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Judicial Review of International Commercial Arbitral Awards by National Courts in the United States and India

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**JUDICIAL REVIEW OF INTERNATIONAL COMMERCIAL ARBITRAL AWARDS BY
NATIONAL COURTS IN THE UNITED STATES AND INDIA**

By

APARNA DEVI JUJJAVARAPU

(Under the Direction of Professor Gabriel M. Wilner)

ABSTRACT

Article V of the New York convention lays down the provisions under which the recognition and enforcement of an arbitral award may be refused. The United States and India are signatories to the Convention. Section 10(a) of the Federal Arbitration Act in the United States limits the scope of judicial review of the arbitral awards to a clear list of grounds of vacatur. The national courts of the United States have recognized several non-statutory grounds of which "manifest disregard of the law" as a standard of review is the focus in this thesis. In fact, the state of Georgia has also adopted this ground into its statute in 2003. Section 34 of the Indian Arbitration and Conciliation Act of 1996 lays down the provisions for setting aside arbitral awards of which the ground of 'public policy' has been interpreted by the Supreme Court of India broadening its scope to include 'patent illegality' which essentially meant "error of law" as a new ground for setting aside an arbitral award. Scope of judicial review by national courts, both in the United States and in India, should be limited to the statutory provisions so as to not frustrate the purpose of arbitration.

INDEX WORDS: Setting aside, Arbitral awards, New York Convention, Judicial Review, Federal Arbitration Act, public policy, manifest disregard of the law, Unites States, India, Indian Arbitration and Conciliation Act of 1996, patent illegality, error of law.

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B.A, M.L, University of Madras, India, 2000.

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CHAPTER I - International Commercial Arbitration - General Provisions for recognition and enforcement of Arbitral Awards

“By and large, parties to international transactions choose to arbitrate eventual disputes *not* because arbitration is simpler than litigation, *not* because it is cheaper, *not* because arbitrators may have greater relevant expertise than national judges, although any one of those factors maybe of interest; they arbitrate simply because neither will suffer its rights and obligations to be determined by the courts of the other party’s state of nationality.”¹

Introduction

With the explosive globalization of trade and investment, there has been a corresponding increase in commercial disputes between parties across national boundaries.² International arbitration is being increasingly sought after as the best mode of alternative dispute resolution in such commercial disputes.

Arbitration offers a number of advantages over litigation. In fact, even if an agreement to arbitrate does not already exist when a dispute arises, the parties may still agree to submit the dispute to arbitration for resolution and take advantage of the benefits that arbitration affords.³ This thesis focuses upon the judicial review of international commercial arbitral awards by national courts both in the United States and India in terms of their recognition and enforcement,

¹ INTERNATIONAL ARBITRATION IN THE 21ST CENTURY: TOWARDS “JUDICIALIZATION” AND UNIFORMITY? Introduction at x [Twelfth Sokol Colloquium] (R.Lilich & C.Brower eds., 1993).

² Earl McLaren, *Effective use of International Commercial Arbitration: A Primer for In-house Counsel*, 19 J. INT’L ARB. 473, 473 (2002).

³ *Id.* at 474.

where the courts have gone beyond the statutory scope of review and have attempted to either review or set aside arbitral awards on non-statutory standards such as the “manifest disregard of the law” in the United States or “error of law” in India. In this thesis, an attempt has been made to analyze the judicial decisions by various national courts in the United States and India (updated until September 2007) so as to highlight the latest trend in judicial review of arbitral awards. The scope of the ‘public policy’ defense employed in the United States for setting aside arbitral awards has been first discussed, following which the general trend of the national courts going beyond the scope of the statutory grounds in reviewing arbitral awards under the “manifest disregard of law” is discussed in detail. The state of Georgia in the United States has, in fact, adopted this standard of review in its statute in 2003 which has paved the way for courts in Georgia to freely interpret the arbitral awards and for parties to seek review under the statute itself. This thesis then proceeds to explain the scope of ‘public policy’ laid down in India by its Supreme Court initially and the Court’s subsequent review of the ‘public policy’ defense in 2003, broadening it to include ‘patent illegality’, which essentially meant ‘error of law’ as a standard for setting aside arbitral awards. The thesis concludes with a few observations on this trend of review by national courts both in the United States and in India while setting out that in order to preserve the scope and purpose of arbitration, it is desirable that the national courts desist from broadening the scope of judicial review beyond the statutory principles set out in the arbitration laws of the respective countries.

A. Advantages of International Arbitration

Arbitration can be a superior or an inferior alternative to litigation, depending on the circumstances of the case. Some of the advantages most often associated with international arbitration are:⁴

- 1) Flexible process;
- 2) Neutral forum;
- 3) Confidentiality;
- 4) Specialized Tribunal;
- 5) Finality and Enforcement; and
- 6) Cost.

Though all of the above advantages are self-explanatory, “Finality and Enforcement” is perhaps most relevant and is discussed in detail with reference to the recognition and enforcement of arbitral awards.

B. Recognition and Enforcement of Arbitral Awards

The recognition and enforcement of an award has always been understood to be separate from the making of the award itself, the reason being, the award is given by an arbitrator whose authority is based on the contract between the parties and who does not possess the authority of the State.⁵ Further, the international treaties that govern the enforcement of an arbitral award, such as the New York Convention,⁶ have much greater acceptance internationally than treaties

⁴ *Id.*

⁵ V.S Deshpande, *Enforcement of Foreign Awards in India, U.K and U.S.A*, 4 J. INT'L ARB., 41, 53 (1987).

⁶ Convention on the Recognition and Enforcement of Foreign Arbitral Awards, art. V, 7 June 1959, 21 U.S.T. 2517, 330 U.N.T.S. 38, (effective in the United States on December 29, 1970) (hereinafter “the New York Convention”).

for the reciprocal enforcement of court judgments.⁷ Indeed, the United States, which is a party to the New York Convention, “is not a party to a single treaty providing for enforcement of foreign judgments.”⁸ Article V of the New York Convention lays down the provisions under which the recognition and enforcement of an arbitral award may be refused under the Convention, which are set out hereunder.

C. New York Convention - Article V

1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority, where the recognition and enforcement is sought, proof that:

(a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or

(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

⁷ McLaren, *supra* note 2, at 475.

⁸ *Id.*

(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or

(e) The award has not yet become binding, on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.

2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:

(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or

(b) The recognition or enforcement of the award would be contrary to the public policy of that country.⁹

⁹ Art V of The New York Convention.

CHAPTER II - Review of Arbitral Awards in the United States - Statutory Provisions

Commercial arbitration in the United States has continued to evolve and has continued to gain importance as compared to litigation. As the evolution unfolds, several important questions have emerged, the answers to which will do much to shape the nature, character, and viability of commercial arbitration in the future.¹⁰ The most important among these questions is the proper standards for judicial review of commercial arbitration awards.

A. Scope of ‘Public Policy’ defense under Article V 2(b) of the New York Convention

Article V(1) contains a list of general defenses to enforcement of arbitral awards. Article V(2) contains two additional defenses: the “in arbitrability” defense and “public policy” defense. The approach of federal courts in the United States to the arguments made under Article V 2(b) that foreign arbitration awards should not be enforced when they violate public policy could be understood from the following four Supreme Court decisions, which involve international commercial agreements containing forum selection clauses that provided for the resolution of disputes in a forum outside the United States.¹¹

The Supreme Court in 1972 in *M/S Bremen v. Zapata Off-Shore Co.*¹² upheld a forum selection clause in an agreement between an American oil company and a German towing firm.

¹⁰ Stephen L. Hayford, *Law in Disarray: Judicial Standards for Vacatur of Commercial Arbitration Awards*, 30 GA. L.REV. 731, 734 (1996).

¹¹ Andrew M. Campbell, *Refusal to Enforce Foreign Arbitration Awards on Public Policy Grounds*, 144 A.L.R. FED. 481 (1998).

¹² 407 U.S. 1 (1972)

Two years later in *Scherk v. Alberto-Culver Co.*,¹³ the Court again upheld a forum selection clause providing for arbitration of disputes. Subsequently, the Supreme Court in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,¹⁴ held that a provision in an agreement providing for the arbitration before arbitrators in Japan of disputes arising out of an automobile dealership agreement was enforceable, even though it covered anti-trust claims under United States laws. The Court concluded that the concerns of international comity, respect for the capacities of foreign and transnational tribunals and sensitivity to the need of the international commercial system for predictability in the resolution of disputes required that it enforces the parties' agreement, even assuming that a contrary result would be forthcoming in a domestic context because of the traditional view that anti-trust claims are not subject to arbitration.¹⁵ However, the dissent by Justice Stevens in this case was very strong. He stated that, "vague concerns over comity were not to outweigh public policy."¹⁶ He distinguished the *Mitsubishi Motors* case from *Scherk* as the facts in *Mitsubishi Motors* did not involve foreign laws and were totally under the realm of U.S. antitrust laws.¹⁷ He pointed out that Congress did not authorize the transfer of decision-making authority of statutory claims from courts to the arbitrators,¹⁸ and noted that under the New York Convention, "agreements requiring arbitration of disputes that were non-arbitrable under domestic law were not to be honored".¹⁹ The *Mitsubishi Motors* case is a clear example of how the Supreme Court sacrificed public policy in the name of international comity. Finally, the Supreme Court in *Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*,²⁰ in an arbitration regarding a bill of lading, stated that any dispute arbitrated in Japan under Japanese

¹³ 417 U.S. 506 (1974)

¹⁴ 105 S. Ct. 3346 (1985).

¹⁵ *Id.*

¹⁶ *Id.* at 3365 (Stevens, J., dissenting).

¹⁷ *Id.* at 3373.

¹⁸ *Id.* at 3364.

¹⁹ *Id.* at 3371.

²⁰ 515 U.S. 528 (1995)

law was enforceable under the Federal Arbitration Act²¹ notwithstanding the argument that it reduced the liabilities of the carrier in violation of the Carriage of Goods by Seas Act because it would be more difficult for the owner of the cargo to sue the shipper in Japan than it would be elsewhere. The federal courts have echoed the Supreme Court's emphasis on the importance of avoiding a parochial viewpoint in their enforcement of foreign arbitral awards by enforcing them despite claims that the arbitration procedures violated United States public policy in various ways.²²

Currently, U.S. law does not require commercial arbitrators to set forth their reasons for their decision in a written award.²³ Earlier, federal courts had continuously held that absence of express reasoning by the arbitrators does not warrant vacatur of the arbitral award.²⁴ Nevertheless, in recent years, particularly since the mid-1980s, there is evidence of an increasing willingness by the federal courts to look behind commercial arbitration awards in an effort to ascertain whether the arbitral reasoning which lead to that result is so flawed by grave errors of law, fact, or contract interpretation as to warrant its vacatur by a reviewing court.²⁵

B. Federal Arbitration Act of the United States – Section 10(a)

The Federal Arbitration Act (FAA) was passed by the Congress in 1925²⁶ in the wake of agitation and pressure from the business-led reform movement against the costliness and delay of

²¹ United States Arbitration Act, Pub. L. No. 68-401, 43 Stat. 883 (1925) (codified as amended at 9 U.S.C. §§ 1-307 (2000)).

²² See Campbell, *supra* note 11.

²³ Bernhardt v. Polygraphic Co. of America, 350 U.S. 198, 204 n.4 (1956) [“(A)rbitrators need not disclose the facts or reasons behind their award”].

²⁴ French v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 784 F.2d 902, 907-08 (9th Cir. 1986).

²⁵ See Hayford, *supra* note 10 at 735.

²⁶ United States Arbitration Act, Pub. L. No. 68-401, 43 Stat. 883 (1925) (codified as amended at 9 U.S.C. §§ 1-307 (2000)).

litigation.²⁷ While enacting the FAA, Congress recognized the need for finality of arbitration awards and therefore limited the scope of judicial review of arbitral awards to a clear list of grounds of vacatur.²⁸ Section 10(a) of the FAA sets out the following grounds upon which a commercial arbitration award may be vacated:

In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration-

- (1) Where the award was procured by corruption, fraud, or undue means.
- (2) Where there was evident partiality or corruption in the arbitrators, or either of them.
- (3) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced.
- (4) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.
- (5) If an award is vacated and the time within which the agreement required the award to be made has not expired, the court may, in its discretion, direct a rehearing by the arbitrators.²⁹

²⁷ Brent S. Gilfedder, "A Manifest disregard of Arbitration?" *An analysis of recent Georgia legislation adding "manifest disregard of the law" to the Georgia Arbitration Code as a statutory ground for vacatur*, 39 GA. L REV. 259, 269 (2004).

²⁸ *Id.*

²⁹ 9 U.S.C. § 10(a) (2000).

C. Uniform Arbitration Act - Section 23(a)

The National Conference of Commissioners on Uniform State Laws promulgated the Uniform Arbitration Act (UAA) in 1955.³⁰ By far the UAA has been one of the most successful uniform laws to date as over thirty-five states have adopted it in its entirety and fourteen more use it as a model for their state arbitration acts.³¹ The UAA was designed for the same reasons as the FAA—to ensure the enforceability and finality of arbitration agreements and to overcome state judicial hostility³²—and, in fact, the drafters of the UAA used the FAA as a model.³³ The drafters revised the Uniform Arbitration Act in 2000³⁴ in order to deal with the increased use of arbitration, greater complexities of underlying arbitration disputes, and intervening changes in arbitration law.³⁵ The statutory grounds for vacatur under the revised UAA are found in Section 23.³⁶ Section 23(a) provides:

Upon [motion] to the court by a party to an arbitration proceeding, the court shall vacate an award made in the arbitration proceeding if:

(1) the award was procured by corruption, fraud, or other undue means;

³⁰ See Gilfedder, *supra* note 27, at 269.

³¹ See generally Stephen J. Ware, "Opt-in" for Judicial Review of Errors of Law under the Revised Uniform Arbitration Act, 8 AM. REV. INT'L ARB. 263 (1999) (noting Uniform Arbitration Act is one of most successful uniform laws ever and discussing changes made in Revised Uniform Arbitration Act).

³² *Id.*

³³ Timothy J. Heinsz, *The Revised Uniform Arbitration Act: Modernizing, Revising, and Clarifying Arbitration Law*, J. DISP. RESOL. 1 (2001).

³⁴ See Unif. Arbitration Act §§ 1-23 (amended 2000), 7 U.L.A. 6 (Supp. 2004).

³⁵ See Heinsz, *supra* note 33, at 2. The Drafting Committee sought to accomplish three main goals through the Revised Uniform Arbitration Act (RUAA): 1. Because arbitration is at heart a consensual process, the RUAA gives party autonomy primary consideration 2. Many parties choose arbitration because of its relative speed, lower cost, and greater efficiency. The RUAA intends to give these factors sufficient weight whenever possible. 3. In most cases, parties intend the arbitrators' decisions to be final with little or no court involvement unless there is clear unfairness or denial of justice. The RUAA recognizes this contractual nature of arbitration by limiting the grounds on which a court may review an arbitrator's award. *Id.*; see also Unif. Arbitration Act Prefatory Note (amended 2000), 7 U.L.A. 2 (Supp. 2004) (stating similar goals for revisions to UAA).

³⁶ Unif. Arbitration Act § 23(a) (amended 2000), 7 U.L.A. 46 (Supp. 2004).

(2) there was: (A) evident partiality by an arbitrator appointed as a neutral arbitrator; (B) corruption by an arbitrator; or (C) misconduct by an arbitrator prejudicing the rights of a party to the arbitration proceeding;

(3) an arbitrator refused to postpone the hearing upon showing of sufficient cause for postponement, refused to consider evidence material to the controversy, or otherwise conducted the hearing contrary to Section 15, so as to prejudice substantially the rights of a party to the arbitration proceeding;

(4) an arbitrator exceeded the arbitrator's powers;

(5) there was no agreement to arbitrate, unless the person participated in the arbitration proceeding without raising an objection under Section 15(c) not later than the beginning of the arbitration hearing; or

(6) the arbitration was conducted without proper notice of the initiation of an arbitration proceeding as required in Section 9 so as to prejudice substantially the rights of a party to the arbitration proceeding.³⁷

In essence the revised UAA focused towards preserving the integrity of the arbitration process by refusing vacatur merely because the "relief [granted by arbitration is] such that it could not or would not be granted by a court of law or equity."³⁸

³⁷ *Id.*

³⁸ See Unif. Arbitration Act, § 12(a), 7 U.L.A. 280-81 (1997); see also Amy J. Schmitz, *Ending a Mud Bowl: Defining Arbitration's Finality Through Functional Analysis*, 37 GA. L. REV. 123, 155-56 (2002) (recognizing foregone vacatur options where arbitrator acts on principles of fairness and equity in balancing parties' rights). An arbitrator's treatment of substantive law principles is untouched by the UAA just as it is in the FAA. See Murray S. Levin, *The Role of Substantive Law in Business Arbitration and the Importance of Volition*, 35 AM. BUS. L.J. 105, 108 (1997) (reiterating shallow pool for vacatur justification). The UAA implicitly denies recognition to "error of law" claims, even those that are egregious. *Id.* at 110.

When the drafting committee in 1997 assembled to review the UAA and current trends in state arbitration, a heated debate surrounded a new proposal that would have provided for vacatur if the parties "opted in" for review based on errors of law where a decision substantially prejudiced one party.³⁹ A similar conflict arose over the common-law application of the "manifest disregard of the law" standard employed by certain courts as a non-statutory basis to review arbitral awards.⁴⁰ Neither proposed provision gained inclusion into the Revised Uniform Arbitration Act (RUAA), leaving arbitration "a desirable alternative to litigation ... [without making] arbitration simply another form of litigation."⁴¹

Since the scope of this thesis is the "manifest disregard of the law" under the "non-statutory" standards of vacatur of arbitral awards in the United States, analysis under the above statutory provisions both under the FAA and RUAA are not discussed here.

³⁹ See Heinsz, *supra* note 33, at 27 (recognizing failure to revise UAA to include "opt in" error of law reviewability).

⁴⁰ *Id.* at 30 (mentioning past circuit and state court use of "manifest disregard of the law" non-statutory ground).

⁴¹ See RUAA Drafting Committee, Policy Statement: Revised Uniform Arbitration Act (RUAA) (May 15, 2000), <http://www.law.upenn.edu/bl/ulc/uarba/arb0500.htm> (expressing committee's desire to keep arbitration process efficient, expeditious, economical, fair, and final). The drafters determined that a new "manifest disregard" standard could overload the trial courts with arbitration award appeals and that no bright-line test for vacatur existed. Heinsz, *supra* note 33, at 34-35 (highlighting lack of clear standard for applying "manifest disregard of the law"). The RUAA does not prohibit challenges to arbitrator authority on these grounds; common law dictates if and when these non-statutory grounds may be used.

CHAPTER III - Review of Arbitral awards in the United States – Non-Statutory Provisions

In addition to the four statutory grounds articulated in section 10(a) of the FAA,⁴² several federal circuit courts of appeals have recognized one or more "non-statutory" grounds warranting vacatur of an otherwise valid commercial arbitration award. Primary among those non-statutory grounds is a "manifest disregard" of the law by the arbitrator, a conflict between the award and a clear and well established "public policy," an award that is "arbitrary and capricious" or "completely irrational," and a failure of the award to "draw its essence" from the parties' contract.⁴³

Only the Fourth Circuit has unequivocally rejected the non-statutory grounds for vacatur. In *Remmey v. PaineWebber, Inc.*,⁴⁴ the Fourth Circuit stated:

Courts are not free to overturn an arbitral result because they would have reached a different conclusion if presented with the same facts. In the Federal Arbitration Act, Congress has limited the grounds upon which an arbitral award can be vacated, namely, a court may vacate an award [on the basis of the four grounds set forth in section 10(a)]. The statutory grounds for vacatur permit challenges on sufficiently improper conduct in

⁴² 9 U.S.C. § 10 (2000).

⁴³ See Hayford *supra* note 10 at 739.

⁴⁴ 32 F. 3d 143 (4th Cir. 1994), cert. denied 115 S. Ct. 903 (1995).

the course of the proceedings; they do not permit rejection of an arbitral award based on disagreement with the particular result the arbitrators reached.⁴⁵

The Fourth Circuit case law has thus far followed the clear rule set down in *Remmey*. Accordingly, the Fourth Circuit falls to place in the "statutory-grounds-only" category.⁴⁶

It is clear that most of the federal circuit courts do not limit their scope of review of commercial arbitration awards to a strict reading of section 10(a) of the FAA.⁴⁷ These courts believe that they "retain a very limited power to review commercial arbitration awards outside of Section 10"⁴⁸ under several judicially created, non-statutory grounds for vacatur. The manner in which this judicially created power of review has been exercised by the several circuit courts that do not limit themselves to the section 10(a) statutory grounds for vacatur is the subject of discussion below.

A. "Manifest disregard of the Law" as a standard for reviewing arbitral awards

Despite the facial clarity of Section 10(a), all twelve U.S Circuit Courts of Appeals (save the Federal Circuit) have embraced one or more non-statutory grounds of vacatur.⁴⁹ Seminal among the non-statutory grounds for vacatur is the "manifest disregard" of the law standard, which was derived from the dictum in the United States Supreme Court's 1953 opinion in *Wilko v. Swan*.⁵⁰ Although Section 10 of the FAA⁵¹ does not contain the words, "manifest disregard of the law," courts have found that if an award is found to be in manifest disregard of the law, it can be

⁴⁵ 32 F. 3d 143, 146 (4th Cir. 1994).

⁴⁶ See Hayford *supra* note 10, at 764.

⁴⁷ See *Bowles Fin. Group, Inc. v. Stifel, Nicolaus & Co.*, 22 F.3d 1010 (10th Cir. 1994) ("Federal courts have never limited their scope of review [of an arbitration award] to a strict reading of 9 U.S.C. § 10") (alterations in original) (quoting *Jenkins v. Prudential Bache Sec., Inc.*, 847 F.2d 631, 633 (10th Cir. 1988)).

⁴⁸ *Advest, Inc. v. McCarthy*, 914 F. 2d. 6, 8 (1st Cir. 1990).

⁴⁹ Stephen L. Hayford, *Reining in the "Manifest Disregard" of the Law Standard: The Key to Restoring Order to The Law Of Vacatur*, J.DISP. RESOL. 117, 118 (1998).

⁵⁰ 346 U.S. 427 (1953).

⁵¹ 9 U.S.C. § 10 (2000).

vacated on judicial review.⁵² The First Circuit observed that, ‘Where a reviewing court is inclined to find that arbitrators’ reasoning, if given, would have strained credulity, the absence of explanation may reinforce the reviewing court’s confidence that the arbitrators engaged in manifest disregard.’⁵³

Thus, courts have vacated awards that show a “manifest disregard of the law,” directly conflict with “public policy”, are arbitrary and capricious.⁵⁴ The federal circuit courts of appeals, based on Supreme Court dicta, created the manifest disregard of the law standard.⁵⁵ While this standard has existed for many years, it has been applied infrequently.⁵⁶ One reason for this sporadic use is the difficulty in defining exactly what constitutes a manifest disregard of the law. This difficulty is illustrated by the federal U.S. circuit courts of appeals, which have been unable to fashion a uniform standard.⁵⁷ This lack of a clear definition or a clear method of application raises serious doubts as to how effective this standard can be in the judicial review of arbitration awards⁵⁸. In addition, what were the judiciary's original reasons for enacting these additional grounds for vacatur and whether they contradict the fundamental goals of the arbitration process are more questions that arise when considering expanded judicial review of arbitration awards.⁵⁹

⁵² See *Wilko v. Swan*, 346 U.S. 427 (1953); *Management Recruiters Intern., Inc. v. Bloor*, 129 F. 3d 851 (6th Cir. 1997) (stating that manifest disregard for the law, in contrast to misinterpretation, misstatement, or misapplication of law, can constitute grounds for vacating an arbitration decision).

⁵³ *PCS 2000 LP v. Romulus Telecommunications, Inc.*, 148 F. 3d 32 (1st Cir. 1998)

⁵⁴ See Stephen L. Hayford & Scott B. Kerrigan, *Vacatur: The Non-Statutory Grounds for Judicial Review of Commercial Arbitration Awards*, 51 OCT. DISP. RESOL. J. 22, 26-27 (1996) (discussing different nonstatutory grounds for vacatur that federal courts have fashioned).

⁵⁵ *Id.* at 26.

⁵⁶ See Hayford, *supra* note 54 at 29. (noting that as of 1998, there were only two cases where Federal Circuit Courts of Appeals had vacated commercial arbitration awards for manifest disregard of law).

⁵⁷ See *e.g.*, *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930, 933 (2d Cir. 1986) (stating that manifest disregard of law clearly means more than arbitral error or misunderstanding with respect to law); *Halligan v. Piper Jaffray, Inc.*, 148 F.3d 197, 204 (2d Cir. 1998) (applying manifest disregard of law standard when error is clearly discernible from record); *Montes v. Shearson Lehman Bros., Inc.*, 128 F.3d 1456, 1461-62 (11th Cir. 1997) (recognizing manifest disregard standard for first time in Eleventh Circuit and concluding "that a manifest disregard for the law, in contrast to a misinterpretation, misstatement or misapplication of the law, can constitute grounds to vacate an arbitration decision").

⁵⁸ See Gilfedder, *supra* note 27 at 261.

⁵⁹ *Id.*

B. Origin of the “manifest disregard of law” as a standard of review

1. *Wilko v. Swan*

The manifest disregard of the law standard first originated in the United States Supreme Court case of *Wilko v. Swan*.⁶⁰ This case involved a claim of fraud brought against a securities brokerage firm pursuant to the Securities Act of 1933.⁶¹ The respondent moved for a stay of trial pending the outcome of arbitration that the parties had agreed upon prior to entering into their contractual relationship to deal in securities.⁶² The district court denied the stay, but the second court of appeals reversed the judgment.⁶³ The United States Supreme Court’s reasoning displayed its traditional hostility toward arbitration.⁶⁴

In dicta, the Court stated: While it may be true that a failure of the arbitrators to decide in accordance with the provisions of the Securities Act would "constitute grounds for vacating the award pursuant to section 10 of the Federal Arbitration Act," that failure would need to be made clearly to appear. In unrestricted submissions, such as the present margin agreements envisage, the interpretations of the law by the arbitrators in contrast to *manifest disregard* are not subject, in the federal courts, to judicial review for error in interpretation.⁶⁵ The Supreme Court held that parties could not arbitrate issues relating to Securities law because of public policy concerns underlying the Securities Act of 1933 and because of the underlying concern about the

⁶⁰ 346 U.S. 427 (1953).

⁶¹ *Id.* at 428

⁶² *Id.* at 429

⁶³ *Id.* at 430

⁶⁴ *See Id.* at 435-436. The court stated: This case requires subjective findings on the purpose and knowledge of an alleged violator of the Act. They must be not only determined but applied by the arbitrators without judicial instruction on the law. As their award may be made without explanation of their reasons and without a complete record of their proceedings, the arbitrators' conception of the legal meaning of such statutory requirements as "burden of proof," "reasonable care" or "material fact." . . . cannot be examined.; see also *Southland Corp. v. Keating*, 465 U.S. 1, 14 (1984).

⁶⁵ 346 U.S. at 436-37 (*emphasis added*) (quoting *Wilko v. Swan*, 201 F.2d 439, 445 (2d Cir. 1953)).

in arbitrability of securities law issues.⁶⁶ That the Supreme Court's opinion in *Wilko v. Swan*⁶⁷ has, even after over fifty years, left the federal circuit courts of appeals in a state of confusion regarding the grounds on which a commercial arbitration award properly may be vacated is an understatement.⁶⁸

2. *Rodriguez de Quijas v. Shearson/American Express*

In 1989, the Supreme Court reversed *Wilko* in *Rodriguez de Quijas v. Shearson/American Express*.⁶⁹ The issue in *Rodriguez* as to “whether a pre-dispute agreement to arbitrate claims arising under the Securities Act of 1933 is unenforceable, requiring resolution of the claims only in a judicial forum”⁷⁰ centered on the very same question decided by the Court in *Wilko*. Here, the Supreme Court reversed its own precedent of some 36 years in this case by ignoring the rule of *Wilko* that section 12(2) claims under the 1933 Act were not arbitrable.

The Supreme Court's rejection of *Wilko* and the “old judicial hostility to arbitration”, which pervaded its former characterization of the commercial arbitration process, was founded on what the Court described as an “erosion” of generally held views over the years,⁷¹ as intensified by the Court's holdings in *Shearson/American Express v. McMahon*,⁷² *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*,⁷³ *Dean Witter Reynolds v. Byrd*,⁷⁴ and *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*⁷⁵ In particular, the *Rodriguez* Court focused on the

⁶⁶ *Id.* at 434-35

⁶⁷ *Id.* at 436, overruled by *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477 (1989).

⁶⁸ Brad A. Galbraith, Note, *Vacatur of Commercial Arbitral Awards in Federal Courts: Contemplating the Use and Utility of the “Manifest Disregard” of the Law Standard*, 27 IND. L.REV. 241, 249 (1993). (discussing the extent to which *Wilko* left lower courts in confusion about proper grounds for vacatur).

⁶⁹ 490 U.S. 477 (1989).

⁷⁰ *Id.* at 478.

⁷¹ *Id.* at 480-81.

⁷² 484 U.S. 220 (1987).

⁷³ 473 U.S. 614, 628 (1985).

⁷⁴ 470 U.S. 213 (1985).

⁷⁵ 460 U.S. 1 (1983).

statement in Mitsubishi that "by agreeing to arbitrate a statutory claim, a party does not forego the substantive rights afforded by the statute; it only submits their resolution to an arbitral, rather than a judicial forum."⁷⁶ The Court then stated emphatically: "to the extent that *Wilko* rested on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants, it has fallen far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes."⁷⁷

When it reversed *Wilko* in *Rodriguez*, the Court did not address the "manifest disregard" of the law dictum.⁷⁸ And in the 56 years since *Wilko*, the Supreme Court has never clarified the meaning and effect it attributes to the "manifest disregard" of the law standard.⁷⁹ Similarly, the Court has never clarified the manner in which the "manifest disregard" construct relates, if at all, to the statutory grounds for vacatur of commercial arbitration awards articulated in Section 10(a) of the FAA.⁸⁰ Because a majority of the Supreme Court has never spoken definitively to the continued viability of the "manifest disregard" of the law standard in light of *Rodriguez*, the question as to whether the *Wilko* dictum is still a proper basis for this and all of the other non-statutory grounds for vacatur remains open.⁸¹ Nevertheless, the broad acceptance of the

⁷⁶ *Rodriguez*, 490 U.S. at 481 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985)).

⁷⁷ *Id.* at 481-82.

⁷⁸ The "manifest disregard" standard has been mentioned in Supreme Court opinions only three times since 1953, always in dictum, always in passing, twice in dissent. In his dissent in *Mitsubishi Motors*, Justice Stevens noted, without further comment, "arbitration awards are reviewable for manifest disregard of the law." *Mitsubishi Motors*, 473 U.S. at 656 (1985). (Stevens, J., dissenting). In his concurring in part opinion in *Shearson/American Express v. McMahon*, 514 U.S. 938 (1995), Justice Blackmun observed: "judicial review is still substantially limited to the four grounds listed in § 10 of the [Federal] Arbitration Act and to the concept of 'manifest disregard' of the law." 482 U.S. 220, 259 (1987). The third reference by the Court to the *Wilko* manifest disregard dictum is found in a parenthetical phrase in the 1995 case, *First Options of Chicago v. Kaplan*, 514 U.S. 938 (1995).

⁷⁹ See Hayford, *supra* note 49, at 122.

⁸⁰ *Id.*

⁸¹ *Al-Harbi v. Citibank, N.A.*, 85 F.3d 680, 684 n.1 (D.C. Cir. 1996) ("Although the holding in *Wilko* was overruled by *Rodriguez de Quijas v. Shearson/American Express, Inc.*, the dicta that constitutes the core of appellant's argument [relying upon the 'manifest disregard of the law' ground for vacatur] was unaffected by the grounds of the overruling. ").

"manifest disregard" of the law ground by the U.S. circuit courts of appeals demonstrates they do not question its legitimacy and continued viability.⁸²

C. The Development of the “manifest disregard of the law” Standard

Most of the circuit courts of appeals have, in one way or other, reviewed arbitral awards based on the ‘manifest disregard’ of the law standard. Selected cases of the various circuits, showing the development of the “manifest disregard” standard, are discussed below:

First Circuit

The U.S. Court of Appeals for the First Circuit held in *Advest v. McCarthy*⁸³ that manifest disregard of the law entails a showing that the arbitrator "appreciated the existence of a governing legal rule but willfully decided not to apply it."⁸⁴

Later in *Bull H N Information Systems, Inc.*,⁸⁵ the First Circuit confirmed an award, which had been vacated by the District Court. With regard to the standards for setting aside awards, the Court held: Beyond the specific grounds enumerated in Section 10, courts “retain a very limited power to review arbitration awards”. Essentially, arbitration awards are subject to review “where an award is contrary to the plain language of the [contract]” and “instances where it is clear from the record that the arbitrator recognized the applicable law—and then ignored it”.⁸⁶ In the parlance of this and other circuits, a reviewing court may vacate an arbitration award if it was made in “manifest disregard” of the law.⁸⁷

⁸² See Hayford, *supra* note 49 at 122.

⁸³ 914 F. 2d. 6 (1st Cir. 1990).

⁸⁴ *Id.* at 10.

⁸⁵ Bull HN Information Systems, Inc., v. Charles J. Hutson, 229 F.3d 321 (1st Cir. 2000).

⁸⁶ *Id.*

⁸⁷ *Id.* at 331 (quoting *Advest, Inc. v. McCarthy*, 914 F.2d 6, 9 (1st Cir. 1990)).

Second Circuit

Initially the U.S. Court of Appeals for the Second Circuit was consistent with the other circuits following *Wilko* and *First Options in Merrill Lynch v. Bobker*⁸⁸ and *Willemijn Houdstermaatschappij, BV v. Standard Microsystems Corporation*.⁸⁹ However, in *Halligan v. Piper Jaffray*,⁹⁰ when considering an appeal from a district court decision that confirmed an award that denied relief to the petitioner, the court made an extensive review of the evidence at the arbitration hearing. The opinion cited reference to a lower court's statement that the record "does not indicate the Panel's awareness, prior to its determination, of the standards for burden of proof."⁹¹ The Second Circuit, without any other reference to disregard of a specific law, and after observing that the Panel made no explanation of its award, concluded: At least in the circumstances here, we believe that when a reviewing court is inclined to hold that an arbitration panel manifestly disregarded the law, the failure of the arbitrators to explain the award can be taken into account. Having done so, we are left with the firm belief that the arbitrators here manifestly disregarded the law or the evidence or both.⁹² In this case, the Second Circuit indicated for the first time that the consideration and weighing of the evidence by the Court could be factors in determining whether an award should be rejected under the manifest disregard standard.

Finally in *Westerbeke Corp. v. Daihatsu Motor Co.*,⁹³ the Second Circuit set forth its own two-prong test⁹⁴ that an arbitrator first must be aware of the well-defined, explicit applicable law and then must have ignored it completely.⁹⁵

⁸⁸ 808 F.2d 930 (2d Cir. 1986).

⁸⁹ 103 F.3d (2d Cir. 1997)

⁹⁰ 148 F.3d 197 (2d Cir. 1998).

⁹¹ *Id.*

⁹² *Id.* at 204.

⁹³ 304 F. 3d. 200 (2nd Cir. 2002).

⁹⁴ *Id.* at 209.

Third Circuit

Although the issue concerned the interpretation of a contract, the Third Circuit in *United Transportation Union Local 1589 v. Suburban Transit Corporation*⁹⁶ recited the following rule: “Only when an arbitrator ‘acted in manifest disregard of the law, or if the record before the arbitrator reveals no support whatsoever for the arbitrator’s determination,’ may a district court invade the province of the arbitrator.”⁹⁷

Fifth Circuit

Prior to the decision of *First Options v. Kaplan*,⁹⁸ the U.S. Court of Appeals for the Fifth Circuit had declined to recognize the manifest disregard standard in FAA cases involving commercial contract disputes between securities brokers and investors.⁹⁹ An early Fifth Circuit case stated in dictum that judicial review of a commercial arbitration award was limited to section 10 and 11 of the FAA.¹⁰⁰ In fact, it was not until after *Wilko* and *First Options* decisions that the Fifth Circuit recognized the manifest disregard standard in the 1999 case of *Arthur H. Williams v. Cigna Financial Advisors, Inc.*¹⁰¹

In our opinion, clear approval of the “manifest disregard” of the law standard in review of arbitration awards under the FAA was signaled by the Supreme Court’s statement in *First Options* that “parties (are) bound by (an) arbitrator’s decisions not in manifest disregard of the law.” . . . Accordingly, each of the other numbered federal circuit courts and the

⁹⁵ *Id.* (citing *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F. 2d 930, 934 (2nd Cir. 1986).).

⁹⁶ 51 F.3d 376 (1995).

⁹⁷ *Id.* at 380.

⁹⁸ 514 U.S. 938 (1995).

⁹⁹ See generally *McIlroy v. PaineWebber, Inc.*, 989 F.2d 817 (5th Cir. 1993); *R. M. Perez & Associates, Inc. v. Welch*, 960 F.2d 534 (5th Cir. 1992).

¹⁰⁰ *Forsythe Int’l, S. A. v. Gibbs Oil Co.*, 915 F.2d 1017 (5th Cir. 1990).

¹⁰¹ 197 F.3d 752 (5th Cir. 1999).

DC circuit have recognized manifest disregard of the law as either an implicit or non-statutory ground for vacating under the FAA.¹⁰²

After a review of evidence from the manuscript of the arbitration proceedings, the Court concluded: “Consequently, we conclude that based on the record presented for our review, it is not manifest that the arbitrators acted contrary to the applicable law and that their award should be upheld”.¹⁰³

Sixth Circuit

The position of the U.S. Court of Appeals for the Sixth Circuit is clearly set forth in *Dawahare v. Spencer*:¹⁰⁴ An arbitration decision “must fly in the face of established legal precedent” for the court to find manifest disregard of the law. An arbitration panel acts from manifest disregard if “(1) the applicable legal principle is clearly defined and not subject to reasonable debate; and (2) the arbitrators refuse to heed that legal principle.”¹⁰⁵ Thus, to find manifest disregard a court must find two things: the relevant law must be clearly defined and the arbitrator must have consciously chosen not to apply it.”¹⁰⁶

Seventh Circuit

After reviewing the decisions of other circuits, the U.S. Court of Appeals for the Seventh Circuit in *Watts v. Tiffany*¹⁰⁷ stated: “The law in other circuits is similarly confused, doubtless because the Supreme Court has been opaque. The dictum in *Wilko* and *First Options* was unexplained and un-illuminated by any concrete application”.¹⁰⁸ The court went on to state its

¹⁰² *Id.* at 760.

¹⁰³ *Id.* at 764.

¹⁰⁴ 210 F.3d 666, 669 (6th Cir. 2000).

¹⁰⁵ *Id.*, see also *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Jaros*, 70 F. 3d. 418 (6th Cir. 1995).

¹⁰⁶ *Id.*, citing *M & C Corp. v. Erwin*, 87 F.3d 844, 851 n.3 (6th Cir. 1996).

¹⁰⁷ 248 F.3d 577 (7th Cir. 2001).

¹⁰⁸ *Id.* at 580.

position in regard to manifest disregard of the law, which is substantially different from the positions of other circuits:

There is, however, a way to understand “manifest disregard of the law” that preserves the established relation between court and arbitrator and resolves the tension in the competing lines of cases. It is this: an arbitrator may not direct the parties to violate the law. In the main, an arbitrator acts as the parties’ agent and as their delegate may do anything the parties may do directly.¹⁰⁹

In a concurring opinion, Judge Williams agreed with the final decision of her two colleagues in that the district court had properly enforced the arbitration award. However, she was critical of the majority’s reasoning Court and its pronouncement of what appeared to be a new, or at least different, definition of manifest disregard:

Because the majority has effectively rejected the manifest disregard doctrine, I will briefly express my concern with that holding. It should be noted that the doctrine of manifest disregard has been substantively uniform in federal courts, requiring that (1) the arbitrator knew of a governing legal principle yet refused to apply it or ignore it altogether, and (2) the law ignored by the arbitrator was well defined, explicit and clearly applicable to the case. [citing cases] Every court of appeals, including our own, has held that a court may review the decision of an arbitrator for “manifest disregard of the law,” and has adopted, in substance, that very definition. Moreover, the words in the doctrine itself are more in accord with such an interpretation. (Citations omitted.) The majority’s holding conflicts with that precedent, and leaves the doctrine internally inconsistent and effectively impotent.¹¹⁰

¹⁰⁹ *Id.*

¹¹⁰ *Id.* at 580, 581.

Eight Circuit

The U.S. Court of Appeals for the Eighth Circuit in *Homestake Mining Co. v. United Steelworkers*¹¹¹ considered an appeal from the decision of the district court, which overruled a motion to vacate an arbitration award. One of the grounds for the motion was that the arbitrator's decision evidenced a manifest disregard for law. The Eighth Circuit's opinion affirmed the district court's decision and reinstated the arbitral award: "The arbitrator's interpretation of this regulation in plain language is neither "completely irrational [nor] evidences a manifest disregard for law,"¹¹² and is therefore "insulated from review."¹¹³

In *Hoffman v. Cargill*,¹¹⁴ the Eighth Circuit overruled a decision of the district court that had vacated an arbitration award because of the panel's manifest disregard of the law and because the panel's decision was irrational:

We have allowed that "beyond the grounds for vacation provided in the FAA, an award will only be set aside where it is completely irrational or evidence of manifest disregard of the law." These extra-statutory standards are extremely narrow: An arbitration decision may only be said to be irrational where it fails to draw its essence from the agreement, and an arbitration decision only manifests disregard for the law where the arbitrators clearly identified the applicable, governing law and then proceed to ignore it. We may not set an award aside simply because we might have interpreted the agreement differently or because the arbitrators erred in interpreting the law or in determining the facts.¹¹⁵

¹¹¹ 153 F.3d 678 (1998).

¹¹² *Lee v. Chica*, 993 F.2d 883, 885 (8th Cir. 1993)

¹¹³ 153 F. 3d. 678, 681 (1998).

¹¹⁴ 236 F.3d 458 (2001).

¹¹⁵ *Id.* at 461-62.

Ninth Circuit

In *Barnes v. Logan*,¹¹⁶ the U.S. Court of Appeals for the Ninth Circuit reviewed its prior holdings in setting forth their standards of review:

Judicial review of an arbitrator's decision "is both limited and highly deferential."¹¹⁷ An award will not be set aside unless it manifests a complete disregard of the law.¹¹⁸ Thus, an award must be confirmed if the arbitrators, even arguably, construed or applied the contract and acted within the scope of their authority.¹¹⁹ We may affirm the judgment of the District Court on any ground fairly supported by the record.¹²⁰

In a subsequent case, *Investors Equity Life Insurance Co. of Hawaii, Ltd. v. ADM Investor Services, Inc.*,¹²¹ the Ninth Circuit Court held: "Before the Court can conclude that arbitrators acted in 'manifest disregard', it must be clear from the record that the arbitrators recognize the applicable law and then ignored it."¹²²

Tenth Circuit

*Kelley v. Michaels*¹²³ was an appeal to the U.S. Court of Appeals for the Tenth Circuit from the district court's ruling that confirmed an arbitration award in a securities law arbitration. One of the grounds for the appeal and for setting aside the award was that punitive damages were awarded where the parties had agreed in a choice of law provision that any dispute would be

¹¹⁶ 122 F.3d 820 (9th Cir. 1997).

¹¹⁷ *Sheet Metal Workers' Int'l Ass'n v. Madison Indus. Inc.*, 84 F.3d 1186, 1190 (9th Cir. 1996).

¹¹⁸ *Id.*

¹¹⁹ *United Food and Commercial Workers Int'l Union v. Foster Poultry Farms*, 74 F.3d 169, 173 (9th Cir. 1995).

¹²⁰ *Kruso v. Int'l Tel. and Tel. Corp.*, 872 F.2d 1416, 1421 (9th Cir. 1989).

¹²¹ 1997 U.S. Dist. LEXIS 23881, 22 (1997).

¹²² *Michigan Mutual*, 44 F.3d at 832. *See also Prudential-Bache Securities, Inc. v. Tanner*, 72 F.3d 234, 240 (1st Cir. 1995) ("there must be some showing in the record, other than the result obtained, that the arbitrators knew the law and expressly disregarded it.").

¹²³ 59 F.3d 1050 (10th Cir. 1995).

governed by New York law, which prohibited the award of punitive damages.¹²⁴ The uniform submission agreement, however, provided for arbitration pursuant to National Association of Securities Dealers Inc. (NASD), and the NASD arbitrators' manual provided for a possible award of punitive damages.¹²⁵

An identical matter had come before the Supreme Court in *Mastrobuono v. Shearson Lehman*.¹²⁶ The Court in that case stated:

. . . [T]he FAA insures that parties' agreements will be enforced according to their terms even if a rule of state law would otherwise exclude such claims from arbitration. In resolving this matter the Supreme Court noted: The best way to harmonize the choice of law provision with the arbitration provisions is to read "the laws of the State of New York" to encompass substantive principles that New York courts would apply, but not to include special rules limiting the authority of arbitrators. Thus, the choice of law provision covers the rights and duties of the parties, while the arbitration clause covers arbitration; neither sentence intrudes upon the other. In contrast, the respondents' read sets up the two clauses in conflict with one another; one foreclosing punitive damages, the other allowing them. This interpretation is untenable.¹²⁷

The Tenth Circuit stated in *Kelley v. Michaels*, that based on the holding in the *Mastrobuono* it was compelled to find that the arbitration panel did not exceed its authority in awarding the *Kelleys* punitive damages.¹²⁸ *Mastrobuono* and *Kelley* hold that where there are specific conflicts between the arbitration clause and the choice of law provisions, full effect shall be given to the

¹²⁴ *Id.*

¹²⁵ *Id.*

¹²⁶ 514 U.S. 52 (1995).

¹²⁷ *Id.* at 63-64.

¹²⁸ 59 F.3d 1050, 1055 (10th Cir. 1995).

arbitration clause where it defines the limits of the authority of arbitrators, notwithstanding a conflict with a choice of law provision.

Eleventh Circuit

In *Brown v. ITT Consumer Fin. Corp.*,¹²⁹ the U.S. Court of Appeals for the Eleventh Circuit disposed of an appeal from the district court's refusal to vacate the arbitrator's award. The Court held that the party alleging the manifest disregard of the law had failed to show that the arbitrator in fact acted with such disregard. Arbitration awards will not be reversed due to an erroneous interpretation of the law by the arbitrator.¹³⁰ "To manifest disregard the law, one must be conscious of the law and deliberately ignore it."¹³¹

District of Columbia Circuit

In *Laprade v. Kidder, Peabody & Co., Inc.*,¹³² the U.S. Court of Appeals for the DC Circuit considered an appeal from the district court's decision that had rejected an argument that the arbitration panel had acted in manifest disregard of the governing law:

Manifest disregard of the law "means more than error or misunderstanding with respect to the law."¹³³ Consequently, "to modify or vacate an award on this ground, the Court must find (1) that the arbitrator knew of a governing legal principle yet refused to apply it or ignored it altogether and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case."¹³⁴

¹²⁹ 211 F.3d 1217 (2000).

¹³⁰ *Montes v. Shearson Lehman Bros., Inc.*, 128 F.3d 1456, 1460 (11th Cir. 1997).

¹³¹ *Id.* at 1461.

¹³² 246 F. 3d 702 (2001).

¹³³ *Id.*

¹³⁴ *Id.*

D. Elements of “manifest disregard of the law” standard

The case law makes clear that "a party seeking to vacate an arbitration award for ‘manifest disregard’ of the law may not proceed by merely objecting to the results of the arbitration."¹³⁵ All of the circuit courts have more or less found that "manifest disregard" of the law "clearly means more than [an arbitral] error or misunderstanding with respect to the law."¹³⁶ As a result of the Supreme Court's failure to define manifest disregard of the law, the federal appellate courts have taken up the role of fleshing out this standard. At first glance, the resulting cases seem chaotic; however, at least one commentator has discerned a pattern among the decisions.¹³⁷ Professor Stephen Hayford argues that almost all the appellate courts seem to have arrived at a consensus that manifest disregard of the law consists of two separate elements.¹³⁸ First, there is an "actus reus" element of the offense.¹³⁹ The arbitrator must make such a "blatant, gross misapplication of law [to the facts such] that it is apparent on the face of the award."¹⁴⁰ Second, an arbitrator must be aware of the law in the relevant area but nonetheless consciously or deliberately disregard the law where an ordinary, reasonable person could discern the applicable legal standard.¹⁴¹ This is the "mens rea" element of the defense.¹⁴²

Thus, even if a reviewing court finds a blatant misapplication of the relevant law (reflected in an arbitral result it believes to conflict with that law), vacatur is warranted under the "manifest disregard" of the law ground only if the court is able to conclude that the arbitrator knew, correctly interpreted the relevant law, but nevertheless made a conscious, intentional decision to

¹³⁵ O.R.Sec., Inc. V. Professional Planning Assocs., 857 F. 2d 742, 747 (1st Cir. 1995).

¹³⁶ See Merrill Lynch, 808 F.2d at 933 (2nd Cir. 1986).

¹³⁷ See Hayford, supra note 49, at 124-125 (Hayford’s model is helpful to understand both the standard as the courts now perceive it and the trend in their thinking).

¹³⁸ *Id.* at 124.

¹³⁹ *Id.* at 125.

¹⁴⁰ *Id.* at 124.

¹⁴¹ *Id.*

¹⁴² *Id.* at 125.

ignore it.¹⁴³ Both aspects of the "mens rea" requirement must be satisfied—the arbitrator must have been aware of the correct law and further must have consciously or intentionally chosen not to apply it to the facts of the case in rendering the award.¹⁴⁴

Despite this consensus, appellate courts have varied widely in their application of this two-step process, and have responded to these criteria in three general ways.¹⁴⁵ These categories do not represent three distinct groupings of the manifest disregard of law standard, but rather a continuum of deference that the courts give to non-reasoned awards handed down by arbitrators.¹⁴⁶

1. The "Futility Acknowledged" Approach to the "Manifest Disregard" of the Law Analysis

In this approach, the reviewing courts, in the absence of reasoned awards which is often the case in commercial arbitration, attempt to determine the criteria that the arbitrators utilize to arrive at their decisions. In this endeavor, the courts often cannot determine if the arbitrators willfully disregarded the law.¹⁴⁷ The majority of circuit appeals opinions applying the "manifest disregard" of the law standard follow this approach. Because this analytical tack never leads to vacatur, it reduces the "manifest disregard" of the law ground to a nullity.¹⁴⁸

¹⁴³ *M & C Corp. v. Erwin Behr & Co.*, 87 F.3d 844, 851 (6th Cir. 1996) (observing that, on the facts of the case before it, no "manifest disregard of the law" was shown because "any mistake by the arbitrator in applying [the relevant law] was more likely the result of inadvertence, rather than *a conscious decision to ignore the relevant law*" (emphasis added)).

¹⁴⁴ *Eljer manufacturing, Inc. v. Kowin Development Corp.* 14 F.3d 1250, 1254 (7th Cir. 1994).

¹⁴⁵ *See Hayford, supra* note 49, at 125.

¹⁴⁶ *Id.* at 125-132.

¹⁴⁷ *Id.* at 125-26.

¹⁴⁸ *Prudential-Bache Sec., Inc. v. Tanner*, 72 F.3d 234, 240 (1st Cir. 1995) ("[Because the] arbitrators do not explain the reasons justifying their award . . . appellant is hard pressed to satisfy the exacting criteria for invocation of the doctrine. In fact, when the arbitrators do not give their reasons, it is nearly impossible for the court to determine whether they acted in disregard of the law." (citations omitted)).

A reviewing court that requires direct evidence of arbitral knowledge of the correct interpretation of the law (the "mens rea" element) will never vacate an award that does not set forth the arbitrator's conclusions of law and fails to reveal the manner in which the arbitrator applied that law to the facts of the controversy.¹⁴⁹

2. The "Big Error" Approach to the "Manifest Disregard" of the Law Analysis

The court, in this approach, focuses only on the 'actus reus' element.¹⁵⁰ Under this view, the key for the petitioner seeking vacatur is convincing a reviewing court that the controlling law is so clear and well-settled as to warrant the inference that the arbitrator must have been aware of it. So the strategy of the petitioners would be to convince the court that the law is so clear that the arbitrator must necessarily have violated the law.¹⁵¹

Courts that follow this approach assumes that arbitrators have disregarded the law. The second circuit in *Willemijn Houdstermaatschappij, BV, v. Standard Microsystems Corp.*¹⁵² observed that, "a court may infer that the arbitrators manifestly disregarded the law if it finds that the error [of law] made by the made by the arbitrators is obvious [as measured by whatever degree of error standard the particular court has embraced]."¹⁵³ Under the Standard Microsystems formulation of the "manifest disregard" of the law test, vacatur can transpire if the court perceives in the award what amounts to a gross error of law that offends its sense of justice.¹⁵⁴

¹⁴⁹.See Hayford, *supra* note 49, at 126.

¹⁵⁰ *Id.* at 127.

¹⁵¹ *Id.*

¹⁵² 103 F. 3d 9 (2nd Cir. 1997).

¹⁵³ *Id.*

¹⁵⁴ See Hayford, *supra* note 49 at 127.

3. The Presumption-Based Approach to the "Manifest Disregard" of the Law Analysis

The presumption-based approach gives the least amount of deference to the arbitrator's findings of fact and interpretations of law, substituting instead the opinion of the court.¹⁵⁵ The Eleventh Circuit in *Montes v. Shearson Lehman Brothers*¹⁵⁶ and the Second Circuit in *Halligan v. Piper Jaffray Inc.*¹⁵⁷ followed this approach, but to date are the only two cases at the federal appellate court level that have found that the arbitrators manifestly disregarded the law.¹⁵⁸

In *Halligan*, an employee submitted evidence in an employment discrimination arbitration claiming that his former employer fired him because he was too old.¹⁵⁹ The panel denied *Halligan* any relief and offered no explanation or rationale for the result.¹⁶⁰ The district court judge found that

The record . . . [did] not indicate the Panel's awareness, prior to its determinations, of the standards for burdens of proof . . . [and that] where [the panel] did not issue a written opinion, [the district court could not] conclude that the panel did in fact disregard the parties' burdens of proof" because it was not the district court's job to reconsider evidence after the arbitral panel had already done so.¹⁶¹

The appellate court noted that the manifest disregard of the law defense, which *Halligan* raised on appeal, consisted of two elements: "(1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether and that (2) the law ignored by the

¹⁵⁵ *Id.* 129-31.

¹⁵⁶ 128 F.3d 1456, 1461 -62 (11th Cir. 1997).

¹⁵⁷ 148 F. 3d 197 (2nd Cir. 1998).

¹⁵⁸ See Hayford, *supra* note 49 at 202, 204.

¹⁵⁹ *Halligan*, 148 F. 3d at 198.

¹⁶⁰ *Id.* at 200.

¹⁶¹ *Id.*

arbitrators was well defined, explicit, and clearly applicable to the case."¹⁶² In this case the court in fact went ahead and evaluated the evidence that the tribunal had considered.¹⁶³ The court noted that the parties' counsel had explained the applicable standards of law to the panel (though no evidence showed that the panel actually understood the law) and that *Halligan* presented strong evidence in his favor.¹⁶⁴ The court assumed that the panel understood the law and found *Halligan's* strong evidence convincing: "[Combined with] the agreement of the parties that the arbitrators were correctly advised of the applicable legal principles, we are inclined to hold that they ignored the law or the evidence or both."¹⁶⁵ Additionally, the court determined that the arbitrators must have acted in manifest disregard of the law because the panel did not issue a written award.¹⁶⁶

In *Montes v. Shearson Lehman Bros.*,¹⁶⁷ an employee appealed against the denial of her petition to vacate an arbitrator's decision "denying her claim for over-time pay from her former employer."¹⁶⁸ Specifically, she claimed that her employer's lawyer urged the arbitration panel to ignore the relevant law of the Fair Labor Standards Act and to find in favor of the employer.¹⁶⁹ As in *Halligan*, the court in *Montes* engaged in a lengthy review of the facts used by the arbitration tribunal and determined that manifest disregard of the law consists of two steps -- that the arbitrator was "conscious of the law" but "deliberately ignored it."¹⁷⁰ However, the court went on to find the following:

¹⁶² *Id.* at 202.

¹⁶³ *Id.* at 204.

¹⁶⁴ *Id.* at 203-204.

¹⁶⁵ *Id.*

¹⁶⁶ *Id.*

¹⁶⁷ 128 F. 3d 1456 (11th Cir. 1997).

¹⁶⁸ *Id.* at 1458.

¹⁶⁹ *Id.*

¹⁷⁰ *Id.* at 1462-64.

In the absence of any stated reasons for the decision and in light of the marginal evidence presented to it, we cannot say that this [manifest disregard of the law] is not what the panel did . . . as the arbitrators recognized that they were told to disregard the law (which the record reflects they knew) in a case in which the evidence to support the award was marginal. Thus, there is nothing in the record to refute the suggestion that the law was disregarded. Nor does the record clearly support the award.¹⁷¹

The court concluded that, since the facts did not support the ruling and since there was no presumption in favor of the arbitrator, the arbitrator must have disregarded the law at the urging of the employer's counsel.¹⁷²

Both of these cases illustrate the essential components of the presumption-based approach.¹⁷³ This approach allows the court to work backwards, in that.¹⁷⁴ To vacate an unsatisfactory award, a court needs to conduct a review of the record, find satisfactory evidence that the arbitrator knew the correct law, and assume as a result that he necessarily disregarded the law to arrive at such an unjust result¹⁷⁵.

The court presumes and assumes too many issues in this approach and in fact, attempts to conduct an independent review of the evidence, the facts and the law, and tries to match its conclusions with that of the arbitral award.¹⁷⁶ Hence, in the absence of written opinions for awards, the court is often second guessing an arbitrators' evaluation of the law or fact.¹⁷⁷ In essence, the courts almost frustrate the entire purpose and process of arbitration in commercial matters since the courts end up spending the time that arbitration was designed to save;

¹⁷¹ *Id.* at 1461-62.

¹⁷² *Id.* at 1464.

¹⁷³ *See* Hayford, *supra* note 49 at 129.

¹⁷⁴ *Id.* at 130.

¹⁷⁵ *Id.* at 130.

¹⁷⁶ *Id.* at 131.

¹⁷⁷ *Id.*

arbitrators should not have their findings of facts second guessed in the guise of judicial review on the law.

E. “Manifest Disregard of the law” - statutory provision for vacatur in Georgia

In 1988, the Georgia Legislature adopted the current Georgia Arbitration Code.¹⁷⁸ This Code, based largely on the UAA, replaced the previous common law arbitration procedures codified in sections 9-9-1 through 9-9-11.¹⁷⁹ Georgia courts have recognized the same fundamental goals of arbitration as that of the UAA and the role it plays in the interaction between arbitration awards and the judiciary.¹⁸⁰ The Georgia Supreme Court has noted that arbitration provisions must be strictly construed because they are in derogation of common law.¹⁸¹ The courts of Georgia have long recognized that the Georgia Arbitration Code provides the exclusive grounds for vacating an arbitration award.¹⁸² "The power of a court to vacate an arbitration award has been severely limited in order not to frustrate the legislative purpose of avoiding litigation by resorting to arbitration."¹⁸³ Notably, no other state has adopted manifest disregard of the law as a statutory ground for vacatur.¹⁸⁴ In fact California and New Jersey have expressly rejected manifest disregard of the law as a ground of vacatur.¹⁸⁵

¹⁷⁸ Ga. Code Ann. §§ 9-9-1- -18 (2003).

¹⁷⁹ *Id.*

¹⁸⁰ *See* Greene v. Hundley, 468 S.E.2d 350, 354 (Ga. 1996) ("A primary advantage of arbitration is the expeditious and final resolution of disputes by means that circumvent the time and expense associated with civil litigation.").

¹⁸¹ *Id.* at 352.

¹⁸² *Id.*

¹⁸³ Haddon v. Shaheen & Co., 499 S.E.2d 693, 695 (Ga. Ct. App. 1998).

¹⁸⁴ *See, e.g.*, Texas General Arbitration Act, TEX. REV. CIV. STAT. ANN. art. 237, § A (Vernon 1973); VT. STAT. ANN. tit. 12, § 5677 (2002).

¹⁸⁵ Siegel v. Prudential Ins. Co., 79 Cal. Rptr. 2d, 726, 732-33 (Cal. Ct. App. 1998); Tretina Printing, Inc. v. Fitzpatrick & Assocs., Inc., 640 A.2d 788, 792 (N.J. 1994).

Until recently, the Georgia Arbitration Code's section on vacatur did not differ significantly from its federal counterpart.¹⁸⁶ However, in the 2003 legislative session, the Georgia Assembly passed a law to add the “manifest disregard of the law” standard as another defense to the Georgia Arbitration Code's section on vacatur.¹⁸⁷ The addition of the “manifest disregard of the law” defense was proposed as a consumer protection measure.¹⁸⁸

The amendment was enacted in response to the Georgia Supreme Court's decision in *Progressive Data Systems, Inc. v. Jefferson Randolph Corp.*,¹⁸⁹ which reversed a Georgia Court of Appeals' decision that had vacated an arbitration award on the basis of what the Court of Appeals found was a manifest disregard of the law.¹⁹⁰ The case, however, was not a consumer dispute but rather a contract dispute in which, after a two-day arbitration hearing, the arbitrator ruled for Progressive Data and awarded compensatory damages of \$81,540 plus attorney fees and expenses.¹⁹¹ The Georgia Court of Appeals set aside the award holding that the arbitrator had confused the applicable damages and thus the award amounted to a "manifest disregard of the law."¹⁹² The Georgia Supreme Court, however, held that, "in as much as the Code does not list 'manifest disregard of the law' as a ground for vacating an arbitration award, it cannot be used as an additional ground for vacatur."¹⁹³ Judge Carley, writing for the dissent, noted that, while

¹⁸⁶ David Boohaker, *Note, The Addition of the "manifest disregard of the law" defense to Georgia's Arbitration Code and potential conflicts with Federal law*, 21 GA. ST. U.L. REV. 501, 515 (2004).

¹⁸⁷ The only change to the arbitration code proposed by H.B. 91 and eventually adopted by H.B. 792 was the addition of a fifth defense: "the arbitrator's manifest disregard of the law." GA. CODE ANN. § 9-9-13(b)(5) (Supp. 2004); H.B. 792, 147th Gen. Assem., Reg. Sess. (Ga. 2003); H.B. 91, 147th Gen. Assem., Reg. Sess. (Ga. 2003).

¹⁸⁸ Representative Mary Margaret Oliver of the Georgia House of Representatives introduced a bill stating that over half of the Georgian citizens submit to arbitration, knowingly or unknowingly. She said, "As a Visa card owner, I have submitted contractually to arbitration and this is a significant phenomenon of our businesses to avoid traditional litigation." Representative Oliver's remarks revealed her belief that arbitration is a trap for the unwary consumer.

¹⁸⁹ 568 S.E. 2d 474, 474 (Ga. 2002).

¹⁹⁰ *Id.*

¹⁹¹ *Id.*

¹⁹² *Id.*

¹⁹³ *Id.* at 475.

manifest disregard of the law was not on the list of enumerated defenses, "in the very rare instance where an arbitrator intentionally ignores a controlling legal principle, he or she lacks the requisite impartiality . . ." and that in such cases, the arbitrator necessarily oversteps the authority vested upon him.¹⁹⁴ The dissent also tried to qualify the manifest disregard of the law defense by noting that it entailed more than just a misunderstanding or misinterpretation of the law.¹⁹⁵

The principle of "manifest disregard of the law" was enacted as a statutory defense in Georgia in 2003. The provisions of the amended statute are as follows:

§ 9-9-13. Vacation of award by court; application; grounds; rehearing; appeal of order:

(a) An application to vacate an award shall be made to the court within three months after delivery of a copy of the award to the applicant.

(b) The award shall be vacated on the application of a party who either participated in the arbitration or was served with a demand for arbitration if the court finds that the rights of that party were prejudiced by:

(1) Corruption, fraud, or misconduct in procuring the award;

(2) Partiality of an arbitrator appointed as a neutral;

(3) An overstepping by the arbitrators of their authority or such imperfect execution of it that a final and definite award upon the subject matter submitted was not made;

(4) A failure to follow the procedure of this part, unless the party applying to vacate the award continued with the arbitration with notice of this failure and without objection; or

(5) The arbitrator's manifest disregard of the law.¹⁹⁶

¹⁹⁴ *Id* at 477.

¹⁹⁵ *Id.*

¹⁹⁶ GA. CODE ANN. § 9-9-13 (2007).

Nonetheless, in a recent judgment decided in July 2007 in *ABCO Builders, Inc. v. Progressive Plumbing, Inc.*,¹⁹⁷ the Georgia Supreme Court emphatically stated that in the absence of any evidence of a specific intent to disregard the appropriate law, an arbitration award cannot be vacated under the manifest disregard of the law standard.¹⁹⁸ The court in *Progressive Plumbing* argued, with regard to certain damages awarded to *ABCO Builders, Inc.* in a construction contract dispute that the arbitration panel was presented with the proper legal formula to calculate these damages, but it did not employ this formula.¹⁹⁹ However, without providing any concrete evidence of it, the court, went on to conclude in *Progressive Plumbing* that this erroneous computation could not have been a mistake or misinterpretation, but, instead, was an intentional disregard of the law.²⁰⁰

The Georgia Supreme Court cited to *B.L. Harbert Intl. v. Hercules Steel Co.*, which held that "even if we were convinced that we would have decided this contractual dispute differently, that would not be nearly enough to set aside the award"²⁰¹ and *Health Services Mgmt. Corp. v. Hughes*, which stated that "There must be something beyond and different from mere error in law or failure on the part of the arbitrators to understand or apply the law; it must be demonstrated that the majority of arbitrators deliberately disregarded the law in order to reach the result they did."²⁰²

¹⁹⁷ 282 Ga. 308 (2007).

¹⁹⁸ O.C.G.A. § 9-9-13 (b) (5) (2007).

¹⁹⁹ 282 Ga. 308, 310 (2007).

²⁰⁰ *Id.*

²⁰¹ 441 F.3d 905, 911 (11th Cir. 2006).

²⁰² 975 F. 2d 1253, 1267 (7th Cir. 1992)

F. Implications of the “Manifest Disregard of the Law” Standard in Georgia

Georgia's manifest disregard of the law defense is new and contains no statutory explanation of the elements of the defense, leaving the courts to interpret the law.²⁰³ Hence the new law only creates situations that could severely hamper the finality of arbitration awards and increase costs, and provides little benefit to the system of commercial arbitration.²⁰⁴

Further, the FAA may preempt Georgia's Arbitration Code whenever an arbitration clause is at issue in a contract that affects interstate commerce.²⁰⁵ This might lead to a collision between principles of the Georgia Arbitration Code and the FAA. The Supreme Court of United States in *Southland* noted that the FAA limited the enforceability of arbitration provisions to contracts "evidencing a transaction involving commerce."²⁰⁶ Further the Supreme Court in *Allied-Bruce Terminix Cos. v. Dobson*²⁰⁷ held that "involving commerce" was functionally equivalent to "affecting commerce," which in essence implies a very wide meaning to "interstate commerce".²⁰⁸ Hence, to the extent that statutory recognition of manifest disregard of the law exists in Georgia as a barrier to enforcement of arbitration awards that are otherwise enforceable under federal law, the FAA would preempt Georgia law and nullify the manifest disregard defense when the contract in question affects interstate commerce because the defense is inconsistent with the broad scope and public policy that FAA envisioned.²⁰⁹

²⁰³ See Boohaker, *supra* note 186, at 522.

²⁰⁴ *Id.*

²⁰⁵ *Southland Corp. v. Keating*, 465 U.S. 1, 12 (1984).

²⁰⁶ *Id.* at 10-11.

²⁰⁷ 513 U.S. 265 (1995).

²⁰⁸ *Id.* at 278-279.

²⁰⁹ See *Southland Corp.*, 465 U.S. at 11 ("We see nothing in the Act indicating that the broad principle of enforceability is subject to any additional limitations under state law.").

In Georgia, the legislature enacted the doctrine to provide protection to consumers from what it perceived to be unfair arbitration practices.²¹⁰ However, the manifest disregard of the law doctrine offers little in the way of consumer protection and instead would hamper commercial enterprise, a major beneficiary of arbitration in Georgia.²¹¹

²¹⁰ See Boohaker *supra* note 186 at 537.

²¹¹ *Id.*

CHAPTER IV – Review of Arbitral Awards in India – Statutory Provisions

A. International Commercial Arbitration in India – Finality and Enforcement

India has always held a deep-rooted commitment to the philosophy of arbitration in general. Mahatma Gandhi, in 1927 wrote, “Differences we shall always have but we must settle them all, whether religious or other, by arbitration.”²¹² Foreign arbitral awards have always been treated as final on merits in India for the purposes of enforcement with limited or no scope for judicial review except strictly under the statute.²¹³ India became a party to the New York Convention with effect from October 11, 1960.²¹⁴ In order to implement its obligations under this Convention, India enacted the Foreign Awards (Recognition and Enforcement) Act, 1961.²¹⁵ The 1961 Act has since been repealed and replaced by the new Indian Arbitration and Conciliation Act, 1996.²¹⁶ The focus of the 1996 Act is the minimization of court intervention in the process and enforcement of foreign arbitral awards.²¹⁷

²¹² Lodha R.S., *Enforcement of foreign arbitral awards in India*, in INTERNATIONAL ARBITRATION AND NATIONAL COURTS: THE NEVER-ENDING STORY (A.J. Van den Berg, gen. ed., with the assistance of the International Bureau of Permanent Court of Arbitration, The Hague) (2001).

²¹³ *Id.*

²¹⁴ India signed the New York Convention on June 10, 1958 and ratified the same on July 13, 1960. According to Art. XII of the Convention, the Convention came into force for India ninety days after the date of ratification.

²¹⁵ Pemmaraju Sreenivasa Rao, *Enforcement of Foreign Arbitral Awards in India: Conditions of Reciprocity International arbitration and national courts*, in INTERNATIONAL ARBITRATION AND NATIONAL COURTS: THE NEVER-ENDING STORY (A.J. Van den Berg, gen. ed., with the assistance of the International Bureau of Permanent Court of Arbitration, The Hague) (2001).

²¹⁶ The Indian Arbitration and Conciliation Act, Act No. 26, Acts of the Parliament, 1996 (*hereinafter* called the 1996 Act).

²¹⁷ Anil Malhotra and Ranjit Malhotra, *Enforcement of Foreign Judgments and Foreign Arbitral Awards in the Indian Civil Jurisdiction*, 32 Commonwealth Law Bulletin 431-42, 438 (No.3 2006).

B. Indian Arbitration and Conciliation Act, 1996

The Indian Arbitration and Conciliation Act, 1996, is a unification statute in the sense that it was intended to give effect to multiple international commitments undertaken by India, namely the UNCITRAL Model Law on International Commercial Arbitration, 1985, the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, 1958, the Geneva Convention on Execution of Foreign Arbitral Awards, 1927 and the Geneva Protocol on Arbitration Clauses, 1923.²¹⁸

The Act seeks not only to consolidate, but also to unify Indian law both on domestic and international arbitration. In other words, under the Act, Indian law would be same for both domestic and international arbitrations that take place within the Indian territory²¹⁹. The 1996 Act is divided into four parts: Part I is concerned with domestic arbitrations; Part II deals with the enforcement of New York Convention awards and European Convention on International Commercial Arbitration (“Geneva Convention”) awards; Part III makes legislative provisions for conciliation based on the 1980 UNCITRAL Conciliation Rules²²⁰; and finally, Part IV adds supplementary provisions.²²¹ Chapters one and two of Part II deal with the enforcement of the New York and Geneva Conventions awards respectively.²²² A foreign award in India is enforceable either under the New York Convention,²²³ the Geneva Convention or under common law as applicable in India.²²⁴

²¹⁸ A.Jayagovind, *International Commercial Arbitration under The Arbitration and Conciliation Act, 1996*, 37 INDIAN J. INT’L LAW 658, 658-59 (No.4 1997).

²¹⁹ *Id.*

²²⁰ Available at <<http://www.jus.uio.no/lm/un.conciliation.rules.1980/>>

²²¹ P. Ramasamy, “*Enforcement of Annulled Awards, An Indian Perspective*”, 19 J. INT’L ARB. 461, 462 (No.5 2002).

²²² *Id.* at 463.

²²³ India has adopted the New York Convention with reciprocity and commercial reservations.

²²⁴ Indian courts have generally been guided by English common law where no statutory provisions to the contrary exist, *see* B.G. Kedia v. Girdharilal [1966] 1 S.C.R. 656, 664 (Ind.). However, there is no obligation as such on the court to apply common law. The common law is looked upon as a body of rules that reflect justice, equity and good

Before the 1996 Act, the Indian Arbitration Act 1940 (which was repealed by the 1996 Act) did not make any reference to international arbitrations taking place in Indian territory.²²⁵ Since the 1940 Act was to be applied to all arbitrations taking place within Indian territory, international arbitrations were also *ipso facto* covered by the enactment.²²⁶ The new enactment, however, makes a special reference to international commercial arbitrations and has defined the same under Section 2(f) of the 1996 Act.

C. Recourse against Arbitral Awards

Section 34 under Part I of the 1996 Act lays down the provisions under which applications could be filed to set aside arbitral awards. Section 48, Part II of the 1996 Act provides the conditions for enforcement of foreign awards. Section 34 and 48 of the 1996 Act essentially mirror each other in terms of their provisions, although an application challenging an arbitral award is filed under section 34 of the Act.

In relation to the enforcement of foreign awards, the Indian Supreme Court in *Fuerst Day Lawson Ltd. v. Jindal Exports Ltd.*,²²⁷ held that there is no need for separate proceedings in order to enable the court to decide the enforceability of an award or to make it binding as a order or decree and to execute the award. The Supreme Court made the following observations:

Part II of the Act relates to enforcement of certain foreign awards. Chapter I of this Part deals with New York Conventions Awards. Section 46 of the Act speaks as to when a foreign award is binding. Section 47 states what evidence the party applying for the enforcement of a foreign award should produce before the Court. Section 48 states the conditions for enforcement of foreign awards. According to Section 49, if the Court is

conscience; if the rule is inequitable or has been abrogated or modified by statute in England, it will not be applicable in India; see *Mukul Dutta v. Indian Airlines Corp.*, A.I.R.1962 311(Calcutta H.C.) 319.

²²⁵ See *Ramasamy*, *supra* note 221, at 462.

²²⁶ *Id.*

²²⁷ A.I.R. 2001 S.C. 2293, 2302, para 30.

satisfied that a foreign award is enforceable under this Chapter, the award shall be deemed to be a decree of that Court and that Court has to proceed further to execute the foreign award as a decree of that Court.

Specifically, a court hearing an application to set aside an award under the 1996 Act is, on the face of the wording of the 1996 Act, precluded from reviewing--even indirectly--the merits of the award since setting-aside is no longer possible for errors of law or fact.²²⁸

Section 34 of the 1996 reads as follows:

Application for setting aside arbitral award. –

(1) Recourse to a court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and subsection (3).

(2) An arbitral award may be set aside by the court only if-

(a) The party making the application furnishes proof that-

(i) A party was under some incapacity, or

(ii) The arbitration agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law for the time being in force; or

(iii) The party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or

(iv) The arbitral award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration:

Provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the arbitral award which contains decisions on matters not submitted to arbitration may be set aside; or

²²⁸ See Nariman, India, 42 ICA International Handbook on Commercial Arbitration Suppl. 30 (2000) 42.

(v) The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Part from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Part; or

(b) The court finds that-

(i) The subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force, or

(ii) The arbitral award is in conflict with the public policy of India.

Explanation. -Without prejudice to the generality of sub-clause (ii), it is hereby declared, for the avoidance of any doubt, that an award is in conflict with the public policy of India if the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81.²²⁹

D. Meaning and scope of “Public Policy” according to the 1996 Act

The explanatory notes which follow Sections 34(2)(b)(ii) and 48(2)(b) of the 1996 Act make clear that a party seeking to set aside or resist recognition and enforcement of an arbitral award on grounds of public policy faces a very high threshold.²³⁰ Essentially, in order to be contrary to the public policy of India, the award must rise to the level of having been induced by fraud or corruption.²³¹ Furthermore, the explanation to Section 34(2)(b)(ii) also specifies that a violation of public policy arises where there is a breach of the confidentiality provisions contained in Section 75 of the 1996 Act, or where evidence obtained in conciliation proceedings has been

²²⁹ Section 34 of The Indian Arbitration and Conciliation Act, Act No. 26, Acts of the Parliament, 1996.

²³⁰ Nadia Darwazeh and Rita F.Linnane, “*The Saw Pipes Decision: Two Steps Back For Indian Arbitration?*” 19-3 MEALEY’S INTL. ARB. REP. 15 (2004).

²³¹ *Id.*

adduced in the arbitration.²³² In short, pursuant to the examples specified in the explanatory notes included in the 1996 Act, only a serious violation of due process will amount to a violation of Indian public policy.

Thus, the explanatory notes provided in the 1996 Act are clearly in line with the interpretation given to the corresponding provisions in the UNCITRAL Model Law.²³³ Indeed, according to the UNCITRAL Model Law Commission Report, the term "public policy" comprises: [F]undamental notions and principles of justice. . . . It was understood that the term 'public policy,' which was used in the 1958 New York Convention and many other treaties, covered fundamental principles of law and justice in substantive as well as procedural respects. Thus, instances such as corruption, bribery or fraud and similar serious cases would constitute a ground for setting aside.²³⁴

Based on the foregoing, the public policy standard set by the 1996 Act is--consistent with the intention underlying the corresponding UNCITRAL Model Law provision--intended to be high.²³⁵ Accordingly, the 1996 Act provides that only where an award is based on a serious violation of due process can the public policy ground be successfully invoked to set aside or resist enforcement of such an award.

As regards the recognition and enforcement of foreign arbitral awards, the Indian Act embodies the New York Convention. However one of the main problems that arose in the application of the New York Convention was the interpretation of the meaning and scope of "public policy" by the National Courts. Indian courts tended to equate the term "public policy" with the term "law" as they were conditioned by section 13(f) of the Code of Civil Procedure of

²³² See § 81 of The Indian Arbitration and Conciliation Act, Act No. 26, Acts of the Parliament, 1996.

²³³ *Id.*

²³⁴ BINDER, INTERNATIONAL COMMERCIAL ARBITRATION IN UNCITRAL MODEL LAW JURISDICTION, 212 (2000).

²³⁵ See Darwazeh & Linnane, *supra* note 230.

India 1908, which provided that a foreign judgment may be refused recognition and enforcement in India if it sustains a claim founded on a breach of any law in force in India.²³⁶ The repercussions of such an approach are self-evident any foreign arbitral award that is not in conformance with the provisions of any of the laws in India could be struck down by adopting this view.²³⁷ This would mean that hardly any foreign arbitral award could be enforced in India.²³⁸

1. Renusagar Power Co. Ltd. v. General Electric Company

Fortunately, the Supreme Court of India in *Renusagar*²³⁹ dispelled many of the doubts with regard to the scope of “public policy” and clarified the meaning of “public policy” when used in enforcement of foreign awards. The Court said the terms should not be equated with the law of India: “Something more than the violation of the law of India must be established.” By applying this criterion, the enforcement of foreign awards would be refused, if such enforcement would be contrary to:

- (i) the fundamental policy of Indian law; or
- (ii) the interests of India; or
- (iii) justice or morality²⁴⁰.

This decision set an extremely high standard for Indian courts to refuse to enforce a foreign arbitral award.

The Supreme Court of India has recognized that international arbitral awards are enforceable internationally, and therefore should be international in their validity and effect.²⁴¹ The Supreme

²³⁶ Section 12(f) reads: “A foreign judgment shall be conclusive as to any matter directly adjudicated upon between the same parties or between parties under whom they or any of them claim litigating under the same title except when it sustains a claim founded on a breach of any law in force in India.”; See Jayagovind, *supra* note 220 at 670.

²³⁷ Vinay Reddy and V.Nagaraj, *Arbitrability: The Indian Perspective*, 19 J. INT’L ARB., 117, 140, (No.2 2002)

²³⁸ *Id.*

²³⁹ A.I.R. 1994 S.C. 860.

²⁴⁰ *Id.*

Court, in *Renusagar*,²⁴² recognized the pro-enforcement bias of the New York Convention, and thus held that a court in India should restrict itself to the grounds outlined in Section 48 of the Act. Those grounds, moreover, do not enable a party to challenge an arbitral award on its merits.²⁴³ The Supreme Court also endorsed the view that foreign awards must be more liberally enforced.²⁴⁴ The Court held that mere violation of a law would not lead to the conclusion that “public policy” has been infringed.²⁴⁵

The High Court of Delhi recognized in *Ludwig Wunsche & Co. v. Raunaq International Ltd.*²⁴⁶ that under Section 7 of the Foreign Awards (Recognition and Enforcement) Act, 1961 (the implementation legislation of the 1958 New York Convention), the “Court has no power to set aside the award, the Court can only refuse enforcement of the award.”²⁴⁷ The provisions of the New York Convention have greatly influenced the UNCITRAL Model law, and since the 1996 Act has adopted the Model law, there is no reason why Indian courts will not apply this reasoning to awards under the new Act.²⁴⁸

²⁴¹ *Brace Transport Corp. of Monrovia, Bermuda v. Orient Middle East Lines Ltd.*, A.I.R. 1994 S.C. 1715, 1720.

²⁴² A.I.R. 1994 S.C. 860.

²⁴³ *Id.* at 881

²⁴⁴ The Supreme Court cited with approval several U.S. decisions e.g., *Mitsubishi Motor Corp. v. Soler Chrysler Plymouth Inc.* 105 S. Ct. 3346 (1985).

²⁴⁵ *Id.*

²⁴⁶ (1989) 2 Arb.L. R.122.

²⁴⁷ *Id.* at 136, para 26.

²⁴⁸ *See Ramasamy, supra* note 221, at 466.

CHAPTER V - Review of Arbitral Awards in India – Scope Broadened

A. Scope of Judicial Intervention Broadened

The efficacy of any legislation must be judged by its implementation rather than its intentions.²⁴⁹ Unfortunately, in practice, the Indian courts have vastly enlarged the scope of challenge of awards to much more than what is available under the 1996 Act.

1. *Oil & Natural Gas Corp. Ltd. v. SAW Pipes Ltd.*

In this case, the Supreme Court of India adopted a broad interpretation of the term “public policy” by essentially including “error of law” as a new ground for setting aside an arbitral award.²⁵⁰ This “error of law” ground was not provided for under the 1996 Act. The Court then effectively used this new ground as a basis to review the merits of the case. While the Saw Pipes decision is, at first glance, only relevant to proceedings to set aside awards with seat of arbitration in India, the ramifications of this decision may potentially extend to recognition and enforcement proceedings of foreign awards in India.²⁵¹

The Supreme Court of India's decision in the *SAW Pipes* case concerned an arbitral award rendered in a dispute between two domestic parties in India. SAW Pipes Ltd. (“SAW Pipes”), the respondent in the case before the Supreme Court, had agreed to supply Oil and Natural Gas Corp. Ltd. (“ONGC”), the appellant, with casing pipes for offshore oil exploration.²⁵² The contract between SAW Pipes and ONGC provided that a delay to the contractually agreed date

²⁴⁹ Aloke Ray & Dipen Sabharwal, *What next for Indian arbitration?*, The Economic Times, 29 Aug. 2006.

²⁵⁰ (2003) 5 S.C.C. 705.

²⁵¹ See Darwazeh & Linnane, *supra* note 230.

²⁵² (2003) 5 S.C.C. 705, para 32.

for the supply of the pipes would entitle ONGC to a stipulated amount as liquidated damages.²⁵³ SAW Pipes delivered the pipes late, claiming force majeure based on strikes, and sought a time extension.²⁵⁴ ONGC denied this request and claimed liquidated damages for the late delivery of the pipes.²⁵⁵ SAW Pipes disputed this application of liquidated damages and the matter was referred to the Arbitral Tribunal.

In its award, the Arbitral Tribunal held that although the strikes did not fall within the contractual definition of force majeure, ONGC was not entitled to liquidated damages for the delay since it had failed to establish that it had suffered any loss as a result of the late delivery.²⁵⁶ Accordingly, the Arbitral Tribunal held that ONGC had wrongfully applied for liquidated damages.²⁵⁷ ONGC sought to set aside the arbitral award before the Indian courts on grounds of public policy pursuant to section 34(2)(b)(ii) of the 1996 Act.

The Supreme Court set aside the award on the basis that the Arbitral Tribunal had erred when it concluded that ONGC must prove the loss it suffered in order to seek liquidated damages.²⁵⁸ It held that, as a matter of contractual interpretation and statutory law, the appellant was not required to prove its loss and, therefore, was entitled to liquidated damages.²⁵⁹

B. New standard – “Patent Illegality”

The Supreme Court of India has also introduced a new ground for setting aside an award called “patent illegality”. The basis for the same has been explained as follows: "In our view, reading section 34 conjointly with other provisions of the 1996 Act, it appears that the legislative

²⁵³ *Id.* para 33 & para 38 for liquidated damages clause.

²⁵⁴ *Id.* at para 34.

²⁵⁵ *Id.*

²⁵⁶ *Id.*

²⁵⁷ *Id.*

²⁵⁸ *Id.* at para 74.

²⁵⁹ *Id.*

intent could not be that if the award is in contravention of the provisions of the 1996 Act, still however, it couldn't be set aside by the Court."²⁶⁰

The Court then analyzed whether the award could be set-aside on public policy grounds. The Court regarded the standard of public policy laid down in *Renusagar*²⁶¹ as "narrow" meaning of public policy and held in *Saw Pipes* as follows:

. . . [I]n a case where the judgment . . . is challenged before the . . . court exercising revisional jurisdiction, the jurisdiction of such court would be wider. Therefore, in a case where the validity of award is challenged, there is no necessity of giving a narrower meaning to the term 'public policy of India.' On the contrary, wider meaning is required to be given so that the '**patently illegal award**' passed by the Arbitral Tribunal could be set aside.²⁶²

Thus, the Supreme Court lowered the threshold of the public policy ground for setting-aside arbitral awards. It ruled that, certainly in cases of set-aside proceedings in India, an award can be set aside on public policy grounds, not only if the award is contrary to one of the three public policy grounds enumerated in *Renusagar*, but also if it is "patently illegal."²⁶³

The question that therefore arises is: What exactly did the Court mean when it stated that an award would also be contrary to public policy if it were "patently illegal"? Close scrutiny of the *SAW Pipes* Decision shows that the Indian Supreme Court employed a substantially different meaning of the term "patent illegality" than had been generally accepted and used in the public

²⁶⁰ *Id.* at para 13.

²⁶¹ A.I.R. 1994 S.C. 860.

²⁶² (2003) 5 S.C.C. 705. at para 22 (*emphasis added*).

²⁶³ *Id.* at para 74.

policy case law developed in international arbitration.²⁶⁴ First, the Court stated that there is no definition of "public policy" for the purposes of Section 34(2)(b)(ii) of the 1996 Act:

The phrase 'Public Policy of India' is not defined under the 1996 Act. Hence, the said term is required to be given meaning in context and also considering the purpose of the section and scheme of the 1996 Act. . . . Hence, the concept 'public policy' is considered to be vague, susceptible to narrow or wider meaning depending upon the context in which it is used.²⁶⁵

Second, since the Court concluded that there was no definition of public policy at hand, it decided that--in apparent disregard of the high threshold for public policy provided for in the explanatory note to Section 34(2)(b)(ii)--it would adopt a broader meaning of "public policy."²⁶⁶

Finally, the Court set forth its definition of "patent illegality." It held that an award was "patently illegal" if the Arbitral Tribunal had committed an error of law.²⁶⁷ By interpreting the concept of "public policy" to include "error of law," the Supreme Court went beyond the scope of the 1996 Act.²⁶⁸ Indeed, the 1996 Act did not mention error of law as a ground for setting aside an award based on public policy.

In short, the Supreme Court effectively used the public policy ground as means to conduct a review of the merits of the case and to "substitute its own view for the view taken by the Arbitrators. . ."²⁶⁹ The Court's interpretation of public policy is so broad that it potentially opens the floodgates to more and more challenges of arbitral awards before the Indian courts.²⁷⁰

²⁶⁴ *Id.*

²⁶⁵ (2003) 5 S.C.C. 705 at para 16.

²⁶⁶ *Id.* at para 16 & para 22.

²⁶⁷ *Id.*

²⁶⁸ *See* Darwazeh & Linnane, *supra* note 230.

²⁶⁹ *Id.*

²⁷⁰ *Id.*

C. Enforcement Proceedings of Foreign Awards.

While the Saw Pipes Decision was rendered in the context of an Indian award, and therefore arguably does not apply to the recognition and enforcement proceedings for foreign awards pursuant to Section 48 of the 1996 Act, the Court did not specifically exclude foreign awards from its reasoning.²⁷¹ Since the provisions on public policy with regard to the setting aside and the recognition and enforcement of awards in Sections 48(2)(b) and 34(2)(b)(ii) essentially mirror each other, it is uncertain whether the Court will in the future apply its broad interpretation of public policy to the enforcement of foreign arbitral awards, i.e., awards rendered outside India.

This uncertainty is further compounded by the Supreme Court's decision of 2001 in *Bhatia International v. Bulk Trading SA & Another*.²⁷² In this case, the Court ruled that Part I of the 1996 Act, which includes Section 34 on set-aside proceedings, would also apply to foreign awards unless impliedly or expressly excluded by the parties. Specifically, the Court stated:

To conclude we hold that the provisions of part I would apply to all arbitrations and to all proceedings relating thereto. Where such arbitration is held in India, the provisions of part I would compulsory [sic] apply. . . . In cases of international commercial arbitrations held out of India, provisions of part I would apply unless the parties by agreement, express or implied, exclude all or any of its provisions. In that case, the laws or rules chosen by the parties would prevail. Any provision, in part I, which is contrary to or excluded by that law or rules will not apply.²⁷³

²⁷¹ *Id.*

²⁷² A.I.R. 2002 S.C. 1432.

²⁷³ *Id.* at para 32.

The Bhatia decision has been the subject of much debate as it reversed the established understanding that Part I of the 1996 Act would not apply to arbitrations with a seat outside of India.²⁷⁴ Therefore, it cannot be ruled out that in the future, an ill-considered decision could construe the reasoning in the Saw Pipes case--which, of course, arose in the context of a set-aside proceeding under Part I--to also somehow apply to recognition and enforcement proceedings under Section 48 contained in Part II of the 1996 Act.

D. Judicial Intervention on the grounds of error of fact or law

The 1996 Act was brought into existence mainly to achieve, among other objectives, the minimization of the supervisory role of courts in the arbitral process and to provide that every final arbitral award is enforced in the same manner as if it were a decree of the court.²⁷⁵

Courts in India have given varied opinions from time to time as regards judicial intervention and review of arbitral awards. The courts have held that, “as the parties choose their own arbitrator, they cannot, when the award is good on the face of it, object to the decision either on law or on facts and the award will neither be remitted nor set aside.”²⁷⁶ The mere fact that the arbitrators have erred in law or facts can be no ground for interference by the court and the award will be binding on the parties.²⁷⁷

However, courts have not been always consistent in their views with regard to reviewing of arbitral awards. The Supreme Court, in one case, observed, “when an arbitrator instead of giving effect to the statutory formula contained in the contract, coined one of his own which he thought

²⁷⁴ P.C. MARKANDA, LAW RELATING TO ARBITRATION & CONCILIATION ACT, 1996, 23 & 69 (2001).

²⁷⁵ Purushottam Das Chokhani v. Sarita Devi Nathani, (2006)20 Arb. L.R. 176 (Gawhati DB).

²⁷⁶ Allen Berry & Co. Pvt. Ltd. v. Union of India, A.I.R. 1971 S.C. 696.

²⁷⁷ Lakshmi Mathur v. Chief General Manager, MTNL, (2000) Arb. L.R.(Bom.) 684.

was just and reasonable, the arbitrator committed jurisdictional error and the award could not be sustained.”²⁷⁸

The court should not substitute its own reasons for that of the arbitrator as long as the arbitrator’s reasons do not suffer from an error apparent on the face of the record or that is otherwise unreasonable and based on surmises and conjectures.²⁷⁹ In *Maharashtra State Electricity Board v. Sterlite Industries (India)*,²⁸⁰ the Supreme Court stated that, “An error in law on the face of the award means, that you can find in the award or document actually incorporated thereto, as for instance, a note appended by the arbitrator stating the reasons for his judgment, some legal propositions which is the basis of the award and which you can then say is erroneous.”²⁸¹

On the issue of error of law and error of fact patent on the face of the award, which may be grounds to set aside an award, the Supreme Court in the *Saw Pipes*²⁸² case, relied upon *Arosan Enterprises Limited v. Union of India*.²⁸³ There, the Court stated,

Where the error of finding of fact having a bearing on the award is patent and is easily demonstrable without the necessity of carefully weighing the various possible view points, the interference in the award based on erroneous finding of fact is permissible and similarly, if an award is based by applying a principle of law which is patently erroneous, and but for such erroneous application of legal principle, the award could not have been made, such award is liable to be set aside by holding that there has been a legal misconduct on the part of the arbitrator.²⁸⁴

²⁷⁸ D.C.M. Ltd. v. Municipal Corp. of Delhi, (1997) 7 S.C.C. 123.

²⁷⁹ S.Dhanaveni v. State of Tamil Nadu, (1997) 2 Arb L.R. (Mad. DB) 218.

²⁸⁰ (2001) 8 S.C.C. 482.

²⁸¹ *Id.* at para 60.

²⁸² S.K. CHAWLA, LAW OF ARBITRATION AND CONCILIATION: PRACTICE AND PROCEDURE 542 (2004).

²⁸³ *Id.*

²⁸⁴ *Id.* at para 60.

In a recent decision in *Hindustan Zinc Ltd. v Friends Coal Carbonization*,²⁸⁵ the Supreme Court again set aside the portion of the arbitral award, which was opposed to the specific terms of the contract. The Court, relying on *Saw Pipes*, observed that it is open to the court to consider whether the award is against the specific terms of contract and if so, whether to interfere with it on the ground that it is patently illegal and opposed to the public policy of India.²⁸⁶ However, the proper approach of the courts in matters relating to setting aside of arbitral awards is limited and is expressly stated in the 1996 Act.²⁸⁷

E. Standard of Review entailed by the principle of “Competence-Competence”

A strict interpretation of “Competence-Competence” would dictate that courts limit themselves to establishing the prima facie existence of an arbitration agreement, and the arbitral tribunals be left to substantively rule their own jurisdiction.²⁸⁸ Though this principle does not deal with the finality and enforcement of arbitral awards, it certainly involves the issue of court intervention and judicial review in the arbitral process. Besides, there is a counterargument that, rather than courts intervening with the awards when they are later challenged for lack of jurisdiction, parties are better off if courts definitively ruled on the existence and validity of the arbitration agreements at the outset.²⁸⁹ The recent Indian Supreme Court decisions on this principle raise more questions than they answer, but do at least give cause for optimism that in

²⁸⁵ (2006) 4 S.C.C. 445.

²⁸⁶ *Id.*

²⁸⁷ See CHAWLA, *supra* note 282, at 511.

²⁸⁸ Alope Ray & Dipen Sabharwal, *Competence-Competence: An Indian Trilogy*, 22-4 MEALY’S INT’L ARB. REP. 15 (2007).

²⁸⁹ *Id.*

grappling with the standard of review entailed by Competence-Competence, Indian courts are inching towards a less interventionist, pro-arbitration stance.²⁹⁰

In *Shin-etsu Chemicals Co. v. Aksh Optifibre Ltd.*,²⁹¹ the question before the Indian Supreme Court was whether Section 45 of the 1996 Act,²⁹² which incorporated Article II(3) of the New York Convention,²⁹³ required a prima facie or a final review by the national courts when faced with a challenge to the validity and existence of an arbitration agreement.²⁹⁴ The Supreme Court held by a 2-1 majority that, when considering a challenge to the existence or validity of an arbitration agreement, "the court is required to take only a prima facie view for making the reference to arbitration, leaving the parties to a full trial either before the Arbitral Tribunal or before the court at the post-award stage."²⁹⁵ *Shin-etsu* was hailed as a progressive and pro-arbitration judgment.²⁹⁶

Less than three months after *Shin-etsu*, the Supreme Court in *SBP & Co. v. Patel Engineering*²⁹⁷ permitted further court intervention in the arbitral process. The case concerned the appointment of an arbitrator by the chief justice of the Supreme Court in circumstances where the parties' chosen method for constituting the tribunal had failed.²⁹⁸ The issue was

²⁹⁰ *Id.*

²⁹¹ (2005) 7 S.C.C. 234.

²⁹² Section 45 of the 1996 Act states: "Notwithstanding anything contained in Part I or in the Code of Civil Procedure, 1908, a judicial authority, when seized of an action in a matter in respect of which the parties have made an agreement referred to in section 44, shall, at the request of one of the parties or any person claiming through or under him, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed."

²⁹³ Article II(3) of the New York Convention states: "The court of a contracting state, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed."

²⁹⁴ *Shin-etsu* (2005) 7 S.C.C. 234, 296.

²⁹⁵ *Id.* at para 25.

²⁹⁶ Emmanuel Gaillard, *Prima Facie Review of Existence, Validity of Arbitration Agreement*, 225 N.Y. L. J. 6 (105, 2005) also available at http://shearman.jp/files/Publication/b639f98b-ae76-42c1-a4e5-104cf34054ad/Presentation/PublicationAttachment/cb7e8c80-d1b7-473b-ba23-19d4c2ad7332/IA_120105.pdf.

²⁹⁷ (2005) 8 S.C.C. 618.

²⁹⁸ *Id.*

referred to a seven-judge bench of the Supreme Court for a definitive ruling, and the court by a majority of 6-1 held that the Chief Justice, while discharging this function, is entitled to adjudicate on contentious preliminary issues such as the existence of a valid arbitration agreement.²⁹⁹ It rejected the argument that the chief justice's role be limited to a prima facie review of the facts while making such a determination and instead held that the chief justice was entitled to call for evidence to resolve jurisdictional issues.³⁰⁰

Significantly, the Supreme Court ruled that the Chief Justice's findings on these preliminary issues would be final and binding on the arbitral tribunal.³⁰¹ This makes a mockery of the well-established principle of Competence-Competence—the power of an arbitral tribunal to determine its own jurisdiction—as enshrined in section 16 of the 1996 Act. It also encourages parties to sabotage the appointment process of arbitrators, to make spurious arguments about preliminary issues, and to use evidentiary hearings in courts to delay arbitral proceedings.³⁰²

Almost fifteen months after *Patel Engineering*, the Supreme Court was again faced with the issue of whether a dispute existed between the parties that must to be referred to arbitration in *Agri Gold Exims Ltd. v. Sri Lakshmi Knits and Wovens*.³⁰³ Although the Court did not discuss *Shin-etsu* or *Patel Engineering*, the limited standards of review, which it applied in determining the arbitrability of a dispute, made it significant for the purposes of Competence-Competence. The Supreme Court held that where there an arbitration agreement exists, an Indian court is obligated under Section 8 of the 1996 Act³⁰⁴ to refer the parties to arbitration.³⁰⁵ The Court's

²⁹⁹ *Id.* at para 47.

³⁰⁰ *Id.*

³⁰¹ Alope Ray & Dipen Sabharwal, *Indian Arbitration at a Crossroads*, available at http://www.whitecase.com/publications_01052007/

³⁰² *Id.*

³⁰³ Civil Appeal No. 326 of 2007 decided on January 23, 2007.

³⁰⁴ Section 8 of the 1996 Act states: "(1) A judicial authority before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party so applies not later than when submitting his first statement

approach in *Agri Gold* is consistent with *Shin-etsu* in championing a pro-arbitration attitude involving minimal interference by courts in the arbitral process. *Agri Gold* is a step in the right direction as it shows an inclination on the part of Indian courts to respect arbitration clauses and hold parties to their bargain by referring them to arbitration.

On their face, the legislative provisions regarding the set-aside and recognition and enforcement of awards contained in the 1996 Act are promising and are in line with international standards.³⁰⁶ However, decisions such as *Saw Pipes* and *SBP Patel* are changing the standard of review to be applied by the Courts, which seriously calls into question the independence of arbitral awards from judicial review on the merits.³⁰⁷

on the substance of the dispute, refer the parties to arbitration. . . . (3) Notwithstanding that an application has been made under sub-section (1) and that the issue is pending before the judicial authority, an arbitration may be commenced or continued and an arbitral award made."

³⁰⁵ See *Agri Gold*, Civil Appeal No. 326 of 2007 decided on January 23, 2007.

³⁰⁶ See *Darwazeh & Linnane*, *supra* note 230.

³⁰⁷ *Id.*

CHAPTER VI - Standards of Judicial Review in the United States and India – Observations

Both India and the United States are common law countries and signatories to the New York Convention. As to the potential for a review of an award on merits by the Indian judiciary, it has to stated that though India has not effectively recognized many non-statutory standards for reviewing arbitral awards, Indian courts have been inconsistent in their approach in setting-aside of the arbitral awards under the 1996 Act. This is a cause for concern since it is precisely this independence from the courts which is imperative for achieving some of the key goals of arbitration, namely speed and efficiency.³⁰⁸

The Arbitration and Conciliation (Amendment) Bill, 2003, was introduced before the Indian Parliament in December 2003 and it aims to add a Section allowing an award to be set-aside “where there is an error apparent on the face of the arbitration award giving rise to a substantial question of law”.³⁰⁹ This bill is envisioned to apply to domestic awards.³¹⁰ The Parliament is now effectively trying to provide an additional ground of challenge under Clause 27 of the Amendment Bill to provide that where the award is not an international award in India, the parties can challenge it award on the additional ground that there is an error apparent on the face of the award that gives rise to a substantial question of law.³¹¹ In terms of the uncertainty caused

³⁰⁸ *Id.*

³⁰⁹ Suman Khaitan & Co., *The Ambit and Scope of Judicial Intervention in Domestic Arbitral Awards.* (Indian Review (2005)) available at <http://www.asialaw.com/default.asp?Page=20&PUB=68&ISSO=12855&SID=477516>

³¹⁰ *Id.*

³¹¹ *Id.*

by the Supreme Court's introduction of error of law as a new ground for setting aside an award, as mentioned above, the December 2003 bill specifically sets forth "error of law" as a ground for setting aside a domestic award.³¹² This bill is currently before the Parliament of India.³¹³ While it may--if passed--put to rest this uncertainty, it will potentially open the door wide for the courts to revisit otherwise final arbitral awards on the merits.³¹⁴

In the United States, the Second Circuit court in *Toys "R" Us* found that a non-domestic award made in the United States would be subject to vacatur 'in accordance with its domestic arbitration law and its full panoply of express and implied grounds for relief' including "manifest disregard of the law".³¹⁵ The United States remains a victim of a self-inflicted competitive disadvantage imposed by its single legal framework for arbitration.³¹⁶ The adaptation of "manifest disregard of the law" as a standard of review under the Georgia law in its statute has only further expanded the general trend of court intervention in review of arbitral awards often involving second guessing the interpretations of the arbitrators in their awards. The spillover of domestic precedents into international cases will inevitably chill the selection of U.S cities for arbitration, as foreign parties understandably hope to avoid excessive judicial interference.³¹⁷ The never-ending debate over 'manifest disregard of the law', as well as the constant evolution of judicially crafted grounds for setting aside arbitration awards, indicate that the time has probably come to reform the FAA.³¹⁸ The FAA should be amended to provide a separate

³¹² See Ray & Sabharwal, *supra* note 301.

³¹³ *Id.*

³¹⁴ *Id.*

³¹⁵ 126 F.3d 15 (2nd Cir. 1997).

³¹⁶ William W.Park, Symposium, *International Commercial Arbitration: The Specificity of International Arbitration: The Case for FAA Reform*, 36 Vand. J.Transnat'l 1241, 1248 (2003).

³¹⁷ *Id.*

³¹⁸ Noah Rubins, "Manifest Disregard of the Law" and Vacatur of Arbitral Awards in the United States, 12 AM. REV. INT'L ARB. 363, 386 (2001).

framework for international arbitration that would restrict default rules limiting judicial review of awards to only the narrowest grounds.³¹⁹

The Eleventh Circuit, in an attempt to quell an appeal of arbitration brought under the “manifest disregard of law” in *B.L. Harbert International v. Hercules Steel Co.*, warned counsel that they would be sanctioned for frivolous challenges to arbitration awards.³²⁰ The court stated:

This Court is exasperated by those who attempt to salvage arbitration losses through litigation that has no sound basis in the law applicable to arbitration awards. The warning this opinion provides is that in order to further the purposes of the FAA and to protect arbitration as a remedy we are ready, willing, and able to consider imposing sanctions in appropriate cases.³²¹

Some legal scholars even suggest that arbitral institutions should create a mechanism for appeal so as to avoid judicial intervention and excessive review by the courts.³²² As Professor Thomas Klitgaard remarked, speed and finality are virtues, but only if you win. They are not virtues if a fundamental mistake has been made.³²³

However, on a more optimistic note, at the end of the day, the United States non-statutory “manifest disregard of the law” test establishes an extremely high hurdle for those seeking to apply it to avoid liability for an arbitration award.³²⁴ It is difficult to imagine an international arbitrator writing an award in which he or she painstakingly sets out an applicable legal principle

³¹⁹ See Park, *supra* note 316. See generally Richard W. Hulbert, *Should the FAA be Amended?* 18-12 MEALY’S INT’L. ARB. REP. 14 (2003).

³²⁰ 441 F.3d 905 (11th Cir. 2006).

³²¹ *Id.*

³²² William H. Knull, III & Noah D. Rubins, *Betting the Farm on International Arbitration: Is It Time to Offer an Appeal Option?*, 11 AM. REV. INT’L. ARB. 531, 563 (2000).

³²³ *Id.*

³²⁴ Lucy Reed & Phillip Riblett, *Expansion of Defenses to Enforcement of International Arbitral Awards in U.S Courts?*, 13 SW. J.L. & TRADE. AM. 121, 133 (2006).

and then defiantly ignores it or states that he or she will not apply it. It is hard to argue that such an arbitrator would not deserve to see the award set aside or not enforced.

Conclusion

Judicial review of the merits of arbitral awards by national courts whether in the United States or India, clearly runs the risk of impinging upon arbitration as an effective method of dispute resolution. The trend has been such that the, parties to an arbitration agreement can no longer be confident that an arbitral award, once rendered, is final.³²⁵ If disputes are anyway going to end up in courts, there is very less incentive for parties to arbitrate in the first instance.

In sum, it is clear that judicial standards of review, like judicial precedents, are not the property of private litigants.³²⁶ That said, federal appellate courts must continue to develop predictable precedents involving statutory grounds for judicial review.³²⁷ They also should take a more uniform approach to the manifest disregard doctrine.³²⁸ When they do so, parties and their counsel may be able to recognize the likelihood of success on appeal of most arbitration awards.³²⁹ Arbitration's goals are unquestionably best served by ensuring the finality of arbitration awards.³³⁰ This is consistent with the bargain the parties have made, and the remedy for any flaws in the system of arbitration should be for having the parties to choose better arbitrators, not to appeal arbitration awards.³³¹ However on a positive note, at least one commentator has argued that the frequency of judicial review of awards has not sapped

³²⁵ See Ray & Sabharwal, *supra* note 301.

³²⁶ *Hoelt v. MVL Group*, 343 F.3d 57, 65. (2nd Cir. 2003).

³²⁷ Katherine A.Helm, *The Expanding Scope of Judicial Review of Arbitration Awards: Where Does the Buck Stop?*, 61 JAN DISP. RESOL. J. 16, 25 (2007).

³²⁸ *Id.*

³²⁹ *Id.*

³³⁰ *Id.*

³³¹ *Id.*

arbitration of its efficiency.³³² The system works despite pervasive motions and appeals because non-reviewability is relatively inconsequential to arbitration's efficiency.³³³

³³² Kenneth R.Davis, *When Ignorance of the Law is no excuse: Judicial Review of Arbitration Awards*, 45 BUFF. L. REV. 49, 136 (1997).

³³³ *Id.*

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