Substantially broadening parties' rights in arbitration, the California Supreme Court has held that an arbitration agreement may expressly provide for judicial review of the merits of the arbitrator's decision. *Cable Connection, Inc. v. DirectTV, Inc.*, No. S147767 (Cal. Aug. 25, 2008). The Court based its ruling on the express language of the parties’ agreement, finding that it could be enforced through the California Arbitration Act’s provision that permits review of arbitration decisions where “[t]he arbitrators exceeded their powers.” Accordingly, the Court reversed the judgment of the Court of Appeal and directed the matter to be returned to arbitration for further proceedings.

The defendant, a satellite television broadcaster, contracted with retailers, pursuant to written sales agreements, to provide customers with satellite equipment. The agreements included arbitration clauses which provided, in relevant part, that “the 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.” The agreements were silent regarding class arbitration, but provided that California substantive law should apply to the proceedings.

A group of retailers sued the defendant in a nationwide class action for alleged unpaid commissions and improper charges. The defendant moved to compel arbitration, and the trial court granted the motion. The parties proceeded to arbitrate the dispute. Following briefing and argument, a majority of the arbitration panel ruled that the class arbitration was permitted, although not required, by the agreement. The defendant appealed. It argued, among other things, that the award reflected errors of law that the arbitration clause placed beyond the arbitrators' powers and made these errors subject to judicial review. The trial court vacated the award, but the Court of Appeal reversed, holding that the judicial review provision was unenforceable. The California Supreme Court granted the petition for review.

The Court noted first that, under the CAA, arbitration agreements are “valid, enforceable and irrevocable, save upon such grounds as exist for the revocation of any contract.” Cal. Civ. Proc. § 1281. Further, the CAA provides only limited grounds for judicial review of an arbitration award, such as fraud, corruption, misconduct, or that the award exceeded the arbitrators’ powers. Cal. Civ. Proc. § 1286.2. The Court then noted that, in prior cases interpreting the CAA, it ruled, “[i]n the absence of some limiting clause in the arbitration agreement, the merits of the award, either on questions of fact or of law, may not be reviewed except as provided in the statute.” *Moncharsh v. Helly & Blase*, 3 Cal. 4th 1 (Cal. 1992).

Here, however, the court examined the arbitration agreement and found that it had a “limiting clause.” The parties had agreed to limit the arbitrator’s powers by prohibiting the arbitrator from committing “errors of law or legal reasoning.” As a result of this “limiting clause,” an express restriction on the arbitrator's powers, the Court recognized that the parties could seek to have the arbitrator's decision reviewed pursuant to the CAA’s provision that the award exceeded the arbitrator's powers. Accordingly, the Court held that the provision was enforceable under California law, reversed the contrary ruling of the Court of Appeal, and remanded the case to arbitration.

As a result of this significant decision, parties to arbitration agreements in California now have grounds for court enforcement of judicial review clauses. Businesses seeking to include such provisions in arbitration agreements should consult with counsel to review the benefits and risks of
inclusion. One of the key benefits to arbitration, like other forms of alternate dispute resolution, is its relative speed and finality. By including judicial review provisions in arbitration agreements, parties open themselves to possible prolonged judicial proceedings — the costs and risks of which may outweigh the benefits of arbitration in the first instance.

“There definitely are competing interests in deciding whether to include a judicial review provision in an arbitration agreement,” said Mark Askanas, a partner in Jackson Lewis’ San Francisco office. “On the one hand, such provisions may be at odds with the notion that arbitration is a speedy, binding and cost efficient alternative to litigation. On the other hand, without such a provision, the losing party has absolutely no recourse where an award violates the law, because legal error usually is not a basis for overturning an arbitrator’s result. The employer needs to weigh these competing interests in making a decision as to what is right for that company.”

Employers, particularly those outside of California, will want to be cautious in implementing a judicial review provision, as it will likely render the Federal Arbitration Act unavailable as a vehicle for enforcing the agreement to arbitrate.

Jackson Lewis counsels employers in all aspects of alternative dispute resolution, from creating, designing and evaluating pre-dispute issue resolution procedures to training management, coordinating implementation, and assessing effectiveness.