

## Incompetent Drafting and Complex Laws: Automatically Waiving Set-Aside of Foreign Arbitration Awards in the United States

Tiina E. Vaisanen

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# Incompetent Drafting and Complex Laws: Automatically Waiving Set-Aside of Foreign Arbitration Awards in the United States

Tiina E. Vaisanen†

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## Introduction

Imagine a situation in which a well-known U.S. chain—perhaps whose logo with golden arches, an apple with a bite taken from its right side, or a red bull's-eye has been seared into Americans' consciousness and is internationally recognizable—decides to open more branches abroad.<sup>1</sup> The chain seeks out foreign investors and, seeing a prime opportunity despite local opposition, begins negotiations with potential partners in the Middle East. During these negotiations, the chain insists that the foreign branch imitate other stores of the U.S. chain as closely as possible to maintain the integrity of its brand internationally. The deal is worth millions, and consequently the parties spend significant time ironing out the numerous details, among them the prominence of the chain's logo, the interior design of the business space, minimum revenue requirements, and other factors common to all branches of the chain worldwide.

Imagine further that when drafting the agreement between the chain and the investors, the parties agree to submit any disputes arising from the transaction to international commercial arbitration rather than leaving dispute resolution to a court.<sup>2</sup> However, although the parties call in numer-

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1. The fact pattern in the hypothetical is based on *Alghanim & Sons*, which involved a dispute over several Middle Eastern branches of the U.S. toy store chain Toys "R" Us. See Yusuf Ahmed Alghanim & Sons, W.L.L. v. Toys "R" Us, Inc., 126 F.3d 15, 17-18 (2d Cir. 1997). Facts have been added, deleted, and altered for the purposes of this hypothetical.

2. Submitting disputes to international commercial arbitration is not out of the ordinary in cross-border transactions. See PRICEWATERHOUSECOOPERS & SCH. OF INT'L ARBITRATION, QUEEN MARY, UNIV. OF LONDON, INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006 2 (2006), available at [http://www.pwc.be/en\\_BE/be/publications/ia-study-pwc-06.pdf](http://www.pwc.be/en_BE/be/publications/ia-study-pwc-06.pdf) [hereinafter INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006] (finding that 73% of respondents in an empirical study researching the views of leading corporations towards the use of international commercial arbitration to resolve cross-border disputes use international commercial arbitration as either the sole dispute resolution mechanism or in concert with other mechanisms). Companies conducting cross-border business select international commercial arbitration as their preferred method of dispute resolution mainly due to the flexibility and autonomy inherent in the arbitration process. See *id.* at 6 (citing "[f]lexibility of procedure" as arbitration's most widely recognized advantage and referring to autonomy by noting that "[t]he active participation of the parties in determining and shaping the procedure inspires confidence in the process."); see also Peter Behrens, *Arbitration as an Instrument of Conflict Resolution in International Trade: Its Basis and Limits*, in CONFLICT RESOLUTION IN INTERNATIONAL TRADE: A SYMPOSIUM 14 (Daniel Friedmann & Ernst-Joachim Mestmäcker, eds. 1993) ("[A]rbitration roots in the principle of party autonomy."); *infra* Part I.A. Furthermore, these arbitration cases are often worth millions of dollars. In 2010, the amount in dispute was under \$1 million in only 24.1% of new arbitration cases before the International Chamber of Commerce in Paris. See Int'l Ct. of Arbitration, *Facts and Figures on ICC Arbitration - 2010 Statistical Report*, INT'L CHAMBER COM. (Feb. 2011), <http://iccwbo.org/court/arbitration/index.html?id=41190>.

ous lawyers with the relevant expertise to work out the provisions relating to international taxation, foreign employment laws and such, when it comes to the arbitration clause the parties spend barely any time negotiating the arbitration details. Instead, in accordance with popular practice, they insert into the agreement a short and simple standard arbitration clause recommended by the International Chamber of Commerce (ICC): “All disputes arising out of or in connection with the present contract shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with the said Rules.”<sup>3</sup> The parties do, however, specifically agree that any arbitration shall occur in the United States, believing that the venue will be fair and efficient for both parties.

The parties sign the agreement and the branches in the Middle East begin operation. One day the CEO of the U.S. chain visits these branches and sees that they in no way mirror the U.S. chain. Specifically, the logo—those famous golden arches or perhaps the celebrated apple with a bite taken from its right side—is not clearly and respectfully displayed, the standards of the branches do not mirror those of the U.S. chain, and the revenues are pitiful. The CEO, concerned about the harm this will do to the brand’s international reputation, demands that the branch fulfill the requirements of the agreement. The branch fails to do so, and, after futile communication between the parties and mounting political tension in the Middle East, the frustrated U.S. chain terminates the agreement and looks for new investors. Consequently, the Middle Eastern investors submit the issue to arbitration, and, in accordance with the agreement, the parties arbitrate in the United States. Unfortunately, during the arbitration proceedings, the U.S. chain is not given a full and fair chance to be heard. At the close of these flawed proceedings, the arbitrators award the Middle Eastern branches \$40 million in damages for breach of contract.

The U.S. chain, unhappy with the arbitrators’ decision, subsequently seeks to have the award set aside in a U.S. court on the ground that the arbitration proceedings were flawed. If the U.S. chain were to succeed in its quest, it would not have to pay damages and the award would be nullified. Now imagine that, much to the surprise of the U.S. chain and its lawyers, U.S. law in the circuit where the U.S. chain is seeking set-aside does not, in fact, allow parties to set aside an arbitral award. In that case, the potential difference in cost between choosing to arbitrate in one circuit over another would be \$40 million based on the set-aside alone. Had the lawyers been aware of this difference in the circuits’ laws, they would have, at the time of drafting the clause, chosen to arbitrate in a circuit where set-aside is possible. Instead, the U.S. chain is now stuck paying \$40 million in damages with no recourse, simply because (1) the lawyers did not foresee the consequences of the different circuits’ interpretations of a complex

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3. See Int’l Ct. of Arbitration, *Standard ICC Arbitration Clause*, INT’L CHAMBER COM. (Mar. 15, 2012), <http://www.iccwbo.org/court/arbitration/id4090/index.html>.

body of law and (2) they did not think through the details and consequences of the arbitration clause.

This hypothetical—and the U.S. chain's plight over a complicated and unexpected law for which lawyers do not account when drafting the arbitration clause—is not completely improbable. Indeed, this Note argues that a circuit split between the Second and Eleventh Circuits—perhaps unintentionally and certainly unforeseeably—leaves parties vulnerable to an automatic waiver of the right to set aside an arbitration award. This means that by choosing to arbitrate in the Eleventh Circuit, parties may automatically eliminate the opportunity for the losing party to oppose the confirmation of the award in court; effectively, the court stamps its approval on the award as is. Conversely, in the Second Circuit parties are able to petition to have an award set aside in court. This Note recommends that the circuit split be resolved to eliminate the possibility of an automatic waiver of set-aside rights because such a law would be incompatible with U.S. and international set-aside waiver law and policy. Further, this Note recommends that even if the circuit split were resolved in this way, the United States should modernize its set-aside waiver law to allow provisions waiving set-aside in arbitration clauses. Such a change would promote autonomy in international commercial arbitration in the United States, in addition to increasing the attractiveness of the country as a seat of arbitration.

Part I of this Note outlines the basics of international commercial arbitration and the legal framework regarding set-aside in the United States. More importantly, Part I illustrates a circuit split between the Second and Eleventh Circuits. Specifically, according to the Second Circuit's interpretation of the New York Convention and the Federal Arbitration Act, the primary vehicles governing international commercial arbitration in the United States, parties arbitrating in the Second Circuit are able to petition a court to set aside an arbitration award. On the contrary, the Eleventh Circuit's interpretation of the same laws does not allow parties to seek to have an award set aside in court. Regardless of whether the set-aside effects arising from the circuits' interpretations of the laws are unintentional, from the perspective of our U.S. chain, the chain's decision whether to arbitrate in New York, NY, Atlanta, GA, or Miami, FL affects whether the chain can petition the court to set aside the \$40 million award that was the result of faulty arbitration proceedings.

Part II of this Note recommends that courts resolve the circuit split in favor of the Second Circuit's rule, which does not leave parties like the U.S. chain vulnerable to an automatic waiver of set-aside. This recommendation is based on an analysis of the policies surrounding set-aside waiver law in different jurisdictions—specifically the policy of protection in the United States and the policy of autonomy in several European jurisdictions—and the observation that the concept of an automatic waiver is incompatible with both policies.

The Note concludes by recommending that even if a court resolved the circuit split to eliminate the possibility of automatic waiver, the United States should modernize its set-aside waiver laws to allow parties to con-

tractually waive set-aside. Current U.S. law does not allow parties such flexibility, and this Note argues that modernizing the U.S. law would be more compatible with the principle of autonomy and freedom of contract that otherwise pervades U.S. arbitration law. In addition, such renewed focus on autonomy would make the United States a more attractive seat for arbitration and would make U.S. arbitration law more accessible to both American and foreign lawyers.

## I. Background

### A. The Benefits of Including an Arbitration Clause in Agreements for Cross-Border Transactions

It is not uncommon for parties like our U.S. chain and the internationally located branches—parties engaged in lucrative cross-border transactions—to contract for international commercial arbitration to be the method of dispute resolution. These parties choose international commercial arbitration because of the benefits of arbitration compared to litigation.<sup>4</sup> Specifically, the U.S. chain and the international branch would prefer international commercial arbitration because they see huge benefits in the flexibility and autonomy of the procedure that arises from their ability to choose the location, the arbitrators,<sup>5</sup> and rules of arbitration that are less formal and rigid than those mandated by, for example, the United States Federal Rules of Civil Procedure or the French *Code de Procédure Civile*.<sup>6</sup> In our hypothetical, the U.S. chain and the investors chose the rules that govern their proceedings in a simple way by defaulting to an already existing set of rules—here the ICC rules—because the rules suited

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4. See, e.g., COVINGTON & BURLING, *A PRIMER ON INTERNATIONAL ARBITRATION* 1 (1998) (providing a basic overview of issues involved in the practice of international commercial arbitration). Note that while enforceability and finality of awards are considered benefits of arbitration, some commentators are concerned that, unlike litigated disputes, arbitration awards cannot be efficiently appealed. Specifically, although disappointed parties can challenge arbitration awards to be set aside by a court, the process is difficult and challenging given the deference that courts show to arbitration. See *id.*; Harout Jack Samra, *Two to Tango: Domestic Grounds for Vacatur Under the New York Convention*, 20 AM. REV. INT'L. ARB. 367, 373 (2009) (discussing federal arbitration policy in the United States); Richard Stim, *The Benefits of Arbitration*, BLOOMBERG BUSINESSWEEK (Jan. 10, 2006), [http://www.businessweek.com/smallbiz/tips/archives/2006/01/arbitration\\_is.html](http://www.businessweek.com/smallbiz/tips/archives/2006/01/arbitration_is.html) (providing practical advice to business owners). But see William H. Knull, III & Noah D. Rubins, *Betting the Farm on International Arbitration: Is it Time to Offer an Appeal Option?*, 11 AM. REV. INT'L. ARB. 531 (2000) (arguing that the finality of awards is not necessarily a benefit of arbitration and suggesting that it is time to create an appeals mechanism for arbitration). Such a struggle in court can also be disappointing and frustrating to parties, who originally chose arbitration specifically to avoid a struggle in court.

5. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 2; see also INTERNATIONAL COMMERCIAL ARBITRATION IN NEW YORK 3-4 (J. Stewart McClendon & Rosabel E. Everard Goodman eds., 1986) (discussing the advantages of international commercial arbitration).

6. See, e.g., COVINGTON & BURLING, *supra* note 4, at 1.

their needs. Alternatively, the parties could have also written every rule from scratch had they deemed it necessary.<sup>7</sup>

The U.S. chain and the international investors may also prefer to arbitrate because of the comparative ease of enforcing arbitral awards.<sup>8</sup> Commentators have noted that arbitral awards are more easily enforced than court judgments in international cases because enforcement of arbitral awards is governed by international treaty in contrast to enforcement of foreign court judgments, which relies on principles of international comity that are frequently cumbersome.<sup>9</sup> Adding to the ease of enforcing awards is the current pro-arbitration sentiment prevalent in courts, with courts exhibiting a “highly deferential [attitude] to arbitration in general . . . .”<sup>10</sup> This sentiment is attractive to parties like the U.S. chain and its international investors, who certainly would prefer to reap the gains of any damages awarded to them as quickly and with as little legal maneuvering as possible.

Arguably, in choosing arbitration over litigation, the U.S. chain and the international investors might be concerned with some of the disadvantages associated with arbitration: the length of the arbitration process from filing to award, the expense of the process, the risk of national court intervention in the arbitration process, and the problems associated with joining third parties to the process.<sup>11</sup> Commentators have also expressed concerns that arbitration is not as predictable as litigation.<sup>12</sup> However, for the U.S. chain and the international investors—as for many other parties negotiating cross-border transactions—the benefits of arbitration outweigh the possible disadvantages.

## B. The Role of Set-Aside Within the Process of International Commercial Arbitration

Set-aside, the topic of this Note, becomes a concern to the U.S. chain and the international investors towards the end of the arbitration process. The process of arbitration begins when a breach of contract claim arises

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7. See generally INT'L TRADE CTR., ARBITRATION AND ALTERNATIVE DISPUTE RESOLUTION: HOW TO SETTLE INTERNATIONAL BUSINESS DISPUTES 131-49 (2001) (noting that parties may rely on standard clauses that arbitration institutions draft, but also enumerating various elements—categorized essential, useful, and other—that the parties can choose to include to tailor their clause).

8. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 2.

9. See, e.g., COVINGTON & BURLING, *supra* note 4, at 4. *Contra* Charles Adams, *The State of Arbitration*, GLOBAL ARB. REV. (Mar. 13, 2012), <http://www.globalarbitrationreview.com/journal/article/30392/the-state-arbitration/> (observing that today many are under the impression that international arbitration has become “unnecessarily cumbersome”).

10. Samra, *supra* note 4, at 373.

11. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 2.

12. See Knull & Rubins, *supra* note 4, at 532-33 (commenting on the experience of a European lawyer who had “exposed [his client’s] company to the unpredictability of an arbitral award”).

and the perturbed parties submit the issue to arbitration pursuant to the arbitration clause that the U.S. chain and the international investors included in their agreement.<sup>13</sup> A panel of arbitrators, also referred to as the arbitration tribunal, hears arguments and evidence from both parties and subsequently renders an arbitral award that is generally binding on the parties involved.<sup>14</sup> If a court recognizes and enforces the arbitral award in accordance with the national laws and international treaties of the country where the enforcement is sought, the losing party then has to pay damages to its opponent—these damages can be in the millions, as in our hypothetical where the Middle Eastern branches were awarded \$40 million.<sup>15</sup> However, when the losing party is dissatisfied with the award—and in our hypothetical the U.S. chain has every reason to be dissatisfied with paying \$40 million in damages where it believes the arbitration procedure was unfair—the party may seek to have the award set aside by the court in the country where the award was rendered.<sup>16</sup> National laws determine the courts in which the parties can bring set-aside proceedings: in the United States, parties can do so in a district court in the jurisdiction where the arbitration occurred.<sup>17</sup>

Setting aside an award is the functional equivalent of nullifying the award. Therefore, if the court agrees with the U.S. chain and sets aside the award, the award would have no effect in that jurisdiction and the international investors would have no remedy in the country where the award is set aside.<sup>18</sup> In our hypothetical case, the Middle Eastern investors would not be able to collect the \$40 million award in the United States if a court sets aside the award. In such a case, the investors can still seek to have the award recognized and enforced in another country, but that country is also entitled to refuse to do so based on the foreign court's decision to set aside the award.<sup>19</sup> Furthermore, even if the award were enforced in another country, in the absence of significant U.S. chain assets in the country there is no guarantee that Middle Eastern investors will be able to collect the full \$40 million.<sup>20</sup>

On the other hand, if the court does not agree with the U.S. chain and refuses to set aside the award, the U.S. chain will have to pay the full \$40 million. This would also be the case if the U.S. chain and the Middle East-

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13. See, e.g., Int'l Ct. of Arbitration, *supra* note 3 (referring parties to the ICC rules of arbitration).

14. See Gloria Miccoili, *International Commercial Arbitration*, AM. SOC'Y INT'L L., <http://www.asil.org/erg/?page=arb> (last updated Dec. 1, 2012).

15. See New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards art. III, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38 [hereinafter New York Convention].

16. See, e.g., INT'L TRADE CTR., *supra* note 7, at 111.

17. See Federal Arbitration Act of 1925, 9 U.S.C. § 10 (2006). Note that "vacate" refers to set-aside.

18. See, e.g., INT'L TRADE CTR., *supra* note 7, at 113.

19. See generally RICHARD H. FIELD, BENJAMIN KAPLAN & KEVIN M. CLERMONT, *CIVIL PROCEDURE: MATERIALS FOR A BASIC COURSE* 493-508 (Robert C. Clark et al. eds., 10th ed. 2010) (discussing jurisdiction over things).

20. See generally *id.*



ern investors had contractually waived their right to have the award set aside in the agreement, thus effectively eliminating the right to appeal the arbitrator's decision and leaving the losing party, here the U.S. chain, stuck with an unfavorable \$40 million award.<sup>21</sup> The role of set-aside, therefore, is crucial in arbitration proceedings because it affects the finality of the arbitral award.

### C. The Legal Framework for Setting Aside an Award in the United States

In setting aside an award in the United States, the U.S. chain and the Middle Eastern investors are subject to complex laws. As in most countries, in the United States international commercial arbitration is governed by both a federal statute, the Federal Arbitration Act (FAA),<sup>22</sup> and an international treaty, the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention).<sup>23</sup> Arbitration is thus subject to the interplay between the two sources of law.<sup>24</sup>

Congress enacted the FAA in 1925, which generally governs arbitration in the United States. In Chapter 1, the FAA provides the process for enforcing an arbitral award<sup>25</sup> and the procedure and grounds for setting aside an award.<sup>26</sup> Specifically, a district court in the district where the award is made can order the arbitral award to be set aside in situations where the award or the process of arbitration is deemed to be unfair or defective.<sup>27</sup> For example, corruption, fraud, arbitrator misconduct, and partiality constitute grounds for setting aside an arbitration award under § 10 of the FAA.<sup>28</sup> Furthermore, courts in the United States have recognized additional, non-statutory grounds for setting aside an arbitral award, but "this doctrine is presently in flux."<sup>29</sup>

Chapter 2 of the FAA incorporates the New York Convention, enacted at a 1958 ICC conference designed to address the demands of post-WWII increased international trade,<sup>30</sup> provides broad guidelines on how courts should apply the convention.<sup>31</sup> There are two important aspects to the applicability of the New York Convention to any given award. First, the FAA states that any award or agreement that is "considered as commercial"

21. See, e.g., INT'L TRADE CTR., *supra* note 7, at 149.

22. Federal Arbitration Act of 1925, 9 U.S.C. §§ 1-16 (2006). Note that the Federal Arbitration Act applies to both domestic and international arbitration.

23. New York Convention, *supra* note 15.

24. See Samra, *supra* note 4, at 367-90.

25. See *id.* at 368; see also 9 U.S.C. § 9.

26. See 9 U.S.C. § 10.

27. See *id.*; see also Samra, *supra* note 4, at 367-90.

28. See 9 U.S.C. § 10; see also Samra, *supra* note 4, at 368-69.

29. Samra, *supra* note 4, at 369 (discussing the "manifest disregard" of the law standard as a controversial and circuit split-causing ground for setting aside an award).

30. See Richard W. Hulbert, *The Case for a Coherent Application of Chapter 2 of the Federal Arbitration Act*, 22 AM. REV. INT'L ARB. 45, 52 (2011) (discussing the history of the New York Convention).

31. See 9 U.S.C. §§ 201-08; see also Samra, *supra* note 4, at 369.

falls under the New York Convention.<sup>32</sup> However, the FAA also “carves out an important exception”<sup>33</sup> to this, demanding an international component to the dispute before the case will be deemed to fall under the New York Convention.<sup>34</sup> Second, the New York Convention applies to the “recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought . . . [and] to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought.”<sup>35</sup> The precise definition of “award not considered as domestic” (non-domestic award) has received considerable attention in the United States.<sup>36</sup> Although the title of the New York Convention refers to “foreign awards,” U.S. courts have determined that the New York Convention applies to arbitral awards that have been rendered in the United States if they qualify as “non-domestic.”<sup>37</sup> However, for these foreign and non-domestic awards *rendered in the United States*, as this Note discusses below, courts are split

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32. 9 U.S.C. § 202; *see also* Samra, *supra* note 4, at 369.

33. Samra, *supra* note 4, at 369.

34. 9 U.S.C. § 202 states the following:

An agreement or award arising out of such a relationship which is entirely between citizens of the United States shall be deemed not to fall under the Convention unless that relationship involves property located abroad, envisages performance or enforcement abroad, or has some other reasonable relation with one or more foreign states. For the purpose of this section a corporation is a citizen of the United States if it is incorporated or has its principal place of business in the United States.

35. New York Convention, *supra* note 15, art. 1(1).

36. *See* Samra, *supra* note 4, at 371.

37. *See, e.g.,* *Bergesen v. Joseph Muller Co.*, 710 F.2d 928, 932 (2d Cir. 1983). However, commentators have met such court decisions with criticism, suggesting that the courts have expanded the scope of the convention. *See* Samra, *supra* note 4, at 371. Academic commentators especially have criticized U.S. courts for interpreting this provision of Article 1 of the New York Convention too broadly by applying it to cases where arbitration occurs in the United States. *See* Albert Jan van den Berg, *When is an Arbitral Award Nondomestic Under the New York Convention of 1958?*, 6 *PACE L. REV.* 25, 46 (1985); *see also* Samra, *supra* note 4, at 371 (discussing van den Berg’s argument). Critics especially point to the Second Circuit decision in *Bergesen v. Joseph Muller Co.* that an arbitral award awarded in a dispute in the United States between two foreign entities falls under the New York Convention’s category of “[arbitral] awards ‘not considered as domestic.’” *Bergesen*, 710 F.2d at 932; van den Berg, *supra*; Samra, *supra* note 4, at 371 (discussing *Bergesen*). These critics have noted that such a decision makes the United States a “more hospitable forum for foreign parties intending to arbitrate within the United States” because their awards are more likely to be enforced in federal courts: the enforcement of an award under Chapter 1 is “almost automatic” because enforcement can be avoided only through a set-aside action, while under Chapter 2 enforcement “can be resisted on a number of grounds” which, admittedly, closely correspond to set-aside grounds in many national arbitration statutes. van den Berg, *supra*, at 50, 54–55; *see* Samra, *supra* note 4, at 371. Compare these criticisms, however, to one academic’s statement that it took over a decade for courts to decide whether the New York Convention applies to awards rendered in the U.S., “[d]espite the unambiguous language of [§] 202 and the specific references in the venue and enforcement provisions of [§§] 204 and 206 to arbitrations in the United States . . .” Hulbert, *supra* note 30, at 59.

on whether both Chapters 1 and 2 are available for the parties to scrutinize the award in U.S. courts.<sup>38</sup>

Article V of the New York Convention provides grounds under which “recognition and enforcement of the award may be refused.”<sup>39</sup> For example, Article V permits such an action if there is evidence that the agreement was invalid, parties were not given proper notice, the award does not fall under the scope of the issue the parties presented for arbitration, the arbitration procedure did not reflect party agreement, the award has been set aside, the award considers subject matter that is unarbitrable under the enforcing country’s laws, or the award is contrary to public policy.<sup>40</sup> This list of grounds for refusing to enforce an award set forth in Article V is exhaustive, and courts cannot read other grounds into the convention by implication.<sup>41</sup>

Although both Chapter 1 and Chapter 2 of the FAA refer to situations in which courts might not enforce an award, it is important to note that *only* Chapter 1 provides the grounds for, and thus the right to, set-aside in U.S. law.<sup>42</sup> The language in the New York Convention—“recognition and enforcement of the award may be refused”<sup>43</sup>—does not refer to set-aside, but simply enumerates circumstances in which a court may refuse to enforce a foreign or non-domestic award.<sup>44</sup> The two concepts are not interchangeable: only a court in the country where or under whose laws an award is rendered can set aside an award,<sup>45</sup> while courts in both the country where the award was rendered and in other countries where enforcement is sought can refuse recognition and enforcement.<sup>46</sup> That the two concepts are not interchangeable is evident in that Article V(1)(e) of the New York Convention allows for a court to refuse to enforce a foreign award if it “has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.”<sup>47</sup> The distinction between a court setting aside an award and a court refusing

38. See *infra* Part I.D.

39. New York Convention, *supra* note 15, arts. V(1)-(2).

40. *Id.*

41. See DOMENICO DI PIETRO & MARTIN PLATTE, ENFORCEMENT OF INTERNATIONAL ARBITRATION AWARDS: THE NEW YORK CONVENTION OF 1958 135 (2001) (noting that case law, leading authorities in the field of international commercial arbitration, and the convention’s “pro-enforcement bias” all support the proposition that the list of grounds on which to set aside an award is exhaustive); see also Samra, *supra* note 4, at 371.

42. Compare New York Convention, *supra* note 15, art. V (refusal to recognize and enforce), with 9 U.S.C. § 10 (set-aside). See also van den Berg, *supra* note 37, at 55-56 (“[A]n action for the enforcement [under the New York Convention] is essentially different from an action for the setting aside of an award. . . . [T]his distinction is clearly made by the Convention itself.”).

43. New York Convention, *supra* note 15, arts. V(1)-(2).

44. See *id.*

45. See *id.*

46. See *id.* Specifically, a court can refuse recognition and enforcement of an award rendered in its own jurisdiction if the award is considered foreign or non-domestic, thus falling under Article V of the New York Convention. See *Bergesen v. Joseph Muller Co.*, 710 F.2d 928, 932 (2d Cir. 1983).

47. New York Convention, *supra* note 15, art. V(1)(e).

to recognize and enforce an award is important because if a court sets aside an award, the award is effectively cancelled in that jurisdiction;<sup>48</sup> however if a court refuses to recognize and enforce the award, the parties can seek to have the award enforced elsewhere.<sup>49</sup> The difficult distinction between FAA Chapters 1 and 2 regarding set-aside is not the only cause for confusion in U.S. courts reviewing arbitral awards. Reconciling the FAA provisions regarding set-aside with the New York Convention's provisions appears to be a "rather complex" challenge.<sup>50</sup>

That there is confusion in courts regarding set-aside law is cause for concern. It is true that given the deference that courts show arbitration, very few arbitral awards are set aside and the process is challenging.<sup>51</sup> It is also true that parties like our U.S. chain and international investors specifically contract for arbitration knowing the benefits as well as the risks. However, this does not mean that the risks of arbitration should be ignored and that the parties should not have the opportunity to appeal. After all, the grounds enumerated in the FAA for setting aside an award—such as arbitrator partiality, misconduct, fraud, and arbitrator misconduct<sup>52</sup>—are certainly procedural defects that, were they present during litigation, would create cause for an appeal. For our hypothetical U.S. chain that gets an unfavorable award following an unfair arbitration procedure, confusion in set-aside law is certainly not preferable, as the chain would want the decision set aside. Unfortunately, in the United States the confusion in set-aside law is especially problematic because circuit courts have interpreted set-aside law in different ways, leading to potential problems that parties' lawyers do not foresee. Specifically, a circuit split between the Second and Eleventh Circuits regarding the interpretation of the interplay between FAA Chapters 1 and 2 gives rise to an automatic waiver of the right to set aside an arbitration award in the Eleventh Circuit, with no such effect in the Second Circuit and those states that follow the Second Circuit's rule.<sup>53</sup>

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48. See, e.g., *INT'L TRADE CTR.*, *supra* note 7, at 113. But see *Chromalloy Aeroservices v. Egypt*, 939 F. Supp. 907, 914 (D.D.C. 1996) (holding that, under certain circumstances, U.S. courts could recognize and enforce an award that Egyptian courts had set aside).

49. See *New York Convention*, *supra* note 15, art. V (stating that actions for recognition and enforcement are not limited to one such action).

50. *Samra*, *supra* note 4, at 372-73 (noting that the cumulative effects of the provisions in the Federal Arbitration Act and New York Convention have indirectly caused confusion in courts); see also *infra* Part I.D.

51. See *Samra*, *supra* note 4, at 373 (discussing deference); Lawrence R. Mills et al., *Vacating Arbitration Awards*, *DISP. RESOL. MAG.* 23, 24 (Summer 2005) (finding that only about 14% of all successfully filed challenges to an arbitration award resulted in the court vacating the award); see also *COVINGTON & BURLING*, *supra* note 4, at 1 (noting that a disadvantage of arbitration is that awards are "difficult to challenge effectively").

52. See *Federal Arbitration Act of 1925*, 9 U.S.C. § 10 (2006).

53. See *TIBOR VÁRADY, JOHN J. BARCELÓ & ARTHUR T. VON MEHREN, INTERNATIONAL COMMERCIAL ARBITRATION: A TRANSNATIONAL PERSPECTIVE* 771 (4th ed. 2009) (suggesting that this particular circuit split would lead to such an outcome).

#### D. A Circuit Split Causing Unforeseen Legal Complications

In the United States, courts have struggled with the question of whether both Chapter 1 and Chapter 2 of the FAA are available for parties to scrutinize an arbitral award where the arbitration occurred in the United States and the award is considered foreign or non-domestic, thus making the New York Convention applicable. This struggle has culminated in a circuit split, where the Second Circuit makes both Chapters 1 and 2 available for parties in such circumstances, while the Eleventh Circuit only makes Chapter 2 available to parties whose arbitration in the United States resulted in a foreign or non-domestic award. Given that set-aside is only available under Chapter 1, this circuit split has significant implications for the parties' ability to seek to set aside an arbitral award.

##### 1. The Second Circuit

The Second Circuit considered the issue in the seminal case *Yusuf Ahmed Alghanim & Sons, W.L.L. v. Toys "R" Us, Inc. (Alghanim & Sons v. Toys "R" Us)* where it held that both Chapters 1 and 2 are available to such parties.<sup>54</sup> The case involved a dispute over the termination date for a license and technical assistance agreement and a supply agreement between the privately held Kuwaiti business Alghanim & Sons and the U.S. toy-store chain Toys "R" Us.<sup>55</sup> Following disagreements over business conducted in Kuwait, the parties participated in arbitration. The arbitration culminated in an award in favor of Alghanim & Sons that the Kuwaiti business sought to enforce and the U.S. chain moved to set aside in protracted litigation.<sup>56</sup>

The Second Circuit relied on its interpretation that Chapters 1 and 2 of the Federal Arbitration Act have "overlapping coverage"<sup>57</sup> to hold that both Chapters 1 and 2 are available to foreign parties to scrutinize an award rendered in the United States.<sup>58</sup> Consequently, the court determined that the New York Convention gives courts authority to apply the FAA's grounds in Chapter 1 for setting aside an award.<sup>59</sup> Specifically, the

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54. *Yusuf Ahmed Alghanim & Sons, W.L.L. v. Toys "R" Us, Inc.*, 126 F.3d 15, 21, 23 (2d Cir. 1997).

55. *Id.* at 17.

56. *Id.* at 18. The Second Circuit quickly determined that the New York Convention applied to the case because the arbitral award leading to the action was a non-domestic award. Relying on FAA § 202 and *Bergesen v. Joseph Muller Corp.*, the court explained that the award was non-domestic because the dispute involved two non-domestic parties and a U.S. corporation and was mainly concerned with conduct and contract performance in the Middle East. *Id.* at 18-19. After concluding that the FAA provided grounds for set-aside in the case, the *Alghanim & Sons* court noted that nonetheless "the showing required to avoid summary confirmation is high." *Id.* at 23 (quoting *Ottley v. Schwartzberg*, 819 F.2d 373, 376 (2d Cir. 1987)). Consequently, the court determined that this high bar had not been met in regards to the set-aside grounds it examined—namely manifest disregard of the terms of the agreement and manifest disregard of the law. The court thus refused to set aside the award. *Id.* at 23-25.

57. *Id.* at 20.

58. *See id.* at 21, 23; *see also* VARADY, BARCELÓ & VON MEHREN, *supra* note 53, at 771.

59. *See Alghanim & Sons*, 126 F.3d at 21.

court noted that under Article V of the New York Convention, U.S. courts “are authorized to apply United States procedural arbitral law, i.e., the FAA, to nondomestic awards rendered in the United States.”<sup>60</sup> To support its position, the court looked to case law, commentary, and the plain language and history of the New York Convention.<sup>61</sup>

Importantly, the court in *Alghanim & Sons v. Toys “R” Us* noted that it was the first court to consider whether “Article V(1)(e) [of the New York Convention] authorizes an action to set aside an arbitral award under the domestic law of the state in which, or under which, the award was rendered,” since it was the first court faced with a fact pattern in which the arbitral award was rendered in the United States and the confirmation and set-aside were both sought in the United States.<sup>62</sup> The court emphasized that the “[New York] Convention mandates very different regimes for the review of arbitral awards”<sup>63</sup> (1) in the state where, or under the laws of which, the award was made—where domestic laws provide grounds for set-aside; and (2) in other states where recognition and enforcement are sought—where the New York Convention provides grounds to refuse recognition and enforcement of the award.<sup>64</sup> The crucial point here is that the New York Convention itself does not allow for court review for the purposes of set-aside—only domestic laws can allow for that, as FAA Chapter 1 does in the United States. The *Alghanim v. Toys “R” Us* court essentially made such review available when the arbitration occurs in the United States and results in a foreign or non-domestic award.<sup>65</sup>

Several circuits have followed the Second Circuit’s reasoning in *Alghanim & Sons v. Toys “R” Us*.<sup>66</sup> Notably, the Fifth<sup>67</sup> and Sixth<sup>68</sup> Circuits and the District of Columbia<sup>69</sup> have agreed that in a case where a foreign party arbitrates in the United States, the FAA and the New York Convention make both FAA Chapters 1 and 2 available for scrutinizing the award. In contrast, the Eleventh Circuit<sup>70</sup> takes a different approach to the overlap

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60. *Id.* at 19-20.

61. *See id.* at 20-23.

62. *Id.* at 20-21 (noting, however, that the Seventh Circuit has “agreed, albeit in passing, that the Convention ‘contemplates the possibility of the award’s being set aside in a proceeding under local law.’”).

63. *Id.* at 23.

64. *Id.*

65. Compare Federal Arbitration Act of 1925, 9 U.S.C. § 10 (2006), with New York Convention, *supra* note 15, art. V.

66. See Lucy Reed & Phillip Riblett, Essay, *Expansion of Defenses to Enforcement of International Arbitral Awards in U.S. Courts?*, 13 SW. J. L. & TRADE AMERICAS 121, 129-30 (2006) (discussing this particular circuit split in the context of an increase in the availability of the manifest disregard standard for setting aside arbitral awards, which is available under FAA Chapter 1).

67. See, e.g., *Bridas S.A.P.I.C. v. Gov’t of Turkm.*, 345 F.3d 347, 365 (5th Cir. 2003). Note that Reed & Riblett, *supra* note 66, list the circuits on both sides of the split.

68. See, e.g., *Jacada (Eur.), Ltd. v. Int’l Mktg. Strategies, Inc.*, 401 F.3d 701, 709 (6th Cir. 2005), *overruled on other grounds*.

69. See, e.g., *Chromalloy Aeroservices v. Egypt*, 939 F. Supp. 907, 910 (D.D.C. 1996).

70. See *Indus. Risk Insurers v. M.A.N. Gutehoffnungshütte GmbH*, 141 F.3d 1434, 1441 (11th Cir. 1998); *Four Seasons Hotels & Resorts, B.V. v. Consorcio Barr, S.A.*, 267

between the New York Convention and the Federal Arbitration Act, giving rise to the circuit split.

## 2. *The Eleventh Circuit*

In *Four Seasons Hotels and Resorts, B.V. v. Consorcio Barr, S.A.* (*Four Seasons v. Consorcio Barr*), the United States District Court for the Southern District of Florida elucidated the Eleventh Circuit's position on the interaction between Federal Arbitration Act Chapters 1 and 2 under the New York Convention and held that only Chapter 2 is available to foreign parties arbitrating in the United States to scrutinize the award.<sup>71</sup> *Four Seasons v. Consorcio Barr* involved a dispute between the Dutch, Canadian, and Venezuelan Four Seasons corporations (Four Seasons) and Consorcio Barr, a Venezuelan corporation.<sup>72</sup> Prior to the litigation in a U.S. court, the parties had engaged in arbitration in Florida.<sup>73</sup> Four Seasons had initiated the arbitration due to breach of contract regarding hotel properties that Consorcio Barr owned in Caracas, Venezuela.<sup>74</sup> The arbitral tribunal had awarded a partial award enjoining Consorcio Barr from pursuing litigation against Four Seasons in Venezuelan courts.<sup>75</sup> Despite the Tribunal's award, Consorcio Barr filed a motion in a Venezuelan court to prevent Four Seasons from operating a hotel that Consorcio Barr owned and Four Seasons managed.<sup>76</sup> The Venezuelan court eventually granted Consorcio Barr's motion to suspend execution of the award and declared the substance of the award null and void.<sup>77</sup> Consequently, in *Four Seasons v. Consorcio Barr*, Four Seasons alleged that Consorcio Barr violated the tribunal's award.<sup>78</sup> In response, Consorcio Barr demanded that the U.S. court set aside the award.<sup>79</sup>

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F. Supp. 2d 1335, 1341 (S.D. Fl. 2003) (relying on *Indus. Risk Insurers v. M.A.N. Gutehoffnungshütte GmbH*, 141 F.3d 1434 (11th Cir. 1998)), *overruled on other grounds* by *Four Seasons Hotels & Resorts, B.V. v. Consorcio Barr, S.A.*, 377 F.3d 1164 (11th Cir. 2004).

71. The district court determined that the award in question was non-domestic and therefore fell under the New York Convention. *See Four Seasons*, 267 F. Supp. 2d at 1339. The court noted that because the Tribunal Award applied Venezuelan law for substantive issues and arose from a dispute between Venezuelan and other foreign entities concerning performance of a contract in Venezuela, the award was non-domestic even though it had been rendered in Miami. *See id.* (citing *Bergesen v. Joseph Muller Corp.*, 710 F.2d 928, 932-33 (2d Cir. 1983) ("We adopt the view that awards 'not considered as domestic' denotes awards which are subject to the [New York] Convention not because made abroad, but within the legal framework of another country, e.g., pronounced in accordance with foreign law or involving parties domiciled or having their principal place of business outside the enforcing jurisdiction . . . . Had Congress desired to exclude arbitral awards involving two foreign parties rendered within the United States from enforcement by our courts it could readily have done so. It did not.")).

72. *Id.* at 1337.

73. *Id.*

74. *Id.*

75. *Id.*

76. *Id.*

77. *Id.* at 1338.

78. *Id.* at 1337.

79. *Id.* at 1338-39.

The *Four Seasons v. Consorcio Barr* court diverged from the Second Circuit's analysis when analyzing the overlap between FAA Chapters 1 and 2. Specifically, the court elucidated the Eleventh Circuit's position that only Chapter 2 is available to foreign parties who arbitrate in the United States, as set up in *Industrial Risk Insurers v. M.A.N. Gutehoffnungshütte GmbH*.<sup>80</sup> The court analyzed that, according to Chapter 2 of the Federal Arbitration Act, "Chapter 1 applies to actions and proceedings brought under this chapter to the extent that that chapter is not in conflict with this chapter or the [New York] Convention as ratified by the United States."<sup>81</sup> Furthermore, the court stated the following:

Nothing in *Industrial Risk Insurers* or [FAA Chapter 2] indicates that Chapter 1 is capable of serving as the primary framework for confirming an award "not considered as domestic" under the [New York] Convention . . . . Rather Chapter 1 of the FAA merely augments the Convention to the extent no conflict exists between the two instruments.<sup>82</sup>

Therefore, according to the district court, the Eleventh Circuit does not interpret there to be any overlap between FAA Chapters 1 and 2, which subsequently eliminates the ability of a party arbitrating in the United States to rely on both Chapters when seeking to enforce or set aside a foreign or non-domestic arbitral award.<sup>83</sup>

### 3. *Unforeseen Legal Complications: Automatic Waiver of Set-Aside in the Eleventh Circuit*

The Eleventh Circuit's interpretation is particularly worrying for parties like our U.S. chain and international investors who arbitrate in the U.S. and are awarded either a foreign or a non-domestic award. If those parties cannot use FAA Chapter 1 to scrutinize an award in the Eleventh Circuit, set-aside is not available to those parties at all, as only Chapter 1 provides for set-aside.<sup>84</sup> Consequently, the Eleventh Circuit's rule would leave foreign parties that choose a city in the Eleventh Circuit as the seat of arbitration unable to set aside their award at all, in practice creating an automatic

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80. In *Industrial Risk Insurers v. M.A.N. Gutehoffnungshütte GmbH*, 141 F.3d 1434 (11th Cir. 1998), the Eleventh Circuit held that the New York Convention governed a motion to set aside an award that had been rendered in Florida, had been governed by Florida substantive law, and had arisen from a dispute between a U.S. entity and a German corporation. The Eleventh Circuit held that the New York Convention provided exclusive jurisdiction because "an arbitral award made in the United States, under American law, falls within the purview of the New York Convention—and is thus governed by Chapter 2 of the FAA—when one of the parties to the arbitration is domiciled or has its principal place of business outside of the United States." *Id.* at 1141. Despite the holding in *Industrial Risk Insurers*, it was not until *Four Seasons v. Consorcio Barr* that the Eleventh Circuit's rejection of FAA Chapter 1 became clear.

81. *Four Seasons*, F. Supp. 2d at 1340 (quoting 9 U.S.C. § 208).

82. *Id.* at 1342.

83. See *id.*; see also VARADY, BARCELÓ & VON MEHREN, *supra* note 53, at 771 (noting this specific circuit split and its potential consequences).

84. Compare 9 U.S.C. § 10 with New York Convention, *supra* note 15, art. V.



waiver of the FAA-provided right to have an arbitration award set aside.<sup>85</sup> This is the functional equivalent of waiving the right to appeal a court decision.<sup>86</sup> Interestingly, such a case has not yet been heard in the Eleventh Circuit,<sup>87</sup> and it is likely that the automatic waiver is simply an unintended consequence<sup>88</sup> of the Eleventh Circuit's interpretation of the FAA. Nonetheless, the circuit split leaves unlucky parties—like our U.S. chain with an unfavorable \$40 million award—potentially unable to even *seek* to have an award set aside depending on whether their hastily agreed-upon arbitration clause lists Atlanta, GA or New York, NY as the seat of arbitration.<sup>89</sup>

## II. Analysis

### A. Confusing Laws and Incompetent Arbitration Clause Drafting: A Pressing Need to Resolve the Circuit Split

Complexities in the law are nothing new; neither are circuit splits that require lawyers to research the law in different jurisdictions. With the issue of set-aside in international commercial arbitration, however, the circuit split—and the resulting complexity in the law—is especially dangerous because many decisions relating to arbitration are made hastily at the time of drafting the arbitration clause,<sup>90</sup> yet have far reaching consequences. One of these often hastily made decisions is choosing where the arbitration will occur—called the “seat of arbitration”—and for parties arbitrating in the United States this decision can affect whether parties can set aside an award. Indeed, for parties like the U.S. chain and the international investors in our hypothetical, the practical reality of poor strategic planning and awareness when drafting arbitration clauses, combined with an unexpected waiver of set-aside, creates a recipe for disaster in the form of undesirable and irreversible awards worth millions. Therefore, it is crucial to resolve the circuit split between the Second and Eleventh Circuits.

Admittedly, zealous proponents of arbitration might argue that parties like our U.S. chain have the resources to hire sophisticated lawyers and

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85. See VÁRADY, BARCELÓ & VON MEHREN, *supra* note 53, at 771 (suggesting that the result of this particular circuit split is an automatic waiver in the Eleventh Circuit). Note that parties must seek to have an award set aside in a district court in the district where the arbitration occurred, see 9 U.S.C. § 10, and consequently any party who arbitrates in a city in the Eleventh Circuit is subject to the Eleventh Circuit's interpretation of the overlap between FAA Chapters 1 and 2.

86. See generally INT'L TRADE CTR., *supra* note 7, at 111-13 (discussing set-aside in general); JONES DAY, COMMENTARY: ARBITRATION IN FRANCE: THE 2011 REFORM (2011), <http://www.jonesday.com/files/Publication/b9ce7786-7e7e-47b9-a628-bc2a9361e704/Presentation/PublicationAttachment/d609618d-63cc-43e9-a0e7-bc6ae3b7663e/Arbitration%20in%20France.pdf> (using “annulment” as a synonym for set-aside).

87. To qualify this statement, the author could not find that such a case had been heard or that parties had encountered such a situation.

88. For a discussion of contractual set-aside waiver laws in the United States and the state of contractual set-aside waiver law in the Eleventh Circuit, see *infra* Part II.B.1.

89. See *supra* note 53 and accompanying text.

90. See generally INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 10 (pointing to the “lack of attention to the negotiation of a suitable international arbitration clause”).

businessmen to carefully choose the seat of arbitration with all possible consequences in mind.<sup>91</sup> However, in reality even sophisticated parties do not always pay enough attention to the consequences of the choices they make when drafting arbitration clauses—after all, they have been taught to keep the clauses short and simple, and they often rely on standard clauses.<sup>92</sup>

First, parties do not always give enough credence to the tactical potential of the contents of an arbitration clause.<sup>93</sup> A well-crafted arbitration clause “can provide a distinct advantage,”<sup>94</sup> because a well-crafted clause can allow parties to include terms that will be advantageous to those parties and will safeguard the parties’ interests in the event that a dispute arises and the parties are left to resort to their dispute resolution mechanism.<sup>95</sup> Conversely, “[t]he lack of attention to the negotiation of a suitable international arbitration clause can leave a corporation adversely exposed should a dispute arise.”<sup>96</sup> Regardless of the tactical potential, a study by PricewaterhouseCoopers about the practices of in-house counsel regarding arbitration clauses found that the majority of the in-house counsel interviewed in the study stated that “their corporations will concede points when negotiating these clauses if faced with strong objections from the counterparty.”<sup>97</sup> While the study focused on in-house counsel specifically, academic commentators writing about lawyers generally in the context of drafting arbitration clauses have similarly pointed to the tactical potential. Commentators discussing the theory of procedural contracts have noted that in circumstances where one party is more sophisticated than the other, the sophisticated parties can “lock-in significant tactical advantages.”<sup>98</sup>

Second, and indicative of the fact that parties do not consider the tactical advantages of their arbitration clauses, parties also often do not pay attention to the consequences of choosing the seat of arbitration. Specifi-

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91. See generally *Southland Corp. v. Keating*, 104 S. Ct. 852, 856 (1984) (discussing the role of sophisticated businessmen); Patrick Gill, Note, *No Do-Overs for Parties who Agree to Limit Review of an Arbitrator’s Decision*, 2006 J. DISP. RESOL. 643, 654 (2006) (discussing bargaining power).

92. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 11 (more corporations use standard clauses than tailored clauses); INT’L TRADE CTR., *supra* note 7, at 125 (advising practitioners that the “two basic principles that should guide any drafter of an arbitration clause are simplicity and precision” and noting that “the more specific and detailed a clause is designed to be, the greater the risk of it becoming inoperable”) (emphasis omitted).

93. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 14.

94. See *id.* at 10.

95. See *id.*; see generally Gill, *supra* note 91, at 654–55 (discussing bargaining power in the context of negotiating arbitration clauses).

96. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 10.

97. See *id.* (noting that of the in-house counsel interviewed in 2006, 60% made this statement).

98. See Peter B. Rutledge & Christopher R. Drahozal, *Contract and Procedure*, 94 MARQ. L. REV. 1103, 1104–05 (2011) (discussing a 1996 argument by Paul Carrington and Paul Haagen).

cally, the PricewaterhouseCoopers study found that while a majority of in-house counsel considered legal considerations to be the most important factor when choosing a seat for arbitration, the concern of convenience was a close second.<sup>99</sup> Consequently, the study noted that

The fact that many in-house counsel see the choice of seat as more a matter of convenience than of concern with legal issues might suggest that some do not fully appreciate the significance of choosing the right seat for international arbitration. It may not be clear to some in-house counsel that the choice of seat is a tactical decision that can help them achieve the best outcome for their side.<sup>100</sup>

The fact that parties drafting arbitration clauses may not realize the significance of choosing the right seat can have drastic consequences in the circuit split between the Second and Eleventh Circuits. Specifically, if the parties choose the seat to be in the United States—one of the most popular seats<sup>101</sup>—they can only apply for set-aside in U.S. courts. If the Eleventh Circuit applies the automatic waiver, choosing whether to arbitrate in a circuit where set-aside is automatically waived is in itself a tactical advantage: had our hypothetical U.S. chain anticipated losing the arbitration and being liable for \$40 million in damages, strategically speaking it should not have chosen to arbitrate in the Eleventh Circuit. However, recognizing the tactical advantage and avoiding the pitfall requires lawyers who are aware of the difference in the law between the two jurisdictions. Furthermore, in the circuit split the legal considerations certainly outweigh convenience; after all, whether a party like our U.S. chain can successfully set aside an award might come down to whether the parties arbitrated in Atlanta, GA, or New York, NY. For the U.S. chain, the possibility of being unable to challenge the \$40 million award would outweigh the potentially greater convenience of the Eleventh Circuit location.

It is possible that parties fail to consider the tactical advantages and the consequences of the seat simply because they are used to relying on standard and simple arbitration clauses. The International Bar Association recommends that lawyers use standard clauses as a starting point, emphasizing that lawyers should add to the standard clause to tailor it to best suit the client's purpose and needs.<sup>102</sup> However, of the in-house counsel participating in the PricewaterhouseCoopers survey, nearly half claimed to use standard clauses, while slightly fewer in-house counsel choose to tailor the

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99. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 14.

100. See *id.*

101. See *id.* at 3.

102. IBA GUIDELINES FOR DRAFTING INTERNATIONAL ARBITRATION CLAUSES, 7-8 (Int'l Bar Ass'n 2010), available at [http://www.ibanet.org/ENews\\_Archive/IBA\\_27October\\_2010\\_Arbitration\\_Clauses\\_Guidelines.aspx](http://www.ibanet.org/ENews_Archive/IBA_27October_2010_Arbitration_Clauses_Guidelines.aspx) (noting the benefits of choosing a standard clause, while still recommending that the standard clause be used as only a starting point).

clauses.<sup>103</sup> Seeing potential pitfalls with both approaches, the arbitration experts at PricewaterhouseCoopers warn that

Standard clauses, whether recommended by arbitration institutions or drafted by the corporation, are invariably well tested but may not suit the circumstances of the contract under negotiation. Tailored clauses, on the other hand, may suit business needs more precisely but arbitration experts should be involved in the drafting as there may be pitfalls and missed opportunities when clauses are drafted by those who are unfamiliar with the arbitration arena.<sup>104</sup>

This warning about the pitfalls of arbitration clause drafting is sound, particularly in situations such as the circuit split in question in this Note. The state of the law is complex and—at least until the Eleventh Circuit hears a case where it rules that the parties have automatically waived set-aside—unexpected. Given the practical reality of poor strategic planning and awareness when drafting arbitration clauses, combined with the uncertainty regarding set-aside, the circuit split must be resolved. Otherwise, a hypothetical like our U.S. chain’s plight might become reality, but in that reality there may be much more at stake than \$40 million.

#### B. Resolving the Circuit Split: An Automatic Waiver Is at Odds with Broader Policies

The circuit split should be resolved to reflect the law in the Second Circuit. While an automatic waiver of set-aside would enforce several of the perceived benefits of arbitration and assuage some of the concerns that surround arbitration, it also runs contrary to the policies of protection and autonomy that have characterized the laws relating to the waiver of set-aside in both the United States and abroad.

Arguments in favor of an automatic waiver of the right to have an award set aside revolve around the main advantages—namely enforceability<sup>105</sup> and finality<sup>106</sup> of awards—and perceived disadvantages of arbitration—namely that the process of arbitration is lengthy<sup>107</sup> and that national

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103. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 10–11 (48% claimed to use standard clauses as they are, while only 43% tailor the clauses).

104. See *id.* at 11; see generally INTERNATIONAL COMMERCIAL ARBITRATION IN NEW YORK, *supra* note 5, at 3–4 (discussing the advantages of international commercial arbitration).

105. See, e.g., INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 2 (noting that one of the top reasons why in-house counsel choose international arbitration as their preferred dispute resolution mechanism is the enforceability of awards); see also COVINGTON & BURLING, *supra* note 4, at 1 (noting that arbitration awards are “difficult to challenge effectively,” which increases enforceability).

106. See, e.g., INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 15 (noting that “one of the main advantages associated with international arbitration has been its finality”). The importance of finality is shown by the fact that an overwhelming majority of in-house counsel is opposed to the creation of an appeals mechanism for arbitration awards, because such a mechanism would make arbitration “more cumbersome and litigation-like[,] . . . essentially negat[ing] a key attribute of the arbitral process.” See *id.*

107. See *id.* at 7.

courts might intervene in the process.<sup>108</sup> First, automatic waiver of set-aside clearly would increase the enforceability of awards: Section 10 of the FAA would no longer be available to parties, so the ways that parties could avoid enforcement would be limited to those in Article V of the New York Convention.<sup>109</sup> Second, automatic waiver of the right to have an award set aside would increase the finality of awards, since the award in such a case would be much less likely to be contested.<sup>110</sup> Third, waiving the right to set-aside would assuage concerns about the lengthiness of the arbitration process, as it would not be stretched by set-aside proceedings. Finally, waiving set-aside would similarly assuage concerns about national court intervention, as awards can be set aside only by courts in response to a request for set-aside by one of the parties; if such a request is not made because the parties have waived the right, a court will not set aside an award.<sup>111</sup>

However, despite the reasons above supporting automatic waiver of set-aside, the policies of protection and autonomy that have been integral to different countries' set-aside waiver laws run against the idea of automatic waiver.<sup>112</sup> It should be noted that no country has an arbitration statute specifying that set-aside is automatically waived, and no case discusses automatic waiver of set-aside.<sup>113</sup> However, the issue of waiving set-aside *contractually* is not novel: U.S. courts have confronted the issue,<sup>114</sup> some European legislatures have specifically addressed the issue in statutes,<sup>115</sup> and academic commentators have written about it.<sup>116</sup> The policies that apply to contractual waiver of set-aside provide an analytical framework for the automatic waiver of set-aside. In the United States, the policy of protection has dictated set-aside waiver law, as courts have been concerned with the danger that waiving set-aside contractually would pose to both parties and to the courts as the final enforcers of arbitration awards.<sup>117</sup> Con-

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108. See *id.* Domestic laws that determine the level of court intervention in the proceedings vary from country to country, and “[w]hile many modern arbitration statutes specifically limit court intervention, if the jurisdiction allows courts to intervene, there is little an arbitration tribunal can do.” See *id.*; see also *infra* Part II.B-C.

109. See generally Federal Arbitration Act of 1925 (FAA), 9 U.S.C. §§ 1-16 (2006) (enumerating the grounds under which an award can be set aside; these grounds for avoiding having an award enforced are no longer available to parties).

110. See JONES DAY, *supra* note 86.

111. See generally FAA § 10 (stating that an award can be set aside “upon the application of any party to the arbitration”).

112. See *infra* Part II.B-C.

113. This statement is based on the knowledge of the author after extensive research.

114. See, e.g., *Hoefl v. MVL Grp., Inc.*, 343 F.3d 57 (2d Cir. 2003).

115. See *infra* Part II.B.2.a.

116. See, e.g., Thomas S. Meriwether, Comment, *Limiting Judicial Review of Arbitral Awards Under the Federal Arbitration Act: Striking the Right Balance*, 44 HOUS. L. REV. 739 (2007). Notably, the topic of limiting judicial review of arbitration awards by waiving set-aside has received little attention from academic commentators when compared to its counterpart: the contractual expansion of judicial review of an arbitration award. In fact, in a 2007 comment, Thomas Meriwether noted that he could only find five articles discussing the issue in considerable detail. See *id.* at 742 n.21 (2007). While the number has increased in the subsequent five years, it has not received much attention.

117. See *infra* Part II.B.2.

versely, in several European countries the policy of autonomy has played a decisive role.<sup>118</sup> Neither of these policies, however, supports an automatic waiver of the right to have an award set aside, and consequently the courts should resolve the circuit split to reflect the law in the Second Circuit.

1. *The Automatic Waiver Is at Odds with the U.S. Policy of Protecting the Parties and Courts*

In the United States, while the issue of automatic waiver of set-aside has not come up in courts or in academic commentary, courts *have* explicitly shown in cases concerning the contractual waiver of set-aside that set-aside-waiver jurisprudence is driven by a policy of protecting both the parties from unfair and defective awards and the integrity of the courts. As the U.S. policy of protection does not support contractual waiver of set-aside, it similarly does not support an automatic waiver.

a. U.S. Case Law Emphasizes Protection

In the United States, the issue of contractually limiting judicial review by waiving the right to have an award set aside is not codified in the Federal Arbitration Act,<sup>119</sup> and the issue has consequently been left to the courts. The U.S. Supreme Court has not yet decided the issue, and while the circuits are split in their interpretation of the FAA and contractual waiver of set-aside, the circuits' decisions are driven by the policy of protecting the parties.

The prominent case on the issue is *Hoeft v. MVL Group, Inc.*,<sup>120</sup> which was decided by the Second Circuit in 2003. In *Hoeft*, the court was presented with the issue of whether the FAA allows parties to waive judicial review of an arbitration award.<sup>121</sup> The parties included in their arbitration agreement a provision stating that the arbitrator's decision "shall be binding and conclusive upon each of the parties hereto and shall not be subject to any type of review or appeal whatsoever."<sup>122</sup> The Second Circuit refused to enforce this provision because "while arbitration is a contractual creation, the judicial review of an arbitration award is not contractual in nature and cannot be deprived by a private agreement."<sup>123</sup> Consequently, and significantly, the court held that parties cannot contractually eliminate judicial review of an arbitration award, because there is "a floor for judicial review of arbitration awards below which parties cannot require courts to

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118. See *infra* Part II.B.2.a.

119. See Federal Arbitration Act of 1925 (FAA), 9 U.S.C. §§ 1-16, 201-08 (no mention of waiving set-aside).

120. See *Hoeft v. MVL Grp., Inc.*, 343 F.3d 57 (2d Cir. 2003).

121. See *id.* at 60, 66; see also Meriwether, *supra* note 116, at 760; Mark R. Trachtenberg & Christina F. Crozier, *Risky Business: Altering the Scope of Judicial Review of Arbitration Awards by Contract*, 69 TEX. B.J. 868, 869 (2006).

122. See *Hoeft*, 343 F.3d. at 60.

123. See Gill, *supra* note 91, at 650; see also *Hoeft*, 343 F.3d. at 66 (holding that judicial review cannot be limited contractually).

go, no matter how clear the parties' intentions."<sup>124</sup> Several other circuits—including the Third and Eleventh Circuits—<sup>125</sup>agree with the Second Circuit's holding that judicial review of arbitration awards cannot be waived.

The Second Circuit's reasoning emphasized protecting the judicial process and parties involved from the negative consequences of their agreement to waive judicial review. First, the court was concerned with protecting the integrity of the judicial process.<sup>126</sup> Specifically, the court saw the arbitration and the judicial review processes as separate and "expressed its fear that turning over control of judicial procedures to the parties would compromise the integrity of the judiciary and the arbitration process as a whole, potentially rendering the courts mere 'rubber stamps.'"<sup>127</sup> Second, the court was concerned with protecting the parties from unfair and defective awards.<sup>128</sup> The court considered the FAA's set-aside standards and the common law manifest disregard standard<sup>129</sup> to be "critical safeguards" imposed by Congress and the Supreme Court.<sup>130</sup> Specifically, the court noted that if it were to uphold the waiver provision, then courts would be required to enforce arbitration awards that have been "tainted by partiality,

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124. See *Hoelt*, 343 F.3d. at 64; Trachtenberg & Crozier, *supra* note 121, at 869 (discussing *Hoelt*).

125. Similar to the Second Circuit, the Third Circuit does not allow parties to completely waive the right to set aside an arbitral award in the agreement. In *Communications Consultant, Inc. v. Nextel Communities of the Mid Atlantic, Inc.*, the Third Circuit considered the effect of a clause that read: "[T]he decision of the arbitrators shall be final and unreviewable for error of law or legal reasoning of any kind and may be enforced in any court having jurisdiction of the parties." *Commc'ns Consultant, Inc. v. Nextel Cmty. of the Mid Atl., Inc.*, 146 F. App'x 550, 552 (3d Cir. 2005). Significantly, the Third Circuit noted that although the language in the clause prevented parties from challenging an arbitrator's legal determinations in federal court, "[i]n the presence of such language, the only permissible basis upon which a litigant may challenge the panel's award is if the litigant can show that the panel's actions were influenced by 'corruption, fraud, or partiality,' or that the panel failed to provide a hearing to consider each party's views prior to issuing its decision." *Id.* at 552-53. Despite the Eleventh Circuit's disagreement with the Second Circuit regarding the overlap between FAA Chapters 1 and 2, it agrees with the Second Circuit in prohibiting parties from contractually waiving the right to set aside an award. In *Rollins, Inc. v. Black*, the Eleventh Circuit analyzed the effects of a clause rendering an award "binding, final, and non-appealable." See *Rollins, Inc. v. Black*, 167 F. App'x 798, 799 n.1 (11th Cir. 2006). The court did not interpret such language to mean that an award could not be reviewed by a court: although the parties could not appeal the merits of the dispute, they could still appeal the award if the award had resulted "from an arbitrator's abuse of authority, bias, or manifest disregard of the law." *Id.* See also *Kim-C1 LLC v. Valent Biosciences Corp.*, 756 F. Supp. 2d 1258, 1265-66 (E.D. Cal. 2010) (providing an overview of different circuits' law on contractually limiting judicial review of arbitration agreements). Even the Tenth Circuit in *Gorelick*, discussed *infra* Part II.B.1.a, noted that it would agree with the Second Circuit if the provision had entirely eliminated judicial review of the award. See *Meriwether*, *supra* note 116, at 765-66.

126. See *Meriwether*, *supra* note 116, at 761 (analyzing the nuances and implications of *Hoelt*).

127. See *id.*; *Hoelt*, 343 F.3d. at 64.

128. See *Hoelt*, 343 F.3d. at 64; *Meriwether*, *supra* note 116, at 760.

129. See generally Annie Chen, *The Doctrine of Manifest Disregard in the Law After Hall Street: Implications for Judicial Review of International Arbitrations in U.S. Courts*, 32 *FORDHAM INT'L L.J.* 1872 (2008) (discussing the manifest disregard of law standard).

130. See *Hoelt*, 343 F.3d. at 64; *Meriwether*, *supra* note 116, at 761.

a lack of elementary procedural fairness, corruption, or similar misconduct,”<sup>131</sup> clearly indicating the Second Circuit’s focus on protecting the parties’ due process rights when faced with complete contractual waiver of the right to juridical review and of the right to have an award set aside.

The same emphasis on protection remained prominent in the Tenth Circuit’s decision in *MACTEC, Inc. v. Gorelick*. Unlike *Hoefst*, in which the Second Circuit considered a set of facts in which parties had completely waived judicial review in their arbitration clause, the Tenth Circuit in *Gorelick* was faced with a case where the parties had not entirely waived or eliminated judicial review of the award.<sup>132</sup> Rather, the provision agreed to by the parties stated that “[j]udgment upon the award rendered by the arbitrator shall be final and nonappealable and may be entered in any court having jurisdiction thereof.”<sup>133</sup> Notably, the provision in this case did not eliminate all judicial review because it bound the parties to the judgment of the trial court. Because the provision did not eliminate all judicial review, the Tenth Circuit upheld the provision, holding that parties are allowed to contractually eliminate *appellate-level* review.<sup>134</sup>

In *Gorelick*, like in *Hoefst*, the court considered whether the parties were adequately protected under the rule. The *Gorelick* court, however, based its decision on the requirement that the limited review rule does not conflict “with the federal policies furthered by the FAA.”<sup>135</sup> In addition to the fundamental policy of reducing litigation costs by providing a more efficient forum, another important policy concern is ensuring that arbitration awards enforced by courts are not procedurally unfair or defective.<sup>136</sup> This statutory goal of avoiding procedurally unfair or defective awards serves to protect parties from the risks inherent in arbitration proceedings. In sum, despite the *Hoefst* and *Gorelick* courts’ different methods of analysis, the courts’ emphasis on protecting the parties and the judicial system demonstrates an underlying *policy* of protection in the United States.

#### b. Automatic Waiver and U.S. Policy and Law

The concept of an automatic waiver of the right to set aside an arbitration award is inconsistent with U.S. law on contractual waiver of set-aside and the policy of protecting parties and courts that has driven that body of law. First, if parties automatically waive the right to set aside an award, then the courts—who must still confirm the award—would have no choice

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131. See *Hoefst*, 343 F.3d. at 64; Meriwether, *supra* note 116, at 761; see also Gill, *supra* note 91, at 650 (noting that Congress, when enacting the FAA, sought to “balance the importance of a flexible dispute resolution system with the need to prevent patently unfair arbitration awards by delineating specific safeguards in section 10(a)”).

132. See Meriwether, *supra* note 116, at 762.

133. See *MACTEC, Inc. v. Gorelick*, 427 F.3d 821, 827 (10th Cir. 2005).

134. See *id.* at 829-30 (distinguishing *Gorelick* from *Hoefst*); see also Gill, *supra* note 91, at 651; Meriwether, *supra* note 116, at 762-63.

135. See *Gorelick*, 427 F.3d at 829 (citing *Bowen v. Amoco Pipeline Co.*, 254 F.3d 925, 935 (10th Cir. 2001)); see also Meriwether, *supra* note 116, at 763.

136. See *Gorelick*, 427 F.3d at 829 (mentioning costs and efficiency and referring to the “policy concerns implicated by *Hoefst*”); see also Meriwether, *supra* note 116, at 763.



but to function as “rubber stamps.”<sup>137</sup> Indeed, if set-aside proceedings were no longer an option, courts would be forced to confirm unfair and defective awards absent allegations that the entire contract was invalid due to fraud, coercion or duress.<sup>138</sup>

Second, where there is an automatic waiver of set-aside there is arguably even less protection—or more risk to parties—than with a contractual waiver of set-aside. When parties expressly contract to waive set-aside, they presumably had a fair opportunity during negotiations to weigh the consequences of that waiver. After all, despite the discussion above about parties’ failure to recognize tactical advantages and pitfalls, parties that expressly waive set-aside must add that provision to the standard arbitration clause. In consciously giving up the right to set-aside, parties likely take into account the consequences that could stem from that decision if a court issues an unfavorable award against them; the monetary consequences are perhaps more readily apparent to parties than, for example, the consequences of choosing one U.S. jurisdiction over another. Conversely, in the case of automatic waiver, the parties would need foresight to anticipate such consequences when choosing the seat of arbitration; and indeed, as this Note has already discussed, parties drafting agreements do not always take into account tactical opportunities and pitfalls of choosing a certain seat.<sup>139</sup> Therefore, an automatic waiver might provide less protection than a contractual waiver simply due to the parties’ lack of foresight regarding when an automatic waiver could be imposed and current attitudes towards drafting arbitration clauses.

In addition, and on a more basic level, the concept of an automatic waiver of set-aside—which completely eliminates set-aside proceedings and consequently eliminates judicial review of the award—is in direct conflict with the current state of the law wherein complete contractual waiver of set-aside and judicial review will not be enforced by courts.<sup>140</sup> Given this incompatibility of the automatic waiver with U.S. law concerning the issue of contractual waiver of set-aside and the policies underlying that law, the courts should resolve the circuit split to reflect the state of the law in the Second Circuit, where the rule does not result in an automatic waiver.

## 2. *The Automatic Waiver Is at Odds with the International Focus on Autonomy*

### a. *The Modern International View Promotes Autonomy*

While U.S. policies and law advocating for a resolution in favor of the Second Circuit should factor in heavily in deciding how the circuit split is resolved, it is important to recognize that the policy of autonomy that has driven the set-aside waiver laws of several European states also speaks against the introduction of an automatic waiver. Indeed, contrary to the

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137. See *Hoelt v. MVL Grp., Inc.*, 343 F.3d 57, 64 (2d Cir. 2003).

138. See generally Federal Arbitration Act of 1925 (FAA), 9 U.S.C. § 10; New York Convention, *supra* note 15, art. V.

139. See *supra* Part II.A.

140. Compare *supra* Part II.B.1.a, with *supra* Part I.D.3.

United States, several European countries have codified their laws relating to the contractual waiver of set-aside, and in the countries that have done so, the law overwhelmingly allows for parties to contractually waive the right to set aside an award.<sup>141</sup> Note, however, that these European laws only speak to contractual waiver of set-aside and that these countries have not addressed the issue of automatic set-aside.<sup>142</sup>

One example of the European approach to contractual waiver of set-aside is Article 1522 of the new French arbitration law,<sup>143</sup> which came into effect on January 13, 2011. The French law allows parties to waive the right to have the award set aside in front of French courts where the seat of arbitration was in France. This waiver must be clearly expressed in a “specific agreement.”<sup>144</sup> However, the article also states that even if the parties agreed to waive the right to set-aside proceedings, the parties can still challenge the enforcement of an award in France on any of the five grounds for annulment in the French Arbitration Act.<sup>145</sup> Therefore, the French law allows for parties to challenge the enforcement of the award in France, even if the validity of the award cannot be challenged because parties waived the right to set-aside.<sup>146</sup>

Unlike the French law, the other European laws that allow for waiver of set-aside proceedings require the parties to have no link to the seat of arbitration. For example, Article 192 of the Swiss Private International Law Act allows parties to waive the right to set aside proceedings where the seat of arbitration has been in Switzerland only if the waiver is expressly stated and if neither of the parties is domiciled in Switzerland, has a habit-

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141. See, e.g., Bundesgesetz über das Internationale Privatrecht [IPRG] [Swiss Private International Law Act], Dec. 18, 1987, SR 291, art. 192.

142. To the knowledge of the author, none of the European laws consider automatic waiver of set-aside. See, e.g., *id.* (no mention of automatic waiver).

143. See Loi 2011-48 du 13 janvier 2011 portant réforme de l'arbitrage [Decree No. 2011-48 of 13 January 2011 reforming the law governing arbitration], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Jan 14, 2011, p. 777. The text of Article 1522 of the new French arbitration law states:

Par convention spéciale, les parties peuvent à tout moment renoncer expressément au recours en annulation. Dans ce cas, elles peuvent toujours faire appel de l'ordonnance d'exequatur pour l'un des motifs prévus à l'article 1520. L'appel est formé dans le délai d'un mois à compter de la notification de la sentence revêtue de l'exequatur. La notification est faite par voie de signification à moins que les parties en conviennent autrement.

The official English translation reads as follows:

By way of a specific agreement the parties may, at any time, expressly waive their right to bring an action to set aside. Where such right has been waived, the parties nonetheless retain their right to appeal an enforcement order on one of the grounds set forth in Article 1520. Such appeal shall be brought within one month following notification of the award bearing the enforcement order. The award bearing the enforcement order shall be notified by service (*signification*), unless otherwise agreed by the parties.

*Id.*, translated in French Decree of 13 Jan. 2011, INT'L ARB. INST. PARIS, [http://www.iaiparis.com/pdf/FRENCH\\_LAW\\_ON\\_ARBITRATION.pdf](http://www.iaiparis.com/pdf/FRENCH_LAW_ON_ARBITRATION.pdf) (last visited Nov. 4, 2012).

144. See *id.*

145. See *id.*

146. See *id.*; see also JONES DAY, *supra* note 86, at 4.

ual residence in Switzerland, or has a business establishment in Switzerland.<sup>147</sup> Similarly, § 51 of the Swedish Arbitration Act permits parties to expressly waive the right to set-aside if neither of the parties is domiciled or has its place of business in Sweden.<sup>148</sup> However, while the Swiss and Swedish laws have requirements about the parties' links to Switzerland and Sweden, these requirements do not necessarily limit parties' ability to waive set-aside beyond the French law, because often the seat of arbitration

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147. See Bundesgesetz über das Internationale Privatrecht [IPRG] [Swiss Private International Law Act] Dec. 18, 1987, SR 291, art. 192. The text of Article 192 of the Swiss Private International Law Act states:

X. Verzicht auf Rechtsmittel

1. Hat keine der Parteien Wohnsitz, gewöhnlichen Aufenthalt oder eine Niederlassung in der Schweiz, so können sie durch eine ausdrückliche Erklärung in der Schiedsvereinbarung oder in einer späteren schriftlichen Übereinkunft die Anfechtung der Schiedsentscheide vollständig ausschliessen; sie können auch nur einzelne Anfechtungsgründe gemäss Artikel 190 Absatz 2 ausschliessen.

2. Haben die Parteien eine Anfechtung der Entscheide vollständig ausgeschlossen und sollen die Entscheide in der Schweiz vollstreckt werden, so gilt das New Yorker Übereinkommen vom 10. Juni 1958 über die Anerkennung und Vollstreckung ausländischer Schiedssprüche sinngemäss.

The official English translation reads as follows:

X. Waiver of annulment

1. If none of the parties have their domicile, their habitual residence, or a business establishment in Switzerland, they may, by an express statement in the arbitration agreement or by a subsequent written agreement, waive fully the action for annulment or they may limit it to one or several of the grounds listed in Art. 190, subsection 2.

2. If the parties have waived fully the action for annulment and if the award is to be enforced in Switzerland, the New York Convention of June 10, 1958 on the Recognition and Enforcement of Foreign Arbitral Awards applies by analogy.

*Id.*, translated in SWITZERLAND'S PRIVATE INTERNATIONAL LAW STATUTE OF DECEMBER 18, 1987 165 (Pierre A. Karrer & Karl W. Arnold trans., Kluwer Law and Taxation Publishers 1989) (1987).

148. See 51 § LAG OM SKILJEFÖRFARANDE (Svensk författningssamling [SFS] 1999:116). Section 51 of the Swedish Arbitration Act states:

Har inte någon av parterna hemvist eller driftställe i Sverige, får de i ett kommersiellt förhållande genom en uttrycklig skriftlig överenskommelse utesluta eller begränsa tillämpligheten av de grunder för upphävande av en skiljedom som anges i 34 §. En skiljedom som omfattas av en sådan överenskommelse erkänns och verkställs i Sverige enligt de regler som gäller för en utländsk skiljedom.

The official translation reads as follows:

Where none of the parties is domiciled or has its place of business in Sweden, such parties may in a commercial relationship through an express written agreement exclude or limit the application of the grounds for setting aside an award as are set forth in section 34. An award which is subject to such an agreement shall be recognised and enforced in Sweden in accordance with the rules applicable to a foreign award.

*Id.*, translated in *The Swedish Arbitration Act (SFS 1999:116)*, ARB. INST. STOCKHOLM CHAMBER COM., <http://www.chamber.se/?id=23746> (last visited Nov. 4, 2012).

is chosen for the purposes of neutrality where neither party has ties to the seat.<sup>149</sup>

The crucial commonality between the French, Swiss, and Swedish laws, however, is that parties can contractually waive the right to set aside an award arising from arbitration in those countries, provided that the waiver is clear and explicit. Notably, this requirement that the waiver be clear and explicit addresses some of the concerns about protecting the parties from unfair and defective awards that worry U.S. courts. Interestingly, however, even though these foreign laws and statutes take into account concerns of protecting the parties and their due process rights,<sup>150</sup> the main policy driving these laws is not protection.

Rather, the main policy behind the French, Swiss, and Swedish laws' permissive approach to contractual waiver of set-aside is the promotion of party autonomy.<sup>151</sup> The PricewaterhouseCoopers study found that the most important advantage of arbitration for in-house counsel was the flexibility and the autonomy inherent in the arbitration process.<sup>152</sup> In the same vein, the official French commentary on the new law noted that the ability to waive set-aside proceedings can be useful,<sup>153</sup> and this runs tandem with the in-house counsels' preference for the flexibility to choose provisions, such as a waiver of set-aside, that they deem useful for their company's arbitration goals and strategy.<sup>154</sup>

Academic commentators have explained the European regimes' focus on autonomy—and the consequent liberal attitude towards contractual set-aside—using the theory of “denationalization of international arbitration.”<sup>155</sup> Specifically, these countries reform and modernize their arbitration laws to focus on autonomy by “curtail[ing] national court involvement in international commercial arbitration.”<sup>156</sup> While no state has entirely denationalized international commercial arbitration, some of the more modern states have “effectively incorporated denationalized arbitration

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149. See WHITE & CASE, 2010 INTERNATIONAL ARBITRATION SURVEY: CHOICES IN INTERNATIONAL ARBITRATION 17–20, available at [http://www.whitecase.com/files/upload/fileRepository/2010International\\_Arbitration\\_Survey\\_Choices\\_in\\_International\\_Arbitration.pdf](http://www.whitecase.com/files/upload/fileRepository/2010International_Arbitration_Survey_Choices_in_International_Arbitration.pdf) (finding that the most important factor for practitioners choosing the seat of arbitration was the formal legal infrastructure of the seat, which includes neutrality and impartiality).

150. See, e.g., JONES DAY, *supra* note 86, at 4.

151. See *id.* (noting that the ability to waive annulment proceedings increases party autonomy).

152. See *supra* Part I.A and the sources cited therein.

153. See Rapport au Premier ministre relatif au décret no 2011-48 du 13 janvier 2011 portant réforme de l'arbitrage [Report to the Prime Minister on the Decree No. 2011-48 of January 13, 2011 to reform arbitration], JOURNAL OFFICIEL DE LA RÉPUBLIQUE FRANÇAISE [J.O.] [OFFICIAL GAZETTE OF FRANCE], Jan. 14, 2011, p. 177.

154. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 3.

155. See Behrens, *supra* note 2, at 20.

156. See KATHERINE LYNCH, THE FORCES OF ECONOMIC GLOBALIZATION: CHALLENGES TO THE REGIME OF INTERNATIONAL COMMERCIAL ARBITRATION 279 (2003) (using the examples of Belgium, Switzerland, Sweden, and Tunisia, all of which permit contractual waiver of set-aside).

detached from the scrutiny and regulation of the national court systems.”<sup>157</sup> Applying this theory to the concept of contractual waiver of set-aside, national courts have less influence in the process of arbitration when such a provision is included in the arbitration clause, because the courts will only be able to enforce the award and will not be able to scrutinize it on its merits. However, it should be noted that because the courts must enforce the award, they are not completely isolated from the arbitration process. Interestingly, this denationalization of arbitration that characterizes the European regimes’ approach runs contrary to the U.S. courts’ concerns about contractual waiver of set-aside rendering the courts mere rubber stamps and possibly explains the stark differences between the U.S. and European approaches to contractual waiver of set-aside.

Furthermore, academics have noted that this focus on denationalization and autonomy aims to attract a greater share of the lucrative arbitration business by making their country a more attractive seat for arbitration.<sup>158</sup> In support of this assertion, following the reform of the French arbitration law in 2011, numerous law firms noted in their client alerts and commentaries that the new French law—especially its innovative set-aside waiver provision—increases party autonomy and makes France a more attractive seat for arbitration.<sup>159</sup> In addition, the French Justice Minister, Michel Mercier, confirmed in an interview that “one of the aims of the new law is to maintain the leading role of Paris as a seat for international arbitration and to ensure that the ICC, including its Court of Arbitration, maintains its headquarters in France.”<sup>160</sup>

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157. See *id.* at 279, 282.

158. See *id.*; see also Behrens, *supra* note 2, at 37–38 (noting that “[i]t should furthermore not be forgotten that arbitration is a business in itself. The stakes are high. . . . [D]ifferences in national regulation of arbitration generate intense international competition between arbitration centers. Such competition leads to national deregulation of the arbitration process.”).

159. See JONES DAY, *supra* note 86, at 4 (noting the increase in autonomy); see also Michael Ostrove & Théobald Naud, *France Reforms its Arbitration Law*, DLA PIPER (Mar. 16, 2011), <http://www.dlapiper.com/france-reforms-its-arbitration-law/> (noting that the new law “indisputably improves the clarity and efficiency of French arbitration law and will reinforce the position of Paris as a leading arbitration centre”); Herbert Smith, *The New French Arbitration Law*, JAPAN DISP. AVOIDANCE NEWSL., (on file with author) (“[T]his waiver option aims to modernise French law by giving greater autonomy to parties.”); Norton Rose, *New French Arbitration Law Reflects a Boldly Liberal Approach*, INT’L ARB. (Feb. 2011), <http://www.nortonrose.com/files/international-arbitration-new-french-arbitration-law-reflects-a-boldly-liberal-approach-pdf-762-kb-34983.pdf> (noting that the law “to a very great extent . . . has achieved the objective of innovating, simplifying and strengthening French arbitration law—and also of reinforcing the attraction of Paris as a seat of choice for conducting arbitral proceedings”); Christoph von Krause et al., *Alerts: New French Arbitration Law*, WHITE & CASE (Jan. 2011), <http://www.white-case.com/alerts-01202011/> (hailing the new law as “enhancing France as one of the most arbitration friendly jurisdictions in the world”).

160. See John V.H. Pierce, Gary Born & Maxi Scherer, *Revision to French Arbitration Law Arrives*, N.Y. L.J. (May 16, 2010), <http://www.wilmerhale.com/files/Publication/c44d85e0-53cb-404d-b71f-0afaddbf8d75/Presentation/PublicationAttachment/5f4e59e0-8088-426c-87a7-0f20ba53800e/Revision%20to%20French%20Arbitration%20Law%20Arrives.pdf>.

### b. Automatic Waiver and International Policy

Just as the concept of automatic waiver is incompatible with the U.S. policy of protection, it is similarly incompatible with the European policy of autonomy. It is true that with an automatic waiver national courts do not regulate the arbitration and do not scrutinize the award, thus reflecting the European movement towards denationalization of arbitration. However, it is questionable whether the European liberal approach towards waiver of set-aside—and the consequent minimal court involvement—would reach to an automatic waiver, as a cornerstone of the French, Swiss, and Swedish waiver laws is the requirement that the waiver be clear and explicit.<sup>161</sup> With an automatic waiver, such a requirement—that effectively acts as a safeguard of the parties' due process rights—is not possible. Even more significantly, the denationalization of arbitration rests heavily on the concept of party autonomy. However, with an automatic waiver, parties are stripped of the opportunity to choose whether they want to waive the right to set-aside, effectively negating the flexibility that the opportunity for contractual waiver of set-aside provides.<sup>162</sup> Furthermore, insofar as the requirement that the waiver be explicit can be viewed as a safeguard of party autonomy by serving to demonstrate that the parties are making a conscious choice, an automatic waiver similarly fails in that function by not requiring explicit consent. Given that both the policies of protection and autonomy that have driven set-aside waiver laws in the United States and Europe, respectively, are incompatible with the concept of an automatic waiver of set-aside, the courts should resolve the circuit split in favor of the Second Circuit's rule.

### C. Time to Modernize and Simplify: Making the United States a More Attractive Seat for Arbitration

While many international jurisdictions have focused on autonomy when drawing up their set-aside waiver laws, the United States has emphasized the need to protect the parties and the integrity of the judicial system.<sup>163</sup> Even if the U.S. Supreme Court were to resolve the circuit split to eliminate the possibility of an automatic waiver of the right to set aside an award in the Eleventh Circuit, the United States should also modernize its laws and allow contractual waiver of set-aside to reflect a commitment to party autonomy. The United States' current policy focus on protection in set-aside waiver law, while understandable, is not only at odds with the more modern and liberal arbitration regimes advocating autonomy, but also at odds with the focus on the freedom of contract that pervades other aspects of U.S. arbitration law.<sup>164</sup> Furthermore, if the United States were to increase its focus on autonomy and allow for contractual waiver of set-

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161. See *supra* Part II.B.2.a (discussing the French, Swiss and Swedish laws' requirement that the waiver be explicit).

162. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 2.

163. See *supra* Part II.B.1.

164. Compare *supra* Part II.B.1 with *supra* Part II.B.2. and *infra* Part II.C.1.

aside, it would reinforce its position as an attractive and popular seat for arbitration, thus potentially bringing to the United States a bigger share of the lucrative arbitration business that the European arbitration regimes are similarly seeking with their liberal arbitration laws.<sup>165</sup>

### 1. Refocusing on Freedom of Contract

U.S. law should shift its focus to autonomy in set-aside waiver law and allow parties to contractually waive the right to set-aside proceedings, because in areas of arbitration law not relating to waiver of set-aside or the limitation and expansion of judicial review, U.S. legislators and courts have already noted and adhered to the importance of freedom of contract principles. First, the legislative history of the FAA indicates that the purpose of the Act was the specific enforcement of arbitration agreements.<sup>166</sup> For example, a House committee report stated that “[a]rbitration agreements are purely matters of contract.”<sup>167</sup> According to legislative history, the purpose of the FAA is to “provide a simple method by which the parties may be brought before the court in order to give enforcement to that which they have already agreed to.”<sup>168</sup>

Second, U.S. courts have similarly held that freedom of contract principles are crucial in arbitration. For example, the U.S. Supreme Court in *Volt Information Sciences v. Board of Trustees of Leland Stanford, Jr. University* stated that the FAA only provides the right to obtain an order directing that the arbitration proceed in the manner provided for in the parties’ agreement.<sup>169</sup> Furthermore, the U.S. Supreme Court in *Southland Corp. v. Keating* pointed to the fact that as arbitration contracts are negotiated “by experienced and sophisticated businessmen, . . . absent some compelling and countervailing reason it should be honored by the parties and enforced by the courts.”<sup>170</sup> Such legislative and judicial history emphasizing freedom of contract principles, autonomy, and the strict enforcement of party agreements regarding arbitration support the argument that agreements providing for waiver of set-aside should be enforced and are not in conflict with the spirit of the FAA and U.S. arbitration law.

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165. See *infra* Part II.C.2.

166. See Milan Koptsiovsky, Note, *A Right to Contract for Judicial Review of an Arbitration Award: Does Freedom of Contract Apply to Arbitration Agreements?*, 36 CONN. L. REV. 609, 614-15 (2004) (discussing the emphasis on freedom of contract principles in U.S. legislative history and in U.S. case law regarding arbitration).

167. See *id.* at 614 (discussing and citing H.R. REP. NO. 68-96, at 1 (1924)).

168. See *id.* (discussing and citing 65 CONG. REC. H1931 (daily ed. Feb. 5, 1924) (statement of Rep. Graham)).

169. See *id.* at 623 (discussing and citing *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Jr. University*, 489 U.S. 468, 474-75 (1989)).

170. See *id.* at 624 (discussing and citing *Southland Corp. v. Keating*, 465 U.S. 1, 7 (1984) (original citation omitted)); but see *supra* Part II.A (noting that the drafters of arbitration clauses do not always draft the clauses competently).

## 2. *Increasing the United States' Attractiveness as a Seat of Arbitration*

In addition to legislative history and case law that support modernizing contractual set-aside waiver law to allow for contractual waiver in the United States, U.S. law should also allow for contractual waiver of the right to set-aside proceedings because it will increase the attractiveness of the United States as a seat of arbitration, as it has done for its European counterparts.<sup>171</sup> While the United States is already a popular choice among corporations as a seat of arbitration,<sup>172</sup> the United States would benefit from further increasing its attractiveness as a seat of arbitration. Not only is arbitration a lucrative industry,<sup>173</sup> but increasing the attractiveness of the U.S. as a seat also would (1) potentially forge closer links between foreign corporations and the United States and (2) increase the arbitration knowledge and skills of U.S. practitioners who would be exposed to more arbitration.

Modernizing the contractual set-aside waiver law would increase the attractiveness of the United States as a seat of arbitration, first and foremost because parties will be attracted to the flexibility and autonomy offered by U.S. laws to create the kind of arbitration proceedings that suit their arbitration needs and strategy.<sup>174</sup> Second, the United States will be more attractive as a seat for arbitration if the law regarding contractual waiver of set-aside is clarified by increasing its consistency with other aspects of U.S. arbitration law. Currently, set-aside waiver law is not as deferential to party agreement as other areas of U.S. arbitration law.<sup>175</sup> In this aspect, the United States could benefit from looking to France's modernization of its arbitration law, as France reported that its efforts to attract arbitration to France involved both increased autonomy and a clarification of its laws that make them more accessible to foreign practitioners drafting arbitration agreements with France as the seat of arbitration.<sup>176</sup> Since the arbitration process can fail to meet parties' expectations due to poor drafting of the clause or because parties did not take into account all legal consequences, strategic opportunities and pitfalls, any additional clarity and accessibility in the U.S. arbitration law will certainly be a welcome development to everyone who has to draft international commercial arbitration clauses.

## Conclusion

This Note recommends that the circuit split between the Second and Eleventh Circuits, which logically results in an automatic waiver of the right to set-aside proceedings when an arbitration in the Eleventh Circuit

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171. See sources cited in *supra* note 159.

172. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 3.

173. See Behrens, *supra* note 2, at 37-38.

174. See *supra* Part I.A and the sources cited therein.

175. See *supra* Part II.C.1.

176. See sources cited in *supra* note 159.



results in a foreign or non-domestic award, should be resolved in favor of the Second Circuit's rule. This Note argues that while an automatic waiver is compatible with some of the benefits of arbitration and assuages some of the inherent concerns, it is fundamentally incompatible with the policies of protection and autonomy, which have dictated contractual set-aside waiver law in the United States and abroad, respectively. Furthermore, this Note recommends that even if the courts were to resolve the split to eliminate the possibility of an automatic waiver, Congress and the Supreme Court should allow contractual set-aside to increase the consistency of U.S. arbitration law and the attractiveness of the United States as a seat of arbitration.

While this Note explores the concept of an automatic waiver, this Note at its core argues that because drafting arbitration clauses poses unique challenges by affecting both the procedure and outcome of arbitration, there is no need to further complicate the process. Unfortunately, in the United States the process has been complicated by a complex legal regime that is inconsistent with the policies surrounding arbitration and that can surprise parties with undesired and expensive consequences. PricewaterhouseCoopers' study noted that 95% of in-house counsel expected to use international commercial arbitration as their method of cross-border dispute resolution, and they expect the number of such cases to increase.<sup>177</sup> Unless complex laws such as those resulting in the circuit split discussed in this Note are simplified and made more uniform, it is increasingly likely that as more parties resort to arbitration they will end up in a losing situation like our hypothetical U.S. chain and its international investors. In our hypothetical, it is entirely possible that the U.S. chain and the international investors chose to arbitrate in the Eleventh Circuit. It is also possible that due to the attorneys' oversight or lack of understanding of tactical advantages when drafting the clause the U.S. chain would be on the hook for \$40 million with no recourse through set-aside proceedings. Furthermore, what adds insult to the U.S. chain's injury is the fact that the theoretical arbitration proceedings were unfair: the U.S. chain was not given a full and fair chance to be heard before the \$40 million award was rendered. If this situation were to occur in reality, no explanation of the attorneys' shortcomings or the fact that it is industry practice to rely on a standard clause will be of much comfort to the U.S. chain. In fact, it is not too far of a stretch to say that losing recourse to set-aside proceedings would lead the U.S. chain to launch a warranted malpractice suit against its attorneys.

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177. See INTERNATIONAL ARBITRATION: CORPORATE ATTITUDES AND PRACTICES 2006, *supra* note 2, at 3.

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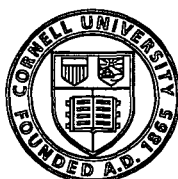
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