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HYDRAULIC FRACTURING LITIGATION

BY KEITH B. HALL & LAUREN E. GODSHALL

HYDRAULIC FRACTURING IS A PROCESS used to facilitate the production of oil or gas from low-permeability formations. The process was commercially developed in the late 1940s, and it has been used in more than a million wells since then, but for several decades the process drew little public attention. Recently, however, the process has received substantial attention and has become controversial, with many people expressing several concerns, including a fear that hydraulic fracturing might adversely affect underground sources of drinking water. Indeed, plaintiffs have filed litigation in several states, alleging such contamination.

This is one of multiple articles to discuss hydraulic fracturing litigation in this volume of *The Advocate*. This article will: (1) provide basic background information regarding the pending litigation; (2) describe the causes of action being asserted (other than trespass and nuisance, which will be discussed in the another article) and discuss those legal theories in context of oil and gas disputes; and (3) briefly discuss general defenses and expert issues.

Hydraulic fracturing is a process that uses a fluid—typically water, sand, and various additives—at high pressure to create fractures in an underground rock formation, thereby facilitating oil or gas production by providing pathways (the fractures) for oil or gas to flow to the well.

1. Pending Hydraulic Fracturing Litigation

Hydraulic fracturing is a process that uses a fluid—typically water, sand, and various additives—at high pressure to create fractures in an underground rock formation, thereby facilitating oil or gas production by providing pathways (the fractures) for oil or gas to flow to the well. Regulatory officials and industry representatives agree that there have been few, if any, documented cases in which groundwater has been contaminated by hydraulic fracturing operations. But there have been numerous anecdotal claims of contamination. Further, plaintiffs have filed suit in several states, including Texas, Arkansas, Pennsylvania, and New York, alleging that their groundwater has been contaminated by hydraulic fracturing.

In the hydraulic fracturing litigation filed to date, plaintiffs have requested money judgments for several types of alleged harm, including: personal injury caused by use of contaminated water; medical monitoring; fear of cancer; replacement of their domestic water supply; remediation or clean-up of their property or an underground aquifier; loss of property value; and punitive damages.[1] The most commonly asserted causes of action in hydraulic fracturing litigation include clams based on: (a) the abnormally dangerous activity doctrine; (b) negligence; (c) breach of contract; (d) private attorney general or citizen suit statutes; (e) fraud; (f) trespass; and (g) nuisance. [2]

2. Description of the Causes of Action Asserted

a. Abnormally dangerous activity doctrine

The common law has long recognized a theory of strict liability for defendants who engage in "ultrahazardous" or "abnormally dangerous" activities.[3] The leading case is the English case *Rylands v. Fletcher*, 3 H.L. 330 (1868). In *Rylands*, the defendants were mill owners who constructed a large reservoir in which they stored water on their land. The water broke through material used to plug an abandoned mine shaft and flooded the plaintiff's coal mine. The lower courts held that the defendants were not negligent and that they could not be liable in the absence of negligence. The House of Lords disagreed with the conclusion that the plaintiff had to prove negligence in order to recover, and held that a defendant can be strictly liable for an abnormal and inappropriate use of his property. This holding gave rise to the "abnormally dangerous activity" doctrine.

Under this doctrine, a defendant who engages in an "abnormally dangerous activity" and thereby causes harm can be liable even if he was not negligent.[4] Further, the defendant can be liable even if some intervening cause, such as the negligence of a third person or some force of nature, leads to the accident that causes the harm.[5]

To determine whether an activity is "abnormally dangerous," courts look to several factors. Factors that would weigh in favor of classifying an activity as abnormally dangerous include the following: (1) the activity involves a high degree

of risk; (2) any harm caused by the activity probably will be great harm, rather than minor harm; (3) it is impossible to eliminate risk associated with the activity even by the use of reasonable care; (4) the activity does not involve a matter of common usage; (5) the activity is inappropriate to the place where it is conducted; and (6) the risk of the activity outweighs value of the activity to the community.[6] Classic examples of "abnormally dangerous" activity include blasting with explosives and pile driving.

But the "abnormally dangerous activity" cause of action will not necessarily apply to hydraulic fracturing claims. Some of the current hydraulic fracturing cases are pending in Texas, and Texas does not recognize the abnormally dangerous activity doctrine.[7] Louisiana recognizes the doctrine, but limits its application to blasting and pile driving.[8] Thus, the doctrine would not apply to hydraulic fracturing cases in Louisiana.

Further, even in states that do not exclude the doctrine altogether or construe it as narrowly as Louisiana does, courts will not necessarily conclude that hydraulic fracturing constitutes an abnormally dangerous activity. Defendants likely will argue that various facts weigh against hydraulic fracturing being deemed abnormally dangerous, including the utility of the process, an ability to limit risk by careful well construction, and the historical fact that the process has been used more than one million times with few (if any) documented cases in which hydraulic fracturing has caused contamination of groundwater. Indeed, in a hydraulic fracturing case in Pennsylvania, a court denied the defendants' Federal Rule of Civil Procedure 12(b)(6) motion to dismiss an abnormally dangerous activity claim, but suggested in dicta that the court had doubts that plaintiffs' abnormally dangerous activity claim would survive a summary judgment motion later in the case.[9]

If a court determines that hydraulic fracturing is abnormally dangerous, that does not conclusively establish liability because there are potential defenses. For example, Restatement (Second) Torts § 523 recognizes that assumption of the risk is a defense. Comment (b) to § 523 provides an example of assumption of the risk. The comment states that, if a possessor of land who knows the risk of blasting consents to allow blasting on neighboring property, he cannot recover if he is harmed by the blasting. Most oil and gas companies operate their wells pursuant to mineral leases. If a lessor who understands the alleged risk of hydraulic fracturing consents to a lease, knowing that the lessee might conduct hydraulic fracturing, the defense of assumption of the risk might apply. Contributory negligence is also a recognized defense.[10] An example of a situation in which this defense might apply is if a person drinks water after he suspects it is contaminated, and he later claims that he was harmed by drinking the water.

b. Negligence

A person can be liable for negligence if he causes harm to another by failing to be as careful as a reasonable person would.[11] If legislation or regulations mandate or prohibit certain conduct, a court may adopt that mandate as the standard of conduct of a reasonable person for purposes of negligence liability.[12] If a court does so, violation of the statute or regulation establishes negligence per se.[13] In the alternative, a court might stop short of adopting the legislation or regulations as the standard of conduct, but may allow a plaintiff to use the legislation or regulations as evidence of the proper standard of care.[14] In Texas, the Supreme Court has explained that the adoption of prohibitory statutes into tort law is a matter of judicial discretion. The Court has used a test that includes five nonexclusive factors in determining whether a statute establishes an appropriate standard for negligence per se liability.[15]

If a plaintiff asserts that contamination was caused by a well construction failure, but the defendant can establish that it complied with all applicable well construction standards, the defendant should argue that such compliance establishes an absence of negligence.

Numerous regulations apply to oil and gas drilling, including regulations that establish standards for well construction, and regulations that require well operators to take precautions against spills of fluids. If a plaintiff asserts that contamination was caused by a well construction failure, but the defendant can establish that it complied with all applicable well construction standards, the defendant should argue that such compliance establishes an absence of negligence.[16] Similarly, if a plaintiff can show that a defendant's failure to comply with spill prevention and control regulations resulted in a spill that harmed the plaintiff, the plaintiff should argue that the defendant's violation of the regulations conclusively establishes negligence.

c. Breach of contract

Companies typically drill and operate oil and gas wells pursuant to a mineral lease with the person holding mineral rights to the land on which the well is drilled (the mineral rights owner may or may not be the landowner). In addition to the mineral lease, the oil and gas company may have a surface use agreement with the landowner. These contracts may contain express clauses which would give the landowner a basis for a contract claim in the event his land or the groundwater beneath his land becomes contaminated.

In addition, courts typically impose implied covenants that require oil and gas lessees to conduct their activities as reasonably prudent operators. This standard of conduct sounds very much like a negligence standard, and a landowner could argue that a lessee has breached an implied covenant if the lessee negligently causes contamination of the landowner's property or the groundwater beneath it. In response, the lessee might argue that the plaintiff's claim sounds only in tort. A few cases have held that a plaintiff may assert an implied covenant claim based on the lessee allegedly causing an accident,[17] but there are not many such cases. Generally, implied covenants are used to ensure that lessees are diligently exploring for and producing minerals, marketing any product that is found, and protecting the property against drainage by wells on neighboring property. [18]

Courts frequently impose implied covenants in the context of oil and gas leases – more frequently than with other types of contracts. The reason for this is a particular characteristic of oil and gas leases. Namely, because of the uncertainties involved in mineral exploration, an oil and gas lease generally does not specify in detail the exploration and production activities the lessee will conduct.[19] Thus, some of the most important aspects of a lessee's performance are left to his discretion. Because so much is left to the discretion of the lessee, courts protect the lessor by imposing implied covenants that require the lessee to act as a reasonably prudent operator.[20] But implied covenants arguably are not needed to guard against negligent conduct because negligence law itself already does that. Accordingly, if a plaintiff claims that the lessee negligently caused contamination, the lessee can make a strong argument that such a claim sounds only in tort, and that the plaintiff has not stated a breach of contract claim.

d. Private attorney general or citizen suit statutes

Usually, a plaintiff does not have a cause of action merely because a defendant allegedly violated a law. Instead, the plaintiff must show that he was harmed by the defendant's conduct in some way that the public at large was not harmed. But many environmental statutes contain "private attorney general" or "citizen suit" provisions which provide that if the government fails to bring an enforcement action against a defendant who allegedly has violated an environmental law, then a private citizen can do so.[21] Citizen suit provisions generally place various limitations and conditions on the right of a prospective plaintiff to sue pursuant to a citizen suit provision. Accordingly, a person considering bringing such an action, or a defendant sued in such an action, should examine the language of the citizen suit provision, as well as the facts of the case, to determine whether the plaintiff has standing to assert a citizen suit.

e. Fraud

Many observers view fraud as an unlikely legal theory for hydraulic fracturing contamination claims, but some plaintiffs have asserted fraud claims, alleging that a defendant made a misrepresentation about, or failed to warn of, some danger. To recover in fraud, a plaintiff generally must establish that he was harmed by acting in reliance on the alleged misrepresentation or omission. If a plaintiff already knew about the alleged dangers of hydraulic fracturing, or would have taken the same actions even in the absence of the alleged fraud, the defendant may be able to defeat the fraud claim by arguing that the plaintiff did not act in reliance on the alleged fraud.[22]

f. Trespass

Trespass claims raise interesting issues. These are discussed in an article by Professor Hannah Wiseman that appears in this issue of *The Advocate*.

g. Nuisance

Nuisance claims are discussed in Professor Wiseman's article.

3. General Defenses and Expert Issues

a. Statutes of limitation

Statutes of limitation may provide a defense. For most hydraulic fracturing contamination claims, the statute of limitations will be a matter of state law, and the applicable limitations period may depend on the type of damages alleged and the particular cause of action asserted. In Texas, claims based on contamination caused by oil and gas drilling activity generally must be brought within two years of discovery.[23]

b. Experts

In any jurisdiction, the plaintiff will have to prove that the harm he alleges was caused by the defendant. Texas courts apply a strict causation standard in allegations of subsurface contamination. For example, in *Mitchell Energy Corp.*, a Texas appellate court held that it was not sufficient for the

plaintiff's expert witness to testify that identical hydrogen sulfide isotopes were detected in both a polluted aquifer and the defendant's nearby oil well; the expert witness also was required to "rule out other causes of the presence of hydrogen sulfide in appellees' water."[24]

In several of the cases in which a landowner claims that his water has been contaminated, he alleges that it has been contaminated with methane, the main component in natural gas. But in many parts of the country it is common for water wells to contain methane even if there is no active oil or gas activity in the area. For this reason, it often will be important to determine the source of any methane that allegedly contaminates a water well. An environmental chemist can perform isotopic analyses of the methane to determine whether the methane was formed thermogenically, which would indicate that the methane was created deep beneath the ground, or whether the methane was created biogenically, which would indicate that the methane was created by biological processes nearer the surface. This can provide clues regarding the source of the natural gas.
In hydraulic fracturing litigation, the plaintiffs often will allege that contamination resulted from a well construction failure, such as inadequate casing or cementing. Accordingly, parties often will need experts who can testify about well construction and well failure. This may be a petroleum engineer or a mechanical engineer. Further, parties may wish to consult with hydrologists who can evaluate how a plume of contaminants might spread.

In addition to the types of experts discussed above, particular cases may call for a variety of other experts. For example, if the plaintiff alleges personal injuries or seeks compensation for medical monitoring, medical experts likely will be needed. If the plaintiff alleges that his property value has decreased, real estate appraisers may be needed. If the plaintiff seeks damages for remediation or clean up of his property, environmental consultants may be needed.

Conclusion

Plaintiffs have filed hydraulic fracturing contamination claims in several states, and it is likely that similar actions will continue to be filed. The plaintiffs assert legal theories similar to those asserted in other types of litigation, but the resolution of hydraulic fracturing cases often will turn on fact patterns and circumstances unique to the oil and gas industry, and one or more experts likely will be needed to properly litigate the case.

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1 *See, e.g., Fiorentino v. Cabot Oil & Gas Corp.*, No. 3:09-2284 (M.D. Pa.); *Harris v. Devon Energy Co., L.P.*, No. 4:10-0708 (N.D. Tex.).

2 *See, e.g., Fiorentino v. Cabot Oil & Gas Corp.*, No. 3:09-2284 (M.D. Pa.); *Harris v. Devon Energy Co., L.P.*, No. 4:10-0708 (N.D. Tex.).

3 *See* Restatement (Second) Torts § 519.

4 *See* Restatement (Second) Torts § 519.

5 *See* Restatement (Second) Torts § 523.

6 *See* Restatement (Second) Torts § 520.

7 *See Turner v. Big Lake Oil*, 96 S.W.2d 221 (Tex. 1936) (release of a large quantity of produced water); *Doddy v. Oxy USA, Inc.*, 101 F.3d 448, 461-62 (5th Cir. 1996) (alleged migration of toxic chemicals from oil and gas well); *see also Hall v. Amoco Oil Co.*, 617 F. Supp. 111, 112-13 (S.D. Tex. 1984) (operation of oil refineries).

8 *See* La. Civ. Code art. 667.

9 *See Berish v. Southwestern Energy Production Co.*, 763 F. Supp. 2d 702, 706 (M.D. Pa. 2011).

10 *See* Restatement (Second) Torts § 524.

11 *See* Restatement (Second) Torts § 283.

12 *See* Restatement (Second) Torts § 286; *Perry v. S.N.*, 973 S.W.2d 301, 304 (Tex. 1998).

13 *See* Restatement (Second) Torts § 288B.

14 *See id.*; *Reeder v. Daniel*, 61 S.W.3d 359, 361–62 (Tex. 2001); *Perry*, 973 S.W.2d at 304.

15 *Perry*, 973 S.W.2d at 304; *Discovery Operating, Inc. v. BP Am. Prod. Co.*, 311 S.W.3d 140, 162 (Tex. App. - Eastland 2010, pet. denied).

16 *See, e.g., Mieth v. Ranchquest, Inc.*, 177 S.W.3d 296, 305 (Tex. App. - Houston [1st Dist.] 2005) (applying negligence per se standard to violation of Texas Railroad Commission rule against pollution of subsurface water).

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Under the Influence

PLUS

BY LAUREN E. GODSHALL

Using Effective Contract Language in Arbitration Agreements

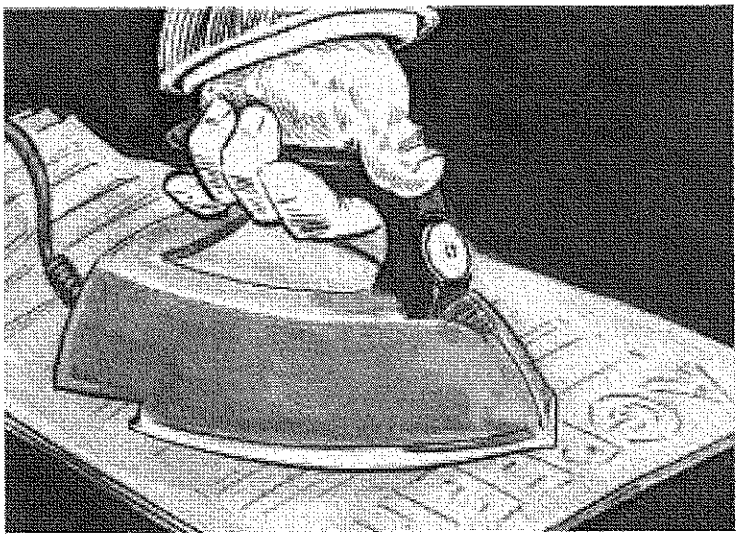
THE MAJORITY OF ATTORNEYS may get through three years of law school and complete the bar exam without ever having encountered the term "arbitration," but the fact is that arbitration is almost inevitably going to be encountered in any legal practice. Mandatory binding arbitration clauses appear in almost every type of contract, from joint venture agreements between business partners to cell phone contracts. Except in the very rare instance in which the arbitration provision in a contract, or the entire contract, can be found unenforceable due to its basic unconscionability, an arbitration provision is mandatory, and a court will enforce it.[1]

In addition to being mandatory, the typical arbitration provision leads to a result that is more or less unreviewable by a court. This immediate finality is commonly perceived as one of the great benefits to arbitration, in that litigation and appeals are completely avoided. The question still remains, however, how unreviewable the decision of an arbitrator actually is. This is important for business attorneys drafting contracts that incorporate a mandatory binding arbitration provision because they need to ensure that the benefits of arbitration that they seek are actually realized. Likewise, a litigator faced with an arbitration decision that the client insists was erroneous and unjustified also needs to be able to explain to that client whether an appeal of that decision to a court of law would be a worthwhile exercise or a waste of time and money.

It is well known and often repeated in case law that an arbitrator is free to be wrong. A merely erroneous decision on the facts of the matter will not be reversed by a court.[2] The chance that an arbitrator may simply just get it wrong is a risk inherent in the arbitration process, and the reason why time and effort is well spent by attorneys in choosing their arbitrator or arbitration panel.[3] But it is also essential to remember that arbitration is itself a contract.[4] While an arbitrator is free to decide the matter presented, however rightly or wrongly, the arbitrator must not stray outside the limitations of the arbitration contract. A court will look only to the language of the arbitration agreement and will use that language to make all determinations about the propriety and reviewability of the outcome.

Because the outcome of an arbitration is unreviewable, lawyers must craft their agreements to arbitrate to limit or control the outcome so that review becomes unnecessary. This is easily accomplished—and can only be accomplished—in the language of the arbitration contract. Parties can limit the powers or arbitrators to specific questions or require the application of specific law.[5] For example, a franchise agreement may require submission of any dispute to binding arbitration, require the application of the American Arbitration Association's commercial arbitration rules, and limit the arbitrator's discretion by specifically proving "in no event may the material provisions of this agreement be modified or changed by the arbitrator at any arbitration hearing."

This was the issue in the franchise agreement litigation presented in *Gueyffier v. Ann Summers, Ltd.*, an opinion of the California Supreme Court.[6] This case demonstrates that even when arbitrators seem to go beyond the limits of their authority as defined by the contract, their decision is still likely to be found unreviewable.



RICHARD EWING

In *Gueyffier,* the arbitrator was bound to apply the provisions of the contract to the dispute in question and was expressly prohibited from modifying or changing any element of the contractual requirements. The arbitrator, however, found that compliance with the contractual provisions was excused and therefore the mandatory provisions did not need to be applied to the dispute. The losing party immediately took the arbitration decision to court, insisting that this was a violation of the arbitrator's powers. The supreme court disagreed and made the important distinction that excuse of a contractual term is not the same as a modification of a contractual term.

The Franchise Contract

The *Gueyffier* opinion concerned a dispute over a franchise agreement between Celine Gueyffier and Ann Summers, Ltd., a British company that franchised lingerie and adult novelty stores throughout the United Kingdom. Ann Summers entered into the franchise agreement with Gueyffier in an attempt to open the first American Ann Summers store. Ann Summers and Gueyffier signed a franchise agreement under which Gueyffier was to open an Ann Summers location in Beverly Hills. Ultimately, Gueyffier opened her store, but the opening was a total failure, as the store was greeted with open hostility. Gueyffier was quickly forced to close the store.

Disputes almost immediately arose regarding whether each party had performed its obligations under the contract. Gueyffier claimed that Ann Summers had violated the franchise agreement by failing to properly provide training and support as it was obliged to do under

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the contract. Ann Summers countered that the contract had a notice-and-cure provision that would have required Gueyffier to first provide notice of the problem to Ann Summers and give the company a 60-day opportunity to cure this problem prior to closure of the store and declaration of breach. Ann Summers claimed that Gueyffier should have immediately notified the company when she realized that it was not fulfilling its training and support obligations. Because Gueyffier failed to give this notice, Ann Summers alleged that Gueyffier was, in fact, the party in breach.

The franchise agreement contained an arbitration clause providing for mandatory arbitration in the event of a dispute between the parties. It specifically limited the arbitrator's discretion, explicitly stating: "In no event may the material provisions of this Agreement...be modified or changed by the arbitrator at any arbitration hearing."[7]

The dispute accordingly went to arbitration. The arbitrator ultimately found that the breach by Ann Summers in failing to provide the necessary training and support for Gueyffier was incurable. Because the breach was incurable, the notice-and-cure provision was necessarily mooted due to impossibility. Therefore, the arbitrator concluded, Gueyffier's breach of the notice-and-cure provision was excused by Ann Summers's own breach of that same contract.

On appeal to the trial court, the question became: Was the equitable principle of excuse within the arbitrator's powers to grant? After all, under the terms of the contract, the arbitrator was limited by the contract from modifying or changing any provision. By excusing Gueyffier's failure to comply with one of the provisions, was the arbitrator in fact changing that provision and adding an "impossibility of cure" defense?

The arbitrator did not provide a lengthy written justification for the award. Under the contract to arbitrate, this was perfectly acceptable. A reasoned decision by the arbitrator was neither required under the arbitration provision nor requested by the parties. This was not an unusual situation. Due to the usually unreviewable nature of arbitration decisions, there is little need to require something akin to a trial court order and reasons for judgment. Litigators should know, however, that if clients see arbitration as merely a first step toward eventual litigation, written decisions should be required and requested. Otherwise, the arbitrator's reasons for reaching the decision that he or she did are inscrutable and are extremely unlikely to be reversed.

The *Gueyffier* arbitrator did write a final award in which he expressly stated that he found that the notice-and-cure provision of the contract had been rendered moot by Ann

Summers's actions. Gueyffier was awarded over $650,000 in damages. Ann Summers immediately appealed to the trial court, which in due course affirmed the arbitrator's award. Ann Summers then appealed further to the California Court of Appeal, which surprised many by reversing the trial court and finding that the arbitrator had in fact exceeded his authority.[8]

Simply put, the appellate court decided that the "no modification or change" provision in the arbitration agreement prevented the arbitrator from finding that a contractual obligation did not have to be complied with. In making this finding, the appellate court relied heavily on *O'Flaherty v. Belgum*.[9] In *O'Flaherty*, the court of appeal also reversed an arbitration award by concluding that an arbitrator exceeded his powers under the contract. In that case, the contract limited the arbitrator in his choice of remedies (he was only allowed to award remedies available either under the terms of the contract itself or in a court of law). The *O'Flaherty* court decided that the arbitrator's decision was not supported by either the terms of the contract or California case law and, therefore, the award represented an act that fell outside the arbitrator's power.

The problem was that the *O'Flaherty* and *Gueyffier* appellate court opinions both appear to contradict or at least severely constrain the supreme court's prior rulings, including *Moshonov v. Walsh*, that deferred to the decisions and interpretations of arbitrators about the scope of their powers under the arbitration agreement. In the *Moshonov* opinion, for example, the supreme court affirmed an arbitrator's decision not to award attorney's fees to the prevailing party. The contract in question called for an award of attorney's fees to the prevailing party. The arbitrator, however, determined that this provision did not apply to the award in question, and accordingly refused to award attorney's fees. The supreme court upheld this decision, noting: "Interpretation of the contract underlying this dispute being within the matter submitted to arbitration, such an interpretation could amount, at most, to an error of law on a submitted issue, which we have held is not in excess of the arbitrator's powers...."[10] This raises a question: Is an arbitrator able to employ equitable principles when determining whether otherwise controlling contractual provisions apply to the facts at hand? *Moshonov* suggests the answer is yes, but *O'Flaherty* and the court of appeal's *Gueyffier* opinion indicate that no, this is not an option.

Seeking resolution of this issue, Gueyffier appealed to the state supreme court, which sided with the arbitrator and the trial court and reversed the court of appeal. The supreme court found that the excuse of a contractual

obligation is inherently different from a change in that obligation. The no-modification clause did not work to bar the arbitrator from deciding that the notice-and-cure provision was simply inapplicable on the facts of the case as he found them. "The arbitrator was empowered to interpret and apply the parties' agreement to the facts he found to exist; included therein was the power to decide when particular clauses of the contract applied."[11] The supreme court insisted that an actual change in a clause by the arbitrator would have been erroneous. For example, they noted that if the notice-and-cure requirement had been changed by the arbitrator from 60 days to 30 days, this would constitute a change of a term. But excusing the entire notice-and-cure provision altogether was not actually a change.

According to this opinion, a change or modification of contract terms only transpires if express, definite terms of the contract are altered to read something else. Arbitrators must apply the terms of the contract as they are presented, no matter how bizarre or egregiously one-sided those terms may prove to be. As the *Gueyffier* opinion recognizes, arbitrators are not merely fact finders. This, in fact, is likely what the court of appeal in *Gueyffier* and in *O'Flaherty* got wrong. These opinions suggest that there is no room in arbitration for an arbitrator to do anything other than apply the facts to the terms of the contract. This is an oversimplification of an arbitrator's role. The supreme court in *Gueyffier* recognized that simple application of factual scenarios to contract terms is not the only thing that arbitrators are faced with. There will be instances in which a contract cannot or should not be applied as written.[12] In those situations, unless the arbitration provision expressly prohibits it, an arbitrator is automatically granted a reasonable amount of discretion and equitable power. Of course, parties can contract to limit or eliminate even that, but unless such limitation is specifically mentioned in the arbitration agreement, the courts will allow a decision based on that discretion or equitable remedy to stand.

As the supreme court itself noted, this entire debacle could have been avoided had the arbitration provision simply limited the scope of the arbitrator's powers so that he could not base his decision on an excuse of any contractual term. When parties fail to make an explicit limitation of the equitable powers of arbitrators, the supreme court has directed that the arbitrator can and will move beyond simple application of the facts in dispute to the terms of the contract.

Careful Drafting

Gueyffier is a lesson in careful writing of the arbitration agreement. The supreme court in

fact made a lesson out of *Gueyffier,* noting that the entire dispute could have been avoided had the arbitration provision included one more clause. That is, instead of simply limiting the arbitrator from modifying or changing any term of the contract, the parties could have agreed in advance to prevent the arbitrator from "modifying, changing, or *excusing performance*" of any material term of that contract. With those two additional words in the contract, the outcome of the matter would have been entirely different.

The *Gueyffier* arbitrator was able to use his own judgment as a sort of on-off switch that he alone controlled. "The arbitrator was empowered to interpret and apply the parties' agreement to the facts he found to exist; included therein was the power to decide when particular clauses of the contract applied."[13] In essence, once the contract was switched on, all of its provisions and demands had to be met. However, if the relevant contract provision was turned off, the parties' compliance with or breach of this provision was irrelevant to the arbitrator's decision. And the arbitrator was holding the switch.

Gueyffier offers clear insight on how courts will treat arbitration decisions as well as how important it is to craft an arbitration agreement. At the onset of a dispute, courts may allow parties to avoid arbitration,[14] but once arbitration is invoked, courts are extremely loathe to reverse or even scrutinize the decisions of arbitrators. If there is any way for an arbitrator to have reached his or her decision while somehow complying with the limitations of authority as set forth in the arbitration agreement, the court will defer to this decision and will not reverse it for either factual misunderstandings or clear legal error.

Construction of an arbitration provision is vitally important. If, for example, parties to a contract must absolutely depend on the fulfillment of certain obligations, an arbitration provision must not allow for the excuse of such provisions, in any situation, even in those where equity would normally excuse performance. On the other hand, if clients hope to protect themselves from bizarre or unforeseen circumstances that make fulfillment of contractual obligations impossible, the ability of an arbitrator to turn to equitable principles should be incorporated into the arbitration provision that sets out the scope and limits of the arbitrator's authority.

Little can be done in litigation once an arbitration decision is rendered. The decisive steps occur when the arbitration provision is drafted and when the arbitrators are chosen. Unlike litigation, which to a certain extent is always under the control of the higher courts, arbitration can really only be effectively directed from the ground up. Parties who agree to binding arbitration are ceding their constitutional rights to a jury trial and appeal. Once attorneys have to begin to search for a means to overturn an arbitration decision, the battle may already have been lost.

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[1] *See, e.g.,* Abramson v. Juniper Networks, Inc., 115 Cal. App. 4th 638, 662-63 (2004).
[2] *See, e.g.,* Moshonov v. Walsh, 22 Cal. 4th 771, 775-76 (2000).
[3] *See* Azteca Const., Inc. v. ADR Consulting, Inc., 121 Cal. App. 4th 1156, 1168 (2004).
[4] CODE CIV. PROC. §§1281, 1281.2(b).
[5] *See* Advanced Micro Advances, Inc. v. Intel Corp., 9 Cal. 4th 362, 372-75 (1994).
[6] Gueyffier v. Ann Summers, Ltd., 43 Cal. 4th 1179 (2008).
[7] *Id.* at 1183.
[8] Gueyffier v. Ann Summers, Ltd., 144 Cal. App. 4th 166 (2006).
[9] O'Flaherty v. Belgum, 115 Cal. App. 4th 1044 (2004).
[10] *See* Moshonov v. Walsh, 22 Cal. 4th 771, 779 (2000).
[11] Gueyffier, 43 Cal. 4th at 1185.
[12] This is recognized in case law that allows for equitable excuse of contract obligations. *See, e.g.,* O'Morrow v. Borad, 27 Cal. 2d 794, 800 (1946); Root v. American Equity Specialty Ins. Co., 130 Cal. App. 4th 926, 939 (2005); Russell v. Johns Manville Co., 20 Cal. App. 3d 405, 413 (1971).
[13] Gueyffier, 43 Cal. 4th at 1185.
[14] *See, e.g.,* Gatton v. T-Mobile USA, Inc., 152 Cal. App. 4th 571, 579 (2007).