

Construction Arbitration Clause Calling for Expanded Judicial Review Must be Explicit and Unambiguous

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Parties to construction arbitrations who are disappointed with the arbitrator's award are often doubly-disappointed to learn that they have very little chance of successfully appealing in a court to overturn the arbitrator's decision. Because arbitration is intended to be a final and complete alternative dispute resolution process, judicial review of the arbitrator's award is quite limited. Ordinarily a court may not review the merits of the dispute, or overturn an arbitration award on ground that the arbitrator made legal errors or erred in applying the law to the facts. In general, a court is authorized to overturn an arbitration award only where (i) the award was procured by corruption or fraud; (ii) there was corruption or misconduct by the arbitrator, (iii) the arbitrator exceeded his or her powers, (iv) the arbitrator refused to postpone the hearing despite there being good cause to do so and that prejudices the parties, or (v) the arbitrator failed to disclose potential grounds on which he or she could be disqualified or refused to disqualify himself when there was cause to do so. See, e.g., Cal. Civ. Proc. Code 1286.2.

To expand the scope of judicial review beyond these parameters and obtain something akin to an ordinary right of appeal, parties have attempted to "contract around" the statutory provisions, and have included language in their arbitration agreements providing for appeal or judicial review of the substance of the arbitrator's decision. In a recent decision, the California Court of Appeal held

that to be enforceable, an agreement for expanded scope of judicial review of the arbitrator's award must be explicit and unambiguous, and language in the arbitration agreement stating that the arbitrator must render an award "in accordance with substantive California law" is not sufficient. *Gravillis v. Coldwell Banker Residential Brokerage Company*, 182 Cal. App. 4th 503 (2010).

In *Gravillis*, the plaintiff had purchased a home using a standard form California purchase agreement which included a clause requiring arbitration of any disputes arising out of the agreement. The arbitration clause stated that the arbitrator "shall render an award in accordance with substantive California law." 182 Cal. App. 4th at 508. Before he moved into the home, plaintiff discovered it had extensive structural damage which left it essentially uninhabitable. Plaintiff filed a lawsuit in court against his real estate brokers for failing to disclose the structural defects. Based on the arbitration clause in the purchase agreement, the trial court ordered the case to arbitration. After a hearing, the arbitrator issued an award in favor of the plaintiff and awarded him damages and costs. The brokers petitioned the court to vacate the award, contending that the arbitrator had made substantive legal errors by (i) finding the brokers had breached a fiduciary duty to plaintiff, (ii) awarding the plaintiff "benefit of the bargain damages" rather than "out of pocket expense" damages; and (iii) awarding the plaintiff his costs incurred in the arbitration. The trial court denied the brokers' petition, and the brokers appealed. On appeal, the brokers asserted they were not subject to the general rule of non-reviewability, but were entitled to have the award overturned on the merits based on the arbitrator's legal errors because the arbitration agreement stated that the arbitrator was required to render an award "in accordance with substantive California law."

The Court of Appeal first emphasized the reasoning underlying the general rule -- because parties to arbitration have a right to expect the arbitration will be a final and binding resolution of their dispute, as a general matter, "the merits of the controversy between the parties [in arbitration] are not subject to judicial review," and the "courts will not review the validity of the arbitrator's reasoning."

182 Cal. App. 4th at 514. The brokers argued that because the arbitrator had made legal errors which were "not in accord with substantive California law," the arbitrator had "exceeded his powers" within the meaning of Code of Civil Procedure § 1286.2, and therefore the award could be vacated under the statutory provisions. The Court of Appeal rejected this contention, explaining that an arbitrator exceeds his or her powers when the arbitrator acts without subject matter jurisdiction, decides an issue that was not submitted to arbitration, upholds an illegal contract, issues an award that violates a statutory right or well-defined public policy, or selects a remedy that is not authorized by law or rationally related to the contract. 182 Cal. App. 4th at 511. The court held that the language requiring the award be "in accordance with substantive California law" was not sufficient to convert ordinary legal errors of the sort alleged by the brokers into acts in excess of the arbitrator's powers.

The court further explained that while California law allows parties to cases governed by the California Arbitration Act to contract for expanded judicial review, because a main purpose of arbitration is to avoid the judicial process, the bar for allowing expanded judicial review of the award is high. First, the arbitration agreement must be governed by the California Arbitration Act rather than the Federal Arbitration Act ("FAA") -- federal law does not allow parties to contract for an expanded scope of judicial review. 182 Cal. App. 4th at 518; *Hall Street Associates LLC v. Mattel, Inc.* (2008) 552 U.S. 576. Thus, for example, if the agreement states elsewhere that it is governed by the FAA, it will not qualify for expanded judicial review. Second, "to take themselves out of the general rule that the merits of the award are not subject to judicial review, the parties must clearly agree that legal errors are an excess of arbitral authority that is reviewable by the courts." 182 Cal. App. 4th at 516 (quoting *Cable Connection*, 44 Cal. 4th at 1361). Hence, an arbitration agreement which states that "[t]he arbitrators shall not have the power to commit errors of law or legal reasoning, and the award may be vacated or corrected on appeal to a court of competent jurisdiction for any such error" is sufficient to allow for judicial review of the

substance of the award under California law. *Cable Connection, Inc. v. DIRECTV, Inc.*, 44 Cal. 4th 1334, 1342 n. 3 (2008).

However, language in an arbitration agreement requiring that the arbitrator render an award "in accordance with substantive California law" does not meet that standard. That language does not expressly deprive the arbitrator of the power to commit legal error, nor does it expressly and unambiguously authorize a court to review the award for legal or other substantive error. *Id.* at 518-519.

PRACTICE TIP: Contractors and developers seeking expanded judicial review of the award should include language in their contracts stating that the arbitrators do not have the power to commit errors of law, that the award can be vacated for such errors, and that arbitration is to be governed by the California Arbitration Act.

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