Section 10240.12 of the Public Contracts Code, for example, provides expressly for a court to vacate an award if not decided in accordance with the laws of California. Fee disputes must be submitted to arbitration by a lawyer at the instance of the client, but the client is not obliged to submit to arbitration. See CAL. BUS. & PROF. CODE § 6201 (West 1987). This arrangement is to compensate for the "dis-

malpractice claims.<sup>131</sup>

Uninsured motorist arbitrations probably have accounted for more arbitration decisions by California courts than any other single category of cases.<sup>132</sup> Arbitration in cases like these is neither the product of negotiated agreement between two parties of relatively equal bargaining power nor imposed by one party upon another, except to the extent insurance carriers may have had more influence with the legislature than insureds. Both sides are bound to the provisions of the statutes.

As discussed above, an early decision held that an arbitrator's power in an uninsured motorist case is limited to deciding the claim according to governing law.<sup>133</sup> Other decisions have been flawed by the "error on the face of the award" fallacy. Assuming that the same standard of review should be followed regardless of whether the alleged error appears on the face of an award or not, the question is whether the statutory mandate, like a fairness review in the case of an adhesion contract, should stand as a surrogate for a truly bargained agreement. The sheer volume of uninsured motorist claims and the relatively small

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parity in bargaining power" in favor of the lawyer on fee matters. See *Manatt, Phelps, Rothenberg & Tunney v. Lawrence*, 151 Cal. App. 3d 1165, 1174, 199 Cal. Rptr. 246, 252 (1984). A lawyer and client may agree that any arbitration be binding. See CAL. BUS. & PROF. CODE § 6204 (West 1987). In the absence of such agreement, however, either party who is dissatisfied by an award has the option of having a trial *de novo*. See *id.*

131. Section 1295 of the Code of Civil Procedure has been seen as encouraging the use of arbitration to resolve medical malpractice disputes. See *Victoria v. Superior Court*, 40 Cal. 3d 734, 744-45, 222 Cal. Rptr. 1, 7, 710 P.2d 833, 839 (1985). However, to the extent that arbitration of medical malpractice claims is the product of an adhesion contract, there is little basis for distinguishing between the standard of judicial review of the resulting award for errors of law and the standard of review in any other case arising out of a contract of adhesion.

132. Uninsured motorist arbitrations have troubled the courts. Former Supreme Court Justice Joseph Grodin, who was then on the Court of Appeal, suggested after *Abbott* that uninsured motorist cases might present a unique situation because the arbitration clause in uninsured motorist coverage "is the product of a statutory requirement rather than voluntary agreement." *Rodriguez v. Keller*, 113 Cal. App. 3d 838, 843 n.3, 170 Cal. Rptr. 349, 352 n.3 (1980). Another court, which followed *Sapp* in a partnership dissolution case, suggested that application of the error-on-the-face-of-the-award standard was limited to uninsured motorist cases. See *Rodriguez v. Keller*, 113 Cal. App. 3d 838, 843 n.3, 170 Cal. Rptr. 349, 352 n.3 (1980). On the other hand, still another court has expressed concern over what it saw as a tendency to review uninsured motorist awards more closely than others. See *Felner v. Meritplan Ins. Co.*, 6 Cal. App. 3d 540, 546 n.1, 86 Cal. Rptr. 178, 181-182 n.1 (1970).

133. See *Allen v. Interinsurance Exch.*, 275 Cal. App. 2d 636, 80 Cal. Rptr. 247 (1969).

amounts involved suggest a greater willingness to accept whole-sale justice in these cases than in adhesion contract claims and, thus, to forego judicial review for errors of law.

So far as medical malpractice claims are concerned, although it is dangerous to speculate on the cause of something the legislature did not do, its failure to provide pro or con in Code of Civil Procedure section 1295 for judicial review of errors of law may leave room for an inference of intent to leave such awards subject to review according to the case law.<sup>134</sup>

### c. Statutory Claims

Two issues are raised by arbitration agreements which purport to cover statutory claims. One is whether the agreement will be effective to preclude an aggrieved party from suing to enforce a claim based on whatever statute is involved. The other is whether to apply any different standard of review to the awards in such cases than in others.

California courts have displayed a continuing hostility to any waiver by arbitration agreement of the right to pursue a statutory claim in court. When California courts have thought that the Federal Act was not applicable and that enforceability of an arbitration agreement was governed instead by the law of the state, they have not hesitated to conclude that a party cannot be foreclosed from access to the courts to pursue a statutory claim.<sup>135</sup> The California Supreme Court has ruled that a plaintiff was not bound to arbitrate a state statutory claim even when it acknowledged that the Federal Act governed enforcement of the applicable agreement to arbitrate.<sup>136</sup> At least one court has been

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134. See notes 129, 131 *supra*.

135. See *Ware v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 24 Cal. App. 3d 35, 43-45, 100 Cal. Rptr. 791, 797-798 (1972), *affirmed*, 414 U.S. 117 (1973) (Labor Code Section 229 wage claim); *Bos Material Handling, Inc. v. Crown Controls Corp.*, 137 Cal. App. 3d 99, 111, 186 Cal. Rptr. 740, 746 (1982) (Cartwright Act claim). The potentially preemptive effect of the Federal Act was not put at issue in *Ware*. When the Federal Act was interposed in a Labor Code section 229 case, the employer's right to arbitration was enforced, preempting the state law right of access. See *Perry v. Thomas*, 482 U.S. 483 (1987).

136. See *Keating v. Superior Court*, 31 Cal. 3d 584, 592-93, 594-604, 183 Cal. Rptr. 360, 364, 645 P.2d 1192, 1196 (1982) (Franchise Investment Act claim). The party seeking arbitration in the *Keating* case was successful in obtaining review by the United

persuaded by the argument that statutory violations should not be insulated from judicial scrutiny by arbitration provisions in adhesive contracts.<sup>137</sup>

In earlier decisions, the United States Supreme Court also displayed a preference for judicial action over arbitration for the enforcement of statutory claims.<sup>138</sup> However, the Federal Act tide has more recently turned in favor of enforcing all-encompassing arbitration clauses as against claims of right to pursue statutory complaints in court.

The new direction was indicated initially in the 1974 case of *Scherk v. Alberto-Culver Co.*,<sup>139</sup> in which the Court enforced an arbitration agreement because it arose out of a transnational transaction, even though the party resisting arbitration sought to pursue an implied right of action under section 10, subdivision (b) of the Securities Exchange Act of 1934.<sup>140</sup> The Court characterized an agreement to arbitrate as a "specialized kind of forum-selection clause." Earlier, in *The Bremen v. Zapata Off-Shore Co.*,<sup>141</sup> it had held that a "freely negotiated" forum selection clause, "unaffected by fraud, undue influence or overweening bargaining power" should be "given full effect."<sup>142</sup>

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States Supreme Court and reversal on the ground that, contrary to the California Supreme Court decision, the broad right to enforcement of arbitration agreements under the Federal Act preempted state efforts to preserve access to the courts for particular claims, including, as in the *Keating* case, claims for violation of California's Franchise Investment Act. See *Southland Corp. v. Keating*, 465 U.S. 1 (1984). The Franchise Relations Act, CAL. BUS. & PROF. CODE §§ 20000 et seq. (West 1987), which became effective on January 1, 1981, after the time of the operative facts in *Keating*, expressly permits franchisors and franchisees to agree to arbitration of disputes between them. *Id.* § 20040.

137. See *Bos Material Handling, Inc.*, *supra*, 137 Cal. App. 3d at 110, 186 Cal. Rptr. at 746.

138. See *Wilco v. Swan*, 346 U.S. 427 (1953); *Alexander v. Gardner-Denver Co.*, 415 U.S. 36 (1974).

139. 417 U.S. 506 (1974).

140. 417 U.S. at 519. The Court in *Scherk* accepted the premise that *Wilco v. Swan*, 346 U.S. 427 (1953), which held that an agreement to arbitrate future disputes under the Securities Act of 1933, would have barred enforcement of the arbitration agreement in a domestic setting. 417 U.S. at 515. However, it foreshadowed its decision in *Shearson/American Express Inc. v. McMahon*, as to which see page 80, *infra*, by stating that the considerations which led to the decision in *Wilco* did not necessarily also apply to a 1934 Act claim. 417 U.S. at 515-516.

141. 407 U.S. 1 (1972).

142. *Id.* at 12-13.



*Scherk* was followed by *Southland Corp. v. Keating*,<sup>143</sup> in which the Court relied upon the supremacy clause to uphold an attempt to compel arbitration of a state statutory claim.

*Keating* in turn was followed by *Mitsubishi Motors v. Soler-Chrysler Plymouth, Inc.*,<sup>144</sup> in which a federal antitrust claim was sent to arbitration under an arbitration provision in a transnational agreement.

The tide came to flood in *Shearson/American Express Inc. v. McMahon*,<sup>145</sup> and *Rodriguez de Quijas v. Shearson/American Express Inc.*,<sup>146</sup> both of which compelled arbitration of domestic disputes involving federal securities law claims. The first of these decisions distinguished *Wilko v. Swan*,<sup>147</sup> which in 1953 had barred waiver of a judicial forum because arbitration was inadequate to protect the substantive rights at issue. The second flat out overruled *Wilko*.<sup>148</sup>

Whether California courts will be influenced to recede from their historical position by the practical factor of calendar pressures and the reasoning of the recent United States Supreme Court cases remains to be seen.

Assuming arbitration of a statutory claim, however, what about judicial review of whether the resulting award applied the law correctly?

We have clear hints of what the United States Supreme Court would do. For example, in *Scherk*, the Court said that,

143. 465 U.S. 1 (1984).

144. 473 U.S. 614 (1985).

145. 482 U.S. 220 (1987).

146. 490 U.S. 477 (1989).

147. 346 U.S. 427 (1953).

148. Overruling *Wilko v. Swan* does not necessarily mean that the United States Supreme Court will uphold arbitration of all statutory claims. In other cases it has concluded that Congress intended judicial enforcement of statutory rights and that "arbitration could not provide an adequate substitute for judicial proceedings." *McDonald v. City of West Branch*, 466 U.S. 284, 289 (1984) (civil rights claim under 42 U.S.C. § 1983); see also *Barrattine v. Arkansas-Best Freight System*, 450 U.S. 728 (1981) (FLSA claim); *Alexander v. Gardner-Denver Co.*, 450 U.S. 728 (1981) (Title 7 claim). *Gardner-Denver* is the best candidate among these for overruling, because the dispute arose in a union setting. In a similar case, the Supreme Court could regard Title 7 as imported into the collective bargaining agreement by operation of law, such that the arbitrator has the power and duty to decide the claim.

although it did not decide the question, “presumably” the alleged securities fraud could be raised in challenging enforcement of an arbitral award as contrary to public policy.<sup>149</sup>

In addition, in *Mitsubishi Motors*, the Court said that, “by agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute.”<sup>150</sup> It also observed that:

Where the parties have agreed that the arbitral body is to decide a defined set of claims which includes, as in these cases, those arising from the application of American antitrust law, the tribunal therefore should be bound to decide that dispute in accord with the national law giving rise to the claim.<sup>151</sup>

And that:

Having permitted the arbitration to go forward, the national courts of the United States will have the opportunity at the award-enforcement stage to ensure that the legitimate interest in the enforcement of the antitrust laws has been addressed.<sup>152</sup>

The Court implied that an award which erred in deciding Soler’s antitrust claim would be denied enforcement as contrary to public policy.<sup>153</sup>

In *Shearson/American Express, Inc. v. McMahon*, the Court cautioned that “judicial scrutiny of arbitration awards necessarily is limited,”<sup>154</sup> but nevertheless asserted that “such review is sufficient to ensure that arbitrators comply with statutory requirements.”<sup>155</sup>

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149. *Scherk v. Alberto-Culver Co.*, *supra*, 417 U.S. at 519 n.14.

150. *Mitsubishi Motors v. Soler-Chrysler Plymouth, Inc.*, *supra*, 473 U.S. at 628.

151. *Id.* at 636-37.

152. *Id.* at 638.

153. *See id.*

154. 482 U.S. at 232.

155. *Id.* The Court also noted that “the SEC has sufficient statutory authority to ensure that arbitration is adequate to vindicate Exchange Act rights.” *Id.* at 238. However, the SEC does not necessarily agree that the arbitral awards deciding securities law disputes should be subject to review for errors of law. *See* 54 Fed. Reg. 21,144, 21,151 n.45 (1989). Industry representatives seem to believe that arbitrators are free to decide cases without reference to applicable legal standards. *See Arbitration Reform: Hearings*

The United States Supreme Court has not yet been confronted with a claim that arbitrators failed to follow applicable law in deciding a statutory claim. Thus, we do not know whether or not the foregoing hints mean that an award deciding a statutory claim will be subjected to a more rigorous review than otherwise under the Federal Act.

California courts have similarly not yet had occasion to opine on the standard of review of an arbitral award which decides a statutory claim. However, it is difficult to suggest any reason why, if two parties of relatively equal bargaining power negotiate an arbitration agreement which embraces statutory claims and which does not express an intent to reserve errors of law for judicial review, the standard of review should not be the same as in any case not involving a statutory claim. As previously stated, a court should stay its hand.

On the other hand, one of the premises upon which the United States Supreme Court decided *Mitsubishi Motors Corp.*, albeit possibly unrealistic on the facts, was that the parties were of relatively equal bargaining power. The Court went on to state:

Of course, courts should remain attuned to well supported claims that the agreement to arbitrate resulted from the sort of . . . overwhelming economic power that would provide grounds 'for the revocation of any contract.'<sup>156</sup>

The question arises as to whether judicial review of alleged arbitral errors in deciding statutory claims will be any different than otherwise when the parties are not of relatively equal bargaining power, but the disparity is not so great as to justify avoiding the obligation to arbitrate.

This is a subset of the general question of whether to modify the standard of judicial review when an arbitration agreement is not the product of negotiation between parties with relatively equal bargaining power, i.e., consensual, but instead has either resulted from a statutory mandate or been embedded in a

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on H.R. 4960, Subcomm. on Telecommunications and Finance of the House Committee on Energy and Commerce, 85-86, 138, 100th Cong., 2d Sess. (1988).

156. 473 U.S. at 627. See also *id.* at 632.

contract of adhesion. A court should be willing to intervene to protect the statutory rights of the adhering party.

#### 4. *Conclusion*

Courts should, of course, review arbitration awards for errors of law when arbitration agreements provides for such review. Moreover, as in the case of any other agreement, courts should interpret arbitration clauses in light of the parties' intent. As may be seen, however, in the absence of a reserved right of review, California courts have not been consistent in limiting judicial review of arbitral awards to the grounds provided in section 1286.2 of the Code of Civil Procedure. However, sound policy considerations support the Supreme Court decisions which suggest that, at least when parties of relatively equal bargaining strength agree to arbitration, a court should limit any inquiry into the resulting award to the issues of fair process raised by section 1286.2 and should refrain from review of the award for legal error, regardless of how tempting the prospect of judicial revision may be. A different rule permitting review of arbitral awards for errors of law should prevail when arbitration is effectively imposed by one party upon the other, as in adhesion contracts, particularly when the scope of the arbitration agreement encompasses statutory claims.