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Reining in the "Manifest Disregard" of the Law Standard: The Key To Restoring Order To The Law Of Vacatur

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I. INTRODUCTION

Section 10(a) of the Federal Arbitration Act (FAA)[1] sets out four very narrow grounds upon which the courts can vacate commercial arbitration awards. Those grounds are:

> Where the award was procured by corruption, fraud, or undue means; Where there was evident partiality or corruption in the arbitrators, or either of them.; Where 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; and Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final and definite award upon the subject matter submitted was not made.[2]

On its face, Section 10(a) does not sanction judicial inquiry of any sort into the merits of commercial arbitration awards. Instead, its clear and unambiguous

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1. 9 U.S.C. § 1 (1994).
2. 9 U.S.C. § 10(a) (1994).

language speaks primarily in terms of party, advocate and arbitrator misconduct or misbehavior affecting the arbitration proceeding or its outcome.

Despite the facial clarity of Section 10(a), all twelve U.S. Circuit Courts of Appeals (save the Federal Circuit) have embraced one or more of a variety of nonstatutory grounds for vacatur. Seminal among the nonstatutory grounds for vacatur is the "manifest disregard" of the law standard first articulated by the U.S. Supreme Court in the 1953 opinion *Wilko v. Swan*.[3] In one fashion or another these nonstatutory standards permit courts deciding petitions for vacatur to evaluate the accuracy (on the facts) and the correctness (on the relevant law and disputed contract language) of challenged awards.[4] The obvious incongruity between Section 10(a) of the FAA and the nonstatutory grounds for vacatur is jumping off point for this analysis.

II. THESIS OF THE ARTICLE AND FRAMEWORK FOR ANALYSIS

The nonstatutory grounds for vacatur, including "manifest disregard" of the law, present a significant impediment to the maturation and institutionalization of commercial arbitration as an effective alternative to traditional litigation. First, they rob the process of its most essential feature — finality — by giving parties disappointed with the result reached in arbitration reason to believe they may be able to circumvent objectionable awards by resort to the courts. Second, by encouraging petitions for vacatur, the nonstatutory grounds increase the expense, time to resolution and consternation associated with commercial arbitration. Finally, because they facilitate judicial review of the reasoning and mode of decision underlying challenged arbitral results, the nonstatutory grounds are an overwhelming disincentive to reasoned awards that reveal the manner in which the arbitrator decides disputed questions of fact, contract interpretation and law.[5] In doing so, they

3. 346 U.S. 427 (1953).

4. Thus, an award may be vacated if it is in "manifest disregard" of the law; is in direct conflict with "public policy;" is "arbitrary and capricious;" is "completely irrational;" or "fails to draw its essence" from the parties' underlying contract. A full analysis of the effect of the nonstatutory grounds for vacatur is beyond the scope of this article. For a comprehensive treatment of this topic see Stephen L. Hayford, *Law in Disarray: Judicial Standards for Vacatur of Commercial Arbitration Awards*, 30 GA. L. REV. 731, 763-842 (1996).

5. The case law makes clear that it is the absence of reasoned awards, revealing the mode of arbitral analysis and decision, that prevents the courts from relying upon the nonstatutory grounds to overturn arbitration awards they find suspect. *See, e.g.*, Prudential-Bache Sec. v. Tanner, 72 F.3d 234, 241, 243 (1st Cir. 1995) ("where arbitrators do not explain the reasons for justifying their award, '[the party seeking vacatur] is hard pressed to satisfy the exacting criteria for [vacatur under the manifest disregard of law criterion]'" (quoting O.R. Sec., Inc. v. Professional Planning Assocs., Inc., 857 F.2d 742, 747 (1st Cir. 1995)); Raiford v. Merrill Lynch, Pierce, Fenner & Smith, 903 F.2d 1410, 1413 (11th Cir. 1990) (observing that in the absence of reasons provided by the arbitrators for the award, judicial review could not be effective); Sargent v. Paine Webber Jackson & Curtis, Inc., 882 F.2d 529, 532 (D.C. Cir. 1989) ("Clearly insistence on an explanation would increase the ability of courts to spot the sort of [arbitral transgression] that justifies overturning an arbitral award."); *O.R. Sec.*, 857 F.2d at 747 ("When the arbitrators do not give their reasons, it is nearly impossible for the court to determine whether [vacation is warranted]."). Consequently, the conventional wisdom of commercial arbitration holds that the advantages on-the-record decision making in commercial arbitration are outweighed by the greatly increased threat of vacatur they would create. *See also* 3 IAN MACNEIL ET AL., FEDERAL ARBITRATION

ensure that arbitral decision making remains off the record and unrevealed—causing many to suspect the rigor and reliability of arbitration as a surrogate for adjudication in the courts.[6]

The thesis of this article is that if the "manifest disregard" of the law standard is either rejected as doctrinally unsound or somehow harmonized with Section 10(a) of the FAA in a manner that precludes judicial intrusion into the merits of commercial arbitration awards, the legitimacy of all of the remaining nonstatutory grounds for vacatur will be eviscerated. If those nonstatutory standards were eliminated, the law of vacatur would be restored to the simple, straightforward standards articulated by Congress in Section 10(a) of the FAA.

At the same time, the substantial barrier to reasoned awards in commercial arbitration presented by the "manifest disregard" of the law standard and the other, lesser nonstatutory grounds would be eliminated. On the record decision-making would become the norm in commercial arbitration. Finally, the time to resolution, expense and overall complexity of commercial arbitration would be significantly reduced. All of these changes would serve to hasten the evolution of commercial arbitration as a distinct and viable alternative to traditional litigation.

The tension at the heart of the contemporary law of vacatur—between the congressionally articulated scheme that does not sanction judicial evaluation of the correctness or accuracy of arbitration awards and a body of judge-made law whose only purpose is to facilitate such judicial inquiry—must be resolved. Until it is, confusion will continue to be the order of the day and commercial arbitration will remain hostage to the specter of judicial vacatur of awards. This article is intended to ameliorate the current confusion in the law of vacatur by carefully explicating the "manifest disregard" of the law standard and demonstrating how it can be removed from the nonstatutory sphere.

In the analysis that follows the various approaches developed by the circuit courts of appeals in implementing and applying the "manifest disregard" of the law standard are described and evaluated. The core elements of the "manifest disregard" of the law inquiry are identified and the four primary modes of analysis found in the current case law are described and critiqued. Next, an alternative mode of analysis is proposed that is both loyal to the *Wilko* standard and harmonizes the "manifest disregard" of the law construct with Section 10(a) of the FAA. The commentary concludes with a discussion of the long-run viability of the "manifest disregard" of the law standard and an assertion that it must either be rejected entirely or brought within the embrace of the Section 10(a) statutory grounds for vacatur.

LAW §§ 37.4.1, 37:12 (Supp. 1994) ("It is often said that the absence of written rationale insulates the award from judicial review."); Whitmore Gray, *Drafting the Dispute Resolution Clause*, *in* COMMERCIAL ARBITRATION FOR THE 1990S 140, 150, (Richard Medalie ed., 1991) ("Some [arbitration] rules, such as those of the AAA, do not require reasoned awards in commercial cases, proceeding from the premise that the less said, the fewer the grounds for attacking the award. . . . Unless the arbitrator makes a commitment to a theory and gives reasons, a party may find it difficult to prove that the arbitrator exceeded his or her authority in the award made."); Thomas J. Stipanowich, *Rethinking American Arbitration*, 63 IND. L.J. 425, 485 (1988) ("The use of substantive written awards in commercial arbitration] would probably increase the likelihood of appeal and judicial review of the award.").

6. *See* Stephen Hayford & Ralph Peeples, *Commercial Arbitration in Evolution: An Assessment and Call for Dialogue*, 10 OHIO ST. J. ON DISP. RESOL. 343, 401-05 (1995).

III. THE ORIGIN OF THE "MANIFEST DISREGARD" OF THE LAW GROUND FOR VACATUR

Ten of the twelve circuit courts of appeals have sanctioned "manifest disregard" of the law as a nonstatutory ground for vacatur of commercial arbitration awards.[7] Only the Fourth and Fifth Circuit Courts of Appeals have declined to approve it. The oft-cited *Wilko* dictum is the sole basis for the "manifest disregard" of the law standard. In *Wilko* the Supreme Court was presented with a question of the enforceability of an arbitration agreement between a broker and a customer in a dispute involving issues arising under the Securities Act of 1933.[8] In holding the arbitration agreement unenforceable with regard to statutory claims arising under the 1933 Act, the Court concluded that the effectiveness of the Act's provisions meant to protect investors "is lessened in arbitration as compared to judicial proceedings."[9]

In the course of an opinion highly critical of commercial arbitration and commercial arbitrators, the Court observed as follows, in dictum

> While it may be true . . . that a failure of the arbitrators to decide in accordance with the provisions of [relevant law] would "constitute grounds for vacating the award pursuant to section 10[a] of the Federal Arbitration Act," that failure would need to be made clearly to appear. In unrestricted submissions [to arbitration] . . . the interpretations of the law by the arbitrators in contrast to manifest disregard [of the law] are not subject, in the federal courts, to judicial review for error in interpretation.[10]

The *Wilko* Court made clear its belief that arbitrators are not well suited to deciding questions of law and/or applying law to fact. In addition, the Court was troubled by the fact that arbitrators need not explain their awards and generally fail to make the type of record necessary to facilitate effective judicial review of their decisions. Those actual and perceived shortcomings of the commercial arbitration process, and the absence of judicial review for error in interpretation of the law, left the Court convinced that arbitration was an inappropriate vehicle for the adjudication of statutory claims.[11]

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7. *See* Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp., 103 F.3d 9 (2d Cir. 1997); Barnes v. Logan, 122 F.3d 820 (9th Cir. 1997); Montes v. Shearson Lehman Bros., Inc., 128 F.3d 1456 (11th Cir. 1997); M & C Corp. v. Erwin Behr & Co., 87 F.3d 844 (6th Cir. 1996); Prudential-Bache Sec., Inc. v. Tanner, 72 F.3d 234 (1st Cir. 1995); United Transp. Union Local 1589 v. Suburban Transit Corp., 51 F.3d 376 (3d Cir. 1995); National Wrecking Co. v. International Bhd. of Teamsters, Local 731, 990 F.2d 957 (7th Cir. 1993); Lee v. Chica, 983 F.2d 883 (8th Cir. 1993); Kanuth v. Prescott, Ball & Turben, Inc., 949 F.2d 1175 (D.C. Cir. 1991); Jenkins v. Prudential-Bache Sec., Inc., 847 F.2d 631 (10th Cir. 1988).

8. Wilko v. Swan, 346 U.S. 427, 438 (1953).

9. *Id.* at 435.

10. *Id.* (citations omitted).

11. *Id.* at 433-437. Specifically, the Court held that an agreement to arbitrate statutory claims arising under the 1933 Act constituted a "stipulation" waiving compliance with a "provision" of the Act (that guaranteeing the right of a disgruntled investor claiming a violation of the Act to select the judicial forum), in violation of its section 14. *Id.* at 434-35. The key to that holding was the Court's conclusion that the effectiveness of the Act's provisions meant to protect investors "is lessened in arbitration as compared to judicial proceedings." *Id.* at 435. By categorizing the right to a judicial forum as a

In 1989 the Supreme Court reversed *Wilko* in *Rodriguez de Quijas v. Shearson /American Express.*[12] The issue in *Rodriguez* -- "whether a predispute agreement to arbitrate claims arising under the Securities Act of 1933 is unenforceable, requiring resolution of the claims only in a judicial forum"[13] -- centered on the very same question decided by the Court in *Wilko*. That question is "whether an agreement to arbitrate future controversies constitutes a binding stipulation 'to waive compliance with any provision' of the Securities Act, which is nullified by § 14 of the Act."[14] In ignoring the rule of *Wilko* that section 12(2) claims under the 1933 Act were not arbitrable, the Fifth Circuit concluded the Supreme Courts' recent decisions concerning commercial arbitration had reduced *Wilko* to "obsolescence."[15] With surprisingly little fanfare, given the fact that it was reversing its own precedent of some 36 years standing, the Supreme Court agreed with the Fifth Circuit's assessment of *Wilko*.

The Supreme Court's rejection of *Wilko*, and the "old judicial hostility to arbitration" which pervaded its characterization of the commercial arbitration process, was founded on what the Court described as an "erosion" of that view over the years, [16] as intensified by the Court's holdings in *Shearson/American Express v. McMahon,*[17] *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.,*[18] *Dean Witter Reynolds v. Byrd,*[19] *and Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*[20] In particular, the *Rodriguez* Court focused on the statement in *Mitsubishi* that "[b]y agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits their resolution to an arbitral, rather than a judicial, forum."[21] The Court then stated emphatically: "[t]o the extent that *Wilko* rested on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants, it has fallen far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes."[22]

In reversing *Wilko* in *Rodriguez* the Court did not address the "manifest disregard" of the law dictum.[23] In the 46 years since *Wilko* the Supreme Court has

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substantive right that is effectively waived by an agreement to arbitrate future disputes, the Supreme Court laid a broad foundation for the presumption that arbitration was not a suitable vehicle for the adjudication of claims based on federal statutory law.

12. 490 U.S. 477 (1989).

13. *Id.* at 478.

14. *Id.* at 479.

15. Rodriguez de Quijas v. Shearson Lehman Bros., Inc., 845 F.2d 1296, 1299 (5th Cir. 1988), *quoted in Rodriguez*, 490 U.S. at 479.

16. *Rodriguez*, 490 U.S. at 480-81.

17. 482 U.S. 220 (1987).

18. 473 U.S. 614, 628 (1985).

19. 470 U.S. 213 (1985).

20. 460 U.S. 1 (1983).

21. *Rodriquez*, 490 U.S. at 481 (quoting Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth , Inc., 473 U.S. 614, 628 (1985)).

22. *Id.* at 481-82.

23. The standard has been mentioned in Supreme Court opinions only three times since 1953, always in dictum, always in passing, twice in dissent. In his dissent in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, Justice Stevens noted, without further comment, "[a]rbitration awards are reviewable for manifest disregard of the law." 473 U.S. 614, 656 (1985) (Stevens, dissenting). In his partial concurring/partial dissenting opinion in *Shearson/American Express v. McMahon*, Justice

never elucidated as to the meaning and effect it attributes to the "manifest disregard" of the law standard. Similarly, the Court has never clarified the manner in which the "manifest disregard" construct relates, if at all, to the statutory grounds for vacatur of commercial arbitration awards articulated in Section 10(a) of the FAA. Because a majority of the Supreme Court has never spoken definitively to the continued viability of the "manifest disregard" of the law standard in light of *Rodriguez*, the question of whether the *Wilko* dictum is still a proper basis for this and all of the other nonstatutory grounds for vacatur remains open.[24]

The broad acceptance of the "manifest disregard" of the law ground by the U.S. Circuit Courts of Appeals demonstrates they do not question its legitimacy and continued viability. Regardless, the numerous Circuit Court of Appeals opinions approving the "manifest disregard" ground have failed to produce a unitary, clearly articulated mode of analysis. The omission by the Supreme Court to clarify whether the "manifest disregard" of the law standard remains operative today, and the disarray that omission has created in the law of vacatur, are the genesis for this article. The section which follows describes the efforts of the U.S. Circuit Courts of Appeals to fill the void left by the Supreme Court's omission to address the "manifest disregard" of the law ground for vacatur in the 45 years since *Wilko*.

IV. ANALYSIS AND CRITIQUE OF THE RELEVANT CASE LAW

The case law makes clear that "a party seeking to vacate an arbitration award for "manifest disregard" of the law may not proceed by merely objecting to the results of the arbitration."[25] "Manifest disregard" of the law "clearly means more than [an arbitral] error or misunderstanding with respect to the law."[26] As the

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Blackmun observed: "[j]udicial review is still substantially limited to the four grounds listed in § 10 of the [Federal] Arbitration Act and to the concept of 'manifest disregard' of the law." 482 U.S. 220, 259 (1987). The third reference by the Supreme Court to the *Wilko* manifest disregard dictum is found in a parenthetical phrase in dictum in the 1995 case, *First Options of Chicago v. Kaplan*. 514 U.S. 938 (1995).

24. For an argument that the reversal of *Wilko* by *Rodriguez* can be viewed as effectively mooting the "manifest disregard of the law" dictum of the latter case see Hayford, *supra* note 4, at 812-23. *But see* E. Al-Harbi v. Citibank, N.A., 85 F.3d 680, 684 n.1 (D.C. Cir. 1996) ("Although the holding in *Wilko* was overruled by *Rodriguez de Quijas v. Shearson/American Express, Inc.*, the dicta that constitutes the core of appellant's argument [relying upon the "manifest disregard of the law" ground for vacatur] was unaffected by the grounds of the overruling."); Baravati v. Josephthal, Lyon & Ross, Inc., 28 F.3d 704, 706 (7th Cir. 1994) (asserting that the reversal of *Wilko* by the Supreme Court and its rejection of the anti-arbitration mindset of the *Wilko* court warrants the conclusion that the "manifest disregard of the law" ground should is void).

25. O.R. Sec., Inc. V. Professional Planning Assocs., 857 F.2d 742, 747 (1st Cir. 1995).

26. Carte Blanche (Singapore) PTE. Ltd. v. Carte Blanche Int'l., 888 F.2d 260, 265 (2d Cir. 1989) (quoting Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker, 808 F.2d 930, 933 (2d Cir. 1986)) (citing Siegel v. Titan Indus. Corp., 779 F.2d 891, 892-93 (2d Cir. 1985)); Drayer v. Krasner, 572 F.2d 348, 352 (2d Cir. 1978); I/S Stavborg v. National Metal Converters, Inc., 500 F.2d 424, 432 (2d Cir. 1974)); *see also* San Martine Compania De Navegacion v. Saguenay Terminals Ltd., 293 F.2d 796, 801 (9th Cir. 1961) ("[M]anifest disregard must be something beyond and different from a mere error in the law or failure on the part of the arbitrators to understand or apply the law."); Kanuth v. Prescott, Ball & Turben, 949 F.2d 1175, 1182 (D.C. Cir. 1991) ("[M]anifest disregard means much more than a failure to apply the correct law."); *E. Al-Harbi*, 85 F.3d at 682 ("[T]his nonstatutory theory of vacatur cannot

Eleventh Circuit observed in *Montes v. Shearson Lehman Brothers, Inc.*:[27] "[a]n arbitration board that incorrectly interprets the law has not manifestly disregarded it. It has simply made a legal mistake."[28] The line between a mere error of law by an arbitrator and "manifest disregard" of the law was not made clear by the Supreme Court in *Wilko*.[29] Nevertheless, the case law indicates consensus among the circuit courts as to the general nature of the judicial inquiry called for in applying this nonstatutory ground for vacatur.

In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*,[30] the Second Circuit stated:

> The [arbitral] error [of law] must have been obvious and capable of being readily and instantly perceived by the average person qualified to serve as an arbitrator. Moreover, the term "disregard" implies that the arbitrator appreciates the existence of a clearly governing principle but decides to ignore it or pay no attention to it." (citation omitted) . . . Judicial inquiry under the manifest disregard standard is therefore extremely limited. The governing law alleged to have been ignored by the arbitrators must be well defined, explicit, and clearly applicable. [The courts] are not at liberty to set aside an arbitration panel's award because of an arguable difference regarding the meaning or applicability of the laws urged upon it.[31]

Similarly, the Ninth Circuit in *San Martine* observed: "[w]e apprehend that a 'manifest disregard of the law' in the context of the language used in *Wilko v. Swan* (citation omitted) might be present when arbitrators understand and correctly state the law, but proceed to disregard same."[32] The First Circuit, speaking in similar terms in *Advest, Inc. v. McCarthy*,[33] stated: "[i]n this context . . . 'disregard' implies that

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empower a District Court to conduct the same de novo review of questions of law that an appellate court exercises over lower court decisions. Indeed, we have in the past held that 'it is clear that [manifest disregard] means more than error or misunderstanding with respect to the law.'" (quoting *Kanuth*, 949 F.2d at 1178)).

27. 128 F.3d 1456 (11th Cir. 1997).

28. *Id.* at 1461.

29. *San Martine*, 293 F.2d at 801 ("[In *Wilko*] [t]he Court did not undertake to define what it meant by 'manifest disregard' or indicate where the line would be drawn between a case of 'manifest disregard' and a case of error in interpretation of the law.").

30. 808 F.2d 930 (2d Cir. 1986).

31. *Id.* at 933, *quoted in* M & C Corp. v. Erwin Behr & Co., 87 F.3d 844, 851 (6th Cir. 1996); International Telepassport Corp. v. USFI, Inc., 89 F.3d 82, 85 (2d Cir. 1996); Conntech Dev. Co. v. University of Connecticut Educ. Properties, Inc., 102 F.3d 677, 687 (2d Cir. 1996), *cited in* Advest. Inc. v McCarthy, 914 F.2d 6, 10 (1st Cir. 1990); *see also* Sobel v. Hertz, Warner & Co., 469 F.2d 1211, 1214 (2d Cir. 1972) ("[I]f [] arbitrators simply ignore the applicable law, the literal application of the "manifest disregard" standard should presumably compel vacation of the award."); Fahnestock & Co. v. Waltman, 935 F.2d 512, 516 (2d Cir. 1991) ("Illustrative of the degree of 'disregard' necessary to support vacatur under [the manifest disregard standard] is our holding that manifest disregard will be found where an 'arbitrator 'understood and correctly stated the law but proceeded to ignore it.'" (quoting Siegel v. Titan Indus. Corp., 779 F.2d 891, 893 (2d Cir. 1985))).

32. *San Martine*, 293 F.2d at 801. The court went on to describe the "manifest disregard of the law" standard as contemplating "manifest infidelity to what the arbitrators know to be the law, but deliberately disregard." *Id.*

33. 914 F.2d 6 (1st Cir. 1990).

the arbitrators appreciated the existence of a legal rule but willfully decided not to apply it."[34] The Eighth Circuit, although declining to adopt the standard in *Marshall v. Green Giant Co.*,[35] nevertheless clarified its view of the two-step inquiry for identifying when an arbitrator has engaged in a "manifest disregard of the law." It observed,"[m]anifest disregard of the law exists when the arbitrator commits an error that was 'obvious and capable of being readily and instantly perceived by the average person qualified to serve as an arbitrator . . . "[and] when "the arbitrator appreciates the existence of a clearly governing legal principle but decides to ignore or pay no attention to it."[36]

A. The Constituent Elements of the "Manifest Disregard" of the Law Inquiry

These articulations of the "manifest disregard" of the law standard reveal its two constituent elements as currently applied by the U.S. Courts of Appeals. One element looks to the result reached in arbitration and evaluates whether it is clearly consistent or inconsistent with the controlling law. For this element to be satisfied, a reviewing court must conclude that the arbitrator misapplied or failed to apply the relevant law touching upon the dispute before her in a manner that constitutes a blatant, gross error of law that is apparent on the face of the award. Thus, this component of the manifest disregard inquiry looks to an "actus reus"-like dimension—the commission of a very serious error of law (actually taking the form of a misapplication of law to fact) by the arbitrator.

Under a proper view of the "manifest disregard" of the law standard, an error of law, no matter how obvious or outrageous a court may deem it to be, cannot alone justify vacatur. That conclusion requires evaluation of the second element of the "manifest disregard" of the law standard—the arbitrator's knowledge, her awareness of the relevant law and the manner in which she behaved in light of that knowledge. Contrasted with the first, "actus reus"-like element of the "manifest disregard" inquiry, this second step of the analysis takes the form of a two-dimensional "mens rea"-like, state of mind determination.

Thus, even if a reviewing court finds a blatant misapplication of the relevant law (reflected in an arbitral result it believes to conflict with that law), vacatur is warranted under the "manifest disregard" of the law ground only if the court is able to conclude the arbitrator knew, correctly interpreted the relevant law, but nevertheless made a conscious, intentional decision to ignore it.[37] Both aspects of

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34. *Id.* at 10. *See also* Montes v. Shearson Lehman Bros., 128 F.3d 1456, 1461 (11th Cir. 1997) ("To manifestly disregard the law, one, must be conscious of the law and deliberately ignore it."); Merrill Lynch, Pierce, Fenner & Smith v. Jaros, 70 F.3d 418, 421 (6th Cir. 1995) (In *Jaros*, the Sixth Circuit stated that vacatur for "manifest disregard of the law" is appropriate where "(1) the applicable legal principle is clearly defined and not subject to reasonable debate; and (2) the arbitrators refused to heed that legal principle.").

35. 942 F.2d 539, 550 (8th Cir. 1991).

36. *Id.*

37. M & C Corp. v. Erwin Behr & Co., 87 F.3d 844, 851 (6th Cir. 1996) (observing that, on the facts of the case before it, no "manifest disregard of the law" was shown because "any mistake by the arbitrator in applying [the relevant law] was more likely the result of inadvertence, rather than *a conscious decision to ignore the relevant law*" (emphasis added)).

the "mens rea" requirement must be satisfied— the arbitrator must have been aware of the correct law and further must have consciously or intentionally chosen not to apply it to the facts of the case in rendering the award. Absent evidence in the record before the reviewing court reliably demonstrating that the arbitrator actually misapplied the relevant law and did so with the knowledge of the error of that action and/or the intention to nullify the law or an awareness that he was doing so, vacatur is not appropriate.

B. The Dilemma Raised by the Absence of Reasoned Awards in Commercial Arbitration

The relevant case law shows that when deciding petitions for vacatur brought under the "manifest disregard" of the law ground, the U.S. Circuit Courts of Appeals unfailingly commence their analysis with an incantation of the two-step, "actus reus—mens rea" standard. As the above-cited opinions demonstrate, the two elements are not always ordered in the same manner. Some courts place the "actus reus" (error of law) dimension first whereas other courts place the "mens rea" (knowledge of the law) element first.

Regardless, having invoked the "manifest disregard" of the law template, those courts inevitably find themselves unable to apply it directly, in two distinct steps. It is simple enough for a court to decide if the first, "actus reus" element of the "manifest disregard" inquiry is satisfied. The court need only determine if the error of law it perceives in the challenged award is of sufficient gravity to satisfy whatever error threshold it has set down under that element. The "mens rea" step of the "manifest disregard" of the law analysis is far more difficult to effect.

Reasoned awards, revealing the manner in which the arbitrator decided the questions of fact, law and contract, and application of law and contract to facts, are the exception in commercial arbitration in the United States.[38] In the absence of reasoned awards setting forth the mode of arbitral decision, courts cannot actually ascertain (and the petitioner for vacatur cannot actually prove) that the arbitrator in fact knew the correct law. Consequently, it is impossible for the courts to determine first hand that the arbitrator knowingly or intentionally disregarded the relevant law in fashioning the award. The case law reveals that when confronted with this dilemma, the circuit courts of appeals have responded in one of three ways. Each of these modes of judicial response is described and critiqued below.

C. The "Futility Acknowledged" Approach to the "Manifest Disregard" of the Law Analysis

In the most simplistic mode of response reviewing courts concede the futility of attempting to divine the arbitrator's state of mind (the "mens rea" element) in the

38. *See* 1 MARTIN DOMKE, DOMKE ON COMMERCIAL ARBITRATION, § 29:06, at 435-36 (Gabriel M. Wilner et al. eds., rev. ed., supp. 1994) ("[C]ommercial arbitration awards . . . are rarely accompanied by written opinions.").

absence of a reasoned award and summarily reject the petition for vacatur.[39] The vast majority of circuit appeals opinions applying the "manifest disregard" of the law standard use this approach. Because this analytical tack never leads to vacatur, it reduces the "manifest disregard" of the law ground to a nullity.

A reviewing court that requires direct evidence of arbitral knowledge of the correct interpretation of the law (the "mens rea" element) will never vacate an award that does not set forth the arbitrator's conclusions of law and fails to reveal the manner in which the arbitrator applied that law to the facts of the controversy. Beside the obvious uselessness of a criterion that cannot be effected, the far bigger problem with this perspective on the "manifest disregard" standard is the substantial disincentive it creates to reasoned awards in commercial arbitration.[40]

Undoubtedly, many of the parties to the commercial arbitration process, and the advocates who represent them, would prefer that arbitrators reveal the findings of fact, and the identification and application of the relevant contract language and law that led to their awards. While the "futility acknowledged" approach to the "manifest disregard" of the law standard effectively insulates awards from vacatur, it at the same time serves to perpetuate the "no reasoned awards" *status quo* in commercial arbitration by effectively precluding the widespread use of reasoned awards in cases which turn in any way on questions of law.

If parties and advocates who desire reasoned awards in such cases could require them without imperiling the finality of the arbitral result, the perception that commercial arbitration is a fair and rigorous alternative to traditional litigation would undoubtedly be enhanced. It can hardly be disputed that an alternative dispute resolution device that features on the record decision-making is superior to, and more acceptable to potential users, than one which does not. Besides minor concerns regarding increased fees for arbitrator study time and extended time to decision, there are no substantial reasons, other than enhanced risk of vacatur, currently preventing parties that desire reasoned awards from directing arbitrators to provide them. Because the "futility acknowledge" approach to the "manifest disregard" of the law ground precludes wider use of reasoned awards, it is deeply flawed. Consequently, it cannot remain the dominant mode of deciding petitions for vacatur brought under the "manifest disregard" of the law ground.

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39. *See* Prudential-Bache Sec. Inc. v. Tanner, 72 F.3d 234, 240 (1st Cir. 1995) ("[W]hen the arbitrators do not give their reasons, it is nearly impossible for the court to determine whether they acted in disregard of the law." (quoting *O.R. Sec.*, 857 F.2d at 747)); *see also* Merrill Lynch, Pierce, Fenner & Smith v. Jaros, 70 F.3d 418, 421 (6th Cir. 1997) ("Where, . . . , the arbitrators decline to explain their resolution of certain questions of law, a party seeking to award set aside faces a tremendous obstacle."); Advest, Inc. v. McCarthy, 914 F.2d 6, 10 (1st Cir. 1990) (" [As] arbitrators need not need explain their award (citation omitted) and did not do so here, it is no wonder that [the petitioner for vacatur] is hard pressed to satisfy the exacting criteria for invocation of [the manifest disregard of the law] doctrine." (citing *O.R. Sec.*, 857 F.2d at 747 & n.4 (observing that a showing of "manifest disregard of the law" is "extremely difficult" in the absence of a reasoned award))).

40. For a full description and analysis of this dynamic see Stephen L. Hayford, *A New Paradigm for Commercial Arbitration: Rethinking the Relationship Between Reasoned Awards and the Judicial Standards for Vacatur*, 66 GEO. WASH. L. REV. 443 (1998).

D. The "Big Error" Approach to the "Manifest Disregard" of the Law Analysis

The second approach to the "manifest disregard" of the law analysis short circuits the two-step inquiry by focusing only on the "actus reus" element. It bypasses the "mens rea" component entirely and relies instead upon an inference of constructive knowledge of the law by the arbitrator based on the clarity of the relevant law and the degree of error reflected in the challenged award. This mode of analysis effectively transforms the "manifest disregard" of the law test into a standard warranting vacatur anytime an arbitrator commits what amounts to a "big error" of law.

Under this view, the key for the petitioner seeking vacatur is convincing a reviewing court that the controlling law is so clear and well-settled as to warrant the inference that the arbitrator must have been aware of it. If a reviewing court concludes that the controlling law is of "widespread familiarity, pristine clarity, and irrefutable applicability . . .[it] can assume the arbitrators knew the rule . . ."[41] Vacatur becomes a reality if the reviewing court is willing to "bootstrap" its way from the inference of constructive knowledge of the law (based on the clarity of the legal doctrine at issue) by the arbitrator to a finding by the court that an individual possessed of a knowledge of that law could not possibly have decided the case as the arbitrator did, unless she chose to disregard the law.[42]

The distinguishing characteristic of this mode of analysis is the predisposition of the court to assume the "mens rea" element of the "manifest disregard" inquiry is satisfied without any objective verification of that finding. This judicial willingness to make a cognitive leap, from the perceived clarity of the controlling law and the strong exception a court takes to the arbitral result, to the conclusion that the arbitrator must have known the law and chose to ignore it, is remarkable.

This second model for the "manifest disregard" of the law analysis is the most troublesome of the three current variants. It raises the prospect of vacatur when a party believes that (i) the controlling law is beyond dispute, and (ii) the award is clearly inconsistent with that law. The problem is that neither of these findings, even if justified, provides any reliable, objective indicia of the arbitrator's actual state of mind, his knowledge of the law. The "Big Error" model effectively dispenses with the second, "mens rea" element of the "manifest disregard" inquiry.

Reduced to its essence, this second approach to the "manifest disregard" of the law analysis consists of nothing more than a determination of whether the arbitrator

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41. *Advest*, 914 F.2d at 10, *quoted in Tanner*, 72 F.3d at 240.

42. *See id.* (holding that a court can find "manifest disregard" of the law where "the governing law [has] such widespread familiarity, pristine clarity, and irrefutable applicability that a court could assume the arbitrators knew the rule and, notwithstanding, swept it under the rug"); Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corp., 103 F.3d 9, 12-13 (2d Cir. 1997) (stating that in the absence of a reasoned award, "a reviewing court *can only infer from the facts of the case whether 'the arbitrator[s] appreciate[d] the existence of a clearly governing legal principle but decide[d] to ignore it or pay no attention to it'*" (quoting Merrill Lynch, Pierce, Fenner & Smith v. Bobker, 808 F.2d 930, 933 (2d Cir. 1986) (emphasis added)); *see also Jaros*, 70 F.3d at 421 (stating that vacatur for "manifest disregard of the law" is appropriate where "(1) the applicable legal principle is clearly defined and not subject to reasonable debate; and (2) *the arbitrators refused to heed that legal principle*").

made an error of law that a reviewing court is unwilling to tolerate. The reality for the courts under this view in the contemporary "no reasoned awards" scenario is well stated by the recent opinion by the Second Circuit in *Willemijn Houdstermaatschappij, BV, v. Standard Microsystems Corp.*[43] The Second Circuit observed that in applying the "manifest disregard" of the law ground a court can "confirm the arbitrator's decision 'if a ground for the arbitrator's decision can be inferred from the rest of the case.'"[44] By this test, the challenged award must be confirmed "if there is 'even a barely colorable justification for the outcome reached . . . .'"[45] Alternatively, "a court may infer that the arbitrators manifestly disregarded the law if it finds that the error [of law] made by the made by the arbitrators is obvious [as measured by whatever degree of error standard the particular court has embraced]."[46]

Under the *Standard Microsystems* formulation of the "manifest disregard" of the law test, vacatur is warranted on two alternative bases. First, an award can be overturned if the court is unable to infer an appropriate ground for the arbitrator's award from the record before it. Alternatively, vacatur can transpire if the court perceives in the award what amounts to a gross error of law that offends its sense of justice.

The *Standard Microsystems* opinion is remarkable for its candor. At once it both strips away the façade of a genuine effort at inferring arbitral knowledge and discloses the true danger posed by the contemporary, error-focused "manifest disregard" standard. To a party that believes it has been seriously wronged in an important case, the temptation to employ this constructive knowledge device in support of a petition for vacatur is undoubtedly great. It presents the prospect of achieving vacatur without being required to prove that the arbitrator actually was aware of the correct interpretation of the relevant law.

It is true that, to date, no court of appeals has vacated a commercial arbitration award under this version of the "manifest disregard" of the law analysis. The reported case law indicates that fact has not deterred substantial numbers of parties from seeking vacatur under the "manifest disregard" standard based solely on the assertion that the arbitrator made a "big" error of law. Given the near certainty that such petitions will be rejected, it seems clear this variant of the "manifest disregard" serves little purpose beyond delaying the time to final resolution in arbitration and increasing the cost and complexity of the process. The destabilizing effect it has on commercial arbitration is unmistakable.

E. The Presumption-Based Approach to the "Manifest Disregard" of the Law Analysis

The third approach to the "manifest disregard" of the law construct has emerged only very recently. It is embodied in the opinion of the Eleventh Circuit

43. 103 F.3d 9 (2d Cir. 1997).
44. *Id.* at 13 (quoting Sobel v. Hertz, Warner & Co., 469 F.2d 1211, 1216 (2d Cir. 1972)).
45. *Id.* (quoting Andros Compania Maritima v. Marc Rich & Co., 579 F.2d 691, 704 (2d Cir. 1978)).
46. *Id.* (citing Merrill Lynch, Pierce, Fenner & Smith v. Bobker, 808 F.2d 930, 933 (2d Cir. 1986)).

in *Montes v. Shearson Lehman Bros*[47] and the opinion of the Second Circuit in *Halligan v. Piper Jaffray, Inc.*[48] To date, *Montes* and *Halligan* are the only cases in which U.S. Circuit Courts of Appeals have vacated commercial arbitration awards for "manifest disregard" of the law. The key to that result in both cases was the willingness of the courts (i) to presume, through various devices, arbitral knowledge of the correct interpretation of the law at issue, based upon the courts independent evaluation of the record made in arbitration, and (ii) based on the presumption, to infer a conscious or intentional disregard of the law.

In *Montes* the Eleventh Circuit's presumption was apparently based solely on the assertion by the prevailing party's counsel at the hearing that the controlling law was "not right," and his repeated exhortations to the arbitration panel that they should do what was right, even if it produced an outcome inconsistent with the pertinent law.[49] The court noted that the summary of the parties' arguments set out in the award demonstrated that the arbitrators recognized they had been "flagrantly and blatantly urged" to ignore the law.[50] Without further explanation it then concluded that the application of the "manifest disregard" of the law construct was justified because "the arbitrators recognized that they were told to disregard the law (which the record reflects they knew) in a case where the evidence to support the award was marginal."[51]

By the Eleventh Circuit's test, the arbitrator's presumed knowledge of the correct law, coupled with the absence of anything in the record "to suggest that the law was not disregarded" (there being no reasoned award) warranted vacatur for "manifest disregard" of the law. What is significant about this analytical tack is the fact that it produced a finding of "disregard" with any concrete indicia that the arbitrators consciously or intentionally chose to dismiss or ignore the law that they were presumed to have known. Instead, the court inferred knowing disregard of the law by the arbitrators because it found no evidence that they did not disregard it. This extraordinary act of "bootstrapping" by the Eleventh Circuit achieved vacatur under the "manifest disregard" of the law standard without the benefit of any objective evidence that the arbitrators actually knew the law, and possessed of the that knowledge consciously or intentionally chose to ignore it.

Halligan involved a petition for vacatur under Section 10(a) of the FAA of an arbitration award centering on a claim of illegal age discrimination brought under the Age Discrimination in Employment Act (ADEA). Following the normal "drill" in "manifest disregard of the law" cases, the Second Circuit first emphasized that the "reach of the doctrine of ["manifest disregard"] is severely limited."[52] It then stated further that in order to vacate for "manifest disregard of the law" a court must "find both that (1) the arbitrators knew of a governing legal principle yet refused to apply

47. 128 F.3d 1456 (11th Cir. 1997).
48. 148 F.3d 197 (2d Cir. 1998).
49. *Id.* at 1459.
50. *Id.* at 1461.
51. *Id.* at 1462. Immediately following this observation the court engaged in more than three pages of analysis of the facts in the arbitral record, following which it concluded that the key question of fact before the arbitrators could not have been resolved in a manner that would have led to the challenged award. *Id.* at 1462-64.
52. Halligan v. Piper Jaffray, Inc., 148 F.3d 197, 202 (2d Cir. 1998).

it or ignored it altogether, and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case."[53]

After discussing the "growing concern" over the problem of employees being held to their a priori agreements to arbitrate statutory-based employment discrimination claims, the court proceeded to review the proof of illegal age discrimination adduced by the claimant employee, characterizing the proof as "overwhelming."[54] It found further that the arbitrators had been advised by the counsel for both parties of the correct legal principles on which the outcome of the arbitration should have turned.[55]

Because of the strong proof of illegal discrimination it found in the record, combined with the fact that the arbitrators had been advised of the correct law, the Second Circuit concluded, "we are inclined to hold that [the arbitrators] ignored the law or the evidence or both."[56] The court made clear that the arbitrators' failure to explain the basis for their award denying the claim of illegal discrimination was a factor in its holding.[57] The decision rule reflected in Halligan echoes that set out in Montes. By its terms vacatur of an award is warranted for "manifest disregard" of the law if a court, after evaluating the facts and the law, concludes the award was wrong and finds nothing in the award itself to demonstrate that the arbitrators did not knowingly ignore the law.

The framework for analysis under this third model works backwards from an arbitral outcome the reviewing court believes to be flawed as a matter of law, confirmed by an exhaustive evaluation of the factual record made in arbitration. This judicial rethinking of the factual questions and the questions of application of law to facts integral to the resolution of the matter in arbitration is coupled with a search for evidence in the record upon which the court can base a presumption of arbitral knowledge of the correct law. Once that evidence is identified the court is free to "bootstrap" its way to the inference that the arbitrator must have ignored the relevant law in fashioning an award the court believes is contrary to the law.

The Montes-Halligan model for the "manifest disregard" of the law inquiry provides a convenient means for circumventing the problem caused by trhe frequent absence in commercial arbitration of reasoned awards revealing the arbitrator's mode of analysis. It does so by using a presumption of arbitral knowledge of the correct interpretation of the law to justify an inference of conscious or intentional disregard of the law—both findings achieved without benefit of any direct evidence of the arbitrator's actual state of mind. Thus, this model solves the dilemma that leads to the "futility acknowledge" mode of analysis under the "manifest disregard" of the law standard. It also avoids blatant dismissal of the "mens rea" element that flaws the "big error" variant of the "manifest disregard" inquiry.

The problem inherent in this approach is that in applying it a court grants itself a de facto license, in the course of deciding whether to vacate a challenged award for "manifest disregard" of the law, to reexamine in depth the outcome determinative

53. *Id.*
54. *Id.* at 202-03.
55. *Id.* at 203-04.
56. *Id.* at 204.
57. *Id.*

questions of fact, law and application of law to fact that the parties had contracted to resolve in arbitration. If the outcome reached in arbitration does not jibe with the result indicated by a court's independent evaluation of the facts and the law, vacatur is triggered.

It is difficult to distinguish this mode of the "manifest disregard" of the law inquiry from a straightforward review of the merits of arbitration awards. As long as counsel for the party petitioning for vacatur is careful to ensure the arbitral record contains an articulation and explanation of relevant law, it can achieve vacatur by convincing a reviewing court that given the facts in the record (as ascertained by the court—not the arbitrator), the arbitral decision could have been achieved only if the arbitrators ignored or misapplied the law.

Instead of looking to the award for evidence of arbitrator misconduct in knowingly or intentionally ignoring the correct law, the court looks to the award for an absence of evidence indicating proper conduct by the arbitrator. Finding none (as invariably will be the case where there is no reasoned award), the court may vacate the offending award by inferring that the arbitrators must have ignored the law. Thus vacatur can occur for "manifest disregard" of the law even though the arbitral outcome might just as likely have resulted from the arbitrators having not understood the legal arguments made to them or from inaccurate arbitral findings of fact. Unless the arbitrators have in some manner articulated their basis for decision, the true source of the erroneous award cannot be reliably determined. Undeterred by this void in the evidence, a court applying the *Montes-Halligan* standard will vacate for "manifest disregard" of the law even though it has no concrete, objective basis for divining what was in the arbitrators' minds (regarding knowledge of the law and intent to nullify it), or ascertaining how the arbitrators resolved the key questions of fact and application of law to facts before them.

Montes and *Halligan* are remarkable opinions that epitomize the danger posed by the current modes of analysis under the "manifest disregard of the law" standard. It is clear the Second Circuit and the Eleventh Circuit both used the "manifest disregard" device as a vehicle, a clever disguise that enabled them to substitute their judgment for that of the arbitrators chosen by the parties to decide the matters in dispute in those cases. This is a most significant development in light of the oft-repeated mantra that in deciding petitions for vacatur courts are not to intrude into the merits of arbitration awards by second guessing arbitrators' decisions of questions of law, contract or fact. The opinions are also remarkable because they virtually mandate reasoned awards in cases involving issues of law, in order to preclude the presumption of "manifest disregard" when a court finds a grave error of law in the arbitral result.

This new, third mode of analysis under the "manifest disregard" of the law standard seems certain to propel many disgruntled parties and their counsel to file numerous petitions for vacatur. For a party bitterly disappointed with the arbitral outcome in an important case, the hope of achieving vacatur by persuading a court that full evaluation of the arbitration record will justify a presumption of arbitral knowledge of the correct law will no doubt often prove irresistible. Widespread judicial willingness to make the substantial cognitive leap from findings as to the nature of the parties' argument and the material facts, to the conclusion that the arbitrator must have known the law and then proceeded to ignore would greatly

diminish the finality and the integrity of the commercial arbitration process. This is a reality the courts and other public policy makers must confront forthrightly.

F. Conclusion

Beyond the factors identified above, there is one overriding reason for rejecting the current paradigm for the "manifest disregard" of the law analysis. Despite the various attempts to distinguish the nature of the judicial inquiry, all three of these formulations begin, with and center upon the perceived degree of legal error reflected in the award.[58] Because many of the circuit courts of appeals opinions applying the "manifest disregard" of the law ground do not clearly describe the process of inference-drawing/presumption that is required in the absence of reasoned awards, they inadvertently misdirect the arguments of parties seeking vacatur. As a result the "manifest disregard" of the law inquiry often permutes from a test centering on the arbitrator's state of mind (knowledge of the correct law and his motivation regarding that law in applying it) and his conduct (failure or refusal to apply that law while possessed of that knowledge), into an analysis concerned only with the purported correctness of the arbitration award on the law, and in some cases the facts.

This core characteristic of the three variants of the contemporary "manifest disregard" of the law analysis encourages losing parties in arbitration who believe they have been wronged to seek vacatur, based largely or solely upon the allegation that the award resulted from an egregious error of law. Those parties petition for vacatur without fully contemplating the great difficulty they will encounter in attempting to prove the second, "mens rea" element of the "manifest disregard" of the law ground—by demonstrating that the arbitrator knew the correct law, and possessed of that knowledge consciously or intentionally chose to ignore the law. That many members of the commercial arbitration bar have not come to grips with the bifurcated, two-element nature of the "manifest disregard" inquiry is confirmed by the numerous reported cases wherein petitions for vacatur are brought absent any allegation that the arbitrator had knowledge (constructive or actual) of the controlling law.

The continued filing of misguided and invariably futile petitions for vacatur invoking this construct prompts the courts to continue their tortured efforts to fashion "degree of error" and inference/presumption-based tests for applying the "manifest disregard" of the law ground in the absence of reasoned awards. As the commentary above demonstrates, without reasoned awards revealing the arbitrator's mode of decision, there is no reliable, objective way for a court to ascertain that both of the components of the "mens rea" element of the "manifest disregard" of the law inquiry (arbitrator knowledge of the correct law and a conscious or intentional decision to ignore or misapply the law) have been satisfied. This phenomenon

58. The analysis under the second and third variants of the "manifest disregard" of the law standard is confused for another reason. The courts applying those two inference-based models generally fail to satisfactorily reconcile their reliance on a significant error of law with the oft-repeated admonition of the Supreme Court in *Wilko* that "interpretations of the law . . . are not subject, in the federal courts, to judicial review for error in interpretation." *Wilko*, 346 U.S. at 436.

destabilizes the process of commercial arbitration, increasing costs and time to resolution in many cases by providing disappointed advocates and parties with an illusory promise of securing justice from a court of law when they believe they have been denied it in arbitration.

Because the three contemporary variants of the "manifest disregard" of the law criterion center upon the correctness of either the arbitrator's interpretation of the law or the manner in which he applies that law to the facts, they are all inconsistent with the oft-repeated admonition of the Supreme Court in *Wilko* that "interpretations of law... are not subject, in the federal courts, to judicial review for error in interpretation."[59] The "error-based" models for the "manifest disregard" of the law analysis also conflict with Section 10(a) of the FAA, which likewise does not contemplate vacatur for errors of law. If the line between confirming and vacating a commercial arbitration award challenged on the arbitrator's resolution of a question of law is determined primarily by the clarity of the relevant law and/or the degree of the arbitrator's purported error in interpreting and applying that law, judicial intrusion into the merits of the arbitrator's decision will always remain a possibility.[60] Section 10(a) does not permit this type of judicial scrutiny of challenged commercial arbitration awards.[61]

The key to vacatur under the "manifest disregard" of the law construct is not an error of law. It is the arbitral act of disregarding the law that warrants vacatur. An arbitrator cannot be proven to have consciously or intentionally ignored or misapplied the correct law until the petitioner for vacatur proves that she knew that law. None of the three current modes of the "manifest disregard" analysis begin with, turn upon, or lead to reliable, objective findings as to arbitral state of mind (his knowledge of the current law and motivation in applying that law) that is the predicate to an award made in disregard of the law. At the same time, none of the three models facilitates vacatur for "manifest disregard" of the law without obliging a reviewing court to delve into the merits of the challenged award—substituting its

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59. *Id.*

60. *See* San Martine Compania de Navegacion, S.A. v. Saguenay Terminals Ltd., 293 F.2d 796, 801 n.4 (9th Cir. 1961) (Criticizing the "degree of error" test for application of the "manifest disregard of the law" standard, the Ninth Circuit observed "[s]uch a 'degree of error' test would, we think be most difficult to apply. Results would likely vary from judge to judge. We believe this is not what the [Supreme] court had in mind when it spoke of 'manifest disregard.'"); *see also* I/S Stavborg v. National Metal Converters, Inc., 500 F.2d 424, 430 n.13 (2d Cir. 1974) ("How courts are to distinguish in the Supreme Court's phrase between 'erroneous interpretation' of a statute, or for that matter, a clause in a contract, and 'manifest disregard' of it, we do not know: one man's 'interpretation' may be another's 'disregard.' Is an 'irrational' misinterpretation a 'manifest disregard?'").

A prime example of the threat of judicial intrusion into the merits of commercial arbitration awards presented by an inordinate focus on the degree of the arbitrator's purported error of law is found in the Sixth Circuit's application of the "manifest disregard of the law" standard in *Glennon v. Dean Witter Reynolds, Inc.* 83 F.3d 132 (6th Cir. 1996). The court, in denying the petitioner's claim described at some length the evidence in the arbitral record concerning the disputed question of law and independently analyzed that evidence in concluding that the challenged award of punitive damages by the arbitration panel was not in manifest disregard of the law. *Id.*

61. *But see* Cole v. Burns Int'l. Sec. Servs., 105 F.3d 1465, 1486-87, (D.C. Cir. 1997) (Discussing the Supreme Court's endorsement of the arbitration of statutory claims, the Court stated: "[the] assumptions regarding the arbitration of statutory claims are valid only if the "manifest disregard of the law" standard is sufficiently rigorous to ensure that arbitrators have properly interpreted and applied statutory law.").

judgment for the arbitrator's with regard to the outcome determinative questions of fact and application of law to fact. Therefore, they must all be rejected because they conflict with Section 10(a) of the FAA and are inconsistent with the true nature of the inquiry called for by the *Wilko* dictum and the "manifest disregard" of the law ground for vacatur which it created.

The Section that follows describes a new framework for analysis of the "manifest disregard" of the law ground that returns the focus where it belongs—to the arbitrator's knowledge of the law and his conduct in light of that knowledge.

V. A BETTER MODEL FOR THE "MANIFEST DISREGARD" OF THE LAW ANALYSIS

The current broad acceptance by the U.S. Circuit Courts of Appeals of the "manifest disregard" of the law ground indicates it will remain a key dimension of the commercial arbitration milieu until or unless it is squarely rejected by the Supreme Court, an event whose timing and occurrence cannot be reliably predicted. For reasons discussed below is quite possible that the Supreme Court will ultimately reject the "manifest disregard" of the law standard. Nevertheless, an effort to frame the "manifest disregard" analysis in a manner that both fully contemplates the "actus reus" and the "mens rea" elements and harmonizes the "manifest disregard" of the law ground with Section 10(a) of the FAA is warranted here. The model described below achieves both of these objectives.

A. The Hallmarks of a Proper Model for Analysis

The full dictum in which the "manifest disregard" of the law construct was first verbalized in *Wilko* demonstrates that the Supreme Court viewed it as something quite different, separate and distinct, from an error of law. Carefully read in its full context, the *Wilko* dictum leaves no doubt that "interpretations of the law by [the] arbitrators," even those that are seriously flawed and readily apparent, are not subject to vacatur.[62] Consequently, as argued strenuously above, correct application of the "manifest disregard of the law" standard cannot turn upon the degree of the arbitrator's purported error of law.[63]

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62. The full dictum reads:

> [w]hile it may be true . . . that a failure of the arbitrators to decide in accordance with the provisions of [relevant law] would "constitute grounds for vacating the award pursuant to Section 10[a] of the Federal Arbitration Act, (citation omitted) that failure would need to be made clearly to appear. In unrestricted submissions [to arbitration] . . . *the interpretations of the law by the arbitrators in contrast to manifest disregard [of the law] are not subject, in the federal courts, to judicial review for error in interpretation.*

Wilko, 346 U.S. at 436 (emphasis added).

63. *See San Martine*, 293 F.2d at 801 n.4 ("Conceivably the words ["manifest disregard"] may have been used to indicate that whether an award may be set aside would be a question of degree. Thus if the award was based upon a mistaken view of the law, but in their assumption of what the law was, the arbitrators had not gone too far afield, then, the award would stand; but if the error is an egregious one, such as no sensible layman would be guilty of, then the award could be set aside. *Such a 'degree of error' test would, we think, be most difficult to apply.*" (emphasis added)); *see also* Hayford, *supra* note

Vacatur for "manifest disregard of the law" should occur when a reviewing court agrees with the arbitrator's interpretation of the law (when it can reliably divine that arbitral state of mind), but subsequently determines that the neutral engaged in intentional or at least knowing misconduct by ignoring or failing to apply that correct reading of the law in resolving the dispute before her.[64] This mode of analysis turns not on the degree of an arbitrator's purported error of law but on the "degree of [her] disregard" of the law.[65] It speaks not to the correctness of the arbitrator's decision on the law, but to the manner in which the arbitrator reached that decision.

If a reviewing court can objectively ascertain the arbitrator's interpretation of the relevant law and disagrees with it (i.e., finds in the award reliable evidence that the arbitrator misunderstood the law), the "manifest disregard" inquiry stops and the award must be confirmed. This is so because an arbitrator cannot "disregard" the law unless she knows it, correctly. This misconduct-centered approach to implementing the "manifest disregard of the law" standard erects an impenetrable barrier to disguised judicial oversight of the arbitrator's resolution of the questions of law and application of law to fact submitted to arbitration for decision.

Evaluation of the extent to which the arbitration award (the product of the arbitrator's application of the relevant law to the material facts) conflicts with relevant law should occur at the back end of the "manifest disregard" analysis, not at the front end. A judicial determination that the award conflicts with the law (at the requisite level of clarity) triggers vacatur only if the court has first reliably and objectively confirmed that the arbitrator understood the law correctly.

Under this framework for analysis the "actus reus" element is not proven by convincing the reviewing court that the arbitrator has made an a grave error of law. Rather, it is the arbitrator's conscious or intentional act of disregarding the law he has been objectively proven to know that completes the inquiry. This act of disregarding the law with the intent to do so, or the knowledge that one is doing so is the precise arbitral misconduct proscribed by the "manifest disregard" of the law ground for vacatur. Absent a reliable judicial finding of that state of arbitral mind (with regard to the arbitrator's knowledge of the law and her intention to misapply or ignore it or at least the awareness that she was doing so), vacatur for "manifest disregard" of the law is not warranted.

4, at 810-19 (discussing the "manifest disregard of the law" nonstatutory ground); *cf.* Kenneth R. Davis, *When Ignorance of the Law is No Excuse: Judicial Review of Arbitration Awards*, 45 BUFF. L. REV. 49, 98 (1997) ("The purpose of [the "manifest disregard of the law" standard] is to provide some measure of review of substantive error in arbitration awards. As a means of correcting error, the standard might reasonably consider the magnitude, quality and consequence of the error under review, rather than the arbitrator's state of mind, a matter of irrelevance."). The analysis in the article above makes clear the present Author's strongly-held belief that the view of the "manifest disregard of the law" standard articulated by Professor Davis is wrong.

64. For a full discussion of this view of the proper interpretation and application of the "manifest disregard of the law" nonstatutory ground for vacatur, see Hayford, *supra* note 4, at 810-19.

65. *See* Fahnestock & Co. v. Waltman, 935 F.2d 512, 516 (2d Cir. 1991) ("[T]here must be 'something beyond and different from a mere error in the law or failure on the part of the arbitrators to understand or apply the law,' (citation omitted) in order to sustain a finding of manifest disregard of the law. Illustrative of the degree of 'disregard' necessary to support vacatur under this standard is our holding that manifest disregard will be found where an 'arbitrator' 'understood and correctly stated the law but proceeded to ignore it.'" (quoting Siegel v. Titan Indus. Corp., 779 F.2d 891, 892, 893 (2d Cir. 1986))).

Undoubtedly this mode of analysis will almost never result in vacatur for "manifest disregard" of the law in the absence of reasoned awards revealing the manner in which the arbitrator applied the relevant law to the facts of the matter in dispute. That is the price the parties pay for foregoing reasoned awards. Even if there is a reasoned award, this paradigm will produce appropriate judicial decisions because it focuses the inquiry on the arbitrator's state of mind and conduct, without requiring or permitting a reviewing court to engage in its own independent evaluation of the facts and the proper application of the law to those facts in order to support subjective inferences in that regard. As such, it returns the judicial inquiry under the "manifest disregard" rubric to an appropriate, very narrow scope.

None of the current models for the "manifest disregard" of the law analysis orders the judicial inquiry in the manner described above and precludes reviewing courts from intruding into the merits of the arbitrator's award (its accuracy on the facts and correctness on the relevant law). Therefore, they should be rejected in favor of the model proposed here. The section that follows describes the manner in which the "manifest disregard" of the law standard can be reconciled with the very restricted, misconduct-focused grounds for vacatur set out in Section 10(a) of the FAA.

B. Harmonizing the "Manifest Disregard" of the Law Ground With Section 10(a) of the FAA

If the "manifest disregard" of the law ground is to survive in the long run it must be harmonized with the "no review on the merits" rule of Section 10(a) of the FAA. The key to achieving that result lies in the *Wilko* dictum from which the "manifest disregard" construct arose. The Court's intonation of the term "manifest disregard" was made within the context of elaborating upon an assertion in the sentence preceding it that "[w]hile it may be true, . . . that a failure of the arbitrators to decide in accordance with the provisions of [the relevant law] would 'constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act' (citation omitted) that failure would have to be made clearly to appear." Careful parsing of this "forgotten" first sentence of the Wilko dictum reveals several things.

The initial clause of that sentence starts with the qualifying phrase "while it may be true" and goes on to refer to the possibility that a failure by the arbitrators to comport their award with applicable law could warrant vacatur "pursuant to section 10[a] of the FAA." On their face, the words chosen by the Court indicate that it was speaking, not to a non-statutory ground for vacatur, but rather to the possibility of vacatur as contemplated by section 10[a] of the FAA.[66] The second and third clauses of the first sentence state that if vacatur for an arbitral failure or refusal to decide a dispute in accordance with the provisions of relevant law were warranted under

66. The Court has never expressly categorized "manifest disregard" of the law as a non-statutory ground. *See I/S Stavborg*, 500 F.2d at 430 ("In *Wilko v. Swan*, (citation omitted), the Court was presented with the narrow question of whether certain provisions of the Securities Act of 1933 invalidated a stipulation in which a purchaser of securities agreed to settle any differences arising out of the purchase by recourse to arbitration. *The Court*, in answering this question in the affirmative, *seemed to say, that a decision by an arbitrator disregarding the applicable securities laws would have been reversible under 9 U.S.C. § 10 . . .*." (emphasis added)).

Section 10[a], "that failure would have to be made clear to appear."

It is within this context that the term "manifest disregard" of the law standard was coined. When the oft-quoted portion of the *Wilko* dictum is returned to, and read within, the context of the full paragraph from which it was drawn, its legitimacy as the basis for a separate, non-statutory ground for vacatur is eviscerated. The standard categorization of "manifest disregard" of the law as a non-statutory ground centering on the merits of commercial arbitration awards and the interpretations and application of relevant law by commercial arbitrators in the course of deciding the merits, does not make sense in light of the manner in which that standard was articulated by the Supreme Court in *Wilko*.

The more plausible reading of the *Wilko* dictum is one whereby its oblique reference to "manifest disregard" of the law is viewed as identifying a type of arbitral misconduct or misbehavior of the nature addressed in section 10(a)(3) of the FAA.[67] If "manifest disregard" is understood only to occur, as the author has suggested, when an arbitrator has correctly interpreted the law and then consciously or intentionally ignored it, then "manifest disregard" describes a kind of untoward arbitral behavior which fits neatly within the proscription on arbitrator "misconduct" and "misbehavior" contained in Section 10(a)(3) of the FAA. If the court concludes that the arbitrator did ignore the law that she correctly understood, then vacatur of the disputed arbitration award would be warranted for arbitrator misconduct in a manner fully embraced by Section 10(a) (3) of the FAA. A party seeking vacatur of a commercial arbitration under section 10(a)(3) on this ground must prove a nexus between the arbitrator's "manifest disregard" of the law and the arbitral result.[68] In other words, the arbitrator's refusal or failure to apply the correct law must be directly linked to the challenged arbitral result. Absent such objective proof, a reviewing court, no matter how incorrect or inaccurate the court may perceive the award to be cannot usurp the award.

Under this paradigm, vacatur of the award transpires, not because the arbitrator made an error of law (i.e., misinterpreted the law), but rather because she intentionally or consciously ignored or misapplied the law. The reason for vacatur is not an erroneous decision, rather it is the manner in which that decision was made. This misconduct/misbehavior-centered approach to implementation of the "manifest disregard" of the law standard erects a substantial barrier to judicial evaluation of the arbitrator's resolution of the merits of the dispute before her.[69] It also precludes a reviewing court from vacating a commercial arbitration award because it disagrees with the arbitrator's interpretation of the law or findings of fact.

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67. *See* Remmey v. Painewebber, Inc., 32 F.3d 143, 146 (4th Cir. 1994) (characterizing the four section 10(a) grounds as warranting vacatur for "sufficiently improper conduct in the course of the [arbitration] proceedings"); *cf.* San Martine Compania de Navegacion, S.A. v. Saguenay Terminals Ltd., 293 F.2d 796, 801 (9th Cir. 1961) (observing that "manifest infidelity to what the arbitrators knew to be the law . . . might well be regarded as the use of 'undue means' within the meaning of [section 10(a)(1) of the FAA)], or amount to 'partiality' within the meaning of [section 10(a)(2) of the FAA]").

68. Hayford, *supra* note 4, at 748.

69. Thus, judicial examination of the arbitrator's alleged error of law, in terms of the arbitral application of law to the facts of the dispute in the course of reaching the arbitral result, does not occur unless there is clear evidence that the arbitrator correctly understood the law.

C. Conclusion

The dynamic just described is a far cry from a "manifest disregard" of the law analysis that begins with ascertaining the degree of the arbitrator's purported error of law and works backwards, by inference, to the conclusion that the arbitrator must have known the law and, possessed of that knowledge, consciously or intentionally disregarded it. It precludes a party from alleging vacatur is warranted based solely on the claim of a gross error of law by the arbitrator. Instead, the petitioner for vacatur must demonstrate at the outset that the "mens rea" element of the "manifest disregard" of the law standard is satisfied.

This approach to the "manifest disregard" standard also prevents a reviewing court from "bootstrapping" its way from an unverified inference or presumption of arbitral knowledge of the correct law to the ultimate conclusion that vacatur for "manifest disregard" of the law is justified. It shifts the focus away from the legal correctness of the arbitrator's decision and obviates the need for judicial "line drawing" between small and big errors of law. It fully respects the contrast seen by the *Wilko* court between an arbitrator's "interpretations of the law" and "manifest disregard" of the law. Vacatur of a challenged award for "manifest disregard" of the law will occur only if the court makes an objective determination that the arbitrator actually knew the law and then consciously or intentionally disregarded it.

The model advocated here sets down a clear, unequivocal standard for vacatur under the "manifest disregard" of the law ground. It should lead to consistent results and drastically reduce the number of futile petitions for vacatur. Because the proposed framework for analysis properly orders and effects the two elements of the requisite inquiry ("mens rea" first and "actus reus" second), it is also fully consistent with the *Wilko* dictum.

This approach also fully legitimates the "manifest disregard" of the law ground for vacatur by moving it out of the realm of the non-statutory grounds and comporting it with section 10(a) of the FAA. As a result it reconciles much of the apparent incongruity between the "manifest disregard" of the law construct and the public policy underlying section 10(a) of the FAA, which clearly does not contemplate judicial review of the merits of commercial arbitration awards. For all these reasons, this framework for decision of petitions for vacatur because of "manifest disregard" of the law should be adopted by the courts.

VI. "MANIFEST DISREGARD" OF THE LAW—THE KEY TO STABILIZING THE LAW OF VACATUR

It is far from clear that, given its present enthusiasm for commercial arbitration and concomitant broad endorsement of the pro-arbitration public policy of the FAA, the present Supreme Court would embrace the "manifest disregard" of the law ground for vacatur.[70] It was created "*ex nihilo*" in what may well have been only a

70. *See* Baravati v. Josephthal, Lyon & Ross, Inc., 28 F.3d 704 ,706 (7th Cir. 1994). Created *ex nihilo* to be a non-statutory ground for setting aside arbitral awards, the *Wilko* formula reflects precisely [the] mistrust of arbitration for which the [Supreme] Court in its

passing, insignificant reference, in dictum.[71] The oblique nature of the Supreme Court's reference to the "manifest disregard" of the law ground in *Wilko*, and the subsequent lack of guidance from the Court as to the proper meaning and effect of this criterion for vacatur, indicate how slender a reed it rests upon. The uncertainty pertaining to, and the long run viability of the "manifest disregard" of the law ground for vacatur most likely will be addressed in one of two ways—either by the Supreme Court rejecting it as inconsistent with Section 10(a) of the FAA, or by the Court bringing it within the embrace of Section 10(a)(3) of the Act consistent with the view articulated in the preceding commentary.

Of at least equal importance is the fact the fact that the *Wilko* dictum was framed at a time when the Supreme Court harbored strong suspicions of the integrity, rigor and competence of both the commercial arbitration process and commercial arbitrators. In rediscovering the FAA in the years since the early 1980s, the Supreme Court has repeatedly rejected the "suspicion of arbitration" (and arbitrators) that underpinned *Wilko*.[72] *Wilko* itself was reversed in *Rodriguez de Quijas v. Shearson/American Express, Inc.*,[73] providing sound basis for arguing that all dimensions of *Wilko*, including the "manifest disregard" of the law dictum, have been mooted.[74]

In resolving critical issues pertaining to the enforceability of contractual agreements to arbitrate, substantive arbitrability and the preemptive effect of the FAA, the Supreme Court has taken a very literal and expansive view of the Act's reach and scope.[75] Given that consistent position, it is difficult to imagine the Court would be willing to set aside the clear and unambiguous language of Section 10(a)

> two Shearson/American Express opinions criticized *Wilko*. We can understand neither the need for the formula nor the role that it plays in judicial review of arbitration [awards] (we suspect none -- that it is just words). If it is meant to smuggle review for clear error in by the back door, it is inconsistent with the entire modern law of arbitration.

Id.

71. *Id.*

72. *See, e.g.*, Gilmer v. Interstate Lane/Johnson, Corp., 500 U.S. 20 (1991); Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987); Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985).

73. 490 U.S. 477 (1989).

74. *See* Forsythe Int'l, S.A. v. Gibbs Oil Co. of Texas, 915 F.2d 1017, 1022 n.5 (5th Cir. 1990) ("*Wilko v. Swan* was overruled on other grounds in *Rodriguez de Quijas v. Shearson/American Express, Inc.* (citation omitted). In *Rodriguez*, the Supreme Court noted *Wilko*'s expressed 'suspicion of arbitration as a method of weakening the protections afforded in the substantive law,' and based its reversal on the extent to which that decision 'had fallen far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes.'" (quoting Rodriguez de Quijas v. Shearson/American Express, Inc., 490 U.S. 477, 481 (1989))).

75. *See, e.g., Mitsubishi,* 473 U.S. at 625-26 ("The preeminent concern of Congress in passing the [FAA] was to enforce private agreements into which the parties had entered," a concern which "requires that we rigorously enforce agreements to arbitrate"); Southland Corp. v. Keating, 465 U.S. 1, 10 (1984) ("In enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration . . . Congress has thus mandated the enforcement of arbitration agreements."); Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1983) (The court characterized section 2 of the FAA as "a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary" that constitutes a "body of federal substantive law of arbitrability applicable to any arbitration agreement within the [FAA].").

and, relying on obiter dictum from an opinion it has reversed and whose underlying principles it has squarely rejected, hold that Congress did not intend for the FAA to set the exclusive standards for vacatur of commercial arbitration awards.

Thus there are sound legal reasons to speculate that the Supreme Court may eventually reject the "manifest disregard" of the law standard as conflicting with Section 10(a) of the FAA and the Act's strong pro-arbitration policy. Other, practical considerations also indicate that is the appropriate outcome. By providing the touchstone for the other nonstatutory grounds for vacatur, all of which sanction judicial review of the merits of awards, the "manifest disregard" of the law standard has prevented the emergence of on the record decision making (i.e., reasoned awards) in commercial arbitration. As explained earlier, in the absence of reasoned awards it is very unlikely that commercial arbitration will ever achieve its full potential as an alternative dispute resolution device.

Even if it passes muster before the Supreme Court, the preceding analysis demonstrates that each of the three current views of this nonstatutory ground for vacatur should be rejected. If it were eventually to be fully confirmed as good law, the "manifest disregard" of the law ground for vacatur should be reconfigured in the manner advocated above and recognized as emanating from section 10(a)(3) of the FAA. The model advocated here would require only a minor "sharpening" of the case law in the circuits that currently recognize this standard. It would serve to impose discipline on what is now a highly disordered sub-component of the law of vacatur and thereby hasten the maturation and institutionalization of the commercial arbitration process. Those are most desirable prospects for those who believe in the potential of commercial arbitration as an alternative dispute resolution device.