



## ARBITRATION

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### *Sanctions for 'Frivolous' Appeals of Arbitration Awards*

The Federal Arbitration Act (FAA)<sup>1</sup> and parallel state statutes do not eliminate the right to appeal from an arbitration award. They do, however, place severe limits on the grounds for vacatur of an arbitration award, and courts have frequently stated that such statutory grounds (and nonstatutory grounds, such as “manifest disregard of law”) will be narrowly construed.

Does the strict limitation of grounds for vacatur necessarily imply a similarly strict view on the appropriateness of sanctions (on parties or their counsel) for “frivolous” attempts to obtain vacatur of awards? Several recent decisions suggest that such a principle may be at work.

#### **Standards for Vacatur, Sanctions**

The FAA sets out four express grounds for vacatur of an arbitration award: “corruption,” “evident partiality,” “refusing to hear evidence,” and arbitrators “exceed[ing] their powers.”<sup>2</sup> In addition, courts have grafted a nonstatutory basis



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for vacatur (“manifest disregard” of law) on this statutory framework. Under all of these grounds, “[a]rbitration awards are subject to very limited review[.]”<sup>3</sup> The aim of such limited review is to support the “twin goals of arbitration, namely, settling disputes efficiently and avoiding long and expensive litigation.”<sup>4</sup>

Arguably, the standards for sanctions match very closely these essential aims. Rule 11(b)(1) of the Federal Rules of Civil Procedure, for example, prohibits pleadings that are presented for improper purposes, such as to “cause unnecessary delay or needless increase in the cost of litigation.” Further, sanctions may be imposed on a lawyer who “multiplies the proceedings in any case unreasonably and vexatiously[.]”<sup>5</sup> And, on appeal, a court may award “just damages” and single or double costs on account of an appeal that is “frivolous.”<sup>6</sup>

#### **Recent Sanction Decisions**

Several recent decisions have noted the close relationship between strict standards for vacatur of arbitration awards, and the authority of courts to impose sanctions for the added delay and cost of “frivolous” attempts to vacate arbitration awards.

These decisions have also emphasized the interest of the courts themselves in encouraging expeditious, final arbitration processes. In *B.L. Harbert Int'l, LLC v. Hercules Steel Co.*,<sup>7</sup> for example, the U.S. Court of Appeals for the Eleventh Circuit provided “notice and warning” that it would approve sanctions in arbitration vacatur cases, based on its view that “[a] realistic threat of sanctions may discourage baseless litigation over arbitration awards and help fulfill the purposes of the pro-arbitration policy contained in the FAA.”<sup>8</sup> The court elaborated:

When a party who loses an arbitration award assumes a never-say-die attitude and drags the dispute through the court system without an objectively reasonable belief it will prevail, the promise of arbitration is broken. Arbitration's allure is dependent upon the arbitrator being the last decision maker in all but the most unusual cases. The more cases there are, like this one, in which the arbitrator is only the first stop along the way, the less arbitration there will be. If arbitration is to be a meaningful alternative to litigation, the parties must be able to trust that the arbitrator's decision will be honored sooner instead of later.<sup>9</sup>

Thus, the court noted, by litigating the case, post-award, without basis,<sup>10</sup> the appellant had deprived its adversary “and the judicial system” of the “principal benefits” of arbitration.<sup>11</sup>

The U.S. Court of Appeals for the Seventh Circuit, in the recent case of *Cuna Mutual Ins. Co. v. Office & Prof.*

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*Employees Int'l Union, Local 39*,<sup>12</sup> affirmed an order granting sanctions (the reasonable attorney's fees of the successful party) for a "groundless" petition to vacate an arbitration award.<sup>13</sup> The court, citing its own 20-year-old precedent, emphasized that a party "will not be permitted to nullify the advantages [of arbitration] by spinning out the arbitral process unconscionably through the filing of meritless suits and appeals.... Mounting federal caseloads and growing public dissatisfaction with the costs and delays of litigation have made it imperative that the federal courts impose sanctions on persons and firms that abuse their right of access to these courts."<sup>14</sup>

Lower courts appear to be following these appellate court directions. In *SII Investments, Inc. v. Jenks*,<sup>15</sup> for example, a federal magistrate judge in Florida (citing *Harbert*) recommended sanctions in a case where a party claimed that an award should be vacated because arbitrators had misapplied the law.<sup>16</sup> The court emphasized the "severely" and "narrowly" limited review under the FAA, and noted that, even if the arbitrators had misinterpreted and misapplied the law, vacatur would not be authorized.<sup>17</sup> The court noted that the benefits of arbitration, "prompt, economical and adequate solution of controversies" imply a compromise: "The arbitrating parties are also agreeing to accept less certainty of a legally correct decision."<sup>18</sup> The court recommended that the moving party's counsel should be sanctioned for their "never-say-die" tack.

In *Rueter v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*,<sup>19</sup> a district judge in Alabama similarly ordered sanctions, even though the responding party had not moved for sanctions.<sup>20</sup> The *Rueter* court (again citing *Harbert*), noted that the responding party had advanced a challenge to the award that had "no reasonable chance of success," and suggested that sanctions were necessary to "protect[] arbitration as a cost effective alternative form of dispute resolution."<sup>21</sup>

## Implications

This new line of authority, represented by *Harbert* and the other cases cited

above, is potentially problematic. To the extent that these new decisions suggest a view that post-award review is generally inappropriate, they may go too far. The law plainly authorizes such review, at least on the statutory grounds recognized by the FAA, and on the nonstatutory ground of "manifest disregard of the law," which has been generally recognized in the federal courts. A substantial line of older cases (especially in the U.S. Court of Appeals for the Second Circuit) suggests that, so long as the movant presents "colorable claims," and "plausible arguments," such review is not improper, and not subject to sanction.<sup>22</sup> Gross violations of arbitration procedure, such as repeated presentation of claims barred by res judicata,<sup>23</sup> or claims against arbitrators (protected by arbitral immunity),<sup>24</sup> may still be sanctioned.

## 'Manifest Disregard' of Law

This older line of authority on the inappropriateness of sanctions for conventional appeals of arbitration awards, moreover, recognizes that the concept of "manifest disregard" of law is somewhat amorphous. Parties arguably should not be sanctioned merely for testing the limits of this sometimes vaguely stated doctrine.

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1. Federal Arbitration Act, 9 USC §§1, et seq.
2. FAA, §10(a).
3. *Folkways Music Publishers v. Weiss*, 989 F2d 108, 111 (2d Cir. 1993).
4. Id.
5. 28 USC §1927.
6. See FedRAppP 38.
7. 441 F3d 905 (11th Cir. 2006).
8. Id. at 913-14.
9. Id. at 913.
10. The appellant in *Harbert* rested its request for vacatur on the contention that there had been "manifest disregard" of law by the arbitrator. The court noted that, in the Eleventh Circuit, only one case had ever found the "exceptional circumstances that satisfy the exacting requirements of this [manifest disregard] exception." Id. at 910. The court termed the dispute before it "a typical contractual dispute in which the parties disagree about the meaning of terms of their agreement." Id. For this type of dispute, the court noted, "[e]ven if we were convinced that we would have decided this contractual dispute differently, that would not be nearly enough to set aside the award." Id. The court thus criticized the appellant for "refusal to accept the law of this circuit which narrowly circumscribes judicial review[.]" Id. at 913.

11. Id. (emphasis added). Despite these observations, the *Harbert* court did not impose sanctions, because

there was at least some "speculative dicta" in support of the appellant's argument, because the opposing party did not move for sanctions, and because the appellant did not have the benefit of the court's opinion before proceeding with its appeal. Id. at 914.

12. 443 F3d 556 (7th Cir. 2006).

13. Id. at 565. The *Cuna* court criticized the appellant for attempting to "sidestep" the deferential standards for review of arbitration awards, by challenging the arbitrability of the issue presented. Id. at 563. The court held, instead, that the case presented only an issue of contract interpretation, and that the award must be upheld "unless there is no possible interpretive route" to the award. Id. at 564.

14. Id. at 561 (quoting *Dreis & Krump Mfg. Co. v. International Assoc. Machinists Dist. 8*, 802 F2d 247, 255-56 (7th Cir. 1986)); see also *Flexible Mfg. Sys. Pty, Ltd. v. Super Prods. Corp.*, 86 F3d 96, 101 (7th Cir. 1996) ("The promise of arbitration is spoiled if parties disappointed by its results can delay the conclusion of the proceeding by groundless litigation in the district court followed by groundless appeal to this court[.]") (quotation omitted).

15. 2006 WL 2092639 (M.D. Fla. July 27, 2006).

16. The *SII Investments* court suggested that the petition to vacate (based on "manifest disregard" of law) was ill-founded because the claimant "never conceded to the arbitrators her position was contrary to the law nor suggested, either directly or inferentially, they ignore the law." Id. at \*4.

17. See id. at \*3-4. Indeed, the court remarked on the fact that there was "no evidence that the arbitrators decided the dispute on the basis of anything other than their best judgment—whether right or wrong—of how the law applies to the facts of the case." Id. at \*6.

18. Id. at \*3 (quoting *Wilko v. Swan*, 346 U.S. 427, 438 (1953)) (brackets and quotation marks omitted).

19. 440 FSupp2d 1256 (N.D. Ala. 2006).

20. The *Rueter* court rejected the contention that an award was "arbitrary" merely because it was arguably contrary to Alabama law. See id. at 1264 (award arbitrary only if there is "no ground for Panel's decision") (quotation omitted).

21. Id. at 1267; see also *Goeben v. Morgan Stanley SW Inc.*, 2006 WL 2711802 at \*2 (E.D. Wis. Sept. 21, 2006) (citing *Harbert*, but declining to impose sanctions against pro se party).

22. See *W.K. Webster & Co. v. American President Lines, Ltd.*, 32 F3d 665, 670 (2d Cir. 1994) (vacating order of sanctions on motion to vacate award for "manifest disregard" of law); see also *ADR/JB Corp. v. MCY III, Inc.*, 299 FSupp2d 110, 116 (EDNY 2004) (denying sanctions where challenge to arbitration award was not "patently unreasonable").

23. See *Weinraub v. Glen Rauch Securities, Inc.*, 419 FSupp2d 507, 514 (SDNY 2005) (awarding sanctions where "no reasonable attorney" could fail to realize claims were barred).

24. See id. at 518 ("the Arbitrator Defendants should never have been named in this lawsuit, regardless of the merits of the breach of contract claim").

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