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GUEST COLUMN

Limits on arbitral remedies under the CAA and FAA

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You represent a client in arbitration, but the arbitrator's final award includes a remedy that no party asked for, no jury could award, and is unprecedented even for bench trials.

This unprecedented remedy means you have a compelling basis to vacate the award, right?

Not at all.

Under Section 10(a)(4) of the Federal Arbitration Act (FAA) and the California Arbitration Act (CAA), specifically California Code of Civil Procedure Section 1286.2(a)(4), an arbitral award–including the remedy awarded–can be vacated where an arbitrator "exceeded their powers." But unless the arbitration agreement expressly prohibits the remedy awarded, the arbitrator has extensive, though not unbridled, discretion in fashioning relief.

When does an arbitral remedy represent the "excessive" exercise of arbitrator power?

Under the FAA, a remedy is within the arbitrator's powers to issue if it draws its "essence from the agreement." *Steelworkers v. Enterprise Corp.*, 363 U.S. 593 (1960). When the remedy is "derived from the 'essence' of the agreement, viewed in light of the agreement's language, as well as the expressed intentions of the parties," then the arbitrator has power to issue the remedy. See *McGrann v. First Albany Corp.*, 424 F.3d 743, 749 (8th Cir. 2005). The reason for this broad remedial discretion is the following:

"When an arbitrator is commissioned to interpret and apply the [agreement], he is to bring his informed judgment to bear in order to reach a fair solution of a problem. *This is especially true when it comes to formulating remedies.* There the need is for flexibility in meeting a wide variety of situations. The draftsmen may never have thought of what specific remedy should be awarded to meet a particular contingency. Nevertheless, an arbitrator is confined to interpretation and application of the ... agreement; he does not sit to dispense his own brand of industrial justice. He may, of course, look for guidance from many sources, yet his award is legitimate only so long as it *draws its essence from the ... agreement." Steelworkers v. Enterprise Corp.*, 363 US at ___ [emphasis added].

Under the FAA, when does a remedy fail the "essence" test?

Federal decisions following *Steelworkers* hold that an arbitral remedy fails the "essence" test when it is "completely irrational" or a "manifest ... disregard of the law" (*Bosack v. Soward*, 586 F.3d 1096, 1104 (9th Cir. 2009)), or based on any "arbitrary and capricious" interpretation of the agreement (*Ainsworth v. Skurnick*, 960 F.2d 939, 940 (11th Cir. 1992)).

The CAA test for the validity of an arbitral award was first articulated in *Advanced Micro Devices v. Intel Corp.*, 9 Cal.4th 362 (1994) (AMD). After referencing the *Steelworkers* FAA "essence" test, the California Supreme Court held that:

Arbitrators are not obliged to read contracts literally, and an award may not be vacated merely because the court is unable to find the relief granted was authorized by a specific term of the contract.... *The remedy awarded, however, must bear*

some rational relationship to the contract and the breach. The required link may be to the contractual terms as actually interpreted by the arbitrator (if the arbitrator has made that interpretation known), to an interpretation implied in the award itself, or to a plausible theory of the contract's general subject matter, framework or intent.... The award must be related in a rational manner to the breach (as expressly or impliedly found by the arbitrator). Where the damage is difficult to determine or measure, the arbitrator enjoys correspondingly broader discretion to fashion a remedy."

AMD is the poster child for an arbitrator's broad, bespoke remedial discretion, beyond that of any judge or jury. There, the arbitrator found that Intel had breached the parties' technology-sharing agreement but, given no quantifiable damages from the breach, rejuvenated for two years the previously terminated sharing agreement and gave the claimant a perpetual license to certain Intel intellectual property.

Despite linguistic differences, there is likely no practical difference between the FAA's "essence" test and the CAA's "rationally related" test. *Timegate Studios, Inc. v. Southpeak Interactive, LLC*, 713 F.3d 797, 802, 806 (5th Cir. 2013) (FAA case citing *AMD); Medi-Soft, Inc. v Royco, Inc.*, 21 Fed Appx. 570, 573 (2001) (noting FAA and CAA tests yield the same result).

Examples of bespoke remedies that satisfy the *AMD* "rationally related" or *Steelworkers* "essence" test include:

· Not enforcing a mandatory attorneys' fees provision due to equity and fairness; *Safari Associates v. Superior Court*, 231 Cal.App.4th 1400 (2014), declining to follow *DiMarco v. Chaney*, 31 Cal.App.4th 1809 (1995)

· Excusing a party's performance of a contract's material condition based on equitable considerations, even where contract mandates that "the arbitrator may not modify or change any material terms of the contract," *Gueyffier v. Ann*, 43 Cal. 4th 1179, 1186 (2008)

· Adding express or implied conditions to a contract performance to prevent an inequitable result; *VVA-Two LLC v. Impact Development Group, LLC*, 48 Cal.App. 5th 985 (2020); *Mutual Ins. Co. v. Unigard Sec.*, 44 F.3d 825, 831 (9th Cir. 1995)

Examples of novel remedies that do not satisfy the *AMD* "rationally related" or *Steelworkers* "essence" test include:

· Ordering that withdrawing partners forfeit their capital accounts, contrary to the express terms of the partnership agreement; *O'Flaherty v. Belgum*, 115 Cal.App. 4th 1044, 1061 (2004)

· Awarding salaries and wages to claimants where claimants received these payments before any dispute and were never sought by the claimants in the arbitration; *Matter of County of Nassau v. Nassau County Sheriffs' Correction Officers Bene. Ass'n.*, 2024 NY Slip Op 00069 (NY App. Div. 2024)

· Imposing a remedy that was contrary to regulations expressly incorporated into the contract; *Aspic Engineering & Construction Co. v. EEC Centcom Constructors LLC*, No. 17-16510, 2019 U.S. App. LEXIS 2774 (9th Cir. Jan. 28, 2019)

The practical lessons from *AMD* and *Steelworkers* are at least the following:

First, the parties by agreement can limit an arbitrator from awarding remedies that are beyond what a jury or judge could award, *AMD*, 9 Cal. 4th at 364, but it is unclear what language would be adequate. Perhaps the following might work:

"(1) The arbitrator may only award damages or other relief that could be issued by a jury. (2) In issuing any relief for any claim arbitrated pursuant to this agreement, the arbitrator may not impose conditions other than those expressly stated in this agreement, may not create, extend, shorten, or otherwise modify any right or duty under this agreement, and must strictly construe the express terms of this agreement. (3) The arbitrator may not award punitive damages, or any award of attorneys' fees or costs to any party identified as being prevailing in the arbitration for any reason whatsoever, including because equity or justice justifies such award. (4) If the arbitrator determines that a breach of this agreement has occurred but that there are no damages associated with such breach, or that any damages are uncertain or indeterminate, the arbitrator must award no damages, injunctive or other relief for such breach. (5) Any remedy issued by the arbitrator that violates in whole or part subsections (1), (2), (3), or (4) are in excess of the arbitrator's powers."

Second, even in the absence of a contractual "remedy limitation," many arbitrators self-impose the constraint that they will impose or award only a remedy that is allowed by law and would be awardable by a judge or jury.

Third, counsel representing a party in arbitration must couch their justification for, or opposition to, any proposed remedy in terms of what is or what is not rationally related to, or based on, the essence of the contract and any alleged breach. This is easier said than done, particularly because the case law applying *AMD* or *Steelworkers* includes cases having inconsistent holdings on what sort of remedy is or is not in excess of the arbitrator's powers.

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