BY STEVEN NUDELMAN

Is an Arbitration Award Really Final?

Arbitration continues to grow in popularity as the preferred method of resolving business disputes. Proponents of arbitration claim that it is generally quicker and cheaper than traditional litigation, and unlike litigation, arbitration offers participants finality. In other words, with rare exception, arbitration awards—unlike trial court decisions or jury verdicts—are final and *not* subject to appeal to another tribunal.

However, this last feature of arbitration begs a question: What do you do if you are the losing party in arbitration?

VACATUR OF AWARDS

The unsuccessful party in an arbitration must look long and hard at the "rare exceptions" that courts use to vacate or overturn arbitration awards and often struggle to fit their case within the contours of one or more such exceptions. Given the legal expenses associated with such an undertaking and the odds (which I unofficially would put at less than 10 percent) of having an arbitration award vacated by a court, most losing parties accept their fate and the finality of the award. However, when the amount of the arbitration award is significant—a subjective measure that varies in the eye of the loser—or the legal bases for vacating an arbitration award are crystal clear, court proceedings may be worth a closer look.

This month we examine a dispute involving the sale of defective pipe, a subsequent arbitration, and the losing party's attempt to utilize two rare exceptions to persuade a court to vacate the arbitrator's award. While this article will educate the plumbing engineer about these two rare exceptions, it is important to note that there are a number of other bases upon which an arbitration award may be vacated. Since this article does *not* purport to be an all-inclusive treatment on vacatur of arbitration awards, the plumbing engineer who receives an adverse arbitration award is thus advised to consult an attorney to learn about all of the available options for relief.

T.CO METALS, LLC V. DEMPSEY PIPE & SUPPLY, INC.

In *T.Co Metals, LLC v. Dempsey Pipe & Supply, Inc.*, the parties entered into two sales contracts pursuant to which T.Co agreed to sell Dempsey 2,440 metric tons of 20-foot plain-end steel pipe to be made in Chile and sent to Philadelphia in four shipments arriving during the spring and summer of 2005. Both contracts provided that the seller was "not responsible for consequential loss or damage." Both contracts contained an arbitration provision that required the parties to arbitrate their dispute under the international arbitration rules of the American Arbitration Association (AAA). The arbitration provision also stated, "The award of the Arbitration tribunal will be final and subject to no appeal."

After the pipe was delivered, Dempsey learned that most of it was bowed or bent and out of tolerance for straightness. Dempsey rejected only a small portion of one of the four shipments and elected to keep the rest and straighten the defective pipe itself. T.Co sent Dempsey an invoice for $1,993,145.53, of which Dempsey only paid $1,655,105.81. T.Co filed a Demand for Arbitration, seeking the difference, or $338,039.72, from Dempsey. Dempsey filed a counterclaim in arbitration, seeking $1,895,052—the alleged diminished value of the defective pipe. Among other things, T.Co argued that Dempsey was improperly trying to seek "consequential damages" by way of its counterclaim.

Original Award

The matter was heard by a single arbitrator, who awarded $338,039.72 to T.Co for the unpaid invoices and $420,537 to Dempsey for the diminished value of the defective pipe (the Original Award). Although the arbitrator agreed that Dempsey was improperly trying to seek consequential damages, he felt that Dempsey was entitled to recover some damages under certain provisions of New York's Uniform Commercial Code. Both parties disagreed with the award and submitted applications to the arbitrator to amend the award. The international rules of the AAA allow an arbitrator to "correct any clerical, typographical, or computation errors or make an additional award as to claims presented but omitted from the award."

Amended Award

The arbitrator issued an Amended Award rejecting T.Co's argument that the Original Award contained "manifest errors of law" by compensating Dempsey for lost profits and diminution of value of the pipe. The arbitrator did find errors relating to four of the 23 invoices that he considered and as a result adjusted Dempsey's award on the counterclaim downward, from $420,537 to $340,587. Both parties applied to the U.S. District Court for the Southern District of New York to modify or vacate the Amended Award.

T.Co continued to press its argument that the arbitrator manifestly disregarded the law in his award to Dempsey. Dempsey argued that the corrections made by the arbitrator were not to clerical or typographical errors; thus, the arbitrator exceeded his authority in reducing the Original Award on the counterclaim by $79,950.

Lower Court Rulings

The District Court rejected T.Co's manifest disregard argument, finding that the United States Supreme Court's recent decision in *Hall Street Associates, LLC v. Mattel, Inc.* eliminated this as a basis for vacating arbitration awards. The District Court further agreed with Dempsey that the arbitrator did not correct a clerical or computational error when he issued his Amended Award. As a result, the arbitrator exceeded his authority by reopening the case and issuing the Amended Award.

Under the *functus officio* doctrine, an arbitrator's power to act is limited once he decides all of the issues submitted to him for arbitration. Thus, once the arbitrator rendered the Original Award, he no longer had any authority to render the Amended Award. The District Court confirmed the Original Award, granting Dempsey $420,537 on its counterclaim.

Manifest Disregard of the Law

T.Co filed an appeal, as of right, of the District Court's decision to the U.S. Court of Appeals for the Second Circuit. The Second Circuit examined the two issues decided by the District Court: whether the arbitrator's rulings demonstrated a "manifest disregard of the law" and whether the Amended Award violated the *functus offico* doctrine.

First, the Second Circuit disagreed with the District Court, finding that the Supreme Court did *not* eliminate the "manifest disregard" standard when it decided *Hall Street*.

The Court found that "manifest disregard of the law" is an extremely narrow standard upon which to overturn an arbitration award. As the Court stated:

[A]wards are vacated on grounds of manifest disregard on in "those exceedingly rare instances where some egregious impropriety on the part of the arbitrator [] is apparent" … That impropriety has been interpreted "clearly [to] mean [] more than error or misunderstanding with respect to the law" . . . or an "arguable difference regarding the meaning or applicability of laws urged upon" an arbitrator … Rather, "the award should be enforced, despite a court's disagreement with it on the merits, if there is a *barely colorable justification* for the outcome reached." (Citations omitted.)

In this case, the appelate court found that the arbitrator's decision was not a "manifest disregard of the law" because the arbitrator reasonably found that Dempsey had a right to recovery under the Uniform Commercial Code, notwithstanding the parties' agreement barring consequential damages.

Functus Officio Rule

While T.Co lost on the first argument on appeal, it fared better on the *functus officio* issue. The Second Circuit rejected Dempsey's argument, finding that the arbitrator had the authority to issue the Amended Award (and reduce Dempsey's recovery by $79,950).

According to the *functus officio* doctrine, "once arbitrators have fully exercised their authority to adjudicate the issues submitted to them, 'their authority over those questions is ended,' and 'the arbitrators have no further authority, *absent agreement by the parties, to redetermine th[ose] issue[s].*'" (Emphasis added.) While arbitrators have limited authority to correct a mistake that is apparent on the face of the award, this is a narrow exception to *functus officio* that applies to clerical mistakes or obvious computational errors.

Here, Dempsey argued, the arbitrator impermissibly corrected more substantive errors in reviewing the underlying invoices. In rejecting this argument, the Second Circuit noted that here the parties *agreed* to have the arbitrator reconsider his decision in accordance with the AAA's international rules. As a result, the Second Circuit sent the case back to the District Court with instructions to confirm the Amended Award.

TWO NOTES OF CAUTION

The *T.Co* case teaches the plumbing engineer two important lessons about arbitration. First, an arbitrator's decision may still be upheld even if it is predicated on a mistake of law. To vacate an arbitration award on legal grounds, one must satisfy the narrow "manifest disregard of the law" standard as explained in the Second Circuit. (Notably, this standard is still valid in the federal courts in the Second Circuit—covering New York, Connecticut, and Vermont. Other courts have rejected this standard altogether.) This was not done by T.Co.

Second, beware of the *functus officio* doctrine. Once the arbitrator renders his award after closing the hearings, he cannot unilaterally reopen them and modify his decision. He must act with the parties' agreement—either expressly or through agreement to adhere to arbitration rules, such as those promulgated by the AAA. To avoid a *functus officio* problem, it is best to ensure that all issues have been addressed by the arbitrator *before* he renders his award and closes the hearings.

As arbitration becomes more prevalent, unsuccessful participants are more likely to try to vacate awards with which they are dissatisfied. This article discussed two legal concepts that may have a direct impact on the success or failure of vacating an arbitration award, and they are worth noting, whether you're the party trying to vacate or confirm an award. PSD

RECOMMENDED READING

1. *T.Co Metals, LLC v. Dempsey Pipe & Supply, Inc.*, 592 F.3d 329 (2d Cir. 2010)
2. *Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008)

STEVEN NUDELMAN is a partner at the law firm of Greenbaum, Rowe, Smith and Davis LLP in Woodbridge and Roseland, New Jersey. He is a member of the firm's Litigation Department and its Construction, Green Building, and Dispute Resolution Practice Groups. He may be reached at 732-476-2428 or **snudelman@greenbaumlaw.com**. To comment on this article, e-mail **articles@psdmagazine.org**.