The
Baker McKenzie
International Arbitration Yearbook
United States
United States

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A. Legislation and rules

The United States is a federal jurisdiction that has arbitration-related legislation at both the federal (national) and state levels. The Federal Arbitration Act (“FAA”) of 1925 continues to be the controlling federal arbitration statute and reflects a well-established national policy that strongly favors arbitration as an alternate means of dispute resolution. There has been no federal legislation in the past year that amends or alters the FAA.

Most state arbitration statutes reflect the same pro-arbitration posture, at least in the commercial context. Some state jurisdictions, such as California, have nevertheless sought to limit the validity of arbitration agreements in the consumer and employment contexts. As state arbitration statutes are subservient to the FAA where they conflict, however, it remains to be seen whether such state legislation would withstand federal scrutiny.

Additionally, efforts at the federal level to limit the effectiveness of arbitration clauses in certain consumer contracts have been largely ineffective. For instance, the Consumer Financial Protection Bureau (“CFPB”), which is a federal administrative office charged with safeguarding the interests of consumers in financial transactions,

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issued an administrative rule in July 2017 which: (1) invalidated pre-dispute arbitration clauses in certain consumer financial contracts that prohibited consumer class action court proceedings; and (2) required certain financial institutions involved in arbitrations commenced pursuant to a pre-dispute arbitration clause to submit records to the CFPB about those matters.

However, in November 2017, a joint Congressional resolution signed by the President invalidated that rule. Consequently, the CFPB’s administrative effort to circumvent US Supreme Court rulings that permit the use of arbitration clauses to limit collective consumer legal action ultimately failed.

B. Cases

B.1 New York state court vacates award for manifest disregard of the law

In *Daesang Corporation v. The NutraSweet Company*, the Commercial Division of the New York State Supreme Court partially vacated a USD 100 million arbitration award that was subject to the New York Convention on grounds that the award manifestly disregarded New York law.

The underlying dispute arose out of a 2003 agreement between The NutraSweet Company (“NutraSweet”) and the Daesang Corporation (“Daesang”) pursuant to which NutraSweet would purchase Daesang’s aspartame business for USD 79,250,000 to be paid in installments over a five-year period. As part of the agreement, the parties executed a Joint Defense and Confidentiality Agreement, which in relevant part provided that NutraSweet could rescind the transaction within five years if any customer with global annual aspartame purchases in excess of one million pounds (mass) filed an antitrust claim concerning the business that NutraSweet was acquiring. In the transactional documents, Daesang further represented

that it was in compliance with all relevant laws, including US antitrust laws.

Three years after the transaction was concluded, NutraSweet and Daesang were sued in US federal court in Pennsylvania by a class of aspartame purchasers who alleged violations of the US federal antitrust laws (the “Antitrust Lawsuit”). NutraSweet subsequently told Daesang that NutraSweet was rescinding the transaction because of the Antitrust Lawsuit and demanded that Daesang return all payments that NutraSweet had made to that point. Daesang responded to that demand by declaring NutraSweet to be in default and itself demanding all remaining payments that NutraSweet would otherwise have owed under the contract.

In 2008, Daesang commenced an arbitration against NutraSweet pursuant to an arbitration agreement that was contained the transaction documents, claiming the balance of the purchase price payments that NutraSweet would have owed. NutraSweet responded by asserting several defenses, including a right to rescission based on the Antitrust Lawsuit. Additionally, NutraSweet counterclaimed for breach of contract and fraudulent inducement, alleging that Daesang knew it was in breach of the antitrust laws at the time it entered into the transaction, but nevertheless warranted that it was in compliance with those laws. In support of the latter contention, NutraSweet offered an affidavit that Daesang’s president had submitted in the Antitrust Lawsuit which purportedly admitted that Daesang had engaged in 10-year conspiracy with other aspartame producers to violate the antitrust laws.

In 2012, the tribunal in the underlying arbitration issued a partial award dismissing all of NutraSweet’s counterclaims and defenses. After receiving that partial award, NutraSweet contended that the tribunal had failed to address NutraSweet’s breach of contract counterclaim against Daesang.

In 2016, the tribunal then issued a final award, which concluded that NutraSweet had waived its breach of contract counterclaim. The final
award granted Daesang in excess of USD 100 million in damages on its claims.

Later that year, Daesang filed a petition in New York state court to confirm the final award. In response, NutraSweet cross-petitioned to vacate the award, in relevant part on grounds that the arbitrators had manifestly disregarded New York law by failing to entertain NutraSweet’s breach of contract and fraudulent inducement counterclaims on the merits.

In the enforcement proceedings, the New York state court rejected NutraSweet’s contention that the arbitrators had manifestly disregarded New York law when they refused to accept NutraSweet’s contention that the Antitrust Lawsuit entitled NutraSweet to rescission. The court found, however, that the arbitrators had manifestly disregarded New York law when they rejected NutraSweet’s breach of contract and fraudulent inducement counterclaims, because the court determined that: (1) the evidence showed that NutraSweet had not waived its counterclaims; and (2) the arbitrators had ignored a principle of New York law that had been presented to them which would have allowed a claim for fraud in the inducement to succeed.

The court therefore vacated that portion of the award that rejected NutraSweet’s breach of contract and fraudulent inducement counterclaims and remanded the matter back to the arbitrators to address those issues. As of the time of this publication, the decision was under appeal.

B.2 US Federal trial court declines to enforce award that it determines was not yet binding

In *Diag Human v. Czech Rep. - Ministry of Health*, the US District Court for the District of Columbia dismissed a petition to enforce a 2008 arbitral award obtained against the Czech Republic Ministry of

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Health on grounds that the award was not final and was therefore not enforceable under the New York Convention.

The underlying dispute, which arose in the early 1990s, concerned allegations by Diag Human (“Diag”), which is a Lichtenstein-registered medical technology company, that the Czech Ministry of Health (“Ministry”) had taken actions which had destroyed Diag’s blood plasma and blood plasma derivatives trading business. After their disputes arose, Diag and the Ministry entered into a submission agreement which provided that their differences would be arbitrated. In relevant part, the submission agreement also set forth an appellate procedure which provided that an aggrieved party could submit an award to a second arbitral tribunal for review within 30 days of receiving the impugned award. Under the appellate review process that the submission agreement established, awards would become final if not appealed to an appellate tribunal within the 30-day deadline or once an appellate award was issued.

In March of 1997, a merits tribunal established pursuant to the submission agreement issued an interim award on liability which found the Ministry liable to Diag. The Ministry submitted that award for review, and in 1998, the appellate tribunal confirmed the award.

In June of 2002, the merits tribunal then issued a partial award on quantum that required the Ministry to pay Diag approximately CZK 327 million in damages (“2002 Partial Award”). The Ministry also submitted the 2002 Partial Award to an appellate tribunal for review. The appellate tribunal upheld the 2002 Partial Award and Ministry subsequently satisfied it.

In 2005, the merits tribunal in the underlying dispute then asked the parties to jointly agree upon the appointment of an expert to determine the amount of any further damages that Diag might be owed beyond the amounts determined in the 2002 Partial Award. An expert was agreed upon, and in 2008, the merits tribunal issued a final award that required the Ministry to pay Diag CZK 8.3 billion plus interest, as
well as daily post-award interest of CZK 1.2 million (“2008 Final Award”).

Both Diag and the Ministry submitted the 2008 Final Award to a third appellate tribunal for review, but in 2010, while that review was pending, Diag withdrew its request. In 2013, while the third appellate review of the 2008 Final Award was pending, Diag petitioned the US District Court for the District of Columbia to enforce the 2008 Final Award. The Ministry responded by moving on several grounds to dismiss the petition to enforce the 2008 Final Award.

In 2014, while the judicial enforcement petition of the 2008 Final Award was pending in the US district court, the third appellate tribunal issued its appellate award. The third appellate award merely discontinued the underlying arbitration and appeal and required each party to bear its own costs.

In 2017, after that third appellate award was issued, the US District Court for the District of Columbia issued its decision on the enforcement petition that had been pending before it since 2013. The district court refused to grant the enforcement application on grounds that “there is no award to enforce.”

Specifically, the court found that the parties’ submission agreement had created a process for resolving their disputes which itself determined when any arbitral award would become final. In relevant part, the court concluded that awards did not become final if they were submitted to an appellate tribunal for review within the relevant timeframes established by the submission agreement, and that Diag had in fact submitted the 2008 Final Award for appellate review within those deadlines, thereby preventing the award from taking effect or becoming final.

The court further found that under the express terms of the submission agreement, while the 2008 Final Award remained under review (and by operation not final or effective), Diag discontinued the review, after which the appellate tribunal terminated the arbitration. The
enforcement court therefore concluded that the 2008 Final Award had become stuck in a state of legal limbo and never became binding on the parties. The court accordingly concluded that the award was not final and binding within the meaning of Article V.1(e) of the New York Convention and consequently refused to enforce it.

B.3 US Federal appellate court refuses to hold alleged instrumentalities of an award debtor state liable for purportedly fraudulent transfers to the state

In *Crystallex International Corp. v. Petróleos de Venezuela, S.A.*, the United States Court of Appeals for the Third Circuit refused to permit an award creditor who had successfully enforced an award against the Bolivarian Republic of Venezuela (“Venezuela”) to employ Delaware’s version of the Uniform Fraudulent Transfer Act (“UFTA”) to claw back assets that were transferred out of the United States to Venezuela by companies that Venezuela owned on grounds that Venezuela was not the transferor of those assets as Delaware’s version of UFTA requires.

The underlying dispute concerned a USD 1.2 billion award that Crystallex International Corp. (“Crystallex”) obtained against Venezuela in 2016 over the expropriation of rights that Crystallex held to a gold mine in Venezuela (the “Award”). In 2016, Crystallex petitioned the US District Court for the District of Columbia to enforce the Award, and in 2017, the Washington court granted that petition.

In 2015, while it was waiting to receive the Award, Crystallex filed suit in the US District Court for the District of Delaware against Petróleos de Venezuela, S.A. (“PDVSA”), PDV Holding, Inc. (“PDVH”) and CITGO Holding, Inc. (“CITGO Holding”), alleging that PDVSA (which is a Venezuelan corporation wholly owned by Venezuela), PDVH (which is wholly owned by PDVSA) and CITGO Holding (which is owned by PDVH) were all assisting Venezuela in

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5 Nos. 16-4012 & 17-1439 (3d Cir. 2017).
preventing its creditors from recovering any monies that Venezuela would owe from arbitral awards such as the Award that Crystallex subsequently obtained (the “Delaware Action”). Specifically, Crystallex alleged that PDVSA had directed PDVH to direct CITGO Holding to issue USD 2.8 billion in debt in the US and to then transfer the resulting funds to PDVH as a dividend, which then issued a dividend in the same amount to PDVSA.

Crystallex alleged that the entire transaction was really just a transfer undertaken by Venezuela to ensure that could repatriate funds out of the US to itself. Specifically, Crystallex alleged that the scheme permitted Venezuela to indirectly transfer USD 2.8 billion out of the US to itself, where those funds could not be reached by Venezuela’s creditors.

In the Delaware Action, Crystallex sought to recover the USD 2.8 billion transferred out of the US to PDVSA in Venezuela on grounds that the transaction was a fraudulent transfer within the meaning of Delaware’s version of the UFTA. As a general matter, the UFTA - versions of which have been enacted in 43 US states, the District of Columbia and the US Virgin Islands - permits creditors to unwind transfers made by a debtor for the general purpose of thwarting recovery by the debtor’s creditors. A key aspect of UFTA, however, is that it facially only prohibits asset transfers by debtors, and not transfers to debtors, which creditors can typically reach without the assistance of UFTA.

Initially, Crystallex enjoyed success in the Delaware Action and defeated a motion by PDVSA to dismiss Crystallex’s claims. Essentially, the trial court allowed Crystallex to proceed with its fraudulent transfer claims on the theory that PDVH could be considered a non-debtor transferor for purposes of the UFTA.

PDVH appealed that conclusion to the Third Circuit, however, which reversed the trial court and granted PDVH’s motion to dismiss the Delaware Action. While recognizing the potentially inequitable consequences of its ruling, the Third Circuit concluded that it was
constrained to grant the motion to dismiss because: (1) transfers by non-debtors cannot be fraudulent within the meaning of the UFTA; and (2) the two potential debtors in this case - Venezuela and PDVSA - were not the transferors of the funds at issue, but were instead the recipients. The Third Circuit therefore found that Crystallex could not employ Delaware’s version of the UFTA to unwind the USD 2.8 billion transfer from Citgo Holding to PDVSA.

B.4 Court refuses to enforce award that was set aside by a body deemed to be a competent authority within the meaning of the New York Convention

In *Getma International v. Republic of Guinea*, the United States Court of Appeals for the District of Columbia refused to enforce an award set aside by the Common Court of Justice and Arbitration of the Organization for the Harmonization of Business Law in Africa (“CCJA”), which is a court of supranational jurisdiction for western and central African states.

The underlying dispute arose out of the Republic of Guinea’s (“Guinea”) decision to terminate a twenty-five year concession agreement that Getma International (“Getma”) had won to operate and expand the port of Conakry in Guinea. Shortly after Guinea terminated that concession, Getma demanded that Guinea arbitrate its dispute under the Arbitration Rules of the CCJA as the concession agreement required.

Guinea and Getma selected a three-person tribunal to resolve their dispute, all of whom were based in France. Following selection of the tribunal, the CCJA fixed the arbitrators’ fees at EUR 61,000.

Fourteen months later, the three arbitrators collectively approached the CCJA’s secretary general and requested that their fees be increased from EUR 61,000 to EUR 450,000. The CCJA denied that request, noting that it was the only authority permitted to establish arbitrator fees and that it had already done so.
The arbitrators subsequently continued with the matter and drafted an award, but before releasing it, wrote two letters to the CCJA renewing their request to increase their fees. Getma also sent the CCJA a letter requesting that the CCJA consider the arbitrators’ demand for increased fees. The CCJA nevertheless remained firm in its position that the fees would stay at EUR 61,000.

In response to the CCJA’s denial, the arbitrators told the parties that they would not release the award until the parties paid them the EUR 450,000 that they had demanded. After learning of that fact, the CCJA secretary general told the arbitrators that their fee request was void and specifically wrote to Getma to inform it that any award it might receive in its favor would be rendered invalid if it concluded an unauthorized fee arrangement with the arbitrators.

The arbitrators subsequently issued an award in Getma’s favor that required Guinea to pay EUR 39 million, plus interest, but continued to demand EUR 450,000 in fees. Getma eventually paid the arbitrators EUR 225,000, or half of that amount. The arbitrators thereafter filed suit in Paris to collect from Getma the balance of the EUR 450,000 they had demanded on the basis that Getma was jointly and severally liable for the full amount of the arbitrators’ fees.

Guinea subsequently filed an annulment petition with the CCJA, requesting that the award be invalidated because of the issues surround the arbitrators’ fee requests. The CCJA, as it had signaled it would do, granted Guinea’s request.

Despite invalidation of the award by the CCJA, Getma sought to enforce the annulled award in the US District Court for the District of Washington. That court refused to enforce the award under Article V.1(e) of the New York Convention on the basis that it had been set aside by a competent authority. On appeal, the US Court of Appeals for the District of Columbia similarly refused to enforce the award.
The appellate court found that the CCJA was a competent authority capable of setting aside the award within the meaning of Article V.1(e) of the New York Convention. While the appellate court recognized that it could, in extremely limited circumstances, enforce an award that had been annulled by a competent authority, it concluded that those circumstances were not present in that case and therefore refused to recognize or enforce the award.

B.5 Court affirms sanctions against plaintiff’s attorney for meritless efforts to avoid arbitration

In *Hunt v. Moore Brothers*, the United States Court of Appeals for the Seventh Circuit upheld sanctions personally imposed on a party’s counsel by the United States District Court for the Southern District of Illinois on grounds that the counsel had frivolously sought to avoid arbitration.

The underlying dispute concerned differences that James Hunt (“Hunt”), who was a truck driver, had with his employer, Moore Brothers, concerning the terms of his independent contractor operating agreement. The operating agreement contained an arbitration clause which required disputes to be resolved by arbitration.

When a dispute arose under the contract, Hunt’s counsel ignored the arbitration clause and filed a complaint in federal court which alleged in relevant part that Moore Brothers had held Hunt in a state of involuntary servitude, had violated the Racketeer Influenced and Corrupt Organizations Act, federal antitrust laws, the Illinois Employee Classification Act, and had allegedly committed the Illinois tort of false representation. In response, Moore Brothers moved to compel arbitration of Hunt’s claims pursuant to the arbitration clause found in the contract.

Hunt’s counsel responded to the motion to compel by primarily alleging that the arbitration clause was unenforceable as a matter of

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6 No. 16-2055 (7th Cir. 2017).
Nebraska law. Moore Brothers ultimately responded with a motion for sanctions, and as the Seventh Circuit noted, “[t]ired of what it regarded as a flood of frivolous argument and motions,” the district court granted Moore Brothers’ sanctions motion and ordered Hunt’s counsel to personally pay USD 7,500. The district court subsequently dismissed Hunt’s court action.

Hunt’s counsel appealed the imposition of sanctions, and the Seventh Circuit affirmed the district court’s order, finding that the matter was a “simple” commercial dispute that Hunt’s counsel unreasonably “blew . . . up . . . beyond all rational proportion.” Moreover, the Seventh Circuit noted that Hunt’s counsel’s “complaint was a disaster” and that counsel’s “efforts to avoid arbitration were meritless.”

Ultimately, however, the Seventh Circuit appears to have found it particularly relevant that in seeking to avoid arbitration, Hunt’s counsel had “disregard[ed] . . . the long line of Supreme Court decisions upholding the enforceability of arbitration clauses exactly like the one in the Hunt-Moore Agreements.” The Seventh Circuit therefore upheld the personally imposed sanctions.

C. Funding in international arbitration

While the US has a long history of permitting contingency actions and other conditional fee arrangements, third-party funding of both litigation and arbitration is a relatively new phenomenon that has nevertheless gained significant prominence over the last ten to fifteen years. The market for funding international arbitrations is arguably the most developed of the US third-party funding markets and is becoming a widely accepted facet of international arbitration practice within the US.

In the early 2000s, third-party funding of international arbitrations in the United States was a relatively new concept that had not yet achieved widespread acceptance. It was typically considered to be the province of a limited number of specialized funders and to be most
frequently employed by resource-constrained claimants in investor-state arbitrations as a means of pursuing claims that might otherwise have gone unprosecuted. There was general skepticism around the practice of third-party funding, and the US international arbitration community was particularly concerned about perceived ethical issues that third-party funding implicated, such as champerty, maintenance and other ethical matters (such as compromised privilege).

Over the past decade, however, as the number of investor-state claims has increased and as funders have continued to educate the international arbitration community about the benefits and propriety of third-party funding in both the investor-state and commercial spheres, the practice has become widely accepted. While the practice has not been regulated or widely tested in US courts, many of the ethical concerns that previously existed within the US international arbitration community have been largely dispelled. Indeed, attitudes towards third-party funding in international arbitration within the US have shifted so dramatically that claimants now oftentimes wish to announce that they have obtained third-party funding to demonstrate the strength of their claims and the depth of their resources. Some clients have even begun to employ third-party funding as a means of managing legal budgets and controlling legal spend.

Moreover, the US market has become sufficiently sophisticated that third-party funders now offer portfolio funding products to companies and law firms whereby the funder provides a set amount of financing that can be applied against multiple cases that meet the agreed funding criteria. Portfolio arrangements, which can provide significant efficiency benefits to clients, law firms, and funders, are merely the latest evolution in the ever-developing third-party funding market, which seems poised to continue growing in the US for the foreseeable future.