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New York Dispute Resolution Lawyer

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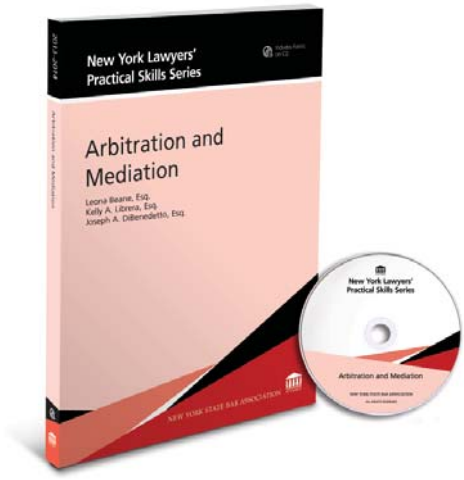
Arbitration and Mediation



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Contents at a glance

This practice guide examines the two most common forms of alternative dispute resolution–Arbitration and Mediation. *Arbitration and Mediation* resolves the misconception that these two procedures are interchangeable by discussing their differences and providing examples of when each procedure should be used.

Complete with valuable practice pointers, sample arbitration forms and appendices, this practice guide also includes **Forms on CD.**

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Message from the Chair

Abigail Pessen

The mood of the country is unsettled these days. But while we are uncertain about where the nation is headed, the presidential election has provided likely answers to some important questions in the dispute resolution field. For example, the next Justice of the U.S. Supreme Court—not yet confirmed at press time—is expected to restore the high court's conservative majority. This portends a pro-arbitration ruling on whether bans on collective employment arbitration violate workers' rights to concerted action protected under the National Labor Relations Act; certiorari has been granted to resolve the circuit split on the issue. Likewise, the Obama administration's attempts via regulatory action to bar mandatory arbitration of financial services and nursing home disputes may very well be scuttled when the current heads of the Consumer Financial Protection Bureau and the Health and Human Services Department are replaced.

As a counterpoint to developments that likely favor mandatory arbitration clauses, public sentiment against "mandatory" or "forced" arbitration appears to be growing in the wake of a *New York Times* series of articles and editorials, Fox News anchor Gretchen Carlson's obligation to arbitrate her sexual harassment claim (now settled), and Wells Fargo customers being compelled to arbitrate their claims of fraudulent accounts.

Mandatory arbitration may indeed be a "mixed bag" for employees like Ms. Carlson, who are required as a condition of their employment to individually arbitrate all claims, including statutory discrimination claims, against their employers. In addition to forgoing a jury trial, participation in a class or collective action, and the right to appeal (since review of arbitration awards is very limited), employees cite the difficulty of discovering the existence and outcomes of similar discrimination claims against their employer, who invoke the confidentiality provisions in their arbitration agreements. Offsetting these drawbacks is the privacy afforded by arbitration, which is often a real—and overlooked—benefit to employees, protecting them from the prying eyes of Internet trolls scanning court filings for future employers eager to avoid hiring "troublemakers." The disallowance of employers' summary judgment motions in most arbitrations is another significant advantage. It is intriguing to wonder whether, if mandatory pre-dispute arbitration clauses were no longer enforceable in the employment context, employee-side counsel might opt for arbitration in some, or even many, cases, finding it a preferable alternative to court litigation.

In the meantime, one unexpected and noteworthy consequence of collective arbitration bans has been the initiation of numerous individual arbitrations by large employee-side law firms, creating employer exposure to multiple attorneys' fee awards and the risk of inconsistent outcomes. This has in turn led in some cases to agreements to engage in collective mediations seeking global resolution of all the individual cases.

Mediation is also on the rise as parties seek to control expense and state and federal trial and appellate courts seek to reduce their dockets by expanding court-annexed mediation programs.

A snapshot of dispute resolution in 2017 thus would show mediation gaining in popularity, while mandatory arbitration continues to fend off challenges which—even if unsuccessful in a conservative, pro-business environment—may sully the reputation of commercial arbitration in general, even when freely agreed to by parties eager for the choice of decision-maker, speed, cost savings, finality, and privacy it offers.

The snapshot would reveal another disquieting fact: despite research concluding that diversity among neutrals leads to better outcomes for the parties, opportunities for minority and female arbitrators and mediators still lag in comparison to their white, male counterparts. Some commentators explain this as a "pipeline" problem, i.e., a lack of minority and female attorneys possessing the needed experience and qualifications to be successful neutrals. However, the much larger numbers of women and minorities in the judiciary cast doubt on this explanation. Others note that end-users or their counsel are reluctant to risk selecting an untried mediator, or, even more so, an unknown arbitrator.

How can this cycle be broken? One suggestion is that ADR providers require that a certain percentage of minority or female neutrals be included in every list of mediators and arbitrators provided to their users. While

laudable, such a policy—already adopted by the American Arbitration Association—does not guarantee the selection of a minority or female neutral by the users. Another approach providers might consider would be to encourage party-appointed arbitrators to select a minority or female arbitrator as their chairperson.

Other suggested remedies call for companies to select neutrals as they select other vendors, requiring a certain percentage to be diverse or at least requiring year-to-year improvement. The New York State Bar Association is considering a recommendation that diversity-related content be made a mandatory part of CLE requirements. Our Section now insists on diverse presenters for all of its panels and programs. We've also started a diversity scholarship program, offering free mediation or arbitration training, Section membership, and mentoring to ten minority or female attorneys every year (see details at nysba.org/drs).

At a recent forum on this topic, dispute resolution processes were celebrated as the "thread" that sews together the gloriously diverse patchwork quilt of our country. If this thread itself can become multi-colored (and multi-gendered), the quality of ADR will be improved immeasurably for parties, advocates and neutrals alike. And that's a good thing.

Abigail Pessen

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Message from the Co-Editors-in-Chief

If you are reading this *Journal* you are part of a growth industry. This issue deals with an astounding breadth of worldwide developments. This scope makes clear that "alternative dispute resolution" is no longer of lesser status than litigation; it has gained worldwide acceptance, providing practical solutions both to routine and to bet your business disputes around the world.

Edna Sussman

Sherman Kahn

Laura A. Kaster

This issue demonstrates, among other things, that (1) cities and countries around the world are competing to attract international arbitration business and to routinize the administration of these matters; (2) champerty and maintenance restrictions have not impaired or slowed the development of third-party funding, a practice which has come into its own, requiring rules in Hong Kong and new concerns to evaluate in our Ethical Compass column; (3) there is a recognized need to establish a stronger regime under the Hague Convention for the enforcement of forum selection clauses and court judgments around the world to complement the dominance of the New York Convention in fostering the growth of arbitration; (4) and despite worldwide parallel development of ADR techniques, cultural differences still have an impact.

The upshot is that all lawyers must understand the worldwide ADR terrain in order to provide transactional and dispute-related advice that anticipates and minimizes the cost of business disputes and manages them when they arise.

We are proud to be the publication of our very dynamic section that is fostering New York as a critical center for these developments.

Laura A. Kaster, Edna Sussman and Sherman Kahn

We note with sorrow the death of renowned mediator Margaret Shaw, who contributed so much to our profession.
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When the Empty ADR Chair is Occupied by a Litigation Funder

By Professor Elayne E. Greenberg

Introduction

Elayne E. Greenberg

The discussion about the $140 million jury verdict against Gawker media for posting a sex video of Terry Bollea, professionally known as Hulk Hogan, having sex with his best friend's wife, quickly shifted to a conversation about the ethics of litigation funding when it was finally disclosed that Peter Thiel had funded Bollea's litigation.[1] The backstory reveals that Gawker outed Thiel, revealing his homosexuality ten years earlier in a more conservative time when such a revelation might have impacted Thiel's earning capacity. Thiel, an icon in Silicone Valley and a co-founder of PayPal, promised revenge. Thiel got his revenge, and Gawker is now bankrupt.

Alternative litigation finance ("ALF"), known by some as litigation funding and pejoratively referred to by others as "pay to play," is the term used to describe

> the funding of litigation activities by entities other than the parties themselves, their counsel or other entities with a preexisting contractual relationship with one of the parties. These transactions are generally between a party to litigation and a funding entity and involve an assignment of an interest in the proceeds from a cause of action.[2]

To date, the discussion about the ethics of litigation funding has centered on ethics in the litigation context. This column will begin to broach the previously untouched ethical issues that litigation funding in arbitration and mediation raise for dispute resolution professionals. As background, this column will review the ethical concerns raised about litigation funding in the adjudication context. Then, the discussion will shift to the mediation and arbitration contexts and preview the ethical concerns and strategies mediators and arbitrators should consider if a litigation funder is occupying the empty chair in your ADR process.

Ethical Concerns About Litigation Funding in the Litigation Context

In the litigation context, it seems that most have an opinion about the ethics of litigation funding. Some accept litigation funding as a natural evolution of our capitalistic society.[3] Others remind us that litigation funding is just another litigation funding source like insurance. Viewed from the opposite perspective, others view litigation funding as a sign of the ethical corruption of our justice system that must be stopped. Still others are unsure which side of the discussion they are on, but they know that the sinking feeling in the pit of their stomach probably signals ethical caution.

If we expand our inquiry from personal opinions to ethical directives and proposed court rules about litigation funding, we learn that litigation funding is ethical provided that certain caveats are observed. For example, the New York State Bar Association Committee on Professional Ethics has issued two ethics opinions that support the use of litigation funding with some cautionary warnings. First, in a 1994 opinion, the Committee affirmed a lawyer's right to refer a client to a litigation funder to cover the cost of the client's living expenses during the client's claim for personal injuries when such repayment of the funding was contingent on the client prevailing on his claim.[4] The opinion clarified that the mere referral was not per se unethical so long as the attorney did not compromise the attorney-client confidentiality; the lawyer had the client's informed consent for any disclosures that had to be made; and the lawyer did not receive any compensation, ownership interest or referral fee from the funding corporation. The Committee reminded that the old English prohibitions against "maintenance," "champerty" as a form of maintenance, and "barratry" are still proscribed in New York.[5]

"Supporters and naysayers of the proposed rule modifications have seized upon this to continue debating the ethics of litigation funding."

Then, in 2003 the NYSBA Committee on Professional Ethics weighed in once more on the ethics of litigation funding when it opined that a lawyer representing a client on a personal injury matter may also represent that client and charge the client an additional fee in arranging litigation funding for the client with a funding institution.[6] However, the lawyer must be vigilant that such representation does not compromise the lawyer's independent judgment about the client's case. The Committee restated all the caveats it had issued in its earlier opinion.

The Committee also emphasized that the lawyer needs to explain and stress that such representation does not mean that the lawyer endorses the transaction. Moreover, the Committee recommended that the lawyer prepare a revised representation agreement to reflect the attorney's expanded scope of responsibility. Although the Committee would not comment on the legality of litigation funding, it did say that if litigation funding were found to be illegal, it would be a violation of the lawyer's ethical code to assist a client in a fraud. Rather than add clarity to the issue of litigation funding, the Committee's opinion could be interpreted as a statement that reflects the ethical ambivalence about litigation funding.

Echoing the concerns voiced in the NYSBA Ethics Opinions, The American Bar Association Commission on Ethics 20/20 Information Report to the House of Delegates expanded the discussion.[7] The Commission recognized that because there are so many variations of litigation funding agreements, it is challenging to identify the all possible ethical pitfalls for lawyers.[8] The Commission also reiterated that the client, as a matter of agency law, has a right to delegate revocable settlement authority to other agents such as a litigation funder.[9] Given those realities, the Commission cautioned the lawyer about any agreement with a litigation funder that would create any disincentive to the lawyer's exercise of his or her independent judgment in managing the case.[10]

Thus, in the litigation context, three caveats emerge from the ethical directives cited above. First, nothing in the litigation funding agreement may interfere with or disincentive the attorney from meeting his or her ethical obligation to exercise independent judgment.[11] Second, before the attorney shares any privileged information about the case with the litigation funding company, the client must make an informed waiver of attorney-client privilege.[12] Therefore, information that was once regarded as confidential because of the attorney-client privilege may lose its confidentiality cloak if it is shared with a litigation funder. Third, any fee-splitting arrangement between the attorney and the litigation funder may create ethical conundrums for the attorney. By way of illustration, does the fee-splitting arrangement adversely impact the attorney's independent judgment? Moreover, if the funder is a non-attorney, might it create a situation where the attorney is practicing law with a non-attorney?[13]

Stoking the controversy about litigation funding, the respective Rules Committees of the Federal Rules of Civil Procedure and the Rules of the Northern District of California have proposed modifications that would require attorneys to disclose the identity of any litigation funder backing their case.[14] Supporters and naysayers of the proposed rule modifications have seized upon this to continue debating the ethics of litigation funding.[15]

The Ethics of Litigation Funding in Dispute Resolution

Turning our conversation to the ethics of litigation funding in dispute resolution, we expect that the ethical requirements that lawyers are required to observe regarding litigation funding in the litigation context are the same ethical requirements that lawyers must continue to observe when they participate in dispute resolution. In addition, this columnist advises that lawyers participating in dispute resolution should ethically be required to disclose the identity of litigation funders at the time that lawyers and their clients consent to participate in dispute resolution. Disclosure is an important part of transparency, a fundamental ethical tenet of dispute resolution practice. Therefore, arbitrators and mediators must know the identity of litigation funders at the beginning of these procedures if these neutrals are to conduct these dispute resolution procedures in accordance with their ethical mandates and maintain the integrity of the arbitration and mediation procedures. Disclosure is needed for five reasons.

"This is a never before broached discussion about the ethical implications of having a litigation funder support a party in arbitration or mediation."

First, disclosure is needed to identify any pre-existing conflicts between the ADR neutral and the funding organization. The integrity of mediation and arbitration is based, in part, on the neutrals disclosing any existing conflicts. The parties then have the right to decide if they want to proceed with the neutral given the conflict, or if they prefer, to employ another neutral. However, if the identifies of the litigation funders are not disclosed at the beginning, neutrals and parties may be unaware of potential pre-existing conflicts with the litigation funder.

Second, disclosure is needed for the neutral to fully understand all the interests that need to be addressed before a settlement is reached. A party's interests may be influenced, in part, by the economic support they receive from a litigation funder. This financial support may fuel the party's feeling of optimistic overconfidence and, at times, dispute the party's own interests. For example, if a party in arbitration has the economic support of a litigation funder, the party may be more likely to demand a drawn-out discovery process. In a mediation example, a party may be less receptive to considering a reasonable settlement if the party overconfidently believes they have enough economic support to secure the desired judgment that awards them all they believe they are entitled to. In another example, the litigation funder, as in the Hulk Hogan example mentioned at the beginning of the article, may have his own interests that need to be addressed before a settlement may be reached.

Third, disclosure is needed to uncover all the invisible pulls that may be dictating settlement terms. The specific economic arrangement between a party and a litigation funder may be such that a party might be less likely to consider a reasonable settlement offer if the party has to repay out of the settlement amount both the litigation funder the borrowed money with interest and also pay their lawyer for services rendered. The net balance might leave little for the party and create a disincentive to settle for anything less than the pot of gold.

Fourth, disclosure is needed to ensure that all participants, including the litigation funder, sign and abide by the agreed-upon confidentiality protections. Depending on the terms between the litigation funder and the party, the party may be required to share other confidential information about the mediation or arbitration. If the litigation funder does not sign a confidentiality agreement regarding the arbitration or mediation, then the litigation funder is not bound to keep that information confidential. This loophole in confidentiality potentially violates the confidentiality expectations of the parties, their lawyers, the neutrals and the ADR provider.

Fifth, disclosure is needed to ensure that the parties' procedural justice expectations are satisfied. The legitimacy of any dispute resolution procedure is based, in part, on whether the party perceives the process as fair, independent of whether or not the ultimate decision was in their favor. However, imagine how a party might feel if after a mediation or arbitration, it was disclosed that a litigation funder supported the other party. Thus, to maintain the procedural justice expectations of participants in arbitration and mediation, a party must disclose the identity of their litigation funders.

Conclusion

This is a never before broached discussion about the ethical implications of having a litigation funder support a party in arbitration or mediation. Even though litigation funding has been around for some time and is gaining popularity, little is known about how litigation funding ethically influences settlement. When a litigation funder occupies the empty chair in an arbitration or mediation, the identity of the litigation funder must be disclosed at the onset of the dispute resolution procedure. This should be a question on the forms of all providers. Disclosure is just the beginning.

However, disclosure is not the end of the ethics dilemma. Litigation funding agreements are not cookie cutter. Rather, they have varied economic terms and requirements that may implicate different ethical concerns when a dispute resolution participant is receiving the support of a litigation funder. As dispute resolution professionals, we need to examine this topic more thoroughly to preserve the integrity of our work. I welcome your thoughts and ideas about this increasingly pressing topic.

Endnotes

1. *See, e.g. Andrew R. Sorkin, Peter Thiel, Tech Billionaire, Reveals Secret War With Gawker,* N.Y. Times (Oct. 7, 2016), http://www.nytimes.com/2016/05/26/business/dealbook/peter-thiel-tech-billionaire-reveals-secret-war-with-gawker.html?_r=1; Mathew Ingram, The Gawker vs. Hulk Hogan Case Just Got a Lot More Important, Fortune, (May 25, 2016, 2:19 PM), http://fortune.com/2016/05/25/gawker-hogan-thiel/.

   > Gawker and Bollea then negotiated a settlement that reduced the amount of the jury verdict to $31 million. http://www.forbes.com/forbes/welcome/?toURL=http://www.forbes.com/sites/mattdrange/2016/11/02/gawker-media-close-to-reaching-settlement-with-hulk-hogan/&refURL=https://www.google.com/&referrer=https://www.google.com (November 14, 2016).

2. ABA Comm. on Ethics 20/20, Informational Report to the House of Delegates, at 1 (2014) [http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212_ethics_20_20_alf_white_paper_final_hod_informational_report.authcheckdam.pdfhttp://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212 (studied the impact of litigation funding on the lawyer/client relationship).

3. Alan L. Zimmerman, Fiona M. McKenna, Daniel J. Bush, & Cheryl Kaufman, *Economics and the Evolution of Non-Party Litigation Funding in America: How Court Decisions, the Civil Justice Process, and Law Firm Structures Drive the Increasing Need and Demand for Capital*, 12 N.Y.U.J.L. & Bus. 635, 636 (2016).

4. N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 666 (1994).

5. *Supra* note 3 at 9."Maintenance, champerty and barratry are closely related but are not identical. '[P]ut simply, maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty.'"

6. N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Opt. 769 (2003).

7. *See* Report to the House of Delegates, *supra* note 3, at 3.

8. *Id.*

9. *Id.* at *27.*

10. *Id.* at *28*.

11. *See, e.g.*, at Geoffrey McGovern et al., RAND Inst. for Civil Justice, Third-Party Litigation Funding and Claim Transfer: Trend and Implication for the Civil Justice System 19 (2010), http://www.rand.org/content/dam/rand/pubs/conf_proceedings/2010/RAND_CF272.pdf.

12. *See, e.g., McGovern, supra* note 11 at 17.

13. *Id.*

14. *See* http://www.therecorder.com/id=1202771211351/Move-to-Expose-ThirdParty-Case-Funding-Stirs-Debate-in-Northern-District?slreturn=20161014214119 (November 14, 2016).

15. *Id.*

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Mediating the "Loose Ends" After Arbitration

By Gerald W. Ghikas, Q.C.

The Temptation to Tie Up Loose Ends

Even the best arbitrators sometimes are tempted to go beyond deciding the dispute before them and to anticipate and head off future disputes. Perhaps the evidence establishes serial breaches of contract, including breaches post-dating the commencement of the arbitration, for which no specific claim is made. Or maybe it seems plain that the parties need "a divorce" but neither has taken any steps to formalize an end to the legal relationship.

"The arbitral tribunal should not yield to the temptation to tie up loose ends."

These unresolved issues, which seem destined to result in further arbitration proceedings, may be thought of as arbitrable "loose ends." A member of an arbitral tribunal may urge her colleagues—*"The parties are looking to us to help them resolve their differences so that they can get on with their lives. They have spent thousands of dollars educating us about the history of their relationship. The last thing they want is to have to start all over again with another arbitration. Don't we have a responsibility to find a way to help them move on?"*

The temptation in such cases may be to fashion relief that was not claimed—for example, by making broadly phrased declarations designed to head off future disputes—or simply to include gratuitous comments in the award about what the tribunal thinks should happen in the future—a sort of "road map" for the parties to follow to tie up their loose ends.

"One possible approach to resolving loose ends without having to commence another arbitration, while allowing the arbitral tribunal to play a role, is a post-arbitration mediation."

The Importance of Resisting Temptation

The arbitral tribunal should not yield to the temptation to tie up loose ends. There is a strong possibility the tribunal lacks jurisdiction to do what the arbitrators, or some of them, think is "the right thing to do." It is also, at the very least, presumptuous, and, at worst, arrogant, for a tribunal to assume that it is better placed than the parties themselves to know what matters need to be decided by the award and what matters should be left for later resolution. The parties have not necessarily shared with the arbitral tribunal all of the facts and considerations that have a bearing on the resolution of those other matters. One or both of the parties may have made well-considered tactical decisions to leave the loose ends unresolved.

One possible solution is for the arbitral tribunal to ask the parties whether they wish it to decide specific matters that are not within the tribunal's existing mandate. In the rare circumstances where such a request may be appropriate, likely at least one of the parties will say *"no, thank you."* They will be reluctant to expand the arbitrators' mandate before having in hand the award with respect to the matters already submitted to arbitration.

Post-Arbitration Mediation of Loose Ends

One possible approach to resolving loose ends without having to commence another arbitration, while allowing the arbitral tribunal to play a role, is a post-arbitration mediation. After a final award in the arbitration is delivered to the parties, with the consent of both parties the arbitrators, or some of them—perhaps a tribunal chair—may act as mediator of the residual disputes. This "arb/med" process is most appropriate in cases where the parties are looking for guidance as to the possible merits of their respective positions in relation to the matters left unresolved by the arbitration award. It is a logical means of obtaining an informed, early, neutral evaluation of the relative merits of the parties' legal positions. The arbitrator serving as mediator will have heard evidence of the history of the parties' relationship and will have a sense of the personalities and the credibility of the witnesses who would be called upon to support a further adjudicated resolution. The understanding of the history of the parties' relationship that an arbitrator gleans over many months of written briefing and an evidentiary hearing simply cannot be replicated by a mediator who has no prior involvement and who is engaged for the purposes of a one- or two-day mediation.

There may be instances where even for the purposes of an "interest-based" mediation, the stature that the mediator has gained in the eyes of the parties through his or her participation as arbitrator can be of significant benefit. The parties may have a higher level of confidence in, and greater respect for, the arbitrator as an interest-based mediator than they would for a mediator who is unknown to them. This is most likely to be the case when the award reflected a genuine understanding and a fair consideration of the parties' respective positions. The respect for the former arbitrator may enhance his or her ability to assist the parties to agree to a resolution.

Recommended Precautions and Ground Rules

As is the case whenever adjudicative and non-adjudicative roles are mixed, precautions are required.

Prudence dictates that the parties should confirm that there is not and will not be any challenge to the award. This is particularly important if there is any possibility that a successful challenge could result in matters being referred back to the arbitral tribunal for decision. The arbitrator's service as mediator likely would preclude re-assuming the role of arbitrator. One might also question the objectivity of the arbitrator as mediator if one party has launched an attack upon the arbitrator's award.

"An arbitrator who is asked to assume the role of mediator must have a clear sense of the permissible boundaries of discussion about the meaning of, or reasons for, findings made in the earlier award."

Also, if only one member of a tribunal is to don the mediator's hat, it is wise to ensure that the other arbitrators consent to his or her doing so. If for any reason one arbitrator has concerns about the propriety of a colleague assuming the mediator role, that concern should be respected. The parties may regard their former arbitrator as the objective custodian of the arbitral tribunal's collective wisdom. If one member of the tribunal has reservations, those reservations should be respected.

An arbitrator who is asked to assume the role of mediator must have a clear sense of the permissible boundaries of discussion about the meaning of, or reasons for, findings made in the earlier award. There is a real risk of tension arising between what the mediation parties would like to hear and what the former arbitrator is prepared to say about the arbitration and the award. The parties may have different views about the award's implications. They may expect the arbitrator to elaborate on the tribunal's reasoning. If so, they will likely be disappointed. The former arbitrator is constrained by obligations of confidentiality owed to his or her co-arbitrators, and by simple prudence, from going beyond what was stated in the award. That should be made clear to the parties before any agreement to serve as mediator is accepted.

An Example of Post-Arbitration Mediation

The writer recently served as chair of an international arbitration tribunal, hearing claims by an American distributor against a Spanish manufacturer that the manufacturer had secretly been breaching the distributor's exclusive rights for several decades, by selling directly into the distributor's exclusive territory. The manufacturer alleged that the distributor had known of and acquiesced in the relevant sales and that the distributor was therefore precluded, based on various legal and equitable theories, from now claiming damages. The arbitral tribunal found that there had been breaches of the exclusive license, and that each time a sale was made into the exclusive territory there was a separate breach of contract. It found that there was no preclusion through waiver, estoppel or otherwise because the manufacturer had not proven that the distributor knew of the manufacturer's activities. Some of the claims were barred by the applicable statute of limitations, on the basis that under the applicable law the limitation period commenced and ran even if the claimant had no knowledge of the breach. Damages were calculated and awarded with respect to those sales which were not statute barred. The evidence presented at the hearing showed sales occurring up to and including the date of commencement of the arbitration. The evidence showed that there had been a complete breakdown of trust and confidence between the manufacturer and the distributor. The exclusive distribution agreement contained termination provisions, but neither party had purported to exercise them.

Although there was evidence that the same pattern of conduct had continued, because there were no claims made based on sales after the date of commencement of arbitration, no determination of breach or award of damages was made in respect of those sales. Because neither party had invoked the termination provisions of the distributorship agreement, the award was silent on the issue of termination. The arbitral tribunal offered no comments concerning logical next steps. The parties were left as they were, although further disputes were inevitable. The arbitral tribunal resisted the temptation to tie up loose ends.

After the award was issued, and after all parties had determined that they would not seek any recourse from the award, the parties asked the chair of the tribunal to mediate their disputes about whether (a) the distributor had claims for damages for breach of contract in respect of sales occurring after the date of commencement of the arbitration, and (b) if, so, what damages were recoverable and (c) whether the distributorship agreement should be terminated and, if so, on what terms. After conferring with his co-arbitrators, the chair agreed to act as mediator. The remaining matters in dispute were successfully resolved by agreement of the parties during a one-day mediation. The parties are convinced that they could not have reached a settlement without the former chair's involvement as mediator.

Conclusion

In appropriate cases and with appropriate precautions, a post-arbitration mediation can effectively resolve disputes that could not properly be determined by the arbitration award. It balances respect for the autonomy of the parties, to select which differences are and which differences are not to be finally resolved on their merits through arbitration, against the benefit of participation by an informed and respected neutral in resolving any "loose ends."

Gerald W. Ghikas Q.C. Gerald Ghikas is an independent arbitrator, and occasionally a reluctant mediator, of international and domestic commercial disputes. He practices from Vancouver Arbitration Chambers, in Vancouver, British Columbia, Canada. You can reach him at gghikas@ghikasarbitration.com.

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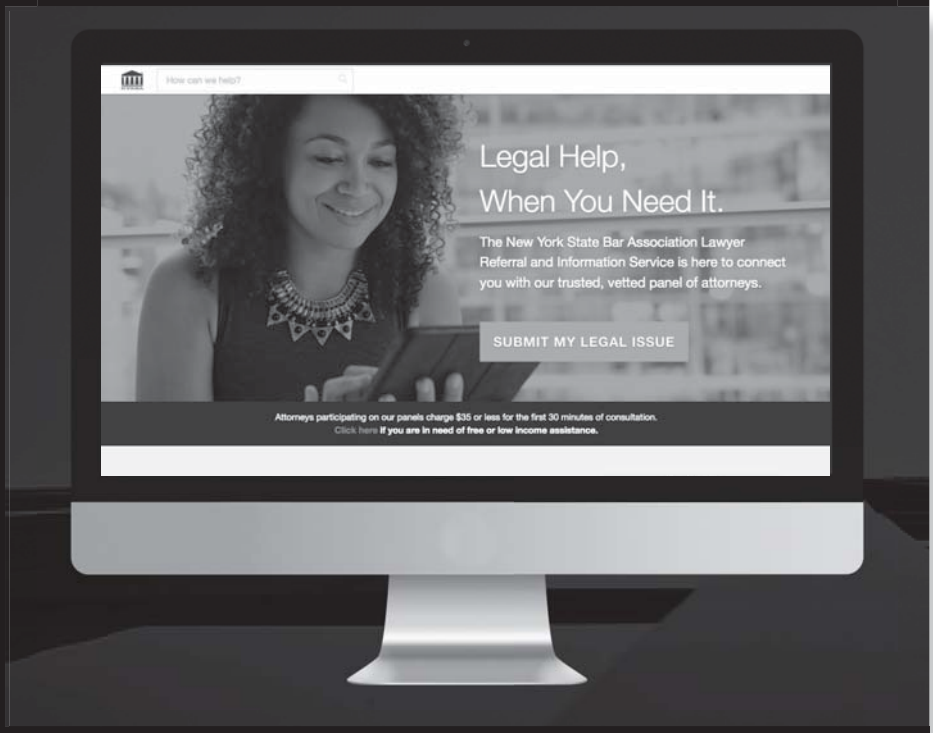

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Second Circuit Reaffirms Manifest Disregard as a Valid Ground for Vacature of Arbitration Award

By Edward Lozowicki

Earlier last year, the Second Circuit elaborated on and reaffirmed its position that manifest disregard of law *or* of the arbitration agreement is a valid ground for vacature of arbitration awards.[1] This decision highlights the current split among the Federal Circuit Courts of Appeal as to whether manifest disregard is a separate ground for vacature under section 10(a) of the Federal Arbitration Act ("FAA").[2]

"…the primary inquiry…is whether the arbitrator's award draws its essence from the agreement…"

In 2008, the U.S. Supreme Court held that § 10(a) provides the "exclusive grounds" for vacature of arbitration awards and cannot be expanded by agreement of the parties.[3] Since then, the Circuit Courts have split on whether manifest disregard survives as a separate ground for vacature. The Fifth, Eighth and Eleventh Circuits have held that manifest disregard of law is no longer a valid ground, while the Second, Fourth and Ninth Circuits have held that manifest disregard is valid either as a "judicial gloss" or "shorthand" for the express grounds in FAA §§ 10(a)(3) and (4). The Third Circuit has not yet weighed in on this issue.

In *Sutherland*, the Second Circuit characterized *Hall Street* as holding that the specific grounds for vacature in section 10 of the FAA are "generally exclusive," but the Circuit Court made an exception: "we have nevertheless held that as 'judicial gloss on the specific grounds for vacature of arbitration awards' in the FAA, an arbitrator's 'manifest disregard' of the law or of the terms of the arbitration agreement remains a valid ground for vacating arbitration awards."[4] Manifest disregard of the arbitration agreement as a ground for vacature appears consistent with FAA § 10(a)(4) which allows vacature if the arbitrator exceeds his or her powers. Such powers may be circumscribed by the parties' arbitration agreement or by law.

In *Sutherland*, appellant argued that the arbitration panel had exceeded its authority and manifestly disregarded the terms of the underlying contract and New York law because one of the material contract documents had not been executed by the parties; and because the panel based the award on work performed by appellant's affiliate contrary to the terms of the contract. The *Sutherland* court was not receptive to these arguments. It stated that the primary inquiry under § 10(a)(4) is whether the arbitrator's award draws its essence from the agreement and provides even a "barely colorable" justification for his or her interpretation of the contract. Applying those standards, it held that the arbitrators had in fact interpreted the relevant provisions in the underlying contract so as to rebut appellant's contentions, and that the court would not scrutinize the panel's contract interpretation or its factual findings.

Appellant also argued that the arbitrators committed legal error in their interpretation of the contract by ignoring a limitation of liability provision. The Circuit Court disagreed, stating that manifest disregard of the *law* applies only in those exceedingly rare instances where some egregious impropriety on the part of the arbitrator is apparent. The court further elaborated: "It is not enough…to show that the panel committed an error—or even a serious error…It is only when [an] arbitrator strays from the interpretation and application of the agreement and effectively 'dispenses his own brand of industrial justice' that his decision may be unenforceable."[5] Since the court found no manifest disregard of either the law or the arbitration agreement, it affirmed the district court's judgment confirming the award.

"…it must be clear from the record that the arbitrator…recognized the applicable law and then ignored it."

A similar conclusion was reached by the Fourth Circuit a few years ago when it rejected a manifest disregard argument.[6] In *Wachovia*, the appellant argued that the arbitrators had manifestly disregarded a state statute by refusing to grant the losing party's request for a separate evidentiary hearing on the victor's claim for attorney's fees. The appellant argued that the arbitrators' ruling violated Section 10(a) (3) which provides for vacature "where the arbitrators were guilty of…misbehavior by which the rights of any party have been prejudiced." In rejecting this argument, the court applied a two-part test that asked: (1) whether the applicable legal principle is clearly defined and not subject to reasonable debate; and (2) whether the arbitrator refused to heed that principle. The court ruled that the arbitrator's failure to follow a state procedural law was not manifest disregard of the

law because the state law was not clearly defined and was subject to debate. It further reasoned: "Whether manifest disregard is a 'judicial gloss' or an independent ground for vacature, it is not an invitation to review the merits of the underlying arbitration…."[7] It then affirmed the district court's denial of the appellant's motion to vacate.

Manifest Disregard Found in Two Cases

While *Sutherland* and *Wachovia* set a high bar for proving manifest disregard in vacature proceedings, one party cleared that bar in a post-*Hall Street* decision by the Ninth Circuit. In that case the court ordered partial vacature of an arbitration award because the arbitrator's interpretation of a valid covenant not to compete conflicted with a state antitrust statute and was in manifest disregard of the law.[8] In *Comedy Club* the licensee in a trademark licensing agreement partially breached certain terms of the agreement and was enjoined by an arbitration award from owning or operating any comedy club facilities anywhere in the United States for the remaining fourteen years' term of the agreement which remained in effect. The arbitrator had interpreted a state statute which prohibited such broad non-compete covenants as being not applicable. The enjoined party appealed a District Court order confirming the award, contending, *inter alia*, that the arbitrator acted in manifest disregard of the law. The Ninth Circuit, which had previously reversed the lower court, had the case on remand from the Supreme Court. The latter ordered reconsideration in light of its ruling in *Hall Street*. Nevertheless the Ninth Circuit held that manifest disregard is a part of FAA section 10(a)(4) and did not change its prior decision. In so doing the court fashioned a test: "… it must be clear from the record that the arbitrator…recognized the applicable law and then ignored it."[9] While acknowledging that the arbitration award was not "completely irrational" the court found that the arbitrator had ignored the relevant state statute and case law in manifest disregard of it and that the award must be partially vacated.[10] The facts in *Comedy Club* were egregious in that the award in effect prevented the licensee from opening new comedy club-type businesses anywhere in the United States for many years. The court described this effect as imposing a "quarantine" on the licensee from engaging in its business in 48 states and contrary to California law, which was controlling.[11] Thus, in the Ninth Circuit's view of FAA § 10 it appears that a court can vacate an award if the arbitrator knowingly interpreted controlling state law so as to ignore it.[12]

After *Comedy Club* was handed down, the Supreme Court decided *Stolt-Nielsen S.A. v. AnimalFeeds International Corp.*[13] In that case the Court stated that it abstained from rejecting manifest disregard as a ground for vacature.[14] However, the Court nevertheless said in *dicta* that the facts in that case did fulfill the assumed test for establishing manifest disregard, namely, that the arbitrator knew of a relevant legal principle and that it controlled the outcome of a disputed issue, but willfully flouted it by refusing to apply it.[15] *Stolt-Nielsen* was a dispute between a shipping company and its customer involving a "charter party" contract between them. The customer claimed *inter alia* that the shipping company engaged in price-fixing. Several customers had similar claims, all of which were subject to arbitration pursuant to a standard form contract with the company. One customer filed a demand for class arbitration pursuant to the rules of the American Arbitration Association which required an arbitrator to determine whether the arbitration agreement allowed the arbitration to proceed "on behalf of or against a class."[16] After conducting an evidentiary hearing the arbitrators decided a class arbitration would proceed and the shipping company then filed a motion to vacate the ruling before the case went forward on the merits. The Supreme Court reviewed the evidence, including expert opinions to the effect that the custom and usage of the chartering business did not support class arbitration. It also cited prior labor arbitration cases which held: "It is only when [an] arbitrator strays from interpretation and application of the agreement and effectively 'dispense[s] his own brand of industrial justice' that his decision may be unenforceable."[17] The Court faulted the arbitrators in its holding: "In sum, instead of identifying and applying a rule of decision derived from the FAA or either maritime or New York law, the arbitration panel imposed its own policy choice and thus exceeded its powers."[18] The Supreme Court regarded the arbitrators' lack of any support for their interpretation of the contract as proof that they had applied their own "policy choice" in deciding on class arbitration, contrary to Section 10(a) of the FAA. The Court's *dictum* regarding the test for manifest disregard makes it clear the Court concluded that the arbitrators had acted in manifest disregard of law. The Court also held that the award directing class arbitration was in excess of the arbitrators' powers because the parties' arbitration agreement was silent on class arbitration. It reversed the Circuit Court decision and directed that the class arbitration award be vacated. While the Court's holding is limited to the controversial issue of class arbitration, it appears that the Court does view manifest disregard as shorthand for the vacature grounds in FAA sec. 10(a)(4).

Whether the Supreme Court will address the circuit split on manifest disregard in a future case is uncertain. But, for the present, these recent cases provide guidance for arbitrators when they are drafting arbitration

awards. Since an award must draw its essence from the underlying agreement, the award should set forth the arbitrator's interpretation of the agreement as it applies to the material issues in the case. Further, the arbitrator should not make statements in the award which suggest that he or she is ignoring a controlling principle of law on a material issue, or determining an issue on policy grounds.

Endnotes

1. *Sutherland Global Services v. Adam Technologies*, 2016 WL 494155 (2d Cir. 2016).
2. 9 U.S.C. §§ 1-16.
3. *Hall St. Assocs. LLC v. Mattel, Inc.*, 552 U.S. 576 (2008).
4. *Id*.
5. *Id.*
6. *Wachovia Securities, LLC v. Brand*, 671 F.3rd 472 (2012).
7. *Id*. at 483.
8. *Comedy Club, Inc., v. Improvwest Associates*, 553 F.3d 1277 (9th Cir. 2009).
9. *Id*. at 1290.
10. *Id.* at 1293. On remand the trial court was ordered to narrow the injunction.
11. *Id.* at 1293 The court characterized the arbitrator's interpretation of the law as "fundamentally incorrect."
12. *Id.*
13. 559 U.S. 662 (2010).
14. *Id.* at 671, fn 3.
15. *Id*.
16. *Id*. at 668.
17. *Id*. at 671.
18. *Id*. at 676-77.

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Please note:
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Interim, Provisional and Conservatory Measures in U.S. Arbitration

By Steven Skulnik

A longer version of this Practice Note was first published by Practical Law Litigation web service at http://us.practicallaw.com/0-587-9225. For more information about Practical Law, visit us.practicallaw.com.

U.S. Legal Framework for Arbitration

Arbitration in the U.S. is governed by both federal and state law. The main source of U.S. arbitration law is the Federal Arbitration Act ("FAA"),[1] which applies in the state and federal courts of all U.S. jurisdictions. The FAA applies to all arbitrations arising from maritime transactions or to any other contract "involving commerce," which is defined broadly. This effectively means that the FAA applies to all international arbitrations and most domestic arbitrations seated in the U.S.

Seeking Interim Relief Before Courts and Arbitrators

Arbitration governed by institutional rules such as the American Arbitration Association ("AAA") Commercial Arbitration Rules (as amended on September 9, 2013, for arbitrations that commence on or after October 1, 2013) ("AAA Rules") and the International Centre for Dispute Resolution ("ICDR") International Arbitration Rules as amended and effective June 1, 2014 ("ICDR Rules") specify that the arbitrators have the power to grant interim, provisional and conservatory measures and specify procedures for obtaining relief even before the tribunal is constituted.[2]

Provisional relief is often necessary before arbitration when:

- A party has evidence that is relevant to the dispute but this evidence is likely to be destroyed, damaged or lost absent an interim order protecting it.
- A dispute is concerned with the ownership of perishable goods that may deteriorate before the dispute can be determined. An interim order requiring the sale of the goods (with the sale proceeds to be held pending the final award), or requiring the goods to be sampled, tested or photographed before the sale is often granted in this case.

Who May Provide Relief

Interim, provisional and conservatory relief in aid of arbitration may be provided by:

- The arbitral tribunal;
- An "emergency arbitrator" appointed by an administering body;
- A federal or state court.

The precise scope of the powers of each of these to act depends on:

- The arbitration agreement;
- Applicable arbitration rules;
- Applicable federal and state law.

Court-imposed Limits

Under the FAA, a court may grant interim relief pending arbitration.[3] The question of whether a federal court should grant preliminary injunction is generally one of federal law even in diversity actions, but state law issues are sometimes considered.[4]

Court-issued interim orders generally last only until the arbitrators have the opportunity to consider the request for emergency or injunctive relief.[5] In effect, restraints issued by courts often serve the same function as temporary restraining orders.

While some U.S. courts have held that they lack power to grant interim relief where the underlying dispute is subject to an arbitration agreement governed by the New York Convention[6] other courts have rejected this approach.[7] In *Sojitz Corp. v. Prithvi Info. Solutions Ltd.*, 921 N.Y.S.2d 14, 17 (1st Dep't 2011), for example, the court held that a creditor can attach assets, for security purposes, in anticipation of an award that will be rendered in an arbitration seated in a foreign country, even where there is no connection between the arbitral dispute and the state, as long as there is a debt owed by a person or entity in the state to the party against whom the arbitral award is sought.

Where admiralty jurisdiction is invoked, federal law governs attachments of ships and other assets.[8] In proceedings begun by libel and seizure of vessels or other properties in admiralty proceedings, Section 8 of the FAA provides the federal courts with jurisdiction to direct the parties to proceed with arbitration and to enter a decree on the award.

Procedure under State Law

Outside of admiralty, state law governs the availability of the provisional remedy of attachment in federal court.[9] Most state laws authorize provisional remedies in aid of arbitration.[10] Some state statutes that have adopted the UNCITRAL Model Law expressly allow for applications for interim measures of protection in aid of an arbitration.[11]

Whether to Apply to the Arbitral Tribunal or the Court

Parties generally can apply either to a court or to arbitrators for interim relief. Parties should consider applying to the court when:

- The arbitral tribunal has not yet been constituted and therefore cannot yet act. In these cases, unless the applicable arbitral rules contain emergency arbitrator provisions, an application to the court is necessary.
- The party seeking interim relief needs judicial compulsion. Although arbitrators can impose negative consequences on parties (for example, drawing adverse inferences if a party does not produce evidence), they have no ability to make a party carry out their orders and no power that can be applied to non-parties.
- The party needs *ex parte* relief. Under most institutional rules, a party seeking emergency measures of protection must notify the other parties.[12] Notice of the application gives the party an opportunity to dissipate the evidence or assets that are the subject of the application. By the time the tribunal makes an order, it can be too late. By contrast, federal courts and most state courts (*e.g.*, California and New York) permit an applicant to proceed without notice in urgent cases.
- The matter is urgent and the arbitrator does not act timely or does not provide an adequate remedy.[13]Absent a showing of urgency, under the RUAA parties may seek relief only from the arbitrator after the arbitrator is appointed and is authorized and able to act.
- The arbitrator may not have the power to grant the relief sought. For example, arbitrators may not have the authority to appoint a receiver.[14]

Parties should consider applying to the arbitral tribunal for interim relief when:

- The tribunal has been constituted and is available on short notice;
- The applicant is satisfied that the other party will respect orders issued by the tribunal;
- The federal or state courts at the place of arbitration are reluctant to grant provisional remedies in aid of arbitration;
- The parties' agreement or the applicable institutional rules empower the arbitral tribunal to grant broader interim relief than would be available in court.[15]

Interim Relief from the Arbitral Tribunal

Institutional Rules

Interim relief is available under, *inter alia*, the:

- AAA Rules;
- ICDR Rules;
- JAMS Arbitration Rules (effective July 1, 2014);
- The International Institute for Conflict Prevention & Resolution (CPR) Administered Arbitration Rules (effective July 1, 2013).

This section summarizes the interim relief available under the AAA and ICDR Rules. A review of the other institutions is included in the online version of this practice note at *http://us.practicallaw.com/0-587-9225.*

AAA Rules

Under the AAA Rules:

- The tribunal may take whatever interim measures it deems necessary, including injunctive relief and measures for the protection or conservation of property.
- Interim measures may take the form of an interim award and the tribunal may require security for the costs of the interim measures.[16]

AAA Rule 38 provides that where a party requires emergency relief before the tribunal has been formed, the AAA appoints an "emergency arbitrator." The emergency arbitrator has the power to order interim measures for the protection or conservation of property and may grant interim measures in the form of an award or an order, giving reasons in either case.[17] The authority of the emergency arbitrator ceases once the panel has been constituted.[18]

The rules also provide for parties to seek temporary relief in court, stating that:

> A request for interim measures addressed by a party to a judicial authority shall not be deemed incompatible with this rule, the agreement to arbitrate or a waiver of the right to arbitrate.[19]

ICDR Rules

Under the ICDR Rules:

- At the request of any party, the tribunal may take whatever interim measures it deems necessary, including injunctive relief and measures for the protection or conservation of property.
- Interim measures may take the form of an interim award and the tribunal may require security for the costs of the interim measures.[20]

Furthermore, the rules expressly permit the tribunal to apportion the costs of the application in any interim award or in the final award.[21] In many cases it is prefer-

able for costs to be dealt with globally at the end of the arbitration, rather than at the application itself.

The rules further provide that where a party requires emergency relief before the tribunal has been formed, the ICDR appoints an "emergency arbitrator."[22] The emergency arbitrator has the power to order interim measures for the protection or conservation of property and may grant interim measures in the form of an award or an order, giving reasons in either case.[23] The authority of the emergency arbitrator ceases once the tribunal has been constituted.[24]

The rules also provide for parties to seek temporary relief in court, stating that:

> A request for interim measures addressed by a party to a judicial authority shall not be deemed incompatible with the agreement to arbitrate or a waiver of the right to arbitrate.[25]

When to Apply

As a general principle, applications for interim and conservatory relief should be made as early as possible. This is because:

- Failure to apply early may prejudice the application for practical reasons. Evidence or assets may be disposed of or property may deteriorate.
- Delay in applying may be taken into account by the tribunal. If the matter is not urgent enough to cause a party to seek relief promptly, a tribunal may decide that the relief is not necessary.

How to Apply

The procedure for applying to the tribunal depends in the first instance on the arbitration agreement or any applicable rules. However, the following points are generally applicable to arbitration under any institution's rules:

- **Apply in writing.** In the absence of any particular procedural requirements, most applications to the tribunal for interim measures should be made in writing.
- **Submit evidence.** The applicant should provide evidence in support of its position. For example, if a party is seeking conservatory orders in relation to property, it should identify the property and its whereabouts, and provide evidence that establishes why the relief sought is necessary. If the applicant is seeking to enforce an employee non-compete agreement, provide affidavits establishing the employer's business interest in enforcing the non-compete and the potential harm to the employer if the tribunal does not issue an order preserving the *status quo*. The applicant should also brief the applicable law regarding its entitlement to the relief sought.
- **Specify relief sought.** State the precise order sought clearly in the application. Do not apply for an order that is too broad in scope. Provide a carefully formulated draft order so that the tribunal can easily see what is being requested and why.

Ex Parte Applications to Arbitrators

The rules of the major arbitral institutions prohibit applications for interim relief being made without notice. In any event, proceeding before an arbitrator on an *ex parte* basis would be ill-advised because:

- Most arbitral tribunals are extremely reticent about proceeding without giving both parties an opportunity to address them.
- Any steps taken without notice may affect the enforceability of the ultimate award. *Ex parte* evidence submitted to an arbitration panel that disadvantages any of the parties in their rights to submit and rebut evidence violates the parties' rights and is grounds for vacatur of an arbitration award.[26]

No Power to Bind Fully Constituted Arbitral Tribunal

Under the institutional rules considered here, the emergency arbitrator does not have the power to bind the full arbitral tribunal. The fully constituted tribunal has the power to vacate, amend or modify any order, award or decision by the emergency arbitrator.

The usual default position is that the emergency arbitrator cannot become a member of the full arbitral tribunal unless the parties agree otherwise.

Enforcing Preliminary Relief Awarded by Arbitrators in Court

Courts have held that they do not have the power to review an interlocutory ruling by an arbitration panel,[27] but have relaxed this rule when parties seek confirmation of provisional remedies awarded by arbitrators.[28]

In *Yahoo! Inc. v. Microsoft Corp.*, the court confirmed an award issued by an emergency arbitrator appointed under the AAA rules to grant emergency relief "until the matter can be fully and fairly decided by a three arbitrator panel of industry experts following discovery."[29] The *Yahoo!* case shows how quickly interim relief can be obtained in arbitration. The emergency arbitrator held two days of evidentiary hearings starting 11 days after Microsoft commenced arbitration and issued a decision six days after conclusion of those hearings. The next day, Yahoo! moved in court to vacate the award and Microsoft cross-moved to confirm. The court ruled for Microsoft less than a week later. In going from commencement to judicial confirmation in merely 25 days, the *Yahoo!* case demonstrates that even where the tribunal is not constituted, the use of emergency procedures provided by arbitral institutions can provide expeditious and effective relief. Moreover, the court respected the parties' agreement to keep proceedings confidential. The motion

papers were filed under seal and the only part of the proceeding that was made public was the judge's decision.

More recently, in *Companion Property & Casualty Insurance Co. v. Allied Provident Insurance, Inc.*, the arbitrators issued an interim award requiring the respondent to post security.[30] When the respondent ignored the interim award, the claimant made a motion in court to confirm it. The court reviewed the case law that supports the court's power to confirm interim awards of security and noted that "[w]ithout the ability to confirm such interim awards, parties would be free to disregard them, thus frustrating the effective and efficient resolution of disputes that is the hallmark of arbitration." Having concluded that it had the power to confirm the interim award, the court noted that it should confirm as long as there is a "barely colorable justification." On that standard, the court confirmed the award because the agreement between the parties required that the respondent provide collateral for its obligations.[31]

Where, on the other hand, a court is asked to vacate an interim award issued by arbitrators, the same considerations may not apply. In *Chinmax Med. Sys. Inc. v. Alere San Diego, Inc.*, the court refused a request to vacate an emergency arbitrator's interim order for certain conservatory measures under the ICDR Rules.[32] In *Chinmax*, the court in addressing a challenge to the interim order found that it did not have jurisdiction to vacate the order because it was not final and binding for the purposes of the New York Convention. The order itself stated that it would be subject to the consideration of the full arbitration tribunal, and on this basis the court refused to grant the motion to vacate.

Courts will only enforce that part of the interim relief that requires judicial intervention at that stage of proceedings. To determine whether to enter grant relief, a court must consider:

- The likelihood that the harm alleged by the party will ever come to pass.
- The hardship to the parties if judicial relief is denied at this stage in the proceedings.
- Whether the factual record is sufficiently developed to produce a fair adjudication of the merits.[33]

Resisting Interim Relief

In response to a request for interim relief, a party should marshal its legal arguments and supporting evidence to convince the tribunal or a court not to grant the requested relief. The opposition should address whether the tribunal or court has the power to grant the request and should give reasons why the application should be denied as a matter of discretion.

In addition to its main argument, the respondent should consider arguing in the alternative that if the relief sought by the applicant is granted, it should be conditioned on the applicant providing adequate security. Most institutional rules provide for security as a condition of interim relief granted by arbitrators.

Before an Emergency Arbitrator

The respondent should check how long it has under the rules to object to the appointment of the arbitrator and make the relevant objections in the permitted time frame. There may be grounds to resist the granting of emergency relief if the respondent has not been given proper notice of the application, or if the application fails to establish that the award to which the applicant may be entitled may be rendered ineffectual without interim relief.

In its response to the application, the respondent may consider whether it can object to the:

- Jurisdiction of the emergency arbitrator;
- Application on these grounds, among others:
  - the emergency arbitrator provision of the relevant rules do not apply;
  - the applicant is unlikely to succeed on the merits;
  - there is no urgent need for the interim relief to be granted;
  - irreparable harm would be suffered by the respondent if the emergency relief were granted; or
  - greater harm would be suffered by the respondent if the interim measure is granted than would be suffered by the applicant if it were not.

Before the Arbitral Tribunal

The respondent should check the applicable rules regarding the power of the tribunal and the procedures for interim relief. In its response to the application, the respondent may consider whether it can object to the application on these, among other grounds:

- The applicant is unlikely to succeed on the merits;
- There is no urgent need for the interim relief to be granted;
- Irreparable harm would be suffered by the respondent if the emergency relief were granted;
- Greater harm would be suffered by the respondent if the interim measure is granted than would be suffered by the applicant if it were not.

Before a Court

The respondent should consider:

- Whether federal or state courts in the state where the arbitration is seated have held that they lack power to grant the relief requested.[34]
- The application can be opposed on the ground that courts should intervene only until the arbitrators

have the opportunity to consider the request for emergency or injunctive relief.[35] Where the arbitral tribunal is authorized to grant the equivalent of preliminary injunctive relief, it has been inappropriate for the district court to do so.[36]

- The applicant is unlikely to succeed on the merits;
- There is no urgent need for the interim relief to be granted;
- Greater harm would be suffered by the respondent if the interim measure is granted than would be suffered by the applicant if it were not.

Endnotes

1. 9 U.S.C. §§ 1-16, 201-208, 301-07.
2. See AAA Rules 37 and 38 and Articles 6 and 24, ICDR Rules.
3. *See Aggarao v. MOL Ship Mgmt. Co.*, 675 F.3d 355, 376 (4th Cir. 2012), *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Salvano*, 999 F.2d 211, 214-15 (7th Cir. 1993) and *Blumenthal v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 910 F.2d 1049, 1051-54 (2d Cir. 1990).
4. *See AIM Int'l Trading LLC v. Valcucine SpA.*, 188 F. Supp. 2d 384, 387 (S.D.N.Y. 2002).
5. *See Fairfield Cnty. Med. Ass'n v. United Healthcare of New England, Inc.*, 557 F. App'x 53, 56 (2d Cir. 2014) and *Next Step Med. Co. v. Johnson & Johnson Int'l*, 619 F.3d 67, 70 (1st Cir. 2010).
6. *See, e.g., McCreary Tire & Rubber Co. v. CEAT S.p.A.*, 501 F.2d 1032, 1037-38 (3d Cir. 1974) and *I.T.A.D. Assocs., Inc. v. Podar Bros.*, 636 F.2d 75 (4th Cir. 1981).
7. *See Borden, Inc. v. Meiji Milk Prods. Co.*, 919 F.2d 822, 826 (2d Cir. 1990); *Aggarao*, 675 F.3d at 376; *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 335 F.3d 357, 365 (5th Cir. 2003); *Rhone Mediterranee Compagnia Francese Di Assicurazioni E Riassicurazoni v. Lauro*, 712 F.2d 50, 54-55 (3d Cir. 1983).
8. *See Result Shipping Co. v. Ferruzzi Trading USA Inc.*, 56 F.3d 394, 399 (2d Cir. 1995).
9. Federal Rules of Civil Procedure (FRCP) 64 states: "[a]t the commencement of and throughout an action [for attachment in federal district court], every remedy is available that, under the law of the state where the court is located, provides for seizing a person or property to secure satisfaction of the potential judgment."
10. Section 7502(c) of the New York Civil Practice Law and Rules ("CPLR"), for example, provides that to obtain provisional relief, the movant must demonstrate that "the award to which the applicant may be entitled may be rendered ineffectual without such provisional relief." CPLR 7502(c) provides that a showing of an ineffectual award is the "sole ground for the granting of the remedy" (compare *JetBlue Airways v. Stephenson*, 932 N.Y.S.2d 761 (Sup. Ct. N.Y. Co. 2010), *aff'd*, 931 N.Y.S.2d 284 (1st Dep't 2011) (denying motion for injunctive relief under CPLR 7502(c) because, although the movant presented arguments regarding the CPLR Article 63 criteria, it ignored the "ineffectual award" requirement) with *Winter v. Brown*, 853 N.Y.S.2d 361 (2d Dep't 2008) (lower court erred when it granted preliminary injunction in favor of seller in breach of contract action where seller failed to satisfy the traditional equitable criteria for preliminary injunctive relief)). CPLR 7502(c) also provides that if an arbitration is not commenced within 30 days of the granting of provisional relief, the order granting relief expires and costs, including reasonable attorneys' fees, are awardable to the respondent.
11. *See, e.g., Bahr Telecomms. Co. v. DiscoveryTel, Inc.*, 476 F. Supp. 2d 176, 184 (D. Conn. 2007) (federal court applying state law of attachment) and *Scottish Re Life Corp. v. Transamerica Occidental Life Ins. Co.*, 647 S.E.2d 102, 105 (N.C. App. 2007) (granting preliminary injunction under the Revised Uniform Arbitration Act (RUAA)). States that have adopted this rule include Colorado, Florida, Minnesota and Washington.
12. *See* AAA Rule 38(b) and Article 6, ICDR Rules.
13. *See* section 8 of the RUAA.
14. *Compare Stone v. Theatrical Inv. Corp.*, No. 14 CIV. 6494 PAE, 2014 WL 6790262, at *12 (S.D.N.Y. Dec. 2, 2014), *reconsideration denied*, No. 14 CIV. 6494 PAE, 2015 WL 195848 (S.D.N.Y. Jan. 14, 2015) (arbitrator has the power to appoint receiver as part of a final award) with *Ravin, Sarasohn, Cook, Baumgarten, Fisch & Rosen, P.C. v. Lowenstein Sandler, P.C.*, 839 A.2d 52, 57-58 (N.J. Super. Ct. App. Div. 2003) and *Pursuit Capital Management, LLC v. Claridge Associates, LLC*, No. 654301/12 (Sup. Ct. N.Y. Co. Mar. 21, 2013) (unpublished) (arbitrators may not appoint a receiver as a provisional remedy).
15. *See, e.g., CE Int'l Res. Holdings LLC v. S.A. Minerals Ltd. Pship*, No. 12 CIV. 8087 CM, 2012 WL 6178236, at *3-*5 (S.D.N.Y. Dec. 10, 2012).
16. AAA Rule 37.
17. AAA Rule 38(e).
18. AAA Rule 38(f).
19. AAA Rule 38(h).
20. Article 24, ICDR Rules.
21. Article 24.4, ICDR Rules.
22. Article 6(2), ICDR Rules.
23. Article 6(4), ICDR Rules.
24. Article 6(5), ICDR Rules.
25. Article 24(3), ICDR Rules.
26. *See Pac. Reinsurance Mgmt. Corp. v. Ohio Reinsurance Corp.*, 935 F.2d 1019, 1025 (9th Cir. 1991).
27. *See Michaels v. Mariforum Shipping, S.A.*, 624 F.2d 411, 414 (2d Cir. 1980).
28. *See Sperry Int'l Trade v. Gov't of Isr.*, 532 F. Supp. 901, 909 (S.D.N.Y. 1982), aff'd, 689 F.2d 301 (2d Cir. 1982) (confirming an arbitrator's order to place a disputed $15 million letter of credit in escrow pending a decision on the merits, finding that the award would be rendered a meaningless exercise of the arbitrator's power if the order were not enforced); *Island Creek Coal Sales Co. v. City of Gainesville*, 729 F.2d 1046, 1059 (6th Cir. 1984) (upheld the confirmation of the award that preserved the status quo, reasoning that the injunction issued by the arbitral tribunal would be meaningless absent judicial confirmation of it) and *S. Seas Navigation Ltd. v. Petroleos Mexicanos*, 606 F. Supp. 692, 694 (S.D.N.Y. 1985) (holding that if "an arbitral award of equitable relief based upon a finding of irreparable harm is to have any meaning at all, the parties must be capable of enforcing or vacating it at the time it is made").
29. 983 F. Supp. 2d 310 (S.D.N.Y. 2013).
30. No. 13-CV-7865, 2014 WL 4804466, at *3 (S.D.N.Y. Sept. 26, 2014).
31. *Zurich Am. Ins. Co. v. Trendsetter HR, LLC*, 2016 WL 4453694 (N.D. Ill. Aug. 24, 2016) (confirming interim award requiring insured to post security for insurance carrier's claims) and *see also Ecopetrol S.A. v. Offshore Exploration & Prod.* LLC, 46 F. Supp. 3d 327, 337 (S.D.N.Y. 2014) (enforcing interim awards requiring seller to tender certain amounts to purchaser with funds not derived from amounts in escrow).
32. No. 10CV2467 WQH NLS, 2011 WL 2135350 (S.D. Cal. May 27, 2011).
33. *See Draeger Safety Diagnostics, Inc. v. New Horizon Interlock, Inc.*, No. MC 11-50160, 2011 WL 653651, at *4 (E.D. Mich. Feb. 14, 2011).
34. *See, e.g., McCreary Tire*, 501 F.2d at 1037-38, *see also Bowers v. N. Two Cayes Co. Ltd.*, 2016 WL 3647339, at *3 (W.D.N.C. July 7, 2016) (confirming arbitrator's grant of injunctive relief ordering a percentage of the sale of certain real estate to be placed in an escrow account pending the outcome of the arbitration but denying confirmation of arbitrator's ruling that that the arbitration is binding on the parties).
35. *See, e.g., Next Step Med.*, 619 F.3d 67 at 70.
36. *See, e.g., Simula, Inc. v. Autoliv, Inc.*, 175 F.3d 716, 726 (9th Cir. 1999).

Provider and Arbitrator Immunity for Acting in Their Official Capacities

By Gerald M. Levine

Once parties have voluntarily agreed to resolve their disputes by arbitration courts have no authority to intervene in the proceeding and only a limited role at the end of the process to determine whether it was tainted in some manner prejudicial to the losing party, and if it was neither tainted nor unfair to confirm the award. Other than that, courts treat providers and arbitrators with deference in considering arguments challenging their decisions. Citing authority in its own jurisdiction an Illinois court noted that "by contracting to arbitrate their disputes, parties must accept 'the arbitrator's view of the meaning of the contract' [with the corollary that] [w]e will not overrule that construction merely because our own interpretation differs from that of the arbitrator."[1] The same sentiment can be found in other jurisdictions.

While in theory decisions can be set aside and awards vacated, they rarely are. In the words of the U.S. Supreme Court, "a court 'must' confirm an arbitration award 'unless' it is vacated, modified, or corrected 'as prescribed' in §§ 10 and 11 of the FAA."[2] If there's any distinction between a "must" and a "shall" in this context it is barely measurable. Parties challenging a decision or moving to vacate "bear[] a high burden of demonstrating objective facts inconsistent with [one of the four statutory grounds]" by "clear and convincing evidence."[3]

Further: "There is nothing malleable about [this standard], which unequivocally tells courts to grant confirmation in all cases, except when one of the 'prescribed' exceptions applies."[4] The best losing disputants can hope for is to avoid having to pay attorney fees and costs incurred for "acting in bad faith, vexatiously, wantonly, or for oppressive reasons," in seeking to overturn the arbitration award.[5]

There is a three-fold rationale for this hands-off policy: to protect the alternative dispute resolution space parties have elected; to assure parties receive the benefits of their agreements; and to support neutrals fulfilling their appointed roles. Immunity of providers and arbitrators acting in their official capacities expands the third prong of the hands-off policy. Unless conduct exposed by the record is so egregious as to support personal liability of providers or arbitrators, courts at every level and jurisdiction reject such claims.

A good place to begin this tour of recent cases is the U.S. Supreme Court's 1991 decision in *Mireles v. Waco*:[6]

> [judicial] immunity is overcome in only two sets of circumstances. First, a judge is not immune from liability for nonjudicial actions, i.e., actions not taken in the judge's judicial capacity. Second, a judge is not immune for actions, though judicial in nature, taken in the complete absence of all jurisdiction.

In *Bell Atl. Corp. v. Twombly*[7] the Court (citing an earlier Eighth Circuit decision[8]) agreed that "[b]ecause an arbitrator's role is functionally equivalent to a judge's role, courts of appeals have uniformly extended judicial and quasi-judicial immunity to arbitrators."[9] As we will see, the policy also extends to providers acting in their official roles. The exclusive remedy for challenging conduct that taints awards lies in federal and state arbitration acts that provide adjudicatory space for the arbitral process.

Arbitrator Immunity

High though the bar is for vacatur it is still higher for finding personal liability. The Second Circuit Court of Appeals has held that the "functional comparability of the arbitrators' decision-making process and judgments to those of judges and agency hearing examiners generates the same need for independent judgment, free from the threat of lawsuits. Immunity furthers this need."[10] The court also pointed out that "the Courts of Appeals that have addressed the issue have uniformly immunized arbitrators from civil liability for all acts performed in their arbitral capacity."

Failure to overcome immunity is illustrated in two New York cases, in 2016 in *Pinkesz Mut. Holdings, LLC v. Pinkesz*[11] and the other from 2014, *Siskin v. Cassar*[12] as well as in federal court, *Miskell v. Chase*.[13] In the federal action the court noted in dismissing the claim that under Maryland law arbitrators are accorded immunity "in the absence of an affirmative showing of malice or bad faith."[14] It also noted that in Illinois, "Parties who, although not judges, engage[d] in adjudication (such as private arbitrators or administrative tribunals)…enjoy absolute immunity."[15] In none of these cases was there evidence the arbitrators conduct was taken "in the complete absence of all jurisdiction" or out of "malice or bad faith."

In *Pinkesz Mut. Holdings* the court vacated the arbitration award (actually, an amended award) on the grounds that the panel lacked authority to amend its prior award. The court held that "immunity also applies to acts taken in excess of authority." Importantly, however, "the plaintiffs failed to allege how any of the acts of the rabbinical court defendants were undertaken in the clear absence of all jurisdiction." Implicit in the decision is that the bar for proving liability cannot be cleared with formulaic allega-

tions such as "merely assert[ing] conduct by the rabbinical defendants in their capacity as arbitrators."

While the fact pattern in *Siskin* is somewhat different, the court reached the same conclusion in dismissing the action against the arbitrator and provider (American Arbitration Association), essentially on the ground that plaintiff's failed to allege predicate facts sufficient to clear the higher bar for personal liability. The court held that "[t]he evidence submitted by the AAA defendants in support of their motion to dismiss the complaint…disproved the essential allegation of the complaint that the AAA defendants acted beyond the scope of their arbitral capacity, and established that the plaintiff does not have a cause of action sounding in negligence and breach of contract against them."

Where arbitrators have acted within the scope of their capacities there can be no basis for a claim beyond vacatur. These New York decisions in turn rest on earlier authority denying complaints against arbitrators for failure to state a claim.[16]

Provider Immunity

This policy ruling also embraces providers, most recently in *Imbruce v. Am. Arbitration Ass'n, Inc*.[17] and in *Owens v. Am. Arbitration Ass'n, Inc*., Civ.,[18] although the tour also includes two lawsuits against the Forum, formerly known as the National Arbitration Forum (NAF), in one of which the Forum was accused of not acting in any official capacity. In *Imbruce*, the Court noted that the "[e]xtension of the policy to sponsoring organizations is also intended to avoid discouraging such organizations from conducting future arbitrations."

The *Imbruce* plaintiffs argued that their claim raised an "issue of first impression, namely whether the doctrine of arbitral immunity should be applied to conduct occurring after issuance of an arbitral award."[19] It appears the AAA was tardy in assessing a fee after the award. According to the plaintiffs the arbitrator and AAA were "stripped of authority under the common law principle of *functus officio*." The court rejected this argument as a "veiled attempt to evade arbitral immunity." The court continued: "If, as plaintiffs maintain, their objection is solely that AAA wrongfully collected a filing fee for a monetary counterclaim from the Henry Parties post award, then plaintiffs have not suffered harm that this suit could redress."

In *Owens*, plaintiff "rais[ed] claims for breach of contract, unjust enrichment, tortious interference with contract, and tortious interference with prospective economic advantage." It took issue with the AAA's "refusal to disqualify [an] arbitrator" and the question was whether doing so was within or outside its official role. The court held the AAA was acting within the "scope of its arbitral process:"

> The cases are clear that an organization that sponsors arbitration is immune from liability for acts it takes "within the scope of the arbitral process." [*Olson v. Nat'l Ass'n of Sec. Dealers*, 85 F.3d 381, 382 (8th Cir. 1996)]. Indeed, one court of appeals specifically stated that a sponsoring organization's "refusal to disqualify [an] arbitrator…falls within the scope of [arbitral] immunity." Jason v. Am. Arbitration Ass'n, 62 F. App'x 557 (table), 2003 WL 1202934, at *1 (5th Cir. Mar. 7, 2003).

The court distinguished the case before it from *In re NAF Nat'l Arbitration Forum Trade Practices Litig*.,[20] (the earlier of the two NAF cases) in which the decision "rested on the allegation that the 'arbitrations' performed by NAF related to consumer debt 'were not arbitrations at all,' but that the NAF would regularly defer to credit-card companies as to the appropriate decision in a given case, rather than having arbitrators make that decision."[21]

In re NAF is particularly noteworthy in that it represents a rare rebuke against a provider. In 2010 a putative class of individuals holding consumer debt sued NAF, asserting "systemic, pervasive, and far-reaching allegations of bias and corruption" that rendered "every single arbitration performed by NAF suspect." NAF moved to dismiss on the grounds of immunity, but the court denied the motion and ultimately held it liable on grounds of "systemic, pervasive, and far reaching allegations of bias and corruption." In that case, the court observed that the

> allegations Plaintiffs make are not procedural irregularities or even violations of the organizations' own rules. Rather, they are systemic, pervasive, and far-reaching allegations of bias and corruption, rendering every single arbitration performed by NAF suspect. At this stage of the litigation, NAF cannot claim arbitral immunity.

The other notable decision featuring the Forum held that it was acting in its official capacity.[22]

Fast forward to the new action against NAF, *Virtualpoint, Inc. v. Poarch Band of Creek Indians and National Arbitration Forum, Inc*.[23] In this case, plaintiff (a domain name investor and reseller) relying on *In re NAF* sought to hold the provider liable for common law fraud. However, the court found the facts in the new case entirely different from the earlier one.

In the administrative proceeding conducted under the auspices of the Uniform Domain Name Dispute Resolution Policy the panel found Virtualpoint to be a cybersquatter and ordered the subject domain name to be transferred to the trademark owner. Under the Policy, losing parties have a statutory right to challenge awards

under the Anticybersquatting Consumer Protection Act.[24] The ACPA part of the action is still pending but the court disposed of the claim against the Forum by dismissing the complaint.

Referring to the circumstances in the earlier case, the court noted that the

> doctrine [of immunity] exists to protect decision makers "from undue influence" and that plaintiffs were in fact alleging that all of NAF's arbitrations were corrupted by the sort of undue influence arbitral immunity is designed to prevent, so the application of immunity would have been improper.

It is significant that in dismissing the claim against the Forum the court (referring to *In re NAF)* "stressed the narrowness of its ruling…by acknowledging the 'undeniably broad' scope of arbitral immunity and noting that the claims before [it] would have been barred had they alleged only 'procedural irregularities or even violations of [the NAF's] own rules.'"

But in *Virtualpoint*, plaintiff

> has produced no examples of courts denying arbitral immunity based on allegations analogous to the ones it advances here, and the Court therefore concludes that its claims against NAF are clearly barred by the doctrine of arbitral immunity.

Instead, plaintiff alleged systematic bias in favor of law firms regularly appearing before it as complainants' counsel in the UDRP process. "But allegations of this sort cannot overcome arbitral immunity," citing a decision from the district court, Hawaii:[25] "[A]llegations of bias, bad faith, malice, or corruption generally do not bar the application of quasi-judicial immunity," although they may be grounds for vacatur.

Conclusion

Whether against arbitrators or providers, the evidentiary demands are significant for vacatur and even greater for overcoming immunity. Conduct that could conceivably result in vacatur of an arbitration award is insufficient to clear the higher bar. The higher bar is cleared only when providers and arbitrators act outside their capacity or in the complete absence of all jurisdiction, but arbitrators appointed and acting within their capacities are absolutely immune. In the rare instance in which a circuit found immunity overcome against a sitting judge, the Supreme Court reversed the judgment ("[I]mmunity applies even when the judge is accused of acting maliciously and corruptly.").[26] Against arbitrators the conduct would have to be extreme to be an inexcusable point, for which there are no recent (and perhaps few ancient) examples.[27]

Endnotes

1. *Cantor Fitzgerald & Co. v. Walton*, 2016 IL App (1st) 152946-U (Ill. App., Sept. 22, 2016).
2. *Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576, 582 (2008) (quoting 10 U.S.C. § 9).
3. *Kolel Beth Yechiel Mechil of Tartikov, Inc. v. YLL Irrevocable Tr.*, 729 F.3d 99, 105, 106 (2d Cir. 2013) (internal quotation marks omitted).
4. *Hall St. Asocs,* at 587.
5. *Local 97, Int'l Bhd. of Elec. Workers, A.F.L.-C.I.O. v. Niagara Mohawk Power Corp.*, 196 F.3d 117, 132 (2d Cir. 1999).
6. 502 U.S. 9, 11-12 (1991).
7. 550 U.S. 544 (2007).
8. *Olson v. Nat'l Ass'n of Sec. Dealers*, 85 F.3d 381, 382 (8th Cir. 1996).
9. *Bell Atl. Corp.*, at 545.
10. *Austern v. Chicago Bd. Options Exchange, Inc.*, 898 F.2d 882 (2nd Cir 1990).
11. 2016 NY Slip Op. 4034 (2nd Dept. May 25, 2016).
12. 122 A.D.3d 714 (2nd Dept. 2014).
13. 16-cv-1460 (D. Md. Oct. 20, 2016).
14. Md. Code Ann., Cts. & Jud. Proc. § 5-615; § 3-2A-04(g).
15. *Coleman v. Dunlap*, 695 F.3d 650, 652 (7th Cir. 2012).
16. *Jacobs v. Mostow*, 69 A.D.3d 575, 893 N.Y.S.2d 560 (2nd Dept. 2010).
17. 15-cv-7508 (S.D.N.Y. Sept. 22, 2016).
18. CV 15-3320 (D. Minn., December 9, 2015).
19. Citing *New England Cleaning Servs., Inc. v. Am. Arbitration Ass'n*, 199 F.3d 542, 545 (1st Cir. 1999).
20. 704 F. Supp. 2d 832, 836 (D. Minn. 2010).
21. *Id., In re NAF*, pg. 5.
22. *Virtualpoint, Inc. v. Poarch Band of Creek Indians and National Arbitration Forum, Inc.*, CV 15-02025 (CD CA, Southern Division June 6, 2016).
23. CV 15-02025 (C.D. Cal., Southern Division June 6, 2016),
24. 15 U.S.C. § 1125(d).
25. *Bridge Aina Le'a v. State of Hawaii Land Use Commission*, 125 F. Supp. 3d 1051, 1077 (D. Hawaii 2015).
26. *Id., Mireles v. Waco,* 116 L.Ed.2d at 10.
27. *Cf. JAMS, Inc. v. Superior Court of San Diego Cnty*, D069862 (Cal. App., 2016) in which the motion court denied the petition of JAMS and "private judge" to dismiss an action against them under the California anti-SLAPP statute. The court denied by motion holding that the statements fell within the commercial speech exemption to the statute because the alleged statements that form the basis of plaintiff's claims were "posted on the JAMS [] [Web site] for the purpose of promoting and securing sales or commercial transactions in defendants' ADR services. The intended audience was [Kinsella], a party involved in dissolution litigation, who actually engaged the services of JAMS and Sonenshine." On a writ of mandate, the Court of Appeal affirmed. It noted that "all allegations of wrongdoing [omissions to her biographical information] relate to information Kinsella specifically viewed on defendant JAMS' [Web site] before he agreed to select Sonenshine as the [privately compensated temporary judge]."

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Arbitration of Disputes in the Aerospace Industry

By Stephen E. Smith and Lester W. Schiefelbein, Jr.

Characteristics of the Aerospace Industry

According to Merriam Webster, the term "aerospace" first appeared in 1958, the year after the first satellite was launched into space and commercial jet transportation became mainstream with the introduction of Boeing 707 flights by Pan American World Airways. Today the aerospace industry may be defined as "the industry that deals with travel in and above the Earth's atmosphere and with the production of vehicles used in such travel."[1] The worldwide aerospace industry, including both civilian and military components, now accounts for nearly $700 billion in annual sales, with slightly over 50 percent coming from the government/military side.

"Virtually all the significant advantages of arbitration, e.g., confidentiality, cost effectiveness, quicker resolution, flexibility, ability to choose arbitrators with technical and subject matter expertise, limited discovery and document production, finality and cross-border enforceability apply to disputes among aerospace industry participants and between those participants and their customers. However, as discussed below, many of those advantages have particular applicability to disputes involving aerospace companies."

Since the mid 1990s there has been a high degree of consolidation among companies in the industry, with the larger players absorbing both formerly major players and many of their first and second tier suppliers. Continued defense budget cutbacks are expected to prompt further consolidations in the years to come. Despite these consolidations, the larger companies still rely heavily on thousands of suppliers whose failures to deliver on time can cause major delays and revenue losses for the larger companies;[2] thus supplier issues are likely to be a major source for disputes.

Major products and services provided by aerospace industry players include commercial and military aircraft, missiles, civil (i.e. government-non-military) commercial and military satellites, and the rockets used to place them in space. To varying extents all the major industry players buy cyber-related products and services, and many furnish such products and services. And, as discussed below, insurance companies are also sometimes involved in disputes involving aerospace firms and their customers.

Virtually all the significant advantages of arbitration, *e.g.*, confidentiality, cost effectiveness, quicker resolution, flexibility, ability to choose arbitrators with technical and subject matter expertise, limited discovery and document production, finality and cross-border enforceability[3] apply to disputes among aerospace industry participants and between those participants and their customers. However, as discussed below, many of those advantages have particular applicability to disputes involving aerospace companies.[4]

Confidentiality and Handling of Government-Controlled and Classified Information

Confidentiality considerations arise when highly proprietary and sensitive information is involved in a dispute. Given the very nature of the products and services offered by the aerospace industry, most disputes with significant sums of money or intellectual property rights at issue involve such information. Many such disputes also involve information that governments regulate, sometimes including export controlled and/or classified information. The confidentiality features of arbitration can greatly simplify the process of disclosing and using such information in arbitrations.

Where classified information is involved in disputes in the aerospace industry, the "state secrets doctrine" frequently comes into play. Virtually every national government has a state secrets doctrine. The doctrine is best defined as a government's ability to prevent disclosure of any information that, if disclosed publicly, would be reasonably likely to cause significant harm to the national defense or foreign relations of a government.

Companies and governments spend huge sums of money to get satellites into space, but an average of one in 20 launches will fail. A hypothetical dispute involving a failed launch of commercial and government satellites is illustrative. Assume that an unmanned commercial rocket with both a commercial and a government classified satellite aboard explodes seconds after takeoff, destroying both the rocket and the satellites, collectively valued at over $500 million. Many such launches are insured, usually by consortia consisting of U.S. and non-U.S. insurers. The rocket insurer refuses to pay under the insurance policy since the government has asserted the state secrets doctrine on the accident investigation report and refuses to allow the insured rocket and satellite manufacturers to provide information their insurers demand.

The rocket manufacturer commences an arbitration against the insurers and there is a tension between the state secrets doctrine and the insurer's ability to evaluate and defend the claim. Without the accident report, the

how or why of the rocket explosion cannot be completely known or understood. There is also a tension for the arbitration panel. Dealing with state secrets is not familiar territory and there are civil and criminal sanctions for violations.

So what guidelines can an arbitration panel look to for guidance? Article 9(2)(f) of the International Bar Association rules on the Taking of Evidence in International Arbitration (2010) ("IBA Rules")[5] provides that an arbitration tribunal may exclude from evidence or production any document, statement or oral testimony on "grounds of special political or institutional sensitivity (including evidence that has been classified as secret by a government or a public international institution) that the arbitral tribunal determines to be compelling."

Application of the IBA Rules would permit the arbitration panel to exclude the state secrets material from the arbitration. However, this approach could also deprive the respondent insurance companies of the due process they are entitled to, thereby potentially imperiling enforceability of an award against them.

"The bottom line is that the confidentiality and procedural flexibility of arbitration arguably makes it particularly well suited to address state secret and related challenges."

An alternative approach is to be creative, nibble at the edges, and if the facts permit, sidestep or otherwise satisfy the states secrets concerns. In the hypothetical explosion the classified satellite most likely was not the cause of the explosion. The rocket engine sits at the base of the rocket. The classified satellite sits 14 building stories above the rocket engine. The explosion was just seconds after lift-off and a standard analysis used by an aerospace company would likely find the explosion was due to a rocket engine anomaly. Perhaps most simply, state secrets information could be redacted from the accident investigation report, thereby removing a procedural constraint to the resolution of the insurance coverage dispute. However, this quite likely would not satisfy the insurers. Other creative solutions would include:

- Arbitrators and other key people in the case could be granted limited security clearances for purposes of the arbitration. Choosing arbitrators experienced in the industry that hold or have held security clearances, or who are quickly "clearable," can greatly expedite the process. This could also involve the government granting access to sensitive information in a secure location that only designated persons could have access to.
- It may be possible to craft confidentiality agreements or orders that limit the people, approved by the government, who can see certain pieces of evidence.
- A mock arbitration may be particularly useful for claimant. If state secrets information would likely be excluded from the arbitration, the mock arbitration could help claimant determine if it could prove its claim without that information.

A dialogue and possible solutions to procedural constraints in state secret matters take time. Arbitrators can start the discussion early, and involve the parties, their counsel and the government in the discussion. Obviously, collective solutions meeting all the interested entities needs are best.

The bottom line is that the confidentiality and procedural flexibility of arbitration arguably make it particularly well suited to address state secret and related challenges.

Disputes Between U.S. Government Contractors and Their Subcontractors

In the United States, the contractual relationships between most U.S. government agencies and their prime contractors (meaning a contractor in direct privity with the government) are generally conducted under provisions and procedures set forth in the Federal Acquisition Regulation (FAR).[6] The U.S. Department of Defense and its individual military services, which account for a very high percentage of dollars spent on aerospace systems, issue their own supplements to the FAR.

"The new normal is the hacking of national security technology and technology products."

Companies wishing to do business with the U.S. government are required to accept the large number of contract terms and conditions set forth in the FAR and FAR Supplements. While some of these provisions are required to be "flowed down" to subcontractors that are not in privity with the government, the governing law of such contracts is typically not, or at least not exclusively, the law pertaining to U.S. government contracts.

In such cases, the advantages of arbitration discussed above frequently apply. The ability to appoint arbitrators with experience in both commercial law and U.S. government contract law can be quite important for several reasons. Such arbitration professionals understand the interplay between commercial and government contract law. Appointing experienced arbitrators can avoid not only a substantial learning curve that might be the case with judges not well grounded in such cases, but can al-

low such cases to be resolved much more expeditiously than in courts.

Cyber-Related Disputes

The new normal is the hacking of national security technology and technology products. United States intelligence officials are centered on the impact that hacker data thefts can have on national security and global politics. James R. Clapper, the outgoing Director of National Intelligence, warned in his annual worldwide threat briefing in February 2016 that Russia was escalating its espionage campaigns against U.S. targets. Recent news reports bear this out.

Given the nature of the technologies they use and develop, aerospace companies are a target-rich environment for hackers and others seeking to exploit information systems weaknesses. When there is a hack of technology that has a national security application, the immediate questions are—who, what, when, where, why and how? In the examination of those issues, a charge of contract breach can be made and the dispute not surprisingly is most appropriately heard by arbitrators. Arbitration permits a singular and necessary advantage—availability of a group of neutrals with industry experience and who hold or are eligible to hold security clearances. Those arbitrators could be permitted access to information concerning a data breach and to technology and technology products destined for national security use.

Arbitration of Commercial Aircraft and Aviation Disputes

Disputes in the commercial aviation sector can arise from a wide variety of business relationships. These could include disputes arising out of aircraft purchase or leasing agreements, delays in delivery of parts or delivery of defective parts, IT disputes arising from airline reservations systems, commissions relating to sales of aircraft and many others. Any of these scenarios could cause significant losses. All of these disputes can benefit from utilizing the flexibility that arbitration affords to craft a bespoke dispute resolution process.

Conclusion

The above examples of the types of issues faced by aerospace industry companies in disputes are illustrative of the many advantages arbitration can provide to industry participants as compared with other dispute mechanisms. As the industry continues to consolidate, and information protection issues grow in importance, the advantages of arbitration are likely to become even more apparent.

Endnotes

1. http://www.merriam-webster.com/dictionary/aerospace.
2. *See* Financial Times, July 26, 2016, "Airbus and Boeing put pressure on supply chain" https://www.ft.com/content/e0d51872-516c-11e6-9664-e0bdc13c3bef.
3. *See* http://www.americanbar.org/content/dam/aba/publications/dispute_resolution_magazine/March_2012_Sussman_Wilkinson_March_5.authcheckdam.pdf.
4. In recognition of this, the American Arbitration Association/International Centre for Dispute Resolution recently created a specialized panel of arbitrators and mediators having extensive experience in aerospace, aviation and national security issues. *See:* ICDR-AAA Aerospace, Aviation and National Security Panel, available at https://www.adr.org/aaa/ShowPDF?doc=ADRSTAGE2044890. The authors are charter members and serve on the Steering Committee for this specialized panel.
5. https://www.scribd.com/document/134332470/IBA-Rules-on-Taking-Evidence-2010 .
6. 48 C.F.R. §§ 1 *et seq.*

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Arbitrating Fair Labor Standard Act Cases—Is the Process a Problem?

By Tracy B. Frisch and Robyn Weinstein

In the 2015 decision *Cheeks v. Freeport Pancake House, Inc., W.P.S. Industries, Inc*. the Second Circuit held, as a matter of first impression that the Fair Labor Standards Act (FLSA) fell under Federal Rule of Civil Procedure Rule 41's "applicable federal statute" exception.[1] Meaning, absent approval of the District Court or Department of Labor (DOL) parties cannot settle FLSA claims through a private stipulated dismissal with prejudice pursuant to the Federal Rule of Civil Procedure 41(a)(1)(A)(ii).[2] Since *Cheeks* was decided, the question has been raised at the District Court level as to whether pre-dispute agreements to arbitrate FLSA claims are considered private settlements requiring approval of the District Courts or DOL. Thus far, the District Courts' answer has been uniformly no.

"Judge McMahon found that nothing in Cheeks *stands for the proposition that FLSA claims cannot be arbitrated; it does, however, mean that any settlement of such a claim must be court-approved."*

The issue of pre-dispute agreements to arbitrate FLSA claims post-*Cheeks* was raised in a handful of New York District Court decisions during 2016. In February 2016 Judge McMahon of the Southern District of New York held, in the case *Moton v. Maplebear Inc*., that *Cheeks* was not applicable in the pre-dispute arbitration agreement context.[3] Judge McMahon reasoned that although *Cheeks* held that stipulated dismissals settling FLSA claims with prejudice pursuant to Federal Rule of Civil Procedure 41(a)(1)(A)(ii) required approval of the District Court or the Department of Labor to take effect, the plaintiff and defendant in *Moton* were not trying to settle a claim asserted in a lawsuit. Instead, the parties were proposing to litigate a claim in an alternative forum. Further, Judge McMahon found that nothing in *Cheeks* stands for the proposition that FLSA claims cannot be arbitrated; it does, however, mean that any settlement of such a claim must be court-approved. In *Moton*, there was an arbitration agreement signed by the parties at the outset of the employment relationship and the parties were compelled to arbitration. Judge McMahon did not dismiss the action but issued a stay and cited *Katz v. Cellco P'ship*, 794 F.3d 341, 343 (2d Cir. 2015). In citing *Katz* Judge McMahon stated, "[f]urther, although Defendant has requested that the Court dismiss this action upon granting its motion, the case will be stayed pending the outcome of arbitration. As the Second Circuit reasoned in *Katz v. Cellco P'ship*, 794 F.3d 341, 343 (2d Cir.), a stay permits the parties 'to proceed to arbitration directly, unencumbered by the uncertainty and expense of additional litigation,' should judicial participation in the arbitral process prove necessary." *Id*. at *9. The plaintiff further argued that under *Cheeks* and other precedent[4] the forum selection clause, fee-splitting, fee-shifting and confidentiality provisions rendered the arbitration clause unenforceable because they amount to an impermissible waiver of statutory rights. Judge McMahon viewed this as an argument of unconscionability and held under New York law that these provisions, to the extent needed, could be severed and the arbitration clause enforced. *Id*. at *8.

Around the same time as *Moton* was decided, Judge Weinstein heard a similar case, also against Maplebear Inc., *Bynum v. Maplebear Inc*.[5] *Bynum* likewise involved a pre-dispute agreement to arbitrate FLSA claims. The plaintiff in *Bynum* asserted that in light of *Cheeks* FLSA claims should not be arbitrated. Judge Weinstein rejected that claim and held that *Cheeks* did not require District Court or DOL approval of pre-dispute agreements to arbitrate FLSA claims. In his opinion, Judge Weinstein wrote that *Cheeks* did not raise the issue of the arbitrability of FLSA claims, and that the plaintiff's reference to the Second Circuit's decision in *Cheeks* was misplaced. Judge Weinstein did find merit in plaintiff's argument that the provisions in the arbitration agreement requiring the arbitrator to award legal fees and costs to the prevailing party were unconscionable pursuant to the applicable state law, which in *Bynum* was California law. Ultimately, Judge Weinstein found that "[w]ithout the objectionable venue, fee splitting and fee shifting clauses, the arbitration agreement is valid and enforceable." *Id*. at 538.

Similarly in *Zambrano v. Strategic Delivery Solutions, LLC*, 15 Civ. 8410 (ER), 2016 WL 5339552 (S.D.N.Y. Sept. 22, 2016), the plaintiffs argued that *Cheeks* should be interpreted to prevent plaintiffs from having to arbitrate their FLSA claims because the potential costs and fees involved would undercut the concerns expressed by *Cheeks*. *Id*. at *8. Judge Ramos rejected that argument, finding that the prohibitive costs were too speculative and ordered the parties to arbitrate under their pre-dispute arbitration clause. Judge Ramos did cite to *Cheeks* in finding that the "arbitration provision cannot preclude [plaintiffs] from recovering their reasonable attorney's fees and costs should they prevail on their claims. '[T]he FLSA is a uniquely protective statute.'" *Id*. at *6. The court held that it is within the arbitrator's authority to modify the agreement and that the provision limiting recovery of attorney's fees was also severable from the agreement to arbitrate, and that the agreement to arbitrate remained enforceable. *Id*. at *8. Like the other District Court judges, Judge Ramos

stayed the case pending arbitration rather than dismissing the case citing *Katz*. *Id*. at *9.

Since *Cheeks* was decided, the New York District Courts have been faced with the argument that *Cheeks* expands judicial review of pre-dispute agreements to arbitrate. Thus far, it appears that the District Courts have rejected that argument based on the fact that the *Cheeks* case itself did not involve an arbitration clause.[6] However, the questions have not yet been answered as to whether the *Cheeks* decision could affect how District Courts view post-dispute agreements to arbitrate, how District Courts might view settlements reached once the matter has been compelled to arbitration, or how arbitrators themselves might apply *Cheeks* to settlement agreements reached during the arbitration process.

Endnotes

1. *See Cheeks v. Freeport Pancake House, Inc., W.P.S. Indus., Inc*. 796 F. 3d 199, 206 (2d Cir. 2015), *cert. denied*, 136 S.Ct. 824 (2016).
2. Rule 41(a)(1)(A) provides in relevant part: "Subject to Rules 23(e), 23.1(c), 23.2, and 66 and *any applicable federal statute*, the plaintiff may dismiss an action without a court order by filing: (i) a notice of dismissal before the opposing party served either an answer or a motion for summary judgment; or (ii) a stipulation of dismissal signed by all parties who have appeared" (emphasis added).
3. *Moton v. Maplebear Inc*. No. 15 Civ. 8879 (CM), 2016 WL 616343, at *6 (S.D.N.Y. Feb. 9, 2016), *appeal dismissed* (2d Cir. 16-555) (Jul. 13, 2016).
4. The other case cited by Plaintiff was *Barrentine v. Arkansas-Best Freight Sys., Inc*., 450 U.S. 728, 101 S.Ct. 1437, 67 L.Ed2d 641 (1981).
5. *Bynum v. Maplebear Inc*. 160 F. Supp. 3d 527 (E.D.N.Y. 2016), *on remand* 15-CV-6263, 2016 WL 4995093, (E.D.N.Y. Sept. 19, 2016) (dismissing action with prejudice in light of plaintiff's repeatedly stated intention to abandon arbitration as sought by plaintiff so could appeal initial decision to Second Circuit), *appeal pending* (2d Cir. 16-3348) (filed Sept. 30, 2016).
6. *Alfonso v. Maggies Paratransit Corp*., No. 16-CV-0363 (PKC)(LB), 2016 WL 4468187 (E.D.N.Y. Aug. 23, 2016) is another District Court case that addresses the issue of pre-dispute agreements to arbitrate FLSA claims. In *Alfonso*, Judge Chen ordered the FLSA case to arbitration and issued a stay. She stated, " [a]s an aside, the Court notes that because the threshold question before it is whether the challenged CBA provisions constitute substantive waivers of Plaintiff's statutory rights at all, Plaintiff's reliance on *Cheeks v. Freeport Pancake House, Inc*., 796 F.3d 199 (2d Cir.2015), for the proposition that an employee's FLSA rights may not be waived without approval by the Department of Labor or a court, is wholly inapposite." *Alfonso* at footnote 6.

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When the Deal Goes South: Mediating Disputes in Post-Merger Litigation

By Arthur H. Rosenbloom

Background

The plot is almost always the same, replete with the unchanging choreography of a classical ballet. Months following the backslapping revelry of the closing dinner, the Buyer (although sometimes the Seller, especially where the Buyer's shares represent the deal's consideration), asserts that the counterparty has been less than forthcoming during the Buyer's pre-merger due diligence. A few such examples include these:

- *Title to assets*
  For example, if the Seller was acquired significantly for the value of its intellectual property, the matter could turn on whether the Seller breached its representation and warranty as to its exclusive title to those assets, especially if it turns out that there was a threatened infringement litigation against the Seller. For its part, the Seller will assert that threatened litigation is meritless and may offer to indemnify the Buyer, often through a key shareholder.

- *Seller's financial statements*
  These involve whether the balance sheet, income statement or sources and applications that the Buyer asserts were negligently or fraudulently prepared. In such settings, the Seller's accountants may be joined as defendants.

- *Regulatory compliance*
  For example, the Buyer acquires a manufacturing facility that turned out to be zoned only for retail sales.

- *Claims and defenses*
  In consequence of the alleged breaches, the Buyer asserts breach of contract, negligence or intentional misrepresentation, unjust enrichment and other claims. It's a virtual certainty that, following the copy book defenses, such as failure to state a claim or waiver, the Seller will assert that it provided adequate notice of the deficiencies undergirding the Buyer's claims and that the Buyer willingly accepted the risks. The Seller may also lob in a counterclaim asserting that the downturn in the Seller's business was caused by the Buyer's post-closing mismanagement of that business or its failure to provide the funding it promised the Seller.

- *Battleground areas*
  While the choreography of the pleadings is quite standard, actual outcomes in these litigations are highly fact sensitive. Outcomes could well turn on the extent to which the Buyer's or the Seller's counsel won the drafting battle. For example, a general disclosure of the problem of which the Buyer now complains, set forth in schedules to the purchase agreement, could tilt the scale in favor of the Seller. Even absent such a display, the Seller could still prevail if its counsel had inserted the words, "The inclusion of any information in any schedule attached hereto or other documents delivered by Seller pursuant to this agreement shall not be deemed to be an admission of the materiality of such items, nor establish a standard of materiality for any purpose whatsoever." Conversely, unqualified representations and warranties made by the Seller, as opposed to those qualified with the proviso "to the knowledge of Seller," could turn the tide in favor of the Buyer.

- *Material in Seller's data room*
  It's customary for sellers to display (usually in virtual form) data concerning its legal, business, tax and accounting affairs in a so-called data room. Because it's the seller that initially determines the content of the data room, thoughtful buyers will insist that the data room include material addressing specific concerns resulting from their due diligence. Further, how forthrightly the Seller responds to the Buyer's questions following the Buyers' data room visit may have evidentiary value in the post-merger litigation period.

- *Damages issues*
  Assuming the Buyer makes out a case sufficient to prevail, following dispositive motion practice by the Seller, damage quantification will become an important part of the mediation process. More on this to come.

Mediating Post-Merger Disputes

A mediator may find him or herself mediating one of these post-merger disputes as a result of a provision in the merger document calling for such intervention, in

consequence of a referral from a trial judge, or through voluntary submission from parties eager to avoid the time, expense and uncertainty of the litigation process. As is generally the case, the post-merger dispute mediation will initially involve a conference call with counsel to establish the nature and length of a pre-mediation written submission by each side. It is typical to have counsel submit to the mediator and each other their initial position on liability, and, for the mediator's eyes only, their initial views on settlement, including the terms of such settlement if it's one other than 100% upfront payment.

"In some circumstances, the Buyer may assert damages based not on a dollar-for-dollar basis but rather on a price/earnings multiple basis."

While the shuttle diplomacy of the mediation process will necessarily address the strength and weaknesses of each side's liability position, in post-merger dispute settings it's more likely that with willing parties, the key question will be the amount it will take to get the case to settle. However, to arrive at that figure in the post-merger dispute, the mediator should encourage the parties to look carefully at the economic elements at bar. So, for example, if the issue on which Buyer complains involves a shortfall, such as inventory shortfalls at the time of the merger agreement or at a true-up post-closing balance sheet, the case may simply settle at a dollar-for-dollar restitution by the Seller of some (or all) of that shortfall. That's because such shortfalls don't adversely affect the net present value of the Seller's future cash flows that represent its going-concern value.

"If, at an appropriate point in the mediation, the parties seem to be going nowhere in their efforts to compromise, the mediator might encourage them to develop "a before and after" discounted cash flow approach that determines the difference between Seller's value with and without considering the disability, with some weighting concerning the likelihood or non-likelihood of complete impairment of Seller's cash flows..."

However, suppose the issue at bar is one that *could* adversely affect the net present value of those cash flows? Consider, for example, the fact pattern previously discussed concerning a Seller that the Buyer can show was acquired in part for the value of its intellectual property, an asset whose viability is put into question by the threatened third party infringement litigation. In such a circumstance, it is likely that potential liability will exceed the upper bounds of the indemnifications if some of the Seller's cash flows could be permanently impaired. In some circumstances, the Buyer may assert damages based not on a dollar for dollar basis but rather on a price/earnings multiple basis. For example, assume the Seller was purchased for 10 times its $2.0 million reported earnings. But the Seller's true earnings, according to the Buyer, were only $1.0 million as a result of the potential threatened intellectual property litigation. The Buyer might calculate its damages as $10.0 million (10 times the $1.0 million shortfall rather than $1.0 million under the dollar-for-dollar method). Alternatively, the Buyer might assert that for $2.0 million of somewhat impaired earnings it would pay a multiple lower than 10 times earnings.

If, at an appropriate point in the mediation, the parties seem to be going nowhere in their efforts to compromise, the mediator might encourage them to develop "a before and after" discounted cash flow approach that determines the difference between Seller's value with and without considering the disability, with some weighting concerning the likelihood or non-likelihood of complete impairment of Seller's cash flows from the intellectual property in question. Performing such an exercise involves use of the essential tools of discounted cash flow analysis, determining Seller's weighted average cost of debt and equity capital, Seller's "before and after" cash flows, the number of years over which the cash flows will be measured and the terminal (or residual) value of the cash flows in perpetuity following the last year of the discounting period. To be sure, such an approach could well involve the intervention of dueling experts with likely quite different value conclusions, but, at a minimum, it could create a bid-ask spread that a mediator could use as a range from which a settlement could ensue.

Conclusion

Post-merger litigation is an ongoing concern, the consequence of buyers who believe they got less than that which they had bargained for and sellers who assert that buyers remorse was not caused by their misconduct. Mediation can provide a means by which compromise by both sides can result in a handshake.

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Twelve Tips for Effective Settlement Negotiations

By Steven H. Reisberg

Here are 12 practical suggestions that can help you achieve a better negotiated settlement of a lawsuit or business dispute.

1. The Most Important Negotiations Occur Before You Meet With the Other Side

A plan based on the principle that we will show up and "negotiate the best deal we can" is not a recommended strategy. Prior to the start of any serious negotiations, you should take the time to meet with your team in order to determine the two objectives. First, what is your "best case" outcome? In other words, what is the most optimistic result that has a realistic chance of being achieved? Second, what is your "bottom line" position, meaning what is the minimum that must be obtained, otherwise you walk away from the negotiations? During the negotiations, be careful not to substitute one for the other.

2. Always Be Negotiating Toward a Specific Goal

Negotiations should not become a series of offers and counter-offers. At all times, you must be negotiating toward a specific concrete result. At trial, we make opening statements, put on evidence, and make legal arguments, all as part of a focused effort to persuade the judge or jury. It is not clear why we fail to follow this same approach of advocacy during negotiations. Effective advocacy and effective negotiations should not be mutually exclusive. You can achieve a better settlement the more you are able to persuade *the other side* of the merits of your position. This means that the process of negotiation should include time for discussion where you explain your position, support and justify it. Being able to present reasoned arguments supporting your position establishes that your request is legitimate. Negotiating toward a specific goal gives your negotiations structure, direction and focus. People who know what they want and why they ought to get it exhibit confidence, strength and commitment.

3. Pay Attention to the Information Being Broadcast by Non-Verbal Communication

A tremendous amount of information is always being exchanged be means of non-verbal communication. And this is a two-way street. You must be "listening" not only to the stated concerns of your negotiating partner but to the non-verbal information being broadcast by others and remain sensitive to the non-verbal information being transmitted from your side of the negotiating table. We know when parties are only half-heartedly asserting an argument, not only because of the words they choose but by the manor in which they are saying them. Confidence, strength and commitment (or the lack thereof) are constantly being communicated by posture, tone, eye contact, and physical behavior.

While you are presenting an argument or making a proposal, the other side is simultaneously giving you a great deal of information—before they say anything. The manner in which we physically react to a proposal while we are listening to it communicates important information in "real time." Please note that this applies to every member of the team in the room. The junior members of your team, while not saying anything, are nonetheless active participants in the conversation. The term "poker face" refers to a skill developed in response to the power of non-verbal communication.

4. Beware of the Moral Imperative to "Split the Difference"

In our culture, there is a strong belief that nothing could be fairer than meeting the other "half way." This statement is as powerful as it is wrong. A settlement is fair only to the extent that we can articulate reasons supporting the result. Otherwise, it is just an arbitrary number. Like the law of gravity, however, the influence of this cultural norm that assumes nothing could be fairer than to "split the difference" must be taken into consideration at all times.

At the beginning of a negotiation, for example, you should be very careful if the exchange of opening offers implies a number in the middle that is unacceptable to you. When faced with such a situation, a better response is to respond by asking questions. Don't make a counter-offer if the "number is the middle" is unacceptable. Instead, ask the offering party to explain the basis of the offer. In the course of this discussion, the initial offer can be exposed as an unjustifiable starting point. One result of responding by asking questions may be the emergence of new starting points.

This is not to say that splitting the difference can never be an effective and efficient strategy. However, use of this technique should limited to situations where it is the final step resulting in agreement on some open point.

5. Successful Negotiations Involve Asking Questions, Not Simply the Exchange of Offers and Counter-Offers

A negotiation is not a ping pong match. The primary interaction between the players should not be offers and counter-offers being swatted over a net. A negotiation is the exchange of information. The primary interaction between the two parties should be a process of asking and answering questions. It is only by asking questions that you can learn how the other party views the situa-

tion, what issues are of more (or less) importance to them, what obstacles exist from their point of view, and what they need in order to reach agreement and why. This is reciprocal. You will also be answering questions and providing both information and reasons in support of your positions. The sharing of information may also open up alternative means of reaching agreement. It is usually a mistake to develop a counter-offer by huddling alone in a conference room conferring only with you own side. Doing so without first asking questions means you are formulating an offer on the basis of incomplete information. The exchange of information is most effective if it can be done in person. However, mediators can also serve this role through "shuttle diplomacy."

One important goal of asking questions is to discover the obstacles which may be limiting the other side's ability to reach agreement, and of which you might be completely unaware. If not identified, these issues can silently interfere with a successful negotiation. Once identified, they become issues to be solved. Finally, by seeking to learn what obstacles stand in the way you will also likely come to a fuller understanding about what the other side stands to lose if there is no agreement.

6. The Best Negotiators Are Problem Solvers

The best negotiators recognize that a negotiated settlement can only be achieved if the issues to be addressed are clearly identified and solutions can be developed that are acceptable to both sides. Negotiators do not need to be overly adversarial in order to achieve outcomes that can legitimately be viewed as a success by both parties. Seeking to understand and help resolve the other side's problems is in your self-interest. It is certainly the case that you sometimes will be involved in negotiations where one side is as acting in a completely irrational, hostile, bullying and unreasonable manner. This, however, is not a valid excuse for a failed negotiation. When faced with such a situation, the more skilled negotiator must act as the problem solver for both sides in order to guide the parties to a successful result.

7. Explore Alternative Forms of "Currency"

Money is often the only valuable consideration that can be exchanged, but not always. Consider whether the other side has a need for something that you can provide that is not monetary. A simple illustration is where one side can provide services to the other, instead of cash. This form of "consideration" is particularly valuable because the value to the person receiving the service is much higher than the cost of providing it. Similarly, explore whether there is a third party that both sides have in common. This "neutral" party can be of assistance in appropriate cases.

8. Find and Identify Shared Goals

A set of common interests will exist in even the most contentious situations. One important type of conversation to have is where you seek to identify and articulate the advantages that a settlement will have for both parties. For example, both sides will save money if litigation expenses can be stopped or avoided. The very process of seeking to identify common goals also helps build a foundation of trust, which is key to lasting resolutions.

Remember also that negotiators are people too. You should explore common social or business connections. If you were negotiating a commercial transaction where a long-term relationship was expected, you would take time to learn about your future business partner, including his or her personal history. There is no reason why similar conversations should not take place during the negotiation of a settlement of a dispute. These types of conversations can also help break through initial barriers and build trust. The more we see each other as individuals seeking a solution to a common problem, the more effective the negotiations.

9. Take Advantage of Natural Negotiation "Windows"

Negotiations often work best when there is an upcoming event or deadline. In litigation, this may be after a decision on a motion to dismiss, after exchange of expert reports, or during the time period a dispositive motion in pending. Of course, many settlements occur "on the courthouse steps" when a case has finally been called for trial. There may also be business-generated deadlines, such as the upcoming end of a fiscal year, a proposed sale of the business or other major transactions. The upcoming event serves to place an external deadline on the process. Everyone works harder in the face of a deadline. These natural windows also make it easier for each side to agree to discussions without any implied admission of weakness.

10. Package Bargaining

Where there are a number of issues on the table, it may be best to start with a general discussion of all of the issues before the exchange of any settlement proposals. This allows for the development of a settlement package. In the subsequent negotiations, you can then make bigger moves on your less important issues. You can also "trade" concessions on different issues.

Be careful to avoid any bargaining style that seeks to reach final agreement in isolation on one issue one at a time. Some issues are more important to one party than the other. When multiple issues need to be resolved, the opening ground rule should be that no issue is closed until all issues have been decided. In this way, both parties retain a higher degree of flexibility when faced with future obstacles. If an impasse is reached later in the process, the parties have the ability to go back and explore different alternative settlement combinations.

11. Who Has the Most to Lose?

Take an inventory of what you and the other side realistically have to lose in the absence of a negotiated resolution. This can help determine your relative leverage in the negotiations. The more leverage you have the more you press the other party to agree to your terms. An objective of the process of exchanging information with the other side during settlement discussions is to try to identify the other party's bottom line. What is the minimum they need from a settlement. This also is where your "bottom line" comes in to play. It helps you identify what you have to lose by walking away. Being committed to your "walk away" position makes you a stronger and better negotiator.

12. Don't Leave the Room Until the Agreement Is Recorded in a Written Document

Do not forget the wisdom of the old saying that a verbal contract is not worth the paper it is written on. Particularly at the end of an in-person negotiation or settlements reached in the context of a mediation, the material terms of the settlement need to be written down and signed by the parties. Such settlement document should always recite that the parties intend such document to be a legally binding and enforceable contract. It many cases it may be that the parties further agree that they will enter into a more formal settlement agreement. While this raises the risk of litigation in the event that the parties fail to agree on the terms of the more formal agreement, this risk can be minimized if the written settlement agreement sets forth all the material terms and expressly recites that the parties intend such agreement to be legally binding and enforceable. In mediation, the parties can also provide that the mediator will have the authority to resolve any disputes that may arise in the context of negotiating the more formal settlement agreement.

Conclusion

All agree that the ability to succeed at trial is built on a foundation of careful preparation; the same is true for the ability to achieve a more favorable result through a negotiated settlement. Indeed, as shown above, many of the skills used at trial are readily transferable and applicable to the settlement conference room so long as the changed audience is recognized. But other skills are also needed. The twelve tips set forth above should assist each of the parties in achieving a more successful negotiated resolution of their dispute.

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Russia's Comprehensive Arbitration Reforms

By Peter Pettibone

On December 29, 2015 Russian President Vladimir Putin signed into law a Law on Arbitration and a Law on Amendments (collectively, the "Laws")[1] which have significantly reformed Russia's domestic and international commercial arbitration regimes. Many of these changes went into effect on September 1, 2016, and February 1, 2017, but some will come into effect later. The drafting of the reform legislation took over two years and was led by the Russian Ministry of Justice with significant input from, and participation by, lawyers in international law firms located in Russia.

The driving forces for the reforms are fourfold:

The first is to make Russia a more attractive place for the arbitration of Russian commercial disputes. In recent years many large Russian disputes, including those that involve only Russian parties, have migrated to international arbitration institutions, such as those in London, Stockholm and Zurich, for resolution. At present, fully one-third of the caseload in the London Court of International Arbitration (the "LCIA") involves Russian parties.[2] In this regard, the arbitration reforms are consistent with other legislative changes in Russia aimed at "de-offshoreization" of Russian economic interests and encouraging the return of capital to Russia.

The second is to make Russian arbitration more attractive for the resolution of domestic disputes and thereby reduce the heavy caseload in the Russian courts.

The third is to significantly restrict the activities of the so-called "pocket" arbitration courts, *i.e.,* those that have been established by corporations or banks to hear disputes between themselves and their contractors. Criticisms of these pocket courts have included concerns over their impartiality, but also that some of them have been used for fraudulent goals, such as enforcing non-existent debts for the purpose of creating bankruptcies.

The fourth is to remove the ambiguity over whether corporate disputes are arbitrable in Russia and provide the circumstances under which corporate disputes may be arbitrated in Russia.

Main Features of the Reforms

The new Law on Arbitration is based on the UNCITRAL Model Law on International Commercial Arbitration (the "Model Law").[3] It aims to enhance the role of arbitration in Russia by, among other things, expressly providing that all civil law disputes are arbitrable except where expressly provided otherwise.[4] This list of non-arbitrable disputes includes bankruptcy disputes, privatization disputes, disputes concerning public procurement,[5] class actions, employment and family matters, certain disputes on protecting intellectual property rights, environmental damage disputes and personal injury cases.[6]

The Laws provide that any doubts as to the validity of an arbitration clause shall be interpreted in favor of its validity and enforceability,[7] that such clauses shall be construed broadly and that the invalidity of the underlying contract shall not mean the invalidity of the arbitration clause.[8] The Laws reduce to one month the time within which an application for the recognition and/or enforcement of, or for the annulment of, a domestic or foreign arbitral award may be considered by the courts.[9] Also, if a losing party seeks to annul an award rendered in Russia and fails, the award becomes immediately enforceable within Russia, and there is no need to file a separate enforcement petition.

Institutional vs. Ad Hoc Arbitrations

The Laws grant new authority to the Russian courts to act as supervising authorities in Russian arbitrations as the appointing authority, considering challenges to arbitrators, removing arbitrators and reviewing interim jurisdictional awards.[10] However, the Laws make a significant distinction between the types of assistance that Russian courts can provide to institutional arbitrations as compared to ad hoc arbitrations. Tribunals in institutional arbitrations may obtain court assistance in obtaining physical evidence and documents (court assistance is not available for witness statements or depositions). They also permit parties to an institutional arbitration (but not parties to an ad hoc arbitration) to opt out of judicial supervision of their arbitration proceedings and to make their awards "final" and not subject to judicial review. This may be a very attractive feature to foreign parties who do not want Russian courts interfering in their arbitrations in Russia. Institutional tribunals may also grant interim

relief, although the enforcement of interim relief orders remains a gray area.

Domestic Arbitral Institutions

The Laws provide that all domestic arbitral institutions, other than the International Commercial Arbitration Court ("ICAC") and the Maritime Arbitration Court ("MAC"), both of which are part of the Russian Chamber of Commerce and Industry, must receive a permit from the Russian government to conduct their activities in Russia.[11] These permits will be issued on the recommendation of a new body, called the Council for the Improvement of Arbitration, which will be formed by the Ministry of Justice and will have members from the public and private sector. All domestic arbitral institutions must be non-profit and, if affiliated with a for-profit entity, they are prohibited from arbitrating disputes involving that entity or any of its personnel. Not surprisingly, many arbitration institutions that have been established by for-profit entities have objected to this requirement.

"Russia's recent arbitration reforms are far-reaching and, by following the Model Law in large part, should enhance the acceptability and use of arbitration in Russia for both domestic and international arbitrations."

For existing arbitral institutions, the deadline for obtaining a permit is November 1, 2017. The criteria for the issuance of a permit include the reputation of the institution, the proposed scope of its activities and the qualification of its arbitrators. A permit once issued may be revoked by the Council if the institution conducts activities that damage the institution's reputation. All domestic arbitral institutions, including the ICAC and MAC, are required to adopt new rules and submit their rules and lists of arbitrators to the Ministry of Justice.[12]

Foreign Arbitral Institutions

Awards of foreign arbitral institutions will be treated as institutional awards for purposes of the Laws if the foreign arbitral institution obtains a permit from the Ministry to conduct its activities in Russia. The only criterion for a foreign arbitral institution to receive a permit is that it must enjoy a "widely recognized international reputation."[13] It does not need to submit its rules or lists of arbitrators to the Ministry of Justice. However, if a foreign arbitral institution does not have a permit, its awards will be treated as ad hoc awards. This status will not prevent a foreign arbitral institution from administering Russian disputes apart from corporate disputes.

The Arbitrability of Corporate Disputes

A significant change in Russian arbitration is that corporate disputes may be arbitrated in Russia under agreements entered into after February 1, 2017.[14] Arbitrability of these disputes was called into doubt in the much-criticized decision of the Supreme Arbitrazh Court of Russia in the *Maximov* case,[15] and the new Laws clarify the conditions, which are based largely on similar provisions in German law, under which they may be arbitrated in Russia.

Corporate disputes may be divided into three categories: (1) a discrete list of non-arbitrable corporate disputes;[16] (2) corporate disputes that involve the rights of third parties or the company itself, *e.g.*, disputes under shareholder agreements and disputes challenging major and interested party transactions, provided that all parties to the dispute have concluded an arbitration agreement or otherwise consented to the arbitration—these are considered arbitrable if the seat of the arbitration is in Russia and the arbitral institution administers the arbitration under special rules for corporate disputes; and (3) corporate disputes that do not involve the interests of third parties, *e.g.*, disputes under asset or share purchase agreements—these are considered arbitrable if they are arbitrated in an institutional setting, but the seat does not need to be in Russia and the arbitral institution does not need to have adopted the special rules for corporate disputes.

"The reforms directly address two major defects in Russia arbitrations—(1) the questionable activities of "pocket" arbitration courts…and (2) the non-arbitrability of corporate disputes in Russia."

In the case of corporate disputes in the second category, a number of foreign arbitral institutions have indicated that they are not considering adopting the special rules for corporate disputes, as they object to a requirement in the rules that the shareholders must be informed of the dispute and may join the proceedings at any stage. The result is that corporate disputes in the second category are likely to be arbitrated only by Russian arbitral institutions.

Arbitration Clauses

The new Law provides that an arbitration agreement must be in writing, but the writing can be evidenced in a number of ways, including by an exchange of correspondence or electronically. The arbitration agreement may also be included in the charters of non-public companies with up to 1,000 shareholders provided the agreement is adopted at a general meeting by unanimous vote of all the shareholders.

There is a form of corporate abuse in Russia known as the "Russian torpedo" in which a shareholder brings a derivative claim in court to invalidate a contract following an arbitration award in favor of the counterparty to the contract. Given the new flexibility in creating arbitration agreements, it may be possible to minimize the efficacy of such tactics by using multiple arbitration clauses in charters and agreements.

Conclusion

Russia's recent arbitration reforms are far-reaching and, by following the Model Law in large part, should enhance the acceptability and use of arbitration in Russia for both domestic and international arbitrations. The reforms directly address two major defects found in Russia arbitrations—(1) the questionable activities of "pocket" arbitration courts, by requiring new standards of conduct by, and a permitting process for, domestic arbitral institutions, and (2) the non-arbitrability of corporate disputes in Russia, by creating a new framework under which many corporate disputes may be arbitrated in Russia. It remains to be seen, though, whether the Russian courts will be able to carry out their new responsibilities as supervising authorities in arbitrations in Russia in the absence of further guidance and whether they will support the reformed arbitration process in Russia as envisioned in the Laws.

Endnotes

1. Federal Law No. 382-FZ dated 29 December 2015, "On Arbitration in the Russian Federation," which applies to domestic arbitrations and also in part to Russia-seated international arbitrations (the "Law on Arbitration"). Also signed into law on 29 December 2015 was a related law, No. 409-FZ, amending existing Russian legislation to conform to the new Law on Arbitration (the "Law on Amendments").
2. Statement by Dr. Jacomijn van Haersolte-van Hof, Director General of the LCIA, at an LCIA Seminar in New York City on November 7, 2016.
3. The version of the Model Law used as a basis for the Laws is the 1985 version.
4. Article 33 of the Arbitrazh Procedure Code of Russia as amended by the Law on Amendments ("APC").
5. The Laws contemplate that disputes concerning public procurement may be arbitrable in the future under rules yet to be established.
6. Article 33 (2) of the APC.
7. Article 7 (9) of the Law on International Commercial Arbitration No. 5338-1 dated July 7, 1993, as amended by the Law on Amendments (the "ICA Law") and Article 7 (8) of the Law on Arbitration.
8. Article 7 (12) of the ICA Law and Article 7 (9) of the Law on Arbitration.
9. Article 243(1) of the APC.
10. Although the Laws provide that a party to an institutional or ad hoc arbitration can request a state court to appoint or terminate the appointment of an arbitrator, there are no provisions in the Laws or in the Russian procedural laws that would guide the courts in doing so.
11. Article 44 (1) of the Law on Arbitration.
12. Disputes that were administered as "international" but where the only "international" connection was the presence of foreign investment in one of the parties will now be referred to domestic arbitration.
13. Article 44 (12) of the Law on Arbitration.
14. Corporate disputes under arbitration agreements entered into prior to February 1, 2017 are expressly not enforceable. Article 13(7) of the Law on Amendments.
15. *Novolipetsk Metallurgical Company v. Maximov.* Ruling of the Arbitrazh (Commercial) Court of Moscow of June 28, 2011, in Matter No. A40-35844/2011-69-311, affirmed by the Federal Arbitrazh Court of the Moscow District and the Supreme Arbitrazh Court of Russia, which held a dispute arising out of a corporate transaction to be nonarbitrable. See also Pettibone, The Nonarbitrability of Corporate Disputes in Russia, Arbitration International, vol. 29, no. 2 (2013), 263.
16. Those relating to or arising out of the convening of general shareholders' meetings, the exclusion of shareholders, challenging resolutions and actions of state authorities with respect to the issuance of stock and those corporate disputes involving strategic legal entities (with some exceptions).

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The Importance of Legal Culture for Contract Construction: Norwegian Law, English Law and International Arbitration

By Giuditta Cordero-Moss

1. The Case

Imagine two parties who negotiate a long-term distribution contract for cogenerated heat. They agree that payment shall be made on a cost basis: none of the parties shall make a profit or a loss out of the contract. However, meters are not sufficiently precise and the parties do not know how to measure how much heat is distributed to whom. After intense and detailed negotiations, they decide the price shall be calculated on the basis of the surface that is being heated. Years later, meter technology improves. One of the parties installs a meter and sees that it is paying for more heat than it actually consumes. The party requests that the price calculation in the contract be adjusted to reflect actual consumption. The other party refuses to change a contract that it views as valid and binding. The price calculation mechanism in the contract was the result of long and detailed negotiations, and both parties were aware of the uncertainties connected with the mechanism when they agreed to it.

2. Different Solutions Under Different Laws

As is reasonable to expect, the outcome of the dispute may differ depending on which law governs. Section 3 of this article will show that, if the case is decided according to Norwegian law, the judge will modify the contract. Section 4 will show that, if the case is decided according to English law, the judge will probably deem the contract to be binding as drafted and agreed by the parties in the original version.

"…the arbitrators' legal culture might have a considerable impact on the outcome of the dispute."

Parties who engage in extensive international activity may wish to avoid these disparities among the various national laws. Therefore, they often choose arbitration to solve their disputes. There are many good reasons for choosing arbitration, of which the most important is that the award can be enforced in over 155 countries that ratified the New York Convention.[1] Also, parties often expect that, thanks to arbitration, they will avoid potential discrepancies in the outcome of international disputes. This is not necessarily a well-founded reason for preferring arbitration. As section 5 will show, the arbitrators' legal culture might have a considerable impact on the outcome of the dispute. Selecting the arbitrators, therefore, may be just as important as negotiating the price mechanism or choosing the governing law.

3. Norwegian Law: The Contract Is Adapted

The case described above was decided by the Norwegian Supreme Court in 1991.[2] The Court considered the parties' intention to avoid profits or losses, and that they agreed on the surface-based price mechanism for want of a more reliable measurement. Supervening developments and considerations of fairness made the court conclude that the surface-based mechanism contained in the contract should be replaced with a meter-based mechanism.

This decision is rather old, and the disputed contract was not a typical commercial contract. Would the court still be likely to interfere with the contract today, and also in disputes involving other kinds of commercial contracts? The answer is yes.

A 2016 Supreme Court decision[3] affirms the principle that commercial contracts shall be construed objectively. The dispute regarded the interpretation of a standard contract for the lease of industrial facilities. A provision stated that the lessee was liable for any damages that were "due to the lessee." The question was whether this provision applied in a situation where the premises were damaged in a fire that was caused in the course of the lessee's recycling activity. The court found that, although the wording seemed to indicate that the lessee would be liable for any damages caused in the course of its activity, the correct interpretation was that liability assumed that the lessee was in breach of contract. As the lessee had not violated any of the contract's provisions, the simple circumstance that the fire was caused in the course of the lessee's activity was not a sufficient basis for liability. The court explained at length that this result was based on an objective construction of the contract. The court explained the meaning of objective construction:[4] "It does not mean that one is supposed to follow a purely literal interpretation. A series of elements will be relevant for interpreting [construing] the contract […] The wording of the terms must be seen, *inter alia*, in light of their purpose, as well as of other considerations of fairness."

This approach had been followed by the Supreme Court in a decision of 2012, in which the court concluded that the buyer had lost its right to exercise contractual remedies against the seller's default.[5] Pursuant to the contract, the buyer had sent a notice of defect. Thereafter, the parties negotiated for some months trying to find a solution to the defect. After negotiations failed, the buyer requested reimbursement for damages resulting from the seller's breach of contract. The Supreme Court found that the original notice of defect was not sufficient (even though it complied with the contract requirements). In

addition to mentioning what the defect consisted of, the notice should have informed that the buyer intended to exercise contractual remedies. This latter specification was not required in the contract—a commercial contract entered into between two professional parties. The Supreme Court reasoned that this information is required by the duty of loyalty between contract parties, which is central in Norwegian contract law.

Thus Norwegian courts take an active role with respect to contract terms: they start with a review of the wording, but they construe the contract in light of its purpose, supervening circumstances, principles of loyalty and considerations of fairness. As a result, the Norwegian courts may ultimately change the terms of the contract. All this is understood as being "objective interpretation."

4. English Law: The Original Contract Is Binding

English courts also interpret contracts objectively. But their understanding of "objective interpretation" is quite different. In 2015, the Supreme Court of the United Kingdom rendered a decision that confirmed the principles of contract interpretation and construction at common law.[6] Quoting Lord Hoffmann in a prior case, it stated that a court shall identify the common intention of the parties "by reference to 'what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean'."[7] Among other things, it referred to recent suggestions in case law toward considerations of "commercial common sense" and toward considering "surrounding circumstances." The Supreme Court said that these "should not be invoked to undervalue the importance of the language of the provision which is to be construed."[8] Also, the court emphasized that supervening circumstances should not be taken into consideration: "The mere fact that a contractual arrangement, if interpreted according to its natural language, has worked out badly, or even disastrously for one of the parties is not a reason for departing from the natural language."[9]

"Both the Norwegian and the English court say that they interpret contracts objectively. Yet the Norwegian court adapted the contract to the new circumstances, the English court confirmed the original wording."

The dispute concerned the interpretation of contract provisions for a yearly service charge contribution of £90 in the leases of a number of chalets in a caravan park in South Wales.[10] As in the Norwegian case, a not purely commercial contract between professional parties. The contract was signed in the 1970s, a time of very high inflation. The contract contained a rather clumsy provision intended to index the service charges payable yearly by the lessees. Instead of writing a typical indexing clause linked to the inflation rate, the contract provided for a yearly increase of the service charges by 10%. In the 70s, this may have reflected the rate of inflation. At the time of the dispute interest rates were very low, and the yearly increase had a dramatically disproportionate effect. As the court put it: "If one assumes a lease granted in 1980, the service charge would be over £2,500 this year, 2015, and over £550,000 by 2072. This appears to be an alarming outcome for the lessees [...]." Yet the Supreme Court confirmed the contract wording. The majority (one Lord dissented) concluded: "It would be very satisfactory to read the wording differently, but there is no basis for that."[11]

For an English court, objective interpretation means focusing on the wording of the terms and on what they would mean to a reasonable person having the same knowledge as the parties did at the moment of entering into the contract. Supervening circumstances are irrelevant, and so are considerations of loyalty and fairness.

5. International Arbitration and the Importance of Legal Culture

The parallels between the Norwegian and the English cases are striking, as are the differences. In both cases, a non-typical commercial contract was written with a certain purpose (provide for payment on a cost basis, protect the service charges against inflation); in both cases, the agreed contract wording worked out badly for one of the parties—in the English case, dramatically so. Both the Norwegian and the English court say that they interpret contracts objectively. Yet the Norwegian court adapted the contract to the new circumstances, the English court confirmed the original wording.

That different courts have different approaches may create uncertainty for parties with extensive international activity. Therefore, parties often choose to submit their international disputes to arbitration. Coupling arbitration with very detailed and standardized contracts, they hope to obtain standardized outcomes. However, the mere fact that the operative terms of the two contracts are written in the same way is no guarantee of a similar outcome of the dispute—even assuming essentially the same facts as the contract performance unfolds. The contract will be construed in accordance with the governing law.

Parties may be tempted to choose always the same law to govern their contract; English law or Swiss law are often chosen to govern international contracts even with no connection with England or Switzerland. Even this, however, is not a guarantee of a standardized outcome.[12] As discussed above, different legal systems have diametrically different approaches to how a contract is to be interpreted—yet both approaches constitute, in the eyes

of the respective lawyers, "objective interpretation." An arbitrator trained in a given legal tradition, will need a thorough exposure to foreign legal systems before she understands that her way of construing contracts is not the only possible way. And it will take extensive international experience before she accepts that her way is not the only fair way. That arbitrators are subject to unconscious influences has been proven particularly in connection with evaluation of evidence.[13] It seems quite realistic that they should be subject to unconscious influences also when construing a contract.[14] A Norwegian arbitrator having to construe a contract according to English law, therefore, may be construing the contract according to the Norwegian approach—and yet be convinced that he or she is making an objective interpretation as English law requires.

The same may be said for the (rare) situations in which the arbitral tribunal applies harmonised, transnational sources such as the UNIDROIT Principles of International Commercial Contracts.[15] It should be expected that these sources will be applied uniformly in an international setting. However, these sources are heavily based on legal standards, such as the principle of good faith. When specifying the content of good faith, the arbitrator runs the risk of being unconsciously influenced by his or her own legal tradition.[16]

6. Conclusion

A party selling its products in many different countries needs to predict the scope of its rights and obligations and will try to standardise its contracts. Contracts will therefore become extensive and detailed. But this will not be sufficient to exclude the influence of the governing law. That party will therefore provide a governing law clause that chooses always the same law in its contracts, and it will submit disputes arising under the contract to arbitration. However, these steps are not sufficient to guarantee that the contracts will be interpreted in the same way: one must also consider the selection of arbitrators to avoid the unconscious influences of their own legal traditions.

Parties are aware of the need to select arbitrators with care. However, usually they are principally concerned with ensuring that the arbitrators have practical experience within a certain industry sector, that the arbitrators understand the commercial aspects of the dispute and are likely to appreciate their party's position, and that they effectively manage the proceeding. This article argues that it is advisable to also take into consideration how the arbitrators will apply the law: are they prone to a literal or to a purposive interpretation of the contract? Do they apply the contract precisely as written or do they see room for implying terms? These and many other aspects will be influenced by the legal tradition to which the arbitrator belongs. So the question that now must be asked is whether an additional criterion should be the appointment of someone whose legal cultural background is consonant with the governing law chosen.

Endnotes

1. 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.
2. Rt. 1991 s. 220 (Sollia Borettslag).
3. HR-2016-1447-A (Norsk Gjenvinning).
4. *Id.*, at para 38.
5. Rt. 2012 s. 1779 (Victocor).
6. Arnold v. Britton, [2015] UKSC 36.
7. *Id.*, at para 15.
8. *Id.*, at para 17.
9. *Id.*, at para 19.
10. The dispute regarded a series of contracts entered into at different times between different parties. As these aspects are not relevant here, for the sake of clarity I have simplified the facts.
11. Fn. 6 *supra,* at para 62.
12. Another reason why choosing the same law is not always a guarantee of same outcome is that the choice of law made by the parties does not cover the whole legal relationship, but only the contract law aspects: *see* G. Cordero-Moss, International commercial contracts, Cambridge University Press, 2014, chapter 4.
13. E. Sussman, *Arbitrator Decision-Making: Unconscious Psychological Influences and What You Can Do About Them*, in The American Review of International Arbitration (2013) Vol 24 No 3, pp. 487-514.
14. G. Cordero-Moss, *Non-national Sources in International Arbitration and the Hidden Influence by National Traditions*, forthcoming in Scandinavian Studies of Law, vol. 63.
15. The third edition (2010) may be found at: http://www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf In 2016, a fourth edition was adopted, expected to be made available soon.
16. On the use of the UNIDROIT Principles *see* G. Cordero-Moss, International Commercial Contracts, Cambridge University Press, 2014, chapter 2.

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Hong Kong's Third Party Funding of Arbitration Law Reform and "Light Touch" Regulation

By Kim M. Rooney

Introduction

Third party funding of international arbitration has become increasingly common, including in Australia, England and Wales and the United States.[1] A party to an arbitration may need third party funding to conduct the proceedings, or may wish to obtain it for cash flow and risk management purposes.

Among the major international arbitration jurisdictions in Asia, only Hong Kong[2] and Singapore had not allowed third party funding for arbitration because of the continuing application of the ancient common law doctrines of maintenance[3] and champerty.[4]

"It is important that Hong Kong...keep up with the latest international development and thereby enhance its competitive position."

However, in 2017 both Hong Kong and Singapore are reforming their law to allow third party funding for arbitration. Thus on 11 January 2017 Singapore passed *the Civil Law (Amendment) Bill 38/2016* allowing third party funding of international arbitration and related proceedings. Regulations by Singapore's Minister of Law have followed to provide for the scope of the permitted arrangements and accompanying regulatory changes.[5]

In Hong Kong on 11 January 2017 the Hong Kong Secretary for Justice, the Hon. Mr. Rimsky Yuen SC (the "Hong Kong SJ") moved the second reading of the *Arbitration and Mediation Legislation (Third Party Funding) (Amendment)* Bill 2016 (the "*Hong Kong Bill*") in Hong Kong's Legislative Council ("HK Legco").[6] In the Hong Kong SJ's second reading speech he said that the proposed amendments to Hong Kong's *Arbitration Ordinance* (Cap 609) (and the *Mediation Ordinance* (Cap 620)) were intended to clarify that third party funding of arbitration, mediation and related litigation proceedings is permitted under Hong Kong law. He explained that the

> [Hong Kong] Government considers that, from the perspective of promoting Hong Kong as an international dispute resolution centre and for the purpose of clarifying the law, the proposed law reform is desirable. It is important that Hong Kong, as one of the leading centres for international legal and dispute resolution services in the Asia Pacific region, can keep up with the latest international development and thereby enhance its competitive position.

The Hong Kong SJ observed that the amendments to the *Arbitration Ordinance* were formulated on the basis of the recommendations made in the *Report on Third Party Funding for Arbitration*, published by the Law Reform Commission of Hong Kong (the "HKLRC") on 12 October 2016 (the "HKLRC's Final Report"). The HKLRC's Final Report includes in Appendix 1 a set of draft proposed amendments to the Arbitration Ordinance to implement the HKLRC's final recommendations for reform of the relevant law.

The Hong Kong SJ also referred to the draft *Third Party Funding of Arbitration Code of Practice* (the "*Draft Hong Kong Code*") which was submitted to Hong Kong Legco on 30 November 2016.[7] As discussed later in this article the *Draft Hong Kong Code* sets out the ethical and financial standards with which third party funders of arbitration should comply. This is to be the subject of a consultation process.

Hong Kong has a unitary arbitration regime, with its *Arbitration Ordinance* based on the *UNCITRAL Model Law on International Commercial Arbitration* (2006). The *Arbitration Ordinance* applies to "*domestic*" arbitration as well as to "*foreign*" arbitration. Hong Kong is adopting a unique approach to regulation of third party funding, drawing on the experience and practices of other international arbitration centres (including Australia and England and Wales) while reflecting Hong Kong's specific needs, culture and approach to regulation. Among other things, Hong Kong's regulatory approach continues the process of consultation with stakeholders that was commenced by the HKLRC's third party funding reference to the HKLRC's Third Party Funding Subcommittee (the "HKLRC's Subcommittee") to review and make recommendations as to Hong Kong law in June 2013.

This article briefly discusses the background to the proposed reform of Hong Kong law to clearly permit third party funding of arbitration and related proceedings. It also outlines the "*light touch*" approach to the Hong Kong regulation of third party funding of arbitration, included by the Draft Hong Kong Code and by the proposed monitoring and review process by an Advisory Committee after the reforms come into effect.

What Is Third Party Funding of Arbitration?

There are almost as many views as to what constitutes third party funding of arbitation as there are commentators. The HKLRC's Final Report observed that:

> The forms of financial assistance offered by Third Party Funders and the structuring of these are becoming increasingly varied and sophisticated. For the present purpose, it is not necessary and we will not address each and every issue that can arise from the increasing number of ways in which Third Party Funders are providing financial assistance to parties to an arbitration (and related proceedings) or to their lawyers. We have adopted the approach that the recommendations as to any reforms should be focused on the consequences of expressly providing that the doctrines of maintenance and champerty (both as a tort and as a criminal offence) do not apply to Arbitration (and related proceedings) under the Arbitration Ordinance.[8]

This article adopts the definition of "third party funding" in section 98G(1) of the Hong Kong Bill 2016 which is as follows:

> Third party funding of arbitration is the provision of arbitration funding for an arbitration—
>
> (a) under a funding agreement;[9]
>
> (b) to a funded party;
>
> (c) by a third party funder; and
>
> in return for the third party funder receiving a financial benefit only if the arbitration is successful within the meaning of the funding agreement.

However, section 98G(2) of the Hong Kong Bill provides that third party funding of arbitration does not include the provision of arbitration funding directly or indirectly by a person practising law, or providing legal services, whether in Hong Kong or elsewhere.

The Law Reform Commission's Third Party Funding for Arbitration Subcommittee 2013-2016

In June 2013 the Hong Kong SJ and the Hong Kong Chief Justice requested the LRC to establish a subcommittee to review the current position relating to third party funding of the arbitration in Hong Kong for the purpose of considering whether reform is needed.[10]

In October 2015, the HKLRC Subcommittee published a consultation paper (the "2015 Consultation Paper").[11] This:

- outlined the current relevant law in Hong Kong;
- reviewed the key elements of third party funding in the context of the elements of maintenance and champerty;
- reviewed the applicable law in 12 major international arbitration jurisdictions including the U.S., England & Wales, Australia, and various European and Asian jurisdictions, as well as under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the "Washington Convention");[12]
- reviewed the pros and cons of third party funding.

The HKLRC Subcommittee referred to the Hong Kong Court of Final Appeal judgment in *Unruh v. Seeberger* (2007) 10 HKCFAR 31 where the Court expressly left open the question of whether the doctrines of mainteance and champerty apply to arbitration taking place in Hong Kong (although clearly stating that Hong Kong law does not prohibit Hong Kong parties agreeing to third party funding of arbitrations taking place outside Hong Kong).[13] The HKLRC Subcommittee proposed that third party funding for arbitration should be permitted under Hong Kong law provided it was subject to appropriate financial and ethical safeguards. The public was invited to comment on the HKRLC Subcommittee's proposal.

"...the common law doctrines of maintenance and champerty do not apply to third party funding of arbitration..."

Seventy three public submissions were received in response to the 2015 Consultation Paper from companies, organizations and individuals including accounting firms, arbitral institutions, arbitrators, barristers, chambers of commerce, consumer and public interest groups, the financial sector, government bureaus and departments, third party funders, insurers and insurers' associations, and law firms. The public's responses overwhelmingly supported the Subcommittee's proposals.[14]

The HKLRC's Final Report of 12 October 2016

The HKLRC's Final Report published in October 2016 recommended, having taken into account the 73 public submissions received during the consultation period, that reform of Hong Kong Law to allow third party funding of arbitration and related proceedings would be in the interests of the arbitration users and the Hong Kong public and consistent with the relevant principles that the Hong Kong Court of Final Appeal has formulated.[15]

Scope of Reforms

The HKLRC recommended that the Arbitration Ordinance be amended to provide that following amendment the common law doctrines of maintenance and champerty do not apply to third party funding of arbitration and associated proceedings under the Arbitration Ordinance (namely emergency arbitrator proceedings, mediation and court proceedings). The HKLRC recommended that the proposed amendments of the law should also apply to the funding of services provided in Hong Kong for arbitrations seated outside Hong Kong.

"...compliance with the ethical and financial safeguards set out [for] monitoring, supervision and review... that they proposed, will protect against potential abuse."

The HKLRC recommended that third party funding provided either directly or indirectly by a person practising law or providing legal services should not be permitted to avoid lawyers' conflicts of interest in serving their clients.[16] This means that lawyers or entities/persons providing legal services will not be covered by the amendments and the doctrines of maintenance, champerty and barratry will still apply to them.

Safeguards

The HKLRC observed that compliance with the ethical and financial safeguards set out in the HKLRC Final Report by a third party funder with the monitoring, supervision and review framework that they proposed will protect against potential abuse.[17]

Mandatory Disclosure

The HKLRC recommended that if a funding agreement is made, the funded party must give written notice of the fact that a funding agreement has been made and the identity of the third party funder, on or before the commencement of the Arbitration, on the commencement of the Arbitration; or, for a Funding Agreement made after the commencement of the Arbitration, within 15 days after the Funding Agreement is made to each other party to the Arbitration and to the Arbitration Tribunal (when established). There should also be disclosure about the termination of third party funding.[18]

Adverse Costs Orders

The HKLRC said that while it considered that, in principle, a Tribunal should be given the power under the Arbitration Ordinance to order costs against a third party funder, in appropriate circumstances, after according it due process, it was premature at this stage to amend the *Arbitration Ordinance* to provide for this power. The *Arbitration Ordinance* applies only to parties to an arbitration agreement (as set out in its section 5(1)). The HKLRC considered that further careful consideration of this issue is warranted, bearing in mind the need to preserve the integrity of Hong Kong's regime for arbitration, to provide due process to a third party, including a third party funder, where an application for an adverse costs order against it has been made, and to provide for equal treatment, fairness and efficiency for all involved. The HKLRC recommended that further consideration should be given in the initial three-year period following implementation of the proposed amendments providing for the power of a Tribunal to award costs against a third party,[19] including a third party funder, in appropriate circumstances. The HKLRC set out a list of matters they recommended should be considered.[20]

Security for Costs

The HKLRC stated that it considered that there is no need to give a Tribunal the power to order security for costs against a third party funder, as the powers of a Tribunal under the *Arbitration Ordinance* to order a party to give security for costs afford adequate protection.[21]

Light Touch Approach to Regulation with Code and Monitoring/Review

The HKLRC proposed the adoption of a "*light touch*" regulatory approach for an initial period of three years, at the centre of which is a Code of Practice setting out the applicable standards with which third party funders should comply. This will be issued by a body authorised under the *Arbitration Ordinance* after public consultation.[22]

The HKLRC recommended that the Advisory Committee on the Promotion of Arbitration[23] should be nominated by the Secretary for Justice to be the Advisory Body under the *Arbitration Ordinance* to monitor the conduct of third party funding for arbitration and the implementation of the Code, and to liaise with stakeholders. The Advisory Body should issue a report reviewing the Code's operation three years after it has come into effect, and make recommendations as to the updating of the ethical and financial standards contained in it.

Hong Kong Legislative Process

On 28 November 2016 the Secretary for Justice and the Chair of the HKLRC Subcommittee briefed the AJLS Panel on the proposed reform and the views of the stakeholders.[24] The Panel expressed support for the introduction of the Bill into the Legislative Council.

The Hong Kong Bill, based on the HKLRC's draft, contains provisions implementing the recommendations of the HKLRC Final Report including to provide:

- that third party funding of arbitration is not prohibited by the common law doctrines of maintenance and champerty[25] (and stating that lawyers and providers of third party funding may not be third party funders);[26]
- for confidentiality;[27]
- for mandatory disclosure;[28]
- for the consequences of non-compliance with the law[29] which are potentially civil, not criminal;
- for financial and ethical safeguards[30] by the Code;[31]
- for an Advisory Body to monitor and review the operation of the amended law.[32]

The Hong Kong Bill includes an additional provision to expand the scope of the amendments to permit third party funding of Hong Kong work on arbitrations that do not have a municipal seat.[33]

The Draft Code

The Draft Code's standards mirrors the provisions for these in the the Hong Kong Bill. Among other things the Draft Code states that it applies to all third party funders.[34] Its purpose, as expressed, is to set out the practices and standards that third party funders are ordinarily expected to adopt when funding arbitrations.[35] It applies to the pre-contractual negotiations, and the making and performance of any funding agreement between a third party funder and a funded party (including a potential funded party) for third party funding of arbitration commenced or entered into on or after date of commencement of the Code.

Implementing the approach of the Hong Kong Bill, the Draft Code addresses the standards and practices with which third party funders of arbitration should comply[36] including such matters as the third party funder's responsibility for Subsidiaries and Associated Entities,[37] promotional materials,[38] and the terms of the the funding agreement, including the obligation of a funder to provide a Hong Kong address for service in the funding agreement and the need for the funding agreement to set out and explain clearly in the funding agreement the key features, risks and terms of the proposed funding and the funding agreement[39] including to reflect the matters addressed in the Hong Kong Bill as to the:

- third party funder's capital adequacy requirements;[40]
- conflicts of interest;[41]
- degree of control by the third party funder;[42]
- whether the third party funder is liable for adverse costs orders;[43]
- termination;[44]
- complaints procedure;[45]
- the third party funder's submission of annual returns to the Advisory Body reporting on any complaints against it by funded parties received during the reporting period and any findings by a court or arbitral tribunal of its failure to comply with the Code or the law during the reporting period;[46] and
- the third party funder's obligation to respond to any request from the Advisory Body for further information or clarification concerning any matter.[47]

Conclusion

It is hoped that the Hong Kong Bill will become law, and that the Draft Code will come into operation, by mid-2017. Reform of Hong Kong law to clearly allow third party funding of arbitration and related proceedings, with appropriate measures and safeguards in place, should serve the interest of arbitration users, support Hong Kong's role as a leading international arbitration and dispute resolution centre, and enhance Hong Kong's competitive position.

Endnotes

1. Consultation Paper—chapter 4 at pages 51 to 109 http://www.hkreform.gov.hk/en/docs/tpf_e.pdf Accessed 11 January 2017.
2. In *Unruh v. Seeberger* (2007) 10 HKCFAR 31 the Hong Kong Court of Final Appeal, confirmed that the principles of mainteance and champerty continue to apply in Hong Kong and to prohibit third party funding of litigation, both as a tort and as a criminal offence, save in three exceptional areas:
   (i) where a third party has a legitimate interest in the outcome of the litigation;
   (ii) where a party should be permitted to obtain third party funding, so as to enable him/her to have access to justice; and
   (iii) in miscellaneous recognised category of proceedings including insolvency proceedings. The Court of Final Appeal expressly left open the question of whether these doctrines apply to arbitration (paragraph [123]).
3. ***Maintenance*** has been defined as: "*the giving of assistance or encouragement to one of the parties to an action by a person who has neither an interest in the action nor any other motive recognised by the law as justifying his interference*." *Winnie Lo v. HKSAR* (2012) 15 HKCFAR16 at para 10.
4. ***Champerty*** has been defined as: "a particular kind of maintenance, namely maintenance of an action in consideration of a promise to give to the maintainer a share of the subject matter or proceeds thereof, if the action succeeds," *Winnie Lo v. HKSAR* (2012) 15 HKCFAR16 at para 10.
5. Singapore has promulgated the following regulations effective 1 March 2017 (1) Civil Law (Third Party Funding) Regulations 2017 and (2) Legal Profession (Professional Conduct) Amendment Rules 2017: http://statutes.agc.gov.sg/aol/home.w3p."
6. http://www.info.gov.hk/gia/general/201701/11/P2017011100487.htm. Accessed 11 January 2017. The Hong Kong Executive Council ordered that it be introduced into the Hong Kong Legco on 20 December 2016: see the Legislative Council Brief by the Hong Kong Department of Justice dated 28 December 2016: http://www.legco.gov.hk/yr16-17/english/bills/brief/b201612301_brf.pdf (accessed on 8 February 2017).
7. On 30 December 2016 the Department of Justice submitted a Brief to the Hong Kong Legislative Council which annexed (a) Annex

A-Bill and Explanatory Memorandum, (b) Annex B-Responses of the Hong Kong Government to the recommendations made by the LRC in the 2016 Final Report and (c) Annex C-Draft Code.

8. Para 1.3 at 7 of the HKLRC's Final Report.
9. Section 98H of the Hong Kong Bill defines a "funding agreement" as being "an agreement for third party funding of arbitration that is (a) in writing; (b) made between a funded party and a third party funder; and (c) made on or after the commencement date of Division 3."
10. The HKLRC's Subcommittee's members were Kim M Rooney (Chair), Theresa Cheng SC, Victor Dawes SC, Justin D'Agostino, Jason Karas and Robert Pang SC.
11. http://www.hkreform.gov.hk/en/docs/tpf_e.pdf Accessed 11 January 2017.
12. Convention on the Settlement of Investment Disputes between States and Nationals of Other States 1965.
13. Para 1.23 of the 2015 Consultation Paper.
14. Please see paragraphs 2.2 at pp. 13–14 of the HKLRC's Final Report, and in the more detailed discussion of the public response that follows.
15. Para 2.1 and 2.6 of the HKLRC's Final Report.
16. The HKLRC recommended that professional conduct rules applicable to barristers, solicitors, and foreign registered lawyers should be amended to expressly state the terms and conditions upon which such lawyers may represent parties in arbitrations and related court proceedings funded by third party funders. Para 2.8(6) of the HKLRC's Final Report.
17. Para 2.9 of the HKLRC's Final Report.
18. Para 2.8 at 8 of the HKLRC's Final Report.
19. The HKLRC noted that this topic is the subject of review internationally, for example, by the Queen Mary International Council for Commercial Arbitration (ICCA) Taskforce on Third Party Funding in International Arbitration and the International Bar Association (IBA). The body considering this issue in Hong Kong will have the benefit of being able to consider its final reports on this topic.
20. Para 2.11 at 23-24 of the HKLRC's Final Report.
21. Para 2.12 at 24 of the HKLRC's Final Report.
22. Para 2.10 of the HKLRC's Final Report.
23. http://www.doj.gov.hk/eng/public/pdf/2016/terms.pdf accessed 8 February 2017.
24. On 22 November 2016, the Department of Justice submitted to the Panel on Administration of Justice and Legal Services of the Hong Kong Legislative Council (the "AJLS Panel") a paper setting out the approach to implementation and response to the Recommendations in the Final Report and attaching a draft Code of Practice for Arbitration, http://www.legco.gov.hk/yr16-17/english/panels/ajls/agenda/ajls20161128.htm.
25. Sections 987 K and L of the Draft Bill.
26. Section 98G(2) of the Draft Bill.
27. Section 98S of the Draft Bill.
28. Section 98T of the Draft Bill.
29. Sections 98R and V of the Draft Bill.
30. Section 98O(1) of the Draft Bill.
31. Section 98O of the Draft Bill.
32. Section 98W(1) of the Draft Bill.
33. Section 98N(1) of the Draft Bill.
34. "Application," at page 1 of the Draft Code.
35. "Purpose," at page 1 of the Draft Code.
36. Section 2 of the Draft Code.
37. Para 2.1 of the Draft Code.
38. Para 2.2 of the Draft Code.
39. Para 2.3 of the Draft Code.
40. Paras 2.5-2.6 of the Draft Code.
41. Paras 2.7-2.8 of the Draft Code.
42. Para 2.11 of the Draft Code.
43. Para 2.14 of the Draft Code.
44. Para 2.15-2.18 of the Draft Code.
45. Para 2.21 of the Draft Code.
46. Para 2.22 (1) of the Draft Code.
47. Para 2.22 (2) of the Draft Code.

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The Hague Convention on Choice of Court Agreements: A Realistic Competitor to the New York Convention?

By Glenn P. Hendrix* and Louise Ellen Teitz*

The Hague Convention on Choice of Court Agreements ("the Convention" or "COCA") is aimed at ensuring the enforceability of exclusive forum selection clauses (choice of court agreements) in contracts between parties to international commercial transactions, as well as judgments resulting from such agreements.

"The Convention was designed as the litigation counterpart to the...New York Convention."

Although completed in 2005, the Convention did not enter into force until October 1, 2015, and then only between Mexico and 27 member countries of the European Union (excluding Denmark). Singapore has since ratified the Convention as well.

"Whether COCA will satisfy that promise will depend in part on whether it achieves the same broad acceptance as the New York Convention, which now has 157 parties."

The Convention was designed as the litigation counterpart to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention").[1] Whether COCA will satisfy that promise will depend in part on whether it achieves the same broad acceptance as the New York Convention, which now has 157 parties.

This article will provide a brief overview of COCA and its benefits as compared to the New York Convention, as well as possible implementation in the U.S.

I. The Hague Convention on Choice of Court Agreements

The United States, which is not a party to any bilateral or multilateral convention on the enforcement of foreign judgments, was a prime mover in the negotiations that resulted in COCA. American courts are among the world's most receptive to enforcing foreign judgments, but other countries are not necessarily as generous in enforcing U.S. judgments. COCA serves to "level the playing field" for U.S. businesses, especially for "middle class litigants"[2] that may lack the sophistication or resources to engage in international arbitration.

Similar to the New York Convention, COCA addresses both (1) jurisdiction over the merits of the dispute (the "dispute stage") and (2) recognition and enforcement of judgments (the "recognition stage"). Generally speaking:

- Chapter II of the Convention covers the dispute stage, providing for the enforcement of certain exclusive choice of court (forum selection) clauses, obligating the chosen court to exercise jurisdiction and hear the matter when a dispute arises, and requiring non-chosen courts to refrain from hearing the dispute (Articles 5, 6);
- Chapter III covers the recognition stage, requiring recognition and enforcement of any resulting judgment rendered by the chosen court (Articles 8, 9).[3]

Article 5 provides that the chosen court shall decide a dispute, "unless the agreement is null and void" under its "law," including its choice of law rules. This denies the chosen court the right to dismiss on *forum non conveniens* grounds, except that Article 19 of the Convention allows state parties to declare that they will not honor choice of court agreements where "there is no connection between that State and the parties or the dispute." Article 6 defines the obligations of the non-chosen forum to respect the parties' choice of forum unless one of the exceptions listed applies: the agreement is null and void under the law of the chosen court; capacity is lacking; or the agreement would lead to "manifest injustice" or be "manifestly contrary to the public policy" of the court seised with the matter. The Convention, in defining "exclusive choice of court agreements," establishes a presumption of exclusivity unless the parties expressly state otherwise.[4]

Article 8 provides for the recognition and enforcement of a judgment by the chosen court, with Article 9 providing exceptions similar to Article 6. Recognition and enforcement of a judgment that results from an exclusive choice of court clause designating a member state may be refused only under narrowly defined circumstances: the agreement is null and void according to the chosen court's whole law, the party lacked capacity under the law of the requested state; the defendant did not have sufficient notice; the judgment was obtained by fraud, or the recognition would be "manifestly incompatible" with public policy.

The Convention is confined only to civil and commercial matters, excluding disputes relating to consumer and employment contracts, most family law matters, insolvency matters, personal injury claims brought by natural persons, and some insurance contracts.

The benefits of the Convention are not limited to parties from contracting states. Thus, a U.S. party could contract to resolve a dispute in a forum in a COCA member state—say, Singapore or London[5]—and any resulting judgments would be enforceable in the courts of all COCA member states.

II. Can COCA Compete with the New York Convention?

If the United States were to ratify COCA, and a critical mass of its trading partners also joined, one of the major advantages of international arbitration over litigation—enforceability—would be reduced, if not effectively neutralized, at least with respect to dispute resolution clauses covered by the Convention.

Would businesses engaged in cross-border commerce then turn their backs on international arbitration in favor of choice of court agreements? Some commentators have opined that this is unlikely to happen because arbitration has several crucial advantages over litigation, including neutrality, finality and flexibility. These advantages are real, but should not be overstated:

Neutrality. The ability of the parties to choose neutral decision-makers and the avoidance of home-cooking in foreign courts are key advantages of international arbitration over litigation. COCA will not eliminate that advantage, but it does offer the possibility of reducing it. As previously mentioned, Article 19 of COCA allows contracting states the option to declare that they will not accept jurisdiction over unconnected cases. Singapore chose not to make such a declaration, and its International Commercial Court (the SICC) is actively seeking to attract cases having no connection with Singapore. While parties will not have a say in picking their judges, as they typically do with an arbitrator, they do have the opportunity to pick a neutral forum. As additional states join the Convention, additional options will become available. These would likely include New York (should the U.S. ratify the Convention), which already accepts jurisdiction over certain unconnected cases.[6]

Finality. For many parties, one of the attractions of arbitration is finality and the concomitant promise of a cost-efficient and timely resolution of the dispute. As any losing party convinced that the arbitrator(s) got it wrong will attest, however, this can be a mixed blessing. Some parties prefer having a second chance at a favorable outcome.

Consolidation and Joinder. Although the major arbitral institutions have amended their rules to facilitate multi-party arbitrations, arbitral tribunals do not have the same coercive power as courts to join third parties.

Confidentiality. While confidentiality has long been a selling point of arbitration, some parties, including, in particular, sovereigns and state commercial enterprises, prefer the transparency of open court hearings and public judgments.

Procedure. While a flexible, "one-size-fits-one" concept of arbitral procedure offers certain advantages over "one-size-fits-all" court procedure—especially in proceedings between parties from different legal traditions—some parties will prefer the predictability of established rules of civil procedure. Indeed, the recent spate of "due process" challenges to arbitral awards—described as the "routine, often incessant and shrill, invocation of multiple procedural complaints under the banner of due process" as a "brazen strategy" to seek to pressurize arbitral tribunals[7]—is perhaps one downside to a lack of hard and fast "rules of the game" that are relatively well understood by all parties going into the process. And in some jurisdictions, litigation might offer the edge of potentially disposing of cases early through motions practice.

Time and Cost. The so-called "judicialization" of international arbitration has shaken the old conventional wisdom that international arbitration is more economical and efficient than litigation. While arbitration certainly still holds that promise—especially where the parties avail themselves of the flexibility inherent in arbitration to fashion a more streamlined process[8]—litigation may be the faster and cheaper dispute resolution option for some cases in some jurisdictions.

One could go on with a lengthy discussion of such factors as the presence of an ethics regime governing the conduct of lawyers, the availability of coercive interim remedies, the utility (and cost) of discovery, the relative ease of enforcing judgments and arbitral awards, and the desire (or not) to establish or evolve a body of jurisprudence, among other considerations. Which is "better"—litigation or arbitration—will depend on the party and the circumstances. Practitioners who indicate that they "always" prefer arbitration to litigation or litigation to arbitration do their clients a disservice.

III. Ratification in the United States?

The U.S. signed COCA in January 2009, on President George W. Bush's final day in office, but signature is only the first step to ratification, and in the U.S. the road between the two is often bumpy and slow. While the Convention seems to enjoy universal support in this country, its transmittal to the Senate for advice and consent to ratification has been held up by a dispute over whether it

should be implemented by federal law or by a combination of federal and state law (often referred to as "cooperative federalism"). Some advocate federalizing both the dispute stage and the recognition stage, with Congress enacting implementing legislation analogous to Chapter 2 of the Federal Arbitration Act (FAA), which implements the New York Convention in the U.S., and which addresses both the arbitration agreement-enforcement stage of court proceedings (when a court is considering whether to compel or stay a lawsuit pending arbitration) and the recognition and enforcement of arbitral awards.

The federal-only approach is opposed by various stakeholders—including, most prominently, the Uniform Law Commission (ULC) and the Conference of Chief Justices—based on state's rights concerns.[9] At present, the recognition and enforcement of foreign judgments is almost exclusively a matter of state law, and the ULC has played a leading role in shaping the law of the states.[10] Thirty-six states have adopted either the ULC's 1962 Foreign Money Judgments Recognition Act or its 2005 Uniform Foreign-Country Money Judgments Recognition Act.

A. U.S. State Department Efforts to Bridge the Gap

Believing that COCA would not be ratified by the Senate absent a consensus on implementing legislation, the State Department's Legal Adviser, Harold Koh, sought between 2009 and 2013 to bridge the differences between the various stakeholders. In a White Paper issued in April 2012, the Legal Adviser outlined a "cooperative federalism" approach whereby Congress would enact federal implementing legislation, but also allow states to opt out of the federal law and instead be governed by that state's enactment of a uniform act developed by the ULC and approved by the State Department. The federal implementing law and the uniform state act would each address both the dispute stage and the recognition stage and would be functionally identical, with variations occurring only to the extent required by the differing federal and state contexts. In what proved to be a controversial provision, the White Paper specified that federal courts would always apply the federal statute, regardless of whether the court was located in a state that had adopted the state uniform act, even in a diversity action.

In comments solicited by the Legal Adviser, many bar groups expressed a preference for the federal-only approach, but nevertheless grudgingly accepted the suggested compromise. The ULC accepted most of the terms outlined in the White Paper, but with one key exception: it insisted that the uniform state law must be applied by federal courts sitting in states that had enacted it. While this might seem a matter of pure form over substance, the ULC maintained that "the proposed compromise would establish an unacceptable precedent for the future implementation of any convention for which implementation by coordinated federal and state substantive legislation is contemplated."[11]

In January 2013, the Legal Adviser, finding an impasse, indicated that "the Department [of State] should focus its energies upon the federal-only approach in order to complete this important implementation effort," while remaining open to "new proposals from key stakeholders regarding how the package of issues under the cooperative federalism approach might be restructured to gain wider support."[12]

Yet no efforts were made in the U.S. to implement COCA through a federal-only approach or otherwise. The Legal Adviser position remained vacant for the next three years, until Brian Egan was approved by the Senate in February 2016. In the meantime, efforts to bring about ratification in the U.S. were dormant.

B. The ABA-SIL Working Group Proposal

In late 2015, a Working Group of the American Bar Association Section of International Law (ABA-SIL) proposed to resolve the impasse by, as a general matter, implementing the dispute stage of COCA through a cooperative federalism approach and the recognition stage through federal law. The proposal gave something to both sides, yielding to federal law one aspect of the enforcement of foreign judgments (those within the scope of COCA), while expanding the role of state law in the area of enforcement of choice of court agreements (because at present, most federal courts sitting in diversity determine the enforceability of such agreements by applying federal law). Under the Working Group proposal, the state uniform act would be applied at the dispute stage in both federal and state courts, if enacted by the state in which the court sits, thus avoiding the ULC's objection to the White Paper.[13]

The Working Group proposal was not simply an exercise in *realpolitik*. Even those members of the Working Group who favored federal-only implementation concluded there is a less compelling federal interest in the treatment of forum selection clauses between private parties than judgments issued by the courts of foreign sovereigns. The dispute stage of a proceeding also potentially implicates issues of state law that are outside the scope of COCA, including whether there was actual or valid consent to a choice of court agreement. Assigning the entire dispute stage to state law might help ensure that state law contract formation/validity principles are aligned and integrated with COCA-implementing legislation. In addition, because COCA mandates that state courts accept jurisdiction over certain cases and precludes them from adjudicating others, the manner in which the Convention is implemented is understandably a sensitive issue for state judiciaries and legislatures, and allowing states

the option of implementing the dispute stage through a uniform state act would afford greater respect to these sensitivities.

"Despite the continuing impasse, there are reasons to be hopeful."

The initial response to the ABA-SIL proposal within the ULC was divided, with support from some key leaders and opposition from others, but the ULC ultimately resolved in November 2016 that the ABA-SIL Working Group proposal "not be pursued."

C. Prospects for Ratification

1. Parallels to U.S. Ratification of the New York Convention

Despite the continuing impasse, there are reasons to be hopeful. Although the New York Convention is now hailed as one of the most successful private international law treaties, many have forgotten that its initial prospects in this country were also grim, precisely due to federalism concerns. Indeed, the U.S. delegation to the drafting conference for the New York Convention "recommend[ed] strongly that the United States not sign or adhere to the convention," concluding that "adherence to the convention would be looked upon as a sudden Federal intrusion in an area in which it hitherto had failed to exercise its constitutional legislative authority to the full limits" and "would raise problems of Federal-State relations."[14]

The Convention was not ratified by the U.S. until 1970, after thirty-six other countries had already joined. As noted in the legislative history to FAA Chapter 2:

> Although the United States participated in the Conference, the Convention was not signed on behalf of our government at that time because the American delegation felt that certain provisions were in conflict with some of our domestic laws.…[A]s a result of increasing support for the convention (both within and without the Government), the United States decided in favor of accession…. In the committee's view, the provisions of [the federal implementing legislation] will serve the best interests of Americans doing business abroad.[15]

Likewise, if COCA continues to gain momentum, the U.S. business community can be expected to join the bandwagon, increasing pressure for the various stakeholders to yield or compromise.

2. Does the Second Phase of the Hague Judgment Project Offer an Opening?

The Hague Conference on Private International Law is presently developing a broader convention that would provide for the recognition and enforcement of judgments in civil and commercial matters in the absence of a choice of court agreement. The U.S. State Department has been actively involved in the negotiations, and a preliminary draft Convention was released in June 2016.[16]

One might reasonably question whether the U.S. should bother engaging in these negotiations when COCA—a relatively non-controversial convention on the enforcement of judgments resulting from forum selection contracts in commercial contracts—continues to languish and a larger judgments convention would implicate the same federalism issues that have bogged down COCA. Yet a new convention would place additional bargaining chits on the table that could conceivably help break the COCA impasse. It is not difficult to imagine a compromise whereby COCA might be implemented on an FAA Chapter 2 model and the second, broader convention implemented through some form of cooperative federalism.

IV. Conclusion

COCA promises to make cross-border litigation a more viable alternative to arbitration by providing for the enforcement of forum selection clauses and judgments, similar to how the New York Convention provides for the enforcement of arbitration clauses and arbitral awards. COCA will not mean the demise of international arbitration, even if the number of COCA state parties ever catches up to the New York Convention, but it offers lawyers and their clients another viable dispute resolution option.

Endnotes

1. Trevor Hartley & Masato Dogauchi (Edited by the Permanent Bureau of the Hague Conference on Private International Law), Explanatory Report: Convention of 30 June 2005 on Choice of Court Agreements, at 16 (June 30, 2005), https://assets.hcch.net/upload/expl37e.pdf.
2. Peter D. Trooboff, *Proposed Principles for U.S. Implementation of the New Hague COCA,* 42 Int. L. & Pol. 237, 241 (2009).
3. The general rules are subject to certain enumerated exceptions that are described in Louise Ellen Teitz, *The Hague Choice of Court Convention: Validating Party Autonomy and Providing an Alternative to Arbitration*, 53 Am. J. Comp. L. 543, 548 (2005).
4. See Article 3(b).
5. A caveat about London—the United Kingdom will cease to be a party to the Convention by virtue of its membership in the E.U. following Brexit, although there is much speculation that the U.K. will accede directly to COCA post-Brexit.
6. *See* GOL § 5-1402.
7. Lucy Reed, Freshfields Arbitration Lecture 2016, "Ab(use) of Due Process: Sword vs Shield," (Oct. 27, 2016), reported at http://

knowledge.freshfields.com/en/Global/r/1699/freshfields_arbitration_lecture_2016.

8. *See, e.g.*, Edna Sussman & Christi Underwood, *Time & Cost Solutions for Commercial Arbitration*, Disp. Resolution J. 23 (Feb.-Apr. 2011).
9. For more on the ULC's perspective on cooperative federalism, *see* Robert A. Stein, *Strengthening Federalism: The Uniform State Law Movement in the U.S.*, 99 Minn. L. Rev. 2253, 2271 (2015).
10. In 2010, Congress passed the SPEECH Act, which federalized one aspect of the law in this area—the recognition and enforcement of foreign defamation judgments. *See* Pub. L. 111-223 (Aug. 10, 2010), codified at 28 U.S.C. §§ 4101-05.
11. Letter from Michael Houghton (ULC) to Harold Koh (U.S. State Dept.) (Sept. 4, 2012).
12. Memorandum of the Legal Adviser Regarding U.S. Implementation of COCA, at 3 (Jan. 19, 2013).
13. The proposal is discussed in detail in Glenn P. Hendrix, et al., *Memorandum of the ABA-SILWorking Group on the Implementation of the Hague Convention on Choice of Court Agreements*, 49 Int'l Law. 255 (2016). The Working Group included Glenn P. Hendrix (Chair), Ronald J. Bettauer, Robert B. Brodegaard, Theodore J. Folkman, Guy S. Lipe, Edward M. Mullins, Steven M. Richman, David P. Stewart, Louise Ellen Teitz, and Peter Winship. The views of the Working Group were solely those of its individual members and not the position of the ABA.
14. *1958 Report of the U.S. Delegation to the U.N. Conference on International Commercial Arbitration*, 19 Am. Rev. Int'l Arb. 91, 115 (2008).
15. H.R. Rep. No. 91-1181, 91st Cong., 2d Sess. (1970), *reprinted in* 1970 U.S.C.C.A.N. 3601, 3601-2.
16. *See* Hague Conference on Private International Law, Special Commission on the Recognition and Enforcement of Foreign Judgments, 2016 Preliminary Draft Convention, https://assets.hcch.net/docs/42a96b27-11fa-49f9-8e48-a82245aff1a6.pdf.

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Investor-State Dispute Settlement Under CETA—A New Permanent Court

By Sarah C. C. Tishler

Introduction

On October 30, 2016, Canada and the European Union concluded their bilateral free trade agreement, the Comprehensive Economic Trade Agreement ("CETA"),[1] estimated to eliminate 99% of all tariff lines and reduce non-tariff barriers to trade.[2] CETA was concluded after almost eight years of negotiations, during which time international public opinion towards globalization significantly deteriorated. In particular, the public on both sides of the Atlantic became increasingly concerned with the fairness of CETA's initial investor-state dispute settlement ("ISDS") provisions that were perceived by many as potentially undemocratic, biased in favor of multinational corporations, and a threat to the signatory states' right to regulate. Many commentators have surmised that negotiations for the Transatlantic Trade and Investment Partnership ("TTIP") treaty and the protests they provoked raised the profile of international trade deals and drew attention to historically uncontentious features of investor-state arbitration, leading to a spill-over effect on the CETA negotiations.[3]

"The Council of the European Union stated that the form of the ICS was meant to signify 'a clear break from the old [ISDS] approach.'"

This concern with CETA's draft ISDS provisions partly arose due to growing hostility toward the traditional method of resolving investor-state disputes via arbitration. In CETA's initial public draft, the procedure followed a typical "ad hoc" procedure whereby the arbitration tribunal would consist of three nominated arbitrators: one arbitrator nominated by the state, a second nominated by the investor, and the third chosen by the first two arbitrators and who would act as chair of the tribunal.[4] Potential conflicts of interest could arise as arbitrators were not forbidden to serve as counsel or arbitrators in other disputes. Additionally, critics said there was no mechanism for appellate review: even in the event of a decision that was inconsistent with precedent, or where a tribunal member had a clear conflict of interest, the tribunal's decision would be final.

To address these concerns, the final draft of CETA was updated to establish a permanent dispute resolution court, named the Investment Court System ("ICS"). The ICS will adjudicate disputes between foreign investors and the CETA signatory states, a radically different approach from the initial draft that was released to the public in August 2014. In the face of substantial public opposition, it appears the drafters decided to take full advantage of the so-called "legal scrubbing" period (the period of finalization of the draft text between August 2014 and October 2016) to consider ways that they could respond to public outcry against arbitration from both sides of the Atlantic. To that end, the ICS is a permanent body composed of 15 members, three of whom are chosen at random to serve on the panel in the event of a dispute. The ICS was designed to "replace the existing… ISDS mechanism in all ongoing and future EU investment negotiations."[5] The Council of the European Union stated that the form of the ICS was meant to signify "a clear break from the old [ISDS] approach."[6] As such, the current form of the ICS stands as an example of a "second generation" investment tribunal that explicitly addresses many of the criticisms levied at typical ad hoc investment tribunals.

Throughout the negotiations, three main debates shaped the final form of CETA's ICS, and the conclusion of all three debates moved CETA further away from traditional investor-state arbitration: an institutionalized appellate mechanism, mandatory ethical standards for the arbitrators, and an acknowledgement of the right of states to regulate.

Appellate Review

First, a unique feature of CETA's investor dispute resolution is its mechanism for appellate review under Article 8.28. The initial draft of CETA released in August 2014 envisaged an ad hoc tribunal system that was similar to many of the existing bilateral investment treaties. Under the ad hoc system, there is no appellate review of decisions by tribunals. While arbitrations conducted under the auspices of the International Centre for Settlement of Investment Disputes ("ICSID") are able to seek annulment of the award through a limited institutional procedure, this procedure is not considered "appellate" due to its limited scope of review (it excludes appeals based on substantive errors of law or fact), and it has been criticized by some practitioners.[7] Outside of ICSID, the only possible recourse for some types of awards is an application to "set aside" the award, available under very limited circumstances according to the provisions of the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("New York Conven-

tion").[8] While supporters of the lack of appeals in the traditional system applaud its finality and efficiency,[9] its detractors point to a lack of standardization in tribunal members' analysis and a divergence in outcomes, and argue it leads to unpredictability and inconsistency in the investment arbitration system as a whole.[10]

In the face of the backlash against the ISDS provision in the 2014 draft CETA text, as well as the simultaneous backlash against the TTIP negotiations between the United States and the European Union, the European Commission proposed an entirely new Investment Court System in September 2015, as discussed above. As part of the ICS, an appellate tribunal has the power to "review awards rendered" under CETA, and may "uphold, modify, or reverse" awards based on "errors in the application or interpretation" of the law, or "manifest errors in the appreciation of the facts, including the appreciation of relevant domestic law," as well as specific grounds under the ICSID Convention.[11] Appellate tribunal members will also be randomly appointed, and must abide by the same independence and ethical requirements discussed below.

"…CETA's final text, and especially the concessions required for its passage, constitute a reflection of recent criticism."

However, many of the details of the appellate tribunal remain unknown. Items such as "administrative support," procedural issues, and the number of members of the Appellate Tribunal remain outstanding while the CETA Joint Committee decides their final form.

Ethical Standards for Tribunal Members

Second, CETA establishes a code of conduct for tribunal members, set forth under Article 8.30. The Article requires the independence of the tribunal members, that they "shall not participate in the consideration of any disputes that would create a direct or indirect conflict of interest," and that they comply with the International Bar Association Guidelines on Conflicts of Interest in International Arbitration. Additionally, and perhaps most importantly, Article 8.30 requires tribunal members to "refrain from acting as counsel or as party-appointed expert or witness in any pending or new investment dispute under this or any other international agreement," upon their appointment to a case.

The draft text of Chapter 8 from August 2014 contained many of the basic elements that would be incorporated into the ICS; however, these ethical provisions were absent and their absence was heavily criticized by private citizens and civil society.[12] Notably, the European Association of Judges (representing 44 national associations of judges in the European Union) criticized the initial standards for the tribunal in a statement released in February 2016, stating that "[CETA's] provisions…for the judges of the ICS do not meet the minimum standards for judicial office as laid down in the European Magna Carta of Judges or other relevant international texts on the independence of judges."[13]

In response to these concerns, and in addition to the provisions mentioned above, the final text of CETA includes explicit selection criteria for its tribunal members at Article 8.27 (the institution, rather than disputing parties, choose the tribunal members), a standardized procedure for contesting the independence of tribunal members (Article 8.30.2-4), and five-year term limits for tribunal members, renewable once (Article 8.27), in addition to other safeguards of their independence and ethics.[14]

The Right to Regulate

Finally, Chapter 8 of CETA reaffirms the member states' right to regulate as set forth under Article 8.9, distinguishing CETA from the vast majority of investment treaties. Similar to the provisions on appeals and tribunal member ethics, this section changed significantly between the draft released in 2014, and the final version. In fact, in the 2014 draft, states' right to regulate (perceived as a counterweight to lawsuits brought by investors) was not mentioned in Chapter 8, although it was included elsewhere in the draft text.[15] Again, after significant public pressure, Article 8.9 was included, providing in part:

> For the purpose of this Chapter, the Parties reaffirm their right to regulate within their territories to achieve legitimate policy objectives, such as the protection of public health, safety, the environment or public morals, social or consumer protection or the promotion and protection of cultural diversity…For greater certainty, the mere fact that a Party regulates, including through a modification to its laws, in a manner which negatively affects an investment or interferes with an investor's expectations, including its expectations of profits, does not amount to a breach of an obligation under this Section.[16]

Furthermore, in the Joint Interpretative Instrument issued on October 27, 2016, the parties reiterated the "fundamental values" at the heart of the agreement, including the recognition of "the importance of the right to regulate in the public interest," and "that economic activity must

take place within a framework of clear and transparent regulation defined by public authorities."[17] Clearly, any attempted abrogation of the right to regulate was viewed as a roadblock to CETA's passage for constituents on both sides of the Atlantic, and the importance of this right was reflected in the final text.

Conclusion

Overall, CETA's final text, and especially the concessions required for its passage, constitute a reflection of recent criticism. The apparent public distrust of globalization and arbitration, combined with strong opposition to TTIP, resulted in an ISDS provision in CETA that moves firmly away from investment treaties of the past. While it remains to be seen whether CETA's new paradigm will create different substantive outcomes for states and investors, future trade negotiators should expect similar battles in the years to come.

Endnotes

1. Comprehensive Economic Trade Agreement (hereinafter "CETA") (Oct. 30, 2016), available at http://ec.europa.eu/trade/policy/in-focus/ceta/.
2. For a summary of CETA's key elements, *see* European Commission, *Facts and Figures of the EU-Canada Free Trade Deal* (Oct. 18, 2013), available at http://trade.ec.europa.eu/doclib/press/index.cfm?id=974.
3. *See, e.g.*, August Reinisch, *The European Union and Investor-State Dispute Settlement: From Investor-State Arbitration to a Permanent Investment Court*, Centre for International Governance Innovation (March 2016), available at https://www.cigionline.org/sites/default/files/isa_paper_series_no.2.pdf.
4. *See* CETA Consolidated Text, European Commission (Aug. 5, 2014), available at http://www.bilaterals.org/IMG/pdf/-2.pdf (hereinafter "August 2014 Draft").
5. *Commission Proposes New Investment Court System for TTIP and Other EU Trade and Investment Negotiations* (Press Release), European Commission (Sept. 16, 2015), available at http://europa.eu/rapid/press-release_IP-15-5651_en.htm.
6. *Joint Interpretative Instrument on the Comprehensive Economic and Trade Agreement (CETA) Between Canada and the European Union and Its Member States, Council of the European Union* (Oct. 27, 2016), available at http://data.consilium.europa.eu/doc/document/ST-13541-2016-INIT/en/pdf (hereinafter "Joint Interpretative Instrument").
7. *See, e.g.*, Hamid Gharavi, *ICSID Annulment Committees: the Elephant in the Room*, Global Arbitration Review (Nov. 25, 2014), available at http://globalarbitrationreview.com/article/1033891/icsid-annulment-committees-the-elephant-in-the-room. *See also* Christian J. Tams, *An Appealing Option? The Debate About an Appellate ICSID Structure*, Essays in Transnational Economic Law (No. 57) (June 2006), available at http://telc.jura.uni-halle.de/sites/default/files/altbestand/Heft57.pdf (describing in detail the debate over whether to introduce an appellate mechanism into the ICSID system). Under the ICSID Convention, there are only five limited grounds under which an award can be annulled: (1)the tribunal was not properly constituted; (2) the tribunal manifestly exceeded its powers; (3) a tribunal member was corrupt; (4) there was a serious departure from a fundamental rule of procedure; or (5) the award did not state the reasoning upon which it was based. The Washington (ICSID) Convention art. 52, opened for signature Oct. 14, 1966, 575 U.N.T.S. 159, available at https://icsid.worldbank.org/en/Pages/icsiddocs/ICSID-Convention.aspx.
8. Convention on the Recognition and Enforcement of Foreign Arbitral Awards art. 5, opened for signature June 10, 1958, 330 U.N.T.S. 3, available at http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/New-York-Convention-E.pdf.
9. *See, e.g.*, Ian Laird and Rebecca Askew, *Finality versus Consistency: Does Investor-State Arbitration Need an Appellate System?*, 7 J. App. Prac. & Process 285, 298 (2005) ("the finality benefit of arbitration is severely undermined" with the addition of an appellate mechanism).
10. *See, e.g.*, *IISD Investment and Sustainable Development Program, Investment-Related Dispute Settlement: Reflections on a New Beginning*, Results of an IISD Expert Meeting held in Montreux, Switzerland, October 17–18, 2014 (Feb. 2015) (identifying the introduction of an "appeals facility" as a proposed area of reform to the ISDS sphere).
11. CETA at art. 8.28. *See also* Wolfgang Alschner, *Legal Scrubbing or Renegotiation? A Text-as-Data Analysis of How the EU Smuggled an Investment Court into Its Trade Agreement With Canada*, Mapping BITs Blog (March 24, 2016), available at http://mappinginvestmenttreaties.com/blog/2016/03/legal%20scrubbing-ceta/ (arguing that the legal scrubbing period that took place was in fact a renegotiation of the ISDS provisions of the treaty).
12. *See* August 2014 Draft.
13. *Statement From the European Association of Judges (EAJ) on the Proposal From the European Commission on a New Investment Court System*, European Association of Judges (Nov. 9, 2015), available at http://www.iaj-uim.org/iuw/wp-content/uploads/2015/11/EAJ-report-TIPP-Court-october.pdf.
14. CETA at art. 8.30.
15. *See, e.g.*, the right to regulate as codified at Chapter X+1 (Trade and Labour) of the August 2014 Draft. See also Chapter XX (Trade and Environment) of the August 2014 Draft.
16. CETA at art. 8.9 (emphasis added).
17. *See* Joint Interpretative Instrument.

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Open and Shut: The Innovative Use of Opening Argument in International Arbitration

By Alexandre de Gramont

In U.S. litigation practice, trial lawyers often see opening argument as a unique opportunity to capture the hearts and minds of the jury at the outset of the case—to win the trial before it has even begun. Over fifteen years ago, as I was preparing for the first jury trial that I would handle in federal court as lead counsel, I recall poring over Professor Thomas A. Mauet's seminal book, *Trial Techniques.* Mauet explained:

> Studies have shown that jury verdicts are, in the substantial majority of cases, consistent with the initial impressions made by the jury during the opening statements. As in life generally, the psychological phenomenon of primacy applies, and initial impressions become lasting impressions. Accordingly, make sure your case gets off on the right footing. This can be achieved only when you forcefully deliver a logical opening statement that clearly establishes your themes and demonstrates the facts that entitle your party to a favorable verdict.[1]

That page of Mauet's book remains dog-eared on my book shelf—the passage highlighted, circled, and starred.

Of course, in a U.S. jury trial, the opening argument is the jury's first real introduction to the substance of the case (apart from the modest tidbits that the jury may have picked up during jury selection). By contrast, in an international arbitration, the opening argument (typically referred to by the more sanitized and less descriptive term, "opening statement") almost always comes at a comparatively late stage of the case. For better or worse, international arbitration combines the civil law approach to written advocacy with the Anglo-American approach to oral advocacy.[2] Thus, international arbitration cases almost invariably begin with an extended "written phase." The parties submit lengthy memorials setting forth all of their factual and legal arguments—accompanied by the written testimony of their fact and expert witnesses, and all of their documentary evidence.[3]

In a large international arbitration case, the written phase can easily last for eighteen months or more. Before the case reaches the evidentiary hearing (*i.e.*, the trial), the parties have often submitted thousands of pages of pleadings, witness statements, expert reports, and exhibits. The arbitral tribunal is presumed to have read all of these materials. By the time the case reaches the hearing, therefore, the tribunal is expected to be deeply familiar with the factual and legal issues presented by the case. In a typical international arbitration, it is only at this point that counsel present their opening arguments to the tribunal.

Oral Argument in International Arbitration: The Traditional View

For these reasons, in the traditional view of oral argument in international arbitration, the purpose of oral argument is *not* to provide the trier of fact with an introduction to the case. Rather, its purpose is to provide a different type of presentation of the case that has already been submitted in written form—and to explain how the oral evidence about to be heard will further advance that case.

In the traditional view, oral argument in international arbitration is therefore important—but not at the same level of importance as in a jury trial, where, as stated by Professor Mauet, "opening statements can often make the difference in the outcome of a case."[4] In international arbitration, oral argument plays a significant but less dramatic role. As explained by two prominent international arbitrators and practitioners in their chapter on opening statements in the immensely useful book, *The Art of Advocacy in International Arbitration*:

> The opening statement is often the first opportunity for the advocate orally and directly to address the tribunal, face-to-face; to make a direct impression; and to gauge the tribunal's reaction. As such, it can be an extremely valuable chance to clarify the facts and law by correcting any misunderstandings created by the written pleadings; to answer questions from the arbitrators; to understand and dispel particular concerns; and, overall, to persuade the tribunal.[5]

Moreover, in an especially large case, counsel may deploy oral argument to synthesize the voluminous materials that have been presented to the arbitral tribunal, and to focus the tribunal on what each side believes to be the most important aspects of the dispute:

> Clearly, the value of this opportunity increases in proportion to the volume of written material that may also be filed. Tribunals, like anyone else, have a finite capacity to absorb and distill lengthy and detailed written submissions and evidence, and whilst written advocacy obviously has its place, it can often be the face-to-face oral presentation that provides the essential path through the mass of the written material.[6]

Yet even as oral argument is meant to provide a guide through the voluminous written submissions, opening

arguments in a large international arbitration case may take several days to complete.[7]

Effective counsel will avoid regurgitating the written submissions and instead use oral argument to present the case in a new and compelling manner. Even so, under the traditional view of oral argument in international arbitration, it is perhaps not surprising that some prominent arbitrators and practitioners find closing argument to be more important. According to Gary B. Born:

> The most significant aspect of oral legal submissions usually occurs *after* the witness testimony has been completed. It is then that counsel has the opportunity to summarize the evidence and argue how the law applies to it. This is an essential part of presenting a party's case and, in many respects, is the most important element of the party's presentation.[8]

Oral Argument in International Arbitration: Innovation

We are often told that one of the principal advantages of arbitration is the ability to tailor the procedure to the case at hand. There is nothing that requires oral argument to be held at the commencement of the evidentiary hearing. Yet most arbitrators and practitioners probably take for granted that that is the when opening arguments will be heard—immediately before the examination of witnesses, and after the main written submissions (including all of the witness statements, expert reports, and documentary evidence) have been tendered to the tribunal.

Interestingly, far more flexibility has been shown with respect to closing arguments. Although closing arguments often are heard at the end of the evidentiary hearing, after the examination of witnesses is completed, it is not uncommon for tribunals to postpone closing arguments for a period of weeks or even months after the conclusion of the hearing.[9] The idea is to allow counsel a certain period of time to study and digest the hearing transcripts, to present a closing argument that is more focused and well-prepared than it might be if given immediately at the close of a long hearing, and to respond to any questions raised by the tribunal. Such a "delayed" closing argument will often (but not invariably) follow the submission of post-hearing briefs. In other cases, however, closing argument might be dispensed with altogether in favor of post-hearing briefs.

Until recently, opening argument has not been treated with the same flexibility. But at least one prominent arbitrator, Neil Kaplan, has publicly called for opening argument to proceed at a relatively early stage of the arbitration. Mr. Kaplan (who, interestingly, served as a High Court Judge in Hong Kong earlier in his career), has observed that opening argument at the start of the evidentiary hearing—*after* all of the main written submissions have been made—may have limited utility at that stage of the case, compared to the role it could play at another juncture:

> By the time the case gets to an oral hearing the tribunal will be drowning in the claimant's memorial on the merits, with witness statements and documents relied upon, the respondent's defense memorial with witness statements and documents relied upon, claimant's reply, and if necessary the defense to counterclaim and at least one rejoinder. On top of all that there may be skeletal opening arguments some of which will be far from skeletal.[10]

Kaplan argues that opening argument at an earlier stage of the arbitration—*e.g.*, after the first round of memorials but before the submission of the reply and rejoinder—is likely to provide the following advantages:

1. It will ensure that the whole tribunal will read into the case at a far earlier stage than hitherto.
2. It will enable the tribunal to understand the case from that point on, and will inform its subsequent case preparations.
3. It will enable the tribunal to have a meaningful dialogue with counsel about peripheral points, unnecessary evidence and gaps in the evidence.
4. It will facilitate the tribunal in putting points to the parties which they will then have time to consider and respond to.
5. It will enable the tribunal to meet and discuss the issues far earlier than hitherto.
6. It will assist in ensuring speedier and, I would suggest, better awards.
7. Bringing the parties together, with their trial counsel, well in advance of the hearing, means that there is a chance that at least part of the case may be settled, or points of disagreement minimised.[11]

Indeed, there is no reason that an earlier opening argument would have to wait until *after* the submission of opening memorials to advance many of these benefits. Nor does an early opening argument preclude counsel from making (shorter) opening statements at the beginning of the evidentiary hearing.

Costs and Benefits

At a time when international arbitration is increasingly under criticism for its cost and duration, it would be irresponsible for any proposed innovation to be undertaken without considering its costs and benefits in light of the particular case for which it is being considered. While some might argue that the main purpose of international arbitration (as opposed to domestic arbitration) is to provide a neutral forum rather than a more cost-effective and

efficient alternative to domestic litigation, there is every reason for counsel and arbitrators to craft a procedure that provides a cost-effective and timely means of resolving the dispute—not least of which is the fact that that is what most clients want and expect.

Having recently acted as counsel in a large and very complex arbitration in which early opening argument was held over a two-day period after the submission of the first round memorials (*i.e.*, the statement of claim and statement of defense), I can confidently state that it had significant benefits for the case in question. This was a case with multiple, unrelated claims, a factual history spanning more than a decade, and damages alleged to be in the billions of dollars. The opening submissions (including witness statements, expert reports, and exhibits) comprised thousands of pages. Counsel for each party was given a full day to present their client's respective cases, followed by questions from the tribunal.

There is no doubt that in this particular case the presentation of opening argument at a relatively early stage helped focus the parties and the tribunal on the key issues in the case—and made for a more efficient evidentiary hearing, which was held some five months after the opening. It also shortened the evidentiary hearing—eliminating the need for lengthy opening arguments at the beginning of the hearing, and allowing the parties and the tribunal to spend more time on the examination of witnesses. (The tribunal also allowed counsel to make short statements at the beginning of the hearing—but they were limited to new developments that had taken place since the early opening argument, and were completed before lunch on the first day of the hearing. The final day of the hearing was devoted to closing argument.)

On the other hand, the two-day hearing for opening arguments in this particular case was not inexpensive. In addition to the extensive preparation required, the parties, counsel, and arbitrators traveled from multiple countries on three different continents for the in-person hearing. But for a case of this size and complexity—and where the stakes were enormously high—the cost-benefit analysis made sense.

Even in smaller cases, some type of early opening argument can help the parties and the tribunal productively grapple with the issues in the case early on. Such opening argument does not have to be as elaborate as the two-day hearing described above. For example, in a smaller case, opening argument could be much shorter and could be held telephonically. It might be crafted to supplement, rather than to replace, opening argument presented at the beginning of the evidentiary hearing. But even when presented in a more streamlined and simple procedure, early opening argument can deliver significant benefits. At a relatively early stage, the tribunal will have a better understanding of the case; the parties will have a better understanding of each other's respective positions (perhaps increasing the likelihood of early settlement); and both the tribunal and the parties will be better informed for the purpose of moving the case forward. Early opening argument may not make sense in every international arbitration case, but it is an innovation that should at least be considered in one form or another for most cases.

In the final analysis, it must be recognized that presenting a case to an international arbitral tribunal – consisting of lawyers or other professionals who typically have considerable expertise in the subject matter at hand—is not the same as presenting a case to a lay jury. Opening argument is less likely to make the difference in the outcome of a case before the tribunal than before the jury. (For many, that may provide an additional reason to choose international arbitration over domestic litigation.) But—as with every component part of an international arbitration—the timing and format of the opening argument should be carefully thought out to maximize the quality, cost-effectiveness, and efficiency of the overall proceeding.

Endnotes

1. Thomas E. Mauet, *Trial Techniques* (Aspen Publishers, 5th ed., 2000) (hereafter, "Mauet") at 61. Professor Mauet's book is now in its Ninth Edition.
2. Toby Landau and Doak Bishop, "Opening Arguments," in *The Art of Advocacy in International Arbitration*, Doak Bishop and Edward G. Kehoe, Eds. (Juris 2010) (hereafter, "Landau and Bishop"), at 359.
3. In an international arbitration case, there will typically be two rounds of merits submissions during the "written phase" phase of the case. The claimant typically submits a Statement of Claim (sometimes referred to as the opening memorial); the respondent then submits a Statement of Defense (sometimes referred to as the counter-memorial); the claimant then submits a reply memorial; and the respondent then submits a rejoinder memorial. If there are counterclaims, the arbitral tribunal may provide for additional rounds of submissions. In addition, arbitral tribunals generally have discretion to divide the arbitration into phases to address different aspects of the case (*e.g.*, jurisdiction, liability, damages, *etc*.). Each such phase may have its own written and oral phases.
4. Mauet, at 61.
5. Landau and Bishop, at 360.
6. *Id*. at 361.
7. Gary B. Born, *International Commercial Arbitration* (Wolters Kluwer, 2d ed., 2009) (hereafter, "Born") at 1863.
8. *Id*.
9. *See id*.
10. Neil Kaplan, *If It Ain't Broke, Don't Change It*, Journal of the Chartered Institute of Arbitrators, Issue 2 (2014), at 173.
11. *Id*.

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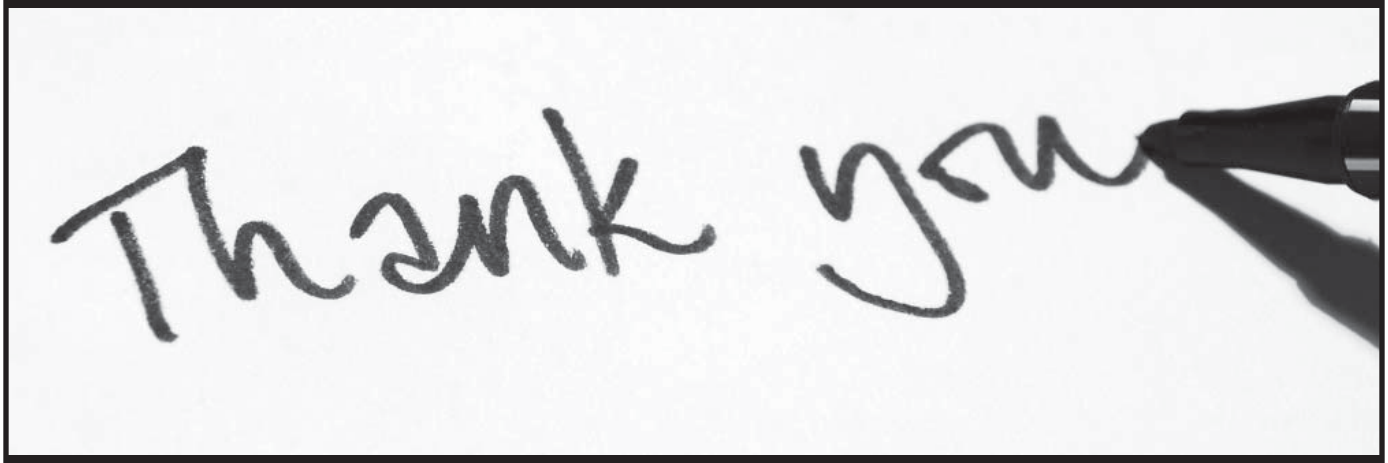

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Book Review
International Arbitration: Commercial and Investment Treaty Law and Practice

By Elliot E. Polebaum
Reviewed by Robert B. Davidson

Much has been written about international arbitration since its appearance in the consciousness of American lawyers, which many date from the days of the Iranian hostage crisis and the experience of the Iran-U.S. Claims Tribunal (the "IUSCT") in the early 1980s. Until that time, international arbitration was largely a European-dominated practice and the province of law professors and an occasional proceeding involving state parties. The Convention on the Settlement of Investment Disputes between States and Nationals of Other States, which established the International Centre for Settlement of Investment Disputes, had been in force since October of 1966 but, with a limited number of signatories, was not in common use. The International Chamber of Commerce also administered a modest number of international commercial arbitrations involving private parties, but the practice was not widespread, at least among U.S. commercial interests. Arbitration was well-known in the London insurance and maritime markets, but these arbitrations were industry-specific and, while many involved cross-border transactions or occurrences, they did not generally involve the procedural framework and cultural issues that are the hallmark of an international arbitration proceeding.

Surely, the New York Convention of 1958, which obtained important acceptance in the ensuing years including U.S. accession in 1970, provided an impetus for international commercial arbitration by establishing a framework for the enforceability of arbitration agreements and resulting awards, but it was the experience of the IUSCT that brought international commercial arbitration into the awareness of big firm lawyers representing private parties in multi-million dollar disputes against a solvent foreign defendant (thanks to the escrow account established at the IUSCT for the payment of Tribunal awards). This established the process as both workable and lucrative, two essentials for its expansion. The fact that international arbitration proceedings took place in such venues as The Hague, Paris and London didn't hurt either. As a result, there has been an explosion of international arbitration in various iterations designed to resolve disputes involving solely private parties or private parties and the agencies or instrumentalities of foreign states. Numerous international arbitration provider organizations have arisen to challenge the ICC's dominance. Thousands of Bilateral and Multilateral Investment Treaties provide for international arbitration to resolve investment disputes. The enactment of the Foreign Sovereign Immunities Act in 1976, 28 U.S.C. Sec. 1601 *et seq.* ("the FSIA") finally articulated a legal regime applicable in the United States to commercial contracts with sovereign entities, and this contributed significantly to the predictability and availability of legal remedies in these transactions. When 28 U.S.C. Sec. 1605(a)(6) was added in 1988, international arbitration became the clear choice for resolving disputes in transactions involving sovereign parties. That subsection provided, by statute, for a sovereign's waiver of immunity when it entered into a commercial contract providing for arbitration subject to the New York Convention.

In recent times international arbitration has become a popular addition to law school curricula and the subject of innumerable conferences, symposia and competitions, the Vis Moot Court Competition in Vienna (and the Vis East in Hong Kong) being in the forefront of those events. The Vienna Vis this year will host over 300 teams from law schools all over the world in what has become that largest such event in the field. If there was ever any doubt about the internationalization of legal work in all fields, just attend an IBA meeting in any given year and stand in awe of the sheer numbers of lawyers, students and professors who work and study in the field of international law generally.

During this period of extraordinary growth, several treatises have gained prominence, foremost among them being *Law and Practice of International Commercial Arbitration* by Blackaby, Partasides, Redfern and Hunter, and Gary Born's multi-volume work on *International Commercial Arbitration*. We can now add another significant contribution: Elliot E. Polebaum's treatise entitled *Inter-*

national Arbitration: Commercial and Investment Treaty Law and Practice.

Mr. Polebaum is well placed to write such a treatise. He led the international arbitration practice group at Fried Frank before stepping down as a partner to focus on sitting as an arbitrator of commercial disputes both international and domestic. He has sat, and continues to sit, as an arbitrator in both administered and *ad hoc* proceedings and has appeared as counsel representing parties in many commercial international proceedings and investment disputes. Among his other many honors, he is an Adjunct Professor at Georgetown University Law Center where he teaches international arbitration.

Like those of Blackaby and Born, Polebaum's work is neither a textbook nor a restatement, but a heavily footnoted treatise on the subject that collects case law and commentary into a coherent and well-organized reference work. Polebaum's work fills the need for a single volume treatise that is a manageable, user-friendly reference not overwhelming in detail.

The work is sold either online or as a hardbound, one-volume binder (about 3 inches thick) bound in the manner of the CCH tax volumes with a removable spine to enable the insertion of new pages for the annual updates. For those of us who find comfort in a tactile sense of scholarship, the paper version gives welcome reassurance. For those of us who like online resources, the treatise is sold online with links to each of the cited and footnoted cases, which number in the hundreds, and is word searchable.

The work is divided into 13 chapters 12 of which are devoted to arbitration generally with a 13th chapter devoted solely to Investment Treaty Arbitration. Each Chapter is divided into sections and then the topics are further subdivided for ease of reference. Chapter 7, for example, is entitled "The Arbitral Tribunal" and has five sections: Importance of the Arbitral Tribunal (section 7.01); Constituting the Tribunal (7.02); Duties and Rights of Arbitrators (7.03); Challenge and Replacement of Arbitrators (7.04); and Disqualification of Counsel (7.05). Under Section 7.05 there are three subheadings [1] through [3]. Section 7.05[1], entitled "The *Hvaska* and *Rompetrol* Decisions" can be found at page 7-43. A quick flip through the volume leads the user to the page where one finds a comprehensive discussion of the two ICSID cases that deal with the approach to the removal of newly appointed counsel—or in the *Hvaska* case, newly disclosed counsel—who have (often on purpose for strategic reasons) a close connection with a tribunal member. The next subsection, Section 7.05[2], entitled "Rules and Guidelines Related to the Removal or Preclusion of Counsel," examines rules promulgated by certain provider organizations that purport to authorize tribunals to deal with challenges to newly disclosed counsel. Section 7.05[3], entitled "The Approach to Removal of Counsel in Other Jurisdictions," discusses how various jurisdictions treat the question of whether private parties should ever be permitted to decide upon the removal of counsel (citing cases that have deferred to a tribunal's ruling on the disqualification of counsel}, or whether counsel removal is a remedy solely in the province of national courts. The discussion, like all topics in the book, is heavily footnoted with references to cases or law review articles that treat the subject matter in greater depth. This structure permits a fairly comprehensive treatment of the subject matter in one section (7.05) written in a total of three pages, which is more than adequate to enable the practitioner to garner the information and case citations needed either for briefing or an understanding of the issues.

Mr. Polebaum's depth of understanding of the issues one confronts in these cases is also evident in the way that he treats situations that do not lend themselves to black-letter rules. In Section 6, for example ("Choice of Law'), subsection 6.03 entitled "Choice of Procedural Law," deals with the dilemma that arises when there is no clear distinction between what is "procedural" and what is "substantive." Subsection 6.03[1] acknowledges the generally accepted rule that the seat of the arbitration controls the applicable procedural law. As experienced international arbitrators know, however, that is only the beginning of the analysis. The next Section (6.03[2]) is entitled "The Procedural Law/Substantive Law Distinction" and contains an in-depth discussion of what issues are considered "procedural" and, therefore, governed by the law of the arbitral seat, and which should be considered "substantive" and, therefore, governed by the parties' choice of substantive law. The subsection also contains the author's view of when and under what conditions a particular rule (governing, say, the statute of limitations in tort cases) should be considered procedural rather than substantive (or vice-versa). This kind of analysis appears throughout the treatise and is extremely helpful to the practitioner needing more than just a general rule.

In sum, this treatise is a valuable contribution that fills the need for a comprehensive, yet manageable, reference. All law firm libraries and practitioners of international arbitration would be well-advised to keep it in easy reach.

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Book Review
International Commercial Arbitration in New York (2nd Edition)

Published by Oxford University Press (2016)
By James H. Carter and John Fellas (eds)
Reviewed by Rory Millson

Since international trade is (we hope) a fact of life, international commercial arbitration is a must, because neither party will want to be relegated to the other's courts.

And for practitioners of international arbitration, this book is a must.

"The book 'is about both the practicalities and the law of international commercial arbitration in New York City.'"

James Carter and John Fellas, two prominent figures in the field, produced the first edition in 2010, consisting of thirteen comprehensive chapters, one written by each of them and the remainder written by a wide variety of other experts. The second edition, largely written by the same authors, builds on the first edition, updating the analysis in detail to reflect developments in the law, including the Supreme Court's recent arbitration decisions. It also provides an expanded view of the practicalities of arbitration in New York, both in the introduction by Carter and Fellas and by a new chapter (Arbitration Hearings in New York). The book is an interesting mix of theory and practice; it "is about *both* the practicalities and the law of international commercial arbitration in New York City."[1]

In an era where countries are competing to set up international arbitration bodies, the book is surprising in that it does not proselytize for New York as a venue for arbitration. Instead, it provides a direct and comprehensive statement of the basic principles and their complexities. Indeed, it is so comprehensive that you may be wondering about how you, a lawyer with a day job, can possibly be a "must" user of this book, with a Table of Cases of over 30 pages.

This review suggests three ways in which you can use the experts' learning to help your clients in international arbitration in the United States.[2] Think of Isaac Newton's seeing further because he was standing on the shoulders of giants.

First, your client should focus closely on the arbitration contract. This is not the litigator's joke that it was negotiated at the last moment by the young lawyers who were still awake. These "governing law clauses should be drafted with more care than is often provided during contract negotiations."[3]

Second, you should have a realistic strategy on the selection of arbitrators. Not only is this the "most important step" in the arbitration, but the rules are (as the book puts it kindly) "murky."

Third, you should consider how your client's arbitration contract should regulate discovery, especially e-discovery.

1. Your Client Should Focus Closely on the Arbitration Contract

"One of the hallmarks of arbitration is its nearly absolute finality."[4] New York courts "apply the laws restricting judicial review of arbitration awards to avoid undermining the arbitration process."[5] Indeed, the Supreme Court has struck down a domestic arbitration clause that attempted to expand the grounds for *vacatur*.[6] This lack of appeal is even more pronounced in international arbitration.[7] The cases in the substantial table of cases thus focus on procedure, especially the procedure specified in the arbitration contract.[8] Scholars like to say that international arbitration as a subject involves procedure.

Since your client's international arbitration is thus going to depend on this procedure, including the rules of any chosen arbitral institution, you should focus on chapter 3 (Drafting Considerations for Clauses Designating New York as the Place of Arbitration).

One way to think of this chapter is that it shows how to avoid many of the complexities discussed elsewhere in the book, topics beloved at arbitration conferences but not by clients. This is not intended as a slight on those chapters, which are fascinating in their own right. Here, however, the focus is on how you can help your client to avoid extraneous issues; if the drafting is correct, you should not have to brush up on some of the more arcane topics (except for their intrinsic interest). Arguments about *Kompetenz–Kompetenz* are for recreation, not your work day.

First, since your client has affirmatively decided to arbitrate, there should be "a clear designation of arbitra-

tion as the agreed dispute resolution mechanism" and "an unambiguously binding undertaking to arbitrate."[9]

Second, there should be a choice of law for the arbitration clause.[10] Note the "importance of careful drafting and understanding the impact of selecting a particular governing law" in order to "avoid surprises once a dispute arises."[11]

Third, the arbitration clause, preferably a model clause, should contain "an appropriately defined scope, which in most instances will be broad."[12]

Fourth, the arbitration clause must have an appropriate mechanism for appointing (and replacing) arbitrators.[13]

Fifth, as discussed below, the client should consider how to regulate discovery.

Sixth, your client can address (as applicable) issues such as:

(a) jurisdiction over non-signatories;

(b) allocation of costs;

(c) class proceedings;[14]

(d) consolidation; and

(e) provisional measures.

2. You Should Have a Realistic Strategy on the Selection of Arbitrators

Chapter 5 (Selection of Arbitrators) proceeds from the premise that the "most important step in any arbitration is selection of the arbitrators."[15]

That statement is in one sense entirely correct. The tribunal will control the procedure and decide the case, without any meaningful review. Nothing can be more "important" than selecting arbitrators who are available to devote time, do in fact devote time, and are fair. You had better select good arbitrators.

In another sense, however, the statement is more controversial. Although "[i]nternational arbitration rules generally require…impartiality by all arbitrators,"[16] the "typical" arbitration agreement in New York provides that "each party or group of parties is to select one arbitrator, and a third arbitrator—the chair of the tribunal—to be chosen," usually by agreement.[17] The advantage of such a system is said to be that it "is intended to give each side a degree of confidence in the tribunal at the outset," which "tends to mitigate natural litigiousness somewhat and induce cooperation when the tribunal sets the initial procedural directions."[18] However, in addition to the specified disadvantages,[19] the chair may view the "wings" with suspicion, which undermines a major advantage of the three-person tribunal, namely that the arbitrators have someone to discuss the case with. Moreover, the system perhaps promotes the idea that the chair is **the** key vote. Indeed, dissents in arbitration are said to be overwhelmingly written by a party-appointed arbitrator in favor of the appointing party.[20]

The chapter refers to a "challenge" in this assumed structure of "how to obtain a tribunal that will be both fair and *favorable*," citing a scholar who argues for a "goal" of appointment of "a majority (at least)…while being independent and impartial…will at the same time be well disposed towards, sympathetic to, or at the very least receptive to that party's position."[21] The extreme position is that the party-appointed arbitrator should have the maximum predisposition towards the appointing party with the minimum perception of bias, as opposed to the view that the entire panel should be chosen in a way that does not involve any arbitrator's knowing who the appointing party is.

This review does not provide an elegant solution in the margin to this debate (akin to Fermat's promise with respect to his last theorem). Indeed, since the review is designed to help you keep your client from becoming a poster child for arbitration buffs, it does not even outline the debate in full. Here instead are some practical comments on why this "goal" may be illusory. Even though you certainly want to find arbitrators who are at the "very least receptive," the pursuit of the "well disposed" may be a pipedream[22]—your ability to find out the views of an arbitrator are limited because you cannot ask those in advance;[23] there is unlikely to be a substantial record of prior writings on the subject;[24] and if you have too close a relationship with the arbitrator, there may well be a challenge.[25] In addition, predicting how someone is going to vote depends on the evidence—arbitrators can change their views when the evidence warrants it.[26] Perhaps the fact of the appointment by the particular party is by itself the impetus for an arbitrator to be "well-disposed."[27] In short, although there is obviously much judgment that can go into the selection of arbitrators, you may not be able to attain the "goal" of "fair and favorable."

Perhaps a more modest "challenge"—good arbitrators—is in order. In the search for such arbitrators, the chapter provides helpful guidance, focusing on three topics.

First, you should consider the applicable tribunal structure dictated by the arbitration agreement, especially the assumed tripartite selection system.

Second, you need to decide your strategy for appointing the arbitrators.

Although the "key to success" is said to be "choosing the proper party-appointed arbitrator,"[28] that is prob-

ably not right. The "key to success" is the selection of the chair, who rarely, if ever, dissents.

Since the dynamics of selecting the chair are even more complicated than selecting the party-appointed arbitrator, let us start with the "proper party-appointed arbitrator." Note the advice. You want "to choose someone who will be perceived to be and will be independent;" be "sympathetic to or at least understanding of the type of arguments the party will advance"; be helpful in the selection of a chair; and "effective in interactions with the chair."[29] In short, if the party-appointed arbitrator is obviously partisan, you will lose the chair (and any advantage you are seeking to gain).

If you follow this advice, you will have a head start on the selection of the chair, the most important member. At that point, you can review the chapter for the complexities—remember the murkiness—of how to select the chair.[30]

Third, the chapter provides a valuable list of places for you to find the names of potential arbitrators.[31]

3. The Arbitration Clause Should Regulate Discovery to Some Degree

The arbitration contract *may* regulate discovery. Parties "are free to specify both the discovery that is permissible between them and the power of the arbitrator respecting such discovery."[32] Indeed, the "first issue for consideration relating to discovery options…is what the arbitration agreement itself provides" because "party autonomy" is "at the top of the pyramid of considerations when looking at the applicable procedure for the arbitration, including discovery issues."[33]

Although such limits are permissible, "international arbitration agreements frequently do not specifically address the scope of discovery in the event of a dispute."[34] Instead, the parties "usually simply specify that a particular set of arbitration rules will govern the arbitral proceedings," and the parties will be held to have incorporated the rules relating to discovery set forth in those rules.[35]

You will want to review the various institutional rules,[36] perhaps even before selecting an institution. Your client should then consider how to adapt those rules.

Not only should you not accept the possibility inherent in several of the institutional rules allowing for full-blown U.S. style discovery,[37] but you want to make *clear* that these principles are not controlling. You want to make sure that discovery is in fact "more limited in arbitration" and, indeed, that "the scope and availability of discovery devices is a significant differentiating factor between judicial and arbitral proccedings."[38]

The authors are obviously aware of the reputation of U.S. discovery. "Extensive discovery—wide-ranging document disclosure and pretrial depositions… is the hall-mark of U.S. litigation."[39] In response to "a concern" that "many parties considering New York as place of arbitration" may have over this "[e]xtensive discovery," one chapter states firmly that this "concern is misguided because international arbitrators sitting in New York need not, and generally do not, follow U.S. litigation standards regarding discovery."[40] Although "the arbitrators' power to compel prehearing discovery on non-parties" is "limited,"[41] this does not solve the issue as fully as the chapter claims.

Here the introduction is helpful, because it explains how the choice of the place of arbitration affects "the dispute resolution culture in which it takes place."[42] The views of "New York based participants in international arbitration in arbitration counsel and arbitrators—have been forged in the crucible of the U.S. system of civil litigation," including "broad discovery."[43] Although experienced arbitrators and counsel may well be able to fashion a process that blends the advantages of diverse systems,[44] the litigation culture may, for example, result in counsel for both parties agreeing on "extensive discovery" without input from your expertly chosen experienced international arbitrators, or perhaps your arbitrators need some reminding too.

To control this issue, Chapter 3 describes how the parties may specify the "rules applicable to discovery" and provides examples of limiting contract language.[45] A different chapter notes the importance of the IBA Rules, which if adopted in the arbitration clause, are "unlikely" to result in "broad discovery."[46]

Moreover, you may want to address the question of e-discovery. Litigators love their opponents' e-mail because these can be very useful for cross-examination. On the other hand, it is fair to say that e-discovery is very costly. There are now various guidelines that you should consider in selecting an institution.[47]

Conclusion

Larry Newman's review of the first edition expressed the hope that the contributors of this fine work would keep it up to date, especially in light of the Supreme Court's interest in arbitration issues. The contributors have exceeded any hope for a mere update. They have created a book that will make you wiser, whether you are an expert studying the finer points, or a practitioner seeking to avoid those points. Here is a hope for the third edition—that the "murkiness" of selecting a panel in our field will have somehow been dispelled. Lux et veritas?

Endnotes

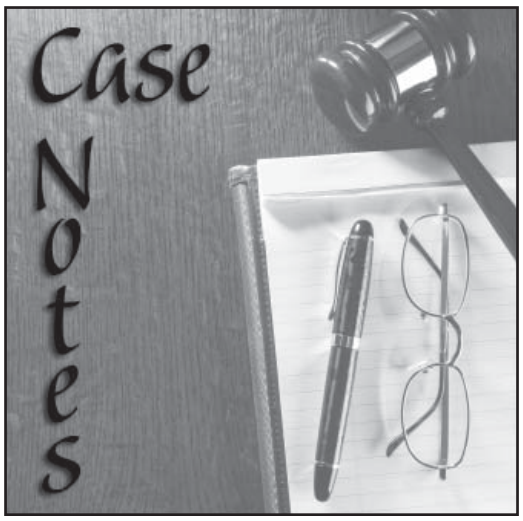
1. § 0.34; emphasis added.
2. The focus of the book is *not* limited to New York. Since "New York City is the center of international commercial arbitration in the United States" (§ 0.01), the authors obviously address practicalities that are New York-centered and also the New York arbitration statute. In addition, the book addresses international commercial arbitration in the United States as a whole. Given the applicability of the FAA and the New York and Panama Conventions, it is not surprising that the book cites a wealth of authority from the entire United States. Indeed, chapter 1 (The Law Applicable to International Arbitration in New York) describes in great detail the interplay among the FAA, the Conventions and state law.
3. § 1.103.
4. § 2.96.
5. § 0.17.
6. § 2.96. Since surveys of clients indicate client concern over this lack of appeal right, some arbitral institutions have designed a regimen that includes an appeal process in the arbitration. (*Id*.).
7. § 0.40. Courts in New York have "never" found "manifest disregard of law" "in the context of an international arbitration award made in New York." (§ 13.130).
8. The place of arbitration determines the procedural law governing the arbitration. (§ 0.40).
9. § 3.04.
10. "Agreements to arbitrate are almost always found as a clause or section of a much larger commercial contract between the parties." (§1.103). The law governing the arbitration agreement (and the conduct of any subsequent arbitration proceeding) is distinct from the law governing the substantive provisions of the contract. (§ 3.11).
11. §§ 1.109–1.110.
12. § 3.02 and § 3.04. An "unnecessarily narrow scope remains an invitation to dispute over whether a given fact-pattern is to be submitted to arbitration." (§ 3.05). Not only are such disputes inherently wasteful, but they may involve who decides the question. Chapter 6 (Jurisdiction: Courts vs. Arbitrators) is a tour de force on the "problem of arbitral jurisdiction," namely "the optimal allocation of authority between courts and arbitrator in interpreting an arbitration agreement and determining whether it is valid, applicable and enforceable." (§ 6.01). Although drafting alone cannot preclude this issue, which "while easily stated, is not easily resolved" (§ 6.01), the over 60 pages of dense analysis should convince any practitioner that the chances of a challenge to jurisdiction should be reduced. Chapter 3 provides drafting advice to promote one forum or the other, in case the problem does arise. (§§ 3.16 *et seq*.).
13. "The most important recommended element is an appropriate mechanism for appointing (and replacing) arbitrators," including a reference to the arbitral rules of any applicable institution. (§ 3.09.) Arbitration clauses often incorporate the arbitration selection (and replacement) procedures of the rules of an arbitration body. (*See* § 5.07) These are summarized at §§ 5.08–5.27.
14. This hotly debated issue, including several recent Supreme Court cases, is discussed at length in Chapter 11 (Class Action Arbitration).
15. § 5.01.
16. § 3.28.
17. § 5.03.
18. § 5.04.
19. There are that "the rules and ethical principles applicable to the selection of the party-appointed arbitrators are not entirely clear" and the process for selecting the chair "tends to be murky." (§ 5.04).
20. One commentator suggests over 95% of dissents are authored by party-appointed arbitrators.
21. § 5.01; emphasis added.
22. The chapter correctly states that "open discussion [of this topic] is relatively scarce" (§ 5.01).
23. § 5.60.
24. § 5.54.
25. *See* §§ 5.56-5.65 for the rules and ethical principles on selecting arbitrators.
26. Think John Maynard Keynes ("When the facts change, I change my mind. What do you do, sir?").
27. CPR has recently posted an article on its website called "Affiliation Bias in Arbitration: An Experimental Approach," which makes this argument. CPR has a "unique provision" allowing party-appointment on a "blind" basis. (§ 5.25).
28. § 5.32.
29. § 5.32. You do not want an arbitrator who believes that his/her role is to make sure that all points are being properly considered. The person whose role that is is called counsel.
30. §§ 5.66–5.76.
31. §§ 5.46–5.53.
32. § 3.41.
33. § 9.01.
34. § 9.13. This is "because it is difficult for parties to predict, let alone agree on in advance, the type of discovery that would be appropriate in the event of a future dispute." John Rawls would not recognize that version of negotiations in the original position.
35. § 9.13.
36. *See* §§ 9.13–9.29.
37. "Careful consideration needs to be given prior to inviting such discovery devices into an international arbitration." (§ 9.09).
38. § 9.11.
39. § 3.38.
40. § 3.38.
41. §§ 3.39.
42. § 0.36.
43. § 0.38.
44. The possible "Americanization" of international arbitration is balanced for "[e]xperienced practitioners and arbitrators in New York" with "practices commonly used in international arbitration proceedings", including the IBA Rules. (§ 0.39). Chapter 2 (The Impact of U.S. Litigation) notes cheerfully that "for non-U.S. litigators," "certain advantages may be achieved by remembering the more salient aspects of the U.S. litigation system that could creep into the arbitration when the participants bring along their U.S. litigation baggage." (§ 2.102).
45. § 3.41.
46. § 9.29.
47. §§ 9.39 *et seq*.

Rory Millson, rmillson@cravath.com, retired after 40 years as counsel in commercial trials and arbitrations, now devotes some of his golden years to ADR.

Moss v. First Premier Bank—The Second Circuit Follows Its Own Precedent—Won't Compel Arbitration When the Exclusively Named Arbitral Provider Is Unavailable to Administer the Dispute

By Bryan J. Branon

If the named arbitration provider in a contract is unable to administer the dispute, can a court compel the parties to arbitrate? While Circuits are split, the Second Circuit Court of Appeals has held "no."



In *Moss v. First Premier Bank*,[1] consumer, Deborah Moss, applied electronically to take out three payday loans from an online provider and was approved. First Premier Bank and Bay Cities Bank (although not the online loan provider) ultimately provided the loan. The electronic loan application included an arbitration clause that read as follows:

> Arbitration of All Disputes: You and we agree that any and all claims, disputes or controversies between you and us, any claim by either of us against the other… and any claim arising from or relating to your application for this loan, regarding this loan or any other loan you previously or may later obtain from us, this Note, this agreement to arbitrate all disputes, your agreement not to bring, join or participate in class actions, regarding collection of the loan, alleging fraud or misrepresentation…including disputes regarding the matters subject to arbitration, or otherwise, shall be resolved by binding individual (and not joint) arbitration by and under the Code of Procedure of the National Arbitration Forum ("NAF") in effect at the time the claim is filed…Rules and forms of the NAF may be obtained and all claims shall be filed at any NAF office, on the World Wide Web at www.arb-forum.com, by telephone at 800-474-2371, or at "National Arbitration Forum, P.O. Box 5091, Minneapolis, Minnesota 55405." Your arbitration fees will be waived by the NAF in the event you cannot afford to pay them.
>
> Further, the following notice appeared immediately below the arbitration provision: "NOTICE: YOU AND WE WOULD HAVE HAD A RIGHT OR OPPORTUNITY TO LITIGATE DISPUTES THROUGH A COURT AND HAVE A JUDGE OR JURY DECIDE THE DISPUTES BUT HAVE AGREED INSTEAD TO RESOLVE DISPUTES THROUGH BINDING ARBITRATION."

Rather than arbitrate, Moss filed a putative class action against First Premier Bank and Bay Cities in federal court alleging violations of the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. § 1962, and state law. The banks moved to compel arbitration on grounds that, although not parties to the electronic loan agreements, the banks were entitled to invoke the arbitration provisions under principles of estoppel. The district court agreed and initially granted the banks' motion to arbitrate.

Moss then filed for arbitration with NAF and NAF responded that it was unable to administer arbitration services due to a consent judgment it had entered into with the Minnesota Attorney General preventing NAF from administering consumer disputes. The 2009 consent judgment stemmed from the Attorney General of Minnesota having sued NAF for consumer fraud, deceptive trade practices, and false advertising. The lawsuit alleged that, although NAF represented itself as an independent and impartial, the forum was in fact "work[ing] alongside creditors behind the scenes…to convince [them] to place mandatory pre-dispute arbitration clauses in their customer agreements and to appoint NAF as the arbitrator of any disputes that may arise in the future." Further, NAF allegedly "ma[de] representations that align[ed] itself against consumers" in order to have creditors use its arbitration services.

After NAF refused to administer Moss's claim, she returned to federal court and moved to vacate the order compelling arbitration. First Premier Bank and Bay Cities Bank argued that Section 5 of the Federal Arbitration Act required the court to appoint a substitute arbitrator as there was a "lapse" in the naming of an arbitrator. Section 5 reads, in part,

> If in the agreement provision be made for a method of naming or appointing an arbitrator or arbitrators or an umpire, such method shall be followed; but… if for any other reason there shall be a lapse in the naming of an arbitrator or arbitrators or umpire, or in filling a vacancy, then upon the application of either party to the controversy the court shall designate and appoint an arbitrator or arbitrators or umpire as the case may require…

The district court granted Moss's motion deciding the language of the arbitration agreements reflected the parties' intent to arbitrate exclusively before NAF and that Moss couldn't be compelled to arbitrate her claims before a substitute arbitrator. First Premier Bank and Bay Cities Bank appealed.

Noting that circuits are split on the issue, the Second Circuit determined it was bound by its own precedent, *In re Salomon Inc. Shareholders' Derivative Litigation*, 68 F.3d 554 (2d Cir. 1995). *Salomon* held that once the parties agreed only one arbitrator could arbitrate any disputes before them (or one arbitration provider was named), a district court must decline to appoint substitute arbitrators or compel arbitration in another forum. The Second Circuit in *Moss* found the arbitration agreement included numerous indicia that the parties contemplated arbitration exclusively before NAF and, like *Salomon*, upheld the district court's determination that Moss could not be compelled to arbitrate outside of the exclusively named provider, NAF. The Court noted that in *Salomon* the FAA "lapse" in Section 5 meant a lapse in the naming of an arbitrator or filling a vacancy on a panel—not a mechanism by which to circumvent the parties designation of an exclusive arbitral forum.

The decision is in line with the Eleventh Circuit decision, *Parm v. Nat'l Bank of Cal.,* which held an arbitration provision in a payday loan agreement unenforceable because the designated arbitrator, the Cheyenne River Sioux Tribal Nation, was unavailable and no substitute could be appointed.[2] The Fifth Circuit has also followed the *Salomon* approach in *Ranzy v. Tijerina,* which held the district court properly denied a motion to compel arbitration due to NAF's unavailability.[3] However, in *Green v. U.S. Cash Advance Ill.,* the Seventh Circuit required the court to appoint a substitute arbitrator[4] and in *Khan v. Dell Inc.* the Third Circuit found *Salomon* "unpersuasive" and held NAF's unavailability did, in fact, constitute a lapse within the meaning of Section 5.[5] Thus, while the Second Circuit followed its earlier decision, the issue of what constitutes a "lapse" under Section 5 of the FAA and whether a court can compel a substitute arbitrator when an exclusively named provider is unavailable, remains an area of arbitral law to be further developed.

What is clear is that consumer arbitration is being closely scrutinized by the judiciary. If parties wish to arbitrate consumer disputes, it may be prudent to revisit their contracts to ensure the provider is viable and that a contingency clause directs a court what to do in the event of unavailability.

Endnotes

1. *Moss v. First Premier Bank*, No. 15-cv-02513, (2d Cir. Aug. 29, 2016).
2. *Parm v. Nat'l Bank of Cal., N.A.*, 2016 WL 4501661 (11th Cir. Aug. 29, 2016).
3. *Ranzy v. Tijerina*, 393 Fed. Appx. 174, 176 (5th Cir. 2010).
4. *Green v. U.S. Cash Advance Ill., LLC*, 724 F.3d 787, 793 (7th Cir. 2013).
5. *Khan v. Dell Inc.*, 669 F.3d 350, 356 (3d Cir. 2012).

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Battle of Munfordville, Kentucky, Sunday, Sept. 14th, 1862, c1863, by Harper's History of the Great Rebellion, Harper's Weekly

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