

# Another Exception for Judicial Review of Arbitration Awards

By John A. Taylor Jr. and Jeremy B. Rosen

Almost two decades ago, in *Moncharsh v. Heily & Blase*, 3 Cal. 4th 1 (1992), the California Supreme Court held that under the California Arbitration Act (CAA), a court is not permitted to vacate an arbitration award based on errors of law by the arbitrator (with certain narrow statutory exceptions). That holding was considered virtually inviolable until two years ago, when one member of the Court observed that “it is arguably the case that [in *Moncharsh*] the [C]ourt went too far in emphasizing arbitral finality at the expense of obtaining a just and reasonable result.” *Cable Connection Inc. v. DIRECTV Inc.*, 44 Cal. 4th 1334, 1374 (2008). The majority in *Cable Connection* found an exception to *Moncharsh* and held that judicial review of arbitration awards based on legal error is permissible where the arbitration agreement itself provides for such review.

Recently, in *Pearson Dental Supplies Inc. v. Superior Court*, 48 Cal. 4th 665, 669 (2010), the Supreme Court created yet another exception to *Moncharsh*, this time permitting judicial review of an arbitration award that would deprive an employee of a hearing on the merits of “an unwaivable statutory claim.”

In *Pearson Dental*, the plaintiff sued his employer, alleging age discrimination in violation of California’s Fair Employment and Housing Act (FEHA). *Pearson Dental* successfully moved to compel arbitration based on an arbitration agreement it had discovered in the plaintiff’s personnel file.

*Pearson Dental* then asked the arbitrator to grant summary judgment based on an arbitration agreement provision requiring any dispute to be submitted to binding arbitration within one year after it arose. The arbitrator granted the motion, but the trial court subsequently vacated the arbitration award, ruling that the arbitrator had made a clear error of law in failing to apply the tolling provisions of California Code of Civil Procedure Section 1281.12.

The Court of Appeal reversed, reinstating the arbitration award. Although agreeing that the arbitrator had misapplied the tolling period provided by Section 1281.12, the court held that the arbitrator’s decision “is insulated from judicial review” and that legal error “is not a proper basis upon which either to deny confirmation of the arbitration award or to vacate the award.” The appellate court also rejected the argument that the one-year limitation period in the arbitration agreement was unconscionable.

The California Supreme Court granted review. In his 4-3 majority opinion, Justice Carlos R. Moreno quickly dispatched the question whether the arbitrator had committed a clear error of law, finding he had misapplied the tolling provisions of Section 1281.12. The Court then turned to whether that legal error provided a basis for the trial court to vacate the award.

Reexamining *Moncharsh*, the Supreme Court cited language recognizing “that there may be some limited and exceptional circumstances justifying judicial review of an arbitrator’s decision” such as when “granting finality to an arbitrator’s decision would be inconsistent with the protection of a party’s statutory rights.” The Court also noted that in a later case, *Armendariz v. Foundation Health Psychcare Services Inc.*, 24 Cal. 4th 83 (2000), involving a FEHA claim, it had held that arbitration agreements in the employment context “cannot be made to serve as a vehicle for the waiver of statutory rights created by the FEHA” and “that a party to such an arbitration agreement must be able to fully vindicate his or her statutory cause of action in the arbitral forum.” To ensure such vindication, *Armendariz* held that, among other things, there must be a written arbitration decision and judicial review that is sufficient to ensure the arbitrators have complied with the requirements of the FEHA.

Turning to the facts before it in *Pearson Dental*, the Supreme Court rejected the argument that “all *Armendariz* requires is a written arbitral award.” Instead, the Court held that as a result of the arbitrator’s clear legal error, the plaintiff was unable to receive a hearing on the merits of his FEHA claim in any forum, which “would be inconsistent with the protection of a party’s statutory rights.” The Court concluded that where an arbitration award’s legal error deprives an employee of a hearing on the merits of his FEHA claims (or other claims based on unwaivable statutory rights), a trial court may vacate the award on the basis of that legal error.

Interestingly, the Supreme Court had held in *Moncharsh* that judicial review of arbitration awards for legal error could not be based on the rationale that an arbitrator has exceeded his or her powers within the meaning of Section 1286.2(a)(4) of the Code of Civil Procedure when the legal error appears on the face of the award, since “[i]t is well settled that ‘arbitrators do not exceed their powers merely because they assign an erroneous reason for their decision.’” But at the end of its analysis in *Pearson Dental*, that is precisely the statutory provision cited by the Court for permitting judicial review of arbitration awards in the FEHA context: “[A]n arbitrator whose legal error has barred an employee subject to a mandatory arbitration agreement from obtaining a hearing on the merits of a claim based on such right has exceeded his or her powers within the meaning of Code of Civil Procedure Section 1286.2, subdivision (a)(4), and the arbitrator’s award may properly be vacated.”

The Supreme Court also held that the language in the arbitration agreement requiring the plaintiff to submit his claims to binding arbitration and limiting resort to an administrative forum did not render the arbitration agreement unconscionable or unenforceable.

Three justices, in a concurring and dissenting opinion authored by Justice Marvin R. Baxter, joined the majority in holding that the arbitration agreement itself was not unconscionable or unenforceable. However, they questioned the remainder of the majority’s decision on a variety of grounds, including that it appears to provide only a one-way street for judicial review of arbitration awards, allowing employees to seek review of adverse arbitration decisions on the basis of legal error, but not allowing any similar exception to *Moncharsh*’s general rule of non-reviewability as

to arbitration awards that wrongly favor employees.

So what are the implications of *Pearson Dental* for the arbitration of disputes, particularly in the employment context? First, *Pearson Dental* makes clear that arbitration agreements can be used by California employers to require employees to submit FEHA (and similar) claims to binding arbitration rather than for adjudication by an administrative entity such as the Labor Commissioner or through a damages action in court.

Second, *Pearson Dental* reflects a growing divide between the CAA and the Federal Arbitration Act (FAA). As held in *Cable Connection*, parties to an arbitration agreement governed by the CAA may provide for judicial review based on legal error in the agreement, whereas the U.S. Supreme Court has reached a contrary conclusion regarding agreements governed by the FAA. See *Hall Street Assocs. L.L.C. v. Mattel Inc.*, 552 U.S. 576 (2008). Parties drafting arbitration agreements will want to think carefully about the advantages and disadvantages of judicial review in determining whether the agreement should be governed by the CAA or the FAA.

Finally, despite Justice Baxter’s pessimism on the subject, employer defendants in future cases should continue to examine whether the principles explored in *Armendariz* and *Pearson Dental* provide employers with the same latitude as employees to seek judicial review of adverse arbitration decisions under FEHA. The majority opinion did not directly address this question, and much of the rationale used to justify the holding for an employee could arguably be used in lower courts to support similar arguments for employers. Likewise, the rationale for affirming review to protect FEHA claims could be used where other important statutes are implicated, either within or outside the employment context.



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