PROVENZANO GRANNE & BADER LLP News & Analysis

International Arbitration & Local Law

One of the principal virtues of international arbitration is supposed to be that it frees the parties from concerns about idiosyncratic or biased local courts. You've carefully selected the law governing the substance of the contract, an arbitration organization to administer the proceedings and a tribunal of eminent practitioners. They will find the facts, apply the law and—win or lose—you won't have to deal with the peculiarities of the national courts.

Well, mostly. Certainly the *enforcement* of a final arbitral award is supposed to be nearly automatic no matter what court you are in. But a couple of recent cases—one from the U.S. Supreme Court and one from New York's highest court—show how domestic procedural law can have a profound effect on the practical results of arbitration. These cases show how selecting the formal location of your arbitration—which may or may not be the location of actual hearings or deliberations—can materially affect the process of arbitration.

The Arbitral Framework

The key international agreement in the arbitral framework is the New York Convention of 1958—The United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards. The U.S. has implemented the New York Convention through the Federal Arbitration Act, or FAA.

In very broad terms, the courts of signatories to the New York Convention must provide both a mechanism to compel parties to arbitrate when appropriate and a mechanism to recognize and enforce arbitral awards rendered in other jurisdictions, subject only to specific exceptions.

These are two different judicial tasks, though, and courts have different powers when it comes to performing them.

The courts of the jurisdiction where the arbitral tribunal sits have the power over the arbitration itself—most significantly, to determine the scope of the arbitration agreement, to compel arbitration when appropriate and to set aside or suspend an award on certain grounds. This is called (in the U.S.) "primary" jurisdiction. All other courts exercise "secondary" jurisdiction, limited to recognizing and enforcing arbitral awards, or refusing to do so on certain limited and enumerated grounds.

Courts with "primary" jurisdiction therefore sometimes have to deal with challenging questions as to the propriety of the arbitration itself. And they often look to their own domestic law to answer those questions.

When Can Parties Be Compelled to Arbitrate Even if They Did Not Sign the Arbitration Agreement?

One such question is whether someone who is not a signatory to an arbitration agreement can nonetheless be compelled to arbitrate a dispute.

It is a common truism that arbitration is a creature of contract and nobody can be compelled to arbitrate absent an agreement to do so. Like many truisms, this one isn't always true. There are circumstances under which the domestic law of a party to the New York Convention permits a party to be compelled to arbitrate even if it did not sign the relevant arbitration agreement.

In *GE Energy Power Conversion France SAS, Corp., f/k/a Converteam SAS, Petitioner v. Outokumpu Stainless USA, LLC, et al.*, 590 U. S. — (2020) (No. 18-1048), resolving a Circuit split, the Supreme Court concluded that Alabama state law could provide grounds under the New York Convention to compel a non-signatory to arbitrate.

In *GE Energy*, Outokumpu's predecessor in interest hired a prime contractor to perform services in connection with a steel plant in Alabama. Those agreements contained arbitration clauses. The contractor then subcontracted with GE Energy to provide motors for cold rolling mills. Those agreements did not contain arbitration clauses. When GE Energy's motors failed, Outokumpu sued them in Alabama state court. GE Energy removed to the District Court and sought to compel arbitration on the basis of the arbitration agreement between Outokumpu's predecessor in interest and the prime contractor, even though GE Energy was not a party to that agreement.

The District Court compelled arbitration relying on the FAA, based on the definitions contained in the relevant agree-

ments, despite the fact that GE Energy was not a signatory. The Eleventh Circuit reversed, concluding that under the New York Convention, the parties must *actually sign* an agreement to arbitrate their disputes in order to compel arbitration. More significant for this analysis, the Circuit concluded that GE Energy could not rely on state-law equitable estoppel doctrines to enforce the arbitration agreement as a nonsignatory because relying on those state law doctrines would conflict with the Convention.

The Supreme Court reversed. It held that the FAA permits courts to look to state law doctrines in determining the scope of arbitration agreements. The Supreme Court explained that the FAA places arbitration agreements "upon the same footing as other contracts" but "does not 'alter background principles of state contract law regarding the scope of agreements (including the question of who is bound by them).'" In *GE Energy*, the relevant doctrine was that of equitable estoppel, which "allows a nonsignatory to a written agreement containing an arbitration clause to compel arbitration where a signatory to the written agreement must rely on the terms of that agreement in asserting its claims against the nonsignatory."

The Supreme Court saw no conflict between the application of equitable estoppel to compel arbitration and the New York Convention. It noted that "the Convention requires courts to rely on domestic law to fill the gaps; it does not set out a comprehensive regime that displaces domestic law."

GE Energy makes clear that a court exercising its "primary" jurisdiction to compel arbitration (or to decline to do so) may look to local contract law to determine whether a party is bound by an arbitration agreement. The key lesson is that state contract law can play a big role in determining whether a party is even entitled to arbitrate.

When Is an Arbitral Award Final?

On the other end of the process, when is the arbitration complete and the award final and ready for enforcement?

"*Functus officio*"—Latin for "the duty/office having been performed"—is a term seen often in arbitral law overseas, but less commonly in U.S. law. When an arbitral tribunal has completed its assigned task and rendered a final award, the tribunal becomes *functus officio*; it has performed its agreed function and forever loses jurisdiction over the dispute, the award, and the parties. This is in sharp distinction with the law of the U.S. federal and many state *courts*, which have jurisdiction to correct their judgments in appropriate circumstances effectively indefinitely. *See, e.g.*, N.Y. C.P.L.R. 5015, Fed. R. Civ. P. 60.

The practical significance of *functus officio* is that once a tribunal's *officio* is *functus*, it has no power to fix an error in its award, no matter how obvious or egregious. It is then over to the courts, whose powers as to arbitral awards are often quite limited. If something is wrong in an award once the tribunal is *functus officio*, it may well be *definitively* wrong.

So when is a tribunal *functus officio*? If you are trying to enforce an award in state court that may well be a question of state law.

In *American International Specialty Lines Insurance Company v. Allied Capital Corporation, et al.*, — N.Y.3d —, 2020 Slip Op. 23 (2020), the New York Court of Appeals considered whether a tribunal had the authority to correct a "Partial Final Award," or whether it had rendered itself *functus officio* by calling it "final."

American International was about insurance coverage. Following a request for summary determination of some issues, the tribunal rendered a "Partial Final Award." That award determined which policies applied, who was insured and whether the loss at issue was an insured loss. The answer to the last question was no, but the Tribunal concluded that Allied Capital was nonetheless entitled to defense costs so the proceedings continued and an evidentiary hearing was set for that issue.

Before the hearing could happen, the losing parties sought reconsideration by the tribunal of the Partial Final Award. The prevailing party opposed both on the ground that the tribunal was right and on the ground that it was now *functus officio* as to those issues. The tribunal rejected the *functus officio* argument and reconsidered the Partial Final Award. It also then reversed course in a Corrected Partial Final Award, determining that the loss *was* covered, and ultimately issuing a Final Award when the amount of the loss was determined.

American International sought to vacate the Corrected Partial Final Award and the Final Award on the ground that the tribunal was *functus officio* after the Partial Final Award. The trial court rejected this view and confirmed the Final Award. The Appellate Division reversed, concluding that "nothing in the record . . . suggest[ed] that the parties or the panel believed that the [Partial Final Award] would be anything less than a final determination" and that "under the

functus officio doctrine, it [was] improper and in excess of the panel's authority" to reconsider the Partial Final Award.

The Court of Appeals reversed, reinstating the Final Award.

The Court first emphasized "New York's 'long and strong public policy favoring arbitration'" and the fact that it has "steadfastly discouraged courts from becoming unnecessarily entangled in arbitrations or from serving 'as a vehicle to protract litigation.'" It emphasized that the grounds for vacating an arbitral award are narrow; the provision allowing *vacatur* when arbitrators exceed their powers applies "only when they issue an award that "'violates a strong public policy, is irrational or clearly exceeds a specifically enumerated limitation on the arbitrator's power.'"

American International argued that the tribunal exceeded its powers by violating the *functus officio* doctrine. Allied Capital took the expansive position that *functus officio* "is no longer valid under New York law inasmuch as that doctrine was grounded upon anti-arbitrational sentiments rejected long ago by our state courts and by Congress in the Federal Arbitration Act."

The Court of Appeals declined the invitation to write *functus officio* out of New York law. Instead, it concluded that, whatever it was called by the tribunal, the Partial Final Award was not really final.

The Court noted that "under our case law, a final arbitration award is generally one that resolves the entire arbitration." It surveyed federal cases where the parties expressly agreed to a bifurcation of the proceedings or that certain issues would be separately submitted for final determination, but saw no reason "to determine whether or under what circumstances parties may agree to the issuance of a final award that disposes of some, but not all, of the issues submitted to the arbitrators." The Court concluded that there was no such agreement and that "[a]bsent an express, mutual agreement between the parties to the issuance of a partial and final award, the *functus officio* doctrine would have no application in this case."

Thus, the Court of Appeals did not wholly endorse the body of federal law on bifurcated proceedings and *functus officio*, but it did suggest that "an express, mutual agreement between the parties" would likely be sufficient. Therefore, a key practice point arising from *American International* is that if a tribunal is seated in New York, and if the parties want a truly *final* partial or interim award as to less than all the issues, but that is no longer subject to arbitral review, they should make that intention as explicit as possible.

Conclusion

The specific holdings of the two cases here are interesting in themselves, but we discussed them together to make a larger point: the local law governing where an arbitral tribunal sits, or where an award is sought to be enforced, can have important—even dispositive—consequences. In the *GE Energy* case, the question of whether a party could be required to arbitrate at all was determined by reference to state contract law—probably not what the original parties had in mind. In the *American International* case, New York adopted an approach to the finality of arbitral awards that could impact how and when they can be enforced, and it is not necessarily the approach that other jurisdictions would take.

It is therefore important for parties to arbitration agreements to understand not only the law they may have selected to govern their agreement, but the law of any other jurisdiction that could affect the arbitration—particularly the place where the tribunal sits. Sensitivity to these issues will help improve predictability and reduce the costs of enforcement.

Provenzano Granne & Bader LLP

July 2020

Partners

S. Christopher Provenzano (NY)
chris.provenzano@pgbfirm.com

Michael A. Granne (NY, PA)
michael.granne@pgbfirm.com

Jennifer Bader (NY)
jennifer.bader@pgbfirm.com