U.S. Supreme Court Clarifies Scope of Judicial Review Under the Federal Arbitration Act

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On March 25, 2008, the U.S. Supreme Court issued its decision in *Hall Street Associates, L.L.C. v. Mattel, Inc.*, in which the Court ruled, by a six-to-three vote, that the scope of judicial review of arbitral awards is exclusively determined by the Federal Arbitration Act (the “FAA”). The Court’s decision in *Hall Street* resolved an issue that had resulted in a long-standing disagreement among the U.S. Courts of Appeals, namely whether parties could, through their arbitration agreement, “customize” the scope of judicial review applicable to an award rendered pursuant to that agreement. The Court’s decision—although leaving open the issue of “other possible avenues for judicial enforcement of arbitral awards,” including the “manifest disregard of the law” standard—affords parties to arbitration agreements an increased degree of certainty regarding the scope and nature of post-arbitral award judicial review under the FAA. However, *Hall Street* also eliminates a significant measure of contractual flexibility that the majority of federal appellate courts had previously recognized and many parties have adopted in their arbitration agreements. Consequently, parties that have included an expanded or narrowed provision for judicial review of arbitral awards in their agreements that are subject to the FAA should be aware that those provisions are likely to be null and void.

**Background: Judicial Review Under the Federal Arbitration Act**

Congress adopted the FAA in 1925 “to replace judicial indisposition to arbitration with a ‘national policy favoring it and placing arbitration agreements on equal footing with all other contracts.’” Section 2 of the FAA provides that any written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

The Supreme Court has construed Section 2 broadly, and has held that the FAA applies to any arbitration agreement that would be subject to regulation by Congress pursuant to its constitutional power to regulate interstate commerce, even if that agreement involves only local, intrastate transactions.

The FAA provides courts with the statutory tools to enforce arbitration agreements and awards. Specifically, the FAA empowers courts to compel arbitration, to stay litigation in favor of arbitration, and to enforce arbitral awards. With respect to enforcement, Section 9 of the FAA provides, in pertinent part, that a U.S. court must, upon motion of a party, grant an order confirming an arbitral award “unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title.” As the Supreme Court noted in *Hall Street*, Section 9’s command requiring courts to confirm arbitral awards “carries no hint of flexibility,” and “unequivocally tells courts to grant confirmation in all cases, except when one of the ‘prescribed’ exceptions applies.”
The “prescribed exceptions” to enforcement are few. Section 10 of the FAA provides that a court may vacate an arbitral award on the motion of a party where:

- the award was procured by corruption, fraud or undue means;
- there was evident partiality or corruption in the arbitrators;
- the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or
- the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final and definite award upon the subject matter was not made.11

Likewise, Section 11 permits a court to modify or correct an award where:

- there was an evident miscalculation of figures or an evident material mistake in the description of any person, thing or property referred to in the award;
- the arbitrators have awarded upon a matter not submitted to them; or
- the award is imperfect as to form, but in a manner not affecting the merits.12

**Hall Street: Procedural History, Holding and Rationale**

As noted above, Hall Street addressed the question of whether parties may expand the scope of judicial review to permit an arbitral award to be vacated or modified on grounds other than those expressly set forth in Sections 10 and 11.

The Hall Street case began as a leasehold dispute involving property in Oregon. Mattel, the lessee, gave notice of its intent to vacate the property after discovering significant amounts of environmental contamination on the site, and Hall Street sued Mattel for indemnification under the lease for that contamination. In the course of the court proceedings, and after an unsuccessful mediation, the parties decided to submit the indemnification portion of their dispute to arbitration. The arbitration agreement, which the parties drafted and which the district court ultimately entered as an order, contained the following provision:

The United States District Court for the District of Oregon may enter judgment upon any award, either by confirming the award or by vacating, modifying or correcting the award. The Court shall vacate, modify or correct any award: (i) where the arbitrator's findings of fact are not supported by substantial evidence, or (ii) where the arbitrator’s conclusions of law are erroneous.

Mattel prevailed in the initial arbitration, where the arbitrator found that Hall Street was not entitled to indemnification because the lease did not require Mattel to comply with a specific Oregon environmental statute. Hall Street then sought to vacate the award in accordance with the parties’ agreement, arguing that the arbitrator's failure to apply the Oregon environmental statute at issue constituted an error of law. The district court agreed with Hall Street, vacated the award and remanded the case to the arbitrator. Following the arbitrator's new ruling, the parties each sought to modify the award; the district court corrected the arbitrator's interest calculations but otherwise upheld the award.

Both parties then appealed to the U.S. Court of Appeals for the Ninth Circuit. The Ninth Circuit, relying on its 2003 ruling in *Kyocera Corp. v. Prudential-Bache Trade Services*,13 reversed and remanded the matter back to the district court with instructions to confirm the initial award unless one of the grounds for vacatur or modification set forth in Sections 10 or 11 of the FAA were present. Following further proceedings before the district court and a second appeal to the Ninth Circuit,14 the Court granted *certiorari*.

The Supreme Court granted *certiorari* to “decide whether the grounds for vacatur and modification provided by §§ 10 and 11 of the FAA are exclusive.” Prior to the Court’s decision in Hall Street, the courts of appeals had disagreed on this question: The Ninth and Tenth Circuits had held that parties could not contract for expanded judicial review,15 while the First, Third, Fifth and Sixth
Circuits reached the opposite conclusion.16 The Supreme Court adopted the view previously taken by the Ninth and Tenth Circuits, holding that the grounds for vacatur and modification in the FAA are exclusive and that parties entering into arbitration agreements lack the ability under U.S. law to modify, through contract, the scope of judicial review with respect to an arbitral award.

The Court rejected each of Hall Street’s efforts to defend the expanded scope of review contained in its agreement with Mattel. First, the Court rejected Hall Street’s claim that the Court’s 1953 decision in Wilko v. Swan,17 in which the Court implicitly endorsed the notion that arbitral awards could be vacated for “manifest disregard of the law,” supported its contention that the parties could, by agreement, alter the scope of judicial review. The Court rejected this reading of Wilko as overbroad, observing that the Wilko Court, by adopting the “manifest disregard of law” standard, was expressly rejecting “just what Hall Street asks for here, general review for an arbitrator’s legal errors.”18

Second, the Court rejected Hall Street’s contention that expandable judicial review was permissible because “arbitration is a creature of contract, and the FAA is ‘motivated, first and foremost, by a congressional desire to enforce agreements into which parties have entered.’”19 While acknowledging that the FAA permits parties to “tailor some, even many features of arbitration by contract,” the Court nonetheless found that “the FAA has textual features at odds with enforcing a contract to expand judicial review following the arbitration.”20 Specifically, the Court, applying the interpretive doctrine of ejusdem generis,21 held that the grounds for vacatur and modification set forth in Sections 10 and 11 of the FAA were exclusive, and that those provisions could not be viewed as a “default” provision intended to establish the scope of review in the absence of contrary provisions in the parties’ agreement. To further illustrate its point, the Court contrasted the language of Sections 10 and 11 (which do not contemplate the parties’ agreement on the scope of post-award judicial review) with that of Section 5 of the FAA, which, in governing the appointment of arbitrators, includes specific language authorizing the court to appoint arbitrators where the parties have failed to provide in their agreements a permissible method for doing so.22

Significantly, the Court’s opinion added that its holding did “not purport to say that [Sections 10 and 11 of the FAA] exclude more searching review based on authority outside the statute,” and that “[t]he FAA is not the only way into court for parties wanting review of arbitral awards[].”23 Specifically, the Court noted that parties to arbitration agreements “may contemplate enforcement under state statutory or common law, for example, where judicial review of different scope is arguable.”24 The Court remanded the case, and left open the question of whether the district court’s approval of the arbitration agreement at issue might be viewed as “an exercise of the District Court’s authority to manage its cases under Federal Rules of Civil Procedure 16.”25

Implications

Several implications flow from the Court’s ruling in Hall Street. First, arbitral awards rendered pursuant to arbitration agreements governed by the FAA may be subject to vacatur or modification only upon the narrow grounds set forth in Sections 10 or 11, and parties may not expand or contract the scope of those statutory provisions. Similarly, arbitral awards will not be subject to judicial review for mere errors of law or fact, and any arbitration agreements to the contrary that are governed by the FAA will be null and void.

Second, although the Court’s holding promotes the fundamental federal policy that seeks to ensure that arbitral awards will be enforced without significant post-arbitral litigation, parties that are contemplating arbitration that may raise novel, complex or technical legal issues should be forewarned that the arbitrator’s decision on a dispute is likely to be the last word, and that they will almost certainly be required to accept arbitral decisions even if they are legally erroneous. Parties should, therefore, carefully consider these risks when choosing the number and characteristics of their arbitrators.

Third, Hall Street calls into question the viability of the “manifest disregard” standard articulated in Wilko v. Swan. Given the Court’s holding that the grounds for vacatur in Section 10 of the FAA are exclusive, parties seeking to defend an arbitral award from challenge under the “manifest disregard” doctrine will rely on the Court’s language questioning the viability of that doctrine. At the very least, it is reasonable to conclude that the “manifest disregard” concept embodied in
Wilko – which has been embraced and applied by the lower federal courts (albeit sparingly) to vacate arbitral awards — will come under further judicial scrutiny.

Fourth, Hall Street permits parties who wish to include more expansive judicial review provisions in their arbitration agreements to do so by providing for their arbitrations to be governed by more flexible state arbitration acts or state common law rather than the FAA.26 Parties that do not want to proceed to confirm, vacate or modify awards under the FAA must clearly demonstrate their intent to contract around the statute. Even here, however, contracting parties should beware. While parties are indeed free to agree that their arbitration agreements will be governed by state law instead of the FAA, the FAA extends to any arbitration agreement “affecting commerce” — an exceedingly broad sweep that the Court has held is coextensive with Congress’s powers under the Commerce Clause — and that any state law that singles out arbitration agreements or awards for unfavorable treatment is preempted.27 Given the potential tension between state laws that permit parties to superimpose a more exacting standard of judicial review over their agreements (and thereby implicitly undermine Section 9, which the Court itself held “carries no hint of flexibility” in commanding reviewing courts to confirm awards that do not run afoul of Sections 10 or 11), lower federal courts will be left to decide whether, in the wake of Hall Street, those state laws permitting expanded judicial review of arbitral awards are preempted by the FAA. Previous decisions concerning federal preemption of state standards for vacatur suggest this may be a fertile ground for further litigation and judicial refinement.28

If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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2 Chief Justice Roberts, together with Justices Alito, Ginsburg, Thomas and Scalia, joined Justice Souter’s majority opinion; Justice Scalia joined in the opinion with the exception of footnote 7, which claimed that the majority’s conclusion was supported by the history of the Federal Arbitration Act. Justices Stevens, Kennedy and Breyer dissented.

3 9 U.S.C. § 1, et seq.


5 Hall Street, slip op., at 4 (quoting Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 400, 443 (2006)).


7 See 9 U.S.C. §§ 4 (authority to compel arbitration), 3 (authority to stay litigation pending arbitration) and 9 (power to confirm arbitral awards).

8 See 9 U.S.C. § 9 (emphasis supplied).

9 Hall Street, slip op. at 10.

10 Id. § 10(a)(1)–(a)(4).

11 Id. § 11(a)–(c).

12 See 341 F.3d 987, 1000 (9th Cir. 2003) (en banc).

13 On remand, the district court vacated the award on the ground that it “rested on an implausible interpretation of the lease and thus exceeded the arbitrator’s power.” The Ninth Circuit reversed, holding that “implausibility is not a valid ground for vacating or correcting an award under § 10 or § 11.” 196 Fed. Appx. 476, 477-78 (9th Cir. 2006).

14 Kyocera Corp. v. Prudential-Bache Trade Servs., Inc., 341 F.3d 987, 1000 (9th Cir. 2003); Bowen v. Amoco Pipeline Co., 254 F.3d 925, 936 (10th Cir. 2001).

15 Puerto Rico Tel. Co. v. U.S. Phone Mfg. Corp., 427 F.3d 21, 31 (1st Cir. 2005); Jacoda (Europe), Ltd. v. Int’l Marketing Strategies, Inc., 401 F.3d 701, 710 (6th Cir. 2005); Roadway Package Sys., Inc. v. Kayser, 257 F.3d 287, 288 (3rd Cir. 2001); Gateway Tech., Inc. v. MCI Telecom. Corp., 64 F.3d 993, 997 (5th Cir. 1995). The Court noted that two circuits, the Fourth and Eighth, had expressed agreement with the First and Sixth Circuit approach in dicta and an unpublished opinion, respectively. Hall Street, slip op. at 6 n.5 (citing Syncor Int’l Corp. v. McEland, 120 F.3d 262 (4th Cir. 1997) and UHC Mgm’t Co. v. Computer Sciences Corp., 148 F.3d 992, 997-98 (8th Cir. 1998)).


17 The Court observed the “vagueness of Wilko’s phrasing” but decided to “take[] the Wilko language as we found it, without embellishment.” Hall Street, slip op. at 8 (citing First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 942 (1995)).

18 Id. at 8-9.

19 Id. at 9.

20 This rule provides that, where a statute sets out a series of specific items ending with a general term, the general term is confined to covering subjects comparable to the specifics it follows. See id. at 9; see also Black’s Law Dictionary 535 (7th ed. 1999).

21 Hall Street, slip op. at 10-11.

22 Id.

23 Hall Street, slip op. at 13.

24 Id.

25 Hall Street, slip op. at 14-15.

26 See, e.g., West’s Annotated California Code of Civil Procedure § 1286.2 (court shall vacate award if “An arbitrator making the award either: (A) failed to disclose within the time required for disclosure a ground for disqualification of which the arbitrator was then aware; or (B) was subject to disqualification upon grounds specified in Section 1281.91 but failed upon receipt of timely demand to disqualify himself or herself as required by that provision.”).


28 See, e.g., Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior University, 489 U.S. 468, 476-77 (1989) (“There is no federal policy favoring arbitration under a certain set of procedural rules; the federal policy is simply to ensure the enforceability, according to their terms, of private agreements to arbitrate. The FAA contains no express preemptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration.”).