

By David Daar

# When Arbitration Loses Its Appeal

## Practitioners should consider a private appeal mechanism in arbitration clauses

Is there anyone in the legal system who wields more unchecked power than an arbitrator who has been appointed without careful planning on the part of the parties in interest? In such instances, the arbitrator reigns virtually supreme. California law provides for no appeal or other form of review on the merits of an arbitrator's decision. This is because so long as the arbitrator does not act beyond his or her powers and provides full disclosure of any conflicts, a review on the merits is not possible unless the contractual arbitration clause expressly creates an appeal process.

Who gives one individual so awesome a power as to not be subject to review? No superior court judge or justice of the court of appeal is beyond review. Nor does any single justice of the California Supreme Court possess such authority. Our judicial system achieves justice because it recognizes that those in high positions can err and has therefore designed well-established procedures to review judicial decisions. In contrast, only a few arbitration tribunals provide for a review mechanism to guard against honest error made in ruling on the merits in an arbitration hearing.

Many companies, large and small, look to arbitration for its well-known benefits: avoiding the unpredictability of jury verdicts and the time and expense of formal litigation. However, those who do not adopt some form of arbitration appellate review will face that arbitrator alone. That means that all the savings of arbitration—indeed, the company, itself—could be wiped out by a single award made by a single arbitrator who is psychologically moved by a particular set of facts. And there would be no appeal from even a rogue decision.

### The Hidden Danger

When parties to a contract agree to an arbitration clause, do they focus on this danger? Are they aware that they are giving up the protective process of a judicial forum? There, parties who think they have been aggrieved by a judicial decision have somewhere else to go. An appeal is available to give them a last chance. Yet no legal principle prevents contracting parties from agreeing to an arbitration clause that includes a system for review on the merits of an award. The parties can designate a panel of other arbitrators to be their "court of last resort."

Recently, California legislators have awakened to the ever-growing importance of arbitration in ADR processes. Arbitration now affects massive numbers of citizens, and legislative efforts are geared to curb purported abuses. At the same time, the legislature should also be concerned that parties often do not understand the vast power they grant to an arbitrator when they agree to arbitration clauses that they probably have had no input in drafting. Unsophisticated signers of contracts containing most of the commonly used arbitration clauses

often do not expect to enter so uncontrolled a forum. Sophisticates, too, accept the system, and only later begin to really wonder what happened to their appeal.

Certainly, many of the fine retired judges who now serve as arbitrators wonder and marvel at the expanded power they wield as arbitrators. They would be the first to admit that arbitrators can, from time to time, reach an erroneous conclusion. As the Ninth Circuit stated forcefully in *Grammer v. Artists Agency*, "[An] arbitrator's 'improvident, even silly, factfinding' does not provide a basis for a reviewing court to refuse to enforce the award."<sup>1</sup>

Agreements containing arbitration clauses can, and many do, designate a private tribunal that will have the power to review the arbitration award. The parties appoint one arbitrator and can provide for another, a neutral, or even three others for review. Arbitration is a creature of contract; there is an opportunity to voluntarily set up the means for arbitration appellate review. Without such a provision, it is, at best, uncertain whether an aggrieved party would ever be able to turn to an appellate court to review an arbitrator's awards.

The federal courts have offered some hope for appellate review. Under the terms of the arbitration clause at issue in *Lapine Technology Corp. v. Kyocera Corp.*, the Ninth Circuit honored a provision that made the arbitration award subject to judicial appellate review.<sup>2</sup> However, in *Crowell v. Downey Community Hospital Foundation*, the first California Court of Appeal decision addressing a clause authorizing judicial review of an arbitration award, the court rejected the clause.<sup>3</sup> The court held that the California Arbitration Act precludes judicial review. Even the dissent recognized that parties could contract for an arbitration review panel. In a recent case, the court of appeal has gone so far as to sanction as a frivolous action an appeal of an arbitrator's decision.

Whatever the merits of these court decisions, we as practitioners need to begin a dialogue—among ourselves and with our clients—on these issues. Let it start here. ■

<sup>1</sup> *Grammer v. Artists Agency*, 287 Fed. 3d 886, 891 (9th Cir. 2002) (quoting *U.P.I. Union v. Misco, Inc.*, 484 U.S. 29, 39 (1987)).

<sup>2</sup> *Lapine Tech. Corp. v. Kyocera Corp.*, 130 F. 3d 884, 889 (9th Cir. 1997) (2-1 decision). The dissent argued that rather than using the public courts, the parties could "contract for an appellate arbitration panel..."

<sup>3</sup> *Crowell v. Downey Cmty. Hosp. Found.*, 95 Cal. App. 4th 730 (2002) (2-1 decision)



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