

US courts continue to show restraint over “manifest disregard” doctrine

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Hughes Hubbard & Reed’s co-chair of international arbitration **Hagit Elul** and associate **Olivia Bensinger** in New York consider a recent decision showing that US courts continue to exercise restraint when it comes to applying the controversial doctrine of “manifest disregard of the law” as a basis for vacating an arbitral award.

One of the more controversial aspects of US arbitration jurisprudence is the doctrine of “manifest disregard of the law.” Under that judicially-created doctrine, a court may vacate an arbitral award where the arbitrator acted in manifest disregard of the law. This requires more than a mere error in interpretation or application of the law. Rather, the decision must fly in the face of clearly established legal precedent. An arbitrator acts with manifest disregard if the applicable legal principle is clearly defined and not subject to reasonable debate; and the arbitrators refused to heed that legal principle.

In 2008, the US Supreme Court called into question the validity of the manifest disregard of the law doctrine in *Hall Street v Mattel*. In that case, the court restricted the grounds for vacatur of an arbitration award to those set forth in section 10 of the Federal Arbitration Act (FAA). While the court declined to specifically decide whether manifest disregard of the law is a separate, non-statutory basis for vacatur, it noted that it could be a “judicial gloss on the specific grounds for vacatur of arbitration awards” that are provided in the FAA.

Following the decision in *Hall Street*, a split between different US Courts of Appeals has arisen as to the continuing vitality of the manifest disregard of the law doctrine. Compare *Med Shoppe Int’l v Turner* in the

Eighth Circuit (holding manifest disregard is no longer an applicable basis for vacating an arbitration award) with *Dewan v Walia* in the Fourth Circuit (allowing arguments to vacate an arbitration award based on manifest disregard of the law). In 2011, the Second Circuit Court of Appeals – which adjudicates vacatur proceedings arising in New York – reaffirmed the manifest disregard doctrine as a potential uncodified basis for vacating arbitral awards (*Schwartz v Merrill Lynch*). The Second Circuit continues to apply the analysis in its decisions, but rarely finds that an arbitrator manifestly disregarded the law.

However, in a recent decision, the Second Circuit chose to use the doctrine of manifest disregard of the law as an opportunity to remand an arbitral award to the arbitrator for clarification, rather than to vacate the award. In *Weiss v Sallie Mae*, the claimant incurred student loan debt to Sallie Mae (a consumer banking provider) on which she subsequently defaulted. After receiving multiple phone calls per day from debt collectors, the claimant brought a claim under the Telephone Consumer Protection Act (TCPA). The parties then submitted to arbitration.

The arbitrator issued a decision that the plaintiff was entitled to statutory damages with regard to some of her claims, but also found that she was a member of a settlement class of which the eventual settlement agreement contained a general release provision preventing class members from filing further TCPA suits against Sallie Mae. The arbitrator did not acknowledge this release provision in his decision. Sallie Mae moved to vacate the award and the district court issued a decision to vacate, holding that the arbitrator manifestly disregarded the law by failing to “apply – or even address – an explicit, unambiguous term of the settlement agreement.”

The Second Circuit observed that there was “incoherence” in the arbitral award and it appeared the arbitrator had improperly disregarded the general release. Specifically, the arbitrator expressly found that the claimant had received the required notice of the settlement and “of her rights and obligations under the terms of the settlement.” The Second Circuit noted that granting statutory recovery despite this finding would ignore the general release provision in the settlement agreement.

Rather than vacate the award under the manifest disregard of the law doctrine, the Second Circuit took a more restrained approach. It remanded the award to the arbitrator, instructing him to explain his decision-making. The court ordered the arbitrator “to clarify whether the class notice was or was not sufficient and, if determined to be sufficient, then to construe the general release provision in the first instance and to vacate or modify the arbitral award if necessary.”

The Second Circuit’s decision not to rush into vacatur on the basis of manifest disregard of the law confirms that the general approach of US courts to use the doctrine only sparingly. There is a high bar to finding manifest disregard – if “the arbitrator has provided even a barely colorable justification for his or her interpretation of the contract” then the award will be upheld (*Schwartz*). Remand of an award to the arbitrator for clarification is not without precedent (see *Hardy v Walsh Manning Sec*, acknowledging the Second Circuit’s authority to seek clarification of “whether an arbitration panel’s intent in making an award evidences a manifest disregard of the law”). The Second Circuit’s decision in *Weiss* evidences the continued deference granted by US courts to arbitrators, and confirms that vacatur on the basis of manifest disregard of the law will rarely be granted.

Cases referenced

Hall St Assocs, LLC v Mattel, Inc, 552 US 576 (2008)
Med Shoppe Int’l, Inc v Turner Invs., Inc., 614 F.3d 485 (8th Cir. 2010)
Dewan v. Walia, 544 F. App’x 240 (4th Cir 2013)
Schwartz v. Merrill Lynch & Co, 665 F.3d 444, 451 (2d Cir 2011)
Weiss v Sallie Mae, Inc, No. 18-2362 (2d Cir Sept 12, 2019)
Hardy v Walsh Manning Sec., LLC, 341 F.3d 126, 134 (2d Cir 2003)