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## ADR Report

### The Arbitrator's Right Even if He's Wrong, Right? Wrong:

#### *Richey v. Autonation*

By Joel M. Grossman

It is a longstanding principle of California law that an arbitration award may not be vacated because the arbitrator made an error of law. As the California Supreme Court stated in *Moncharsh v. Heily & Blase*:<sup>1</sup> “[I]t is within the power of the arbitrator to make a mistake either legally or factually. When parties opt for the forum of arbitration, they agree to be bound by the decision of that forum knowing that arbitrators, like judges, are fallible.”<sup>2</sup> The court went on to say that “[t]he arbitrator’s decision should be the end, not the beginning of the dispute.”<sup>3</sup> The court expressly stated that “[t]he merits of the controversy between the parties are not subject to judicial review.”<sup>4</sup>

In line with judicial opinions prohibiting review of an arbitrator’s award, the Legislature established very limited grounds for vacating an award, set forth in Cal. Code Civ. Proc. § 1286.2: (1) the award was procured by corruption, fraud, or undue means; (2) the arbitrator was corrupt; (3) the award was affected by prejudicial misconduct by the arbitrator; or (4) the arbitrator exceeded his or her powers. The court in *Moncharsh* made clear that an arbitrator does not exceed his or her powers merely by committing an error of law. If that were the case, the exception would swallow the rule and virtually all arbitration awards could be challenged on the grounds that the arbitrator’s interpretation of the law was erroneous.<sup>5</sup> Thus, the state of the law as of *Moncharsh* was that absent the very limited exceptions set forth in the Code of Civil Procedure, an award would not be vacated even if the arbitrator’s award was clearly

wrong. (As this article was going to print, the California Supreme Court unanimously granted review of *Richey*.)

In *Pearson Dental Supplies, Inc. v. Superior Court*,<sup>6</sup> the California Supreme Court first acknowledged that an arbitrator’s erroneous interpretation of law does not mean he or she exceeded their powers. The court held, however, that because the arbitration concerned a claim involving unwaivable statutory rights, the arbitrator exceeded his powers when he incorrectly dismissed the claim based on the statute of limitations, thereby depriving the claimant of a hearing on the merits. In that case, the court determined that the arbitrator had made a clear error of law by misinterpreting a tolling provision that would have extended the claimant’s limitations period. This error of law had the effect of completely denying the claimant the ability to litigate his unwaivable statutory claim under the Fair Employment and Housing Act (FEHA).

The *Pearson* court was careful to explain that it was creating a narrow exception based on the facts before it, stating:

We address only the case before us, and a narrower rule is sufficient for its resolution. Here, as a result of the arbitrator’s clear legal error, plaintiff’s claim was incorrectly determined to be time-barred. . . . We therefore hold that when, as here, an employee subject to a mandatory employment

arbitration agreement is unable to obtain a hearing on the merits of his FEHA claims, or claims based on other unwaivable statutory rights because of an arbitration award based on legal error, the trial court does not err in vacating the award.<sup>7</sup>

The court went on to explain that an arbitrator exceeds his or her powers when an erroneous ruling has the effect of denying the claimant a hearing on the merits.

With the broad policy of limited review of arbitration awards announced in *Moncharsh* and the narrow exception set forth in *Pearson* as background, we come to the recent decision of *Richey v. Autonation, Inc.*<sup>8</sup> In *Richey*, an employee claimed that his employer violated the Moore-Brown-Roberti Family Rights Act (CFRA) by terminating his employment during a CFRA-authorized leave. The employer had a policy prohibiting employees from working for another employer or their own business while on CFRA leave. Several employees informed the employer that the plaintiff worked at a restaurant that he owned while on leave. The plaintiff claimed that his duties at the restaurant were minimal, and they conformed with his doctor’s restrictions. Nevertheless, believing that the plaintiff was abusing his CFRA leave by working at his restaurant, the employer let him go.

The arbitration was held over a period of eleven days. Relying on prior case law, the arbitrator ruled for the employer based on what the

court of appeal called the “honest belief” defense. The court quoted the following from the arbitrator’s award: “An employer who honestly believes that it is discharging an employee for misusing [family and medical leave] is not liable even if the employer is mistaken.”<sup>9</sup> As the court explained, the arbitrator held that the employer did not violate the CFRA if it had an honest belief that the employee was abusing the leave of absence. The plaintiff sought to vacate the award, but the trial court denied the motion, agreeing with the arbitrator that the employer’s good faith belief about the employee’s abuse of his CFRA leave was a valid defense.

The court of appeal held that the arbitrator’s reliance on the “honest belief” defense was clear legal error, and the award should have been vacated.<sup>10</sup> The court therefore reversed the trial court’s decision and ordered the award vacated. The court of appeal relied on *Pearson’s* holding that, notwithstanding the general rule that an arbitration award may not be vacated simply because the arbitrator was wrong, an award may be vacated if there is clear legal error

that has the effect of denying the plaintiff a hearing on the merits of his unwaivable statutory claim: The arbitrator’s “improper acceptance of the honest belief defense in this case had a similarly [i.e. similar to the statute of limitations error in *Pearson*] preclusive effect on Richey’s ability to have his nonwaivable CFRA claims heard on the merits.”<sup>11</sup>

The court noted that the arbitrator’s recognition of the “honest belief” defense was not exactly the same as the *Pearson* arbitrator’s total denial of a hearing on the merits due to the statute of limitations. Still, the court determined that because the arbitrator allowed the employer to rely on this defense, there was not a full and fair hearing on the merits, stating, “the honest belief defense relieves the employer of any obligation to establish its employee was, in fact, misusing authorized family leave and thus subverts the express statutory guarantee of the right to reinstatement, as well as the allocation of the burden of proof in an interference case.”<sup>12</sup> Thus, just as the plaintiff in *Pearson* was denied a hearing on the merits of his statutory

claim, so too, because the arbitrator ruled that it did not matter whether the plaintiff in *Richey* actually engaged in activity that would be deemed an abuse of the CFRA, and instead relied on the employer’s honest belief that the plaintiff had engaged in such conduct, he was denied a full hearing on the merits of his case.

The court of appeal’s holding that a party who spends eleven days in arbitration has been in effect denied a hearing on the merits raises certain questions about how far the *Pearson* holding may be taken. There can be little doubt that the arbitrator’s legal error regarding the statute of limitations in *Pearson* had the effect of denying that plaintiff a hearing on the merits. But is that also the case in *Richey*, considering that the case was litigated over eleven days? Even if the arbitrator was wrong in relying on the honest belief defense, should the award nevertheless have been affirmed under *Moncharsh* because legal error is not enough to support vacating the award? To put it another way, is *Richey’s* holding effectively that legal error will be a basis for

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vacating an arbitration award when the arbitration concerned an unwaivable statutory right?

Consider, for instance, the following example. A plaintiff brings a claim in arbitration against her employer under FEHA, asserting that she has been sexually harassed. She claims that the alleged harasser is a supervisor, and that the employer is therefore liable for the harassment. At the hearing, the employer argues that the alleged harasser was not a supervisor, but rather a co-worker, and the employer had no knowledge of the harassing acts. Each party introduces evidence regarding its position on the status of the alleged harasser. The arbitrator holds that the alleged harasser was a co-worker, and that there is no need to determine whether or not the alleged harassment actually occurred, because the employer is not liable for the harassment.

Here is another example: A worker brings a claim in arbitration, contending that he has worked many hours of overtime but has not been paid at the required overtime rates under the applicable wage order and the Labor Code. The employer argues that the worker is actually a manager, and therefore exempt from overtime. A hearing is held, and each

side introduces evidence on the issue of whether the employer properly classified the employee as exempt. The arbitrator determines that the employee is indeed a manager and exempt from overtime under the applicable wage order. The arbitrator therefore does not determine whether the employee actually worked any hours beyond eight in a day or forty in a week.

Assume that the arbitrators' holdings in each of these two cases—that the alleged harasser was not a supervisor, and that the employee who was denied overtime was exempt—are later determined to be clear error by a reviewing court. Should these arbitration awards therefore be vacated under *Richey* because each asserts an unwaivable statutory claim, and the plaintiffs were each denied a full hearing on the merits of their claims? Or should these cases fall under the general rule set forth in *Moncharsh* that an award may not be vacated just because the arbitrator's ruling was wrong? In other words, when an arbitrator rules that a particular defense applies to a case involving unwaivable statutory rights, must the trial court review that ruling, and vacate the award if the arbitrator committed an error of law? Under *Richey* the answers are

unclear, and may remain so until the supreme court clarifies the scope of its ruling in *Pearson*.<sup>12</sup>

## ENDNOTES

1. 3 Cal. 4th 1 (1992).
2. *Id.* at 10.
3. *Id.*
4. *Id.* at 11, quoting *O'Malley v. Petroleum Maintenance Co.*, 48 Cal. 2d 107, 111 (1957).
5. *Id.* at 28.
6. 48 Cal. 4th 665 (2010).
7. *Id.* at 679-80.
8. 210 Cal. App. 4th 1516 (2012), review granted, 2013 WL 541070 (Feb. 13, 2013). S207536/B234711. As this article was going to print, the California Supreme Court unanimously granted review of *Richey*.
9. *Id.* at 1522.
10. The focus of this article is the issue of when an arbitration award may be vacated based on the arbitrator's legal error. For this reason, the article does not discuss the court of appeal's lengthy analysis of the "honest belief" defense under the CFRA and FMLA.
11. *Richey, supra*, 210 Cal. App. 4th at 1537.
12. *Id.* at 1539.

