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When Regulations and Arbitration Awards Collide: Potential Difficulties for Arbitrators and Parties

*Bangor Gas Co., LLC v. H.Q. Energy Serv. U.S. Inc.*¹

INTRODUCTION

Many commercial transactions are complex. The increasing presence of both arbitration and administrative regulations are part of what creates this complexity.² It is thus possible that parties to a commercial transaction will find themselves in arbitration over a dispute involving regulations. This note will explore the potential difficulties parties and arbitrators face when arbitration awards and regulations collide. The difficulties for parties include grounds for vacatur that are either non-existent or hard to meet, and potentially being forced to choose between violating a regulation or not complying with the award. Additionally, arbitrators face difficulties in fashioning awards that comply with regulations, especially because early communications with agencies are usually non-binding.

FACTS AND HOLDING

Four hundred and ten feet of piping in Maine seems insignificant, but it was sufficient to spark a contentious dispute between two companies in the natural gas industry.³ H.Q. Energy Services Inc. (HQ), a natural gas supplier, and Bangor Gas Company (Bangor), a pipeline owner, entered into an agreement for the transportation of HQ's gas via Bangor's pipeline.⁴ The crux of the agreement was that Bangor would build a pipeline (the "Bucksport") that would carry HQ's gas from an international pipeline (the "Maritimes") to an energy plant nine miles away.⁵ Bangor built a 410 foot pipeline (the "Lateral") to connect the Maritimes to the Bucksport without HQ's knowledge.⁶ Bangor initially paid for the costs of the Lateral's use.⁷ Six years into the agreement, Bangor discovered that its use of the Lateral might violate Federal rules.⁸

1. *Bangor Gas Co., LLC v. H.Q. Energy Serv. U.S. Inc.*, 695 F.3d 181, 183-84 (1st Cir. 2012).

2. 2 Robert L. Haig, N.Y. PRACTICE SERIES — COMMERCIAL LITIGATION IN NEW YORK STATE COURTS § 9:29 (2013).

3. *Bangor*, 695 F.3d at 183-84.

4. *Id.* at 183.

5. *Id.* Bangor would transfer HQ's gas for 15 years in return for a \$1,150,662 annual fee, paid in monthly installments. *Id.*

6. *Id.* at 184.

7. *Id.*

8. *Id.*

A Federal Energy Regulatory Commission (FERC) rule requires the shipper of natural gas to hold title to the gas it was shipping.⁹ Bangor feared that it could be deemed to be the “shipper” of the gas going through the Lateral because it owned the Lateral.¹⁰ Since the gas being shipped through the Lateral belonged to HQ, Bangor feared it could be in violation of the rule.¹¹ To avoid this risk, Bangor entered into “capacity releases” on the Lateral with HQ.¹² Bangor also threatened to place the capacity rights to the Lateral on the open market if HQ did not pay the costs of using the Lateral.¹³ HQ disagreed, believing it shouldn’t have to pay additional costs for the use of the Lateral, pursuant to the agreement.¹⁴

A dispute also arose regarding which party should pay the costs of heating the gas at the points at which it entered and left the Bucksport.¹⁵ Bangor had been paying the costs at both points up until the dispute arose.¹⁶ The agreement required that “irreconcilable disputes” be submitted to arbitration.¹⁷ Bangor began the arbitration process in 2010, by submitting several claims.¹⁸

Bangor argued that HQ should pay the costs associated with the use of the Lateral, and expenses required to heat the gas at both the Bucksport entry and exit points.¹⁹ HQ denied that it was obligated to make these payments, and sought reimbursement for the few Lateral payments it had made.²⁰ The three-person arbitration panel held that Bangor was responsible for the Lateral costs.²¹ It reasoned that Bangor’s internal documents showed it had factored the costs of the Lateral into the monthly fee HQ owed, and thus HQ was *already* paying the Lateral costs.²² The panel also designed a payment structure to allow the parties’ Agreement to circumvent the FERC regulation: Bangor would release its Lateral capacity to HQ, and HQ would pay for the Lateral’s use.²³ Bangor would then reduce HQ’s monthly fee to reflect the costs of the Lateral.²⁴ Finally, the panel required that Bangor pay the gas heating costs at the point the gas entered the Bucksport, while HQ would pay the heating costs at the point where it left the Bucksport and entered the energy plant.²⁵ Under the award, HQ was not required to reimburse Bangor for the heating costs that Bangor had previously paid, as HQ had inherently already made these payments in its monthly fee to Bangor.²⁶

9. *Bangor*, 695 F.3d at 184. “The aim of the rule is to prevent big natural distributors from buying up pipeline capacity that they do not need for shipment of their own gas and leveraging their market power by selling capacity to third parties at excessive prices.” *Id.*

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.*

14. *Id.*

15. *Bangor*, 695 F.3d at 184.

16. *Id.* at 185.

17. *Id.*

18. *Id.*

19. *Id.*

20. *Id.*

21. *Bangor*, 695 F.3d at 185.

22. *Id.*

23. *Id.*

24. *Id.*

25. *Id.*

26. *Id.*

Bangor filed a motion to vacate the award in the United States District Court for the District of Maine, based on the panel's order that Bangor pay the Lateral costs, and that HQ need not reimburse Bangor.²⁷ The district court denied Bangor's motion and granted HQ's cross-motion to confirm the award.²⁸ Bangor appealed the district court's decision. On appeal, the United States First Circuit Court of Appeals affirmed the district court's ruling.²⁹

Bangor argued on appeal that the vacatur was necessary because the panel had manifestly disregarded the law in holding Bangor responsible for the costs of the Lateral.³⁰ Bangor also argued that the panel's decision to charge each party for one portion of the heating costs was a compromise, and because the agreement contained a "no compromise" provision, the panel had manifestly disregarded the law.³¹

The First Circuit held that even if the manifest disregard doctrine³² were valid, the panel had not manifestly disregarded the law in holding Bangor responsible for the costs of the Lateral.³³ Additionally, the panel's solution to ensure the parties were not in violation of the FERC regulation was not in manifest disregard of the law.³⁴ Lastly, the court held that the panel's award did not violate the agreement's "no compromise" clause, and thus the panel had not acted in manifest disregard of the law in deciding which party would pay to heat the gas upon entry and exit of the pipeline.³⁵

LEGAL BACKGROUND

In passing the Federal Arbitration Act (FAA), Congress announced a clear national policy favoring arbitration as a means of resolving disputes.³⁶ The FAA was enacted to combat rampant judicial disfavor of arbitration agreements, and requires courts to enforce such agreements whenever possible.³⁷ The FAA provides four grounds on which a federal court may vacate an arbitration award.³⁸

27. *Bangor*, 695 F.3d at 186.

28. *Id.*

29. *Id.*

30. *Id.* at 188.

31. *Id.* at 190.

32. *Id.* at 187. See also *Bull HN Info. Sys., Inc. v. Hutson*, 229 F.3d 321, 330-331 (1st Cir. 2000) (explaining that in the First Circuit, an arbitrator "manifestly disregards" the law if he recognizes the applicable law, yet issues an order that disregards it).

33. *Bangor*, 695 F.3d at 187.

34. *Id.* at 189.

35. *Id.* at 191.

36. *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984).

37. *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1745-46 (2011).

38. 9 U.S.C. § 10(a) (2012).

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration-- (1) where the award was procured by corruption, fraud, or undue means; (2) where there was evident partiality or corruption in the arbitrators, or either of them; (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

These four grounds are: (1) the award was influenced by corruption or fraud; (2) partiality or corruption on the part of the arbitrators; (3) the arbitrators refusal to postpone a hearing when sufficient cause is shown or refusal to hear evidence relevant and material to the controversy; and (4) where the arbitrators have exceeded their powers.³⁹ Courts have long wrestled with the question of whether these four grounds constitute the exclusive means by which a court may vacate an award.⁴⁰

The First Circuit permitted courts to conduct a limited review of arbitration awards, and vacate under circumstances not contemplated by the four express grounds for vacatur outlined in Section Ten of the FAA.⁴¹ The First Circuit joined other circuits, finding that a “manifest disregard for the law” is implicit in a finding that a court “exceeded [its] powers,”⁴² the First Circuit used the term “manifest disregard of the law.”⁴³

In the First Circuit, the law was considered to have been “manifestly disregarded” when the record showed that the arbitrator recognized the applicable law and then ignored it.⁴⁴ An award is also in manifest disregard of the law if it is contrary to the plain language of the applicable arbitration agreement.⁴⁵ Prior to the 2008 case *Hall St. Assoc., LLC v. Mattel, Inc.*,⁴⁶ courts in the First Circuit were permitted to vacate awards if either of these showings were made.⁴⁷ The Supreme Court’s holding in *Hall St.*, however, brought this practice into question.⁴⁸

In *Hall Street*, the Supreme Court acknowledged that the federal circuits were divided as to whether parties to an arbitration agreement could expand the grounds for vacatur of an award, beyond those listed in Section Ten of the FAA.⁴⁹ In a footnote, the Court mentioned that the First, Third, Fifth and Sixth circuits had previously held that parties were able to contract for additional grounds for vacatur, while the Ninth and Tenth circuits had taken the opposite approach.⁵⁰ Circuits that favored allowing parties to contract for additional grounds for vacatur of an arbitration agreement reasoned that doing so honored party-autonomy, a major goal of the FAA.⁵¹ However, the Supreme Court agreed with the Ninth and Tenth Circuits, holding that the grounds for vacatur found in Section Ten of the FAA were the exclusive means by which a reviewing court could vacate an award.⁵²

In a footnote of its *Ramos-Santiago* decision, the First Circuit stated in dicta that *Hall Street* decision had invalidated the “manifest disregard” ground for vacatur.

Id.

39. *Id.*

40. Stephen L. Hayford, *Law in Disarray: Judicial Standards for Vacatur of Commercial Arbitration Awards*, 30 GA. L. REV. 731, 763 (1996).

41. *Arvest, Inc. v. McCarthy*, 914 F.2d 6, 8 (1st Cir. 1990).

42. *Comedy Club, Inc. v. Improv W. Assocs.*, 553 F.3d 1277, 1290 (9th Cir. 2009) (stating that the “manifest disregard” ground is “shorthand” for the “exceeded their powers” ground).

43. *McCarthy v. Citigroup Global Mkts. Inc.*, 463 F.3d 87, 91 (1st Cir. 2006).

44. *Bull HN Info. Sys., Inc. v. Hutson*, 229 F.3d 321, 330-31 (1st Cir. 2000).

45. *Id.* (citing *Advest Inc. v. McCarthy*, 914 F.2d 6, 9 (1990)).

46. *Hall St. Assoc., LLC v. Mattel, Inc.*, 552 U.S. 576 (2008).

47. *Id.*

48. *Id.* at 592.

49. *Id.* at 583.

50. *Id.*

51. *Kyocera Corp. v. Prudential-Bache Trade Servs.*, 341 F.3d 987, 1000 (9th Cir. 2003).

52. *Hall St. Assocs.*, 552 U.S. at 586.

tur, as it was not among the four grounds expressly enumerated in Section Ten.⁵³ Two years later, the First Circuit clarified that while it had “referred” to whether “manifest disregard” had survived *Hall Street*, it had done so in dicta and had therefore not “squarely” determined whether it was still a viable ground for vacatur.⁵⁴ Another two years passed before the First Circuit was again faced with the validity of the “manifest disregard” standard for vacatur, in *Bangor*.

There has been a circuit split as to whether the manifest disregard standard survived the Supreme Court’s decision in *Hall Street*; the First Circuit’s hesitation to make a sweeping declaration is not unique.⁵⁵ The Second Circuit and Ninth Circuits held that the manifest disregard standard is still a viable ground for vacatur.⁵⁶ The Sixth Circuit adheres to this approach as well.⁵⁷ It held that it would be “imprudent” to interpret *Hall Street* as having eliminated “manifest disregard” because the doctrine was “universally-recognized” prior to the decision.⁵⁸ However, other courts have come to the opposite conclusion.

One year after the Supreme Court’s *Hall Street* decision, the Fifth Circuit held that, as a non-statutory ground for vacatur, “manifest disregard” was invalid after *Hall Street*.⁵⁹ District courts throughout the country have come to the same conclusion.⁶⁰ Federal district courts in Texas and Minnesota have reasoned that since *Hall Street* limited review of awards to *statutory* grounds, the judicially-created “manifest disregard” doctrine is no longer viable.⁶¹ Despite this circuit split, the Supreme Court recently declined to consider the issue.⁶² In *Stolt-Nielsen, S.A. v. AnimalFeeds Int’l Corp.*, the Court stated in a footnote that it had not decided whether its decision in *Hall Street* did away with the “manifest disregard” standard.⁶³ However, “Manifest disregard” is not the only ground for vacatur that the courts have derived from Section Ten of the FAA.

Some courts have allowed vacatur under the “exceeds their powers” prong of FAA Section Ten to include vacatur when an award violates public policy.⁶⁴ Like the “manifest disregard” doctrine, this theory was borrowed is derived from the common law rule that courts can refuse to enforce illegal contracts.⁶⁵ The implicit “public policy” ground for vacatur is narrow in scope, and courts are hesitant to invoke it.⁶⁶ Reliance on this exception requires a showing that the public policy

53. Ramos-Santiago v. U.P.S., 524 F.3d 120, 124 (1st Cir. 2008).

54. Kashner Davidson Secs. Corp. v. Mscisz, 601 F.3d 19, 22 (1st Cir. 2010).

55. Leigh F. Gill, *Manifest Disregard After Hall Street: Back from the Dead – the Surprising Resilience of a Non-Statutory Ground for Vacatur*, 15 LEWIS & CLARK L. REV. 265, 268 (2011).

56. T.Co Metals, LLC v. Dempsey Pipe & Supply, Inc., 592 F.3d 329, 340 (2d Cir. 2010); Comedy Club, Inc. v. Improv W. Assocs., 553 F.3d 1277, 1290 (9th Cir. 2009).

57. Coffee Beanery, Ltd. v. WW, L.L.C., 300 F. App’x 415, 419 (6th Cir. 2008).

58. *Id.*

59. Citigroup Global Mkts., Inc. v. Bacon, 562 F.3d 349, 355 (5th Cir. 2009).

60. The Householder Group v. Caughran, 756 F. Supp. 2d 796, 800 (E.D. Tex. 2008); Prime Therapeutics LLC v. Omnicare Inc., 555 F. Supp. 2d 993, 999 (D. Minn. 2008).

61. *Householder Group*, 756 F. Supp. 2d at 800; *Prime Therapeutics*, 555 F. Supp. 2d at 999.

62. *Stolt-Nielsen, S.A. v. AnimalFeeds Int’l Corp.*, 130 S. Ct. 1758, 1768 (2010).

63. *Id.*

64. *Bangor Gas Co., LLC v. H.Q. Energy Serv. U.S. Inc.*, 695 F.3d 181, 187 (1st Cir. 2012); *United Paperworkers Int’l Union, AFL-CIO v. Misco, Inc.*, 484 U.S. 29, 42 (1987); 1 Jay E. Grenig, *ALT. DISP. RESOL.* §24:19 (3d ed. 2013).

65. *Mercy Hosp., Inc. v. Mass. Nurses Ass’n*, 429 F.3d 338, 343 (1st Cir. 2005).

66. *Id.*; *United Food & Commercial Workers Int’l Union, Local 588 v. Foster Poultry Farms*, 74 F.3d 169, 174 (9th Cir. 1995).

allegedly violated is “explicit, well-defined and dominant.”⁶⁷ While expressions of public policy are generally found in statutes and constitutions,⁶⁸ they can also be found in administrative regulations.⁶⁹

Both the California Supreme Court and the Third Circuit have used the public policy exception to vacate arbitration awards.⁷⁰ Both cases involved public health and safety regulations, and both courts stressed that public policy reasons for vacating an arbitration award more readily found when such considerations are present.⁷¹

Administrative agencies possess the authority to give administrative guidance and advice as to the application of the statutes and regulations that they are responsible for promulgating.⁷² Agencies often provide guidance on a particular statute or regulations due to its complex nature.⁷³ However, administrative guidance, whether in written or oral form, is merely instructive, and does not bind the agency.⁷⁴ In *Bangor*, administrative guidance as to the application of a Federal Energy Regulatory Commission (FERC) rule was at issue.⁷⁵ The advice was in the

67. *Int'l Bhd. of Elec. Workers, Local 97 v. Niagara Mohawk Power Corp.*, 143 F.3d 704, 715 (2d Cir. 1998).

68. Sandra J. Rosenthal, *Kulch v. Structural Fibers, Inc.: Clarifying the Public Policy Exception*, 45 CLEV. ST. L. REV. 681, 683 (“public policy . . . can stem from a federal statute, the Ohio and United States Constitutions”).

69. *Id.*; *Exxon Shipping Co. v. Exxon Seamen’s Union*, 993 F.2d 357, 360-61 (3d Cir. 1993) (holding that Coast Guard regulation an expression of public policy).

70. *Green v. Ralee Eng’g Co.*, 950 P.2d 1046 (Cal. 1998); *Exxon Shipping*, 993 F.2d 357.

71. *Id.*

72. Donna M. Nagy, *Judicial Reliance on Regulatory Interpretations in SEC No-Action Letters: Current Problems and a Proposed Framework*, 83 CORNELL L. REV. 921, 935 (1998). Examples include “no-action letters” from the Securities and Exchange Commission and “private letter rulings” from the Internal Revenue Service. *Id.*

73. See *supra* note 60; Nagy, *supra* note 71, at 933-934.

Notwithstanding the SEC’s efforts to clarify provisions in the federal securities laws through rulemaking, adjudication, and the issuance of SEC releases, securities law practitioners constantly struggle to apply statutory provisions and SEC rules to specific securities transactions contemplated by their clients. The Commission has long recognized and appreciated this struggle. Consequently, from its earliest days, the Commission has encouraged its staff to provide advice and guidance to those seeking assistance.

Id.

74. *The Householder Group v. Caughran*, 756 F. Supp. 2d 796, 800 (E.D. Tex. 2008); *Prime Therapeutics LLC v. Omnicare Inc.*, 555 F. Supp. 2d 993, 999 (D. Minn. 2008). Nagy, *supra* note 72, at 936 (“The SEC’s procedural rules, for example, describe the availability of ‘informal administrative interpretations’ and specifically provide that ‘opinions expressed by members of the staff do not constitute an official expression of the Commission’s views.’”).

75. *Bangor Gas Co., LLC v. H.Q. Energy Serv. U.S. Inc.*, 695 F.3d 181, 182 (1st Cir. 2012). “The rule is not a codified regulation but was announced by FERC in an adjudication of a specific dispute.” *Tex. E. Transmission Corp.*, 37 FERC 61260, 61685 (1986). See also William Demarest, *Gas Marketing by the Operator Under a JOA — Unrecognized Regulatory Risks and Practical Solutions*, 64 Okla. L. Rev. 135, 136-38 (2012).

A central requirement of the Commission’s open-access transportation program is that all shippers must have title to the gas at the time the gas is tendered to the pipeline or storage transporter and while it is being transported or held in storage by the transporter. Interstate pipeline tariffs include provisions requiring shippers to warrant good title to the gas tendered for transportation on the pipeline. Although specific language of each interstate pipeline’s tariff varies, the Commission has made clear that the shipper of record and the owner of the gas must be one and the same throughout the course of the transportation or duration of storage on any pipeline.

Nat’l Energy & Trade, L.P. Mission Valley Pipeline Co., 134 FERC 61072, 61347 (Jan. 31, 2011).

form of an oral statement by an FERC staff member, and was not binding on the agency.⁷⁶

INSTANT DECISION

Bangor made clear that, after *Hall Street*, the First Circuit does not recognize the “manifest disregard” doctrine as a ground for vacatur.⁷⁷ This finding alone was dispositive of the case, as all of *Bangor*’s vacatur arguments were premised on “manifest disregard.”⁷⁸ *Bangor* had argued that the arbitrators had manifestly disregarded the law by requiring it to pay the Lateral use costs, and not requiring HQ to reimburse it for previously paid heating costs.⁷⁹ The court stated that even if “manifest disregard” had survived the Supreme Court’s decision in *Hall Street*, *Bangor*’s arguments would still fail.⁸⁰

Bangor argued that the arbitration panel’s decision ordering *Bangor* to pay for the costs of the Lateral pipeline were the result of the panel ignoring the law, and therefore acting with “manifest disregard” of the law.⁸¹ The court responded by stating that while the plain language of the contract required *Bangor* to pay this cost,⁸² the court found the contract did not mention the Lateral pipeline, and that *Bangor* had incorporated the cost of the Lateral pipeline into HQ’s monthly fee.⁸³ Requiring HQ to pay for the Lateral would mean HQ was paying for the same service twice.⁸⁴ Therefore, the court found the panel had not ignored the plain language of the contract.⁸⁵

Bangor also argued that ordering it to pay for the costs of the Lateral violated FERC’s “shipper must have title” rule, and therefore ignored the law.⁸⁶ *Bangor* argued that this was the case even though the panel had come up with a unique payment structure specifically to ensure that the award was in compliance with the FERC regulation.⁸⁷ The court acknowledged that agency regulations were “sovereign commands” and that an award would be “vulnerable” if it ran afoul of them.⁸⁸ However, it found the panel’s payment mechanism did not ignore the law.⁸⁹

First, the court explained the panel had considered the “shipper-must-have-title” rule at issue when it specifically crafted its award to comply with the regulation.⁹⁰ The court next stressed that the only communications between the parties

76. *Bangor*, 695 F.3d at 190 (citing *Indianapolis Power & Light Co.*, 48 FERC 61040, 61203 (July 11, 1989)).

77. *Id.* at 187.

78. *Id.* at 186.

79. *Id.*

80. *Id.* at 187.

81. *Id.* at 188.

82. *Bangor*, 695 F.3d at 188.

83. *Id.*

84. *Id.*

85. *Id.*

86. *Id.*

87. *Id.*

88. *Bangor*, 695 F.3d at 188.

89. *Id.*

90. *Id.* at 189.

and the FERC was through letters between Bangor and FERC.⁹¹ FERC officials also explicitly said these letters were not binding or definitive.⁹² Finally, the court held the payment structure did not contravene the purpose of the “shipper-must-have-title rule,” which was to ensure that gas companies did not purchase long stretches of pipeline in order to drive up costs for competitors.⁹³ The FERC regulation did not apply to the Lateral, as it was a small line, the only purpose of which was to transfer gas from the Maritimes to the Bucksport.⁹⁴

Bangor’s final argument was that the award was in “manifest disregard” of the law because the panel had ignored the “no compromise” provision of the agreement.⁹⁵ Bangor argued that requiring HQ to begin paying the end-of-the-line heating costs, but not requiring it to reimburse Bangor for the six years Bangor had paid the costs, constituted a compromise.⁹⁶ The court was not persuaded, and held that who should pay end-of-the-line heating costs from the date of the arbitration decision, and who should shoulder the previous costs, were separate questions.⁹⁷ As such, the court explained that the arbitration panel had not ignored the law by deciding each question on the merits, even if the individual decisions didn’t benefit the same party.⁹⁸ The court pointed out that judges regularly separate retroactive issues and issues affecting future conduct, and generally have less “freedom than arbitrators.”⁹⁹

COMMENT

The arbitration panel that decided the dispute between Bangor and HQ was responsible for ensuring that its award complied with the FERC’s “shippers must have title” rule. Where arbitrators are required to consider the legality of their decisions under a complex set of regulations uncertainty and confusion are likely. This is especially true where the relevant agency has only expressed its position through a private letter ruling, as was the case in *Bangor*.

91. *Id.* at 188. Bangor requested a “No-Action Letter” from the FERC, to provide it “assurance” against an FERC enforcement action. *Id.* FERC’s General Counsel denied Bangor’s request, but sent a letter expressing the view that the panel’s remedy violated the rule. FERC staff also told Bangor that the letter was not binding. *Id.*

92. *Id.* at 190.

93. *Id.* at 189.

94. *Bangor*, 695 F.3d at 189.

95. *Id.* at 190.

96. *Id.* at 190-91. The “no compromise” clause in the agreement stated that:

In the event that the arbitration requires a decision (i) as to the allocation or payment of any monetary amounts or valuations to be reduced to monetary amounts, or (ii) the methodology or accuracy of any calculation related thereto, the arbitrators shall select the position of that Party which the arbitrator believes most appropriate under the circumstances. No “compromise” determination or alternate calculations shall be made by the arbitrator who is bound to adopt the position of one Party to the exclusion of the other on such matters.

Id.

97. *Id.* at 191.

98. *Id.*

99. *Id.*

Arbitration agreements are increasingly present in the commercial setting.¹⁰⁰ Both state and federal administrative regulations are also relevant in commercial arbitration.¹⁰¹ Naturally, arbitration awards and agency regulations can coexist, as they did in *Bangor*. A fundamental concept of arbitration is that parties to arbitration are bound by the arbitrator's decision.¹⁰² As a result, the collision of regulations and the arbitration process can put arbitrators and the parties in a difficult position.

If an arbitrator misinterprets a regulation and fashions an award, compliance with which would require a party to violate a regulation, the party may be liable for civil penalties.¹⁰³ Additionally, failure to comply with an arbitration award may put a party at risk of further legal action from the adverse party. The solution to this problem seems clear: an award that forces a party to violate a regulation cannot possibly be valid. This may be the case, but a party seeking to vacate such an award may face an uphill battle.

A party bound by an arbitration award that is not in compliance with a relevant regulation can seek to have the award vacated on public policy grounds. This ground requires the establishment of a dominant, well-defined public policy through "laws and legal precedents."¹⁰⁴ As mentioned above, some courts have read the "exceeds their powers" prong of Section Ten of the FAA as allowing vacatur when an award violates public policy.¹⁰⁵ An award that violates a regulation would seem to inherently be in violation of public policy.

Violation of an economically-focused regulation, like the one in *Bangor*, might not meet this standard. The key is the establishment of a strong public policy, dominant and fundamental enough to meet the standard. A California Supreme Court case, *Green v. Ralee Engineering Co.*, illustrates this dilemma.¹⁰⁶ The *Green* court stated that public policy objectives are often preserved in regulations, they are *especially* found in regulations that promote important legislative objectives and those that protect public health safety.¹⁰⁷ The court specifically found that a Federal Aviation Administration regulation dealing with manu-

100. Stephen Hayford & Ralph Peeples, *Commercial Arbitration in Evolution: An Assessment and Call for Dialogue*, 10 OHIO ST. J. ON DISP. RESOL. 343, 347 (1995) (stating "the use of commercial arbitration has begun to accelerate.")

101. Thomas W. Merrill, *Toward A Principled Interpretation of the Commerce Clause*, 22 HARV. J.L. & PUB. POL'Y 31, 35 (1998).

102. *Daisy Mfg. Co., Inc. v. NCR Corp.*, 29 F.3d 389, 392 (8th Cir. 1994) ("party is bound by an arbitral award only where it has agreed to arbitrate").

103. FED. ENERGY REGULATORY COMM'N, *Civil Penalty Actions*, available at <http://www.ferc.gov/enforcement/civil-penalties/civil-penalty-action.asp> (last visited Jan. 23, 2013).

104. *W.R. Grace & Co. v. Local Union 759*, 461 U.S. 757, 766 (1983).

105. *Bangor Gas Co., LLC v. H.Q. Energy Serv. U.S. Inc.*, 695 F.3d 181, 187 (1st Cir. 2012); *United Paperworkers Int'l Union, AFL-CIO v. Misco, Inc.*, 484 U.S. 29, 42 (1987); 1 Jay E. Grenig, *ALT. DISP. RESOL. §24:19* (3d ed. 2013); Jonathan A. Marcantel, *The Crumbled Difference Between Legal and Illegal Arbitration Awards: Hall Street Associates and the Waning Public Policy Exception*, 14 *FORDHAM J. CORP. & FIN. L.J.* 615 (2009) ("the federal courts began using the public policy exception as an extra-statutory basis for vacatur under the FAA.").

106. *See generally Green v. Ralee Eng'g Co.*, 960 P.2d 1046 (1998).

107. *Id.* at 1054-55 (discussing 14 C.F.R. § 21.143, "Quality control data requirements; prime manufacturer," the court stated, "[t]he FAA . . . used the congressional grant of authority to establish an intricate regulatory scheme in order to ensure that aircraft design meets safety standards and aircraft manufactures conform to the design. Regulations require prime manufacturers (such as Boeing) to establish quality control inspection").

facturing and inspection requirements of airline parts was a valid source of public policy, in no small part because it promoted public health and safety.¹⁰⁸

A similar public policy argument was used in *Exxon Shipping Co. v. Exxon Seamen's Union*, a Third Circuit case that addressed the intersection of arbitration and regulations.¹⁰⁹ In *Exxon*, an arbitration panel forced Exxon to reinstate a helmsman who had tested positive for drugs.¹¹⁰ The award was eventually vacated as being in violation of public policy. The court found that a Coast Guard regulation prohibiting the operation of a ship by one under the influence of drugs or alcohol was "well-defined and dominant" public policy.¹¹¹ Like in *Green*, the *Exxon* court stressed that an important public policy was found because of the safety concerns at play: specifically the potentially "disastrous effects" of a large oil spill.¹¹²

In *Green* and *Exxon*, compelling arguments were made that the violation of the regulations is against public policy, given the potentially grave consequences of these violations. However, not all regulations lend themselves to such compelling arguments. For example, the purpose of the FERC regulation in *Bangor* was to create a competitive marketplace.¹¹³ This is certainly a worthwhile economic goal, but it does not involve the issues of public health and safety that the courts cited in *Green* and *Exxon*. Parties seeking to rely on the public policy rationale to vacate an arbitration award because it violates an FERC rule cannot rely on the fear of tragic airplane crashes or oil spills to motivate vacatur. The public policy exception is narrow, and courts are hesitant to use it. Thus, to successfully vacate an award on this ground a party must have a very compelling and persuasive argument. Without compelling and persuasive public health and safety considerations, arguing that public policy requires the vacatur of an arbitration award, that a party contracted for, can be a difficult task. What makes this position all the more unenviable is that if a court does not vacate the award, the party challenging it may be required to pay civil penalties for violating the relevant regulations.

Section Ten of the FAA does not specifically discuss "public policy" as a justification for vacatur. Therefore, it is entirely possible that some courts may hold that the public policy exception is no longer available, after *Hall Street*.¹¹⁴ Reliance on the "manifest disregard" doctrine is rife with problems as well. "Manifest disregard" suffers from the same legal uncertainty as reliance on a public policy argument. As discussed *supra*, several courts have interpreted *Hall Street* as invalidating the "manifest disregard" doctrine.¹¹⁵ Therefore, in some circuits, "manifest

108. *Id.*

109. See generally *Exxon Shipping Co. v. Exxon Seamen's Union*, 993 F.2d 357 (3d Cir. 1993).

110. *Id.* at 359. A helmsman is responsible for steering ships, and in this case, ships carrying gas.

111. *Id.* at 362; 33 C.F.R. § 95.020(b) ("An individual is under the influence of alcohol or a dangerous drug when: The individual is operating a vessel other than a recreational vessel and has an alcohol concentration of .04 percent by weight or more in their blood.")

112. *Id.* at 367.

113. *Bangor Gas Co., LLC v. H.Q. Energy Serv. U.S. Inc.*, 695 F.3d 181, 190 (1st Cir. 2012).

114. Jonathan A. Marcantel, *supra* note 105, at 623 (2009) ("While none of the courts discussing *Hall Street Associates* have specifically ruled on whether the public policy exception has survived the opinion, application of basic statutory construction principles indicates the public policy exception has not survived post-*Hall*.")

115. *Bull HN Info. Sys., Inc. v. Hutson*, 229 F.3d 321, 330-31 (1st Cir. 2000).

disregard” is not even a valid option. There are also problems in circuits where manifest disregard is thought to have survived.

“Manifest disregard” is a strict standard, requiring that a party seeking vacatur on this ground shoulder a heavy burden of proof.¹¹⁶ For vacatur to be appropriate, the arbitrator must recognize the applicable law and then ignored it.¹¹⁷ In fact, courts have held that an arbitrator simply misunderstanding the law, and therefore misapplying it, does not amount to “manifest disregard” of the law.¹¹⁸ This strict standard for “manifest disregard” may be problematic for parties seeking vacatur. In *Bangor*, for example, the court explained that the arbitration panel considered the FERC “shipper must have title” rule, and believed that the award that it fashioned complied with the regulation.¹¹⁹ In situations where the arbitrator simply misunderstands the impact of its award on a regulation, and thus causes violation of a regulation, it seems to follow that “manifest disregard” would not be found. Misunderstanding of the law, or a regulation, simply does not rise to the level of “manifest disregard.”

The arbitration panel in *Bangor* had the benefit of a no-action letter from FERC to help it fashion an award that complied with the relevant FERC regulation.¹²⁰ Arbitrators with such guidance are in a good position, as they have additional insight on the relevant regulation. Agency guidance, however, does not bind an agency. As the *Bangor* court explained, the FERC may well act differently than indicated in its no-action letter.¹²¹ Thus, fashioning an award to comply with agency advice could be an exercise in futility. If an arbitrator relies on agency advice in making its decision, and the agency later acts contrary to the advice given in a no-action letter, the arbitrator will have acted reasonably, but still put the parties bound by the award in a difficult position. If the award violates a regulation, as discussed above, it may be difficult for the parties to have the award vacated.

Many arbitrators have specialized knowledge and possess expertise specific fields, such as labor, copyright, or business disputes.¹²² If a specialized arbitrator relies on agency guidance that she believes, due to her expertise in a given field, misinterprets the regulation at issue, the arbitrator is faced with a difficult decision. She must choose to either rely on the agency’s informal, non-binding advice addressing the specific dispute at issue in structuring an award, or ignore this advice and fashion an award that she believes is actually in compliance with the relevant regulation. Either way, the arbitrator is put in a difficult position in reconciling the award with the regulation at issue.

116. *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056, 1060 (9th Cir. 1991).

117. *AT&T Mobility LLC v. Concepcion*, 131 S. Ct. 1740, 1745-46 (2011).

118. *Todd Shipyards Corp.*, 943 F.2d at 1060.

119. *Bangor*, 695 F.3d at 188.

120. *Id.*

121. *Id.*

122. L. Vincent Poupard, *First Person: The Two Types of Business Arbitrators*, Yahoo! Finance (May 21, 2012), available at <http://finance.yahoo.com/news/first-person-two-types-business-arbitrators-173700696--finance.html>.

CONCLUSION

Bangor illustrates the potential problems facing arbitrators and parties when arbitration awards must be fashioned to comply with a complex regulatory scheme. Parties may be forced to violate regulations in order to comply with an arbitration award by which they have contractually agreed to be bound. The uncertainty surrounding the viability of the “public policy” and “manifest disregard” grounds for vacatur, neither of which is expressly endorsed by Section Ten of the FAA, creates an initial obstacle for parties seeking to vacate such an award. Further, even if both grounds are viable in a given circuit, both require parties seeking vacatur to surmount a very high standard of proof. *Bangor* is illustrative of this situation, as the regulation at issue was economic in nature, and the arbitration panel fashioned its award with regulation compliance in mind. Finally, arbitrators may also be in a difficult position of having to predict how an agency may act in the future, given the non-binding nature of most agency “letter rulings” and “no action” letters.

GREG MITCHELL

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