Dear Members of the International Arbitration, International Litigation, and International Mediation Committees of the Section of International Law:

We would like to thank you for your continued interest and support of The International Dispute Resolution News. We are pleased to announce that the inaugural edition was a success, receiving the Section’s 2010 Outstanding Newsletter Award.

In this second edition, we have four articles addressing a variety of issues that we believe will be of interest to members of the committees. First, this issue includes a thought-provoking article on the current state of the law in the United States on when parties to failed contract negotiations can be required to resolve their disputes in arbitration, notwithstanding the fact that no contract containing an arbitration clause was ever signed. Next, we offer a very interesting and timely article on the role of mediation in resolving legal disputes in Afghanistan. Finally, we have two articles addressing current issues in international litigation – the first article discusses special challenges posed by e-discovery to foreign litigants and nonparty witnesses in the U.S. courts; the second article provides updates on recent changes to Swiss law on civil procedure and debt enforcement that may affect international practitioners.

As always, we have included a number of case notes, summarizing recent decisions that may be relevant to your practice, as well as a 2010-2011 calendar of events that may be of interest to the committees’ members.

We invite submissions of proposed articles and case notes for future editions. If you are interested in submitting an article or a case note for publication, please contact Ekaterina Schoenefeld at eschoenefeld@schoenefeldlaw.com.

We hope that you had the opportunity to attend the outstanding programs in Paris at the just-concluded Fall Meeting and that we will see you in Washington in April at the Spring 2011 meeting and in Dublin in October at the Fall 2011 meeting.

The Editors
Hanging by a Thread – Finding Arbitrability without Clear Evidence of a Contract

By Bruce M. Polichar

It is not unusual for business deals to fall apart just at the moment when everyone thought they were concluded. Well, not everyone – actually about half of those involved. The other half feel that it was just a potential deal that never came together. This scenario plays out in business every day, and just as frequently spawns legal disputes over whether enforceable contractual rights and obligations have been created or not. If and how businesses may seek an arbitrated resolution of these disputes is the subject of this article. Suggestions for drafting arbitration provisions to address these issues appear at the end of this article.

This article was near completion when the United States Supreme Court issued a ruling that may have a significant bearing on the legal analysis on which my discussion is based. In order to deal with the issues with some level of clarity, I have chosen to first explore the specific subject matter of establishing arbitrability even where a complete agreement between the parties may not have been reached. Then we will examine whether the Court’s June 2010 ruling in Granite Rock Co. v. International Brotherhood of Teamsters, ___ U.S. ___, 130 S.Ct. 2847 (2010) may displace or impact prior law in this area.

A classic example of disputed arbitrability arose in an international commercial arbitration I recently ruled on involving an American company, “Americo,” and a European company, “Euroco.” The notice of arbitration that commenced the proceeding quickly generated a vigorous response from Euroco contending that no arbitration could take place inasmuch as the parties had never entered into a contract and, thus, there was no agreement to arbitrate. As is often the case, an arbitrator was being asked to make a threshold determination as to whether the matter could proceed at all – whether the dispute was arbitrable or, to put it another way, whether the arbitrator and the arbitral institution under whose rules the proceeding was initiated had jurisdiction to conduct an arbitration.

Whether by the instincts born of time at this practice or otherwise, my initial inclination in reviewing the arbitrability challenge was to take a step back from trying to determine the overall scope of the possible agreement of the parties. Indeed, well-established federal law in such situations makes it clear that the arbitrator has a fine line to walk in assessing the arbitrability issues without becoming immersed in the potential merits of the larger contract claims.

Factual Background

A brief overview of the exchange between Americo and Euroco presented a fact situation quite common in commercial disputes, particularly those where arbitrability is challenged. I describe it in some detail because it serves to highlight a body of very typical arbitration disputes in which the overall contractual context can be quite detailed but nevertheless inconclusive as to the overall intentions of the parties to conclude a fully binding contract. The documents provided to me represented many months of negotiations between Americo and Euroco in an attempt to reach a final and comprehensive agreement on their overall business arrangement. Americo argued that by reason of alleged oral agreements reached between the parties concerning the business Euroco was to conduct for Americo in certain European territories, certain draft deal memos were intended to confirm the parties’ agreement (“the deal memo”). Americo also argued that by virtue of other written communications between the parties, a legally binding written agreement was entered into establishing jurisdiction to arbitrate before the “XYZ” arbitral institution. It appeared from a surface review that the parties may not have fully reached an agreement on the terms of the underlying transaction, but the exercise was to refrain from being drawn into any conclusions or leanings on that issue, and to focus only on whether they had sufficiently agreed to confer jurisdiction on an arbitrator to resolve the dispute.

The version of the deal memo that Americo included in its notice of arbitration contains a provision that states, “In case of any dispute the parties agree to XYZ arbitration.” The deal memo does not appear to have been signed by either of the parties. There appeared to have been various notes between the parties evidencing an exchange of comments and proposed modifications and revisions by each of the parties to the original draft of the deal memo. Additional exhibits to the notice of arbitration included a series of e-mails between the parties containing comments by each upon the terms set forth in the deal memo, and a continuing thread of subsequent comments relating to it, and what appear to be further revisions of the original deal memo, i.e., a classic paper trail of back-and-forth negotiations.

The correspondence suggested that the parties concurred on numerous points, some potentially significant and material to the formation of a contract, and others seemingly much less important. There appeared to have been agreement on a number of negotiated points by the comment “okay” offered

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2 Although we focus here primarily on commercial disputes, the legal framework and analysis below applies to arbitrability challenges broadly.

3 The institutional rules referenced herein are quite consistent with those of most of the best-known international arbitration organizations, and their application to these situations may thus be generalized.

4 The situation also arises frequently in labor disputes, as we will see in Granite Rock, as well as in consumer and employment cases.
by one or the other at various points in the course of the communications. In one e-mail exchange there is a comment from Americo’s negotiator which reads, “13. In case of any disputes, we would like to use XYZ arbitration.” [Emphasis mine]. Appended to that, and admittedly written by Euroco’s negotiator is the comment, “Okay.” As discussed in greater detail below, Euroco acknowledged this “Okay” comment, but raised issues concerning its meaning, intent, and significance to this inquiry.

On that same date Euroco’s negotiator incorporated the XYZ arbitration clause into a revised draft of the deal memo and sent it back to Americo along with various other comments reflecting their ongoing negotiations. At some point, following this last written exchange, Euroco notified Americo that Euroco did not intend to proceed with the deal, with no reference being made to any unacceptable terms or other reason for withdrawing from the discussions of a business arrangement. Sometime thereafter, Americo initiated the arbitration.6

Procedural Discussion
In its objection to the jurisdiction of the tribunal, Euroco argued that, under the XYZ’s published Rules and California law, a written contract between the parties agreeing to arbitration was a pre-requisite to the conduct of an arbitration, and no such written agreement had been consummated by the parties.6 Euroco’s various related arguments in opposition to arbitrability and jurisdiction of the arbitrator can be summarized as follows: (i) the arbitration mechanism did not apply to this case because the parties had not entered into a written contract, as required by the Rules, as well as California Code of Civil Procedure (“CCP”) Section 1281, requiring that there be a written agreement between the parties in order for arbitrability to exist; (ii) there was no contract that Americo could submit to the arbitrator or the XYZ to satisfy a submission requirement; (iii) Euroco did not voluntarily agree to arbitrate the dispute, and therefore, it was not brought within the scope of other XYZ Rules describing situations in which the parties affirmatively agree to arbitrate; and (iv) there was not even an oral agreement between the parties because the parties never reached a substantive mutual agreement on the draft terms that were circulated between them. The overall thrust of the challenge was that there was no contract upon which to base an agreement to arbitrate.

Analysis
The ruling on the motion to dismiss focused solely on the question of arbitrability and jurisdiction of the tribunal to proceed under the XYZ Rules. The larger range of questions concerning a comprehensive agreement between the parties, its contents if any, or any questions regarding any breach of such an alleged agreement, was explicitly deemed outside the scope of the discussion and my ruling. The sole question addressed was: “Did the parties agree to arbitrate?” As noted below, this distinction is central to the applicable case law.

It is well-established that arbitration is a matter of private contract, and arbitrability and the jurisdiction of an arbitration tribunal require that the parties entered into a written agreement to arbitrate.7 The XYZ Rule in question states that “the Arbitrator shall exercise all powers granted to commercial Arbitrators under the laws of the State of California, USA or the laws of the jurisdiction where the arbitration takes place . . . .” Under the XYZ Rules, all such arbitrations are conducted under California law unless the parties agree otherwise. With respect specifically to international arbitrations, the governing California law is found in CCP Section 1297 et seq. Section 1297.72 provides that:

An arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telegrams, or other written means of communications which provide a record of this agreement, or in an exchange of statements of claim and defense in which the existence of an agreement is alleged by one party and not denied by another. . . .

(Emphasis added).8

The XYZ Rule granting the arbitrator authority to rule on his/her jurisdiction was modeled on CCP Section 1297.161.

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5 Among other complexities for the arbitrator, Euroco’s reply to various provisions of the deal memo stated that all its comments and all changes were subject to actual approval rights. They simply note that there could be additional revisions or comments on the deal memo overall. Subsequently, Euroco claimed that its board of director’s approval was required in order to conclude an agreement, and no such approval was ever given. But the purported reservation language following the “Okay” to Americo’s comment #13 and other of Americo’s points, transmitted together with a revised deal memo incorporating the requested “XYZ” arbitration clause, merely says that the negotiator is circulating the draft amongst other company executives, “so I must reserve their right to make additions and/or revisions.” From that point forward, and following upon Euroco’s adding the requested arbitration clause to the revised draft deal memo, there is nothing to suggest that Euroco’s agreement to, or inclusion of, the arbitration language was either conditioned or reconsidered by anyone in Euroco’s company.

6 This correctly reflects the rules of virtually all arbitration tribunals as well as both state and federal statutory and case law. Euroco’s response was treated as a Motion to Dismiss the proceedings, and additional arguments and authorities were submitted by the parties. [Note: Under the XYZ Rules, as well as California Code of Civil Procedure Section 1297.72, it is the province of the arbitrator to rule on issues of his or her jurisdiction and arbitrability. This also mirrors the rules of the other major arbitral institutions. In some states, such as California, there are separate sections of these laws dealing with domestic and international arbitrations. California Code of Civil Procedure, Sections 1280 et seq. (domestic); and 1297.11 et seq. (international), which are largely, but not completely, the same. The particular facts of this challenge bring the Federal Arbitration Act strongly into play for guidance in handling such an international commercial dispute, because Congressional policy is specifically focused on these issues where international business transactions are involved.]


8 There is an interesting question of whether the Rules intended “USA” to reference the Federal Arbitration Act, or merely identify California as a State within the United States for the benefit of non-American participants. The point would appear to be moot since the Federal Arbitration Act, by its terms, applies to both interstate and international commerce. 9 U.S.C. 1.

9 It is interesting to note that there is virtually no case law interpreting CCP, Sections 1297 et seq. While it may be helpful to refer to the Section 1281 provisions and cases thereunder, it is perhaps more appropriate under the arbitral institution’s rules to draw upon the Federal Arbitration Act, which governs the enforceability of arbitration agreements in all contracts involving both interstate and international commercial arbitration.
The language of both provisions is almost identical. Section 1297.161 of the Code states:

The arbitral tribunal may rule on its own jurisdiction, including ruling on any objections with respect to the existence or validity of the arbitration agreement and for that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract, and a decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause.10

If the contract containing the arbitration agreement designates such rules of a named tribunal, then the court is to defer to them and leave arbitrability and all other issues to the arbitrator. Dream Theater, Inc. v. Dream Theater, 124 Cal. App. 4th 547 (2004) (“Just as they may limit by contract the issues which they will arbitrate...so too may they specify by contract the rules under which that arbitration will be conducted.” (quoting *Volt Info. Sciences, Inc. v. Leland Stanford Jr. Univ.*, 489 U.S. 468, 478-79 (1989)).

The *Nicaragua Line of Cases*

Americo cited *Republic of Nicaragua v. Standard Fruit Co.*, 937 F.2d 469 (9th Cir. 1991), cert. denied, 503 U.S. 919 (1992) (“*Nicaragua*”), for the general proposition that “even the most minimal indication of the parties’ intent to arbitrate international disputes must be given effect.” The case is instructive with respect to the complex issues presented in cases such as *Americo vs. Euroco.* In any case in which the Federal Arbitration Act (“FAA”) applies, federal substantive law governs the question of arbitrability. *Simula, Inc. v. Autoliv, Inc.*, 175 F.3d 716,719 (9th Cir. 1999); *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983); *Nicaragua*, 937 F.2d at 474-75. This means the FAA applies to all cases involving interstate or international commerce. *Nicaragua* is a pivotal decision on this issue (having been cited favorably in over one-hundred subsequent state and federal decisions), and deserves careful analysis.

In *Nicaragua*, the newly-installed Sandinista government had begun negotiations with a group of affiliated American and Nicaraguan corporate entities comprising Standard Fruit Company (“Standard”) with respect to an expansive new arrangement for the growing and export of the nation’s economically-critical banana crop. This followed an initial attempt by the rebels to nationalize the industry – an effort which they came to realize could be economically disastrous.

While a written memorandum of agreement regarding certain aspects of the overall arrangement had been reached with some of the Standard-affiliated entities through an extended series of negotiations, additional implementing contracts were required to fully realize the overall understanding the contracting parties intended, and some of the Standard entities had not even signed the initial memo. However, the memo did contain a somewhat clumsy and incomplete arbitration provision which the parties intended to further refine and document in what ultimately became a failed series of further negotiations on the overall business arrangement between the parties. It read, very simply: “Any and all disputes arising under the arrangements contemplated hereunder... will be referred to mutually agreed mechanisms or procedures of international arbitration, such as the rules of the London Arbitration Association.” The court noted that “Nicaragua admits that this is less than crystal clear, and in fact refers to an association that does not exist.... During the negotiations themselves, neither side could remember the name of the arbitration body in London.” *Nicaragua*, 937 F.2d at 473.11

In reversing the district court’s denial of Nicaragua’s motion to compel arbitration, the Ninth Circuit carefully reviewed the provisions and policies of the FAA and the various federal court cases interpreting them. To begin with, the court stated that the FAA reflects the strong Congressional policy favoring arbitration by making arbitration clauses “valid, irrevocable, and enforceable.” *Id.* at 475. Citing *Perry v. Thomas*, 482 U.S. 483, 489 (1983), the court in Nicaragua said that “the standard for demonstrating arbitrability is not a high one: in fact, a district court has little discretion to deny an arbitration motion.” 937 F.2d at 475. The court noted that “as with any other contract, the parties’ intentions control, but those intentions are generously construed as to issues of arbitrability.... The only issue properly before the district court was whether the parties had entered into a contract evidencing a transaction involving commerce under the Act and committing both sides to arbitrate the issues of the contract’s validity.” *Id.* at 475.12

**A Surgical Look at the Initial Evidence**

We are all trained as lawyers, and certainly as quasi-judicial officers, to refrain from drawing conclusions until all of the evidence is in and carefully examined. However, that normally appropriate approach is exactly what the cases have historically warned against in assessing challenges to arbitrability based on claims of “no contract.” Instead, an arbitrator must avoid delving into the merits of whether the parties had entered into a fully binding comprehensive agreement, and only seek out clear evidence of an *agreement to arbitrate.*

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11 In all likelihood they contemplated the London Court of International Arbitration which had been a major center for international commercial arbitration for many years.

12 That standard, in fact, was the one applied in ruling on the Motion to Dismiss in *Americo v. Euroco*. 
Nicaragua’s reversal of the district court turned significantly upon the fact that the lower court had looked to the existence of a contract as a whole to determine arbitrability. This was squarely contrary to the Supreme Court’s landmark ruling in *Prima Paint v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967). *Prima Paint* expressly held that *courts may not consider challenges to a contract’s validity or enforceability as defenses against arbitration*. That case “demands that arbitration clauses be treated as severable from the documents in which they appear unless there is clear intent to the contrary. An arbitration clause may thus be enforced even though the rest of the contract is later held invalid by the arbitrator.” *Nicaragua*, 937 F.2d at 476 (citing *Prima Paint and Teledyne, Inc. v. Cone Corp.*, 892 F. 2d 1404, 1410 (9th Cir. 1990)). In a footnote in *Nicaragua*, the court stated:

The district court reasoned that an arbitrator can derive his or her power only from a contract, so that when there is a challenge to the existence of the contract itself, the court must first decide whether there is a valid contract between the parties. Although this appears logical, it goes beyond the requirements of the statute and violates the clear directive of *Prima Paint*. Because of the presumption of arbitrability established by our Supreme Court, courts must be careful not to overreach and decide the merits of an arbitrable claim. Our role is strictly limited to determining arbitrability and enforcing agreements to arbitrate, leaving the merits of the claim and any defenses to the arbitrator.

*Nicaragua*, 937 F.2d at 478 (emphasis added).

Euroco had argued that, while it did respond to America’s request that disputes be resolved under XYZ arbitration with an “Okay,” it only meant that it was agreeable if all the rest of the terms of the arrangement were fully finalized. However, this reservation or explanation of the assent to arbitration was not included in any of the communications between the parties, and appears only to have been raised in defense of the effort by America to engage the arbitration process. A statement that a party did not intend to arbitrate, made only after a dispute over arbitrability has arisen, when the circumstances demonstrate otherwise, is ineffective to avoid the obligation to arbitrate.13

**Severability of the Arbitration Clause Is Key**

What was pivotal for my analysis in *Americo v. Euroco* was the portion of *Nicaragua and Prima Paint* that requires the arbitrator to disregard the surrounding contract language as formulated in the communications exchanged by the parties, and “consider only issues relating to the making and performance of the agreement to arbitrate.” *Nicaragua*, 937 F.2d at 477 (emphasis added). The correct analysis, according to *Nicaragua*, is set forth in *Sauer-Getriebe v. White Hydraulics, Inc.*, 715 F.2nd 348, 350 (7th Cir. 1983), in which the court said:

White argues that if there is no contract to buy and sell motors there is no agreement to arbitrate. The conclusion does not follow its premise. The agreement to arbitrate and the agreement to buy and sell motors are separate. Sauer’s promise to arbitrate was given in exchange for White’s promise to arbitrate and each promise was sufficient consideration for the other.

Thus, the court in *Nicaragua* concluded that in the absence of anything in the ambiguous arbitration clause that was included in the incomplete agreement between the parties showing that it was not intended to be severable, “we must strictly enforce any agreement to arbitrate, regardless of where it is found.” 937 F.2d at 477. The arbitrator or a court “can only determine whether a written arbitration agreement exists, and if it does, enforce it in accordance with its terms.” *Howard Elec. & Mech. V. Briscoe Co.*, 754 F.2d 847, 849 (9th Cir. 1985). As noted above, and taking CCP Section 1297.72 as a guide, various types of writings evidencing the agreement to arbitrate are appropriate to evaluate the existence of the agreement. Similarly, the doctrine of severability of an arbitration clause is firmly based on both state and federal statutory and case law.

**Policy and the Agreement to Arbitrate**

“It is well established ‘that where the contract contains an arbitration clause, there is a presumption of arbitrability.’” *AT&T Techs, Inc., v. Communications Workers of America*, 475 U.S. 643, 650 (1986); *Comedy Club v. Improv West America*, 553 F.3d 1277 (9th Cir. 2009). The *Nicaragua* court discussed what, in fact, constitutes an agreement to arbitrate. It begins by emphasizing “the emphatic federal policy in favor of arbitral dispute resolution [which] applies with special force in the field of international commerce.” 937 F.2d at 478 (citing *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth Inc.*, 473 U.S. 614, 631 (1985) and *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972)). “The Federal Arbitration Act’s presumption in favor of arbitration carries ‘special force’ when international commerce is involved.” Id.; see also, Domke on Commercial Arbitration, 3d (“Domke”) Sec. 7:4 (citing *Sandvik AB v. Advent Intern. Corp.*, 220 F.3d 99 (3rd Cir. 2000)). And,

According to the Supreme Court, when international companies commit themselves to arbitrate a dispute, they are in effect attempting to guarantee a forum for any disputes. Such agreements merit great deference, since they operate as both choice-of-forum and choice-of-law provisions, and offer stability and predictability regardless of the vagaries of local law. The elimination of all such uncertainties by agreeing on a forum acceptable to both parties is an indispensable element in

13 *See Castile v. Berrie & Co.*, 2008 WL 453281 (C.D. Cal. October 6, 2008) (claim that party did not intend to arbitrate claims is ineffective, relying on Nicaragua for the proposition that there is no discretion to deny arbitration where an agreement to arbitrate exists).
international trade, commerce, and contracting. An agreement to arbitrate before a specified tribunal is, in effect, a specialized kind of forum-selection clause that posits not only the situs of suit but also the procedure to be used for resolving the dispute.

Nicaragua, 937 F.2d at 478 (citing Scherk v. Alberto-Culver Co., 417 U.S. at 518-519 (1974)).

“The fact that the United States has enacted the International Convention on the Recognition and Enforcement of Foreign Arbitral Awards as part of the Federal Arbitration Act, 9 U.S.C. Sec. 201-208, is further evidence of this federal policy.” Nicaragua, 937 F.2d at 478.14

Even where there are problematic issues about the clarity of an agreement to arbitrate, “the clear weight of authority holds that the most minimal indication of the parties’ intent to arbitrate must be given full effect, especially in international disputes,” and “the scope of the clause must also be interpreted liberally.” Nicaragua, 937 F.2d at 478 (emphasis added). “As a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense of arbitration.” Id. at 479 (citing Moses H. Cone Mem’l Hospital, supra). “Any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.” Moses H. Cone Mem’l Hospital, 460 U.S. at 24-25. “If the purported agreement...is susceptible of an interpretation that would allow arbitration, any doubts...should be resolved in favor of arbitration.” Howard Elec. & Mech. V. Briscoe, 754 F. 2d 847 (9th Cir. 1985) (emphasis added).

[The FAA] is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary. . . . The effect of the section is to create a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act. Domke, Sec. 7:5.

A commonly-related issue in the various lines of arbitrability cases, including Granite Rock as we will see, is the scope of the arbitration clause in terms of what issues are claimed to be subject to arbitration. Inasmuch as the most common types of arbitration clauses found in commercial agreements tend to be along the lines of “all matters arising hereunder,” or various permutations of that sort of language, it seems odd that the courts have sometimes engaged in forced and hair-splitting exercises in deciding when to apply or reject arbitration in a particular contractual situation.15 It is also very common practice in both pure commercial contracts and in collective bargaining agreements to explicitly exclude any specific issues that the contracting parties want to keep out of the arbitration process. As a matter of normal business practice, it is fair to say that when parties include an arbitration clause, they anticipate that arbitration will be the mechanism for resolution of any sort of dispute they may later encounter. Courts seem to turn a blind eye to real world practices when they perform micro-word surgery to “discover” some other intention in these cases. Nevertheless, this practice continues, and the law becomes more strained and makes the results more unpredictable on what should be a fairly easy issue. A bit more on this when we examine Granite Rock.

A State Law Perspective

As regards consideration of arbitrability in Americo v. Euroco, the propositions articulated in the Nicaragua line of cases are, of course, consistent with California state court opinion as well. “Doubts concerning the scope of arbitrable issues are to be resolved in favor of arbitration.” Blatt v. Farley, 226 Cal. App. 3d 621 (1960). “Under both federal and California law, arbitration agreements are valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.” Armentariz v. Foundation Health Psychare Services, Inc., 24 Cal. 4th 3 (2000); see also Horton v. California Credit Corp., 2009 WL 2488031 (S.D. Cal. August 13, 2009)). In light of the comprehensive statutory scheme regulating private arbitration, courts will indulge every intention to give effect to such proceedings. Woolls v. Superior Court, 127 Cal. App. 4th 197 (2005). This is generally consistent with arbitration in most other jurisdictions, particularly where the Uniform Arbitration Act has been used as a foundation for state arbitration statutes. See Domke, Secs. 8:4 and 8:8.16

Thus, even though the proposal to submit the dispute to XYZ arbitration and the responsive “Okay” were exchanged between Americo and Euroco in the course of negotiating a preliminary agreement regarding the proposed business arrangement, such a preliminary agreement appears to be binding under both California and federal law regardless of whether a subsequent contract is finalized. Hotel del Coronado Corp. v. Foodservice Equip. Assn., 783 F.2d 1323, 1325 (9th Cir. 1986); Nicaragua 937 F.2d at 479. Parties may identify the arbitrable claims indirectly by choosing a body of private arbitration rules, such as the XYZ Rules, that specifies the scope of arbitrable claims. Zakarian v. Bekov, 98 Cal. App.

14 It should be noted that the XYZ arbitral institution has been established and has operated for over 25 years, with specific recognition of the effects of the Convention upon arbitration awards entered pursuant to the XYZ Rules.

15 "Where a contract provides for arbitration of ‘any controversy or claim arising out of or relating to this agreement or breach thereof,’ such broad language covers contract generated or contract related disputes between the parties however labeled...” Acredo Maldonado v. PPG Industries, Inc., 514 F.2d 614 (1st Cir. 1975).

16 According to Domke, there is a body of state law that holds that, if the parties fail to agree on all of the terms of a contract, there is no contract and an arbitration clause cannot be invoked. Domke, Sec. 8:4. However, these cases do not arise under the FAA, and would not appear to be controlling where the doctrines stated in Nicaragua and the large body of cases following it apply. “The rules of contract interpretation employed under the FAA are the same as those under the CAA [C.C.P. Sec. 1280 et seq.], and the relationship of state and federal law is recognized in cases in other circuits.” Valencia v. Smyth, 185 Cal.App.4th 153 (2010).
The facts in Granite Rock are somewhat convoluted. Briefly, the Granite Rock Company and the Teamsters Local had a collective bargaining agreement (“CBA”) which expired in April 2004. Negotiations for a successor CBA broke down and the Local struck. There ensued a series of disputed ratification votes on a new CBA that took place between July and December 2004. In the end the parties conclusively adopted the new CBA with a specific provision that made it and all of its terms retroactive to May 1 – the day immediately following the expiration of the predecessor CBA. The new CBA contained a broadly-worded arbitration clause (“all disputes arising hereunder”), with three specific areas explicitly excluded – none of which were material to the dispute before the Court. The substantive target of Granite Rock’s filing in the district court was an attempt to obtain judicial recognition of a novel tort claim under the LMRA, Section 301(a), growing out of its claim that the Local’s lengthy and costly strike violated the CBA and caused damages.

The district court submitted the question of ratification to a jury which found for Granite Rock that the effective date of the CBA was in July. The Ninth Circuit reversed, holding that under Prima Paint and related cases, the matter was one for the arbitrator from the inception, and ordered the case to go to arbitration. The Ninth Circuit held that there was no viable tort action under the LMRA, Section 301(a) – a proposition ultimately affirmed in the Supreme Court ruling as well. In its ruling, the Supreme Court rejected all of the Ninth Circuit’s bases for holding that the dispute was for the arbitrator, and not the court.

The core arbitration ruling in Granite Rock, with Justice Thomas writing for the majority, is that the question of whether the CBA containing the arbitration clause and a no-strike provision was validly formed during the strike period is one for the court, not for the arbitrator. That is, the question of when a contract came into existence was held to be a question for a court. The Court distinguished this case from its 2006 ruling in Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 440 (2006), which it referred to as a case presenting the question of whether the contract came into existence, i.e., a contract formation/validity issue. I would submit that this is not an accurate characterization of the Buckeye decision. Buckeye states very clearly that it follows the long line of cases, starting with Prima Paint, that distinguishes between challenges to the validity of the arbitration clause

17 Without delving into the various exchanges between the parties, certain points raised in Euroco’s opposition to the arbitration proceeding should be mentioned. Although Euroco asserted that at all times it was clear that its board approval was a requirement of a binding agreement, there is no mention of board approval in any of the communications that were provided to the arbitrator. There are various references in the correspondence stating a reservation to address possible additional revisions or additions to the pending deal memo – but no statement (or suggestion) of a condition precedent to board approval. It is open to question whether some form of corporate approval was in fact a condition precedent to conclusion of a binding commercial contract. Even if that were the case, an arbitrator would have to further find that there was some clear understanding among the parties that the imbedded agreement to arbitrate was also conditional in order to conclude that the dispute was not arbitrable. Nicaragua, 937 F.2d at 477. It is worth noting that following my jurisdictional ruling denying the Motion to Dismiss the parties entered into a binding settlement agreement. As it was not submitted to me, I am unable to say whether it includes an agreement to arbitrate in the event that one of the parties claims a breach of the settlement agreement.

18 Prior efforts by the Local to get agreement on a back-to-work agreement containing a hold-harmless clause on the no-strike issues was refused by Granite Rock, leaving the Local vulnerable to the claims asserted in the federal court action.

19 This meant that a substantial part of the strike activity fell within the effective date of the CBA. One of the issues that faces the Ninth Circuit as this case goes back under a remand order is that what is essentially a petition to compel arbitration is a court proceeding, not a jury matter under FAA, Sec. 4.

20 Although there remain a number of substantive claims to be resolved on remand, the rejection of the “hot button” issue for both of the parties at every level of this litigation makes one wonder why the Court took this case on in the first place. The arbitration issues would certainly not seem to justify certiorari on their own.
itself (a matter for court determination), and challenges to the validity of the contract as a whole (which are for the arbitrator to decide). 546 U.S. at __. The Granite Rock Court’s attempt to distinguish the purported “when” question from a “whether” question is vague and not well-articulated or supported by precedent, thus creating a false distinction that only blurs Buckeye’s quite meticulously-reasoned opinion. The Court states that, “For purposes of determining arbitrability, when a contract is formed can be as important as whether it was formed.” The Court finds this important because “thus determines whether the agreement’s provisions were enforceable during the period relevant to the parties’ dispute.” But, as the dissent points out quite crisply, this is the sort of question that arbitrators are commonly called upon to decide in contract disputes.

In so ruling the Court rejected all three of the Ninth Circuit’s bases for delegating the issue to the arbitrator. The first of those reasons was that the arbitration clause clearly covered the related strike claims. Starting with the obligatory statement that arbitration is a matter of the parties agreement to arbitrate certain matters, the Court cites Howsam v. Dean Witter Reynolds, Inc., 537 U.S. 79 (2002), a case questioning the proper forum in which to challenge the limitation period for bringing claims before the NASD tribunal. Justice Breyer, writing for the majority, held that the question is one for the arbitrator, not the court. Although not a “gateway” issue case, Howsam notes that the original gateway ruling in AT&T Technologies deals with cases in which a challenged arbitration provision does not delegate the arbitrability issue to a forum, and a court must therefore carefully determine whether a party is being forced to engage a forum to which it did not agree. Howsam also goes on to say that the Court has found many other situations in which the parties’ clear expectations were that the question of arbitrability would be decided by an arbitrator. This reaction in Granite Rock to the Ninth Circuit’s reasoning is the first step leading to the majority’s conclusion that the CBA’s arbitration clause did not encompass a contract formation dispute. Thus, contrary to all apparent precedent, the Court is saying that rather than engaging every assumption in favor of broad coverage of the arbitration clause, it chooses to assume instead that the question of the ratification date is not covered by the arbitration clause.

The Court in Granite Rock then proceeds to embrace one of several very questionable premises for its ruling. “These principles [about intent] would neatly dispose of this case if the formation dispute here were typical. But it is not. It is based on when (not whether) the CBA that contains the parties’ arbitration clause was ratified and thereby formed.” But the Court offers no explanation for why this distinction is material. As the dissent points out, and as we have seen in the Nicaragua line of cases, arbitrators deal with a wide range of contract formation issues every day. The Court attempts to frame this as critical because it affects the issue of whether the no-strike clause was in effect during the strike period. But other, similar, distinctions could just as easily raise the issue of where the contract was formed, since that might have a bearing on choice of law issues. One could also ask by whom the contract was formed, to get at issues of authority to bind the parties. Again, these are the sorts of questions that arbitrators are regularly called upon to decide, and such distinctions do not seem to be valid bases for a determination that the question is one for a court, rather than an arbitrator, to decide.

More troublesome yet is the Court’s refusal to acknowledge the uncontested fact that the parties specifically and explicitly made the CBA retroactive to May 1 – a date preceding the onset of the strikes. The majority dismisses Justice Sotomayor’s reference to this fact by stating that it was not timely raised and thus violates a rule of Supreme Court procedure. The majority also ignores the fact that the retroactivity provision was argued by the Local in the Ninth Circuit proceeding and referenced again in oral argument to the Supreme Court. Inasmuch as the contract, by its own terms, covers the entire period of the dispute, the odd distinction between whether it was formed and when it was formed becomes even more elusive. The result is that the Court appears to have created a false formation issue. In strained attempt to make this distinction, the Court does not seem to be advancing the underlying policy of the FAA in any meaningful way.

The majority then seeks to remove the entire formation issue from the broad coverage of the arbitration clause as written. It begins by again characterizing “these unusual facts” without offering any explanation as to what is so unusual about them. The parties have simply taken different positions about when an effective ratification took place – not particularly unusual in contract disputes. The Ninth Circuit saw it the same way, and held that the arbitrator could decide the case based on two basic principles. The first is that where the parties have agreed to arbitrate some matters pursuant to an arbitration clause,

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21 The courts refer to “gateway” issues as those basic threshold questions about whether a dispute can be considered arbitrable at all – i.e., whether there is a basis for asserting a right to arbitrate the dispute in question. Note that the CBA in Granite Rock does not appear to have language comparable to that found in the XYZ Rules, or other institutional rules or California Code of Civil Procedure Section 1297.161, with specific delegation of all issues, including validity, to the arbitrator, as well as clear severability of the arbitration agreement.

22 The Court in Howsam makes an observation that undercuts one of the realizations ignored by the majority in Granite Rock but clearly stated by Justice Sotomayor in a cogent dissent. The Howsam Court said: “Moreover, the NASD arbitrators, comparatively more expert about the meaning of their own rule, are comparatively better able to apply it. In the absence of any statement to the contrary in the arbitration agreement, it is reasonable to infer that the parties intended the agreement to reflect that understanding...And for the law to assume an expectation that aligns (1) decisionmaker with (2) comparative expertise will help better to secure a fair and expeditious resolution of the underlying controversy – a goal of arbitration and judicial systems alike.” 537 U.S. at 85.

23 Justice Sotomayor also noted Litton Financial Printing Div., Litton Business Systems, Inc. v. NLRB, 501 U.S. 190, 201 (1991), which recognizes that “a collective-bargaining agreement might be drafted so as to eliminate any hiatus between expiration of the old and execution of the new agreement.” This, of course, is exactly what occurred in Granite Rock.

24 See the Granite Rock dissent: “Given the CBA’s express retroactivity, the majority err in treating Local 287’s ratification-date defense as a ‘formation dispute’ subject to judicial resolution.” 130 S.Ct. at 2868 (Sotomayor, J., dissenting).
any doubts concerning the scope of arbitral issues should be resolved in favor of arbitration. The second principle is that of severability found in the FAA, Prima Paint and many other cases noted in the Ninth Circuit’s opinion. But Justice Thomas says, “Local, like the Court of Appeals, over-reads our precedents.” This is the start of a dissembling of prior rulings that raises important questions as to where our arbitration jurisprudence goes after Granite Rock.

Rejecting a line of cases cited by the Local, the majority states, That is not a fair reading of the opinions, all of which compelled arbitration of a dispute only after the Court was persuaded that the parties’ arbitration agreement was validly formed and that it covered the dispute in question and was legally enforceable . . . That Buckeye and some of our cases applying a presumption of arbitrability to certain disputes do not discuss each of these requirements merely reflects the fact that in those cases some of the requirements were so obviously satisfied that no discussion was needed . . . . In Buckeye, the formation issue of the parties’ arbitration agreement was not at issue because the parties agreed that they had ‘concluded’ an agreement to arbitrate and memorialized it in an arbitration clause in their loan contract.

130 S.Ct. at 2858.

It should be pointed out that at no time does the Court suggest that there is any question as to whether Granite Rock and the Local had concluded an agreement to arbitrate and memorialized it in their contract. To the contrary, the Court explicitly acknowledges that this is not disputed. Thus, the attempt to distinguish and, thereby, dismiss the clear holding in Buckeye, is difficult to comprehend. Buckeye, relying in depth on Prima Paint and Southland Corp. v. Keating, 465 U.S. 1 (1984), reiterates the severability rule and the proposition that only challenges to the arbitration clause itself – as opposed to the agreement as a whole – are appropriate for judicial determination of arbitrability. This is exactly the tack the Court took in deciding Rent-A-Center, West, Inc. v. Jackson, __ U.S. ___, 130 S.Ct. 2772 (2010) less than a week before issuing its ruling in Granite Rock. It is difficult to reconcile the Court’s handling of Buckeye and Rent-A-Center and Granite Rock in such a different manner so close in time.

The Court’s lack of cogent explanation for why the date of contract formation differs from all the other potential formation questions we have noted, is compounded by a footnote stating, “Our conclusions about the significance of the CBA’s ratification date to the specific arbitrability question before us do not disturb the general rule that parties may agree to arbitrate past disputes or future disputes based on past events.” Granite Rock, 130 S.Ct. at 2860 n. 11. But that is precisely what Granite Rock and the Local did in making the CBA retroactive to May 1, and excluding from the arbitration clause only three specific matters that are not involved in this discussion. They explicitly agreed in writing that a future dispute could be based upon past events by making the CBA retroactive to the end of the prior CBA. Based on the language of the quoted footnote, the majority seems to have created an arbitrability issue that does not appear to be presented by the facts of the case.

Finally, the Court, not content to reverse on all of the foregoing bases, chose to question whether the formation issue itself falls within the scope of the arbitration provision. The Court says, “The dispute here, whether labeled a formation dispute or not, falls outside the scope of the parties’ arbitration clause on grounds the presumption favoring arbitration cannot cure.” Without any explanation, the Court then states that the question of the ratification date, a question that goes to the CBA’s very existence [despite statements that neither party questions the existence of the CBA] cannot fairly be said to “arise under” the CBA. The Court says that even if the formation could be considered to “arise under” the CBA, a mandatory mediation provision in the CBA undermines such a conclusion. That proviso is similarly left to conjecture, as the Court fails to connect any of these concepts in any clear manner. According to Domke, and the large body of arbitrability presumption cases, issues will be deemed arbitrable unless “it is clear that the arbitration clause has not included them.” Domke, Section 12:02. No such clear intention exists under the facts of Granite Rock.26

Despite this lengthy additional effort to assay a place for Granite Rock in the otherwise linear and cogent body of case law on arbitrability, I am forced to say that the opinion makes little sense. Far from clarifying the parameters of arbitrability, it instead calls into question the meaning and future significance of those parameters. It leaves potentially uncertain all those many rules of arbitration that specifically delegate arbitrability questions to the arbitrator. It also causes us to question how the principle of severability and the concepts built upon Nicaragua might be met if they are brought before the current Court. Finally, it raises a question as to whether an arbitrator or a court should refrain from questioning the formation or validity of an overall contract, but ask only whether there is clear evidence of an agreement to arbitrate, in order to proceed in an arbitration forum. Although these issues call out for more clarity, the Court has instead given us uncertainty. If the Court truly believes that it is federal policy to encourage arbitration, rather than limit it, we must wonder why the Court would reach so far to place the issue of a


26 I believe the ruling which better expresses the policy of the FAA and prior Supreme Court rulings (as well as the legacy of Prima Paint), is found in Simula, where the court said: “This appeal presents the question of how broadly an arbitration clause containing the phrase ‘arising in connection with this Agreement’ should be construed. The district court held that it encompassed all disputes having their origin or genesis in the contract and granted appellee’s motion to compel arbitration. We affirm.” Simula, 175 F.3d at 718.
It is clear that both the Granite Rock Company and the ratification date exclusively in the hands of already over-burdened federal trial courts. The result seems more likely to drive more disputes into the courts that have routinely and effectively been resolved by arbitrators chosen by the parties for that purpose.

The Court’s notion that it was dealing with an unusual issue on the ratification date seems disconnected from the realities that arbitrators engage in on an ongoing basis. This decision gives the feel of law being shaped in a vacuum. The Court has repeated the touchstone proposition that arbitration is based upon the consent and intent of the parties. I would add that arbitration is also thus based upon the expectations of the parties. This is clearly emphasized in Mitsubishi. As anyone who has actually been responsible for making decisions about, and writing agreements for, arbitration knows, the realistic expectations of the parties are that future disputes are going to be arbitrated. That is why they consciously place an arbitration agreement in their contracts.27 It is clear that both the Granite Rock Company and the Teamsters Local anticipated that their disputes would be arbitrated. The Supreme Court emphatically recognized this reality in The Bremen v. Zapata Off-Shore Co., 407 U.S. 1, 12 (1972) when it observed that a contract fixing a particular forum for resolution of disputes

was made in an arm’s length negotiation by experienced and sophisticated business men, and absent some compelling and countervailing reason it should be honored by the parties and enforced by the courts…. [T]he forum clause was a vital part of the agreement, and it would be unrealistic to think that the parties did not conduct their negotiations, including fixing the monetary terms, with the consequences of the forum clause figuring prominently in their calculations.

“As was stated in Metro Industrial Painting Corp. v. Terminal Construction Co., 287 F.2d 382, 387 (2d Cir. 1961), ‘the purpose of the act [FAA] was to assure those who desired arbitration and whose contracts related to interstate commerce that their expectations would not be undermined by federal judges, or… by state courts or legislatures.’” Southland, 465 U.S. at 14. Regrettably, the Court has now given us a decision which does not realistically recognize those expectations, and instead applies tortured reasoning to cases whose lower court rulings hew to guidelines that the Court had wisely and clearly laid out in the past.

The FAA is a relatively general statement of Congressional policy (with some simple procedural rules set out), intended to nurture and support the use of arbitration in interstate and international commerce.28 In its most recent efforts to further define and flesh out the Act, the Supreme Court may have unwittingly confused, destabilized and impaired Congress’ core policy and purpose in creating the Act. Under such circumstances it seems an appropriate and necessary moment for the Congress to take a fresh look at how its own intentions and expectations through the FAA have evolved in the case law. Those decisions which have shaped arbitration policy in ways that support Congressional policy should be considered for adoption into a revised FAA. Those that defeat the policy should be clearly put to rest.

Considerations in Drafting: Early Focus, Delegation and Scope Are Critical

There are three principal issues involved in the creation of a contractual arbitration provision: (i) whether arbitration is desired at all, and when to address that choice; (ii) the so-called “delegation” questions defining the arbitrator’s authority to rule on arbitrability and jurisdiction; and, (iii) the scope of arbitral issues.

(i) Consider Arbitration as a Potential Forum Early in the Process

In most business dealings, negotiators will tend to focus on major commercial terms in the early stages of discussions and in the preparation of deal memoranda or draft agreements. Choice of forum issues tend to arise as afterthoughts or become important points only when a deal has failed to conclude or was concluded but has later gone sour, and the parties are seeking remedies. As we have seen, casual treatment of the question of where and under what rules disagreements are addressed may produce surprises that one or more parties may not be happy experiencing when a dispute subsequently arises. In-house corporate counsel (or other contract negotiators) need to determine early on in a business negotiation the issue of forum selection in the event the contracting process aborts, and to lay the groundwork accordingly. Likewise, it behooves outside advisors to counsel their clients on the importance of thinking through the arbitration issues even as they begin to consider new business dealings. This starts with the not-always simple issue of whether or not to adopt arbitration as the designated forum for dispute resolution.

Just as a specific choice of law provision will address the rule structure for future disputes, the designation of a particular forum or arbitral institution for dispute resolution may also serve to define a set of rules which, in themselves, affect issues such as authority to rule on arbitrability and the scope of the arbitration provision’s coverage. It would therefore be prudent to look carefully at both a specific designation of governing law as well as the language of the arbitration provision to assure that the choices are complementary to the desired result, i.e., whether the choice of law is favorable to the selection of a particular arbitration institution and its rules. As noted earlier, there may be

27 Admittedly, this may not be true for parties to whom contracts with arbitration mechanisms are given with no choice in the matter. It is for these situations that the proponents of the Arbitration Fairness Act now before the Congress have addressed the issue in a legislative context.

28 It was driven initially by a need to overcome hostility in the courts toward the arbitral process which was seen by the judiciary as an encroachment on its historical territory.
potential issues to consider on procedural as well as substantive matters concerning the interplay of state and federal law. The extent to which an arbitration clause can anticipate and can be negotiated so as to determine how those issues will be decided in future proceedings is open to some question as the law in this area is not stable. These choices may arise as part of the early contract negotiation process without being initially apparent, and counsel should identify and make clients aware of them as they begin the process of exchanging proposals and early-stage forms of agreement. Inasmuch as a focused approach to these issues is going to arise as soon as any form of agreement – interim or more formal – is exchanged, the nature of the communications among the parties deserves close attention. As seen from Am erico v. Euroco, the arbitration issue may often arise very casually, but often has substantial impact on the outcome of the dispute. To the extent that participants in the deal-making process have reservations about pinning themselves down to various choices of forum and law, they may want to consider explicitly stating in their written exchanges that all terms, including dispute resolution provisions, remain conditioned upon finalization of a full and formal written agreement.

(ii) Delegate Issues as Specifically Within the Authority of the Arbitrator

While courts often suggest that the question of whether a matter is clearly within the purview of the arbitrator is unequivocally a threshold issue for a court, I would submit that a survey of the cases makes this anything but clear and predictable. If a decision has been made to submit future potential disputes to arbitration, one would be well-advised to adopt the language used by most of the major arbitral institutions, which tends to track the language of CPP 1297.161 noted above. I am not aware of any reported case in which a specific, explicit delegation of authority of the arbitrator to rule on his or her jurisdiction has been rejected by a court. Bear in mind, however, that the matter of delegation of arbitral authority, and the delineation of the scope or range of issues that fall within the authority of the arbitrator to rule, are often expressed in one comprehensive arbitration clause. In drafting these provisions it is important to analyze each of these arbitrability issues with a clear focus and careful choice of language. We have seen that the attempt to use broad and general language may not be sufficient to assure the desired scope of authority.

(iii) Consider Defining the Scope of the Arbitrator’s Authority

As we have seen in Granite Rock, a broadly-worded arbitration clause is by no means certain to be honored and applied by a court, even with comprehensive, inclusive language employed. Thus, issues of who – court or arbitrator – should decide arbitrability, the inclusion or exclusion of any issue, including the formation, ratification/finalization, validity, enforceability or other application of the overall terms of the agreement, are subjects that might be wise to explicitly incorporate in the arbitration clause itself. After Granite Rock, the need for more specific delegation of authority to the arbitrator with respect to all issues that the parties expect to have arbitrated has become even more critical. However, one must also be cognizant of the current case law and Congressional exploration of certain subjects as possible exclusions from the arbitral forum, namely the issue of unconscionability and, potentially, contracts involving employment and consumer dispute-resolution mechanisms. If the drafter’s desire is to achieve the most comprehensive, inclusive arbitrability coverage, he or she should consider adding to the customary broad language of the arbitration clause language, such as, “any and all matters arising under, related to, growing out of, or otherwise pertinent to the subject matter of this agreement, including, but not limited to, all issues of any nature concerning the formation, ratification, validity, enforcement or breach of this agreement; save only those matters which, by law raise challenges specifically to this arbitration provision, and/or whose substantive subject matter has been removed from arbitral jurisdiction by statute.”

However, if the parties negotiating a commercial contract are only prepared to have disputes submitted to arbitration once the contract has been fully completed and executed, they would be well-advised to state that specifically in their negotiation communications from the very beginning. A failure to do so may well result in the application of arbitral jurisdiction under the principles that I have explored in this article. Similarly, negotiation communications might also address the question of where arbitrability is to be determined in the absence of a fully-detailed arbitration clause that would normally be the place to fix a venue, either explicitly or by reference to a body of arbitration rules of a chosen institution.

In light of the recent cases, arbitrability has become more of an unsettled question. The expressions of the parties’ expectations and intent must therefore be thought through carefully and expressed with precision.
Mediation in Afghanistan: Rebuilding Justice and the Rule of Law

By Kindra Mohr*

Abstract

Mediation practices have served as the bedrock for the administration of justice in much of Afghanistan; they will continue to flourish as the basis for dispute resolution in local communities in the future. This article posits that mediation will remain central to Afghan life primarily because of the country’s history and traditional foundations. Furthermore, mediation recognizes the practicalities of contemporary life in many parts of the country and the incapacity of the formal court system to administer justice effectively to a majority of Afghans. For these reasons, mediation practices must feature prominently in Afghanistan’s strategy to reconstruct its legal system and judicial institutions. While traditional Afghan mediation has its shortcomings, namely the exclusion of women, it could nonetheless still play an integral role in the government’s current rule-of-law reform efforts, especially if such modernization efforts acknowledge the importance of including women in mediation practices. Without developing a strategy that accounts for rural mediation practices, democratization efforts will likely fall short of establishing a legitimate and functional system of justice accessible to all Afghan people.

After three decades of conflict and war, Afghanistan is a country in search of peace and security. Over this period, Afghanistan has endured domestic strife, transnational threats, foreign occupation, and endemic corruption, all of which have debilitated government institutions and the rule of law. As a result, the Afghan people have relied almost exclusively on traditional, informal, community-based dispute resolution systems to cope with the absence of a legitimate and accessible formal judiciary. Since the fall of the Taliban in 2001, domestic and international efforts to reestablish the formal justice system have been slow and, in some ways, misguided. This has left the majority of the population with few alternatives to informal dispute resolution mechanisms, which have become embedded within the local practices in most of Afghanistan. Because these mechanisms have deep roots in Afghan culture and tradition, they are particularly essential for maintaining order during these periods of upheaval and unrest. Today, for example, mediation is widespread and forms the basis of justice and harmony within local, rural communities.

This article contends that mediation will continue to be the cornerstone of the administration of justice in Afghanistan well into the future, despite efforts to establish a more formalized system throughout the country. Thus, any rule-of-law reform plan should incorporate current mediation methods, as well as some new elements, in order to rebuild the foundations of the rule of law and a sustainable system of justice. Reformers should not aim to simply disassemble and replace traditional dispute resolution mechanisms with a formal system of justice; such efforts are likely to be fruitless and rejected in local communities where mediation is part and parcel of daily life. Instead, reformers should design and implement strategies that harmonize newly-created or reformed formal mechanisms with informal methods like mediation.

To provide a context for this argument, the article will first canvass the country’s history and recent developments, emphasizing the roles of both its formal and informal justice systems. In the second section, it will introduce some of the most common characteristics of mediation practiced today in Afghanistan. Third, it will provide three compelling reasons why mediation will remain an indispensable part of local Afghan justice and therefore should feature prominently in current and future reform initiatives: history and tradition, practicalities of contemporary life, and the incapacity of the formal system to administer justice.

The fourth section will address one of the fundamental flaws of local mediation practices – the exclusion and abuse of women – and posit that, by introducing new elements into the existing structure, the government and local communities can mitigate the effects of this flaw. Lastly, the article will conclude with some parting thoughts on the future of rule-of-law reform efforts and their relation to Afghan mediation practices. Mediation has served the Afghan people through the torments of war and political and economic disarray, and will continue to be the principle source of local conflict resolution. In order to establish a functioning and lasting system of justice that will reach all Afghans, the Afghan government, with continued assistance from the international community, should implement rule-of-law reform strategies that recognize the critical role that mediation plays in most of the country.

I. History and Recent Developments

Afghanistan has long possessed deep legal customs and a substantial body of laws and codes. Throughout its history, independent tribal communities developed a diverse system of traditional practices and customary law to resolve local disputes. As a centralized system of governance coalesced in the late 19th century, a formal legal system materialized mainly in urban areas, becoming the vehicle to administer justice and extend the reach of the state. During this time, informal traditional practices and the formal state-driven

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1 While other forms of informal dispute resolution exist throughout Afghanistan, this article will focus on local mediation practices.

system co-existed autonomously, although the government’s institutionalization of Islamic law, or sharia, would carry into the informal system.3

Soon thereafter, tension grew between the relatively new formal system and the pre-existing informal system, which was seen by the government as a rival in the country’s administration of justice. They not only competed in the application of law and custom, but they also had competing values: the formal system emphasized uniform rules and consistency in judgments, whereas the informal system, based primarily on customary laws, stressed fairness and equity among parties.4 By the middle of the 20th century, as the state’s power expanded, central authorities strove to subvert traditional practices, and the formal state-driven system gradually began to engulf the informal system.5 Nonetheless, given the geography of the country and the relative isolation of many rural settlements, these informal practices, such as mediation, survived at the local levels.6

By the end of the 1970s and through the 1980s, Soviet occupation had destabilized formal government institutions and created chaos throughout the entire country. Continued war and civil unrest took its toll on the formal judicial system, which over time had grown corrupt and illegitimate in the eyes of urban and rural Afghans alike.7 Violent conflict persisted, resulting in a civil war (1989-2001) that unraveled any remaining institutional capacity of the state and disintegrated the formal judicial system in the process.8 When the Taliban assumed power in the mid-1990s, it revamped the legal system and judiciary to fit its needs, destroying copies of secular and pre-Taliban codes and filling the judiciary’s ranks with religious adherents, which again left many Afghans wary of interacting with the formal system.9

Consequently, during this time, local communities revived informal dispute resolution mechanisms, most notably mediation, to provide some semblance of justice and order in the countryside. Traditional practices reemerged as tribal leaders, chosen by the disputing parties, gathered in ad hoc councils, known as shura or jirga, and served as fact finders and mediators to help solve local problems.10 Although the councils in some communities were subject to the pressures of the Taliban and regional warlords, there were those that remained loyal to local tradition and garnered the respect of community members.11

When the Taliban fell from power in 2001, the interim government, led by current-President Hamid Karzai, began the slow process of rebuilding the state and its institutions. The government adopted a constitution in 2004 and has since implemented new laws and legal training programs, reconstructed judicial buildings and prisons, and circulated legal materials.12 However, progress even on these projects has been modest at best and commitment to deeper rule-of-law reforms has been limited, as there has been a clear absence of donor coordination and long-term strategy for the judicial system as a whole. Until recently, other than the law enforcement sector, donors largely neglected other rule-of-law institutions. Only within the last few years, after the London Conference in 2006, has attention shifted toward a broader conception of rule-of-law reform and the puzzle on if or how to integrate a new formal system of justice with existing traditional dispute resolution methods.13

Thus, over the course of its history, Afghanistan has steadily developed, and come to rely on, an informal system to resolve disputes, largely out of necessity for lack of sustained, legitimate central governance. Despite the occasional “surges” in the formal administration of justice, mediation has remained a central component in the lives of those in local communities. The current government and the international community are now struggling with the challenge of addressing parallel systems of justice.

II. Common Characteristics of Mediation

Informal dispute resolution practices in Afghanistan are based on Islamic norms and customary law,14 which vary in composition by locality, and rest upon the principles of reconciliation, community harmony, and restitution.15 Mediation is the predominant practice for resolving civil disputes16 within rural communities, which make up nearly 80 percent of the country’s total population.17 Mediation in this context conforms to a common description that mediation practitioners identify as “a process in which an impartial third party acts as a catalyst to help others constructively address and perhaps resolve a dispute, plan a transaction, or define the contours of a relationship.”18

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3 AMIN TARZI, HISTORICAL RELATIONSHIP BETWEEN STATE AND NON-STATE JUDICIAL SECTORS IN AFGHANISTAN 7-9 (2006).
5 Id.
6 Id.
8 BARFIELD ET AL., supra note 4.
9 See NOJUMI ET AL., supra note 7.
10 BARFIELD ET AL., supra note 4, at 6-7.
11 NOJUMI ET AL., supra note 7, at 249-51.
14 Islamic law, or sharia, and customary law comprise distinct legal systems. In fact, they conflict on issues such as revenge, punishment, and family disputes. Informal dispute resolution mechanisms have roots in Islamic norms but not Islamic law per se. See BARFIELD ET AL., supra note 4, at 6, 12-13.
15 TOOMEY & THIER, supra note 11, at 3.
16 Although parties also use mediation in criminal matters, the scope of the article is limited to a discussion of civil disputes.
17 See BARFIELD ET AL., supra note 4, at 6-7, 11.
While specific techniques differ depending on regional and local traditions, current forms of mediation throughout the country generally share the same foundation and defining characteristics, and emphasize the importance of familial and local relationships.

First, one virtually universal feature of mediation in local communities is the mediator selection process. Disputing parties agree in advance on who will facilitate the process, which involves selecting among members of the community or even respected outsiders. Each party has the opportunity to choose a mediator and invite family or friends who they believe will support their case. The selected group of mediators traditionally consists of tribal leaders and elders (almost exclusively male) who form councils, referred to above as *shura* or *jirga*, when a dispute arises. Members of *shura/jirga* hold unique and well respected positions due to their knowledge of the parties, Islamic norms, and local customs, in addition to their ability over time to help maintain harmony within the community. Each disputant has the opportunity to choose a mediator and invite those who they believe will support their case. When the dispute is relatively common or involves a minor offense, the size of the *shura/jirga* can be relatively small. In contrast, if there is a complex issue at hand or a problem that could have extensive consequences for the community, as many as ten mediators may join the *shura/jirga*.19

Second, the disputing parties who participate in the mediation process almost always consist of men who come forth with an intra-community problem. Men are charged with representing the interests of females in their household. Women are largely absent from the process, although they may have more freedom to express their concerns to the family behind closed doors, depending on community and family dynamics. In some cases, female councils may convene for female disputants. However, this is not a common practice. As discussed below, the process tends to silence women’s voices and views, and thus they do not play a particularly conspicuous role.20

Furthermore, the disputing parties are traditionally members of the same local community or ethnic group. This appears to be mostly a result of mere pragmatism, given the complications associated with selecting unbiased mediators, as well as the variegation of customary laws, language, and norms throughout even neighboring regions of the country. Although there may be situations that call for inter-community mediation, such as the need to resolve a land dispute or calm growing ethnic tensions, by and large, mediation does not often involve members of different ethnic groups or communities. In fact, when a major inter-community conflict arises, communities have resorted to bloodshed to settle grievances, provoking government intervention to quell the violence.21

Third, the mediation process tends to follow a similar pattern in most local Afghan communities. Usually the process begins with an open exchange among the disputing parties and the mediators, who ensure that the dialogue fosters a sense of equality among the parties. Participants sit in a circle and speak in turn, each having a right to voice his thoughts.22 Mediators will question the parties about the dispute, and sometimes embark on their own fact-finding missions upon the parties’ requests. More experienced mediators desist from proposing recommendations until it appears that a positive solution – one that incorporates the interests and objections of the parties – is possible. The mediation process may entail one meeting or several over the course of months, and the parties may not resolve the disagreement at all.23

When disputants meet with the *shura/jirga* council, their participation in the mediation process is wholly voluntary, and the council refrains from imposing solutions or enforcing outcomes. Seldom is there social or financial pressure on the parties to reach an agreement; both the community and the council prefer to maintain the neutrality of the process and discourage imposed outcomes. Local communities view this as a core reason that the process is accepted.24

Since autonomy is fundamental to the mediation process, parties decide on a matter through their own personal will. Resolution depends entirely on the consensus of the disputants. They can signal their opposition to an agreement by departing from the circle and rejecting an invitation to return and participate further.25 Decisions are oral and non-binding (i.e., self-enforcing), but it is infrequent that parties diverge from the agreed outcome, given the consensual nature of the mediation process and the fact that parties regard their agreements as a part of their obligation to maintaining peace and order within the tribe or community.26

Fourth, an opportunity to contest or enforce the outcome under certain circumstances exists for mediation participants. This usually only occurs after the parties have reached an agreement and new evidence emerges about the disputed matter or regarding the legitimacy of the mediation process.

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19 ATTORNEY GEN. OFFICE OF THE ISLAMIC REPUBLIC OF AFG., JUSTICE SYSTEMS IN AFGHANISTAN 10 (2009); BARFIELD ET AL., supra note 4, at 7, 9; NOJUMI ET AL., supra note 7, at 249-52.
21 BARFIELD ET AL., supra note 4, at 7.
23 BARFIELD ET AL., supra note 4, at 7-9.
24 U.N. DEV. PROGRAMME, supra note 22; BARFIELD ET AL., supra note 4.
25 BARFIELD ET AL., supra note 4.
26 TOOMEY & THIER, supra note 11.
itself, or alternatively, if one party wishes to force the other to comply with the agreement. In the case where the contesting party seeks to “void” the earlier process, he is usually attempting to either clear his family’s name for refusing to abide by the agreement or renegotiate another settlement. Because parties come together voluntarily and can leave at any time, appealing to another authority is very infrequent and requires good cause. Nonetheless, in the rare instance that a disputant has reason to contest or enforce, he may turn to a larger group of elders and/or leadership from other clans within the same tribe to oversee the dispute resolution process or impose a “binding” community judgment. While a binding community judgment is still technically non-binding, the consequences of non-compliance are severe, and may include complete exile from the tribe. As a last resort in either scenario, the party can commence litigation through the courts, which record mediation decisions when they are finally settled in the formal system.

These four characteristics – the mediator selection process, disputing parties, the mediation process, and the opportunity to contest or enforce the outcome – are common features among the variants of the informal system. They serve as the conduits for sustaining relationships and promoting community reconciliation, harmony, and restitution. Given their commonplace throughout much of Afghanistan, they are likely to be a part of local communities for the foreseeable future. As the government undertakes rule-of-law reforms, it should be mindful of the history and respect that mediation has among a majority of the population.

III. Mediation Will Endure and Must Be Central to Current Reforms

A. History and Tradition
Perhaps one of the strongest, yet most simplistic, arguments for why mediation will continue to be the preferred mode of dispute resolution for a majority of Afghans, and thus should be incorporated into current reform efforts, is because it is an inherent part of Afghan history and tradition. Mediation and other informal dispute resolution mechanisms have existed for centuries, over time becoming a building block of social relationships and community stability. Communities have turned to mediation to resolve disputes through times of peace, centralized authoritarian rule, foreign occupation, and civil war, and Afghans have historically and systematically rejected the imposition of formal mechanisms. They see no reason to espouse a system that appears foreign and discordant with their traditions and customs when mediation has served them well. Political and legal studies indicate that where an existing practice of law (formal or informal) has become embedded within the norms of a community, it is highly likely to persist, and efforts to impose or “transplant” a different system without regard to this existing practice will ultimately fail.

One reason that the historical and traditional aspects of mediation will drive its continued practice is because they in part define tribal identity and sustain relationships that ensure tribal survival. One cannot underestimate the weight that local Afghans place on their ethnic and community heritage, such that exile or shunning is equivalent to a social death. Mediation is part and parcel of this identity because it integrates the core traditional values of reconciliation, community harmony, and restitution, which history has embedded into Afghan culture. In contrast to the state-driven system, which detaches dispute resolution from relationships, mediation seeks to restore and nurture them, reflecting the belief that relationships, whether familial or communal, are pillars to tribal existence and the sense of self. Unlike judges and those associated with the formal legal system, council members are trusted “insiders” who have prior relationships with the parties and a longstanding history with the community.

Moreover, mediation practices have been flexible enough to adapt to local idiosyncrasies, and yet hold fast to those fundamental values that are shared across ethnic divisions – a quality that is absent from the rigid formal system. Afghans are unlikely to renounce a dispute resolution mechanism that underscores their autonomy as individuals and as communities for one that is dictated from Kabul. Rather, because the practice of mediation carries with it the history and identity of the Afghan people, it will endure despite the imposition of a “reformed” formal system that nonetheless disregards this practice.

Another reason that history and tradition are significant relates to perceptions. History and tradition have shaped local views and attitudes toward the practice of mediation, as well as toward the formal system. These perceptions are deeply entrenched in local communities, and as with any engrained point of view,

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27 See U.N. DEV. PROGRAMME, supra note 22, at 93.
28 See id.
29 BARFIELD ET AL., supra note 4, at 10.
30 Id., at 7.
32 See U.N. DEV. PROGRAMME, supra note 22, at 96.
34 BARFIELD ET AL., supra note 4, at 7 n.6.
36 See BARFIELD ET AL., supra note 4, at 2.
37 See id., at 4, 5.
they are unlikely to change. In essence, these perceptions reflect a widespread sentiment that: (1) mediation is a respected community tradition and a fair, equitable, and legitimate means for resolving disputes, and (2) the formal judicial system is corrupt, slow, and inaccessible, and it fails to produce results that benefit both parties and the community overall.\(^{39}\) In fact, “[r]efusal to accept civil verdicts [in the courts] is common…[t]he informal system is much more popular because it is cheaper, quicker and more respected than the formal system for civil cases.”\(^{40}\) The findings of a recent United Nations Development Programme (UNDP) study and the research of the Sanayee Development Organisation (SDO) suggest that local perceptions, which developed over time through historical experience and tradition, will not only remain unchanged, but will also impede the reception of a formal system that does not account for rural practices.\(^{41}\)

The UNDP study, involving a sample of 2000 random men and women in 32 of the country’s 34 provinces,\(^{42}\) uncovered that a higher percentage of respondents felt that shura/jirga councils were effective, fair, and trustworthy as compared to the courts; more respondents also said they trusted tribal elders and the councils as compared to judges.\(^ {43}\) The survey also revealed that 78 percent of respondents saw elders as having the dominant role in resolving disputes.\(^ {44}\) In addition, 80 percent of participants responded that councils followed the local norms and values of the local people.\(^ {45}\)

The research of SDO supplements UNDP’s empirical data. Researchers found that “[t]he reputation of the courts is not high among the local population, [and] many people think of the formal judiciary as of [sic] a corrupt institution. So far, most people think that local councils rather than courts provide for a fair process.”\(^ {46}\) They also concluded that many rural communities will reject government interference in local dispute resolution processes because it jeopardizes their “long tradition” of autonomy and self-administration.\(^ {47}\) Afghans are far more likely today and in the future to rely on the council’s mediation practices than dispute resolution through state institutions. Without adequate measures to include mediation practices in current rule-of-law reform initiatives, they will be ineffective.\(^ {48}\)

History and tradition, as manifested through the Afghans’ sense of identity and their perceptions about mediation and the formal judicial system, will continue to play a powerful role in perpetuating the practice of mediation. To forgo the mediation process at the local level for the formal system is perceived as an abandonment of community values and one’s ethnic heritage. Thus, Afghans will cling to a process that they know and trust, and will distance themselves, as history has shown, from the formal system if it is divorced from their practices. To achieve effective and sustainable rule-of-law reforms, the government must first have a vision for joining informal practices with the formal system.

### B. Practicalities of Contemporary Community Life

Aside from the historical and traditional bases, there are several reasons why mediation is particularly suitable for the practicalities of contemporary life in Afghan communities, and thus why it will continue to thrive. Admittedly, other informal mechanisms may be equally effective in some situations, such as party negotiations, resolutions by community consensus, or various forms of arbitration by shura/jirga councils; however, because of the prominence that mediation has enjoyed in local history and tradition, it is perhaps a more obvious choice for settling civil grievances. While the practical reasons discussed here are by no means exhaustive, they provide a window into why mediation continues to be vital to dispute settlement today. Three of these reasons are: (1) the types of disputes in contemporary local communities; (2) local education levels; and (3) poverty.

First, the types of disputes that one encounters on the ground today in Afghan communities are remarkably similar to those that existed throughout the development of local mediation practices. The two most common civil conflicts today (and historically) are property disputes and family grievances.\(^ {49}\) Other routine conflicts, such as business partnership and small-scale commercial disputes, which primarily affect the local economy, also have important social consequences on a community.\(^ {50}\) Communities adopted mediation techniques to respond to these disputes because, at their core, they involved issues that could threaten the stability and viability of tribal life. Mediation allowed the disputants to search for an agreeable remedy together – a benefit not available in the formal system – and restore intra- (or occasionally inter-) community harmony and relationships. While the specific facts of the disputes and the circumstances surrounding them have changed with time, the central issues at stake today closely resemble those for which mediation was originally developed.\(^ {51}\) Given that these conflicts will continue to be commonplace in community life, any reforms should account

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\(^{39}\) LAUREL MILLER & ROBERT PERITO, ESTABLISHING THE RULE OF LAW IN AFGHANISTAN 5 (2004); See EL SAMAN, supra note 12, at 20, 22.

\(^{40}\) BARFIELD, supra note 31, at 1.

\(^{41}\) See EL SAMAN, supra note 12, at 12-24; U.N. DEV. PROGRAMME, supra note 22, at 95-100.

\(^{42}\) U.N. DEV. PROGRAMME, supra note 22, at 10.

\(^{43}\) Id., at 95-96.

\(^{44}\) Id., at 99.

\(^{45}\) Id., at 95.

\(^{46}\) EL SAMAN, supra note 12, at 36.

\(^{47}\) Id.

\(^{48}\) Id., at 35.

\(^{49}\) INT’L LEGAL FOUND., supra note 20, at 16, 29, 45.

\(^{50}\) BARFIELD ET AL., supra note 9, at 12; U.S. AGENCY FOR INT’L DEV., FIELD STUDY OF INFORMAL AND CUSTOMARY JUSTICE IN AFGHANISTAN AND RECOMMENDATIONS ON IMPROVING ACCESS TO JUSTICE AND RELATIONS BETWEEN FORMAL COURTS AND INFORMAL BODIES 8, 22 (2005).

\(^{51}\) Id.
for the fact that mediation has been and continues to be a successful tool in resolving grievances and promoting local peace.

Conflicts over property compose the largest portion of disputes in local communities. These disputes consist of disagreements over unrecorded boundary lines, tribal rights to individual plots, limitations on land usage (e.g., specific property delineated for commercial, residential, agricultural, or religious uses), and trespass of roaming livestock.54 In addition, in the aftermath of Taliban rule, local communities have experienced a rise in property disputes related to the return of previously confiscated land.55 Recent studies reveal that a majority of Afghans still settle property disputes with shura/jirga councils,56 likely because council members are familiar with land divisions and inheritance agreements that largely go unrecorded.

Mediation has also maintained a principle role in family disputes. “Internal family disputes are highly sensitive in Afghanistan’s insular culture, and families prefer to resolve them at the local level, often within their own extended network.”55 Family conflicts cover marital and sibling disputes, generational differences, and even friction between close friends who consider themselves as family.56 Female shura/jirga councils may convene for conflicts between women in the community, however, women struggle to find their voice in other kinds of intra-family disputes.57 Nonetheless, today, as in the past, community members turn to mediation because they wish to treat these matters as private within their network and avoid the public court system.58

Furthermore, shura/jirga councils are often involved in resolving local commercial disputes through mediation.59 The councils help establish, amend, and dissolve contracts, and settle labor disputes as well as issues related to business partnerships, loans, and financial credits.60 Members of the business community have often turned to informal dispute resolution mechanisms because of the widespread familiarity with the shura/jirga process, which is seen as reliable and efficient. Local entrepreneurs trust councils because they have the ability to select council members who have no economic or personal stake in the outcome of a given commercial matter.61 This neutrality provides a sense of fairness in the process and relieves tensions and discord between employers and employees and within the business community as a whole. Moreover, the corruption and backlogs that plague the courts have deterred businesses from participating in the formal judicial system.62 These inefficiencies add significant transaction costs that local businesses cannot afford.

Second, the realities of contemporary local life in terms of education and literacy lend themselves to informal dispute mechanisms like mediation. Given the improbability that there will be a dramatic improvement in rural education levels in the short or medium term,63 disputants will rely on mediation practices to resolve their grievances well into the future, especially if the reformed formal system excludes mediation and the use of shura/jirga councils.

Some reports approximate that 85 percent of Afghans are illiterate, with even starker rates in rural areas.64 Few men in rural communities have received a basic primary education, if at all, and studies estimate that less than 10 percent of all Afghan women have attended a primary school at some point.65 While there has been a recent increase in the number of children attending schools in some regions, the attendance rate for girls is far less than for boys, and “schools for boys are primarily religious and do not prepare the boys for an economically active future or to attend higher levels of schooling.”66 In many rural communities, there is no formal schooling, and where it does exist, teachers are ill-prepared and un/underequipped to provide a meaningful education.67

These startling facts and statistics illustrate in part why tradition-based, oral dispute resolution through mediation is so widespread in rural Afghanistan today. Unless mediated disputes reach the courts, virtually all of them are unrecorded. Illiteracy plays a key role in deterring rural participation in the formal system, which requires extensive paperwork and a willingness to bear through the complexities of an unknown process.68 This is compounded by the natural discomfort that most rural Afghans feel about the rigid, sophisticated procedures in the courts and their lack of emphasis on reparation and forgiveness. Furthermore, ordinary rural
Third, poverty defines contemporary rural life in Afghanistan and the formal judicial system prohibitively expensive. The per capita gross domestic product (in purchasing power parity terms) for Afghans was only $968 in 2005, and Afghanistan has one of the worst rankings in terms of the global human poverty index. While currently there are no statistics on the costs of pursuing formal litigation for average rural Afghans, the field research available indicates that “[t]he costs caused by formal procedures are a crucial aspect for most people…and the ongoing increase of living costs probably provides more reason not to refer to the courts.” In contrast, mediation through shura/jirga councils is often free or only requires a small fee. Hence, formal litigation is hardly a cost-effective and efficient alternative to going to court. Considering poverty levels and the low costs associated with shura/jirga councils, local Afghans have no incentive to initially bring their grievances through the formal system. Unless reforms incorporate mediation and perhaps provide legal assistance, there will be little movement toward the courts.

C. Incapacity of Formal System
In addition to factors relating to history and tradition and the practicalities of life in rural Afghanistan, the incapacity of the formal system to administer justice serves as yet another explanation for why mediation will remain the bedrock of rural dispute resolution. As stated in a recent report by the United States Institute of Peace, “since the fall of the Taliban little progress has been made toward building a functioning justice system.” Given the judiciary’s current state of disarray and unconvincing efforts to introduce rule-of-law reforms, Afghan policymakers and the international community should recognize the functionality and advantages of combining formal reforms with local mediation practices.

The inadequacies of the formal system are substantial, and in conjunction with the barriers discussed above, they hinder rural involvement with the judiciary. First, courts are generally limited to urban areas. This presents consequential challenges to physical access to the formal system. Despite funding for court-related infrastructure projects, minor improvements have only occurred in Kabul and in some of the larger cities. Where courthouses exist in remote areas, they are dilapidated and have no space to perform even basic administrative duties. Filing systems and reference materials, for example, are mere luxuries. Furthermore, the government has yet to develop a country-wide court management system to facilitate communication between urban and rural judicial authorities; currently, it may take months or more to transmit legal information across provinces, adding to an already delayed process. Without physical access to a local functioning court system (or incurring great expense to reach an urban courthouse), the informal council gatherings for mediation sessions are the most plausible mechanisms for rural dispute resolution.

Second, the formal legal system lacks a sufficiently trained cadre of legal professionals and support staff who have adequate knowledge of formal laws and codes as well as a thorough comprehension of customary law and informal practices. This not only reinforces a perception of illegitimacy, but it also undermines the judiciary’s ability to operate at even a basic level. As with judicial infrastructure projects, the Afghan government and international development organizations have allocated resources to improving the quality and professionalism of the legal community, but the results are minimal at best. Judicial appointments are frequently based on “personal or political connections without regard to legal training or other qualifications…and judges routinely make decisions without reference to the written law.” Judges, even those with long careers on the bench, have virtually no experience writing opinions, studying legal terminology, or working with defense advocates, of which there are very few. The system of legal education is very poor, as there is no national judicial training center, and universities lack the faculty, resources (including libraries, administrative staff, and facilities), and broad range curriculum to carry out an effective degree program. If and when the government turns to deeper rule-of-law reforms that include an overhaul of the legal education system, it should use the opportunity to

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69 Id., at 61-67; BARFIELD ET AL., supra note 4, at 20, 23.
70 U.N. DEV. PROGRAMME, supra note 22, at 19. The human poverty index accounts for deprivations of basic human needs, considering barriers to health, a reasonable standard of living, and a lack of education and reading skills.
71 EL SAMAN, supra note 12, at 36.
72 Id., at 37.
73 MILLER & PERITO, supra note 39, at 5.
74 Id., at 8-9.
75 Id.
76 Id., at 5-6.
78 MILLER & PERITO, supra note 39, at 5.
79 NOJUMI ET AL., supra note 7, at 218.
80 MILLER & PERITO, supra note 39, at 5.
81 Id., at 5, 10; U.N. DEV. PROGRAMME, supra note 22, at 71-72.
82 J. ALEXANDER THIER, supra note 71; U.N. DEV. PROGRAMME, supra note 22, at 71.
develop a knowledge base on rural mediation practices and to invite participation in the process by local councils. Without this development and interaction, rural communities will maintain the status quo.

A third defect of the formal system that contributes to its operational incapacity is the disorganized nature of existing laws, which in part has led to a sizeable gap between the written law and its application. Many legal texts were destroyed in the course of three decades of war, and as a result, there are considerable overlaps and contradictions within written laws that remain in effect, as well as between written and customary law. Without a clear set of rules, the formal legal community has responded by either selectively choosing which laws to apply or ignoring them altogether, creating a haphazard and unpredictable administration of justice that local communities avoid at all costs. In addition, recent legal reforms have primarily focused on commercial law, which the government has justified as a priority in order to attract investment and business development. This policy decision, however, disregards the law and practices that govern a majority of disputes between Afghans. It also ignores the need to systematize the entire legal system if Afghanistan is to promote the rule of law and access to justice for all Afghans. As a result, the formal system in its current state will not take hold in local communities, which, for all intents and purposes, already have a functioning and reliable mediation system. As the government undertakes future reforms, it should turn to the benefits of rural mediation and construct a system that draws from both customary and formal law in an organized manner.

IV. Fundamental Flaw of Local Mediation Practices: Exclusion and Abuse of Women

Thus far, this article has argued that local mediation practices are likely to persist in Afghan communities, and if current rule-of-law reforms are to take root throughout the country, they must incorporate mediation into the new legal structure. However, this is not to suggest that local mediation practices are without fundamental problems. The fourth section of this article discusses one of the major flaws of local practices: the exclusion and abuse of women through the mediation process. While there are arguably many shortcomings associated with local mediation practices, the disempowerment of women is a principal failing of the informal system.

Male-dominated traditions and norms govern daily life in Afghanistan, and have historically denigrated women within rural society. These traditions have instilled notions of gender inequality and the acceptance of the abuse of women, which appears in the practice of mediation. Despite the occasional assembly of female councils, women are generally prohibited from participating in the mediation process, meaning that they are wholly dependent on male family members to represent their interests in the traditional shura/jirga gatherings. The system provides no recourse for women to challenge their subjugation, which can manifest itself in domestic violence, servitude, and forced and/or underage marriages. This is not simply a matter of women choosing not to assemble on their own; the male-dominated rural culture dictates the rare terms and conditions on which a female council can convene. Because these practices deprive women of a voice in local disputes, it can fail to deliver meaningful justice to nearly 50 percent of the population.

In addition to the denial of female participation in the traditional mediation process, mediation can lead to resolutions that violate the basic human rights of women and girls, who have no ability to contest these outcomes. The abuse of women through mediation outcomes can range from subtle to severe, depending on the community and its customs. A handful of communities still settle grievances from subtle to severe, depending on the community and its customs. A handful of communities still settle grievances through the practice of “bad,” an Afghan word describing the transfer of a family’s daughter or female relative to the victim’s family. In other rare instances, when a girl refuses to enter into a forced marriage, the disputing families may agree to exile her.

For these reasons, there has been some strong opposition to rule-of-law reforms that feature local mediation practices. Opponents have suggested dismantling local practices in their entirety and replacing them with a formal system that upholds international human rights standards and gender equality. The exclusion of women and their abuse through mediation practices and outcomes is an inexcusable defect of the informal system. However, this deficiency can be mitigated through the implementation of reforms without attempting to destroy local practices.

Rule-of-law and development practitioners working with women’s groups and local communities on the ground have recommended a number of reforms that would potentially reconcile the negative effects of mediation in local communities. Despite existing cultural norms, their research

82 MILLER & PERITO, supra note 39, at 9.
83 Id.
84 Id.
85 NOJUMI ET AL., supra note 7, at 218-20.
86 ATTORNEY GEN. OFFICE OF THE ISLAMIC REPUBLIC OF AFG., supra note 20, at 10; BARFIELD ET AL., supra note 4, at 17; EL SAMAN, supra note 12, at 32; INT’L LEGAL FOUND., supra note 20, at 8; TOOMEY & THIER, supra note 11, at 2; U.N. DEV. PROGRAMME, supra note 22, at 97; Wardak, supra note 38, at 330-31, 338.
87 BARFIELD ET AL., supra note 4, at 9, 12, 17; EL SAMAN, supra note 12, at 33; INT’L LEGAL FOUND., supra note 20, at 8.
90 EL SAMAN, supra note 12, at 25.
91 U.N. DEV. PROGRAMME, supra note 22, at 97-99.
revealed that a majority of rural Afghans would actually support change in the treatment and status of women, yet many did not know how to undertake such a transformation.92 The following descriptions provide a brief overview of the reform possibilities under discussion.

One proposal is to leave the local process in place and provide avenues for women to bring direct legal action through the reformed formal system. This would fall under a broader reform measure to create a hierarchical legal structure in which the first-instance and appellate levels of the formal system would trump informal outcomes, enabling women to settle disputes formally and enforce court decisions at the local level (assuming the development of local enforcement mechanisms).93 A second recommendation is to expose more women to the role of shura/jirga council members and train them on mediation practices so as to amplify their voice in the dispute resolution process. This may also involve holding a series of community meetings to negotiate the scope of female council members and to educate all sides on the benefits of gender equality.94 A third reform proposal would involve the introduction of local gender-mixed human rights panels throughout the country, that would work alongside council members (male and female) to ensure that all have access to mediation and that resolutions respect individual human rights. If panel members find that there has been an abuse, the government could require that they notify a regional human rights court and enforcement unit that could then take action.95

These suggested reforms are not overnight solutions, nor will they go unchallenged; the inclusion and equality of women will take considerable time and require local support. They will also involve parallel reforms to rebuild rule-of-law institutions and physical infrastructure in order to make these proposals effective in practice. Furthermore, as in the past, without local input and involvement in the reform process, it will fail to produce fruitful results. The reform approach must go beyond legislation or top-down decrees, and it must include the voice of local communities in order to be sustainable. Nonetheless, the aforementioned recommendations illustrate how the exclusion and abuse of women in the mediation process is not a fatal flaw of the entire informal system, and that there is merit in developing the means to mitigate the negative aspects of mediation practices. Thus, in recognizing that the informal system is an essential part of rural life, the government should not only seek ways to incorporate it into reforms, but it should also seek solutions that will address the failings of local mediation practices.

V. Conclusion

This article has argued that mediation will continue to thrive throughout much of Afghanistan, serving as the foundation for dispute resolution in local communities. Rural history and tradition, the practicalities of contemporary rural life, and the incapacity of the formal system to administer justice are some of the underlying factors that explain why mediation will remain a viable rural institution. Overall, mediation has and does promote the fundamental principles of reconciliation, community harmony, and restitution that govern community relationships and thus enhance tribal survival. For these reasons, it is essential that current and future rule-of-law reforms incorporate elements of local mediation practices into the broader plan to overhaul the legal and judicial systems in the country.96 While these practices are not without serious imperfections, namely the role of women in mediation, reformers can remedy such defects with the support of local communities through a number of suggested reforms.

One of the main challenges facing Afghanistan today is the growing divide between the “re-emerging” formal system of justice and existing informal shura/jirga practices. As the Afghan government and international community turn their attention toward deepening the rule of law and enhancing the institutional capacity of the state, they will need to devise strategies to bridge this divide with the support of local communities. Any reform plan must recognize, however, that “Afghan law will have to be supplemented to reflect respect for informal mechanisms.”97 Building the relationship between mediation practices and a reformed formal system will be essential to ensuring lasting harmony, increasing access to justice, and developing relationships between the state and the Afghan people.

This article highlighted many of the issues that illustrate the importance and value of mediation to the majority of Afghan people, and serves as a starting point for dialogue among policymakers about how to approach and implement rule-of-law reforms that address these dual systems of justice. Mediation practices have emerged from the tumultuous political and social upheaval of the last 30 years as a viable local institution, and will continue to dominate traditional notions of justice in rural Afghanistan. In order to strengthen the rule of law throughout the country, local mediation practices must play a central role in the government’s reform efforts. Without this emphasis, these efforts will likely fall short of developing a functional system of justice that will be legitimate and accessible to all Afghan people. ■

92 EL SAMAN, supra note 12, at 33.
93 See U.N. DEV. PROGRAMME, supra note 22, at 98-100.
94 See NOJUMI ET AL., supra note 7, at 95.
95 See Wardak, supra note 38, at 337-388.
96 The author acknowledges and applauds the current work of many rule-of-law practitioners and development organizations that are striving to create reforms that recognize the role of informal dispute resolution practices.
97 BARFIELD ET AL., supra note 4, at 23.
E-Discovery in Cross-Border Litigation: Taking International Comity Seriously

By Edmund M. O'Toole and David N. Cinotti*

With the possible exception of civil jury trials, no feature of the U.S. legal system is treated with as much apprehension abroad as pretrial document discovery. Most other national legal systems do not permit the kind of party-conducted and intrusive pretrial document discovery that U.S. litigators believe is essential to a full and fair settlement of disputes. Other countries restrict or prohibit parties from obtaining documents and often place pretrial investigation in the hands of judges. Differing fundamental views on the nature of state sovereignty and the proper balance of competing values in dispute resolution account for these differences in practice. The divergent value judgments have long been apparent in cases involving foreign litigants or witnesses in U.S. courts and have led foreign states to object to executing requests for documentary evidence for use in U.S. proceedings, sometimes frustrating the effective functioning of the Hague Convention on the Taking of Evidence Abroad in Civil and Commercial Matters.1 But the gulf between the United States and other countries when it comes to discovery practices has further widened with the rapid expansion of e-discovery in the United States.

This article discusses the ways in which the discovery of electronically stored information (“ESI”) poses special challenges to foreign litigants (both parties and nonparty witnesses) in U.S. courts – who are often stuck between conflicting legal obligations – and strains the channels of international judicial cooperation. We suggest that international comity, which the Supreme Court has explained should play a prominent role in district courts’ regulation of international discovery and should have heightened application when it comes to requests for ESI because unfettered e-discovery is so offensive to many foreign legal systems’ concepts of fairness, privacy, and sovereignty. Faithful adherence to comity would lead more judges to order e-discovery from foreign nationals through the Hague Evidence Convention rather than the Federal Rules of Civil Procedure. This would allow foreign states to subject foreign litigants in U.S. proceedings to conflicting national rules on discovery; explains how the Federal Rules of Civil Procedure generally favor truth-seeking over other interests such as privacy, cost-containment, and sovereignty; and outlines how other nations’ balancing of these interests can subject foreign litigants in U.S. proceedings to conflicting legal obligations. Part II discusses the principle of international comity and its application to discovery disputes. Finally, Part III outlines the considerations that courts should take into account when deciding whether to order a foreign litigant to produce ESI located abroad.

I. The Nature of the Conflict: E-Discovery and Foreign Law

The evolution of rules of evidence and procedure has required rulemakers to balance often competing values. Pretrial document discovery obviously advances the truth-seeking function; the parties are required to produce to one another requested documents bearing on the strengths and weaknesses of their claims and defenses. A system that favors truth-seeking above all else would provide for broad disclosure of facts and evidence and would permit few privileges to prevent such disclosure. The U.S. civil-litigation system has developed in accordance with this model. Other systems, however, put greater emphasis on values such as the privacy rights of companies and their employees and what might be called “cost-containment”2 – protection from the sometimes enormous costs associated with strict rules to preserve, locate, and produce in litigation all potentially relevant documents. In addition, U.S. discovery orders and party-conducted discovery might offend other nations’ views of sovereignty, including, in civil-law jurisdictions, the central role played by the court or investigating magistrate. All three of these interests – privacy, cost-containment, and sovereignty – can come into conflict with the U.S. system’s emphasis on truth-seeking that allows virtually unbridled access to vast amounts of ESI.

A. The U.S. System Favors Truth-Seeking Over Other Interests

The baseline rule of the U.S. evidentiary system is that “the public...has a right to every man’s evidence.”3 As the U.S. Supreme Court has stated, the “exceptions to the demand for every man’s evidence are not lightly created nor expansively construed, for they are in derogation of the search for truth.”4 Accordingly, U.S. discovery rules are designed

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3 Jaffee v. Redmond, 518 U.S. 1, 9 (1996) (internal quotation marks omitted).

for the parties to obtain the fullest possible knowledge of the issues and facts before trial.” Privileges to prevent disclosure are therefore limited under U.S. law.

This general preference for open discovery applies to ESI. Pursuant to Rule 26, “[p]arties may obtain discovery regarding any nonprivileged matter that is relevant to any party’s claim or defense – including the existence, description, nature, custody, condition, and location of any documents or other tangible things and the identity and location of persons who know of any discoverable matter.” Discovery requests need only be “reasonably calculated to lead to the discovery of admissible evidence.” Rule 34 of the Federal Rules of Civil Procedure was amended in 2006 to “confirm that discovery of electronically stored information stands on equal footing with discovery of paper documents.” Parties are not merely required to produce ESI and other documents that they physically possess; Rule 34 requires production of documents in a party’s “possession, custody, or control,” which under some circumstances has been held to reach a party’s related companies located abroad. Rule 45 also provides that parties may seek ESI from nonparties.

Recognized privileges for withholding documents and ESI under U.S. law are limited. A general right to privacy is not among them, and business or trade secrets are ordinarily not shielded from production, though courts may limit disclosure beyond the parties and/or counsel in the litigation.

Although U.S. courts have the power to protect parties and nonparties from unduly burdensome requests for e-discovery, the liberal federal disclosure rules, obligation to preserve evidence, and rapid expansion of modes of electronic communication – such as e-mail, text messaging, and instant messaging – combine to make U.S. e-discovery expensive, intrusive, and time-consuming, especially for business and governmental entities that have large amounts of data. As Judge Posner has commented, “[w]ith the electronic archives of large corporations or other large organizations holding millions of emails and other electronic communications, the cost of discovery . . . has become in many cases astronomical. And the cost is not only monetary; it can include . . . the disruption of the [entity’s] operations.”

Due to its enormous costs, litigants, litigators, judges, nonprofit entities, and other stakeholders have expressed dissatisfaction with e-discovery in the United States. According to the Sedona Conference:

The costs associated with adversarial conduct in pre-trial discovery have become a serious burden to the American judicial system. This burden rises significantly in discovery of [ESI]. In addition to rising monetary costs, courts have seen escalating motion practice, overreaching, obstruction, and extensive, but unproductive discovery disputes – in some cases precluding adjudication on the merits altogether . . . .

Other groups have expressed similar views. In May 2010, the Federal Judicial Conference Advisory Committee on Civil Rules sponsored a conference on proposed amendments to the Federal Rules of Civil Procedure at Duke Law School to which it invited representatives from five legal organizations.

Many of these organizations expressed concern with the costs associated with e-discovery. The costs of modern discovery also contributed to the Supreme Court’s decision in Bell Atlantic Corp. v. Twombly to narrow its interpretation of the pleading requirements to survive a motion to dismiss.

Given these acknowledged problems with the U.S. e-discovery system, it is not so surprising that other national legal systems take into account, and even favor, values other than truth-seeking when it comes to disclosure of documentary evidence.

B. Other Nations Put Greater Emphasis on Different Values

Truth-seeking is not necessarily the predominant value driving other nations’ procedural rules. For example, English procedural rules emphasize proportionality in pretrial disclosure of information. Litigants must show that requested documents are directly relevant to the case, and requests for

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6 FED. R. CIV. P. 26(b)(1).
7 Id.
8 Id. RULE 34(a) advisory committee’s notes to 2006 amendment.
10 See FED. R. CIV. P. 45(A)(1)(C), (3)(d).
11 See id. RULE 26(C).
12 See id. RULE 26(b)(2)(B)-(C). Id. (c), 45(c).
14 The Sedona Conference, Cooperation Proclamation, 10 SEDONA CONF. J. 351, 331 (2009).
16 See id. at iii (stating view of the ABA Litigation Section that advances in communications and information storage “have increased exponentially the costs and burdens on the litigants, particularly defendants who must preserve, identify, review for privilege and produce relevant electronic data”), iv (stating view of New York City Bar Federal Courts Committee that “[c]ivil litigation has become too cumbersome, expensive and time consuming, and the exponential growth of [ESI] over the past decade has simply added strains to an already overburdened system”), 1 (stating view of American College of Trial Lawyers that courts rarely apply proportionality in discovery rulings “because of the longstanding notion that parties are entitled to discover all facts, without limit”), 26 (stating view of Lawyers for Civil Justice that “the repeated efforts to address the catastrophic costs, burdens, and abuses of discovery through judicial intervention . . . ha[ve] not solved to the problems”).
18 See id. at 558-59 (holding that district courts may “insist upon some specificity in pleading before allowing a potentially massive factual controversy to proceed,” citing statistics showing that discovery accounts for as much as 90% of litigation costs in federal cases that make it to discovery, and noting “the common lament that the success of judicial supervision in checking discovery abuse has been on the modest side” (internal quotation marks omitted)).
information to third parties must identify specific documents. Civil-law jurisdictions are even more limited in the amount of discovery permitted, which dramatically reduces the costs and burdens on litigants. These rules flow from the civil-law view that “[i]t is for the party to the litigation to offer evidence in support of its case. Should the other side require information, the burden is upon them to be able to know and identify it.”

Two important values other than truth-seeking apparent from these more limited procedural rules are the privacy of litigants, witnesses, and third parties, and economic efficiency or cost-containment. A third competing interest also arises in international litigation – territorial or judicial sovereignty. All nations have an interest in protecting their nationals from the imposition of unreasonable burdens by a foreign sovereign. Civil law takes an especially dim view of foreign discovery orders because the investigation of civil claims and defenses is a public, not private, function in the civil-law system. A conflict can arise between the obligation of a party or nonparty to produce documents located abroad in U.S. proceedings because of other nations’ objection to the burdens and costs and burdens on litigants. These rules flow from the civil-law view that “[i]t is for the party to the litigation to offer evidence in support of its case. Should the other side require information, the burden is upon them to be able to know and identify it.”

As recognized by the E.U. Article 29 Working Party, established as an independent advisory board under Article 29 of Directive 95/46, “[t]here is tension between the disclosure obligations under U.S. litigation or regulatory rules and the application of the data protection requirements of the EU.” This tension is exacerbated when it comes to ESI because there is simply more personal data to store and hence to seek in a discovery request. Sensitive data, such as bank account information, personal identification numbers, credit card numbers, and healthcare information, are all likely to be found among a company’s ESI.

In order to search for and collect personal data in response to a U.S. discovery request, persons subject to the Directive must either obtain the consent of those whose data will be transferred, show that processing the data “is necessary for compliance with a legal obligation to which the controller [of the data] is subject,” or demonstrate that processing of the data “is necessary for the purposes of the legitimate interests pursued by the controller or by the third party or parties to whom the data are disclosed, except where such interests are overridden by the interests for fundamental rights and freedoms of the data subject.” Consent is not always possible when the data pertain to lower-level employees or third parties such as vendors and customers. The Working Party has suggested that in many cases consent will not be a possible option for processing data in response to a U.S. discovery request.

The Working Party also noted that “[a]n obligation imposed by a foreign legal statute or regulation may not qualify as a legal obligation by virtue of which data processing in the EU would be made legitimate.” The Working Party left open the possibility, however, that in some cases those subject to the Directive could justify compliance with a U.S. discovery order by reference to this provision. Compliance in order to defend or prosecute a case in the United States might also qualify as a “legitimate interest[ ]” under the Directive, but processing personal data pursuant to this exception can only occur if the requested party’s interest is not outweighed

20 See, e.g., Boll & Wheatley, supra note 2, at 6 (noting that under German law “parties’ right to information is sharply limited, there are no depositions, and only the court may order the production of documents”).
22 Art. 29 Working Party Report 158.
23 See, e.g., Convention for the Protection of Human Rights and Fundamental Freedoms art. 8, Nov. 4, 1950, C.E.T.S. No. 005 ("Everyone has the right to respect for his private and family life, his home and his correspondence.").
24 See, e.g., supra note 21, at 8-9. The Working Party has suggested that in many cases consent will not be a possible option for processing data in response to a U.S. discovery request.
25 The Working Party also noted that “[a]n obligation imposed by a foreign legal statute or regulation may not qualify as a legal obligation by virtue of which data processing in the EU would be made legitimate.” The Working Party left open the possibility, however, that in some cases those subject to the Directive could justify compliance with a U.S. discovery order by reference to this provision. Compliance in order to defend or prosecute a case in the United States might also qualify as a “legitimate interest[ ]” under the Directive, but processing personal data pursuant to this exception can only occur if the requested party’s interest is not outweighed
26 Id. at 9; see also Rau et al., supra note 24, at 120 (suggesting that the “European Union has not generally regarded US discovery as either a sufficient ‘legal obligation’ or a ‘legitimate interest’ for EU data protection purposes”).
29 See Art. 29 Working Party Report 158, supra note 21, at 1 ("The case with which electronic records can be downloaded, transferred or otherwise manipulated has meant that the discovery process in litigation often gives rise to a vast amount of information which the parties need to manage . . . .")
30 Directive 95/46/EC, arts. 7(a), (c), (f); see also Art. 29 Working Party Report 158, supra note 21, at 8.
32 Id. at 9; see also Rau et al., supra note 24, at 120 (suggesting that the “European Union has not generally regarded US discovery as either a sufficient ‘legal obligation’ or a ‘legitimate interest’ for EU data protection purposes”).
“by the interests for fundamental rights and freedoms of the data subject.” 54

Entities subject to the Directive would also need to establish a basis under Article 26(1) of the Directive to transfer the data to the United States, a country that does not provide the same level of protection as required under E.U. law. 55 A number of exceptions might allow transfer to the United States of ESI for litigation purposes. 36 These exceptions include transfers that are “necessary or legally required on important public interest grounds, or for the establishment, exercise or defence of legal claims.” 37 However, the Working Party has explained that this and other exceptions in Article 26(1) “must be interpreted restrictively” and that member states “may provide for the exemptions not to apply in particular cases.” 38 In addition, the Working Party has stated that “this exception can only be applied if the rules governing criminal or civil proceedings applicable to this type of international situation have been complied with, notably as they derive from the Hague [Evidence] Convention[].” 39 It therefore appears that, in the Working Party’s view, the data must be requested through the Hague Convention for it properly to be transferred for use in a legal proceeding in the United States, although the basis for such an interpretation of the Directive is not clear.

In addition to general privacy laws, some countries have enacted, or protect by privilege, sector-specific data such as banking information. 40 Switzerland, for example, notably protects banking information. 41 Other countries such as Israel also have bank-confidentiality laws to protect bank customers’ privacy. 42

2. Cost-containment

One English judge observed long ago, “Truth, like all other good things, may be loved unwisely – may be pursued too keenly – may cost too much…. ” 43 It may be said that other nations’ pretrial disclosure law, especially in civil-law jurisdictions, reflects acceptance of this adage more than modern U.S. discovery rules, which impose broad requirements to preserve and produce ESI. Indeed, e-discovery has changed business and legal practice in the United States. General counsels throughout the country oversee multidisciplinary teams established to prepare for, and respond to, e-discovery requests. Many U.S. litigators spend more time working with e-discovery vendors and technology staff than they do writing briefs, researching the law, advising clients, and trying cases. Document discovery can take months and can involve the page-by-page review of literally millions of documents, with sometimes mind-boggling costs to the parties. A sub-industry of e-discovery vendors has emerged to assist in the complex, expensive, and time consuming process of collecting, searching, processing, reviewing, and producing ESI. These e-discovery tasks inevitably distract “people who should be conducting a business, running a government agency, or otherwise contributing to the public wea l…. ” 44

While these costs are part and parcel of modern U.S. business and discovery, they are foreign to the commercial and legal systems of other nations. Indeed, fear of U.S. discovery costs continues to be a major driving force in the popularity of international arbitration to resolve commercial disputes when the United States is a potential venue for litigation. 45

3. Sovereignty

“Discovery for use in a judicial or administrative proceeding is an exercise of jurisdiction by the state.” 46 While the United States may not view a discovery order to a foreign entity over which it has, pursuant to U.S. law, personal jurisdiction to be the exercise of extraterritorial authority, other nations disagree. The American Law Institute has noted, “The common theme of foreign responses to United States requests for discovery is that, whatever pretrial or investigative techniques the United States adopts for itself, they may be applied to persons or documents located in another state only with permission of that state.” 47 A number of nations took the position before the Supreme Court in Société Nationale Industrielle Aériospatiale v. U.S. District Court for the Southern District of Iowa (discussed in more detail below) that U.S. discovery orders aimed at the production of documents located within their territories violate their sovereignty. Germany, for example, argued that “only a German court has the legal power to enforce compliance with an order to produce documents located in Germany,” and that “[e]ven though issued in the United States, such [an] order constitutes an extraterritorial assertion of sovereignty, because it requires acts to be performed in the Federal Republic of Germany where the evidence must be gathered.” 48

54  Id.
55  Id. at 13; see also Directive 95/46, art. 26 (providing that, when a country to which data will be transferred does not provide an adequate level of data protection, a transfer may only take place under enumerated circumstances).
57  Directive 95/46, art. 26(1)(b).
59  Id. at 15.
60  See Davola, supra note 23, at nn. 47-52.
61  See, e.g., Baub et al., supra note 24, at 121.
67  Id. reporters’ note 1.
Switzerland similarly informed the Court, “If a U.S. court unilaterally attempts to coerce the production of evidence located in Switzerland, without requesting governmental assistance, the U.S. court intrudes upon the judicial sovereignty of Switzerland.”

Accordingly, foreign nations oppose compliance with U.S. discovery requests based on their view that evidence-gathering is a function of the nation in which the evidence is located; and extraterritorial application of U.S. law, including discovery law, offends their rights to “control…[their] territory generally to the exclusion of other states...to govern in that territory, and...to apply law there.” These foreign states can point to the “first and foremost restriction imposed by international law upon a State…that – failing the existence of a permissive rule to the contrary – it may not exercise its power in any form in the territory of another State.”

U.S. discovery requests or orders issued directly to citizens of civil-law countries also contravene the role of the judge in civil-law procedure. In the civil-law tradition, “the central task…is for the judge to identify the legal and factual issues involved and to decide them correctly.” Because common-law pretrial discovery is meant to inform the parties, not the judge, and is carried out by the litigants themselves, civil-law judges and advocates may view it as an usurpation of the judicial role. Thus, “an American discovery demand…addressed directly to a foreign party,…comes across as an attempt to circumvent the judiciary.”

Moreover, inherent in the concept of territorial sovereignty is the right to provide for national security. This process also involves striking a balancing among different values. China, for example, strikes a balance between individual rights and collective authority in a manner that favors collective security. Chinese secrecy laws are broad and prohibit disclosure by Chinese nationals of technological and economic data that might be requested during discovery.

4. Expressions of Foreign Interests

Foreign states have expressed their interest in shielding their nationals from U.S. pretrial document discovery without their permission in two important ways: (a) declarations pursuant to Article 23 of the Hague Evidence Convention, and (b) so-called blocking statutes.

(a) Article 23

One obvious and explicit expression of opposition to U.S. discovery lies in Article 23 of the Hague Evidence Convention. That provision states: “A Contracting State may at the time of signature, ratification or accession, declare that it will not execute Letters of Request issued for the purpose of obtaining pre-trial discovery of documents as known in Common Law countries.” In 2003, a Special Commission of the Hague Conference explained that “Article 23 was intended to permit States to ensure that a request for the production of documents must be sufficiently substantiated so as to avoid requests whereby one party merely seeks to find out what documents may generally be in the possession of the other party to the proceeding.” Despite this intended meaning, many parties to the Hague Convention have issued unqualified declarations that they will not execute letters of request to provide pretrial document production. Some of these countries may have done so out of the mistaken belief that “pre-trial discovery” means disclosure of information before a suit has been filed. These declarations, if understood to prohibit all letters of request for pretrial document discovery, stand as an impediment to one of the major purposes of the Hague Convention: to provide “a bridge between common law and civil law procedures.”

The United Kingdom, the original proponent of Article 23, has issued an Article 23 declaration but has clarified that its declaration is limited to requests “to produce any documents other than particular documents specified in the Letter of Request as being documents appearing to the requested court to be, or to be likely to be, in [the requested person’s] possession, custody or power.” The Hague Conference has encouraged other countries to follow the United Kingdom’s lead, and some have done so; however, many countries appear to retain their blanket rejection of requests for the pretrial disclosure of documents. France has also made a declaration under Article 23, but it will only allow the execution of letters of request for documents that are specifically identified and have a precise link to the

50 See RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 206 cmt. b (defining sovereignty).
51 S.S. Lotus (Fr. v. Turk.), 1927 P.C.L.J. (see At No. 10, at 18 (Sept. 7).
53 Id. at 1022.
54 Id.
58 2003 SPECIAL COMMISSION REPORT, supra note 56, ¶ 31.
59 Id. ¶ 27.
60 Id. ¶ 29.
litigation. The requesting party must describe the documents with a reasonable degree of specificity using things like the date, nature, and author of the documents.65

(b) Blocking Statutes

As one commentator has put it, “[v]arious episodes of expansionism in American law, largely antitrust and securities law, have led to the adoption in many countries of ‘blocking’ statutes designed to frustrate American discovery.”66 U.S. courts have frequently encountered blocking statutes that would prevent foreign nationals’ acquiescence in U.S. courts’ discovery orders.67 The statutes vary in their scope and enforcement.68 Seven parties to the Hague Evidence Convention and the European Community recently reported to the Permanent Bureau of the Hague Conference that they have some form of blocking statute that prevents those subject to their jurisdiction from giving evidence under defined circumstances to foreign courts, though the nature of these statutes varies.69

Perhaps the most well-known is the French blocking statute, which imposes criminal penalties on French nationals and residents for “communicating...to foreign public authorities, economic, commercial, industrial, financial, or technical documents or information, the communication of which [would] infringe upon the sovereignty, security, or essential economic interests of France or upon the public order.”70 Although U.S. courts have noted that the French blocking statute has not regularly been enforced,71 a French lawyer was convicted and fined €10,000 for violating the statute by providing documents in response to an order of the U.S. District Court for the Eastern District of New York.72 The French Cour de cassation upheld the conviction.73

The Supreme Court has held that blocking statutes “do not deprive an American court of the power to order a party subject to its jurisdiction to produce evidence even though the act of production may violate that statute.”74 However, the Court also noted that blocking statutes are evidence of foreign “sovereign interests in non-disclosure of specific kinds of material.”75

C. ESI Escalates the Conflicts

Conflicts between U.S. discovery rules and foreign interests in protecting privacy, ensuring the efficient functioning of businesses and government agencies, and preventing encroachments on territorial sovereignty can arise to a greater degree when the requesting party seeks ESI from a foreign national. Developments in technology have made electronic communication easier and faster to complete and to store, and more difficult to purge completely. Thus, foreign parties and third-party witnesses are often likely to possess ESI that is potentially relevant to disputes before U.S. courts and that contains sensitive business and personal information. The sheer volume of data that needs to be searched, collected, and reviewed imposes a greater risk of expense and intrusion.

Moreover, employees use e-mail both to conduct their employers’ business and for personal communications, thereby implicating the privacy of the employees. Finally, U.S. litigators have come to rely on ESI as the primary means of proving their case, and U.S. courts have become accustomed to ordering the production of ESI despite its sometimes heavy costs and to sanctioning parties for spoliation when such information has not been adequately preserved. Thus, in nearly all commercial disputes in U.S. courts, a substantial amount of ESI is demanded and, if necessary, ordered to be produced. ESI, more than traditional paper-based document discovery, has the potential to place foreign litigants in the position of violating U.S. court orders or their own country’s law.

II. International Comity

The U.S. Supreme Court has long-recognized international comity as a principle of federal law that calls for recognition of “the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws.”76 Comity is relevant when there is a true conflict between domestic and foreign law.77 What U.S. courts call comity, however, is closely related to a principle of customary international law that prevents unreasonable efforts by states
to prescribe law outside their borders.\textsuperscript{76} Indeed, the Supreme Court suggested that the comity analysis is aimed at determining whether a U.S. court’s compulsion of foreign discovery would be reasonable.\textsuperscript{77}

As discussed below, the Supreme Court has made clear that district courts must take into account the interests of foreign nations and the requirements of foreign law when deciding whether, and the manner in which, to order foreign nationals to produce documents located abroad.

**A. Aérospatiale**

In a decision that has a continuing effect on international judicial cooperation, the U.S. Supreme Court held in *Société Nationale Industrielle Aérospatiale v. U.S. District Court for the Southern District of Iowa* that the Hague Evidence Convention is not the exclusive means for parties in U.S. litigation to obtain evidence located abroad. The Court held that the Hague Convention does not deprive a district court “of the jurisdiction it otherwise possess[e]s to order a foreign national party before it to produce evidence physically located within a signatory nation.”\textsuperscript{78} Thus, a court may order a foreign national over which it has personal jurisdiction to produce discovery under the Federal Rules of Civil Procedure. The Court also rejected a rule that would require a U.S. party requesting discovery from a foreign litigant to first use the Hague Evidence Convention. Such a “rule of first resort” would be, in the Court’s view, “unwise” because the Convention’s procedures might sometimes “be unduly time consuming and expensive, as well as less certain to produce needed evidence than direct use of the Federal Rules.”\textsuperscript{79}

The Court did acknowledge, however, that the principle of international comity requires courts to examine “the particular facts, sovereign interests, and likelihood that resort to [the Hague Evidence Convention] procedures will prove effective” before deciding whether a party must request evidence through the Hague Convention or can do so through the Federal Rules.\textsuperscript{80} The Court cited the Third Restatement of Foreign Relations Law for factors that might be useful in this comity analysis, although it did not mandate that district courts adhere to any particular test.\textsuperscript{81} These factors are:

1. the importance to the litigation of the evidence sought;
2. the degree of specificity of the request;
3. whether the information originated in the United States;
4. the availability of alternative means of securing the information; and
5. the extent to which noncompliance with a discovery request would undermine important U.S. interests, or compliance would undermine important interests of the state where the evidence is located.\textsuperscript{82}

The Court also noted that the nature of the discovery request should be considered because “[s]ome discovery procedures are much more ‘intrusive’ than others.”\textsuperscript{83}

Whether to order a party to submit a Hague request rather than a request for documents under Rule 34 or a subpoena under Rule 45 is a matter for the trial court to determine “based on its knowledge of the case and of the claims and interests of the parties and the governments whose statutes and policies they invoke.”\textsuperscript{84} But the Court issued an admonition to lower courts:

American courts, in supervising pretrial proceedings, should exercise special vigilance to protect foreign litigants from the danger that unnecessary, or unduly burdensome, discovery may place them in a disadvantageous position.... When it is necessary to seek evidence abroad.... the district court must supervise pretrial proceedings particularly closely to prevent discovery abuses.... Objections to ‘abusive’ discovery that foreign litigants advance should therefore receive the most careful consideration. In addition,... American courts should.... demonstrate due respect for any special problem confronted by the foreign litigant on account of its nationality or the location of its operations, and for any sovereign interest expressed by a foreign state.\textsuperscript{85}

**B. Lower Courts’ Application of Aérospatiale**

Despite the Supreme Court’s direction to examine closely discovery demands on foreign nationals, U.S. courts have sometimes given short shrift to privacy and burden arguments made by foreign litigants, often because U.S. judges disfavor the procedures that the Hague Convention requires. In one commentator’s view, lower courts after *Aérospatiale* “have generally placed the burden on those urging resort to the [Hague] Convention and appear to assume that Convention procedures will be less effective than American discovery.”\textsuperscript{86} This preference for the Federal Rules over the Hague Convention, which would allow a foreign state to assert its interests by limiting or refusing to execute the request, also “emphasizes the centrality of discovery to the American world view.”\textsuperscript{87}

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\textsuperscript{76} See RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 403 cmt. a.

\textsuperscript{77} See Aérospatiale, 482 U.S. at 545-46.

\textsuperscript{78} Id. at 539-40.

\textsuperscript{79} Id. at 543.

\textsuperscript{80} Id. at 544.

\textsuperscript{81} See id. at 544 n.28.

\textsuperscript{82} Id. (quoting RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES §437(1)(c) (Tentative Draft No. 7)). These factors are now found in Section 442 of the Third Restatement of Foreign Relations Law.

\textsuperscript{83} Id. at 545.

\textsuperscript{84} Id. at 546.

\textsuperscript{85} Id.

\textsuperscript{86} Marcus, Retooling American Discovery, supra note 64, at 191.

\textsuperscript{87} Id.
Lower courts have concluded that Aérospatiale requires them to consider the particular facts of the case, the sovereign interests of the United States and the foreign states, and the likelihood that discovery through the Hague Convention will be effective to determine whether a requesting party should be ordered to use the Hague Convention rather than the Federal Rules of Civil Procedure. To carry out this analysis, most courts have looked to the factors set out in Section 442 of the Third Restatement of Foreign Relations Law: (1) the importance of the information to the litigation, (2) the degree of specificity of the request, (3) whether the information originated in the United States, (4) the availability of alternative means to secure the information, and (5) the interests of the United States and the state where the documents are located.

Although these courts have applied a comity analysis, many of them have failed to consider adequately the interests of foreign sovereigns. For example, the Third Circuit in In re Automotive Refinishing Paint Antitrust Litigation rejected German companies’ argument that ordering discovery of documents located in Germany would offend German sovereignty. The court rather unpersuasively reasoned that, because the case involved allegations of price-fixing and German law prohibited such conduct, “presumably Germany…would welcome investigation of such antitrust violation to the fullest extent.” Whether the German government would welcome investigation into price-fixing involving its nationals simply fails to respond to the argument that Germany considers it a violation of its sovereignty for a U.S. court to order those German nationals to turn over information for use in a U.S. proceeding. Courts have also found that discovery under the Federal Rules instead of the Hague Convention was appropriate due to a foreign state’s domestic laws that would prevent disclosure or Article 23 declaration, or due to the general inefficiency of the Convention.

These and other cases support the observation of Judge Roth in Automotive Refinishing that “many courts are simply discarding the [Hague Convention] as an unnecessary hassle” and have failed to “exercise[] the ‘special vigilance to protect foreign litigants’ that the Supreme Court anticipated.”

III. Refocusing on Comity

At a time when stakeholders throughout the U.S. legal system are questioning the wisdom of U.S. e-discovery practices, U.S. courts should be even more solicitous of the interests and values of foreign legal systems when regulating e-discovery in cases involving foreign litigants. Courts should do more than pay lip service to international comity and should not reject foreign nations’ interests, especially those explicitly stated by the foreign state, merely because the U.S. legal system balances privacy, truth-seeking, and cost-containment differently than other states in crafting procedural rules. Courts must take seriously the Supreme Court’s direction that international comity is a principle of U.S. law that must be rigorously applied to determine the appropriate scope of cross-border discovery. The increased and sometimes outlandish burdens imposed by the identification and production of foreign ESI require even closer scrutiny of e-discovery requests than requests for other types of discovery. Importantly, the Court in Aérospatiale recognized that the comity analysis depends in part on the intrusiveness of the requested discovery. The Supreme Court has held that other interests sometimes outweigh the “search for truth” in civil proceedings, and has contrasted the interests and checks present in criminal cases with those in civil actions. Moreover, document discovery required judicial approval prior to 1970. It would therefore not be wholly alien to the administration of civil justice in the United States to balance the quest for truth with other values such as comity and respect for the interests of other nations.

Consistent with Federal Rule of Evidence 44.1, courts should consider any evidence of foreign law, including expert declarations, to support a party’s argument that the discovery request would require it to violate foreign law.

89 See RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 442(1)(c).
90 358 F.3d 288 (3d Cir. 2004).
91 See id. at 304.
92 Id.
94 Auto. Refinishing, 358 F.3d at 307 (Roth, J., concurring).
95 See 482 U.S. at 545.
97 See FED. R. CIV. P. 16(a) advisory committee’s note to 1570 amendment (noting that amendment eliminated need for requesting party to show “good cause” for obtaining documents in possession of requested party).
98 482 U.S. at 544 n.29.
Such an argument would fit within Federal Rules of Civil Procedure 26(c) and 45(c), which allow courts to limit or deny requests for documents that would subject the requested party to an undue burden. Of course, courts must retain the discretion to weigh the particular circumstances of the case, including whether the foreign party is a plaintiff and thus has willfully invoked the court’s jurisdiction.99

Courts also should not order discovery pursuant to the Federal Rules merely because of a belief that the foreign state would deny a letter of request for the information sought. The foreign state might conclude that production would not in fact violate domestic law or that the state’s obligations under the Hague Convention trump domestic legal restrictions. For those nations that have asserted blanket Article 23 declarations, it is possible that, in practice, they will not interpret their declaration as broadly as worded. If the request is denied and the information is specifically identified and essential to the case, the district court can craft remedies other than ordering the foreign litigant to violate its nation’s laws, such as restricting the discovery rights of the foreign litigant so that neither side is at a competitive disadvantage.

Finally, it cannot be denied that execution of a letter of request under the Hague Convention is more time-consuming than simply serving ordinary requests for the production of documents. But until a more efficient means of cross-border evidence-gathering is devised, U.S. courts should accept the delay as necessary to further the important interest in demonstrating respect for foreign sovereignty, which will in turn make other nations more likely to respond favorably to U.S. requests for evidence located abroad.

In sum, international judicial cooperation would be better served if courts paid as much attention to Aérospatiale’s admonition to weigh carefully discovery requests directed to foreign litigants as courts pay to the Supreme Court’s holding that the Hague Evidence Convention is not mandatory. Courts should take into account the ways in which e-discovery poses special challenges to foreign litigants and has the potential to offend the interests of foreign states, which arise because of these states’ emphases on values other than truth-seeking. While it is true that the Hague Evidence Convention is often inefficient, at present it provides the most assurance that a U.S. discovery request for ESI does not violate another nation’s views of the right to privacy, the need to protect its nationals against the high costs associated with U.S. e-discovery, and territorial or judicial sovereignty. At the same time, however, foreign states must reconsider blanket denials of pretrial document discovery under Article 23 of the Hague Evidence Convention. Without compromises on both sides, it is likely that U.S. courts will continue to order foreign nationals to produce ESI located abroad under U.S. domestic law. ■

99 See, e.g., Reino de Espana, 2005 WL 1813017, at *9 (ordering Spain to produce documents after comity analysis despite claim that doing so would violate Spanish law because, among other reasons, Spain chose to sue in a U.S. court and therefore should have to comply with the court’s procedural law).
Recent Changes in Switzerland’s Civil Procedure and Debt Enforcement Legislation – Update for International Practitioners

By Nicolas Herzog and Niccolò Gozzi*

I. Introduction

Switzerland is a federal state comprised of 26 cantons (states). While Switzerland’s substantive private law – such as the law of contracts, corporations and intellectual property law, to name but a few – is overwhelmingly federal law that is uniformly applicable in the entire territory of Switzerland, the situation is different for procedural law in civil matters. An important exception is debt collection and bankruptcy law, which has long since been unified in a federal statute. This statute comes into play for the enforcement of monetary claims and comprises the important attachment remedy (see infra section IV).

As far as civil procedure law is concerned, until the end of 2010 each of the 26 cantons has its own code of civil procedure in place. Even though over time principles derived from federal statutes and constitutional law have increasingly permeated this body of cantonal laws, the codes of civil procedure ultimately remain cantonal (state) laws with their nuances and idiosyncrasies. Unsurprisingly, the collection of 26 more or less different codes of civil procedure renders litigating before Swiss state courts an undertaking where local elements always are part of the equation and need to be accounted for. Foreign companies doing business in Switzerland, a country approximately one half the size of South Carolina, sometimes are astonished by this remarkable characteristic.

However, the reign of cantonal civil procedure legislation will soon come to an end. The Swiss legislature decided to unify this important area of the law and devised a federal code of civil procedure (“CCP”) that will become law on January 1, 2011. The objective of this paper is to inform international practitioners of the most salient features of the new federal code of civil procedure so as to facilitate their communication with Swiss counsel when litigation, enforcement, or judicial assistance issues arise in Switzerland.

The introduction of the federal code of civil procedure is accompanied by other important legislative milestones which we will discuss as well: the Lugano Convention, which parallels the Brussels I Regulation (Council Regulation [EC] No 44/2001 of December 22, 2000 on jurisdiction, recognition and enforcement of judgments in civil and commercial matters), has been updated so as to bring it in line with the Brussels I Regulation. Lastly, the law on attachments has been amended (effective as of January 1, 2011) and will introduce an important additional ground for freezing a debtor’s assets.

In contrast, at this juncture it should be noted that the important realm of international commercial arbitration is not affected by this recent legislative activity. The often used Swiss framework legislation for arbitrations, where at least one party does not qualify as a Swiss-domiciled entity or entity habitually residing in Switzerland, remains regulated in the 12th chapter of Switzerland’s private international law act (“PILA”). Apart from a recent amendment relating to the competence-competence of arbitral tribunals, this body of law has not been revised.† The opposite holds true for domestic arbitrations between parties domiciled in Switzerland. Beginning next year, the framework rules for such arbitrations will be found in the forthcoming federal code of civil procedure (Art. 353 et seq. CCP). It is worth mentioning that parties subject to the domestic arbitration rules remain at liberty to opt out of them and may instead choose the less detailed framework rules for international arbitration.

II. The New Federal Code of Civil Procedure

1. Some Noteworthy Features

While court organization is left to the province of the cantons, the CCP contains detailed provisions on jurisdiction for domestic cases. In the international context, however, nothing changes in this regard since jurisdiction remains governed by either the provisions of the PILA or applicable international treaties, the most important of which in civil matters is the Lugano Convention (see infra section III).

To begin with, oftentimes non-Swiss counsel or clients wonder whether court proceedings in civil matters are public, as they are, for example, as a general rule in U.S. courts. The short answer is that, apart from family matter disputes, litigation before Swiss state courts is in principle open to the public, which is entitled to attend hearings and the declaration of the judgment. Yet, what seems to be substantially different from U.S. litigation is that the parties’ filings and the record are not generally available to the public. However, it is sometimes possible to obtain access to court papers by filing a motion to that effect. The court will weigh the parties’ request for privacy against the outsider’s interest in obtaining access to the court papers.

Another key issue is costs. Put simply, the CCP adheres to the traditional continental principle that costs follow the event. It implies that the losing party has to bear the court costs and the prevailing opponent’s attorneys’ fees in proportion to the extent it lost the case. Both items are to be computed according to cantonal tariffs, which take the amount in

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‡ The new provision is Art. 186(1bis) PILA. Pursuant to this provision, an arbitral tribunal shall decide on its jurisdiction regardless of whether the same matter has been brought before a state court or another arbitral tribunal, unless there are important reasons mandating a stay of the proceedings. This amendment was introduced in order to prevent a party from seizing a (non-Swiss) state court, in spite of an existing arbitration clause, in order to disturb the arbitration proceedings. The amendment was conceived in the aftermath of the much debated Fomento case in which the Swiss Federal Supreme Court ruled that an arbitral tribunal shall stay its proceedings when the same matter is pending in a foreign state court that is expected to render a decision that can be recognized in Switzerland (ATF 127 III 279).
In order to facilitate the service of court orders and decisions, the Swiss court may order the foreign litigant to appoint a representative domiciled in Switzerland (Art. 140 CCP). In the event of non-compliance, the CCP provides for the taking of security for the costs and fees (Art. 99(1)(a) CCP). For instance, U.S. litigants are not covered by the 1954 Hague Convention on Civil Procedure, the 1980 Hague Convention on International Access to Justice or by the treaty between Switzerland and the U.S. of December 17, 1850/July 21, 1855 and therefore they can be requested to post bonds.2

In order to facilitate the service of court orders and decisions, the Swiss court may order the foreign litigant to appoint a representative domiciled in Switzerland (Art. 140 CCP). Such order must be properly served on the foreign litigant by way of the methods of service provided for in the pertinent sources of international legal assistance in civil matters (e.g., with respect to a U.S.-domiciled party, the 1965 Hague Convention on the Service Abroad of Judicial and Extrajudicial Documents in Civil or Commercial Matters).

As to legal privilege in civil proceedings, the CCP introduces an important improvement for litigants and third parties. Pursuant to Art. 160(1)(b) CCP, a party’s or third person’s correspondence and other documents relating to legal advice with their attorneys are exempted from the general obligation of production to the court when so rightfully requested by the opposing litigant. This represents a significantly enhanced protection of attorney-client communication and a step towards the common law style work-product doctrine. Presently, such communications are only protected from disclosure if the respective documents remain in the possession of the attorney. Copies of correspondence with an attorney that are in a party’s (or third person’s) possession have to be disclosed if so ordered by the court. Beginning January 1, 2011, litigants and third persons will have a right to withhold copies of documents that pertain to communication with their attorneys. To be sure, the documents must qualify as genuine attorney work product in order to be afforded the privilege. For example, counseling with respect to pending or future litigation will fall under the privilege but not an attorney’s activity as a board member or advisor to the commercial management of a client’s assets. As a practical matter, in order to facilitate the screening of protected communication, it should explicitly be earmarked as such.

Useful features at the pre-trial stage are protective briefs, which are explicitly regulated in Art. 270 CCP. If a party has a reason to believe that its opponent may enter the fray by filing a request for injunctive relief in an ex parte proceeding, including the filing of an ex parte request for an attachment of assets, it can, as a preemptive measure, file a brief setting out its arguments as to why such relief should not be granted. Such a protective brief will not be forwarded to the opponent until it actually files a motion. The court will keep the protective brief on file for six months, after which it will be returned to the filing party. It goes without saying that this instrument can be very important in defending against ex parte applications of the potential opponent, in that it ensures that the court will hand down a decision only after having taken notice of both parties’ arguments.

2. The Ordinary Proceeding

Depending on the amount in dispute and the nature of the dispute, the CCP provides for different types of proceedings (ordinary, simplified and summary). Commercial disputes will predominantly be dealt with in an ordinary proceeding, which is available when the disputed amount exceeds the threshold of CHF 30,000. As a general rule, such proceedings will be commenced by filing a request for conciliation with a conciliation authority. However, if the defendant is a non-Swiss party, the plaintiff may forego this preliminary procedural step and file the statement of claim directly with the competent court. Similarly, if the dispute falls within the jurisdiction of a commercial court, no conciliation proceeding is necessary. Commercial courts exist in the cantons of Aargau, Berne, St. Gallen and Zurich. In the event the amount in controversy exceeds CHF 100,000 (roughly USD 100,000), the parties are at liberty to jointly waive the conciliatory proceeding and directly make an appearance before the court.

In matters with an amount in dispute higher than CHF 30,000, the plaintiff initiates the proceeding before the court of first instance by filing a written statement of claim, in which the plaintiff essentially puts forward its prayers for relief, the statement of facts with reference to the supporting evidence. Already at this early stage, plaintiff’s counsel should make sure that the relevant facts are pleaded with sufficient detail so that they can be made the subject of an evidentiary proceeding, to the extent the plaintiff bears the burden of proof. In addition, the plaintiff may include its legal reasoning in the statement of claim. As a next step, the defendant will file its statement of defense, which shall be crafted in the same fashion as the statement of claim.

Whether there will be another exchange of briefs (reply and rejoinder) lies in the discretion of the court. The court will also weigh whether it is conducive to summon the parties to a preliminary hearing where the court can pose questions to the parties to clarify the facts and to explore the possibility of a settlement. Apart from that, such a preliminary hearing will serve to prepare for the forthcoming main hearing before the court. Counsel will have to be mindful of the exact

2 Federal Supreme Court, ATF 121 I 108.
procedural steps taking place, as they have a bearing on the requirements that must be met in order to be allowed to plead new facts and adduce new evidence in the main hearing. However, the general rule is that it is always admissible to plead genuinely new facts in the main hearing, regardless of what procedural steps have taken place prior to the hearing. To qualify as “genuinely new,” the fact or evidence at issue must have come into existence after the second exchange of briefs or the preliminary hearing. This is quite a tricky distinction and requires great diligence of counsel in charge.

The CCP envisages that taking of evidence shall take place at the main hearing. Yet, in complex matters this oftentimes will not be possible for practical reasons. Thus, evidence will have to be taken in separate hearing sessions. At the conclusion of the evidence taking, the parties are entitled to comment on the evidence, which can happen either in oral pleadings or in written briefs, if the parties jointly so request.

3. Appeals
The CCP provides for different types of appeals. Relevant differentiating factors are the nature of the decision to be appealed (final, interlocutory or procedural) and, again, the amount in dispute. Assuming a final decision of the court of first instance where there remains a part in dispute with a value exceeding CHF 10,000, the available appeal will be the ordinary one (Art. 308 et seq. CCP). It allows for a full review of the lower court’s application of law (de novo review) as well as an examination of whether the establishment of the facts was correct. By default, the filing of an appeal will suspend the enforceability of a judgment. However, in cases of monetary disputes upon the application of a party, the court can order that the judgment be provisionally enforceable. It is possible to plead new facts and evidence in the appeal proceeding, provided that this is done without delay and that, despite diligent behavior, such new allegations could not have been put forward in the proceeding of the first instance.

Interlocutory decisions and decisions on preliminary relief must be challenged with a different type of appeal (recourse, Art. 319 et seq. CCP), which by default does not suspend enforceability. In addition, the review of the facts is limited to the “clearly erroneous” standard. No new facts and evidence can be adduced in this type of appeal. Finally, a litigant can avail itself of the motion for retrial if, inter alia, new facts or evidence are discovered only after the conclusion of the main proceeding that, by the standard of reasonable diligence, could not have been pleaded during the main proceeding.

If the cantonal court of first instance is not a lower court but is, for instance, a commercial court, the appeal will be filed directly with the Swiss Federal Supreme Court. Appellate remedies to this court are regulated by a separate statute, the federal act on the Federal Supreme Court. From a practical perspective, it is noteworthy that the lodging of an appeal to the land’s highest court will not affect the enforceability of monetary judgments unless suspensive effect is granted upon submitting such a request.

III. Revision of the Lugano Convention
1. The Lugano Convention
The Lugano Convention was signed in Lugano on September 16, 1988 by the states of the European Community and the European Free Trade Association. Its purpose was to extend the uniform rules on jurisdiction and enforcement found in the Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters agreed to by the original members of the European Community in 1968 (Brussels Convention). In Switzerland, the Lugano Convention came into force on January 1, 1992.

The Brussels Convention was revised and replaced by the Brussels I Regulation (Council Regulation [EC] No 44/2001 of December 22, 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters), which came into force on March 1, 2002. Negotiations ensued regarding the revision of the Lugano Convention to reflect the rules enacted in the Brussels I Regulation. Due to a long debate whether the European Community had exclusive or shared competence to conclude the revised Lugano Convention (“Lugano Convention or LC”),1 the amended treaty was only signed on October 30, 2007 by the European Community and individual member states of the European Free Trade Association (Norway, Iceland and Switzerland). The revised Lugano Convention will come into force in Switzerland on January 1, 2011.

The major amendments to the provisions of the Lugano Convention are highlighted below.

2. Scope of Application
The most important change pertains to the territorial applicability of the Lugano Convention, which will apply to member states of the European Free Trade Association as well as the European Community. Moreover, in the future, the Lugano Convention will automatically apply to any new member state of the European Community, since the latter – and not an individual member state – is formally a contracting party to the Lugano Convention.2

In principle, the Lugano Convention follows the legal framework set forth in the Brussels I Regulation. Therefore, the rules on jurisdiction and enforcement of judgments will be identical both in the member states of the European Community and of the European Free Trade Association (except for Liechtenstein).

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1 On February 7, 2006, the European Court of Justice held that the European Community was exclusively competent to conclude the Lugano Convention revisions.
2 The current Lugano Convention applies to only 16 out of the 27 member states of the European Community. It does not apply to the Czech Republic, Slovenia, Hungary, Malta, Cyprus, Estonia, Latvia, Lithuania, Bulgaria or Romania.
3 As such, the Lugano Convention forms part of the laws of the European Community and will also be subject to the adjudication of the European Court of Justice (see Protocol No 2 to the Lugano Convention).

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The Lugano Convention applies whenever the defendant in a legal dispute is domiciled in a state bound by it, regardless of where the plaintiff is domiciled. So, a U.S. plaintiff can invoke the jurisdictional provisions of the LC when suing a Swiss-based defendant. In addition, the Lugano Convention provides for exclusive jurisdiction of the courts of the member states in proceedings regarding: (i) rights in rem or tenancies of immovable property situated in a member state; (ii) the validity of the constitution, the nullity or the dissolution of companies or legal persons with seats in a member state, or the validity of the decisions of their organs; (iii) the validity of entries in public registers kept in a member state; (iv) the registration or validity of patents, trademarks, designs, or other similar rights required to be deposited, registered, applied for, or taken place in a member state; and (v) the enforcement of judgments in a member state (Art. 22 LC).

The Lugano Convention applies to jurisdiction as well as the recognition and enforcement of judgments in civil and commercial matters. It does not apply to tax, customs and administrative matters, or to the status and legal capacity of persons domiciled in a state bound by the Convention may be sued in that state, regardless of their nationality (Art. 2 LC).

As a general rule, the Lugano Convention provides that the place of performance with regard to the most common and important types of contracts, i.e. contracts for the sale of goods and contracts for the provision of services, regardless of the specific contractual obligation at issue. According to this rule, the place of performance for contracts for the sale of goods or the provision of services lies in the state bound by the Lugano Convention where the goods/services were delivered/provided, or should have been delivered/provided. These new rules should help facilitate the establishment of the place of performance in cross-border disputes involving states bound by the Lugano Convention. However, in case the place where the goods or services were delivered/provided, or should have been delivered/provided, is located outside a state bound by the Lugano Convention, jurisdiction has to be established in line with the guidelines formulated by the European Court of Justice.

Another set of rules important to practitioners are the provisions on jurisdiction in matters involving consumer contracts according to Art. 15 et seq. LC. These provisions aim to protect a consumer, who is typically the weaker contracting party, by granting the same different venues of his choice, as well as restricting the possibility to contractually impose upon the consumer a specific jurisdiction as the choice for dispute resolution.

The specific rules of jurisdiction in matters relating to consumer contracts set forth in the Lugano Convention apply to specifically defined contracts concluded by a person (the consumer) the purpose of which can be regarded as being outside his trade or profession (Art. 15(1) LC). Under the revised Lugano Convention, the group of contracts that fall within the specific rules of jurisdiction has been expanded considerably. In particular, it encompasses all contracts in which the consumer’s counter-party either “pursues commercial or professional activities in the member state of the consumer’s domicile or, by any means, directs such activities to that state or to several states including that state, and the contract falls within the scope of such activities” (Art. 15(1)(c) LC).

The term “directing commercial or professional activities by any means” in the afore-mentioned provision is extremely broad and refers to any general business activity. For example, the rules of jurisdiction in consumer contracts already apply in cases where a company sells its products over a web-based
platform to consumers in a state bound by the Lugano Convention. Exceptions only apply if the respective website clearly states that the goods sold will not be shipped abroad or if the services offered are obviously restricted to the state where the company is domiciled.

4. Recognition and Enforcement of Judgments
Art. 32 et seq., of the Lugano Convention contains specific provisions relating to the recognition and enforcement of judgments rendered by a court of a state bound by the convention.

Under the revised Lugano Convention, the procedure for recognition and enforcement of judgments has been streamlined considerably. A party seeking recognition/enforcement of a judgment has to file a corresponding application with the competent court indicated for each member state in Annex II to the Lugano Convention (Art. 39 LC), along with a copy of the judgment satisfying the conditions necessary to establish its authenticity, as well as the certificate pursuant to Annex V of the Lugano Convention issued by the court that handed down the judgment (Art. 53 and 54 LC). The court shall decide on such application in summary proceedings ex parte, i.e. without hearing the opposing party. Moreover, the court shall declare the judgment enforceable immediately if the documents mentioned above have been produced according to Art. 53 and 54 LC. In other words, the court will not check whether there are grounds for denying recognition/enforcement of the judgment. The grounds set out in Art. 34 et seq. of the LC can only be argued on appeal against the court order recognizing the judgment (Art. 43 et seq. LC). It should be noted that the revised Lugano convention narrows the grounds for denying recognition/enforcement compared to the Lugano Convention provisions currently in effect (Art. 34 et seq. LC).

Under no circumstances, may the judgment to be recognized/enforced be reviewed as to its substance (Art. 36 LC).

Under the Lugano Convention provisions already in effect, the party seeking recognition and enforcement of a foreign judgment may request provisional measures, including protective ones, in accordance with the law of the state where it is requested (Art. 47 LC). Such request can be filed together with the application for recognition of the judgment and will be ruled upon by the same court without hearing the opposing party.

In Switzerland, the learned writing and case law have been highly controversial as regards what protective measures are available in connection with the recognition/enforcement of a judgment ordering the payment of a sum of money under the Lugano Convention. As of January 1, 2011, this issue will be clarified once and for all. In the wake of the revision of the Lugano Convention, the Swiss legislature also overhauled the rules on the freezing of assets located in Switzerland (so-called attachment) set forth in Art. 271 et seq. in the Swiss Debt Enforcement and Bankruptcy Act (DEBA). Based on the new provision of Art. 271(1)(6) DEBA, attachment is the (only) protective measure available in connection with the recognition procedure under the Lugano Convention in so far as judgments for payment of a sum of money are concerned.

IV. Amendments to the Grounds for Attachment
Switzerland ranks among the leading financial market places in the world with a particular focus on private banking and, accordingly, Swiss banks and other financial institutions hold a significant volume of foreign assets. For this reason, attachment orders designed to freeze assets held in Switzerland are often sought in both national and international disputes in order to secure monetary claims against debtors.

As previously mentioned, the Swiss rules on the freezing of assets are found in Art. 271 et seq. of DEBA and have been considerably amended in connection with the revision of the Lugano Convention. The respective amendments of the attachment rules will become effective on January 1, 2011.

The most important change pertains to the grounds for obtaining an attachment, which have been expanded. According to the newly introduced provision of Art. 271(1)(6) DEBA, a creditor is entitled to attach the debtor’s assets located in Switzerland based on a binding Swiss or foreign judgment – provided that the latter is recognizable and enforceable in Switzerland, it being irrelevant where the debtor is domiciled. In addition, the court from which the attachment order is sought will have jurisdiction to grant an order regarding assets located within the whole territory of Switzerland. Currently, the jurisdiction of the courts is limited to the territories within their respective canton.

Without doubt, these amendments to the attachment rules will offer to creditors holding an enforceable judgment against their debtors an extremely efficient means to secure monetary claims. One can fairly assume that the numbers of attachment requests will grow dramatically over the next few years.

This is even truer, since the procedure to obtain an attachment order is relatively straightforward and swift. An attachment order is issued in ex parte expedited summary proceedings, which usually last only a few days or even a few hours if the urgency is established by the creditor. The court fees are rather modest, ranging between CHF 1,000 to CHF 2,000, depending on the canton where the application is made. The attachment order will be granted if the creditor makes a prima facie showing that: (i) the creditor has a claim, (ii) there exists a ground for an attachment order according to Art.271(1) DEBA, and, (iii) there are assets in Switzerland belonging to the debtor. The standard of proof varies depending on what ground the request for an attachment is based on.
Supreme Court Upholds Arbitrator’s Authority to Decide Unconscionability Challenge to Arbitration Agreement


The Supreme Court’s recent decision in Rent-A-Center adds a rather extraordinary layer to the American arbitration jurisprudence on the doctrines of separability and competence-competence. Jackson commenced an employment discrimination suit in Nevada federal court against his former employer Rent-A-Center. Based on an arbitration agreement signed as a condition of employment, Rent-A-Center moved under Sections 3 and 4 of the Federal Arbitration Act (FAA) to stay or dismiss the suit and compel arbitration. Jackson challenged the validity of the arbitration agreement arguing that the arbitration agreement, itself, was unconscionable because of the fee-splitting provision, limited discovery provisions, and the fact that it was non-negotiable. The arbitration agreement contained a contractual provision for competence-competence, or, as the Supreme Court labeled it, a delegation provision, vesting the arbitrator of the contractual authority to decide the interpretation, applicability, enforceability, or formation of the agreement. The District Court granted Rent-A-Center’s motion finding that the arbitration agreement “clearly and unmistakably [sic] placed enforceability of the arbitration agreement and arbitrability within the arbitrator’s exclusive authority.” The Ninth Circuit reversed based on the nature of Jackson’s challenge, holding that “the threshold question of unconscionability is for the court.” The Supreme Court reversed.

While the parties framed the issue for the Supreme Court as one of their intent and the validity of the arbitration agreement under Section 2 of the FAA, the Court chose to develop further the famous dicta in First Options regarding contractual competence-competence to create a rule characterized by the dissent as “Russian nesting dolls.” The Court held that the delegation provision was separable from the arbitration agreement for the purpose of deciding the latter’s validity just as the arbitration agreement was separable from the container contract. Accordingly, under Prima Paint, Jackson’s unconscionability challenge to the arbitration agreement as a whole, as opposed to a challenge to the delegation provision specifically, was insufficient to divest the arbitrator of the contractual authority to decide the validity of the arbitration agreement. Although the Court’s reasoning logically flows from the prior precedents, this case together with the decision in Hall Street essentially creates absolute competence—competence, without any provision for later review by a court – a concept in apparent conflict with the New York Convention. In Hall Street, the Supreme Court made it clear that Sections 9–11 of the FAA provide exclusive grounds for confirming, modifying or vacating an arbitral award. As a result, an award cannot be set aside in the United States under the FAA on the ground that the arbitrator lacked jurisdiction, because it is not one of the grounds enumerated in Sections 9–11. In Rent-A-Center, on the other hand, the Court eliminated judicial review of arbitral jurisdiction under Section 4 of the FAA where the parties agreed to arbitrate the “gateway questions of arbitrability” unless a challenge is directed to such a delegation provision specifically.

Therefore, as a practical matter, it appears that the United States does not currently provide judicial review on the issue of arbitral jurisdiction if the arbitration agreement delegates the jurisdictional decision to the arbitrator. Such result is at odds with the New York Convention, which provides that invalidity of an arbitration agreement is a ground for non-enforcement. It appears rather impractical to require a party opposing arbitral jurisdiction to fight enforcement of an award under the New York Convention in potentially several jurisdictions instead of allowing judicial review at the arbitral situs.

District Court Upholds Arbitrator’s Class Arbitration Determinations


An exemplary post-Bazzle international class arbitration is Fellows of Harvard College v. Surgutneftegaz. The decisions of the arbitrators and the courts in this dispute are particularly interesting in light of the recent decision of the Supreme Court in Stolt-Nielsen S.A. v. Animalfeeds International Corp., 130 S.Ct. 1758 (2010), which rejected class arbitration under an agreement that was silent as to class arbitration under circumstances in which the arbitrators found that the parties had reached no agreement on class arbitration. This case note...
discusses the decisions in the Harvard case and explores the potential impact that Stolt-Nielsen might have today on a case with facts similar to those in Harvard.

**Facts.** Harvard University filed this class arbitration with the AAA against the Russian gas company Surgutneftegaz (Surgut). The arbitration was based on an American Depository Receipt (ADR) deposit agreement between the parties. Harvard claimed that Surgut did not pay the fixed annual dividends it had agreed to pay to it.

Surgut denied breaching the deposit agreement. It claimed that it had correctly calculated the dividends and that Harvard lacked standing to challenge its dividend policy because Harvard’s claims were not arbitrable.

After Harvard started the arbitration, Surgut brought an action in New York state court to stay the arbitration, arguing that Harvard’s claims were not arbitrable. Harvard removed the case from the state court to the United States District Court for the Southern District of New York. That court denied Surgut’s petition and referred the parties to the arbitration on the grounds that the arbitrators should decide the issue of arbitrability.

Surgut appealed to the United States Court of Appeals for Second Circuit. The Second Circuit affirmed the district court’s decision and held that the parties intended to submit the question of arbitrability to the arbitrators.

After the Second Circuit’s decision, three arbitrators were appointed: one from New York, one from Russia, and one from the Netherlands, who was the Chairman. Surgut objected to the arbitrability of Harvard’s claims and asserted that the arbitration clause did not allow claims to be brought on behalf of a class.

**Arbitration Panel’s Holding.** The Panel’s two-arbitrator majority found that the arbitration clause, “properly construed, does not preclude the arbitration from proceeding on a class basis.” The Panel reached its decision on four grounds:

1. The members of the class on whose behalf the case is brought—owners and beneficial owners of the deposit agreement—were all parties to the same agreement, and therefore, a class proceeding could be maintained without the need for consolidation.
2. The arbitration clause in the deposit agreement was broad and extended to “any...claim” brought by “any party,” which necessarily includes a claim on behalf of an individual as well as on behalf of a class.
3. Surgut agreed that the claims based on U.S. securities laws could be litigated in U.S. courts—which necessarily implicitly included in a class action—in the same document in which it agreed to the arbitration of “any...claim” brought by “any party.”
4. And finally, Surgut did not identify any international arbitration principle or norm that would invalidate an arbitration clause that permitted class arbitration when properly construed under the governing law and the procedure of the situs of the arbitration.

The award was challenged by Surgut. But the district court confirmed it, finding that “the arbitrators in this case correctly determined, among other things, that the ’plain language of the agreement...permits class arbitration.’”

This rationale for the district court’s decision upholding the arbitrator’s “class arbitration” determination potentially distinguishes this case from the Supreme Court’s recent decision in Stolt-Nielsen. The Court in Stolt-Nielsen focused on the fact that the arbitrators had relied on public policy and not contract language or the custom and usage in the industry that reflected the intent of the parties to permit class arbitration. Instead, in Stolt-Nielsen, the parties stipulated that the agreement did not address the issue of class arbitration, and the arbitrators found that the parties had reached no agreement on class arbitration. The district court’s conclusion in the Harvard case that the “plain language of the agreement...permits class arbitration” arguably distinguishes the two cases.

1 This case note was prepared by Ulyana Korzhevych, International Attorney, Americas Dispute of White & Case, Washington, DC; LL.M. in International Dispute Settlement of Geneva Law School and Graduate Institute of International and Development Studies.
3 Id.
4 Panel Award, President and Fellows of Harvard College Against Surgutneftegaz (AAA Case No. 1116870165404, Aug. 1, 2007) at 8, appended Julie Bedard, President and Fellow of Harvard College Against Surgutneftegaz, in International Arbitration 2008, 77 PLI/Lit 127 (2008)(emphasis supplied) [hereafter Julie Bedard].
5 Id.
9 Id.
10 Id. at *1 - *3.
11 Id.

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**Supreme Court Rejects Class Arbitration When the Agreement Is Silent on the Issue**

**Stolt-Nielsen S.A. v AnimalFeeds International Corp., 130 S.Ct. 1758 (2010).**

In Stolt-Nielsen S.A. v. AnimalFeeds International Corp., 559 U.S. ___ (April 27, 2010), the United States Supreme Court held that the Federal Arbitration Act (FAA) prohibits arbitrators from imposing class arbitration where the agreement is silent on that issue.

Petitioners were Stolt-Nielsen and other shipping companies who had entered into charter party contracts with customers, such as respondent AnimalFeeds. AnimalFeeds brought a class action antitrust suit against petitioners for price fixing,
and that suit was consolidated with other similar claims. The charter party that AnimalFeeds used contains a standard maritime arbitration clause, and AnimalFeeds sought arbitration of the antitrust claims on behalf of a class of customers against petitioners. The parties agreed to submit the question of whether their arbitration agreement allowed for class arbitration to a panel of arbitrators. The parties further stipulated that there was “no agreement” on the issue of class arbitration. The panel determined that the arbitration clause allowed for class arbitration, but the Southern District of New York vacated the award, concluding that the arbitrators’ award was made in “manifest disregard” of the law. The Second Circuit reversed, holding that because of New York vacating the award, concluding that the arbitrators’ decision was not in manifest disregard of maritime law. The Supreme Court not only reversed and remanded to the Second Circuit, but went so far as to vacate the arbitration award, finding that the “only possible outcome” was that class arbitration was not permitted under the present circumstances. Writing for the 5-3 majority, Justice Alito held that the arbitrators had exceeded their powers under the FAA by relying on public policy, and that the arbitrators should have instead identified the rule of law from the FAA, federal maritime law, or New York law to determine whether the parties intended to permit class arbitration. Further, the Court noted that under both New York and maritime law, where the contract is ambiguous, evidence of “custom and usage” is relevant and admissible to determine the parties’ intent. The record contained evidence that the settled expectation in the shipping industry was that class arbitration would not be permitted, and that class proceedings are not found in either foreign courts or maritime arbitrations. The Court established a rule that, because arbitration “is a matter of consent, not coercion,” under the FAA arbitrators cannot compel class arbitration unless a contractual basis exists to conclude that the parties to the agreement agreed to it. Applying that rule, the Court held that no such contractual basis existed under the circumstances because the parties had stipulated that there had been no agreement as to class arbitration.

As pertinent to international arbitration, this decision is noteworthy in that the Court took special consideration of certain international commerce customs – e.g., expectations of the international shipping community – in rejecting the public policy arguments which would have made international arbitration more closely resemble U.S.-style litigation.

Some international arbitration practitioners had hoped the Court would address whether, in the wake of Hall Street Assoc. LLC v. Mattel, Inc., 128 S. Ct. 1396 (2008), the “manifest disregard” test is still valid under the FAA. The Court ducked the issue, though, stating only that, assuming such a standard applied, it would have been satisfied under the circumstances. Finally, the decision circumscribes the plurality opinion in Green Tree Financial Corp. v. Bazzle, 559 U.S. 444 (2003), which some courts had (mistakenly, it now seems) interpreted as the Supreme Court’s endorsement of class arbitration notwithstanding the contract’s silence on that point.

Foreign Sovereign Immunities Act Does Not Apply to Foreign Officials


In Samantar v. Yousuf, the U.S. Supreme Court (the Court) considered whether the Foreign Sovereign Immunities Act (FSIA) extends to a foreign official acting in their official capacity. The defendant served as Somali Prime Minister and in other high-ranking positions between 1980 and 1990. The plaintiffs, former citizens of Somalia, brought suit against Samantar for his alleged authorization of torture and extrajudicial killings against plaintiffs and their family members. Samantar asserted immunity under the FSIA and moved to dismiss the case. The district court, after a failed attempt to solicit the views of the U.S. State Department, granted the motion. The Fourth Circuit reversed, holding that the FSIA does not apply to foreign officials.

The Supreme Court, in its opinion by Justice Stevens joined by five other justices, affirmed. The Court held that, while the FSIA governs immunity determinations for foreign states, it does not govern immunity determinations for foreign officials. The Court’s primary task was to determine whether the FSIA’s definition of a “foreign state” included agents or officials of the state. In concluding that it did not, the Court carefully scrutinized the language of the FSIA, finding that nothing in the definition of “foreign state” suggested a Congressional intent to apply the FSIA to individual officials or agents. The Court also rejected Samantar’s argument that, when Congress codified immunity for foreign states in the FSIA, it necessarily codified the related common law of immunity for foreign officials.

The Court concluded its opinion by addressing the concern, which was previously raised by various lower courts confronted with the issue, that excluding foreign state officials from the FSIA’s coverage would encourage plaintiffs with claims against foreign states to artfully plead around the FSIA by naming state officials instead of the state itself. In rejecting this idea, the Court confirmed that the common law doctrines of immunity that it had found were not merged into the FSIA and remained independently cognizable. The Court also stated that if a plaintiff attempted to avoid the FSIA by naming officials alone, the plaintiff could nonetheless have to...
confront the FSIA’s provisions, if the court found the state to be an indispensable party pursuant to Rule 19(a) of the Federal Rules of Civil Procedure. Additionally, the Court found that, in certain cases, the trial court could find that the state, not the named official, was the real party in interest, in which case the FSIA’s provisions would also become applicable. Finally, the Court noted that a party seeking to avoid the FSIA would be required to establish a constitutionally-sufficient basis of personal jurisdiction over the individual defendant, which could be problematic and something that the plaintiff would generally not be required to do if the defendant was a foreign state.1

The immediate significance of the Court’s ruling in Santantar is clear – foreign states will be subject to the FSIA’s statutory scheme, while state officials, at least at the outset of a case, will not be. To the extent foreign state officials continue to be able to claim immunity from suit or liability, they will be required to do so by invoking the common law immunity doctrines that are set forth in the Second Restatement of Law of the Foreign Relations of the United States and which, as the Supreme Court confirmed, will continue to govern claims against them.2

Additional ramifications are also likely. First, notwithstanding the Court’s rejection of the notion that its ruling will lead to artful pleading, plaintiffs bringing cases in response to the actions of foreign governments will likely engage in a comparison of the FSIA and the common law in deciding whom to name as a defendant in their case. Second, the Court’s ruling will force lower courts to pay increased attention to the common law immunity doctrines – which, as the Solicitor General noted in her amicus brief, are “not necessarily co-extensive” with the immunities granted under the FSIA – and likely lead to their continued jurisprudential development, since the doctrines will necessarily play a far more prominent role than they have at any time since 1976. For this reason and because the common law doctrines continue to heavily rely upon individual suggestions concerning immunity from the executive branch, claims of sovereign immunity may well be characterized by the lack of precision that, in part, led to the adoption of the FSIA in the first place.

1 This case note was submitted by James E. Berger, of counsel with Paul, Hastings, Janofsky & Walker LLP; Julie O’Neill, a summer associate with Paul Hastings, also assisted in preparation of this case note.

2 28 U.S.C. § 1330(b) provides that where subject matter jurisdiction has been established in a case against a foreign state and where service of process is effected pursuant to Section 1608 of the FSIA, the court shall have personal jurisdiction over the case. While courts had initially held that personal jurisdiction under Section 1330(b) could not be exercised in a manner inconsistent with the due process considerations set forth in International Shoe v. Washington, 326 U.S. 310 (1945), recent decisions have held that foreign states are not “persons” within the meaning of the Constitution’s Due Process Clause, and that Section 1330(b)’s grant of personal jurisdiction is not tempered by any constitutional considerations. See, e.g., Frontier Resources Azerbaijan Corp. v. State Oil Co. of Azerbaijan, 582 F.3d 393 (2d Cir. 2009).

3 See Mata v. Dichter, 563 F.3d 9, 14 (2d Cir. 2009) (applying Section 66(f) of the Second Restatement to determine whether Israeli official was immune from suit as a result of acts taken in his official capacity).

Washington Supreme Court Holds that State Statutes of Limitations Generally Do Not Apply in Arbitration


The Washington Supreme Court recently upheld a lower court decision vacating an arbitration award, holding that the arbitrator’s ruling that the claimant’s causes of action were time-barred was a “facial legal error,” because Washington State’s statutes of limitations generally do not apply to claims brought in arbitration. In particular, the Court found those statutes, which specifically require that “actions” be commenced or parties “sue” within a certain time period, do not apply in the context of arbitration proceedings, which are not “actions” or “suits,” unless the parties expressly provide for such applicability in their arbitration agreement.

This decision may allow parties to bring claims under existing Washington arbitration agreements long after those same claims would be time-barred if brought in state court. In addition, it could have a broader effect on arbitration, including international arbitration, in at least two ways. First, the Court’s decision was based on its comparison of the language of Washington’s statutes of limitations with the text of Washington’s versions of the Uniform Arbitration Act and Revised Uniform Arbitration Act, which are similar to those adopted in many other states. Thus, other courts could apply a similar analysis to hold that their statutes of limitations do not apply in arbitration. Second, as prior Washington case law suggests that the “facial legal error” standard for vacating arbitration awards can provide a basis for a court to refuse to confirm an arbitration award, see Equity Group, Inc. v. Hidden, 943 P.2d 1167 (Wn. Ct. App. 1997), parties who come to Washington to confirm foreign arbitration awards involving time-barred claims may be unable to obtain the relief they seek.

Factual Background. Broom involved claims of mismanagement relating to retirement investment accounts that Mr. Broom had kept with Morgan Stanley. In connection with those accounts, the parties had executed an arbitration agreement that required the parties to submit disputes to the National Association of Securities Dealers (NASD) for resolution under its Code of Arbitration Procedure (NASD Code). Mr. Broom died in 2002. In 2005, Mr. Broom’s children, the beneficiaries of the retirement accounts, commenced arbitration against Morgan Stanley with the NASD. In the arbitration, Morgan Stanley moved to dismiss the Broom’s claims, asserting among other things that they were barred by the applicable statutes of limitations. The arbitration panel agreed. The Brooms moved to vacate the arbitration award in state superior court. The trial court vacated the award for “facial legal error,” finding that the state statutes of limitations did not apply in arbitration.
The Washington Court of Appeals upheld that ruling, and Morgan Stanley appealed the case to the Washington Supreme Court.

“Facial Legal Error” as Ground to Vacate Arbitration Award. The Court began its analysis by finding that “legal error on the face of the award” is a proper basis to vacate an arbitration award. While the Washington Arbitration Act (WAA) does not expressly include legal error as a ground to vacate an award, the Court held that the enumerated ground – “where the arbitrators exceeded their powers” – includes legal error. As the dissent noted, this approach appears inconsistent with (and would thus properly be preempted by) Section 10 of the Federal Arbitration Act (FAA), which governs arbitrations involving interstate commerce, such as Mr. Broom’s brokerage dealings with Morgan Stanley. Notably, the Court’s “facial legal error” approach appears far broader than the non-statutory “manifest disregard” rationale that numerous federal courts have applied to vacate arbitration awards under the FAA.

The NASD Rule. Morgan Stanley also argued that the NASD Code the parties had adopted to govern their arbitration granted the arbitrators (not the courts) the authority to determine whether a particular state statute of limitations applied to the Brooms’ claims. The Court agreed that the arbitrators were responsible for interpreting the NASD Code, but found this issue was not dispositive because “we determine independently whether our state statutes of limitations may apply to arbitral proceedings.” The Court ultimately found the arbitrators’ right to interpret the NASD Code is limited by Washington case law and statutes, and thus the arbitrators cannot interpret a state statute in contravention of state law.

Statutes of Limitations Do Not Automatically Apply to Arbitrations. The Court then considered whether the arbitral panel’s ruling concerning the applicability of state statutes of limitations was a facial legal error. It noted prior cases holding that arbitration proceedings are not “actions” under Washington statute and that Washington’s catch-all statute of limitations does not apply to arbitration. The Court then looked at the language of the applicable statutes of limitations, which discuss “actions” and parties “suing,” but do not mention arbitrations. It compared this terminology with the language of the WAA, which consistently refers to arbitration as “arbitration,” “hearing,” or “proceeding,” while discussing lawsuits as “civil actions,” “actions,” or “suits.” The Court relied on this distinction, as well as its rulings in prior cases, to hold that arbitrations are not “actions” subject to state statutes of limitations. However, recognizing the concern that its ruling would expose parties to stale and untimely claims, the Court noted that state statutes of limitations will apply in arbitration where parties make express provision for those statutes to apply in their arbitration agreement.

Swiss Federal Supreme Court Sets Aside an International Arbitral Award After More than a Decade as the Arbitral Tribunal had been Misled by a Fraud1


In 1989, Taiwan was interested in acquiring six frigate type warships from the French company, Thomson-CSF (today called and hereinafter referred to as Thales). The French authorities approved the transaction at first, but later revoked a required export license after China had expressed its firm opposition to the deal. Thales thereafter entered into an agreement with the now liquidated Swiss company Frontier AG (Frontier) under which Thales de facto promised Frontier the equivalent of 1 percent of the purchase price of USD 2.5 billion, if the political resistance to the deal could be overcome. The agreement contained an arbitration clause (ICC Rules).

In 1991, the French government authorized the export of the warships. Frontier claimed its commission of USD 25 million and initiated arbitral proceedings in 1992 after Thales had refused to pay. Thales argued that the agreement was null and void as Frontier had been involved in illegal influence peddling with French authorities. However, the arbitral tribunal accepted Frontier’s defense in 1996. It had been convinced by witness statements and evidence presented by Frontier that only licit lobbying had taken place in China. Thales unsuccessfully appealed this award to the Swiss Federal Supreme Court (SFSC). Subsequently, it initiated criminal proceedings in France based on an alleged “procedural fraud,” thereby suspending the enforcement of the award in France.

In 2008, the French examining magistrate closed the criminal investigation because of the death of the main perpetrator, but stated in the closing order that the deceased person had committed fraud in obtaining the arbitral award by having falsified documents and given false testimony. The magistrate held that a complex scheme of illegal influence peddling in France had been the real purpose of the agreement.

On this basis, Thales filed for a reopening of the case with the SFSC. According to Article 123 of the Supreme Court Act (SCA), a case that has become res judicata can be reopened by means of “revision,” if it has been established in a criminal investigation that a crime or a felony had been committed to the detriment of the applicant, even if no conviction had ensued. This provision applies mutatis mutandis to arbitral awards.

The SFSC clarified that criminal proceedings in foreign countries may permit a revision provided that they were conducted in compliance with the procedural guarantees of the pertinent human rights treaties. The court further held that the French investigation had been meticulously

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1 This case note was submitted by Jonathan M. Lloyd of Davis Wright Tremaine LLP, 1201 Third Avenue, Suite 2200, Seattle, WA 98101-3045. Mr. Lloyd may be contacted by telephone at (206) 737-8088 and by e-mail at jonathanlloyd@dwt.com.
Because of a recent decision of the Supreme Court of Canada, parties seeking recognition and enforcement of foreign arbitral awards in Canada must not delay.

In an arbitration held in Russia, Rexx Management Corp., based in the Province of Alberta, Canada, was ordered to pay damages to Yugraneft Corporation. The tribunal issued its award on September 6, 2002, but Yugraneft did not make an application to the Alberta Court of Queen’s Bench for recognition and enforcement of the award until January 27, 2006. While Alberta’s Reciprocal Enforcement of Judgments Act provides for a six-year limitation period for judgments and arbitral awards rendered in reciprocating jurisdictions, Russia is not a reciprocating jurisdiction.

Yugraneft’s delay was the basis for Rexx’s argument that the application was time-barred under the Alberta Limitations Act, which set a two-year limitation period for remedial orders for the payment of money. In response, Yugraneft argued that the foreign arbitral award was a “judgment” for which a ten-year limitation period applied. At the Court of Queen’s Bench and the Alberta Court of Appeal, Rexx’s argument in favor of the two-year limitation period prevailed.

**Supreme Court of Canada Decision**

In Alberta, the International Commercial Arbitration Act, which governs foreign arbitral awards, incorporates both the New York Convention and the UNCITRAL Model Law. Thus, the Alberta courts are required to recognize and enforce arbitral awards except in certain enumerated circumstances. As limitation periods are not listed as an enumerated ground under which the recognition and enforcement of an award may be refused, the Supreme Court first considered whether local limitation periods could apply to foreign arbitral awards. Specifically, Article III of the Convention provides that contracting states shall enforce arbitral awards “in accordance with the rules of procedure of the territory where the award is relied upon.” The Supreme Court concluded that local limitation periods fell within the ambit of such “rules of procedure” under the Convention and thus applied to foreign arbitral awards.

On the question of which limitation period applied to foreign arbitral awards under Alberta’s Limitations Act, the Supreme Court rejected Yugraneft’s contention that an arbitral award is akin to a judgment to which a 10-year limitation period applies. In support of its finding, the Supreme Court cited its decision in *Dell Computer Corp. v. Union des consommateurs*, 2007 SCC 34, for the proposition that “[a]rbitration is part of no state’s judicial system” and “owes its existence to the will of the parties alone.” Unlike a judgment of a court, an arbitral award is not directly enforceable and the Supreme Court found that the legislature could have explicitly included arbitral awards in the definition of “judgment” under the Limitations Act, but failed to do so. Further, applying a 10-year limitation period to foreign arbitral awards would mean that plaintiffs with awards from non-reciprocating jurisdictions would be allowed more time to seek recognition and enforcement of their awards than those from reciprocating jurisdictions. Such a situation would be incongruous, according to the Supreme Court. Ultimately, therefore, the lower court rulings were upheld by the Supreme Court and Yugraneft’s application for recognition and enforcement of the award was time-barred.

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1. This Case Note was submitted by Douglas Harrison, Partner, Stikeman Elliott LLP, Toronto.
Toyo Tire was a partner in a tire manufacturing partnership (GTY) with two other tire manufacturers and distributors, Continental and Yokohama. Continental and Yokohama threatened to dissolve the partnership, acquire Toyo’s share of the partnership’s annual tire production, and seek to enforce a non-competition clause. Pursuant to an arbitration clause in the parties’ Partnership Agreement, Toyo requested arbitration with the International Chamber of Commerce (ICC) International Court of Arbitration, seeking interim injunctive relief in its Request for Arbitration. The same day, Toyo sued Continental, Yokohama and GTY in California state court. After the appellees removed the case to federal court, Toyo sought a temporary restraining order and preliminary injunction, which the district court denied, relying on the Simula case.

The Ninth Circuit began its analysis by noting federal district courts’ general authority to grant equitable relief in aid of arbitration, drawing on its 1988 decision, *PMS Distributing Co. v. Huber & Suhner, A.G.*, 863 F.2d 639. Since it takes time to form an arbitral panel, and as parties may seek strategic advantage by delaying arbitration proceedings, the Ninth Circuit recognized that interim injunctive relief from a district court may be necessary to allow a party to effectively avail itself of an agreement to arbitrate. It therefore held that a federal district court “may issue interim injunctive relief on arbitrable claims if interim relief is necessary to preserve the status quo and the meaningfulness of the arbitration process – provided, of course, that the requirements for granting injunctive relief are otherwise satisfied.”

The court found additional support for this conclusion in Article 23(2) of the ICC Rules, which the parties had selected to govern their dispute, and which expressly permits parties to seek interim relief from other competent judicial authorities pending formation of the arbitral tribunal, and, in appropriate circumstances, even thereafter. The court also noted that seven of the eight other federal Courts of Appeals that have considered the issue have reached the same conclusion (the Eighth Circuit’s *Peabody Coal Sales Co. v. Tampa Elec. Co.*, 36 F.3d 46 (1994) decision being the exception).

The appellees also argued that the appeal was moot, as the ICC had formed the arbitral panel by the time the case reached the Ninth Circuit. The court denied the motion for dismissal, noting only that Article 23(2) of the ICC Rules permitted continued court involvement until the arbitral panel ruled on Toyo’s request for interim relief. However, the court’s overall reasoning suggests that the Ninth Circuit would reach the same result even if the relevant arbitral rules contained different – or no – express language regarding interim judicial relief.

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**Malaysian Historical Salvors SDN, BHV v. The Government Of Malaysia Annulment Committee**

**Splits on the Definition of “Investment”**

In *Malaysian Historical Salvors v. the Government of Malaysia*, ICSID Case No. ARB/05/10, decision on the Application for Annulment (April 1, 2009), two members of the annulment committee held that the Tribunal manifestly had exceeded its powers by failing to exercise jurisdiction over the dispute. This case arose out of a “no find no pay” marine salvage contract between the Applicant, Malaysian Historical Salvors (MHS) and the Respondent, the Government of Malaysia. MHS had salvaged and auctioned $2.98 million USD of cargo from a British vessel that had sunk in 1817. MHS claimed that the Malaysian government had not sold all the items and had given MHS a smaller portion of the profits than the level agreed to in the contract.

Following unsuccessful attempts to commence arbitration proceedings in Malaysia, the Applicant filed a request for arbitration at ICSID based on the Malaysia-UK BIT. Michael Hwang was appointed Sole Arbitrator in the case. The Malaysian government filed a Notice of Objection to ICSID’s jurisdiction stating, among other things that the subject of the dispute was not an “investment.” Mr. Hwang ruled in favor of the Respondent and found that the subject of the contract did not meet the requirements of investment established by Article 25(1) of the ICSID Convention and ICSID jurisprudence found in cases such as: *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco, Joy Mining Machinery Limited v. Arab Republic of Egypt and Patrick Mitchell v. The Democratic Republic of Congo*.

The Tribunal, in refusing jurisdiction, found that MHS did not fulfill all of the following “hallmarks” or “outer limits” of “investment” established in previous ICSID cases: 1) the regularity of profits and returns; 2) contributions; 3) the duration of a contract; 4) the risks assumed under the contract; and 5) the contributions of an investment to the economic development of the host state. The Sole Arbitrator found that the amount invested by MHS did not compare to the investment levels in other cases and that the fifth hallmark, contribution to the economic development of the host state, was not satisfied.

MHS filed an Application of Annulment under Article 52(1)(b) of the ICSID Convention based on the following arguments: 1) the Tribunal had manifestly exceed its powers by using an overly-restrictive definition of “investment” and failing to look at the *travaux preparatoires* (preparatory works) of the ICSID Convention; 2) the Tribunal had elevated certain hallmarks/characteristics of investment, including the condition that an investment contribute to economic development; and 3) that, even if the Tribunal’s analysis was correct, it had introduced additional requirements to the characteristics of investment. Malaysia argued that the Sole...
Award on Jurisdiction with Judge Stephen M. Schwebel and the Annulment Committee split on its decision to annul the Judge Peter Tomka in the majority and Judge Mohamed Shahabuddeen defending the Award.

The Annulment Committee looked to customary international law’s rules on treaty interpretation codified by the Vienna Convention. The Committee searched for the ordinary meaning of investment by analyzing the purpose of the ICSID Convention - which is to promote the flow of international investment by providing a method to settle investment disputes. Next, the two members of the Committee looked at the travaux preparatoires to determine the intentions of the parties involved in creating the ICSID Convention. Schwebel and Tomka examined the draft language of Article 25(1) and determined that a firm definition of investment was purposely excluded.

Schwebel and Tomka concluded that the subject of the contract was consistent with the meaning of “investment” under the Malaysia-UK BIT. The Annulment Decision stated that the Sole Arbitrator had erred in focusing exclusively on the meaning of “investment” under the Article 25(1) of the ICSID Convention. By not finding jurisdiction over the initial award, the Tribunal disregarded the wishes of Malaysia and the United Kingdom to give “investment” a broad definition. While acknowledging the ICSID jurisprudence behind the Sole Arbitrator’s decision, Schwebel and Tomka concluded that the Tribunal “manifestly exceeded its powers” for: 1) failing to take into account the Malaysia-UK BIT; 2) elevating the condition of contributing to the economic development of a host state; and 3) failing to look at the travaux preparatoires of the ICSID Convention.

In his Dissent, Shahabuddeen disagreed with his colleagues on the following: 1) the absence of an agreement on the “investment” did not bar some outer limits/hallmarks; 2) in this case, the outer limits required an investment to contribute to the economic development of the host State; 3) the Tribunal was correct in finding a substantial or significant contribution to the economic development of the host State necessary; 4) the contract did not significantly promote the economic development of Malaysia; and 5) even if the Tribunal had erred in its holding, it did not manifestly exceed its powers.

The Dissent argued that the inability of ICSID delegates to agree on a description of “investment” did not mean that there was no definition of the term. Citing the ICSID Preamble and previous ICSID cases, Shahabuddeen argued that there was language that supported the notion that an investment must contribute to economic development. Some of travaux preparatoires confirmed the idea that States should realize economic development from investment. Furthermore, the fact that ICSID functions under the auspices of the International Bank for Reconstruction and Development (World Bank) affirms the idea that development is an important element of investment. Finally, Shahabuddeen argued that, since the Sole Arbitrator had provided an extensive analysis, there was no evidence that the Tribunal had reached the threshold of “manifestly” exceeding its powers.

1 This case note was submitted by Manka Azefor, an attorney based in Washington, D.C. Manka is a 2010 LL.M. graduate from the George Washington University Law School and practices international development law. She can be reached at mankaazefor@gmail.com.

The Southern District of Florida’s Ruling on Motion to Dismiss Involving a Forum Selection Clause


The Southern District of Florida recently ruled on multiple motions to dismiss brought by defendants in an international dispute.

Plaintiff Quail Cruises (Quail), a Bahamian corporation in the business of operating passenger cruise ships, alleged that defendants conspired to induce Quail to purchase a ship by misrepresenting its true condition. Plaintiff bought the ship by purchasing the stock of Templetom International, Inc. (Templetom), another Bahamian corporation. Templetom’s shares were previously held by Flameck International (Flameck), a Uruguayan corporation controlled by defendant Agencia De Viagens CVC Tur Limitada (CVC), a Brazilian tour operating company.

Another defendant, SeaHawk North America LLC (SeaHawk), was allegedly responsible for the ship’s management and coordinated its operations and inspections. As part of its efforts, SeaHawk contracted with yet another defendant, Lloyd’s Register North America, Inc. (Lloyd’s) for Lloyd’s to inspect the ship and provide its evaluations as to the ship’s seaworthiness. Lloyd’s inspected the vessel both before Quail purchased it pursuant to Lloyd’s contract with SeaHawk, and after Quail purchased it, when Lloyd’s entered a second agreement with Quail.

Quail sued for fraud, negligent misrepresentations, and breach of fiduciary duty, and the defendants moved to dismiss on various grounds. This case note will address the arguments made by Lloyd’s premised on the forum selection clauses in its agreements with SeaHawk and Quail.

Defendant Lloyd’s moved to dismiss for improper venue, arguing that the forum selection clause in the Request for Survey Contract that it entered with Quail after Quail purchased the ship, as well as the contracts between Lloyd’s...
and SeaHawk, required their dispute be resolved by the English courts. The court disagreed with Lloyd’s. The forum selection clause in each agreement spoke of Lloyd’s “Client,” and as Quail was not Lloyd’s client until after it entered a Request for Survey Contract with Lloyd’s, after it purchased the ship; thus, Quail’s claims focused on Lloyd’s actions before Quail become Lloyd’s client were not covered by the forum selection clause in its Contract with Lloyd’s.

However, the court agreed with Lloyd’s second argument (theory of direct benefit estoppel), that Quail should be estopped under the agreements between Lloyd’s and Seahawk from arguing that the forum selection clause in the contract between Lloyd’s and Seahawk does not apply, when Quail is otherwise attempting to find Lloyd’s liable under its rules and regulations for the work done by Lloyd’s at the behest of Seahawk. Although the court noted that the Eleventh Circuit has never held that a nonsignatory can be bound to a forum selection clause under an estoppel theory, the court did note that the Eleventh Circuit has bound nonsignatories to an arbitration agreement to resolve their disputes by arbitration. Quail Cruises, at *13, citing Blinc v. Green Tree Servicing LLC, 400 F.3d 1308, 1312 (11th Cir. 2005), and MS Dealer Serv. Corp. v. Franklin, 177 F.3d 942, 947 (11th Cir. 1999). The court further noted that other Circuits have applied this theory of direct benefit estoppel to nonsignatories beyond merely the arbitration context. Id. at *13, citing Hellenic Inv. Fund, Inc. v. Det Norske Veritas, 464 F.3d 514 (5th Cir. 2006); Am. Bureau of Shipping v. Tencara Shipyard S.P.A., 170 F.3d 349 (2d Cir. 1999).

In ruling on the motion to remand, the Southern District resolved the following question: was the rule of unanimity applicable to actions removed under 12 U.S.C. § 632? This provision of the Edge Act provides the federal district courts with original jurisdiction of suits involving U.S. corporations, where the dispute arises out of international or foreign banking activities, and further provides that “any defendant” may remove an action from state court that would be covered by this statute, “following the procedure for the removal of causes otherwise provided by law.” (Emphasis added.)

Plaintiffs argued that because the other provisions of the law governing removal found at 28 U.S.C. § 1446(a) require all defendants to join a removal petition, the same requirement applied to lawsuits brought under 12 U.S.C. § 632.

The court disagreed. Persuaded by the approach taken to the question of whether the rule of unanimity applied to actions brought under two other statutes (12 U.S.C. § 1819 (4), which governs certain proceedings involving the FDIC, and 12 U.S.C. § 1730(k)(1)(C), which governs certain proceedings involving the FSLIC), the court held that the statute at issue here was similarly a “special removal statute” and by its inclusion of the language “any defendant,” there was no need for all defendants to consent or join a removal petition for it to be effective.

In a Matter of First Impression in the Eleventh Circuit, The Southern District of Florida Denied a Motion to Remand, Finding that the “Rule of Unanimity” Did Not Apply to Actions Removed Under 12 U.S.C. § 632


In December 2009, plaintiffs CI International Fuels, Ltda. (a Colombian entity) and International Fuel Oil Corporation (a Panamanian entity), sued several banks and other defendants in Florida state court because of the transfer of more than $1 million from plaintiffs’ bank accounts in Florida to bank accounts maintained by the non-bank defendants. One of the defendant banks, Regions Bank, initially filed a notice of removal to federal court on February 3, 2010, but not all of the defendants joined the notice of removal. On March 5, 2010, plaintiffs moved to remand to state court, arguing that the removal was ineffective because of the failure to comply with the “rule of unanimity,” whereby all the defendants would have to consent to and join the notice of removal.

In September 2006, an American lumber firm Merrill & Ring Forestry L.P. (Merrill) brought a NAFTA Chapter 11 claim against Canada for its British Columbia logging regulations. The export of logs from British Columbia is subject to federal and provincial legislation requiring a log surplus test prior to the removal of logs from the province. Logs advertised on provincial/federal lists that receive offers below fair market value are deemed surplus items and approved for export licenses. The federal and British Columbia regulations also impose harvesting requirements, fees, and other measures.

Merrill claimed that both the federal and provincial regulatory measures violated the following sections of NAFTA Chapter 11: Article 1102 (national treatment), Article 1105 (fair and equitable treatment), Article 1106(a)(c)& (e) (barring performance requirements) and Article 1110 (banning measures that are tantamount to expropriation). According to Merrill, the log regime forced the company to sell timber in

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1 This case note was submitted by Manjit Gill of Christopher & Weisberg, P.A. who can be reached at mgill@cwiplaw.com.
Canada instead of exporting it to the United States at higher prices. In addition, Merrill argued that the regulations benefited native British Columbia producers and decreased Merrill’s potential profits.

First, the Award addressed Merrill’s argument that Canada violated the national treatment provisions under NAFTA Article 1102. The Tribunal tackled the question of which investor was the “investor in like circumstances.” Merrill argued that the like investors were the native British Columbia producers. The Tribunal disagreed with Merrill and held that, despite the concurrent jurisdiction, the treatment of foreign investors had to be compared to domestic investors subject to the same government regulations. The Tribunal did not find evidence that any measures were based on the nationality of the investor and therefore ruled that Canada did not violate NAFTA national treatment provisions.

Next, the Tribunal turned to the argument that the Log Export Control regime imposed performance requirements. Merrill argued regulations requiring log producers to cut and sort timber violated NAFTA prohibitions against: 1) imposing the export of a given level of goods, 2) purchasing or using preference to services provided in Canada, and 3) restricting the sale of logs in Canada by relating sales to the volume of its exports. Canada contested that these were incidental consequences of the regulations. Furthermore, the Canadian government stated that investors were free to export as much as they choose and pointed out that Merrill did not export 20 percent of the logs it was licensed to export. The Tribunal agreed that the effects of the law were incidental and not prohibited. Moreover, as the Tribunal explained in its Award, the objective of Article 1106 was to “prohibit performance requirements designed to oblige an investor to export more than it otherwise would have exported.” The Tribunal also rejected Merrill’s claim that the log regulations violated Article 1110(1) prohibiting expropriation of investments.

The question of whether Canada violated the fair and equitable treatment was the Tribunal’s most challenging task. Merrill argued that the log regime in Canada was discriminatory and unfair, created an unstable business environment, and violated Merrill’s legitimate expectations. In response, Canada stated that Article 1105(1) provided a minimum standard of treatment based on customary international law that was noted both in Canada’s 1994 Statement of Interpretation for NAFTA and in the July 31, 2001 FTC Interpretations. Canada also contended that the FTC Interpretations — which are binding on NAFTA tribunals — state that fair and equitable treatment does not require treatment beyond customary international law standards.

In this section of the Award, the Tribunal first noted that the meaning of fair and equitable treatment is still unsettled. Next, the Tribunal acknowledged that Article 1105(1) required host countries to treat foreign investors in accordance to international law. However, the Tribunal then stated that it had still to determine what customary international law required regarding fair and equitable treatment and whether the meaning has evolved over time. The Tribunal discussed the 1926 case of LFH Neer and Pauline Neer v. Mexico (Neer). Pope & Talbot, Inc. v. Canada, describing the Neer standard as conduct that would “shock and outrage” reasonable Canadian citizens. The Tribunal held that “except for cases of safety and due process,” the Neer minimum standard of fair and equitable treatment has evolved within the confines of reasonableness.

Next, the Tribunal examined the facts of the case and how they applied to the fair and equitable standard. Since there was no contract in this case, the Tribunal determined which specific intangible interests needed to be protected. There were two possible scenarios of a possible breach: 1) a low threshold one, or the investor’s view of protection based on Article 1105(1), and 2) a high threshold scenario, or the “but for” test. Under the first scenario, the Tribunal acknowledged that there were some problems, albeit not with the entire Canadian log regime. Under the second scenario, the Tribunal accepted Canada’s argument that its policies served a legitimate public interest. In addition, the Tribunal found that Canadian producers were treated identically to foreign producers and therefore the Tribunal could not find a breach of the minimum standard of treatment. The Tribunal held differing views with respect to the applicable threshold, but concurred that Merrill did not prove its damages to the satisfaction of the Tribunal. Consequently, the Tribunal dismissed Merrill’s claim for damages. After ruling in favor of Canada on all claims, the Tribunal deemed it unnecessary to address Canada’s argument that Merrill’s claims were barred by the time limit set in Article 1116(2).

This case note was submitted by Manka Azefor, an attorney based in Washington, D.C. Manka is a 2010 LL.M. graduate from the George Washington University Law School and practices international development law. She can be reached at mankaazefer@gmail.com.

District of Columbia District Court Refuses Republic of Argentina’s Petition To Vacate International Arbitration Award


The Republic of Argentina (Argentina) entered into a bilateral investment treaty with the United Kingdom (UK) in 1990. To address any disputes arising from their investments, Argentina and the UK agreed to a two tiered system of dispute resolution in which the dispute could be submitted to a “competent tribunal” of the country “in whose territory the investment was made,” after which the matter could be referred to arbitration under certain conditions, or the dispute could be submitted directly to international arbitration.
BG Group, a UK company, invested into an Argentinean state-owned distribution company. In 2002, due to the economic crisis, Argentina enacted an emergency law, implementing regulatory measures that negatively impacted BG Group’s investment. Pursuant to the investment treaty, BG Group initiated international arbitration proceedings. In 2006, an arbitral panel commenced proceedings in New York and Washington D.C. Argentina challenged the arbitral panel’s jurisdiction and the appointment of the arbitrator, both of which were rejected. The arbitration proceeded and on December 24, 2007, the arbitral panel unanimously ruled in favour of BG Group and issued an award in the amount of $185,285,485.85 plus costs, attorney’s fees and interest. As a result of being dissatisfied with the outcome, Argentina filed its petition to vacate or modify the award in the District Court for the District of Columbia on the basis that (1) the arbitrators exceeded their authority by disregarding the terms of the parties’ agreement; (2) the arbitral tribunal misunderstood applicable law and failed to correctly apply such law; (3) the International Court of Arbitration exceeded its authority by failing to disqualify the arbitrator; (4) the award was procured by “corruption, fraud, or under means”; and (5) the arbitral tribunal imposed a disproportionate and unfair award. BG Group filed a cross-motion seeking to confirm the award.

The issue before the court was whether vacating the arbitral award in favour of BG Group was warranted. The court denied Argentina’s petition to vacate the award on the basis that:

- it must remain mindful of the principle that judicial review of arbitral awards is extremely limited;
- the court does not sit to hear claims of factual error by an arbitrator;
- a court must confirm an arbitration award where some colourable support for an award can be gleaned from the record;
- because the court does not sit like an appellate court does in reviewing the decision of lower courts, the court has no choice but to deny Argentina’s petition.

The court took a cautious approach in this matter by first considering whether it had subject matter jurisdiction over the dispute. In so far as entertaining Argentina’s arguments to vacate the award under the Federal Arbitration Act, the court found several of Argentina’s arguments lacked merit and there was no evidence to support its argument. However, even if the court had found the tribunal made a legal or factual error in its decision, it was unlikely to vacate the award because it recognized that its role was not that of an appellate court reviewing the decision.

German Appellate Court Prohibits Service of “Civil” Complaint by New Zealand Competition Commission Seeking Antitrust Fines

Unnamed Petitioner v. State of Hesse, Court of Appeals in Frankfurt am Main (Docket No. 20 VA 15/09, February 8, 2010).

The Court of Appeals in Frankfurt held that a complaint brought by the New Zealand Commerce Commission (NZCC) in the High Court in Auckland, seeking fines for alleged antitrust violations, cannot be served in Germany because it is not a “civil or commercial matter” within the meaning of the applicable international treaty.

Petitioner is a citizen and resident of Germany and a former employee of an airline based in New Zealand. The NZCC had sued Petitioner, the airline, and various other defendants in the High Court in Auckland, claiming that the defendants had violated the New Zealand Competition Act and asking the High Court to impose fines. With the help of the competent judicial authorities of Respondent (the German state of Hesse), the proceedings were served on Petitioner at his home near Frankfurt. Petitioner challenged the validity of the service of process in the Frankfurt Court of Appeals, arguing that the service lacked a legal basis. In a case of first impression, the Court of Appeals agreed, declared the service of process null and void, and ordered Respondent not to issue a certificate of service to be used in the New Zealand proceedings. The Court of Appeals first pointed out that the case was not one under the Hague Service Convention (to which New Zealand is not a party) but was instead governed by the Anglo-German Convention Regarding Legal Proceedings in Civil and Commercial Matters of 1928. Both conventions apply only to “civil or commercial matters.” The Court of Appeals then noted that the dispute constituted a “civil” case under New Zealand law and that the High Court in Auckland had entered it on its commercial list. According to the Court of Appeals, however, German law applied a much more narrow definition of “civil” matters than the laws of New Zealand and other common law jurisdictions. Under German law, a “civil” matter was not present whenever the plaintiff, acting under the color of state authority and in pursuit of the public interest, was seeking fines payable to the state treasury in order to impose sanctions for an alleged offense. The Court of Appeals distinguished the case from situations where plaintiffs sought punitive or treble damages to obtain redress for an alleged loss. In this latter category of cases, German courts regularly allow service of process under the Hague Service Convention because of the “private” nature of the dispute.

This is the first published opinion by a German court on whether service of process in Germany is permitted where a foreign public authority has filed a lawsuit, classified as “civil” in its home country, in which fines are sought as a sanction for
an alleged offense. As Respondent has chosen not to file an appeal with the German Federal Supreme Court, the decision by the Court of Appeals is final and will serve as precedent until further notice. Needless to say, its relevance is not limited to cases from New Zealand but may also apply to lawsuits brought, for example, by the U.S. Securities and Exchange Commission.

1 This case note was submitted by Alfried Heidbrink, a partner with Lindenpartners in Berlin, Germany. Mr. Heidbrink represented the petitioner in this matter. He may be contacted at heidbrink@lindenpartners.eu.

Second Circuit Rules That Federal Courts Must Have Jurisdiction Over the Party or Party’s Property Before Considering Enforcement of an International Arbitral Award but That Foreign States and Their Agents Are Not Entitled to Jurisdictional Protection

Frontera Resources Azerbaijan Corporation v. State Oil Company of the Azerbaijan Republic, 582 F.3d 393 (2d Cir. 2009).

The United States Court of Appeals for the Second Circuit ruled that before a court can consider enforcing an international arbitral award under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (Convention), it must determine that it has personal or quasi in rem jurisdiction. However, the court also held that foreign states and their agents are not entitled to jurisdictional protection under the Due Process Clause.

In 1998, Frontera Resources Azerbaijan Corporation (Frontera) entered into an agreement with the State Oil Company of the Azerbaijan Republic (State Oil) for Frontera to develop and manage oil deposits in Azerbaijan and deliver oil to State Oil. In 2000, the parties got in a dispute over State Oil’s refusal to pay for some oil, and consequently, Frontera sought to sell oil that was meant for State Oil to parties outside of the agreement. State Oil responded by blocking Frontera’s oil exports and seizing the oil.

Frontera sought payment for the previously-delivered oil and the seized oil, but State Oil refused to pay, and Frontera served State Oil with a request for arbitration, as provided for in the agreement. After a full hearing, a Swedish arbitral tribunal found in favor of Frontera.

In 2006, Frontera filed a petition in the Southern District of New York to confirm the award under Article II(2) of the Convention. The district court dismissed the petition for lack of personal or in rem jurisdiction. On appeal, Frontera argued that personal jurisdiction was not required and that State Oil was not entitled to protection under the Due Process Clause.

The Second Circuit noted that although it had previously avoided determining whether personal or quasi in rem jurisdiction was required to confirm international arbitral awards, numerous other courts have required such jurisdiction. According to statutory law implementing the Convention, courts must confirm awards unless they find that a basis for refusing or deferring recognition or enforcement exists, as specified in the Convention. The court reasoned that although the Convention restricts the manner in which a party can challenge a request for confirmation of an award, it does not “alter the fundamental requirement of jurisdiction over the party against whom enforcement is being sought.” Accordingly, the Second Circuit held that the district court was correct in treating personal jurisdiction as a prerequisite for enforcing Frontera’s award.

The Second Circuit next considered whether State Oil was entitled to protection under the Due Process Clause. In analyzing the district court’s decision, the court noted that the lower court was bound by the precedent set in the 1981 case, Texas Trading & Milling Corp. v. Federal Republic of Nigeria. The Second Circuit, however, stated that since its holding in that case, “the case law has marched in a different direction.” Relying largely on the D.C. Circuit’s analysis in Price v. Socialist People’s Libyan Arab Jamahiriya, the court reasoned that if the States of the Union have no rights under the Due Process Clause, then “we do not see why foreign states, as sovereigns wholly outside the Union, should be in a more favored position.” The Second Circuit overruled the Texas Trading case and held that the district court erred in holding that State Oil was entitled to jurisdictional protection under the Due Process Clause.

The Second Circuit went a step further and stated that if State Oil is an agent of the Azerbaijani state, then it is likewise not entitled to due process rights. However, the court noted that if State Oil is not an agent but is merely owned by a foreign state, then the court would have to determine whether it is entitled to protection under the U.S. Constitution – a question that the D.C. Circuit has called “far from obvious.” As this question was not before the court, the Second Circuit remanded the case for a determination of whether State Oil is an agent of Azerbaijan and, if not, whether it is entitled to jurisdictional protection under the Due Process Clause.

The court’s holding in this case may have a significant impact on those who do business with foreign states and their agents, and it will likely increase the number of petitions in the Second Circuit for the enforcement of arbitral awards against foreign states and their agents. However, the full extent of this impact will not be known until the court decides whether foreign corporations are entitled to Due Process protections.

1 This case note was submitted by Joi Leonard.
CALENDAR OF EVENTS

2011

February 9-15
ABA Midyear Meeting
Atlanta, Georgia
Marriott Marquis

April 5-9
Section Spring Meeting
Washington D.C.

August 4-9
ABA Annual Meeting
Toronto, Canada

October 11-15
Section Fall Meeting
Dublin, Ireland

October 30-November 4
IBA Annual Conference
Dubai, UAE
International Arbitration Committee
Laurie E. Foster, Co-Chair
Edna Sussman, Co-Chair
Jose I. Astigarraga, Vice-Chair
Ethan A. Berghoff, Vice-Chair
Alexander Bernet Blumrosen, Vice-Chair
Michelangelo Cicogna, Vice-Chair
Richard Deutsch, Vice-Chair
Catherine M. Doll, Vice-Chair
Joshua L. Fellenbaum, Vice-Chair
Mark W. Friedman, Vice-Chair
Steven Mark Gee, Vice-Chair
Manuel Liatowitsch, Vice-Chair
Steven Lee Smith, Vice-Chair
Mohammad A. Syed, Vice-Chair
Alexander Vesselinovitch, Vice-Chair

Kevin Michael O’Gorman, Immediate Past Co-Chair
Marc J. Goldstein, Senior Advisor
Rusty Park, Senior Advisor
Louise Ellen Teitz, Senior Advisor

International Litigation Committee
Theodore Edelman, Co-Chair
Elaine Merlin, Co-Chair
Maria Cristina Cardenas, Vice-Chair
Scott Fairley, Vice-Chair
Patrick Goudreau, Vice-Chair
Dieter Hofmann, Vice-Chair
Alison LaBoissonniere, Vice-Chair
Eddie James Varon Levy, Vice-Chair
Nathalie Meyer-Fabre, Vice-Chair
Joseph I. Raia, Vice-Chair
Kenneth Rashbaum, Vice-Chair
Charles D. Schmerler, Vice-Chair
Ekaterina Schoenefeld, Vice-Chair
Mohammad A. Syed, Vice-Chair

Alexander Bernet Blumrosen, Immediate Past Co-Chair
Steven M. Richman, Immediate Past Co-Chair

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International Mediation Committee
Birgit Kurtz, Co-Chair
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William Arthur Herbert, Vice-Chair
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Gary P. Poon, Vice-Chair
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Duncan H. Cameron, Immediate Past Co-Chair