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<p>International arbitration is an integral element of the globalized modern economy. It is the principal method of resolving commercial disputes between States, individuals, and corporations in almost every aspect of international trade.</p> <p>Arbitration relies on the notion of party autonomy—that the parties to an agreement may freely choose the law applicable to their agreement and to the resolution of any dispute arising out of it. However, agreements have to be performed and arbitral awards rendered somewhere, and in the modern world in which the preeminent legal authority is the sovereign State, these actions necessarily occur under a legal framework and a public policy not shaped by the parties.</p> <p>When rules of public policy are implicated in the agreement underlying a dispute in arbitration—or in the award resulting from the arbitration proceedings, a State must navigate between the Scylla and Charybdis of lending its authority to the recognition of an agreement or enforcement of an award contrary to its fundamental principles or of appearing not to respect the principle of finality of arbitral awards underpinning the system of modern international commerce.</p> <p>What route should national courts—the “watchmen of public policy”—choose? Should party autonomy be cabined by respect for international public policy? Or should public policy be viewed as a safety valve utilized only in emergencies, where recognition and enforcement would be fundamentally at odds with a State's most cherished principles and values?</p> <p>This thesis details the provisions for refusal of recognition or enforcement of arbitral awards on the grounds of public policy that currently exist in major international conventions and model legislation as well as in the legislation of the United States and selected European Union Member States. The various ways in which public policy can be understood is explained, and the application of the public policy exceptions in the United States and selected European Union Member States are detailed. Finally, trends in the United States and the European Union with respect to public policy and arbitration are examined.</p>			
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**Chameleons, Unruly Horses, Golden Eagles, and Sea Dragons:  
The Menagerie of Public Policy Exceptions to Recognition and  
Enforcement of Arbitral Awards in the United States and Europe**

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## TABLE OF CONTENTS

SOURCES .....	vi
International Materials .....	vi
International Conventions & Treaties .....	vi
Model Legislation & Guidelines.....	vi
Arbitral Awards .....	vii
Constitutions, Legal Codes & Legislation .....	vii
European Union and Member States.....	vii
British Legislative Acts .....	vii
Dutch Legislative Acts .....	vii
European Union Legislative Acts .....	vii
French Legislative Acts .....	vii
United States .....	viii
United States Constitution .....	viii
United States Code .....	viii
United States Federal Rules and Regulations .....	viii
US State Statutory Provisions.....	viii
Cases Cited.....	ix
Court of Justice of the European Union .....	x
French Cases .....	x
Indian Cases.....	x
United Kingdom Cases .....	xi
United States of America Cases .....	xi
Supreme Court of the United States .....	xi
United States Courts of Appeals.....	xii
United States Federal District Courts .....	xiii
Supreme Court of California .....	xiv
Courts of Appeal of California .....	xiv
Scholarly Material.....	xiv
Treatises .....	xiv
Shorter Works in Collections .....	xv
Articles.....	xvi
Miscellaneous .....	xvii
1 INTRODUCTION .....	1
1.1 International Arbitration .....	2
1.2 Impetus for Research .....	3
1.3 Structure.....	4
2 SPECIFIC PUBLIC POLICY EXCEPTIONS .....	4
2.1 Public policy exception to enforcement of arbitral awards under the New York Convention.....	5
2.1.1 The New York Convention’s public policy exception to recognition and enforcement of arbitral awards .....	6
2.1.2 How the Article V(2)(b) challenge works .....	7
2.2 Public policy exception to enforcement of arbitral awards under the UNCITRAL Model Law .....	8
2.3 Public policy exception to enforcement of arbitral awards in legislation of the US and select EU Member States .....	8
2.3.1 Different enforcement regimes under national law for arbitral awards based on whether the award is subject to an international treaty .....	9
2.3.1.1 US provides different enforcement regimes for covered and non-covered awards under the FAA.....	9
2.3.1.1.1 Public policy exception to enforcement of domestic awards under the FAA .....	10
2.3.1.1.2 Public policy exception to enforcement of awards subject to the New York Convention under the FAA .....	12

2.3.1.2	The UK provides different enforcement regimes for covered and non-covered awards under the EAA .....	12
2.3.1.3	The Netherlands provides different enforcement regimes for covered and non-covered awards .....	12
2.3.2	Same enforcement regime under national law for foreign arbitral awards subject to and not subject to international treaties .....	13
2.3.2.1	France applies the same enforcement regime under the Nouveau code de procedure civile to foreign arbitral awards subject to and not subject to international treaties .....	13
2.4	Summary .....	15
<b>3</b>	<b>WHAT IS PUBLIC POLICY?</b> .....	<b>16</b>
3.1	What is public policy according to Article V(b)(2)? .....	17
3.1.1	Public policy under the New York Convention is the public policy of the enforcing State .....	18
3.1.2	Public policy under the New York Convention is international public policy .....	18
3.1.3	Public policy under the New York Convention is transnational public policy .....	19
3.1.4	What forms of public policy are relevant to international arbitrations? .....	20
3.2	What is public policy in the US? .....	22
3.2.1	Public policy .....	22
3.2.2	Arbitration and federalism in the US .....	23
3.3	What is public policy in Europe? .....	25
3.3.1	Public policy in the EU .....	25
3.3.2	Arbitration and federalism in the EU .....	26
3.3.3	Public Policy and arbitration in the EU .....	27
<b>4</b>	<b>PUBLIC POLICY EXCEPTIONS IN PRACTICE</b> .....	<b>28</b>
4.1	Limited public policy exceptions to enforcement of arbitral awards under the Federal Arbitration Act exist in the US .....	28
4.1.1	Public policy exceptions to domestic arbitral awards under the FAA in the US .....	29
4.1.2	Public policy exceptions to enforcement of international arbitral awards in the US under the FAA .....	30
4.1.2.1	US foreign policy does not express the US' "most basic notions of morality and justice" and cannot be considered US public policy .....	31
4.1.2.1.1	<i>Parsons &amp; Whittemore</i> firmly established that US foreign policy is not equivalent to US public policy .....	31
4.1.2.1.2	Even US antiterrorism policy does not rise to the level of US public policy .....	33
4.1.2.1.3	US trade embargoes and economic sanctions are not indicative of US public policy .....	33
4.1.2.2	International arbitration of claims under US federal law is usually permitted even where it would be disallowed as contrary to US public policy in domestic arbitration .....	34
4.1.2.2.1	Foreign arbitral awards may be considered judgments pursuant to US bankruptcy law .....	35
4.1.2.2.2	Agreements to arbitrate claims under the Jones Act will be enforced in US courts, but the enforcement of foreign awards resulting from the such arbitration may be refused if contrary to US public policy .....	36
4.1.2.2.3	International arbitration of claims under the Securities Exchange Act of 1934 is permissible .....	37
4.1.2.2.4	International arbitration of claims under the Sherman Act is permissible, even where domestic arbitration would be impermissible .....	38
4.1.2.3	US courts have refused to enforce foreign arbitral awards where foreign judgments or decrees invalidate the award or its underlying obligation .....	40
4.1.2.3.1	In <i>Sea Dragon</i> , the public policy exception was successfully invoked to prevent enforcement of an foreign	

	arbitral award where enforcement was contrary to the US public policy favoring international comity .....	40
	4.1.2.3.2 Attempts to extend the <i>Sea Dragon</i> decision to other policies have been less successful.....	41
	4.1.2.3.3 The doctrine of comity in <i>Sea Dragon</i> has not been widely adopted by other US courts .....	42
	4.1.2.3.4 Attempts to extend the <i>Sea Dragon</i> decision to other alleged violations of foreign law have not succeeded .....	42
	4.1.2.4 US courts have refused to enforce foreign arbitral awards where the underlying agreement was entered into under duress .....	43
	4.1.2.5 US courts typically enforce foreign arbitral awards where the award or underlying agreement is alleged to be the product of fraud .....	45
	4.1.3 US courts rarely refuse recognition or enforcement of foreign arbitral awards on public policy grounds .....	46
4.2	Limited public policy exceptions to enforcement of arbitral awards under the Arbitration Act of 1996 exist in the UK.....	46
	4.2.1 UK courts refuse enforcement of domestic arbitral awards resulting from an agreement illegal under English law .....	47
	4.2.2 Public policy challenges to the enforcement of foreign awards under the EAA .....	47
	4.2.2.1 UK courts will also refuse enforcement of foreign arbitral awards resulting from an agreement illegal under English law, but are less likely to do so when the agreement is permissible under English law but illegal under foreign law .....	47
	4.2.2.2 UK courts may refuse recognition or enforcement of a foreign arbitral award that is the product of fraud, but only where there has been reprehensible or unconscionable conduct .....	52
	4.2.2.3 UK courts will refuse enforcement of an award invalidated by a foreign judgment only where recognition would be impeachable for fraud, contrary to natural justice, or contrary to public policy .....	54
4.3	Application of French law regarding public policy exception to enforcement of awards.....	55
	4.3.1 France uniquely differentiates between public policy and international public policy, employing the latter in challenges to the recognition or enforcement of foreign awards .....	55
	4.3.2 Application of French law regarding public policy exception to enforcement of awards in domestic arbitration.....	56
	4.3.3 Application of French law regarding public policy exception to enforcement of awards in international arbitration .....	57
	4.3.3.1 Illegality of the underlying contract leads French court to refuse enforcement .....	57
	4.3.3.2 French courts will enforce an arbitral agreement or award invalidated by a foreign judgment or decree because France, uniquely, does not extend judicial comity to foreign judgment concerning arbitral awards .....	59
5	TRENDS IN THE US AND THE EU .....	60
	5.1 The permissive attitude toward arbitration of antitrust disputes in the US can be contrasted with the restricted possibility for disputes involving competition law to be decided in arbitration in the EU .....	60
	5.1.1 Permissive attitude to arbitration of antitrust disputes in the US.....	61
	5.1.2 Restricted ability to arbitrate disputes involving European competition law .....	63
	5.2 Whereas US state consumer law does not stand in the way of US federal policy favoring arbitration, EU consumer law does stand in the way of Member State rules compelling such arbitration .....	66
	5.2.1 US state public policy expressed in consumer protection laws prohibiting mandatory arbitration of consumer contracts is preempted by the federal policy favoring arbitration of contractual disputes .....	66
	5.2.1.1 Pre-empted California State approach .....	66
	5.2.1.2 Federal approach favoring efficient, streamlined resolution of disputes .....	68
	5.2.2 Mandatory arbitration provisions are “unfair terms” under EU consumer law and cannot be enforced even where Member State law holds otherwise .....	70

5.2.2.1	<i>Mostaza Claro</i> : EU consumer laws are a defense to enforcement of arbitral awards .....	72
5.2.2.2	In <i>Asturcom</i> , the CJEU held that the principle of equivalence may require Member States courts to determine ex officio whether arbitration clauses are contrary to EU consumer law.....	76
6	CONCLUSIONS.....	78

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## 1            INTRODUCTION

The legal concept of “public policy” defies easy explanation, or—to be more accurate—it can be defined in so many ways as to be seemingly neither a definitive concept nor a particularly “legal” one. Public policy expresses “the social, moral, and economic values” of society.<sup>1</sup> Its objective is “the common good.”<sup>2</sup> It prohibits acts “injurious to the public, or against the public good.”<sup>3</sup>

But while public policy involves morality, it is not *only* morality.<sup>4</sup> It is often vague,<sup>5</sup> it is “variable,”<sup>6</sup> and its meaning stretches<sup>7</sup> and changes depending on the circumstances<sup>8</sup> and surroundings, like the skin of a “chameleon.”<sup>9</sup> It was perhaps most famously described almost two hundred years ago by Judge Burrough as “a very unruly horse, and when once you get astride it you never know where it will carry you. It may lead you from sound law. It is never argued at all, but when other points fail.”<sup>10</sup>

Public policy is, above all, a product of the courts: “a judicial construct prohibiting courts from enforcing illegal contracts or contracts that, while not illegal per se, are against public interests.”<sup>11</sup>

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1. Sulbha Rai, *How Do or Should Arbitrators Deal with Domestic Public Policy or Regulatory Issues. Does It Affect Arbitrability?*, Jindal Global Law Sch. Working Papers Series (2008), available at <http://ssrn.com/abstract=1433799>; cf. Luca G. Radicati di Brozolo, *Court Review of Competition Law Awards in Setting Aside and Enforcement Proceedings*, in EU AND US ANTITRUST ARBITRATION 758 (Gordon Blanke & Phillip Landolt eds., 2011) (“Although there are many definitions of this concept, public policy can be, broadly speaking, defined as the basic values and principles of a given domestic system.”).

2. Richard H.W. Maloy, *Public Policy – Who Should Make It in America’s Oligarchy?*, 1998 DET. C.L. REV. 1143, 1154 (1998).

3. *Egerton v. Brownlow*, [1853] 10 Eng. Rep. 359 (Q.B.) 437; 4 H.L.C. 1 (H.L.) 196 (Eng.).

4. See *Jones v. Randall*, [1774] 98 Eng. Rep. 954 (K.B.) 955; 1 Cowper 37, 39 (Mansfield, L.) (Eng.) (“Many contracts which are not against morality are still void as being against the maxims of sound policy.”).

5. See FRANÇOIS KNOEPFLER ET AL., *DROIT INTERNATIONAL PRIVÉ SUISSE* 457 n.776f (3d ed. 2004).

6. *Hartford Fire Ins. Co. v. Chicago, M. & St. P. Ry.*, 175 U.S. 91, 106 (1899) (“Public policy is variable; the very reverse of that which is the policy of the public at one time may become public policy at another; hence no fixed rule can be given by which to determine what is public policy.”).

7. GARY B. BORN, *INTERNATIONAL ARBITRATION AND FORUM SELECTION AGREEMENTS: DRAFTING AND ENFORCING* 137 (3d ed. 2010) (“[C]reative counsel can often construct public policy . . . arguments, which can delay enforcement efforts. . . . The elasticity of ‘public policies’ in most states heightens [the] uncertainty [this creates].”).

8. *Funk v. United States*, 290 U.S. 371, 381 (1933) (“The public policy of one generation may not, under changed conditions, be the public policy of another.”).

9. Bernard Dutoit, *L’ordre public: caméléon du droit international privé?*, in GUY FLATTET, *MÉLANGES* 455 (1985).

10. *Richardson v. Mellish*, [1824] 130 Eng. Rep. 294 (Ct. Com. Pl.) 303; 2 Bing. 229, 252 (Burrough, J.) (Eng.); but see *Enderby Town Football Club Ltd. v. The Football Association Ltd.*, [1971] Ch. 591, 606–67 (“[W]ith a good man in the saddle, the unruly horse can be kept in control. It can jump over obstacles. It can leap the fences put up by fictions and come down on the side of justice.”).

11. Jonathan A. Marcantel, *The Crumbled Difference Between Legal and Illegal Arbitration Awards: Hall Street Associates and the Waning Public Policy Exception*, 14 *FORDHAM J. CORP. & FIN. L.* 597, 598 (2008–2009).

## 1.1 International Arbitration

International arbitration is an integral element of the modern globalized economy. It is “the principal method of resolving disputes between States,<sup>12</sup> individuals, and corporations in almost every aspect of international trade, commerce, and investment.”<sup>13</sup> Predictability of outcomes and reduction of uncertainty are essential to commerce and investment.<sup>14</sup> Commercial buyers and sellers utilize the standardized guidelines and rules of procedure of private arbitral institutions to resolve contractual disputes.<sup>15</sup> Recourse to investment arbitration allows private parties to invest with confidence in developing nations by ensuring that any disputes will be decided in a neutral forum.<sup>16</sup>

Rooted in the notion of party autonomy, arbitration allows contracting parties to resolve disputes with little or no State intervention.<sup>17</sup> The disputing parties can utilize arbitration to bypass national substantive and procedural laws.<sup>18</sup> In most international arbitrations, neither the arbitral proceeding nor its outcome is subject to review in State court.<sup>19</sup> International arbitral awards are enforceable in “virtually all developed nations of the world.”<sup>20</sup>

International commercial arbitration “depends for its effectiveness on a reliable scheme for enforcement in one country of awards made in another, and that is only feasible if the grounds for refusal of enforcement of foreign awards are limited (and so reasonably predictable), and are applied by most, and preferably all, trading countries.”<sup>21</sup> Most

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12. This article concerns several varieties of “states”. The term “states” with a lowercase “s” is used to refer to the fifty states of the United States of America. The term “State” with uppercase “S” is used to designate nations/countries. Finally, the States comprising the EU are referred to as “Member States.”

13. NIGEL BLACKABY, CONSTANTINE PARTASIDES, ALAN REDFERN & J. MARTIN HUNTER, REDFERN AND HUNTER ON INTERNATIONAL ARBITRATION 1 (2009) [hereinafter REDFERN & HUNTER]; *see, e.g.*, YVES DEZALAY & BRYANT G. GARTH, DEALING IN VIRTUE 311 (1996).

14. GARY B. BORN, INTERNATIONAL COMMERCIAL ARBITRATION: CASES AND MATERIALS 1 (2011) [hereinafter BORN 2011] (“The international legal regimes for international commercial and investment arbitrations have been established, and progressively refined, with the express goal of facilitating international trade and investment by providing a stable, predictable, and effective legal framework in which these commercial activities may be conducted.”).

15. REDFERN & HUNTER, *supra* note 13, at 1–2.

16. *Id.* at 15–16

17. *See, e.g.*, JULIAN M. LEW ET AL., COMPARATIVE INTERNATIONAL COMMERCIAL ARBITRATION [hereinafter LEW, MISTELIS & KRÖLL] 5 (2003); REDFERN & HUNTER, *supra* note 13, at 2.

18. *See, e.g.*, MICHAEL MCILWRATH & JOHN SAVAGE, INTERNATIONAL ARBITRATION AND MEDIATION 8 (2010); LEW, MISTELIS & KRÖLL, *supra* note 17, at 5–9.

19. LEW, MISTELIS & KRÖLL, *supra* note 17, at 7.

20. Philip J. McConaughay, *The Risks and Virtues of Lawlessness: A “Second Look” at International Commercial Arbitration*, 93 NW. U. L. REV. 453, 453 (1999).

21. JEAN-LOUIS DELVOLVÉ ET AL., FRENCH ARBITRATION LAW AND PRACTICE: A DYNAMIC CIVIL LAW APPROACH TO INTERNATIONAL ARBITRATION 211 (2d ed. 2009).

international arbitral awards are complied with voluntarily.<sup>22</sup> For the purposes of this thesis, arbitration is understood as a mechanism for dispute settlement that is not compulsory under domestic law, is based on an agreement between the parties to the dispute, in which at least one of the parties is a business undertaking or natural person, and the outcome of which, in principle, has the same force as a final and binding judgment.<sup>23</sup> This thesis is primarily concerned with commercial arbitration.

## 1.2 Impetus for Research

Public policy is relevant to arbitration law. Arbitration relies on the notion of party autonomy—that the parties to an agreement may freely choose the law applicable to their agreement and to the resolution of any dispute arising out of it. However, agreements have to be performed and arbitral awards rendered *somewhere*, and in the modern world in which the preeminent legal authority is the sovereign State, these actions necessarily occur under a legal framework and a public policy not shaped by the parties.<sup>24</sup> Parties may agree to what they like but law has never guaranteed without exception to enforce their contracts.<sup>25</sup> Public policy “by definition goes beyond the will of the parties and cannot be waived by their mere agreement.”<sup>26</sup> It can be misused to delay, prolong, or make unduly expensive the resolution of disputes to the unfair advantage of one party.<sup>27</sup>

When rules of public policy are implicated in the agreement underlying a dispute in arbitration—or in the award resulting from the for arbitration proceedings, a State must navigate between the Scylla and Charybdis of lending its authority to the recognition of an agreement or enforcement of an award contrary to its fundamental principles or of

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22. GARY B. BORN, *INTERNATIONAL ARBITRATION: LAW AND PRACTICE* 369 (2012)

23. CHRISTOPH LIEBSCHER, *THE HEALTHY AWARD: CHALLENGE IN INTERNATIONAL COMMERCIAL ARBITRATION* 4 (2003).

24. See Rainer Arnold & Elisabeth Meindl, *The EU Charter of Fundamental Rights and Public Policy in International Arbitration Law*, 2011 CZECH (& CENT. EUR.) Y.B. ARB. 87, 88. See also Charles H. Brower II, *Arbitration and Antitrust: Navigating the Contours of Mandatory Law*, 59 BUFF. L. REV. 1127, 1128 (2011) (“[I]nternational commercial arbitration holds itself out as a system founded on party autonomy, but increasingly unfolds in a setting where tribunals apply public regulatory laws without regard to the law selected by the disputing parties.”).

25. See, e.g., Institutes of Justinian, lib. 3, tit. 19, par. 24 (“*Quod turpi ex causa promissum est, veluti si quis homicidium vel sacrilegium se facturum promittat, non valet* [A promise made to effect a base purpose, as to commit homicide or sacrilege, is not binding]”), translated in THOMAS COLLETT SANDARS, *THE INSTITUTES OF JUSTINIAN, WITH ENGLISH INTRODUCTION, TRANSLATION, AND NOTES* 353 (7th ed. 1917); REDFERN & HUNTER, *supra* note 13, at 655–56 (recognition and enforcement of null and void contracts is internationally refused).

26. Jacob Grierson, *Court Review of Awards on Public Policy Grounds: A Recent Decision of the English Commercial Court Throws Light on the Position Under the English Arbitration Act 1996*, 24 MEALY’S INT’L ARB. REP. 1, 4 (2009).

27. The threat of Touchstone, the court jester, comes to mind: “I will bandy with thee in faction; will o’er-run thee with policy.” WILLIAM SHAKESPEARE, *AS YOU LIKE IT* act 5, sc. 1.

appearing not to respect the principle of finality of arbitral awards underpinning the system of modern international commerce.<sup>28</sup>

What route should national courts—the “watchmen of public policy”<sup>29</sup>—choose? Is it “justifiable and desirable,” as one commentator stated, that “the principle of the absence of a control . . . diminish behind the absolute necessity of the respect of international public policy?”<sup>30</sup> Or should public policy be viewed as a “safety valve” utilized only in emergencies, where recognition and enforcement would be fundamentally at odds with a State’s most cherished principles and values?<sup>31</sup>

### **1.3 Structure**

This thesis is organized in Parts (e.g., Part *n*) sections (e.g., section *n.n*), subsections (e.g., subsection *n.n.n*), paragraphs (e.g., paragraph *n.n.n.n*), and subparagraphs (e.g., subparagraph *n.n.n.n.n*). The structure of this thesis is explained below

Part 2 details the provisions for refusal of recognition or enforcement of arbitral awards on the grounds of public policy that currently exist in major international conventions and model legislation as well as in the legislation of the United States (“US”) and selected European Union (“EU”) Member States.<sup>32</sup> The various ways in which public policy can be understood are explored in Part 3. The application of the public policy exception in the US and selected EU Member States are detailed in Part 4. In Part 5, trends in the US and the EU with respect to public policy and arbitration are examined. Part 6 concludes the thesis.

## **2 SPECIFIC PUBLIC POLICY EXCEPTIONS**

Part 2 details the relevant international conventions and national legislation governing public policy exceptions to enforcement of arbitral awards. First, in section 2.1,

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28. Rai, *supra* note 1, at 5.

29. Bernard Hanotiau & Olivier Caprasse, *Arbitrability, Due Process, and Public Policy Under Article V of the New York Convention*, 25 J. INT’L ARB. 721, 737 (2008).

30. Hanotiau & Caprasse, *supra* note 29, at 738 (internal quotes omitted).

31. Brozolo, *supra* note 1, at 758.

32. *See, e.g.*, Convention on the Recognition and Enforcement of Foreign Arbitral Awards art. V(2)(b), June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38 [hereinafter New York Convention]; Inter-American Convention on International Commercial Arbitration art. 5(2)(b), *opened for signature* Jan. 30, 1975, OAS SER A20 (SEPEF), 14 I.L.M. 336 (1975) [hereinafter Panama Convention]; Convention on the Judicial Cooperation between States of the Arab League art. 37, Apr. 8 1983, *available at* <http://www.unhcr.org/refworld/docid/3ae6b38d8.html> (last accessed Apr. 9, 2013); *but see* Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Mar. 18, 1965, 575 U.N.T.S. 159 (silent on issue of public policy).

the exception found in the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “New York Convention”) is detailed.<sup>33</sup> Second, in section 2.2, the framework for national laws regarding recognition and enforcement of arbitral awards provided by the UNCITRAL Model Law on International Commercial Arbitration (the “UNCITRAL Model Law”) is explained.<sup>34</sup> In section 2.3, the implementation of these international conventions and the UNCITRAL Model Law with respect to public policy exceptions in the actual national legislation of the US and selected EU Member States is explored in detail. Finally, in section 2.4, the aforementioned public policy exception provisions are summarized.

## **2.1 Public policy exception to enforcement of arbitral awards under the New York Convention**

The New York Convention was signed in 1958 and has since been acceded to by nearly 150 States.<sup>35</sup> It is the “cornerstone of current international commercial arbitration”<sup>36</sup> and the “backbone of [its] acceptance . . . by the business world.”<sup>37</sup> The New York Convention concerns the recognition and enforcement of foreign arbitral awards—“arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought”<sup>38</sup>—and non-domestic arbitral awards—“arbitral awards not considered as domestic awards in the State where their recognition and

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33. See New York Convention, *supra* note 32. The New York Convention has entered into force in 148 States worldwide, including all twenty-seven EU Member States, the soon-to-be Member State, Croatia; and all five current candidate States; Iceland, Former Yugoslav Republic of Macedonia, Montenegro, Serbia, and Turkey. A regularly updated list is available at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/NYConvention\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html).

34. United Nations Commission on International Trade Law Model Law on International Commercial Arbitration, G.A. Res. 40/72, 40 U.N. G.A.O.R. Supp. (No. 17), U.N. Doc. A/40/17 (June 21, 1985), *revised in 2006*, G.A. Res. 61/33, U.N. Doc. A/61/33 (Dec. 4, 2006), *available at* [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/1985Model\\_arbitration.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html) [hereinafter UNCITRAL Model Law]. The UNCITRAL Model Law forms the basis of arbitration laws (as of April 2013) in several states in the US; the following EU Member States: Austria, Bulgaria, Cyprus, Denmark, Estonia, Germany, Greece, Hungary, Ireland, Lithuania, Malta, Poland, Slovenia, Spain, and the United Kingdom of Great Britain and Northern Ireland; the soon-to-be EU Member State Croatia; and the following EU Member State candidates: Former Yugoslav Republic of Macedonia, Serbia, and Turkey. A regularly updated list is available at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/1985Model\\_arbitration\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration_status.html).

35. New York Convention, *supra* note 32.

36. BORN 2011, *supra* note 14, at 33.

37. LEW, MISTELIS & KRÖLL, *supra* note 17, at v.

38. New York Convention, *supra* note 32, art. I(1).

enforcement are sought.”<sup>39</sup> Arbitral awards covered by the New York Convention may be the product of either ad hoc or institutional arbitration proceedings.<sup>40</sup>

States party to the New York Convention (“Contracting States”) must recognize agreements in writing entered into by the parties that provide for arbitration of all disputes between the parties “capable of settlement by arbitration.”<sup>41</sup> The courts of Contracting States, when seized of an action wherein the parties have such an agreement, must refer the dispute to arbitration.<sup>42</sup> Contracting States must also “recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon.”<sup>43</sup> Contracting States may not impose “substantially more onerous conditions or higher fees or charges” on recognition or enforcement of awards under the New York Convention than are imposed on recognition or enforcement of domestic arbitral awards.<sup>44</sup>

Many Contracting States, including the US and the Member States of the EU primarily considered in this thesis—France, the Netherlands, and the United Kingdom of Great Britain and Northern Ireland (the “UK”)—have made a special reservation to the New York Convention stipulating that they will only apply the Convention to the recognition and enforcement of award made in the territory of another Contracting State.<sup>45</sup> If arbitration takes place in a State that is not a party to the New York Convention, the resulting award cannot be enforced in a Contracting State under the reservation.

### **2.1.1 The New York Convention’s public policy exception to recognition and enforcement of arbitral awards**

Arbitral awards under the New York Convention are generally challenged on three grounds: jurisdictional, procedural, and substantive.<sup>46</sup> Jurisdictional challenges call the existence of a valid and binding arbitration clause into question.<sup>47</sup> Procedural challenges on

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39. *Id.*

40. *See id.* art. I(2) (“The term ‘arbitral awards’ shall include not only awards made by arbitrators appointed for each case but also those made by permanent arbitral bodies to which the parties have submitted.”).

41. *Id.* art. II(1) An “agreement in writing” consists of an arbitral clause in a contract or an arbitration agreement that is either “signed by the parties” or “contained in an exchange of letters or telegrams.” *Id.* art. II(2).

42. *Id.* art. II(3).

43. *Id.* art. III.

44. *Id.*

45. A list of reservations to the New York Convention is available at [http://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg\\_no=XXII-1&chapter=22&lang=en#15](http://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg_no=XXII-1&chapter=22&lang=en#15).

46. REDFERN & HUNTER, *supra* note 13, at 594–95.

47. *See* New York Convention, *supra* note 32, art. V(1)(a), (c) (dispute not within scope of agreement).



focus on problems in the mechanics of arbitration: appointment of arbitrators, giving proper notice, and so forth.<sup>48</sup> Substantive challenges to arbitral awards allege that the deciding tribunal made a mistake of law or fact when rendering its decision or that the award is contrary to public policy.<sup>49</sup> The latter situation is the subject of this thesis.

Specifically, Article V(2)(b) of the New York Convention provides that an arbitral award may be refused recognition and enforcement if the competent authority in the country where recognition and enforcement are sought finds that “recognition and enforcement would be contrary to the public policy of that country.”<sup>50</sup>

### **2.1.2 How the Article V(2)(b) challenge works**

When the party against whom an award has been rendered (the “award-debtor”) seeks to challenge an award on substantive grounds, it has two procedural paths. First, it may seek to have the award “set aside” or “annulled” by the competent authority of the State in which the award was rendered.<sup>51</sup> An award that has been set aside in the State in which it was rendered may then be refused recognition and enforcement by other States party to the New York Convention.<sup>52</sup> Refusing recognition and enforcement is permissible, but not obligatory. Notwithstanding that caveat, when an award is set aside by the competent authority of the State in which it was rendered, the efforts of parties seeking to enforce it will be stymied. Thus, on the basis of the public policy of the rendering State, parties may be able to thwart enforcement proceedings in States with different (and less strict) public policy standards.

However, where an award cannot be challenged on the basis of the public policy of the rendering State, its enforcement may still be inhibited in other States if it can be successfully challenged on the basis of the public policy of the enforcing State. This is a sensible for the award-debtor, because, as Delvolvé notes, “the grounds for refusal of

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48. *See id.* art. V(1)(b), (d) (composition of tribunal or arbitral procedure not in accordance with agreement).

49. REDFERN & HUNTER, *supra* note 13, at 596.

50. *See* New York Convention, *supra* note 32, art. V(2)(b). “Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that ... [t]he recognition or enforcement of the award would be contrary to the public policy of that country.”

51. UNCITRAL Model Law, *supra* note 34, art. 6 (“Each State enacting this model law specifies the court, courts or, where referred to therein, other authority competent to perform these function.”).

52. *See* New York Convention, *supra* note 32, art. V(1)(e); *see also* REDFERN & HUNTER, *supra* note 13, at 618 (noting that an award that has been set aside “will usually be unenforceable elsewhere”).

enforcement may be wide in one country and narrow in another.”<sup>53</sup> Consider, for example, an award rendered in State A concerning a State B company having the majority of its assets located in State C. The party in whose favor the award was rendered (the “award-creditor”) would naturally be most concerned with securing enforcement in State C so it can receive payment from the assets located therein. If the award-debtor convinces the competent authority in State A to set aside the award, it would then be able to deflect enforcement proceedings in State C on New York Convention V(1)(e) grounds.<sup>54</sup> Where the award-debtor fails to convince the competent authority in State A to set aside the award, it could still avoid enforcement in State C if recognition or enforcement of the award would be contrary to the public policy of State C.

## **2.2 Public policy exception to enforcement of arbitral awards under the UNCITRAL Model Law**

Article 36 of the UNCITRAL Model Law provides that a foreign arbitral award may be denied confirmation or recognition on statutory grounds virtually identical to those of Article V of the New York Convention.<sup>55</sup> Article 36(1)(b)(ii) provides that recognition or enforcement of an arbitral award may be refused . . . “if the court finds that . . . the recognition or enforcement of the award would be contrary to the public policy of [that] State.”<sup>56</sup>

Because the UNCITRAL Model Law is a recommended blueprint for actually binding legislation—i.e., an instrument of soft rather than hard law, no further discussion of its provisions is necessary at this point. The following section will compare provisions of actual national legislation with those suggested in the UNCITRAL Model Law.

## **2.3 Public policy exception to enforcement of arbitral awards in legislation of the US and select EU Member States**

National legislation regarding the enforcement of arbitral awards departs from that suggested by the UNCITRAL Model Law. Two main trends can be distinguished: (1) different enforcement regimes for foreign awards subject to international treaties (“covered awards”) than for those not subject (“non-covered awards”); (2) basically the same

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53. DELVOLVÉ ET AL., *supra* note 21, at 210; *see also id.*, at 210–11 (“In such situations, the same award would thus be enforceable in one country, but not in another.”).

54. *See* New York Convention, *supra* note 32, art. V(1)(e).

55. UNCITRAL Model Law, *supra* note 34, art. 36.

56. *Id.* art. 36(1)(b)(ii).

enforcement regimes applicable to all foreign awards. The US, the Netherlands, and the UK exemplify the first trend, whereas France exemplifies the second.

### **2.3.1 Different enforcement regimes under national law for arbitral awards based on whether the award is subject to an international treaty**

The major proponent of providing a different enforcement regime under national law to covered awards than that applicable to non-covered awards is the US. The legal systems of the UK and the Netherlands make a similar distinction.

#### **2.3.1.1 *US provides different enforcement regimes for covered and non-covered awards under the FAA***

In the US, different enforcement regimes apply to non-domestic arbitral awards subject to the New York Convention or the Inter-American Convention on International Commercial Arbitration (“Panama Convention”) (i.e., covered awards) than to domestic awards (i.e., non-covered awards).<sup>57</sup> Both regimes, however, are defined by US federal law. The US Congress enacted the first federal legislation concerning arbitration in 1925, the United States Arbitration Act.<sup>58</sup> The legislation was renamed the Federal Arbitration Act (“FAA”) in 1947.<sup>59</sup> Prior to the New York Convention’s entry into force in the US, the FAA was amended to ensure the Convention’s enforcement.<sup>60</sup> It was similarly modified later to include awards under the Panama Convention.<sup>61</sup> Thus, the FAA governs the enforcement of all arbitral awards in the US,<sup>62</sup> but provides differing regimes for domestic awards, awards subject to the New York Convention, and awards subject to the Panama Convention.

By providing a remedy in the federal courts, the FAA places agreements to arbitrate “upon the same footing as other contracts”<sup>63</sup> and ensures their judicial enforcement.<sup>64</sup> The FAA provides that agreements in writing to arbitrate are “valid, irrevocable, and

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57. Richard C. Levin & C. Jeffrey Price, *US Enforcement Issues and US Antitrust Law*, in EU AND US ANTITRUST ARBITRATION 1450 (Gordon Blanke & Phillip Landolt eds., 2011).

58. United States Arbitration Act, ch. 213, 43 Stat. 883 (1925) (codified as amended at 9 U.S.C. §§ 1–16, 201–208, 301–307 (2012)).

59. Federal Arbitration Act, ch. 392, § 1, 61 Stat. 669 (1947) (codified as amended at 9 U.S.C. §§ 1–16, 201–208, 301–307 (2012)).

60. Act of July 31, 1970, Pub. L. No. 91-368, § 3, 84 Stat. 693 (codified as amended at 9 U.S.C. §§ 1–16, 201–208, 301–307 (2012)).

61. Act of Aug. 15, 1990, Pub. L. No. 101-369, § 2, 104 Stat. 450 (codified as amended at 9 U.S.C. §§ 1–16, 201–208, 301–307 (2012)).

62. *See* FAA, 9 U.S.C. § 1 (2012) (The FAA covers all “maritime transactions [and] transactions involving commerce.”).

63. H.R. REP. NO. 96, at 1 (1924).

64. *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 219–20 (1985).

enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”<sup>65</sup> It evidences a “liberal federal policy favoring arbitration”<sup>66</sup> and the “fundamental principle that arbitration is a matter of contract.”<sup>67</sup> The FAA requires federal courts to treat arbitration agreements as equal to other contracts<sup>68</sup> and to “enforce them according to their terms.”<sup>69</sup>

Where an arbitration agreement exists, federal courts are empowered to stay court proceedings until “such arbitration has been had.”<sup>70</sup> Parties to court proceeding may petition federal district courts for “an order directing that such arbitration proceed.”<sup>71</sup> The courts are directed to hear the parties and, upon determining the existence of an arbitration agreement, to issue “an order directing the parties to proceed to arbitration in accordance with the terms of the agreement.”<sup>72</sup>

Federal courts may apply the New York Convention to all “non-domestic” awards. This includes both awards issued abroad and those issued in the US but made pursuant to the legal framework of another country. An award made pursuant to foreign law or involving parties that are domiciled or have their principal place of business outside of the US qualifies as non-domestic for purposes of the New York Convention.<sup>73</sup>

#### 2.3.1.1.1 Public policy exception to enforcement of domestic awards under the FAA

The FAA provides no basis for vacating or refusing to recognize or enforce a domestic award on grounds that it is contrary to public policy.<sup>74</sup> Generally, federal courts

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65. 9 U.S.C. § 2 (2012).

66. *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983).

67. *Rent-A-Center, West, Inc. v. Jackson*, 130 S.Ct. 2772, 2776 (2010).

68. *AT&T Mobility LLC v. Concepcion*, 131 S.Ct. 1740, 1745 (2011) (citing *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 443 (2006)).

69. *Volt Information Sciences, Inc. v. Board of Trustees*, 489 U.S. 468, 478 (1989).

70. 9 U.S.C. § 3 (2012).

71. *Id.* § 4.

72. *Id.*

73. *See Levin & Price, supra note 57*, at 1451–52; *see also Bergesen v. Joseph Muller Corp.*, 710 F.2d 928, 931 (2d Cir. 1983). This distinction is not unlike that made in French law, as discussed below.

74. The vast majority of US state arbitration laws also omit any explicit reference to public policy. *See* ALA. CODE § 6-6-14 (West 2013); ALASKA STAT. ANN. § 09.43.500 (West 2013); ARIZ. REV. STAT. § 12-1512 (West 2013); ARK. CODE ANN. § 16-108-223 (West 2011); CAL. CIV. CODE § 1268.4 (West 2013); COLO. REV. STAT. ANN. § 13-22-223 (West 2012); DEL. CODE ANN. tit. 10, § 5714 (West 2009); D.C. CODE § 16-4423 (West 2013); FLA. STAT. ANN. § 682.13 (West 2013); GA. CODE ANN. § 9-9-13 (West 2013); HAW. REV. STAT. § 658A-23 (West 2013); IDAHO CODE ANN. § 7-912 (West 2013); ILL. COMP. STAT. ANN. ch. 710 § 5/12 (West 2013); IND. CODE ANN. § 34-57-2-13 (West 2013); IOWA CODE ANN. § 679A.12 (West 2012); KAN. STAT. ANN. § 5-412 (West 2013); KY. REV. STAT. ANN. § 417.160 (West 2013); LA. REV. STAT. ANN. § 9:4210 (West 2013); ME. REV. STAT. tit. 14, § 5938 (West 2013); MD. CODE ANN., CTS. & JUD. PROC. § 3-224 (West 2013); MASS. GEN. LAWS ANN. ch. 251, § 12 (West 2013); MICH. COMP. LAWS ANN. § 600.5081 (West 2013); MINN. STAT. ANN. § 572B.23 (West 2013); MISS. CODE ANN. § 11-15-23 (West 2013); MO. ANN. STAT. § 435.405 (West 2013); MONT. CODE ANN. § 27-5-312 (West 2013); NEB. REV.

may vacate or modify a domestic award only upon the grounds specified in the FAA.<sup>75</sup> It is “well-established,” however that a public policy exception does exist.<sup>76</sup> That exception, however, is “extremely narrow.”<sup>77</sup> To form the basis for vacating a domestic award, a public policy must be “explicit,” “well-defined and dominant.”<sup>78</sup> “[G]eneral considerations of . . . public interests” cannot alone give rise to public policies.<sup>79</sup> Instead, public policies must be expressly articulated in “laws and legal precedents.”<sup>80</sup> Moreover, the party seeking to vacate or prevent the recognition or enforcement of a domestic award must show that

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STAT. § 25-2613 (West 2013); NEV. REV. STAT. ANN. § 38.241 (West 2013); N.H. REV. STAT. ANN. § 542:8 (West 2013); N.J. STAT. ANN. § 2A:24-8 (West 2013); N.M. STAT. ANN. § 44-7A-24 (West 2013); N.Y. C.P.L.R. 7511 (McKinney 1998 & Supp. 2013); N.C. GEN. STAT. ANN. § 50-54 (West 2013); N.D. CENT. CODE ANN. § 32-29.3-23 (West 2013); OHIO REV. CODE ANN. § 2711.10 (West 2013); OKLA. STAT. ANN. tit. 12, § 1874 (West 2013); OR. REV. STAT. ANN. § 36.705 (West 2013); PA. CONS. STAT. ANN. tit. 42, § 7314 (West 2013); R.I. GEN. LAWS ANN. § 10-3-12 (West 2013); S.C. CODE ANN. § 15-48-130 (West 2013); S.D. CODIFIED LAWS § 21-25A-24 (West 2013); TENN. CODE ANN. § 29-5-313 (West 2013); TEX. CIV. PRAC. & REM. CODE ANN. § 171.088 (West 2013); UTAH CODE ANN. § 78B-11-124 (West 2013); VT. STAT. ANN. tit. 12, § 5677 (West 2013); VA. CODE ANN. § 8.01-581.010 (West 2013); WASH. REV. CODE ANN. § 7.04A.230 (West 2013); W. VA. CODE ANN. § 55-10-4 (West 2013); WIS. STAT. ANN. § 788.10 (West 2013); WYO. STAT. ANN. § 1-36-114 (West 2013). *But see* CONN. GEN. STAT. ANN. § 50a-136 (West 2013) (allowing refusal of recognition or enforcement where “[t]he recognition or enforcement of the award would be contrary to the public policy of this state”).

75. *See, e.g.*, *Diapulse Corp. of Am. v. Carba, Ltd.*, 626 F.2d 1108, 1110 (2d Cir. 1980); *I/S Stavborg v. Nat’l Metal Converters, Inc.*, 500 F.2d 424, 429–30 (2d Cir. 1974); *Office of Supply v. New York Nav. Co., Inc.*, 469 F.2d 377, 379 (2d Cir. 1972).

76. *See* GARY B. BORN, *INTERNATIONAL COMMERCIAL ARBITRATION* 2625 (2009) [hereinafter BORN 2009] (*citing* *United Paperworkers Int’l Union v. Misco, Inc.*, 484 U.S. 29, 41 (1987); *W.R. Grace & Co. v. Local Union 759*, 461 U.S. 757, 766 (1983); *Hurd v. Hodge*, 334 U.S. 24, 34–35 (1948)). The public policy exception is inferred from 9 U.S.C. § 2 (2012) (making arbitral agreements enforceable and irrevocable except “upon such grounds as exist at law or in equity for the revocation of any contract”). The arbitration laws of many US states expressly stipulate that similar exception does *not* exist under state law. *See* ARIZ. REV. STAT. § 12-1512(A)(5) (“[T]he fact that the relief was such that it could not or would not be granted by a court of law or equity is not ground for vacating or refusing to confirm the award.”); COLO. REV. STAT. ANN. § 13-22-223(1.5) (same); DEL. CODE ANN. tit. 10, § 5714(a)(5) (same); FLA. STAT. ANN. § 682.13(1)(e) (same); GA. CODE ANN. § 9-9-13(d) (same); IDAHO CODE ANN. § 7-912(a)(5) (same); ILL. COMP. STAT. ANN. ch. 710 § 5/12(a)(5) (same); IND. CODE ANN. § 34-57-2-13(a)(5) (same); IOWA CODE ANN. § 679A.12(2) (same); KAN. STAT. ANN. § 5-412(a)(5) (same); KY. REV. STAT. ANN. § 417.160(1)(e) (same); ME. REV. STAT. tit. 14, § 5938(1)(F) (same); MD. CODE ANN., CTS. & JUD. PROC. § 3-224(c) (same); MASS. GEN. LAWS ANN. ch. 251, § 12(a)(5) (same); MICH. COMP. LAWS ANN. § 600.5081(3) (same); MO. ANN. STAT. § 435.405(1)(5) (same); MONT. CODE ANN. § 27-5-312(2) (same); NEB. REV. STAT. § 25-2613(a)(6) (same); N.C. GEN. STAT. ANN. § 50-54(a)(5) (same); PA. CONS. STAT. ANN. tit. 42, § 7314(a)(2) (same); S.C. CODE ANN. § 15-48-130(a)(5) (same); S.D. CODIFIED LAWS § 21-25A-24(6) (same); TENN. CODE ANN. § 29-5-313(a)(2) (same); VT. STAT. ANN. tit. 12, § 5677(b) (same); VA. CODE ANN. § 8.01-581.010 (same); WYO. STAT. ANN. § 1-36-114(a)(5) (same). *But see* W. VA. CODE ANN. § 55-10-4 (“[T]his section shall not be construed to take away the power of courts of equity over awards.”).

77. *See* BORN 2009, *supra* note 76, at 2625. The public policy exception does not “sanction a broad judicial power to set aside arbitration awards as against public policy.” *United Paperworkers*, 484 U.S. at 43; *W.R. Grace*, 461 U.S. at 766.

78. *W.R. Grace*, 461 U.S. at 766.

79. *Id.*

80. *Id.*

recognition or enforcement would clearly violate that explicit, well-defined and dominant policy<sup>81</sup> and produce a result that the parties could not have lawfully agreed upon.<sup>82</sup>

#### 2.3.1.1.2 Public policy exception to enforcement of awards subject to the New York Convention under the FAA

The second chapter of the FAA provides for the direct enforcement of the New York Convention in federal courts.<sup>83</sup> Application of the Article V(2)(b) public policy exception by federal courts is discussed at length in section 4.1.<sup>84</sup>

#### 2.3.1.2 ***The UK provides different enforcement regimes for covered and non-covered awards under the EAA***

The United Kingdom's Arbitration Act of 1996 ("EAA") provides separate regimes for domestic awards (i.e., non-covered awards) and awards under the New York Convention (i.e., covered awards). Section 66 of the EAA provides that non-covered awards may "be enforced in the same manner as a judgment or order of the court to the same effect."<sup>85</sup> Recognition or enforcement of covered awards may be refused if "it would be contrary to public policy to recognise or enforce the award."<sup>86</sup>

#### 2.3.1.3 ***The Netherlands provides different enforcement regimes for covered and non-covered awards***

The Dutch Code of Civil Procedure provides separate regimes for domestic awards (i.e., domestic non-covered awards), foreign awards subject to international treaties concerning recognition and enforcement (i.e., covered awards), and foreign awards not subject to such treaties (i.e., foreign non-covered awards).

For non-covered awards rendered within the Netherlands, Article 1063 provides that enforcement may be refused only if the award or the manner in which it was made is

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81. *See, e.g.,* Mercy Hosp., Inc. v. Mass. Nurses Ass'n, 429 F.3d 338 (1st Cir. 2005) (rejecting public policy challenge to award because findings of fact did not establish violation of well-defined and dominant public policy); Prudential-Bache Secs, Inc. v. Tanner, 72 F.3d 234 (1st Cir. 1995) (rejecting challenge on grounds of insufficient showing that award violated asserted public policy). *But see* BORN 2009, *supra* note 76, at 2626 ("It is not clear whether the public policy exception in the US requires proof that enforcement of the arbitral award itself would violate applicable public policy or compel conduct that would violate a public policy. . . . [It is] more likely [that] the public policy exception in US courts is implicated where the substantive claim on which the award is based is contrary to applicable public policy.").

82. Eastern Assoc. Coal Corp. v. United Mine Workers of Am., 531 U.S. 57, 62–63, 67 (2000).

83. 9 U.S.C. § 201 *et seq.* (2012).

84. *See infra*, section 4.1.

85. Arbitration Act, 1996, c. 23, § 66(1) (U.K.).

86. *Id.* § 103(3).

“manifestly contrary to public policy or good morals.”<sup>87</sup> For awards not rendered in the Netherlands, the enforcement regime differs for covered and non-covered awards.<sup>88</sup>

Article 1076 of Dutch Code of Civil Procedure applies to recognition and enforcement proceedings for foreign non-covered awards.<sup>89</sup> Such awards may be recognized and enforced in the Netherlands unless the party seeking to avoid enforcement can prove that a valid arbitral agreement is lacking, the tribunal was improperly constituted or exceeded its mandate, or the award is subject to appeal or has been vacated in the country where it was made.<sup>90</sup> Non-covered foreign awards may be refused recognition or enforcement in the Netherlands if the Dutch court seized of the dispute “finds that the recognition or enforcement would be contrary to public policy.”<sup>91</sup>

Article 1075, in turn, applies to the recognition and enforcement of covered awards. Article 1075 provides that an arbitral award made in a foreign State to which the New York Convention applies may be recognized and enforced in the Netherlands.<sup>92</sup> Thus, the Article V(2)(b) public policy exception must be taken into consideration when recognition or enforcement of a foreign arbitral award under the New York Convention is sought in the Netherlands. Just as Chapter 2 of the FAA directly incorporates the text of the New York Convention (including the public policy exception) into US federal law, Article 1075 of the Dutch Code of Civil Procedure makes foreign awards recognizable and enforceable according to the text of the New York Convention.

### **2.3.2 Same enforcement regime under national law for foreign arbitral awards subject to and not subject to international treaties**

#### **2.3.2.1 *France applies the same enforcement regime under the Nouveau code de procedure civile to foreign arbitral awards subject to and not subject to international treaties***

The French *Nouveau code de procedure civile* (New Code of Civil Procedure) (“N.C.P.C.”)<sup>93</sup> adopts an exclusive list of statutory grounds for denying recognition to foreign arbitral awards regardless of whether the award is subject to the New York Convention. Scholars have argued that by not adopting verbatim the grounds for denial of

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87. Wetboek van Burgerlijke Rechtsvordering [RV] [Code of Civil Procedure] art. 1063 (Neth.), translated in Neth. Arb. Inst., *The Netherlands Arbitration Act 1986*, 4 J. INT’L ARB. 127, 139–40 (1987).

88. See RV arts. 1075–76, translated in Neth. Arb. Inst., *supra* note 87, at 143–44.

89. RV art. 1076, translated in Neth. Arb. Inst., *supra* note 87, at 144.

90. RV art. 1076(1)(A)(a)–(b), translated in Neth. Arb. Inst., *supra* note 87, at 144.

91. RV art. 1076(1)(B), translated in Neth. Arb. Inst., *supra* note 87, at 144.

92. RV art. 1075, translated in Neth. Arb. Inst., *supra* note 87, at 143.

93. NOUVEAU CODE DE PROCEDURE CIVILE [N.C.P.C.] (Fr.);

recognition and enforcement provided in the Convention, France's regime is made more favorable to parties seeking enforcement.<sup>94</sup>

France distinguishes between domestic and international arbitrations. It uniquely defines an arbitration as "international" on the sole basis that, in the arbitration, "international interests are at stake."<sup>95</sup> Thus, unlike under the laws of the US, the UK, and the Netherlands, under French law, the territory in which the award was made does not determine whether it is international. Instead, that classification depends on the existence of a dispute regarding international interests. Poudret and Besson have noted that a "material or immaterial *cross border* transfer" is the "essential criterion" of such international interests.<sup>96</sup> And, in fact, the Paris Court of Appeal has even emphasized that a contract drafted in French, applying French law, and providing for French arbitrators can be considered as imputing "international" interests.<sup>97</sup>

Within the category of "international arbitration," French law does distinguish between international awards made in France ("domestic international awards") and those made abroad ("foreign international awards").<sup>98</sup> For domestic international awards, the only recourse an award-debtor has against enforcement is an action to set aside.<sup>99</sup> Under Article 1520, an award may be set aside where the tribunal wrongly assumed or declined jurisdiction, was not properly constituted, or exceeded its mandate; where due process was violated; or where recognition or enforcement of the award would be contrary to "international public policy" (*l'ordre public international*).<sup>100</sup> A decision of a French court to deny an application to set aside is deemed an enforcement order of the award.<sup>101</sup>

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94. See DELVOLVÉ ET AL., *supra* note 21, at 211.

95. See N.C.P.C. art. 1054; see also See JEAN-FRANÇOIS POUURET & SÉBASTIEN BESSON, *COMPARATIVE LAW OF INTERNATIONAL ARBITRATION* 31 (Stephen Berti & Annette Ponti trans., 2d ed. 2007).

96. POUURET & BESSON, *supra* note 95, at 33 (emphasis added). See *HEALTHY AWARD*, *supra* note 23, at 10. See also Cour d'appel [CA] [regional court of appeal] Paris, Nov. 25, 1993, *Paco Rabannes Parfums et al. v. Les Maisons Paco Rabanne*, 1994 REV. ARB. 730 (Fr.) (holding that transborder movement need not necessarily have occurred, only that it was intended).

97. Cour d'appel [CA] [regional court of appeal] Paris, Jan. 18, 1983, *Sporprom Serv. B.V. v Polyfrance Immo*, 1984 REV. ARB. 87 (Fr.). See also Cour d'appel [CA] [regional court of appeal] Paris, June 20, 1996, *PARIS v. Razel*, 1996 REV. ARB. 657 (Fr.); Cour d'appel [CA] [regional court of appeal] Paris, Oct. 2, 1982, *Colas routière et al. v. Tracet*, 1992 REV. ARB. 625 (Fr.). Compare Cour d'appel [CA] [regional court of appeal] Paris, Jan. 13, 1993, *SADP v. Editions mondiales*, 1995 REV. ARB. 68 (Fr.) (refusing to qualify as "international" a transaction in which the part of the contract to be executed abroad was not significant and did not concern interests of international commerce).

98. See DELVOLVÉ ET AL., *supra* note 21, at 159.

99. N.C.P.C. art. 1518.

100. *Id.* art. 1520 (emphasis added). The distinction between public policy and international public policy is discussed further below.

101. *Id.* art. 1527.



Because a procedure to set aside can only take place in the State where the award is rendered, parties seeking to set aside a foreign international award must do so in the State where that award was made—i.e., not in France. However, a party seeking to have recognition and enforcement of a foreign international award refused in France can only do so on the basis that the award does not meet the Article 1520 requirements. Specifically, Article 1525 provides that the recognition or enforcement of a foreign international award may only be denied on the grounds listed in Article 1520.<sup>102</sup> Thus, crucially, for both domestic and foreign international awards, the applicable public policy exception is not that of the New York Convention (recognition and enforcement would be contrary to the public policy of the country in which enforcement is sought) but an exception that relies on the more ambiguous concept of international public policy.<sup>103</sup>

By classifying as international all arbitrations in which international interests are stake regardless of whether proceedings take place in France or involve French parties and denying recognition and enforcement to the resulting awards only where it would be contrary to international public policy, French law creates a truly extraterritorial arbitration system. That France found it necessary to replace the public policy standard of the New York Convention with the narrower international public policy standard indicates that there is some dispute between signatories of the New York Convention as to what actually comprises “public policy.” That issue is discussed at length in the section 3.

## **2.4 Summary**

The public policy exception in Article V(2)(b) of the New York Convention relates explicitly to the public policy of the State in which enforcement or recognition of a foreign award is sought.<sup>104</sup> The exception contained in the UNCITRAL Model Law is nearly identical that of the New York Convention. Because the UNCITRAL Model Law is only suggested legislation for States to consider in enacting their own legislation, it is helpful to compare it to actually enacted national legislation. By doing so, two trends become apparent: many States apply separate legal regimes to awards under the New York Convention (and other international conventions relating to the recognition and enforcement of foreign awards) and to awards not under it; fewer States apply the same legal regime to awards regardless of whether they are covered by the New York

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102. *Id.* art. 1525.

103. *Id.* arts. 1518, 1520, 1525.

104. New York Convention, *supra* note 32, art. V(2)(b).

Convention. The US, the UK, and the Netherlands are in the former category, whereas France is in the latter.

In the US, the FAA governs the enforcement of all domestic and foreign arbitral awards. Separate enforcement regimes apply to foreign awards covered by the New York Convention and the Panama Convention and foreign awards not covered by it. Non-covered for awards are not subject to any statutory public policy exception, although the existence of an exception is evident from case law. As in the US, the UK applies separate regimes to awards under the New York Convention and awards not under it. English law<sup>105</sup> does not expressly stipulate that a public policy exception exists for non-covered awards, but does provide that they may be “enforced in the same manner as a judgment or order of the court to the same effect.”<sup>106</sup> Covered awards may be refused recognition or enforcement on public policy grounds equivalent to those included in the New York Convention.<sup>107</sup> As in the US and the UK, in the Netherlands there are separate regimes for covered awards and non-covered awards. However, a public policy exception similar to that included in the New York Convention applies to both, as well as to domestic awards.

Unlike in the laws of those three States, French law applies the same enforcement regimes to covered foreign arbitral awards as to non-covered foreign arbitral awards. However, the N.C.P.C. distinguishes between domestic and foreign “international awards.” A public policy exception exists for both varieties, but only if the public policy offended is “international.”

### **3 WHAT IS PUBLIC POLICY?**

As discussed above, the major international conventions and model legislation dedicated to arbitration contain a public policy exception. States also regularly allow a public policy escape clause in their national arbitration legislation. At this point, it is helpful to explain what “public policy” means. As will be shown, in different contexts, the phrase can mean quite different things. Section 3.1 below discusses the ways of understanding of “public policy” within the context of the New York Convention. Sections 3.2 and 3.3 describe the role of “public policy” in the US and the EU, respectively. Each

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105. Several legal systems exist within the UK. At all points in this thesis, the law applied by UK courts under consideration here is English law. In reality, this is, of course, not the case, but the scope of this work does not permit a full inquiry into, *inter alia*, Scottish law.

106. Arbitration Act, 1996, c. 23, § 66(1) (U.K.).

107. *See id.* § 103(3).

section begins with a brief description of the status of public policy within the respective system's larger federal framework.

### **3.1 What is public policy according to Article V(b)(2)?**

Despite its relatively clear language, the public policy exception contained in Article V(2)(b) of the New York Convention is the part of the convention “most prone to misinterpretation and most open to abuse by national courts, displaying skepticism of non-national sources of law and bias against foreigners who wish to enforce awards in their territories.”<sup>108</sup> In the legal systems of most countries that have acceded to the New York Convention, there is no guidance whatsoever on how the public policy exception should be interpreted.<sup>109</sup> Courts have referred to arguments under the public policy exception as “the last resort of the desperate”<sup>110</sup> and dismissed public policy as “a variable notion”<sup>111</sup> that is “open-textured and flexible.”<sup>112</sup>

According to Gary Born, within the New York Convention, “public policy” does not refer only to those public policies of the forum state intended for an international setting and consistent with public international law principles. Instead, “public policy” cannot be interpreted without considering Article V(b)(2)'s role as an escape clause.<sup>113</sup> Thus, public policy allows a State to escape from enforcement of an agreement pernicious to its values. Born's view is consistent with the text of Article 36 of the UNCITRAL Model Law. The UNCITRAL Model Law provides that recognition or enforcement may be refused . . . “if the court finds that . . . the recognition or enforcement of the award would be contrary to the public policy of [the enforcing] State.”<sup>114</sup>

However, because the New York Convention leaves the contents of the term “public policy” open to interpretation, a number of different approaches to interpreting its meaning have been developed.

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108. Jan Paulsson, *The New York Convention in International Practice: Problems of Assimilation*, in THE NEW YORK CONVENTION OF 1958 108 (Marc Blessing ed., 1996).

109. Troy L. Harris, *The “Public Policy” Exception to Enforcement of International Arbitration Awards Under the New York Convention*, 24 J. INT'L ARB. 9, 11 (2007).

110. Harris, *supra* note 109, at 11 (quoting *Deutsche Schachtbau- und Tiefbohrgesellschaft mbH v. Ras Al Khaimah Nat'l Oil Co.*, [1987] 3 W.L.R. 1023 (C.A.) (Eng.)).

111. *Id.*

112. *Id.* (quoting *Renusagar Power Co. v. General Electric Co.*, A.I.R. 1994 S.C. 860 (India)).

113. See BORN 2009, *supra* note 76, at 2622.

114. UNCITRAL Model Law, *supra* note 34, art. 36(1)(b)(ii).

### **3.1.1 Public policy under the New York Convention is the public policy of the enforcing State**

The first approach reads the public policy exception contained in Article V(2)(b) narrowly. According to the plain text of the convention, it is the “public policy of that State [i.e., the enforcing State]” and only the public policy of the enforcing State that is implicated. If the award is contrary to the enforcing State’s public policy, recognition and enforcement may be refused.

### **3.1.2 Public policy under the New York Convention is international public policy**

The second approach responds to concerns that by focusing solely on the public policy of the enforcing State, that State could disrupt the effective enforcement of an arbitral award concerning multiple parties, multiple States, and a myriad of public policies. Scholars have noted that “[public policy] has on occasion also been used by courts in some jurisdictions as licence to review—inappropriately—the merits of a dispute.”<sup>115</sup> For this reason, the concept of “international public policy” has gained prominence in some jurisdictions.

The Committee on International Commercial Arbitration of the International Law Association (the “ILA”) has also embraced the second approach. In its Final Report on Public Policy as a Bar to Enforcement of International Arbitral Awards (the “ILA Final Report”), the ILA recognized that State courts must “carry out a balancing exercise between finality and justice” when a foreign arbitral award conflicts with State public policy.<sup>116</sup> The ILA recommends that finality should be favored, “save in exceptional circumstances”<sup>117</sup> which “may in particular be found to exist if recognition or enforcement of the international arbitral award would be against *international* public policy.”<sup>118</sup> It defines international public policy as “that part of the public policy of a State which, if violated, would prevent a party from invoking a foreign law or foreign judgment or foreign award.”<sup>119</sup>

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115. REDFERN & HUNTER, *supra* note 13, at 615.

116. INTERNATIONAL LAW ASSOCIATION, COMM. ON INT’L COMMERCIAL ARB., FINAL REPORT ON PUBLIC POLICY AS A BAR TO ENFORCEMENT OF INTERNATIONAL ARBITRAL AWARDS 2 (2002) [hereinafter ILA FINAL REPORT].

117. ILA FINAL REPORT, *supra* note 116, at 2, recomm. 1(a).

118. *Id.* at 2, recomm. 1(b) (emphasis added).

119. *Id.* at 3, ¶ 11.

As will be discussed below, French law provides an exception to the enforcement or recognition of international arbitral awards on the basis that enforcement or recognition would be contrary to *international* public policy. The meaning of this term in the French legal system is similar but not identical to the notion of international public policy proposed as the best way of interpreting Article V(2)(b).<sup>120</sup>

### **3.1.3 Public policy under the New York Convention is transnational public policy**

The ILA provides a third, even more restrictive, concept: “transnational public policy” (or “truly international public policy”).<sup>121</sup> Transnational public policy includes “fundamental rules of natural law, principles of universal justice, *jus cogens* in public international law, and the general principles of morality accepted by . . . ‘civilized nations.’”<sup>122</sup> Unlike the national and international interpretations of public policy, transnational public policy exists “independently of purely national conceptions of international public policy.”<sup>123</sup>

Numerous scholars support the transnational public policy view. Blanke & Landolt consider the transnational concept to be the only way of interpreting public policy adapted to the needs of international trade.<sup>124</sup> According to the transnational view, an arbitration clause is valid except in “cases of fraud, duress, or violation of an internationally recognized concept of public policy.”<sup>125</sup> Arnold & Meindl point out that because arbitral tribunals not bound to a particular State’s legal system, when they apply public policy rules in arbitration proceedings, it is a “common international understanding of what public policy means,” rather than the public policy of any one State.<sup>126</sup> Thus, transnational public policy “will even override national mandatory rules of public policy.”<sup>127</sup> However, transnational public policy has seen little practical application and is difficult to support through a textual reading of the Convention.

The ILA notes that no court has expressly applied transnational public policy, but several cases have concluded that activities such as corruption, drug trafficking,

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120. *Id.* at 2, recomm. 1(b).

121. Audley Sheppard, *Interim ILA Report on Public Policy as a Bar to Enforcement of International Arbitral Awards*, 19 ARB. INT’L 217, 220 (2003).

122. Sheppard, *supra* note 121, at 220; *see also* Hanotiau & Caprasse, *supra* note 29, at 731.

123. DELVOLVÉ ET AL., *supra* note 21, at 155.

124. Alexis Mourre, *Arbitrability of Antitrust Law from the European and US Perspectives*, in EU AND US ANTITRUST ARBITRATION 20 (Gordon Blanke & Phillip Landolt eds., 2011).

125. Mourre, *supra* note 124, at 20.

126. Arnold & Meindl, *supra* note 24, at 98.

127. DELVOLVÉ ET AL., *supra* note 21, at 155.

smuggling, and terrorism, are “illicit virtually the world over.”<sup>128</sup> Moreover, the concept of transnational public policy strays far from the plain language of the New York Convention.<sup>129</sup> Article 2(b) states that a competent authority may refuse recognition or enforcement where granting recognition or enforcement “would be contrary to the public policy of that country,” not merely when it would be contrary to the public policies shared by a certain percentage of States party to the Convention.<sup>130</sup> Under the transnational concept, the New York Convention’s public policy exception is redundant. A universally abhorred practice would be contrary to the public policy of every party to the New York Convention. Thus, the award-debtor would just as easily be able to set aside the award for public policy grounds in the State rendering the award as it would be able to challenge the award on those grounds in the State where enforcement is sought.

### 3.1.4 What forms of public policy are relevant to international arbitrations?

The ILA Final Report states that the public policy of a State relevant for purposes of Article V(2)(b) includes:

- (i) fundamental principles, pertaining to justice or morality, that the State wishes to protect even when it is not directly concerned;
- (ii) rules designed to serve the essential political, social or economic interests of the State, these being known as “*lois de police*” or “public policy rules”; and
- (iii) the duty of the State to respect its obligations towards other States or international organizations.<sup>131</sup>

The first category, fundamental principles, can be divided into substantive and procedural fundamental principles. Substantive fundamental principles include, *inter alia*, the principles of good faith and *pact sunta servanda*, the prohibitions against abuse of rights, uncompensated expropriation, discrimination, and activities that are *contra bonos mores*, (e.g., piracy, terrorism, genocide, slavery, drug trafficking, and pedophilia).<sup>132</sup> Fundamental principles of a procedural nature include impartiality of the tribunal; equality

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128. Sheppard, *supra* note 121, at 221 (citing Cour d’appel [CA] [regional court of appeal] Paris, Sept. 30, 1994, *European Gas Turbines SA v. Westman Int’l Ltd.*, 1994 REV. ARB. 359 (Fr.)).

129. See BORN 2009, *supra* note 76, at 2837:

The language and structure of Article V(2) cannot be reconciled with a requirement that Contracting States apply transnational or “truly international” public policy. As discussed above, Article V(2) permits non-recognition where giving effect to an award is “contrary to the public policy of that country,” that is, the country where recognition is sought. It is very difficult to interpret this formulation as a reference to purely international sources of law or public policy; had this result been intended, very different language would have been used.

130. See New York Convention, *supra* note 32, art. V(2)(b) (emphasis added).

131. ILA FINAL REPORT, *supra* note 116, at 6, recomm. 1(d).

132. *Id.* at 6–7, ¶ 28.

of the parties; a reasonable opportunity to present one's case; receipt of proper and adequate notice; adjudication free of fraud, corruption, or bias; respect for the *res judicata* effect of a foreign judgment or decree on an award; and rules of natural justice.<sup>133</sup> *Lois de police* or public policy rules include such rules as antitrust laws, currency controls, price fixing rules, environmental protection laws, trade embargoes, tax laws, and consumer protection laws.<sup>134</sup> International obligations include for example United Nations Security Council resolutions imposing sanctions.<sup>135</sup>

Many aspects of public policy relevant to the enforcement of foreign arbitral awards fall into more than one of the three categories listed by the ILA. Bribery and corruption, for example, are typically considered *contra bonos mores*, and their prohibition is a substantive fundamental principle. Anti-corruption measures may also be part of a State's legislation and thus could additionally be considered *lois de police*. Moreover, a State may have an international obligation to other States to combat bribery and corruption under an international convention.<sup>136</sup>

The ILA Final Report provides recommendations for how each category of public policy provisions should be dealt with by State courts in recognition and enforcement proceedings. With respect to fundamental principles, courts should determine whether the principle is "considered sufficiently fundamental" to justify refusing to recognize or enforce an award, taking into consideration the international nature of the dispute.<sup>137</sup> Where a party could have relied on a fundamental principle but failed to do so during arbitral proceedings, the ILA Final Report recommends that the party should be prevented from raising that principle in recognition or enforcement proceedings.<sup>138</sup>

In respect of an award in violation of a State's *lois de police* or public policy rules, the ILA Final Report suggests that its recognition or enforcement should not be refused unless the implicated rule was specifically intended to encompass the situation under consideration and recognition or enforcement would "manifestly disrupt the *essential* political, social or economic interests protected by the rule."<sup>139</sup> The ILA Final Report further stipulates that violation of such rule should be apparent on the face of the award

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133. *Id.* at 7, ¶ 29.

134. *Id.* at 7, ¶ 30.

135. *Id.* at 7, ¶ 31.

136. *Id.* at 7, ¶ 32. *See, e.g.*, Organisation for Economic Co-operation and Development, Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, Dec. 17, 1997, 37 I.L.M. 1.

137. ILA FINAL REPORT, *supra* note 116, at 9, recomm. 2(b).

138. *Id.* at 9, recomm. 2(c).

139. *Id.* at 10, recomms. 3(a)–(b) (emphasis added).

and that courts should not undertake a reassessment of the facts.<sup>140</sup> Where the rule at issue came into effect after the award was issued, courts should not refuse recognition or enforcement unless the legislator specifically anticipated such a result prior to the rule's enactment.<sup>141</sup>

Regarding international obligations, the ILA Final Report recommends that recognition or enforcement only be refused where recognition or enforcement would constitute a “manifest infringement by the forum State of its obligations towards other States or international organisations.”<sup>142</sup>

Liebscher persuasively argues that the ILA's tripartite categorization is unnecessarily complicated. He notes that the ILA Final Report's inclusion of *lois de police* represents a minority view.<sup>143</sup> The “essentiality” threshold applied to this category is lower than the “fundamentality” threshold applicable to fundamental principles.<sup>144</sup> Moreover, the Report abandons the “fundamentality” threshold entirely with respect to international obligations.<sup>145</sup> Liebscher argues that this stands in opposition to the “clear majority” view that all legal rules must be fundamental in order to be considered public policy.<sup>146</sup>

## **3.2 What is public policy in the US?**

### **3.2.1 Public policy**

The public policy of the US “at all times” restricts and limits the power of federal courts to enforce the terms of private agreements.<sup>147</sup> In the US, public policy is a “rule of decision” that at all times overrides “a general rule of law,” including contract law.<sup>148</sup>

Refusal to recognize an arbitral award because it violates the public policy of the US is rare, but when it does occur, it is usually because “the award conflicts with substantive, rather than procedural, US law or US policy.”<sup>149</sup> Public policy objections to the enforcement of arbitral awards based on procedural laws are generally unsuccessful in the

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140. *Id.* at 11, recomm. 3(c).

141. *Id.* at 11, recomm. 3(d).

142. *Id.* at 11, recomm. 4.

143. Christoph Liebscher, *EU Member State Court Application of Eco Swiss: Review of the Case Law and Future Prospects*, in *EU AND US ANTITRUST ARBITRATION* 807 (Gordon Blanke & Phillip Landolt eds., 2011).

144. Liebscher, *supra* note 143, at 807.

145. *Id.* at 808.

146. *Id.*

147. *Hurd*, 334 U.S. 24, 34–35 (1948) (holding that enforcement of racially discriminatory restrictive covenants would be contrary to US public policy).

148. *Ohio v. Roberts*, 448 U.S. 56, 64 (1980).

149. Levin & Price, *supra* note 57, at 1464.



US.<sup>150</sup> Federal courts have held that an arbitral panel’s consideration of inconsistent testimony was improper and contrary to the policy of maintaining the integrity of the judiciary, but not at the level of being contrary to the public policy of the US.<sup>151</sup> Nor was the failure to disclose a prior relationship to the enforcing party sufficient to rise to the level of being contrary to US public policy.<sup>152</sup> The following discussion of public policy with respect to the US thus focuses on substantive US public policy.

### 3.2.2 Arbitration and federalism in the US

For much of US history, arbitration was governed by traditional rules of common law, the body of continuously evolving jurisprudence originating in the courts of England.<sup>153</sup> Much of the jurisprudence used in applying the FAA steams from the common law. It is an understatement to say that the law governing arbitration in the US is complicated. One observer deemed it to be “a strange mixture of international agreements, federal legislation issued by the Congress, interpretative doctrines developed by the federal courts, and local laws and rules applicable in the individual state of the union involved.”<sup>154</sup>

The US Constitution (“Constitution”) provides for a federal system of shared powers between the federal government and the several states (the “US states”). The Supremacy Clause of the Constitution provides that a federal law that conflicts with a state law will trump, or “preempt,” that US state law.<sup>155</sup> “[US] state laws that conflict with federal law are ‘without effect.’”<sup>156</sup> This is particularly important for the recognition and enforcement of foreign awards in the US because rules of public policy were traditionally and to a large extent still are viewed as the natural domain of the states, but international arbitration is ultimately under the purview of the federal government.

Preemption of US state laws can be either express or implied. Express preemption occurs where a federal statute explicitly states Congress’s intent to preempt US state

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150. *Id.* at 1465.

151. *Waterside Ocean Nav. Co. v. Int’l Nav. Ltd.*, 737 F.2d 150, 151–53 (2d Cir. 1984).

152. *Fertilizer Corp. of India v. IDI Management, Inc.*, 530 F. Supp. 542, 545 (S.D. Ohio 1982).

153. See Mark R. Joelson, *The Interplay of International, Federal and State Law in US Arbitration*, 24 J. INT’L ARB. 379 (2007).

154. Joelson, *supra* note Error! Bookmark not defined., at 379.

155. See U.S. CONST. art. VI, cl. 2:

This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the *supreme law of the land*; and the judges in every state shall be bound thereby, anything in the Constitution or laws of any State to the contrary notwithstanding (emphasis added).

156. *Altria Group v. Good*, 555 U.S. 70 (2008) (quoting *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981)).

law.<sup>157</sup> But even in the absence of explicit statutory language, US state law is impliedly preempted where it addresses a field that Congress intended the US government to exclusively occupy.<sup>158</sup> US state law is also impliedly preempted “to the extent that it actually conflicts with federal law” or impedes the achievement of a federal objective.<sup>159</sup>

Arbitration laws and rules of public policy applicable on the state level are commonplace in the US.<sup>160</sup> Given that the FAA, a federal law, regulates the enforcement of all arbitral awards in the US, conflict between it and state arbitration laws is inevitable, giving rising to pre-emption questions.<sup>161</sup> The solution to a pre-emption is guided by two touchstones: the purpose of Congress in enacting the relevant federal law and, where Congress legislates in a field traditionally occupied by the States, the assumption that Congress did not intend for its legislation to supersede traditional State authority unless that was its “clear and manifest purpose.”<sup>162</sup>

With respect to the FAA, the first test is easily satisfied: Congress’ “principal purpose” in enacting the FAA was to place arbitration agreements on an equal footing with other contracts and ensure that they are enforced according to their terms.<sup>163</sup> The Supreme Court of the United States (“US Supreme Court” or the “Court”) has reiterated that the FAA established an “emphatic federal policy favoring arbitration.”<sup>164</sup> That Congress intended the FAA to supersede state authority is equally apparent. Under the Commerce Clause of the US Constitution,<sup>165</sup> the Congress has the “the power to regulate; that is, to

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157. *See, e.g.*, *English v. Gen. Elec. Co.*, 496 U.S. 72, 78 (1990); *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 95–98 (1983).

158. *See, e.g.*, *Geier v. Am. Honda Motor Co., Inc.*, 529 U.S. 861, 884 (2000); *Freightliner Corp. v. Myrick*, 514 U.S. 280, 287 (1995); *English*, 496 U.S. at 79. *See also* *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977) (“Where . . . the field which Congress is said to have preempted includes areas traditionally occupied by the States, congressional intent to supersede state laws must be clear and manifest.”) (internal quotations omitted).

159. *English*, 496 U.S. at 79. *See, e.g.*, *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142–43 (1963) (finding preemption where it is impossible for a private party to comply with both US federal and US state laws); *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941) (finding preemption where U.S. state law presents an “obstacle to the accomplishment and execution of the full purpose and objectives of Congress”).

160. *See* sources cited above, *supra* note 74.

161. *See* George A. Bermann, *Restating the U.S. Law of International Commercial Arbitration*, 42 N.Y.U. J. INT’L L. & POL. 175, 178 (2009) (discussing federal preemption issues related to the FAA).

162. *Medtronic, Inc. v. Lohr* 518 U.S. 470, 485 (1996); *Jones*, 430 U.S. 519, 525 (1977).

163. *AT&T Mobility*, 131 S.Ct. 1740, 1748 (2011); *Rent-A-Center*, 130 S.Ct. 2772, 2776 (2010); *Buckeye*, 546 U.S. 440, 443 (2006); *Volt*, 489 U.S. 468, 478 (1989).

164. *KPMG LLP v. Cocchi*, 132 S. Ct. 23, 25, 181 L. Ed. 2d 323 (2011); *see, e.g.*, *Nitro-Lift Technologies, L.L.C. v. Howard*, 133 S.Ct. 500, 503 (2012); *AT&T Mobility*, 131 S.Ct. at 1745; *Preston v. Ferrer*, 552 U.S. 346, 353 (2008); *Mitsubishi Motors Corp. v. Soler Chrysler–Plymouth, Inc.*, 473 U.S. 614, 631 (1985); *Southland Corp. v. Keating*, 465 U.S. 1, 10 (1984); *Moses*, 460 U.S. 1, 24 (1983).

165. *See* U.S. CONST. art. I, § 8, cl. 2 (stating that Congress shall have power “[t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes”).

prescribe the rule by which commerce is to be governed.”<sup>166</sup> By enacting the FAA, Congress was exercising its Commerce Clause power, implying “that the substantive rules of the Act were to apply in state as well as federal courts.”<sup>167</sup> It is clear, then, that Congress intended for the FAA to supersede state rules of public policy.

With respect to international arbitration, US public policy is thus quite confused. The FAA requires that recognition or enforcement of covered foreign awards only be refused where recognition or enforcement would be contrary to the public policy of the enforcing State. US states thus may hear actions to enforce but are required, in the case of foreign arbitral awards, to consider whether recognition or enforcement would be contrary to US public policy as opposed to state public policy.

### **3.3 What is public policy in Europe?**

#### **3.3.1 Public policy in the EU**

Just as in the US, each Member State of the EU has its own rules of public policy. As discussed regarding the UK, the Netherlands, and France, each Member State’s understanding of public policy plays a unique role in its respective national arbitration laws. Unlike in the US, there is no overarching federal, EU-level, law governing arbitration in the EU. However, there is an EU-level concept of public policy. In several recent decisions of the Court of Justice of the European Union (“CJEU”) has employed *EU* public policy in an arbitration context.<sup>168</sup>

Yet, the contours of EU public policy remain undefined. One commentator posited EU public policy as being at the crossroads of the three aforementioned approaches to public policy: that of the enforcing State, international public policy, and transnational public policy.<sup>169</sup> Because the first two approaches are nationally defined concepts—linked

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166. *Gibbons v. Odgen*, 22 U.S. 1, 196, 2 Wheat. 1, 196 (1824).

167. *Southland*, 465 U.S. at 12; *see also Buckeye*, 546 U.S. at 445; *Moses*, 460 U.S. at 1, 25, and n.32. The majority view has not been without contention. *See, e.g., Buckeye*, 546 U.S. at 449 (Thomas, J., dissenting) (arguing that the FAA does not apply to proceedings in state courts); *Green Tree Financial Corp. v. Bazzle*, 539 U.S. 444, 460 (2003) (Thomas, J., dissenting) (same); *Doctor’s Assocs., Inc. v. Casarotto*, 517 U.S. 681, 689 (1996) (Thomas, J., dissenting) (same); *Allied–Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 285–297 (1995) (Thomas, J., dissenting) (same); *Southland*, 465 U.S. at 35 (O’Connor, J., dissenting) (finding the FAA to create only a federal procedural law and to not be directly enforceable in state courts).

168. *See, e.g.,* Case C-40/08, *Asturcom Telecomunicaciones SL v Cristina Rodríguez Nogueira*, 2009 E.C.R. I-9579; Case C-168/05, *Elisa María Mostaza Claro v. Centro Móvil Milenium SL*, 2006 E.C.R. I-10437; Case C-127/97, *Eco Swiss China Time Ltd. v. Benetton Int’l NV*, 1999 E.C.R. I-3055.

169. Olivier van der Haegen, *European Public Policy in Commercial Arbitration: Bridge Over Troubled Water*, 16 MAASTRICHT J. EUR. & COMP. L. 449, 459 (2009).

to a particular State, neither is adequate to explain EU public policy, in which “the state or national community as a basis is missing.”<sup>170</sup>

If the position is taken that rules must meet a “fundamentality” threshold to be considered public policy,<sup>171</sup> the lack of an EU-level definition of “fundamentality” becomes problematic.<sup>172</sup> As Liebscher recommends, the CJEU “should deploy some efforts to develop a concept of fundamental EU rules.”<sup>173</sup> It has to this point seemed satisfied to allow Member States to develop their own public policy, which may vary in scope from Member State to Member State.<sup>174</sup>

### 3.3.2 Arbitration and federalism in the EU

The EU constituted a new legal order of international law for the benefit of which the Member States had permanently limited their sovereign rights.<sup>175</sup> The CJEU has noted that EU law would lose its character as Community law if the domestic law of the Member States could override it.<sup>176</sup> The legal basis of the EU itself would be called into question.<sup>177</sup> Bermann has noted that EU public policy stands to serve to ensure the primacy of EU law vis-à-vis the law of the Member States.<sup>178</sup>

EU law and international arbitration are self-contained, autonomous bodies of law. This is for three reasons: the historic separation of EU law and private international law; the exclusion of arbitration from the Brussels Regulation;<sup>179</sup> and the inability of arbitral tribunals to make preliminary references to the CJEU regarding the validity or meaning of EU law provisions.<sup>180</sup>

Initially, any harmonization in the field private international law was expected to occur not under the framework of EU law but through a separate convention entered into

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170. van der Haegen, *supra* note 169, at 459.

171. See HEALTHY AWARD, *supra* note 23, at 42.

172. Liebscher, *supra* note 143, at 812.

173. *Id.* at 821.

174. See HEALTHY AWARD, *supra* note 23, at 54.

175. Case 6/64, *Flaminio Costa v. E.N.E.L.*, 1964 E.C.R. 585, 593; Case 26/62, *NV Algemene Transport- en Expeditie Onderneming van Gend & Loos v. Neth. Inland Revenue Admin.*, 1963 E.C.R. 1; see also PAUL CRAIG & GRAINNE DE BURCA, *EU LAW: TEXT, CASES, AND MATERIALS* 257 (5th ed. 2011).

176. See *Flaminio Costa*, 1964 E.C.R. at 593.

177. See CRAIG & DE BURCA, *supra* note 175, at 257.

178. George A. Bermann, *Navigating EU Law and the Law of International Arbitration*, 28 *ARB. INT'L* 397, 411 (2012) [hereinafter Bermann 2012].

179. Council Regulation 44/2001/EC on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters, 2001 O.J. (L 12) 1; Regulation 1215/2012/EU of the European Parliament and of the Council of the European Union on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (Recast), 2012 (L 351) 1.

180. Bermann 2012, *supra* note 178, at 400–401

by the Member States.<sup>181</sup> Ten years after the entry into force of the Treaty Establishing the European Economic Community in 1958,<sup>182</sup> the Member States entered into such a convention: the 1968 Brussels Convention on Jurisdiction and the Recognition of Judgments in Civil and Commercial Matters (“Brussels Convention”).<sup>183</sup> Authority for the Brussels Convention was derived from Article 293 of the Treaty Establishing the European Community.<sup>184</sup>

However, in *Marc Rich*, the CJEU was called upon to determine the scope of the arbitration exception in Article 1(2)(d) of the Brussels Convention, which states that the convention does not apply to arbitration agreements.<sup>185</sup> The court held that while the New York Convention laid down rules that arbitrators must respect, it did not create obligations on the courts of the contracting States of the Brussels Convention.<sup>186</sup>

### 3.3.3 Public Policy and arbitration in the EU

The CJEU in *Eco Swiss* held that a Member State that treats an offence to domestic public policy as a ground for annulling a local award must treat offenses to EU public policy as a ground for annulment as well.<sup>187</sup> While Member States have “procedural autonomy” to determine the means through which they and their courts implement and enforce European law, they are prohibited from discriminating against legal claims derived from EU law as compared to similar claims provided for in domestic law.<sup>188</sup> Thus, if a Member State were to bar enforcement of an arbitral award on the grounds that it violated public policy, it must do the same when the award violates EU public policy.<sup>189</sup> This dynamic can be compared to the federal-state relationship in US law. Whereas under the FAA, a US state must allow for enforcement of a the arbitral agreement or award that would be barred under state law, an EU Member State must bar the enforcement of an arbitral agreement or award that would otherwise be enforceable under Member State law.

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181. Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11 [hereinafter Treaty of Rome].

182. Treaty of Rome, *supra* note 181, art. 220(4).

183. Consolidated Version of the 1968 Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters, 1972 O.J. (L 299) 31 [hereinafter Brussels Convention].

184. Consolidated Version of the Treaty Establishing the European Community art. 193, 2006 O.J. (C 321 E) 37, 133 [hereinafter TEC] (as in effect 1999) (now Consolidated Version of the Treaty on the Functioning of the European Union art. 101, 2010 O.J. (C 83) 47, 150 [hereinafter TFEU]).

185. *See* Liebscher, *supra* note 143, at 802–803.

186. Case C-190/89, *Marc Rich & Co. AG v. Società Italiana Impianti PA*, 1991 E.C.R. I-3855, ¶ 18.

187. *Eco Swiss*, 1999 E.C.R. I-3055.

188. Bermann 2012, *supra* note 178, at 411.

189. *Id.* at 412.

Moreover, it is the CJEU alone that determines the content and scope of EU public policy.<sup>190</sup> More will be said on that subject below.

#### **4 PUBLIC POLICY EXCEPTIONS IN PRACTICE**

In Part 4, the practical application of provisions in the US and select EU Member States allowing for the refusal of recognition or enforcement of arbitral awards on grounds that recognition or enforcement would violate the public policy of State in which recognition or enforcement is sought is discussed in detail. France and the UK have been highlighted in order to draw a distinction between application of public policy exceptions in civil law and common law systems.

Each State-specific section begins with a brief explanation of the practical application of public policy exceptions in the context of domestic arbitration in that State.

##### **4.1 Limited public policy exceptions to enforcement of arbitral awards under the Federal Arbitration Act exist in the US**

This section describes challenges to the recognition or enforcement of arbitral awards on the grounds of public policy in the US. Subsection 4.1.1 briefly discusses the role of public policy in the application of the FAA to the recognition and enforcement of domestic arbitral awards. Subsection 4.1.2 comprises the bulk of section 4.1, and it explains the application of the public policy exception under the FAA in the enforcement of foreign arbitral awards. It considers in depth the most contentious areas of public policy relevant to enforcement proceedings.

First, in paragraph 4.1.2.1, the issue of whether and to what extent US *foreign* policy can be equated to US *public* policy is explored. The seminal case *Parson & Whittemore*<sup>191</sup> is explained in detail, followed by a discussion of whether US public policy is implicated by anti-terrorism policies, trade embargoes, or sanctions. Second, in paragraph 4.1.2.2, whether a public policy challenge can be sustained on grounds that an arbitral agreement or award is contrary to federal or state law is examined. In that section, emphasis is given to agreements and awards alleged to be or actually contrary to the US Bankruptcy Act,<sup>192</sup> the

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190. *Id.*

191. *Parsons & Whittemore Overseas Co. v. Societe Generale De L'Industrie Du Papier*, 508 F.2d 969 (2d Cir. 1974).

192. Act of Nov. 6, 1978, Pub. L. No. 95-598, title I, § 101, 92 Stat. 2549 (codified as amended at 11 U.S.C. § 101 *et seq.* (2012)).

Jones Act,<sup>193</sup> the Securities Exchange Act of 1934,<sup>194</sup> and the Sherman Act.<sup>195</sup> Third, in paragraph 4.1.2.3, the effect that a foreign judgment or decree invalidating a foreign award or its underlying obligation has on enforcement in the US is considered. In this regard, the doctrine of comity employed in *Sea Dragon* is considered first.<sup>196</sup> The extension of *Sea Dragon* to other policies and other alleged violations of foreign law is then analyzed. Fourth, in paragraph 4.1.2.4, public policy challenges on the ground that an agreement was entered into under duress are examined, focusing on the recent *Changzhou* decision.<sup>197</sup> Finally, in paragraph 4.1.2.5, public policy challenges to enforcement on the grounds that there was fraud by a party to the underlying agreement is explored. Consideration is given to two federal district court decisions: *Indocomex*<sup>198</sup> and *Trans Chemical*.<sup>199</sup>

#### **4.1.1 Public policy exceptions to domestic arbitral awards under the FAA in the US**

While far from the norm, a not insignificant number of applications to vacate awards on public policy grounds have been successful in the US.<sup>200</sup> Most likely to be refused enforcement are agreements or awards that violate *lois de police* or public policy rules. For example, domestic awards in favor of terminated workers were vacated on grounds of well-established public policies against the use of drugs or alcohol by employees engaged in high-risk occupations.<sup>201</sup> Domestic awards are not the focus of this thesis, so it is sufficient to state only that public policy challenges have a low success rate in US courts.

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193. Merchant Marine (Jones) Act of 1920 § 27, 46 § U.S.C. 688 (codified as amended at 46 U.S.C. § 30104 (2012)).

194. Securities Exchange Act of 1934, Pub. L. No. 73-291, ch. 404, title I, § 148 Stat. 881 (codified at 15 U.S.C. § 78a (2012)).

195. Sherman Antitrust Act, ch. 647, 29 Stat. 209 (1890) (codified as amended at 15 U.S.C. § 1 *et seq.* (2012)).

196. *Sea Dragon, Inc. v. Gebr. Van Weelde Scheepvaartkantoor B.V.*, 574 F. Supp. 367 (S.D.N.Y. 1983).

197. *Changzhou AMEC E. Tools & Equip. Co. v. E. Tools & Equip., Inc.*, No. EDCV 11-00354 V, 2012 WL 3106620, at \*1 (C.D. Cal. July 30, 2012).

198. *Indocomex Fibres Pte., Ltd. v. Cotton Co. Int'l. Inc.*, 916 F. Supp. 721 (W.D. Tenn. 1996).

199. *In re Arbitration Between Trans Chem. Ltd. & China Nat. Mach. Imp. & Exp. Corp.*, 978 F. Supp. 266 (S.D. Tex. 1997).

200. *See* case cited BORN 2009, *supra* note 76, at 2626.

201. *See, e.g.*, *Exxon Corp. v. Baton Rouge Oil & Chem. Workers Union*, 77 F.3d 850 (5th Cir. 1996) (public policy against use of drugs by employees working in safety sensitive positions); *Gulf Coast Indus. Workers Union v. Exxon Co.*, 991 F.2d 244 (5th Cir. 1993) (same); *Delta Air Lines, Inc. v. Air Line Pilots Ass'n, Int'l*, 861 F.2d 665 (11th Cir. 1988) (public policy against consumption of alcohol by pilots of passenger airliners); *S.D. Warren Co. v. United Paperworkers' Int'l Union etc.*, 815 F.2d 178 (1st Cir. 1987) (policy against drug use by operator of dangerous machinery); *Amalgamated Meat Cutters & Butcher Workmen v. Great WesternFood Co.*, 712 F.2d 122 (5th Cir. 1983) (public policy against alcohol consumption by truck drivers). *See also* *Iowa Elec. Light & Power Co. v. Local 204*, 834 F.2d 1424, 1426–28 (8th Cir. 1987) (vacating award on grounds that it violated public policy requiring strict adherence to nuclear safety rules”).

#### 4.1.2 Public policy exceptions to enforcement of international arbitral awards in the US under the FAA

In the US, review of international arbitral awards is very limited. US courts are reluctant to allow defenses are not specifically listed in the Convention because title 9, section 207 of the US Code explicitly requires that a federal court “shall” confirm an award unless it finds one of listed grounds for refusal. But just as it is well settled that that domestic arbitral awards that are contrary to public policy will not be confirmed or recognized by US courts under the FAA, the same is true for international arbitral awards.<sup>202</sup> For exceptions to enforcement of international arbitral awards, the FAA refers to “grounds for refusal . . . specified in the . . . Convention.”<sup>203</sup>

US courts routinely address challenges under Article V(2)(b) by stating that there exists a strong US public policy in favor of international arbitration and its twin goals: settling disputes efficiently and avoiding lengthy and costly litigation.<sup>204</sup> But US courts do consider challenges to the enforcement of or applications to set aside international awards on the basis that the award is contrary to US public policy. In defining public policy, US courts have turned to their jurisprudence regarding public policy challenges to domestic awards.<sup>205</sup>

In general, the public policy exception is granted “only where enforcement would violate the forum state’s most basic notions of morality and justice”<sup>206</sup>—in other words, where a fundamental principle of the US would be violated.<sup>207</sup> Case law has developed the notion of US public policy through numerous public policy challenges to awards subject to the New York Convention, including, as detailed below, challenges equating US foreign policy to US public policy; claims that an arbitral agreement or award is contrary to federal or state law; considerations of the effect of a foreign judgment or decree invalidating the award or underlying obligation; allegations the agreement was entered into under duress or fraud by party to the agreement; or that the award is barred by the doctrine of laches.

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202. BORN 2009, *supra* note 76, at 2625.

203. 9 U.S.C. § 207.

204. *Encyclopaedia Universalis S.A. v. Encyclopaedia Britannica, Inc.*, 403 F.3d 85, 90 (2d Cir. 2005).

205. *Sarhank Group v. Oracle Corp.*, 404 F.3d 657, 661 (2d Cir. 2005) (“When we exercise jurisdiction under Chapter Two of the FAA [i.e., under the New York Convention], we have compelling reasons to apply federal law, which is already well-developed, to the quest of whether an agreement to arbitrate is enforceable.”); *Smith/Enron Cogeneration Ltd. P’ship v. Smith Cogeneration Int’l. Inc.*, 198 F.3d 88, 96 (2d Cir. 1999) (“Federal arbitration law controls in deciding this issue.”).

206. *Parsons & Whittemore*, 508 F.2d 969, 974 (2d Cir. 1974).

207. *See* discussion of the ILA Final Report, *supra* note 116.



**4.1.2.1 US foreign policy does not express the US’ “most basic notions of morality and justice” and cannot be considered US public policy**

US courts have been unwilling to equate the foreign policy of the US with “public policy” under Article V(2)(b) of the New York Convention. Repeatedly, courts have stipulated that “‘public policy’ and ‘national policy’ are not synonymous,” even where enforcement of an arbitral award would allegedly benefit States with which the US has poor or no direct relations.<sup>208</sup>

**4.1.2.1.1 Parsons & Whittemore firmly established that US foreign policy is not equivalent to US public policy**

The Second Circuit<sup>209</sup> decision in *Parsons & Whittemore* has become the benchmark test for balancing the US’ foreign policy interests with its interest in the uniform enforcement of foreign arbitral awards under the New York Convention.<sup>210</sup> In that case, a US corporation, Parsons & Whittemore Overseas Co., Inc. (“Parsons”), sought to overturn a federal district court confirmation of an arbitral award in favor of Societe Generale de L’Industrie du Papier (“SG”), an Egyptian corporation.

Parsons had agreed in November 1962 to construct and temporarily manage a paperboard mill in Alexandria, Egypt.<sup>211</sup> The project was to be funded by the US State Department, through purchases of letters of credit from SG in Parsons’ favor.<sup>212</sup> The contract concluded between Parsons and SG included an arbitration clause. Work on the project continued as planned until May 1967. Facing “recurrent expressions of Egyptian hostility to Americans,” the majority of Parsons’ workforce left Egypt in anticipation of the Arab-Israeli Six Day War.<sup>213</sup> On June 6, 1967, the Egyptian government broke diplomatic ties with the US and expelled all Americans from Egypt.<sup>214</sup> Parsons abandoned work on

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208. *Ameropa AG v. Havi Ocean Co.*, No. 10 CIV.3240 TPG, 2011 WL 570130, at \*1 (S.D.N.Y. Feb. 16, 2011) (enforcing arbitral award despite conflict with US foreign policy towards the Islamic Republic of Iran); *see also* *Belship Nav., Inc. v. Sealift, Inc.*, No. 95cv2748, 1995 WL 447656, at \*6 (S.D.N.Y. July 28, 1995) (enforcing arbitral award despite conflict with US foreign policy towards Cuba); *Egerton*, (1853) 10 Eng. Rep. 359 (Q.B.) 437; 4 H.L.C. (H.L) 196 (Eng.) (noting that public policy “has nothing whatever to do” with political policy such as “the degree or nature of interference with foreign States”).

209. For the sake of brevity, United States Courts of Appeals will be referred to by their respective judicial circuit (e.g., First Circuit, Second Circuit, etc.) and collectively as “federal courts of appeals.” United States District Courts will be referred to individually by judicial district (e.g., District of Connecticut, Middle District of Florida, Southern District of Texas, etc.) and collectively as “federal district courts.” The term “federal courts” encompasses both federal courts of appeals and federal district courts.

210. *Parsons & Whittemore*, 508 F.2d 969 (2d. Cir. 1974).

211. *Id.* at 972.

212. *Id.*

213. *Id.*

214. *Id.*

the project, leading SG to invoke the contract's arbitration clause. The arbitral tribunal concluded that the US State Department's withdrawal of funding did not justify Parsons' unilateral decision to abandon the project. It issued a final award in SG's favor in March 1973.<sup>215</sup>

Parsons sought to avoid enforcement of the award in the US by invoking, *inter alia*, the public policy exception to enforcement under the New York Convention.<sup>216</sup> Ultimately holding that the federal district court had properly rejected Parsons' Article V(2)(b) defense, the Second Circuit provided what has become the authoritative analysis of foreign policy vis-à-vis public policy within the meaning of the New York Convention. The court reasoned that the Convention espoused a "general pro-enforcement bias," most apparent in relation to the document it had superseded, the Geneva Convention of 1927.<sup>217</sup> Whereas the burden of proof in enforcement proceedings was placed on the award-creditor under the Geneva Convention, the New York Convention had shifted the burden of proof to award-debtor. This change, the court reasoned, evidenced the basic effort of the New York Convention's framers "to remove preexisting obstacles to [the] enforcement [of awards]."<sup>218</sup> The public policy defense should be read narrowly, the Second Circuit reasoned, in keeping with the Convention's pro-enforcement bias.

Moreover, the Second Circuit noted, "considerations of reciprocity" should persuade US courts to be circumspect in construing Article V(2)(b). Were US courts to read the defense liberally, foreign courts might follow suit, using the defense to prevent the enforcement of arbitral awards rendered in the US.<sup>219</sup> The defense was properly construed to allow enforcing States to deny enforcement of foreign arbitral awards on the basis of public policy only where enforcement would violate the enforcing State's "most basic notions of morality and justice."<sup>220</sup>

Parsons argued that the US State Department's withdrawal of funding to the project required it to abandon the project. By removing its funding, the US State Department had indicated that the project was contrary to US foreign policy. Enforcing an award based on Parsons' obligation to complete the project would thus contravene that foreign policy. The court addressed Parsons' argument dismissively: "In equating national policy with US

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215. *Id.*

216. *Id.*

217. Convention on the Execution of Foreign Arbitral Awards, Sept. 26, 1927, 92 L.N.T.S. 302.

218. *Parsons & Whittemore*, 508 F.2d at 973.

219. *Id.* at 973-74.

220. *Id.* at 974.

public policy, [Parsons] quite plainly misses the mark.”<sup>221</sup> The public policy defense was not meant to be used “as a parochial device protective of national political interests” or “to enshrine the vagaries of international politics under the rubric of ‘public policy.’”<sup>222</sup> Foreign policy disputes with another State did not dislodge the Convention’s policy of providing predictable enforcement of foreign arbitral awards. The court disallowed Parsons’ public policy defense, fearing that “deny[ing] enforcement . . . largely because of the United States’ falling out with Egypt . . . would mean converting a defense intended to be of narrow scope into a major loophole in the Convention’s mechanism for enforcement.”<sup>223</sup>

#### 4.1.2.1.2 Even US antiterrorism policy does not rise to the level of US public policy

The “most basic notions of morality and justice” test developed in *Parsons* was utilized in *National Oil*.<sup>224</sup> Sun Oil, challenging confirmation of an award in favor of the Libyan government-owned oil company, argued that enforcement would penalize it for obeying and supporting US foreign policy and thereby deter other companies from cooperating with US sanctions programs; would be inconsistent with US antiterrorism policies; and would undermine internationally-supported antiterrorism policies by providing funds to Libya which could be used to support terrorist activities.<sup>225</sup> To distinguish the facts from those in *Parsons*, Sun Oil argued that the Libyan government’s support of terrorist activities had been internationally condemned and could not be considered merely a “parochial” interest of the US.<sup>226</sup> The District of Delaware was not persuaded: the US was not at war with Libya, and the executive branch had given Libya permission to bring the action. Under such circumstances, the court could not conclude that enforcement would violate the US’ “most basic notions of morality and justice.”<sup>227</sup>

#### 4.1.2.1.3 US trade embargoes and economic sanctions are not indicative of US public policy

In *Belship Navigation*, the Southern District of New York considered whether the longstanding US foreign policy opposing the political regime in Cuba through the

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221. *Id.* (internal quotes omitted).

222. *Id.*

223. *Id.*

224. *Nat’l Oil Corp. v. Libyan Sun Oil Co.*, 733 F. Supp. 800 (D. Del. 1990).

225. *National Oil*, 733 F.Supp. at 819.

226. *Id.*

227. *Id.* at 820.

imposition of a trade boycott was tantamount to an expression of US public policy.<sup>228</sup> While national economic policy prohibited dealings with Cuba, the public policy exception under the New York Convention did not encompass Washington's embargo of Havana.

Mideast politics and the boycott of Israel surfaced again in *Antco Shipping*, in which the petitioner claimed that opposition to the restrictive trade practices or boycotts imposed by foreign countries against other countries friendly to the US constituted US public policy.<sup>229</sup> The Eastern District of New York relied on *Parsons & Whittemore* to decline a stay of arbitration on the grounds that arbitration would be contrary to US public policy. More recently in *Karen Marine*, US foreign policy opposing the Arab boycott was similarly held not to constitute US public policy for the purposes of refusing enforcement of an arbitral award.<sup>230</sup>

Most recently, the Ninth Circuit upheld a foreign arbitral award in favor of the Iranian Ministry of Defense.<sup>231</sup> The circuit court distinguished between the *confirmation* and the *payment* of an award. While the Iranian Transactions Regulations and the WMD Sanctions Regulations prohibited payment of an award without a specific license, neither regime prohibited confirmation of the award.<sup>232</sup> The respondent had erred by equating US foreign policy with US public policy under the New York Convention.<sup>233</sup> The circuit court affirmed the lower court's confirmation of the award, holding that, even assuming the US had a fundamental public policy against economic support for the government of Iran, "confirmation would not violate that policy."<sup>234</sup>

#### **4.1.2.2 *International arbitration of claims under US federal law is usually permitted even where it would be disallowed as contrary to US public policy in domestic arbitration***

The difference in regimes applied by US courts to international arbitral awards than to domestic awards is most apparent when the dispute involves an arbitral award or agreement that would be contrary to federal or state law. Traditionally, claims arising

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228. *Belship Navigation*, No. 95cv2748, 1995 WL 447656, at \*6 (S.D.N.Y. July 28, 1995).

229. *Antco Shipping Co. v. Sidermar S. p. A.*, 417 F. Supp. 207 (S.D.N.Y. 1976).

230. *Karen Mar. Ltd. v. Omar Int'l. Inc.*, 322 F. Supp. 2d 224 (E.D.N.Y. 2004).

231. *Ministry of Def. & Support for the Armed Forces of the Islamic Rep. of Iran v. Cubic Def. Sys., Inc.*, 665 F.3d 1091 (9th Cir. 2011).

232. *Ministry of Defense*, 665 F.3d at 1098 (referring to Iranian Transactions Regulation, 31 C.F.R. pt. 560.510(a)(3) (2012); WMD Sanctions Regulations, 31 C.F.R. pt. 544.507(c) (2012)).

233. *Ministry of Defense*, 665 F.3d at 1099 ("An expression of national policy is not necessarily dispositive of the public policy issue under the Convention.").

234. *Id.* at 1098.

under federal law were considered not even arbitrable.<sup>235</sup> However, in the benchmark *Mitsubishi Motors*, the US Supreme Court held that concerns of international comity, respect for foreign and transnational arbitral tribunals, and the need for predictability of disputes in international commerce required that it enforce an anticompetitive agreement.<sup>236</sup> It did so “even assuming that a contrary result would be forthcoming in a domestic context.”<sup>237</sup> It remarked that if “Congress intended the substantive protection afforded by a given statute to include protection against waiver of the right to a judicial forum, that intention will be deducible from the text or legislative history.”<sup>238</sup>

#### 4.1.2.2.1 Foreign arbitral awards may be considered judgments pursuant to US bankruptcy law

In *Fotochrome*, the Second Circuit sought to avoid determining whether the Bankruptcy Act constituted a “public policy” contrary to the enforcement of foreign arbitral awards under the New York Convention.<sup>239</sup> The Second Circuit faced a question not contemplated by the FAA, the New York Convention, or the then current Bankruptcy Act: was a foreign arbitral award under the New York Convention a “judgment” pursuant to the Bankruptcy Act, thereby evidencing provable debt, sufficient for a proof of claim in bankruptcy? The circuit court reasoned that although an award was not a judgment within the terms of the statute, it was nevertheless a binding adjudication on the merits. The Second Circuit held, however, that federal bankruptcy courts were not empowered to review arbitral awards: any challenge to the award had to occur in a federal district court.<sup>240</sup>

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235. *See, e.g.*, *McDonald v. West Branch*, 466 U.S. 284 (1984) (holding federal claims asserted under the Ku Klux Act of 1871 not arbitrable); *Barrentine v. Arkansas-Best Freight System, Inc.*, 450 U.S. 728 (1981) (holding employee’s claim based on Fair Labor Standards Act not arbitrable); *U.S. Bulk Carriers v. Arguelles*, 400 U.S. 351, 359–60 (1971) (Harlan, J., concurring) (“[T]he choice of forums inevitably affects the scope of the substantive right to be vindicated.”); *United Steelworks of America v. Warrior & Gulf Navigation Co.*, 363 U.S. 574 (1960) (reasoning that arbitration is good for contractual disputes but not for final resolution of substantive rights); *Wilko v. Swan*, 346 U.S. 427 (1953) (holding claims arising under § 12(2) of the Securities Act of 1933 not arbitrable).

236. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985).

237. *Mitsubishi Motors*, 473 U.S. at 629.

238. *Id.* at 628.

239. *Fotochrome, Inc. v. Copal Co.*, 517 F.2d 512, 516 (2d Cir. 1975).

240. *Fotochrome*, 517 F.2d at 520.

4.1.2.2.2 Agreements to arbitrate claims under the Jones Act will be enforced in US courts, but the enforcement of foreign awards resulting from the such arbitration may be refused if contrary to US public policy

Maritime commerce in US waters and between US ports is federally regulated under the Merchant Marine Act of 1920.<sup>241</sup> Section 27 of the Act, eponymously referred to as the Jones Act after its sponsor Senator Wesley L. Jones, is specifically concerned with cabotage (i.e., coastal shipping of goods between US ports). Under the Jones Act, seamen are provided with rights not typically afforded under international maritime law. Seamen are allowed to bring actions against shipowners for damages based on claims of unseaworthiness or negligence.<sup>242</sup> The Jones Act further entitles seamen to trial of their claims by jury—a right not afforded in maritime law absent express statutory provision.<sup>243</sup>

The Jones Act was at the core of an interesting line of cases in the Eleventh Circuit.<sup>244</sup> In *Williams I*, the Southern District of Florida held that a provision of a seaman’s employment contract and collective bargaining agreement requiring arbitration of his claims in the Bahamas under Bahamian law was not enforceable under the New York Convention on public policy grounds because Bahamian law compromised the seaman’s right to maintenance and cure under the Jones Act by not imposing a continuing duty on his employer to reimburse him for medical expenses due to injury.<sup>245</sup> In *Williams II*, the Eleventh Circuit overturned *Williams I*, distinguishing between the New York Convention Article V(2)(b) policy public defense against the confirmation of a foreign arbitral award and the Article II defense against enforcement of an arbitration agreement. An agreement to submit disputes to arbitration must be enforced unless it is “null and void” as being “obtained through those limited situations, such as fraud, mistake, duress, and waiver, constituting standard breach-of-contract defenses that can be applied neutrally on an international scale.”<sup>246</sup> Failure to provide rights under the Jones Act was not one of

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241. P.L. 66-261, formerly 46 U.S.C. § 688, and codified on Oct. 6, 2006 as 46 U.S.C. § 30104

242. 46 U.S.C. § 688(a) (2012).

243. *Id.*

244. For further discussion of the Jones Act’s relationship to the enforcement of arbitration agreements, see Ashley M. Wheelock, *An Issue of Enforcement: Foreign Arbitration and Choice-of-Law Clauses Within a Jones Act Seaman’s Employment Contract*, 37 TUL. MAR. L.J. 285 (2012).

245. *Williams v. NCL (Bah.) Ltd.* [*Williams I*], 774 F. Supp. 2d 1232, 1237 (S.D. Fla. 2011), *rev’d and vacated*, 686 F.3d 1169 (11th Cir. 2012), *opinion withdrawn and vacated*, 691 F.3d 1301 (11th Cir. 2012). At issue in the case was 46 U.S.C.A. § 30104 (2012), providing that “[a] seaman injured in the course of employment . . . may elect to bring a civil action at law, with the right of trial by jury, against the employer.”

246. *Williams v. NCL (Bah.) Ltd.* [*Williams II*], 686 F.3d 1169, 1171, *opinion withdrawn and vacated*, 691 F.3d 1301 (11th Cir. 2012) (internal quotes omitted).

those situations. Six weeks later, the Eleventh Circuit, acting *sua sponte*, withdrew and vacated its opinion, leaving the line of cases without precedential value.<sup>247</sup>

The reasoning used by the court in *Williams II* remains instructive. The court employed the *Bautista* opinion to distinguish between Article II and Article V(2)(b) defenses.<sup>248</sup> Article II is a defense to the enforcement of an arbitral agreement, whereas Article V(2)(b) is a defense to the enforcement of an arbitral award. In *Bautista*, the Eleventh Circuit affirmed the lower court's decision enforcing an arbitration agreement between a Filipino seaman and Norwegian Cruise Lines that prevented the seamen from bringing a claim under the Jones Act.<sup>249</sup> The argument that enforcing an award that was contrary to the Jones Acts, an expression of US policy, may have been salient at the award enforcement stage but it could not be employed before arbitration proceedings took place. Attempts to prevent enforcement of arbitral agreements that were allegedly "null and void" because they were against public policy have been similarly rejected as "improper . . . under the [New York] Convention *before* arbitration."<sup>250</sup>

#### 4.1.2.2.3 International arbitration of claims under the Securities Exchange Act of 1934 is permissible

In *Scherk*, international arbitration of claims under the Securities Exchange Act of 1934 was held to be permissible.<sup>251</sup> *Scherk* was reinforced by *Shearson*, in which the US Supreme Court held that in order to defeat application of the FAA, a party opposing arbitration has to demonstrate that Congress intended to make an exception to the FAA for that particular claim. Because the party opposing arbitration of its claims under § 10(b) of the Securities Exchange Act was unable to point to any intention of Congress "discernible from the text, history, or purposes of the statute," the Court held the pre-dispute arbitration agreement was enforceable.<sup>252</sup> *Scherk* is discussed further below.

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247. *Williams v. NCL (Bah.) Ltd.* [*Williams III*], 691 F.3d 1301 (11th Cir. 2012).

248. *Bautista v. Star Cruises*, 396 F.3d 1289 (11th Cir. 2005).

249. *Id.* at 1302.

250. *Ballesteros v. NCL (Bah.) Ltd.*, No. 12-24517-C1V, 2013 WL 588328, at \*1 (S.D. Fla. Feb. 13, 2013) (citing *Fernandes v. Carnival Corp.*, 484 F. App'x 361, 362 (11th Cir. 2012)).

251. *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974).

252. *Shearson/Am. Exp., Inc. v. McMahon*, 482 U.S. 220 (1987).

4.1.2.2.4 International arbitration of claims under the Sherman Act is permissible, even where domestic arbitration would be impermissible

Since the famous *Mitsubishi Motors* case, it has been settled law in the US that foreign arbitral awards are enforceable in the US even if, under domestic law, arbitration would be contrary to US policy public.<sup>253</sup>

In *Mitsubishi Motors*, the US Supreme Court provided a definitive ruling as to whether a violation of US antitrust laws constituted a violation of US public policy sufficient to refuse enforcement under Article V(2)(b) of the New York Convention.<sup>254</sup> *Mitsubishi* concerned the dispute between a Japanese automobile manufacturer, Mitsubishi Motors Corporation (“Mitsubishi”), and its distributor in Puerto Rico, Soler Chrysler-Plymouth, Inc. (“Soler”). In 1979, Soler contracted with Mitsubishi and its parent company, Chrysler International, S.A. (“Chrysler”), for the sale of Mitsubishi-manufactured vehicles. The agreement provided that all disputes between Mitsubishi and Soler were to be settled by arbitration in Japan in accordance with the rules of the Japan Commercial Arbitration Association.<sup>255</sup> Soler’s business was initially successful, and its minimum sales volume was significantly increased for the 1981 model year. However, the new-car market slackened, leaving Soler unable to meet the increased sales volume. It sought to ship some unsold vehicles to the US and Latin America, but Mitsubishi and its parent company refused permission for the shipments.<sup>256</sup> Mitsubishi brought an action in the federal district court to compel arbitration under the agreement. Soler counterclaimed, asserting, *inter alia*, a cause of action under the Sherman Act.<sup>257</sup>

In its Sherman Act counterclaim, Soler alleged that Mitsubishi and Chrysler had conspired to divide markets in restraint of trade by refusing to allow Soler to resell the vehicles it had obligated itself to purchase from Mitsubishi, refusing to provide parts which would allow Soler to make its vehicles suitable for resale outside Puerto Rico, and by attempting to replace Soler and its other Puerto Rico distributors with a wholly owned subsidiary.<sup>258</sup> The US Supreme Court held that a breach of antitrust law and damages arising from the breach could be resolved in arbitration.<sup>259</sup> Whereas the case law relied on

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253. *Mitsubishi Motors*, 473 U.S. 614, 629 (1985); *Scherk*, 417 U.S. at 515–20.

254. *Mitsubishi Motors*, 473 U.S. 614 (1985)

255. *Id.* at 617.

256. *Id.* at 618.

257. Sherman Antitrust Act, ch. 647, 29 Stat. 209 (1890) (codified as amended at 15 U.S.C. § 1 *et seq.* (2012)).

258. *Mitsubishi Motors*, 473 U.S. at 620.

259. *Id.* at 625–26.



by Soler had found that “the pervasive public interest in enforcement of the antitrust laws, and the nature of the claims that arise in such cases, combine to make . . . antitrust claims . . . inappropriate for arbitration,” the Court reasoned that such precedent was only applicable to domestic transactions.<sup>260</sup> With respect to international transactions, the Court held that “concerns of international comity, respect for the capacities of foreign and transnational tribunals, and sensitivity to the need of the international commercial system for predictability in the resolution of disputes” required it to enforce agreements to arbitration, “even assuming that a contrary result would be forthcoming in a domestic context.”<sup>261</sup>

Thus, the US Supreme Court established a different standard for international transactions than for domestic transactions. In doing so, the Court followed *Scherk*, in which the Court enforced an arbitral award relating to the international transactions of securities, even while assuming for the purpose of the decision that the controversy would have been non-arbitrable had it arisen out of a domestic transaction.<sup>262</sup> The Court noted that the US had a long established federal policy favoring arbitration and dictating that questions of arbitrability were to be resolved in favor of arbitration.<sup>263</sup> The Court noted that there was no reason to depart from this established policy.<sup>264</sup>

The US Supreme Court went on in *Mitsubishi* to note that there was no basis for assuming that arbitration of an antitrust dispute would be inadequate to or unfair in resolving an antitrust dispute.<sup>265</sup> Nor did the Court consider the potential complexity of the dispute to be outside of an arbitral tribunal’s competence. The Court noted that “adaptability and access to expertise are hallmarks of arbitration.”<sup>266</sup> In response to Soler’s argument that private enforcement of the Sherman Act was too integral to the US public policy in favor of free market competition to be left to the vagaries of arbitration, the Court reasoned that as long as a prospective litigant could effectively vindicate its statutory cause of action in arbitration, the Sherman Act would continue to serve its remedial and deterrent function.<sup>267</sup>

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260. *Id.* at 629 (quoting *Am. Safety Equip. v. J.P. Maguire & Co.*, 391 F.2d 821 (1968)).

261. *Mitsubishi Motors*, 473 U.S. at 629.

262. *Scherk*, 417 U.S. at 516–17.

263. *Mitsubishi Motors*, 473 U.S. at 626.

264. *Id.* at 626–27.

265. *Id.* at 633.

266. *Id.*

267. *Id.* at 637.

**4.1.2.3 *US courts have refused to enforce foreign arbitral awards where foreign judgments or decrees invalidate the award or its underlying obligation***

**4.1.2.3.1 In *Sea Dragon*, the public policy exception was successfully invoked to prevent enforcement of an foreign arbitral award where enforcement was contrary to the US public policy favoring international comity**

*Sea Dragon* provides a rare example of a federal court refusing to enforce a foreign arbitral award on public policy grounds.<sup>268</sup> The award-creditor, a Panamanian corporation, had contracted with the award-debtor, a Dutch corporation, for the shipment of cargoes of sugar. After shipment had been performed, a dispute arose over the non-payment of freight dues. Arbitration ensued. The award-debtor argued without success before the Southern District of New York that it was unable to pay the debt because doing so would violate a Dutch court's sequestration order obtained by its creditor.<sup>269</sup> The creditor, in accordance with Dutch law, had attached the debt owed from award-debtor to award-creditor.

While the general rule favored the confirmation of foreign arbitral awards, the Southern District of New York held that the doctrine of comity did not permit it to confirm an award directing the award-debtor to violate Dutch law.<sup>270</sup> The court reasoned that the decisions of a foreign court are to be accorded comity so long as that court is of competent jurisdiction and the laws and policy of the forum state are respected.<sup>271</sup> Moreover, the court noted, it was "the firm and established policy of American courts to respect a valid foreign decree."<sup>272</sup>

Because the award-creditor had failed to demonstrate either that the Dutch court lacked jurisdiction or that the attachment order violated US law or policy, the Southern District of New York held that it had to give deference to the Dutch order. Otherwise, enforcement of the award would compel the award-debtor to violate Dutch law, and that would be an unacceptable result. Thus, the court held that the public policy exception applied, and it refused enforcement.<sup>273</sup>

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268. *Sea Dragon*, 574 F. Supp. 367 (S.D.N.Y. 1983).

269. *Id.* at 369.

270. *Id.* at 372.

271. *Id.*

272. *Id.* (citing *Hilton v. Guyub*, 159 U.S. 113, 164 (1895)).

273. *Id.* at 372–73.

4.1.2.3.2 Attempts to extend the *Sea Dragon* decision to other policies have been less successful

In *Sea Dragon*, the Southern District of New York held that a foreign arbitration award may be refused enforcement under the New York Convention where the award compels conduct contrary to the US public policy favoring international comity. However, the Southern District of New York has declined to extend *Sea Dragon* in enforcement proceedings for foreign arbitral awards that allegedly compelled conduct contrary to other US public policies.

In *Golden Eagle*, the award-debtor argued that enforcement of an award in petitioner’s favor would violate the laws and policy of the forum state—specifically, the US judicial doctrine of laches.<sup>274</sup> While the doctrine plays a “central role” in the US judicial system, the Southern District of New York reasoned that it was far from the “level of public policy contemplated by the Convention.”<sup>275</sup> The court held that an award must “compel[] the violation of law or conduct contrary to accepted public policy” for its enforcement to be refused under the public policy exception to the New York Convention.<sup>276</sup> Whereas an award compelling the violation of a foreign court decree, as in *Sea Dragon*, “satisfies this standard[,] a misapplication of the equitable doctrine of laches does not.”<sup>277</sup>

Whether an award can be refused enforcement because it compels conduct contrary to public policy was considered by the Ninth Circuit in *Northrop Corp.*<sup>278</sup> The lower district court had refused enforcement of the award. It held that that the award compelled the respondent to pay commissions relating to the sale of weaponry to the Saudi Arabian government, in contravention of a US Department of Defense policy aimed at prohibiting such commissions. The Ninth Circuit disagreed. It reasoned that in order for an award to be refused enforcement because it compels conduct contrary to public policy, the public policy in question must be “well defined and dominant.”<sup>279</sup> Because the Department of

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274. *A. Halcoussis Shipping Ltd. v. Golden Eagle Liberia Ltd.*, No. 88 CIV. 4500 (MJL), 1989 WL 115941, at \*1 (S.D.N.Y. Sept. 27, 1989); see also BLACK’S LAW DICTIONARY 953 (9th ed. 2009) (defining the doctrine of laches as “[t]he equitable doctrine by which a court denies relief to a claimant who has unreasonably delayed in asserting the claim, when that delay has prejudiced the party against whom relief is sought”).

275. *Golden Eagle*, 1989 WL 115941, at \*2.

276. *Id.* at \*2 (quoting *Revere Copper & Brass Inc. v. Overseas Private Inv. Corp.*, 628 F.2d 81, 83 (D.C. Cir. 1980)).

277. *Id.*

278. *Northrop Corp. v. Triad Int’l Mktg., S.A.*, 811 F.2d 1265, 1271 (9th Cir. 1987), *amended sub nom.*, 842 F.2d 1154 (9th Cir. 1988).

279. *Northrop*, 811 F.2d at 1271 (quoting *W.R. Grace*, 461 U.S. 757, 766 (1983)).

Defense policy “arguably was neither,” the Ninth Circuit held that the lower court’s failure to enforce the award was unwarranted.<sup>280</sup>

*Golden Eagle* and *Northrop Corp.* are indicative of the difficulty award-debtors have had in persuading federal courts to deny recognition or enforcement of a foreign arbitral award on the grounds that a foreign judgment or decree invalidates the award or its underlying obligation.

#### 4.1.2.3.3 The doctrine of comity in *Sea Dragon* has not been widely adopted by other US courts

In the *Sea Dragon* opinion, the Southern District of New York gave preference to the US public policy of international comity over the public policy favoring the enforcement of international arbitral awards. Most other US courts to reach the issue have come to the opposite conclusion.

In *Rintin*, the Eleventh Circuit balanced the consideration of international comity with the public policy of the forum, Florida.<sup>281</sup> The respondent in *Rintin* had been ordered to dismiss its ongoing foreign litigation in an arbitral award in the petitioner’s favor. While respect for international comity was Floridian public policy, another of the state’s public policies was “far more directly implicated”—that of “favoring the use of arbitration to resolve disputes arising out of international relationships.”<sup>282</sup> The circuit court reasoned that dismissal of the suits was integral to the relief granted in the award and held that because the respondent had not demonstrated that the award offended “a basic principle of justice or morality,” the award would be enforced.<sup>283</sup>

#### 4.1.2.3.4 Attempts to extend the *Sea Dragon* decision to other alleged violations of foreign law have not succeeded

The *Sea Dragon* holding has not been expanded to cover awards violating other US public policies, and it has also failed to find relevance in other cases where awards allegedly violating a foreign law were at issue.

In *American Construction*, the Southern District of New York declined to refuse enforcement of an award despite a Pakistani judgment that the arbitration clause and

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280. *Id.*

281. *Rintin Corp., S.A. v. Domar, Ltd.*, 476 F.3d 1254 (11th Cir. 2007).

282. *Rintin*, 476 F.3d at 1261 (citing Fla. Stat. ch. 684.02(1)).

283. *Id.*

proceeding were void.<sup>284</sup> Since the proceeding giving rise to the judgment had been “marked by . . . omissions and positive misstatement,” the court held that it would be against public policy for it to refuse enforcement of the award on the basis of the judgment.<sup>285</sup>

The issue was revisited in *Telenor*.<sup>286</sup> In *Telenor*, the respondent invoked *Sea Dragon* and argued that enforcement of a foreign arbitral award in the petitioner’s favor would be contrary to Ukrainian law just as enforcement of the *Sea Dragon* award would have contravened Dutch law.<sup>287</sup> The court was not persuaded. It distinguished the award, which “though not *required* under Ukrainian law . . . , [was] not clearly *prohibited*,” from the award in *Sea Dragon*, which would have compelled action clearly prohibited by a Dutch decree.<sup>288</sup> The court cast doubt on the notion that a public policy against enforcement of arbitral awards that compel a violation of foreign law even existed in New York.<sup>289</sup> But even assuming that such a policy existed, it was “outweighed . . . by the public policy in favor of encouraging arbitration and enforcing arbitration awards.”<sup>290</sup>

Ukrainian law was at issue again in *Unrvneshprom*.<sup>291</sup> The respondent argued that the award in petitioner’s favor should be refused enforcement because it contravened Ukrainian law.<sup>292</sup> However, the respondent failed to provide sufficient documentation in this regard. The court held that, even assuming a “misapplication of Ukrainian law,” enforcement of the award would meet the standard set in *Parsons & Whitmore*—i.e., it would not amount to a violation of the US’ “most basic notions of morality and justice.”<sup>293</sup>

#### **4.1.2.4 US courts have refused to enforce foreign arbitral awards where the underlying agreement was entered into under duress**

Cases in which the arbitral award arises from an agreement allegedly entered into under duress are rare. When faced with other aspects of the public policy defense, many US courts have theorized that duress (whether the party seeking to avoid enforcement had

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284. *Am. Constr. Mach. & Equip. Corp. v. Mechanised Constr. of Pakistan Ltd.*, 659 F. Supp. 426 (S.D.N.Y. 1987).

285. *American Construction*, 659 F. Supp. at 429.

286. *Telenor Mobile Commc’ns AS v. Storm LLC*, 524 F. Supp. 2d 332 (S.D.N.Y. 2007), *aff’d* 584 F.3d 396 (2d Cir. 2009).

287. *Telenor*, 524 F. Supp. 2d at 349.

288. *Id.* at 357 (emphasis in original).

289. *Id.*

290. *Id.* at 358.

291. *Unrvneshprom State Foreign Econ. Enter. v. Tradeway, Inc.*, No. 95 CIV. 10278 (RPP), 1996 WL 107285, at \*1 (S.D.N.Y. Mar. 12, 1996).

292. *Unrvneshprom*, at \*6.

293. *Id.* (quoting *Parsons & Whittemore*, 508 F.2d 969, 974 (2d Cir. 1974)).

been subject to coercion or the arbitral agreement itself was the result of duress) would clearly be a situation in which enforcement of the award would violate public policy.<sup>294</sup> In *Changzhou*, however, the Central District of California actually had to apply the duress branch of the public policy exception to the facts.

In *Changzhou*, the Central District of California considered the award-creditor's motion to confirm and enforce a foreign arbitral award against award-debtors Eastern Tools & Equipment, Inc. and Guoxing Fan under the New York Convention.<sup>295</sup> The award-debtors stipulated that Mr. Fan had been under duress when he signed an agreement with the award-creditor. At that time, Mr. Fan was held in police detention and "his fear of detention deprived him of his free will."<sup>296</sup> Enforcing the arbitral award arising from the agreement would be contrary to the public policy and law of the forum state, California, award-debtors argued. Pursuant to California law, contracts are voidable if made under duress or if a party's assent was the result of the threat of duress.<sup>297</sup> Upon review of the facts, the court held that it had been reasonable for Mr. Fan to believe that if he did not sign the agreement, he would be detained again until he signed.<sup>298</sup> Aware that it was "unusual for a court to deny confirmation under Article V(2)(b)," the court reasoned that it would be "equally unusual" to enforce a contract "created without one party's consent and complied with out of fear of imprisonment."<sup>299</sup>

*Changzhou* is a unique case in which an foreign arbitral award was refused enforcement under Article V(2)(b) because enforcement of an agreement to arbitrate entered into under duress would be contrary to public policy. However, the public policy at issue was that of California—and not necessarily that of the US. Were US public policy to coalesce around the view that the federal policy favoring arbitration outweighed the policy against enforcement of award entered into under duress, the California public policy

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294. See *Ameropa*, 2011 WL 570130, at \*2 (S.D.N.Y. Feb. 16, 2011) ("Enforcement would violate [the US'] 'most basic notions of morality and justice' . . . if [award-debtor] had been subject to coercion or any part of the agreement had been the result of duress."); *Transmarine Seaways Corp. of Monrovia v. Marc Rich & Co.*, 480 F. Supp. 352, 358 (S.D.N.Y. 1979) ("[D]uress, if established, furnishes a basis for refusing enforcement of an award under Article V(b)(2) of the Convention."); see also Homayoon Arfazadeh, *In the Shadow of the Unruly Horse: International Arbitration and the Public Policy Exception*, 13 AM. REV. INT'L ARB. 43, 58–59 (2002) (discussing the approach of common law jurisdictions toward "clearly illegal" contracts).

295. *Changzhou*, No. EDCV 11-00354 V, 2012 WL 3106620, at \*1 (C.D. Cal. July 30, 2012).

296. *Changzhou*, 2012 WL 3106620, at \*14.

297. *Id.* at \*14 (citing *Tarpy v. San Diego*, 110 Cal. App. 4th 267, 276 (2003) ("Duress generally exists whenever one is induced by the unlawful act of another to make a contract or perform some other act under circumstances that deprive him of the exercise of free will.")).

298. *Changzhou*, 2012 WL 3106620, at \*15.

299. *Id.* at \*19.

applied in this case would be pre-empted. *Changzhou* can be usefully compared to *Rintin* and *Telenor*, discussed above.<sup>300</sup> In all three cases, the federal court seized of the matter applied the respective state public policy. However, only in *Changzhou* did the court find that state public policy constituted grounds to refuse enforcement of the award. In *Rintin* and *Telenor*, the courts held that the public policies of Florida and New York, respectively, favoring the resolution of disputes by arbitration outweighed the public policies offered by the award-debtors as grounds to refuse enforcement.

#### **4.1.2.5 US courts typically enforce foreign arbitral awards where the award or underlying agreement is alleged to be the product of fraud**

In *Indocomex*, the Western District of Tennessee confirmed a foreign arbitral award despite the award-debtor's allegation that the underlying contract had been obtained by fraud.<sup>301</sup> Specifically, the award-debtor asserted that the award-creditor committed fraud by failing to provide a letter of credit in a timely manner. The court was not persuaded. It reasoned that fraud, in respect to proceedings under the FAA, involved a showing of bad faith during the arbitration proceedings that had escaped the notice of the arbitrators. The award-debtor had not attempted to make such a showing, and the court enforced the award.<sup>302</sup> The ruling in *Indocomex* is consistent with a line of cases in which enforcement of an arbitral award was challenged on the grounds that because the award was obtained through fraud by party to the agreement, its enforcement would be contrary to US public policy.<sup>303</sup>

In *Trans Chemical*, the Southern District of Texas stipulated that a party alleging fraud must demonstrate that the behavior in question could not have been discovered by due diligence before or during the arbitration proceedings, was materially related to an issue in arbitration, and could be established by clear and convincing evidence.<sup>304</sup> China National Machinery Import and Export Corp. ("CNMIEC"), the party seeking to avoid enforcement, alleged that as a result of Trans Chemical Ltd.'s ("TCL") untimely production of a relevant report, TCL had fraudulently obtained the arbitration award. In the

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300. *Rintin*, 476 F.3d 1254 (11th Cir. 2007); *Telenor*, 524 F. Supp. 2d 332 (S.D.N.Y. 2007), *aff'd* 584 F.3d 396 (2d Cir. 2009).

301. *Indocomex*, 916 F. Supp. 721, 727 (W.D. Tenn. 1996).

302. *Id.* at 728.

303. See Dirk Otto & Omaia Elwan, *Article V(2)*, in *RECOGNITION AND ENFORCEMENT OF FOREIGN ARBITRAL AWARDS* 374–75 (Herbert Kronke et al. eds., 2010).

304. *In re Arbitration Between Trans Chem. Ltd. & China Nat. Mach. Imp. & Exp. Corp.*, 978 F. Supp. 266, 304 (S.D. Tex. 1997) *aff'd sub nom.* *Trans Chem. Ltd. v. China Nat. Mach. Imp. & Exp. Corp.*, 161 F.3d 314 (5th Cir. 1998).

months prior to the proceedings, TCL turned over 40,000 pages of relevant documentation to CNMIEC. However, the report was not among the produced documents, and CNMIEC specifically requested it on several occasions. Found “misfiled among . . . unrelated documents,” the report was finally turned over on the eve of the arbitration proceedings.<sup>305</sup> However, because CNMIEC had failed to offer any evidence—let alone “clear and convincing” evidence—that TCL’s conduct regarding the report was “fraudulent, immoral, illegal, or otherwise in bad faith,” the court dismissed CNMIEC’s claim.<sup>306</sup>

*Indocomex* and *Trans Chemical* demonstrate the difficulty award-debtors have had in the US when seeking to have recognition or enforcement of a foreign arbitral award refused on grounds that it or the underlying agreement was the product of fraud.

#### **4.1.3 US courts rarely refuse recognition or enforcement of foreign arbitral awards on public policy grounds**

As the cases discussed above demonstrate, award-debtors have had little success in utilizing the New York Convention’s Article V(2)(b) public policy exception. While enforcement was refused in *Williams I*, *Sea Dragon* and *Changzhou* on public policy grounds, these cases are at best marginal and are far outweighed by the majority of cases in which federal district courts recognize arbitration agreements and enforce foreign arbitral awards.

#### **4.2 Limited public policy exceptions to enforcement of arbitral awards under the Arbitration Act of 1996 exist in the UK**

The principle of finality is deeply entrenched in English law, and UK courts have traditionally been reluctant to refuse enforcement of a judgment or arbitral award on grounds of public policy.<sup>307</sup> The limited public policy exceptions to the enforcement of domestic and foreign arbitral awards that do exist under the Arbitration Act of 1996 are discussed in this section.

Subsections 4.2.1 and 4.2.2 explore challenges on the grounds of public policy to domestic and foreign awards respectively. The venerable *Soleimany v. Soleimany* decision is used to exemplify the challenges to former, while challenges to the latter are more thoroughly detailed. In paragraph 4.2.2.1, the argument that because an arbitral agreement or award is contrary to English law, its recognition or enforcement should be refused by

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305. *Trans Chemical*, 978 F. Supp. at 305.

306. *Id.*

307. *See, e.g.*, *Henderson v. Henderson*, (1843) 67 Eng. Rep. 313 (Ch.); 3 Hare 100, 103 (Eng.) (expressing the classic rule of *res judicata*).



UK courts is considered. In paragraph 4.2.2.2, the same argument in relation to agreements induced by fraud is discussed. Finally, in paragraph 4.2.2.3, the effect that a foreign judgment or decree invalidating a foreign arbitral award or the underlying obligation has on enforcement proceedings in UK courts is considered.

#### **4.2.1 UK courts refuse enforcement of domestic arbitral awards resulting from an agreement illegal under English law**

In *Soleimany v. Soleimany*, the defendant appealed a judgment enforcing a domestic arbitral award in favor of the plaintiff.<sup>308</sup> The parties had been engaged in an enterprise to illegally smuggle carpets out of Iran and were in dispute over the division of profits. The arbitration took place before the Beth Din which applied Jewish law. The arbitrator had noted that the business activities were illicit under both Iranian and English law but attached no significance to this fact, as it had no effect on the parties' rights under Jewish law.<sup>309</sup> The Queen's Bench Division overturned the lower court's judgment holding that enforcement of a contract illegal under English law would be contrary to UK public policy.

#### **4.2.2 Public policy challenges to the enforcement of foreign awards under the EAA**

##### ***4.2.2.1 UK courts will also refuse enforcement of foreign arbitral awards resulting from an agreement illegal under English law, but are less likely to do so when the agreement is permissible under English law but illegal under foreign law***

While courts in the UK are generally reluctant to employ public policy to refuse the recognition or enforcement of foreign awards under section 103(3) of the EAA, they will do so where the award or underlying agreement is contrary to English law or "the requirements of substantial justice under English law."<sup>310</sup> However, the position of UK courts has considerably softened since Lord Denning declared: "An arbitrator has no jurisdiction or authority to award damages on an illegal contract. It is obvious that the court would not itself enforce such an award."<sup>311</sup>

English courts exhibit a pro-enforcement bias but will refuse enforcement where the underlying contract is illegal under English law. That position was established half a

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308. *Soleimany v. Soleimany*, [1999] Q.B. 785, [1998] 3 W.L.R. 811 (Eng.).

309. *Soleimany*, [1999] Q.B. 785, [1998] 3 W.L.R. 811 (Eng.).

310. Ned Beale et al., *Summary Arbitration Proceedings: A Comparison Between the English and Dutch Regimes*, 26 ARB. INT'L 139, 150 (2010). See *Adams v. Cape Indus. et al.*, [1990] Ch. 433 (C.A.) (Eng.) (stating that breach of the rules of natural justice is an "independent public policy reason for the refusal of recognition or enforcement of an award).

311. *David Taylor & Son v. Barnett Trading Co.*, [1953] 1 W.L.R. 562 (C.A.) 570 (Eng.).

century ago in *David Taylor*, in which the Court of Appeal refused to enforce an award based on a contract for the sale of Irish stewed steak at a higher price than that allowed under the English law.<sup>312</sup> In that case, Lord Justice Denning remarked, “There is one law for all. If a contract is illegal, then arbitrators must decline to award upon it just as the court would do.”<sup>313</sup> Subsequent cases show the situation to be far more ambiguous.

In *Westacre Investments*, the Court of Appeal held that a contract involving influence trading would only be contrary to UK domestic public policy if the contract was in violation of the domestic public policy of the State where it was to be performed.<sup>314</sup> The parties, Westacre Investments Inc. (“Westacre” or the “award-creditor”) and Jugoimport-SPDR Holding Co. Ltd. and Beogradska Banka (collectively, the “award-debtors”) had contracted under Swiss law for the sale of military equipment to Kuwait. When the arbitral award was decided in Westacre’s favor and the award-debtors’ move to have it set aside in Switzerland failed, the award-debtors sought to have it set aside in England.<sup>315</sup>

The award-debtors sought to prevent enforcement of the Swiss award on grounds that it would be “contrary to public policy for recovery to be permitted in the English courts by any available route,” because the parties had mutually intended that the consultancy agreement be performed in a manner contrary to Kuwaiti law and public policy.<sup>316</sup> Under the agreement, the award-creditors were to receive a 15 to 20 per cent commission on all sales of military equipment and related contracts for training and servicing. During the arbitration proceedings, a witness for the award-debtors testified that a commission of 15 to 20 per cent was “unusually high,” leading him to “draw the inference that it must have been appreciated by those involved in the making of the contract that some of the money at least would be applied to ‘illegitimate purposes.’”<sup>317</sup> For procedural reasons, the UK court had to take the facts alleged in the witness’ affidavit to be proven. The court focused on the primary issue of whether, if both parties intended to obtain the weapons contract through the exercise of personal influence over Kuwaiti

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312. *David Taylor*, 1 W.L.R. at 570.

313. *Id.*

314. *Westacre Investments Inc. v. Jugoimport-SPDR Holding Co. et al.*, [1999] Q.B. 740 (Eng.); *see also Euro-Diam Ltd. v. Bathurst*, [1987] 2 W.L.R. 1368 (Q.B.) 1389 (Eng.) (holding that a claim arising from an insurance contract, illegal under German law but legal in the UK, was enforceable in UK courts).

315. *Id.* at 746.

316. *Id.*

317. *Id.* at 748. In reported international arbitration awards, the percentage of an agent’s commission has been found relevant to a determination of the existence of bribery or corruption. *See* Case No. 6497 of 1994, Y.B. COMM. ARB. (1999) 71 (ICC Int’l Ct. Arb.); Case No. 8891 of 1998, 4 J. DU DROIT INT’L (2000) 1076 (ICC Int’l Ct. Arb.) (finding a commission of 18.5% to be indicative of corruption). *But see* Case No. 9333 of 1998, 4 ASA BULL. 757 (2001) (ICC Int’l Ct. Arb.) (finding a commission of 30% to have been justified).

officials, including the payment of bribes, enforcement of the award rendered in Switzerland would be contrary to UK public policy.<sup>318</sup>

The consulting agreement and arbitration clause were governed by Swiss law.<sup>319</sup> The arbitrators unanimously decided the agreement was valid and that the award-debtors' claims were governed by Swiss law which did not prohibit the type of consultancy agreement contemplated.<sup>320</sup> The arbitrators held the agreement to not be invalid as contrary to *bona mores*.<sup>321</sup> While the Kuwaiti Ministry of Defense had issued a circular prohibiting the payment of consulting fees in relation to military contracts, the arbitrators held that the circular had not been established as part of the mandatory law of Kuwait. Nor, in the arbitrators' opinion, did the agreement violate *ordre public international* as neither the lobbying by private enterprises to obtain public contracts nor agreements to carry out such activities were illegal *per se*.<sup>322</sup> The essential test, which had to be applied on a case-by-case base, the court reasoned, was “whether that which invalidates or renders void *ab initio* the underlying contract also strikes down or renders void the agreement to arbitrate.”<sup>323</sup>

Judge Colman provided a detailed framework for analyzing the issue. First, where it is alleged that an underlying contract is illegal and void and that an arbitration award rendered from it is thereby unenforceable, the main question is whether the determination of the specific alleged illegality was within the arbitrator's jurisdiction. Second, Judge Colman reasoned, English law provided no general rule that an arbitration agreement ancillary to a contract illegal at common or statutory law cannot confer jurisdiction on arbitrators. Third, whether such an agreement could in fact confer jurisdiction on arbitrators depends on the nature of the illegality—where it is statutory illegality, the

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318. *Westacre Investments*, [1999] Q.B. at 749.

319. *Id.* at 750.

320. *Id.*

321. *Id.*

322. *Id.* at 751. The arbitrators' view can be disputed on this point. *See, e.g.*, *Trist v. Child*, 88 U.S. 441, 452 (1874) (“We are aware of no case in English or American jurisprudence like the one here under consideration [i.e., payment to lobbyist to influence the passage of a law for the payment of a private claim], where the agreement has not been adjudged to be illegal and void.”); *Providence Tool Co. v. Norris*, 69 U.S. 45, 53 (1864) (“[A]n agreement for compensation to procure a contract from the Government to furnish its supplies,—is against public policy, and void.”); *Noonan v. Gilbert*, 68 F.2d 775 (D.C. Cir. 1934) (“Where the compensation for procuring legislation is contingent, the contract is void as against public policy, regardless of whether corrupt practices are resorted to or contemplated.”); *CapitalKeys, LLC v. CIBER, Inc.*, 875 F. Supp. 2d 59, 64 (D.D.C. 2012) (“[T]he corrupting tendency of contingent fee agreements, not the actual use of improper means, justifies voiding the agreements.”) (internal quotes omitted).

323. *Westacre Investments*, [1999] Q.B. at 756–58 (citing *Harbour Assurance Co. (U.K.) v. Kansa General Int'l Insur. Co.*, [1993] Q.B. 701 (Eng.) (holding not to strike down arbitration agreements collateral to invalidated insurance contracts); *Norske Atlas Insur. Co. v. London General Insur. Co.*, [1927] 28 Ll. L. Rep. 104 (Eng.) (upholding arbitration agreement collateral to marine insurance contract invalid under English law but valid under the Norwegian law that governed it); *Whiteman v. Newey*, [1912] 28 T.L.R. 240 (Eng.) (upholding the reference to arbitration of a dispute about amounts due under illegal betting agreements)).

relevant question is whether the illegality impeaches the agreement as well as the underlying contract; where it is illegality at common law, the question is whether public policy requires that disputes about the underlying contract not be resolved in arbitration. Fourth, when it is necessary at the enforcement stage for the court to determine whether the arbitrators had jurisdiction in respect of the disputes relating to the underlying contract, the court must consider the nature of the disputes in question. If the arbitrators had presided over a dispute in respect of a contract which was “indisputably illegal at common law,” an award in favor of the award-creditor would not be enforced by the court “for it would be contrary to public policy that the arbitrators . . . ignore palpable and indisputable illegality.” If, however, the issue before the arbitrators had been whether the underlying contract was illegal and void, the court would be required to consider whether enforcement of the award would be consistent with public policy were the illegality to be established, thereby impeaching the validity of the underlying contract.<sup>324</sup> Fifth, if the court finds that the arbitration agreement confers jurisdiction on the arbitrators to determine whether the underlying contract was illegal, and the arbitrators determine that it was not, the court should *prima facie* enforce the award. Finally, if the award-debtor then seeks to challenge enforcement of the award on the basis of facts that were not known by the arbitrators but which render the underlying contract illegal, the enforcement court would have to consider whether the public policy against enforcing illegal contracts outweighed the public policy favoring the finality of awards in general and of awards of the same type in particular.<sup>325</sup>

Applying the six-pronged approach to the facts, Judge Colman noted first that the Swiss arbitrators’ jurisdiction could be inferred from the parties’ acquiescence in the arbitration proceedings. The mutual intention of the parties to secure weapons contracts through bribery was plainly illegal under Kuwaiti law.<sup>326</sup> Since enforcement was sought in the UK, Judge Colman then considered whether UK public policy would lead to a different result.<sup>327</sup> He noted that it is “common ground that in English law a contract under which A promises to pay money to B if B will procure by bribery a public body to contract with A is illegal and void *ab initio*.”<sup>328</sup> If B uses or intends to use bribery to secure the contract for A, B cannot enforce the contract with A, regardless of A’s intentions.<sup>329</sup>

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324. *Id.* at 767.

325. *Id.* at 767–68.

326. *Id.* at 768.

327. *Id.*

328. *Id.*

329. *Id.* (citing *Royal Boskalis Westminster N.V. v. Mountain*, [1999] Q.B. 674 (Eng.)).

Judge Colman reasoned that there was no doubt that the broad language of the arbitration clause included the issue whether the agreement was illegal and void, but whether the clause should be, as a matter of UK public policy, should be treated as enforceable depended on weighing the public policy against enforcement of corrupt transactions against the countervailing public policy of sustaining international arbitral agreements.<sup>330</sup> Because the parties had chosen “an impressively competent international body,” the court could assume the arbitrators were competent to determine the issue of illegality.<sup>331</sup> Thus, the risk that the arbitrators would come to an erroneous result was low, and the court reasoned that it could give predominant weight to the public policy sustaining the international arbitral agreements over the public policy of sustaining non-enforcement of contracts illegal at common law.<sup>332</sup>

Since the award-debtor sought to introduce evidence not seen by the arbitrators, the court had to consider which the public policy against enforcement of corrupt contracts outweighed the public policy of finality of international arbitral awards—since what the award-debtor sought by means of the new evidence was essentially a “retrial.”<sup>333</sup> The relevant question, Judge Colman reasoned, was “whether the public policy of discouraging corrupt trading represents a social policy to which effect ought to be given in the interests of international comity . . . in preference to the public policy of sustaining the finality of international arbitral awards.”<sup>334</sup> He noted that “there is mounting international concern about the prevalence of corrupt trading practices.”<sup>335</sup> International comity also had to be considered, but while direct enforcement of the contract “would clearly be offensive to comity,” enforcement of an award under the New York Convention would be “very much

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330. *Id.* at 768–69.

331. *Id.* at 769. The ICC cannot be accused of ignoring public policy concerns relating to its awards. *See* Case No. 2730 of 1982, J. DU DROIT INT’L (Clunet) (1984) 914, 917–18 (ICC Int’l Ct. Arb.):

As a general rule, every contract the object of which is contrary to mandatory laws or the *ordre public* or contrary to moral rules is absolutely null and void. . . . This principle is admitted in all nations and by all legislators. It constitutes an international rule, an element of the common law of contracts in international affairs.

*See also* Case No. 1110 of 1963, Y.B. COMM. ARB. 47 (1996) (ICC Int’l Ct. Arb.) (Judge G. Lagergren famously remarked that the contract in dispute was “condemned by public decency and morality” and “invalid or at least unenforceable.”); Case No. 3913 of 1981 J. D, U DROIT INT’L (Clunet) (1984) 920 (ICC Int’l Ct. Arb.) (ruling that the underlying contract was void because of its illicit nature); Case No. 3916 of 1982, COLL. ICC ARB. AWARDS 507 (ICC Int’l Ct. Arb.) (concluding that contracts that breach acceptable standards of behavior or *ordre public* are void); Case No. 6248 of 1990, 19 Y.B. COMM. ARB. (1994) 124 (ICC Int’l Ct. Arb.) (concluding that international public policy considers contracts involving corruption and bribery to be illegal and unenforceable); Case No. 6497 of 1994, Y.B. COMM. ARB. (1999) 71 (ICC Int’l Ct. Arb.) (confirming general principle that bribery invalidated a contract).

332. *Westacre Investments*, [1999] Q.B. at 770.

333. *Id.* at 771.

334. *Id.*

335. *Id.*

less so.”<sup>336</sup> Notwithstanding that “commercial corruption is deserving of strong judicial and governmental disapproval,” it was not so odious and requiring of “opprobrium” that the public policy opposing the enforcement of corrupt commercial contracts could be given precedence over the public policy favoring the finality of international arbitration awards.<sup>337</sup> The award was enforced.

**4.2.2.2 UK courts may refuse recognition or enforcement of a foreign arbitral award that is the product of fraud, but only where there has been reprehensible or unconscionable conduct**

UK courts recently discussed fraud in the procurement of a foreign arbitral award in the *Naftogaz* series of cases concerning a dispute between Gater Assets Limited (“Gater”) and NAK Naftogaz Ukraine (“Naftogaz”).<sup>338</sup> AO Gazprom (“Gazprom”), a Russian state energy company, had contracted with a Ukrainian state energy company for the transport of natural gas from Russia across Ukraine to various European destinations. The contract included a clause providing for arbitration of disputes before the International Commercial Arbitration Court at the Russian Federation Chamber of Commerce and Industry (“ICAC”). After the Ukrainian energy company merged with other Ukrainian companies to form Naftogaz in 1998, Gazprom took out insurance against the risk of unauthorized withdrawals of natural gas by Naftogaz. The risk was reinsured by Monégasque de Réassurances s.a.m. (“Monde Re”). The following year, a dispute arose over Naftogaz’s unauthorized withdrawal of gas. Gazprom sought and received reimbursement from its insurer, which in turn sought and received reimbursement from Monde Re. Monde Re commenced arbitration against Naftogaz before the ICAC in April 1999. In May 2000, the tribunal rendered an award in Monde Re’s favor.<sup>339</sup>

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336. *Id.* at 772–73.

337. *Id.* at 773; *cf.* *E. D. & F. Man (Sugar) Ltd. v. Yani Haryanto* (No. 2), [1991] 1 Ll. L. Rep. 429 (Q.B.) (Eng.) (finding that public policy against drug trafficking was sufficient to overcome the public policy favoring enforcement of foreign judgments).

338. *Gater Assets Ltd. v. NAK Naftogaz Ukrainiy (Naftogaz I)*, [2006] EWHC (Comm) 460 (Eng.), *enforced*, *Gater Assets Ltd. v. NAK Naftogaz Ukrainiy (Naftogaz II)*, [2007] EWHC (Comm) 697 (Eng.), *rev’d*, *Gater Assets Ltd. v. NAK Naftogaz Ukrainiy (Naftogaz III)*, [2007] EWCA (Civ) 988 (Eng.), *enforced*, *Gater Assets Ltd. v. NAK Naftogaz Ukrainiy (Naftogaz IV)*, [2008] EWHC (Comm) 237 (Eng.), *aff’d*, *Gater Assets Ltd. v. NAK Naftogaz Ukrainiy (Naftogaz V)*, [2008] EWCA (Civ) 1051 (Eng.).

339. *UK No. 79, Gater Assets Limited (British Virgin Islands) v. NAK Naftogaz Ukrainiy (translated as National Joint Stock Company Naftogaz of Ukraine)*, 33 Y.B. COM. ARB. 721, 721–22 (2008) [hereinafter *Naftogaz Case Comment*].

Naftogaz attempted to have the award set aside in Russia but failed for lack of grounds on which a foreign arbitral award may be set aside.<sup>340</sup> Monde Re was equally unsuccessful in its attempt to have the award enforced in the US.<sup>341</sup> In 2006, Monde Re assigned the award to Gater, which sought enforcement in the UK. Naftogaz sought to prevent enforcement and argued that the award was unenforceable on grounds of public policy because, Naftogaz alleged, it had been procured by fraud. Naftogaz claimed that the complete text of the reinsurance agreement, which was purported to show that Monde Re undertook no risk, had been intentionally withheld from the tribunal. According to Naftogaz, the agreement was not an insurance contract but, in fact, “a structure allowing Gazprom to seek payment from former Eastern Bloc partners without any political implication.”<sup>342</sup> Naftogaz alleged that Monde Re had given the arbitrators “an unsigned reinsurance contract in conventional terms whilst suppressing a document in the same terms which was signed only after the occurrence of the insured event and two addenda to the contract which completely changed its character.”<sup>343</sup>

In *Naftogaz I*, the High Court granted an *ex parte* enforcement order which Naftogaz applied to have set aside. In *Naftogaz II*, the High Court was asked to order Gater to pay a security for Naftogaz’s costs. The court reasoned that the allegations of fraud had to be considered. If Naftogaz’s allegations were true, the effect would be that “certainly as a matter of English law the transaction . . . is not a contract of insurance at all.”<sup>344</sup> The High Court held that Naftogaz had succeeded in showing a *prima facie* case of fraud and ordered Gater to pay the requested security.<sup>345</sup>

Gater appealed the *Naftogaz II* ruling, and the Court of Appeal reversed the High Court’s decision, holding that “the ordering of security for costs [. . .] was wrong in principle.”<sup>346</sup> Allowing an award-debtor to obtain security for costs to challenge the validity of an arbitral award on grounds of public policy would be “counter-intuitive,” the

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340. *See id.* (“On 21 March 2001, the Moscow City Court held that under [Russian law] an award may be annulled only on proof of certain listed grounds [equivalent to those contained in Article V of the New York Convention]. There was no such ground here. On 24 April 2001, the Russian Supreme Court affirmed this decision.”).

341. *See* Monegasque de Reassurances S.A.M. (Monde Re) v. Nak Naftogaz of Ukraine, 158 F. Supp. 2d 377 (S.D.N.Y. 2001) (dismissing action to enforce of grounds of forum non conveniens), *aff’d sub nom. In re Arbitration between Monegasque De Reassurances S.A.M. v. Nak Naftogaz of Ukraine*, 311 F.3d 488 (2d Cir. 2002) (confirming lower court dismissal of action to enforce on grounds of forum non conveniens).

342. *Naftogaz* Case Comment, *supra* note 339, at 722.

343. *Naftogaz II*, [2007] EWHC (Comm) 697, [22] (Eng.).

344. *Id.* at [23].

345. *Id.* at [26].

346. *Naftogaz III*, [2007] EWCA (Civ) 988, [76] (Eng.).

court reasoned.<sup>347</sup> In effect, the lower court had made enforcement of the award contingent on Gater's payment of security. Under section 103 of the EAA, paralleling the text of the New York Convention, a UK court can refuse recognition or enforcement of an award "only if one of the exceptions within Article V is made good."<sup>348</sup> Failure to provide security was not one of those exceptions. The Court of Appeal did not reach the question of whether the lower court had jurisdiction to order security, but rather held that notwithstanding the serious allegations of the fraud, there were not sufficient reasons in the case for it to do so.<sup>349</sup>

Following its defeat in the Court of Appeal, Naftogaz sought to have the outstanding *ex parte* enforcement order set aside by the High Court in *Naftogaz IV*.<sup>350</sup> However, Judge Tomlinson was less indulging than Judges Colman and Field had been in *Naftogaz I* and *Naftogaz II*. Judge Tomlinson opined that "nothing short of reprehensible or unconscionable conduct will suffice to invest the court with discretion to consider denying to the award recognition or enforcement."<sup>351</sup> Because the Russian courts had concluded that there had been no intentional misleading of the arbitrators<sup>352</sup> and Naftogaz could not show that "anyone . . . engaged in reprehensible or unconscionable conduct in an attempt to mislead the arbitral tribunal," the High Court held that there was no basis upon which it could set aside the enforcement order."<sup>353</sup> In *Naftogaz V*, the Court of Appeal affirmed.<sup>354</sup>

#### **4.2.2.3 UK courts will refuse enforcement of an award invalidated by a foreign judgment only where recognition would be impeachable for fraud, contrary to natural justice, or contrary to public policy**

English courts have taken an approach similar to that employed by the Southern District of New York court in *Sea Dragon* when considering the effect of a foreign judgment invalidating an arbitral award. Such an award "should be enforced only if recognition of the order setting aside the order would be impeachable for fraud or as being contrary to natural justice, or otherwise contrary to public policy."<sup>355</sup>

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347. *Id.* at [72].

348. *Id.* at [81] (internal quotes omitted).

349. *Id.* at [88].

350. *Naftogaz IV*, [2008] EWHC (Comm) 237 (Eng.).

351. *Id.* at [41].

352. *Id.* at [65].

353. *Id.* at [68].

354. *Naftogaz V*, [2008] EWCA (Civ) 1051, [6] (Eng.).

355. DICEY, MORRIS & COLLINS: THE CONFLICT OF LAWS § 16:143 (Lawrence Collins et al. eds., 14th ed. 2010).



### **4.3 Application of French law regarding public policy exception to enforcement of awards**

Section 4.3 considers the application of public policy exceptions in France, a civil law country. First, in subsection 4.3.1, consideration is given to France's unique differentiation of domestic and international public policy. As discussed below, both types of public policy are defined and understood from a French perspective. In subsections 4.3.2 and 4.3.3, challenges to domestic and international arbitral awards, respectively, on grounds of substantive public policy are examined. Paragraph 4.3.3.1 considers whether illegality of the underlying agreement suffices for a challenge to the recognition or enforcement of an arbitral award in France. Finally, in paragraph 4.3.3.2, the effect that a foreign judgment or decree invalidating an arbitral award or the underlying obligation has on enforcement proceedings in French courts is considered.

#### **4.3.1 France uniquely differentiates between public policy and international public policy, employing the latter in challenges to the recognition or enforcement of foreign awards**

The understanding of public policy in France can be considered transnational. An arbitration agreement is held to be valid unless it is in conflict with fundamental principles of public policy.<sup>356</sup> The N.C.P.C., for example, allows awards to be set aside if the recognition or execution is contrary to international public policy. French law thus differentiates between domestic and international public policy, the latter concept embodying a stricter approach to public policy.

Domestic public policy in France is comprised of rules in the public interest which parties may not disregard.<sup>357</sup> Article 6 of the Civil Code provides: "*On ne peut déroger, par des conventions particulières, aux lois qui intéressent l'ordre public et les bonnes moeurs* (It is not permitted to derogate, by agreement, from laws which are matters of public policy or concern accepted standards of moral behavior)."<sup>358</sup> The Code Civil does not define *ordre public*, and for the more than two hundred years Article 6 has been part of French law, courts have reinterpreted *ordre public* "in the light of changing social and economic conditions, attitudes, and ideas."<sup>359</sup> Unlike the English and American interpretation of public policy as something apart from black letter law, French courts

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356. Mourre, *supra* note 124, at 21.

357. See DELVOLVÉ ET AL., *supra* note 21, at 153.

358. CODE CIVIL [C. CIV.] art. 6 (Fr.).

359. DELVOLVÉ ET AL., *supra* note 21, at 153.

consider *lois* (enacted laws) as a source of *ordre public*.<sup>360</sup> Scholars have noted, however that “only the fundamental notions of the French . . . legal system[] can be regarded as belonging to public policy.”<sup>361</sup>

“International public policy” is something of a misnomer in the French context. It would be more accurately labeled “French international public policy.” It does not designate the public policy of the international community, but rather the public policy of France in the world, consisting of French private international law rules applicable in international situations and in the French public interest.<sup>362</sup> However, international public policy is not a mere addendum to *ordre public* but “an integral part of French law.”<sup>363</sup> Rules of *ordre public* can be separated in three categories: protective public policy rules, which prohibit or require something in the interest of a particular class of persons or things; mandatory rules of law, which safeguard the social, economic, and political organization of France; and “fundamental principles of the universal justice,” which are accepted—if not necessarily respected—by most nations.<sup>364</sup> International public policy falls within the third category. Thus, *ordre public* is a broader set of rules than international public policy, and not every breach of it will justify refusing to recognize or enforce a foreign arbitral award.<sup>365</sup>

#### **4.3.2 Application of French law regarding public policy exception to enforcement of awards in domestic arbitration**

To be enforceable in France, an arbitral award must be brought before a French national court. The *juge de l'exequatur* (the judge before whom the application for enforcement is sought) may issue *l'exequatur* (the order for enforcement) following the procedure provided in the New Code of Civil Procedure.<sup>366</sup> Unlike the leave to enforce provided in the English Arbitration Act,<sup>367</sup> the *exequatur* is an actionable judgment—i.e., the successful party can have it executed without further court process.

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360. *Id.*

361. Hanotiau & Caprasse, *supra* note 29, at 730.

362. DELVOLVÉ ET AL., *supra* note 21, at 153.

363. *Id.*

364. *Id.* at 154–55 (citing Cour de cassation [Cass.] [supreme court for judicial matters] 1e civ., May 25, 1948, *Lautour v. Guirand*, 1949 REV. CRIT. DIP 89 (Fr.)) (“[Fundamental principles of universal justice] were basis of the judgment of the Cour de cassation in the *Lautour* case.”).

365. *See, e.g.*, FOUCHARD, GAILLARD, GOLDMAN ON INTERNATIONAL COMMERCIAL ARBITRATION 996 (E. Gaillard & J. Savage eds., 1999); Hanotiau & Caprasse, *supra* note 29, at 730.

366. *See* DELVOLVÉ ET AL., *supra* note 21, at 189.

367. Arbitration Act, 1996, c. 23, § 66(1) (U.K.).

In domestic arbitration in France, every mandatory rule of French law, including enacted *lois*, is considered to be a rule of public policy. Arbitral tribunals must apply pertinent rules of public policy when adjudicating on the merits of a dispute.<sup>368</sup> Where they have failed to do so properly and enforcement of a domestic arbitral award would be contrary to such a rule, an application for its annulment will be granted.<sup>369</sup>

### **4.3.3 Application of French law regarding public policy exception to enforcement of awards in international arbitration**

#### **4.3.3.1 *Illegality of the underlying contract leads French court to refuse enforcement***

In *European Gas Turbines*, the Paris Court of Appeal made clear the position of French courts with respect to enforcement of arbitral awards where the underlying contract is illegal: “in general, French courts would reject any application to enforce or recognize in France an award which would give effect to, or encourage illegal deals in arms or drugs, criminal activity, religious or racial or sexual discrimination, or any violation of human rights.”<sup>370</sup> French courts’ rejection can be compared to the logic employed by the English court in *Soleimany v Soleimany*. In that case, the court refused to enforce an award under Jewish law because the underlying obligation, while legal under Jewish law, was illegal under English law. French courts would similarly refuse to enforce an award where the underlying obligation conflicts with French law—if that rule of French public policy extends to international situations. In *Lautour*, the judge reasoned that French *ordre public* would be infringed if the application of a foreign rule conflicts with “principles of universal justice which French public opinion considers as having absolute international value.”<sup>371</sup> While the language was more grandiose than that used by the English lord, the result is the same: even if the underlying contract is permissible under the law governing the agreement, enforcement will be refused if the underlying contract is illegal under the rules of the enforcing State.

However, whilst every rule of international public policy is a rule of *ordre public*, the reverse is not necessarily true.<sup>372</sup> Some rules of *ordre public* are not applicable

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368. See DELVOLVÉ ET AL., *supra* note 21, at 155–56.

369. See *id.* at 156 and 258.

370. *Id.* at 259–60 (quoting Cour d’appel [CA] [regional court of appeal] Paris, Sept. 30, 1994, *European Gas Turbines SA v. Westman Int’l Ltd.*, 1994 REV. ARB. 359 (Fr.)).

371. Cour de cassation [Cass.] [supreme court for judicial matters] 1e civ., May 25, 1948, *Lautour v. Guirand*, 1949 REV. CRIT. DIP 89 (Fr.).

372. DELVOLVÉ ET AL., *supra* note 21, at 153.

internationally. For example, “gold clauses”—contractual provisions intended to limit the effects of currency depreciation—are barred in domestic French contracts because they are considered contrary to *ordre public*. In international transactions, however, “gold clauses” are permissible because their prohibition is not considered a principle of universal justice having absolute international value.<sup>373</sup>

Even where a rule of public policy is considered international public policy, French courts apply it narrowly, as exemplified by the Paris Court of Appeals in *Thalès v. Euromissile*.<sup>374</sup> The arbitral award at issue in *Thalès* ordered Thalès to pay damages to Euromissile over a licensing dispute. Neither party alleged an incompatibility of the agreement with EU law, and the arbitrators had not brought it up on their own. However, Thalès filed a request for vacatur before the court, arguing that the underlying agreement was in breach of EU competition law, thereby placing the resulting award in violation of international public policy.<sup>375</sup> The court referred to the *Eco Swiss* judgment and confirmed that Article 101 TFEU constituted international public policy.<sup>376</sup> The court further reasoned that a violation of Article 101 TFEU could result in an award being successfully vacated or refused recognition or enforcement. The court noted, however, that the CJEU had recognized the principle of procedural autonomy of the Member States. The court concluded that French procedural law could thus be applied. It noted that despite the parties having failed to raise the issue during the arbitral proceedings, a court could still exercise control because respect for mandatory rules of EU law “should not be conditioned by the attitude of the parties.” However, the court held that a “judge cannot . . . in the absence of fraud . . . carry out an examination of the application of competition law to the disputed contract.” Commentators have remarked that *Thalès* “clarifies the *Eco Swiss* decision” by stating that an award cannot be invalidated because the arbitral tribunal failed to raise potential violations of EU competition law.<sup>377</sup>

Other French courts have come to similar conclusions. In *Société SNF SAS v. Société Cytec Industrie*, the Paris Court of Appeals considered the effect on the award of an

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373. See Cour de cassation [Cass.] [supreme court for judicial matters] May 17, 1927, *Pélicier du Besset v. The Algiers Land and Warehouse Co.*, D.P. I, at 25 (Fr.); see also DELVOLVÉ ET AL., *supra* note 21, at 5, 153–54; POUDRET & BESSON, *supra* note 95, at 31.

374. Cour d’appel [CA] [regional court of appeal] Paris, 1e ch., Nov. 18, 2004, *SA Thalès Air Défense v. GIE Euromissile*, 2005 REV. ARB. 751 (Fr.).

375. See Liebscher, *supra* note 143, at 792.

376. TEC, *supra* note 184, art. 81 (as in effect 1999) (now TFEU, *supra* note 184, art. 101). Article 101 TFEU prohibits “all agreements and concerted practices which may affect trade between [EU] Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market.”

377. Liebscher, *supra* note 143, at 793.

alleged violation of EU competition law that had been argued before the arbitral tribunal.<sup>378</sup> The court held that it could not substitute its view for that of the tribunal “in the absence of flagrant, real and concrete violation of international public policy.” Its decision was affirmed by the Cour de Cassation.<sup>379</sup>

**4.3.3.2 *French courts will enforce an arbitral agreement or award invalidated by a foreign judgment or decree because France, uniquely, does not extend judicial comity to foreign judgment concerning arbitral awards***

Whereas in *Sea Dragon*, a court in the US employed the US public policy in favor of judicial comity to refuse the enforcement of an arbitral award ordering the violation of Dutch law, French courts do not extend judicial comity to foreign judgments concerning arbitral awards.<sup>380</sup> France’s approach is unique and has been criticized as creating a lack of uniformity in the application of the New York Convention.<sup>381</sup> The approach is rooted in the notion that an international arbitral award has legal force independent of the authority of the courts at the place of arbitration or of those under whose law it was rendered. From this perspective, an international arbitral award is a binding decision on the parties, made by a private tribunal empowered by the parties to affect their rights and obligations; it is the result of an agreement between private parties, not the product of “a judicial organ of any state.”<sup>382</sup> Because the parties chose arbitration over litigation, they—at least impliedly—agreed to exclude the national courts of the place of arbitration from the resolution of the dispute. Thus, the parties intended that the courts would not be able to make a declaration as to the award’s validity that would be binding in the courts of other countries.<sup>383</sup>

France’s approach reflects the concern that a party seeking to avoid enforcement would be unfairly advantaged if were able to prevent the enforcement of the award in every country simply because the award had been invalidated in the courts of its origin.<sup>384</sup> While courts at the origin of the award have the authority under the New York Convention

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378. Cour d’appel [CA] [regional court of appeal] Paris, Mar. 23, 2006, *Société SNF SAS v. Société Cytec Industries BV*, 2006 REV. ARB. 483 (Fr.).

379. Cour de cassation [Cass.] [supreme court for judicial matters] 1e civ., June 4, 2008, *SAS SNF v Société Cytec Industries BV*, 2008 REV. ARB. 473 (Fr.).

380. *See DELVOLVÉ ET AL.*, *supra* note 21, at 218.

381. *See id.* at 210 (noting that while the French approach does lead to a lack of uniformity, “diversity of application is inherent in the very text of the Convention, so that the French approach properly accords with both its aims and text”).

382. *See id.* at 218.

383. *Id.* at 219.

384. *See id.*; *see also* Timo Kaksonen, *Enforcement of Foreign Vacated Arbitral Awards in Finland – contra legem or pro arbitri*, Helsingin yliopisto 2012.

to set aside the award under their national laws, in the French understanding, they do not have the ability to give that decision “extra-territorial effect.”<sup>385</sup>

## **5 TRENDS IN THE US AND THE EU**

In the US, the Federal Arbitration Act has limited the ability of US states to use public policy rules to regulate or prevent arbitration of particular issues. The US Supreme Court recently held that a California consumer protection law prohibiting class action arbitration waivers was preempted by the FAA.<sup>386</sup> Similarly, the US Supreme Court has held that disputes implicating antitrust law can be decided in international arbitration. In Europe, the movement to unify laws amongst the Member States has gone in the opposite direction. European regulations and directives on consumer protection and competition law have worked to prevent arbitration of issues that could be arbitrated under the Member States’ domestic law. Thus, whereas in US, the expansion of federal legislation liberalizes arbitration; in the EU, the expansion of “federal” legislation has limited its scope. It is paradoxical that federal law in US that is largely been unchanged since 1925 allows for more liberal policy towards arbitration than that of the regulations and directives of the EU.

In the EU, public policy has been increasingly relied upon where EU law intersected with commercial arbitration.<sup>387</sup> Two particularly well-known areas in which EU public policy has had an effect on arbitration are antitrust (competition) law and consumer law. Part 5 discusses the approaches to these areas from US and EU perspectives. In section 5.1, antitrust law is considered, and, in section 5.2, the focus shifts to consumer law—consumer contracts in particular.

### **5.1 The permissive attitude toward arbitration of antitrust disputes in the US can be contrasted with the restricted possibility for disputes involving competition law to be decided in arbitration in the EU**

The permissive attitude toward arbitration of antitrust disputes, as exemplified by the US Supreme Court’s decisions in *Mitsubishi Motors* and *Baxter*, is considered in subsection 5.1.1. It is contrasted, in subsection 5.1.2, with the approach in the EU that views mandatory provisions of EU competition law as a part of EU public policy that cannot be entrusted solely to arbitrators.

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385. DELVOLVÉ ET AL., *supra* note 21, at 220.

386. *AT&T Mobility*, 131 S.Ct. 1740 (2011).

387. *See van der Haegen*, *supra* note 169, at 450.

### 5.1.1 Permissive attitude to arbitration of antitrust disputes in the US

The US Supreme Court allowed for the arbitrability of antitrust disputes in *Mitsubishi Motors*, making a sharp departure from the judicial distrust of arbitration of antitrust disputes exemplified by *American Safety*.<sup>388</sup> The Court declined to address *American Safety*'s continued applicability in domestic arbitrations, but forthrightly denied its relevance in international disputes.<sup>389</sup>

Blanke & Landolt argue that the US Supreme Court's endorsement of arbitrability in *Mitsubishi* was based on the legal order's trust in arbitrators, rather than on the ability of courts to verify that the arbitrators have properly applied antitrust laws.<sup>390</sup> Indeed, over time, the *Mitsubishi Motors* decision has been repeatedly enforced in the lower courts and extended to include domestic arbitrations.

In *Gemco*, the Southern District of New York opined that the "foundations of the *American Safety* doctrine [had] been significantly eroded" and predicted its eventual demise.<sup>391</sup> Several years later, the court stated that "the reasoning of *Mitsubishi* should apply with equal force to domestic claims."<sup>392</sup> *American Safety* was then explicitly overruled at the federal appellate level by the Ninth Circuit in 1994. In *Ngheim*, the Ninth Circuit stated that it was persuaded that *Mitsubishi Motors* was not restricted to the international context because the US Supreme Court had subsequently cited *Mitsubishi Motors* for the general proposition that antitrust claims could be arbitrated in *Gilmer*; specifically refuted the *American Safety* analysis in *Mitsubishi Motors*; and dismissed as unfounded the theory supporting the *American Safety* doctrine that the private cause of action is fundamental to enforcing antitrust laws.<sup>393</sup>

The recent *Baxter* case presents a striking example of how far the federal courts are willing to go in favor of the arbitration of antitrust disputes. *Baxter* involved a dispute between Abbott Laboratories ("Abbott") and Baxter International ("Baxter"), a pharmaceutical company. In the 1960s, Baxter invented sevoflurane, an anesthetic gas.<sup>394</sup> At the time, Baxter was unable to commercially exploit sevoflurane, and it was not until

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388. See *American Safety*, 391 F.2d 821 (2d Cir. 1968).

389. *Mitsubishi Motors*, 473 U.S. 614, 629 (1985) ("We find it unnecessary to assess the legitimacy of the *American Safety* doctrine as applied to agreements to arbitrate arising from domestic transactions.").

390. Mourre, *supra* note 124, at 29.

391. *Gemco Latinoamerica, Inc. v. Seiko Time Corp.*, 671 F. Supp. 972, 979 (S.D.N.Y. 1987).

392. *Hough v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 757 F. Supp. 283, 286 (S.D.N.Y. 1991) *aff'd sub nom.*, *Hough v. Merrill Lynch*, 946 F.2d 883 (2d Cir. 1991).

393. *Nghiem v. NEC Elec., Inc.*, 25 F.3d 1437, 1441–42 (9th Cir. 1994) (citing *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20, 26–27 (1991); *Mitsubishi Motors*, 473 U.S. at 632).

394. *Baxter Int'l, Inc. v. Abbott Laboratories*, 315 F.3d 829, 830 (7th Cir. 2003).

the 1980s that Baxter developed a cost-effective production process, for which it received two process patents. However, because it was unwilling to bear the costs of required medical testing in the US, Baxter granted an exclusive worldwide license to the sevoflurane process patents to Maruishi Pharmaceutical Company of Japan (“Maruishi”). Sevoflurane proved to be very profitable for Maruishi, inspiring many other companies to attempt to develop alternative production methods that would not impinge on the process patents. One such company was successful and, after obtaining a process patent for its new development method, it was acquired by Baxter in 1998. Baxter had concluded that it would make more selling sevoflurane manufactured via the new process than it would lose in royalties on reduced sales of the Maruishi sevoflurane.

Abbott, the reseller of Maruishi sevoflurane in the US, was chagrined at the prospect of competition in the US market before the expiry of the original process patents. It initiated arbitration proceedings under the Baxter-Maruishi agreement, to which it had become a party in 1992, and the New York Convention.<sup>395</sup> Abbott argued that Baxter’s sale of sevoflurane manufactured via the new process would violate the exclusivity term of the Maruishi license. Baxter responded that the license prevented it from issuing any further licenses but did not expressly prohibit it from competing with Maruishi. Baxter further argued that if the license did forbid it from competing, it was in violation of section 1 of the Sherman Act and thus unenforceable.<sup>396</sup> The three-member arbitral tribunal sided with Abbott on both issues. It held that the exclusivity term prevented Baxter from competing with Maruishi and that Baxter was responsible for any reduction in competition attributable to its acquisition of a company manufacturing sevoflurane through a new process.<sup>397</sup>

Abbott sought to enforce and Baxter sought to prevent the enforcement of the award in the Northern District of Illinois. The district judge ordered Baxter to comply with the award, rejecting Baxter’s argument that the license violated the Sherman Act and was unenforceable.<sup>398</sup> Baxter appealed the Northern District of Illinois’ decision before the Seventh Circuit, arguing that construing the license to keep sevoflurane manufactured through the new process off the US market was a territorial allocation unlawful under the Sherman Act. The Seventh Circuit rejected even the assumption underlying Baxter’s

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395. *Baxter*, 315 F.3d at 831.

396. *Id.* (citing Sherman Antitrust Act, ch. 647, 29 Stat. 209 (1890) (codified as amended at 15 U.S.C. § 1 *et seq.* (2012))).

397. *Id.*

398. *Abbott Laboratories v. Baxter Int’l Inc.*, No. 01 C 4809, 2002 WL 467147, \*1 (N.D. Ill. Mar. 27, 2002), *aff’d sub nom. Baxter*, 315 F.3d. 829.



argument: that Baxter was entitled to reargue an issue decided by the arbitral tribunal.<sup>399</sup> It reasoned that section 207 of the FAA required a court to confirm a foreign award unless it finds one of the grounds for refusal of recognition or enforcement expressly provided in the Convention. Because those grounds did not include mistake of law, the Seventh Circuit held that it had to confirm the award.<sup>400</sup>

In the *Baxter* decision, the Seventh Circuit opined on the practice of arbitrators deciding antitrust disputes. It noted, “[a]rbitrators regularly handle claims under federal statutes,” and rejected the notion that “things should be otherwise for antitrust issues.”<sup>401</sup> The Seventh Circuit reasoned that the US Supreme Court in *Mitsubishi Motors* found the international arbitration of antitrust disputes to be appropriate and that rearguing the antitrust issue, as Baxter proposed, “would subvert the promises the United States made by acceding to the [New York] Convention.”<sup>402</sup>

### **5.1.2 Restricted ability to arbitrate disputes involving European competition law**

It is often proposed that the principles of European competition law are the most cogent expression of European public policy.<sup>403</sup> Lending considerable weight to this claim is the CJEU’s judgment in *Eco Swiss China Time Ltd. v. Benetton International NV*.<sup>404</sup>

In *Eco Swiss*, questions referred to CJEU were raised in proceedings brought by Benetton International NV (“Benetton”) for stay of enforcement of an arbitration award ordering it to pay damages to Eco Swiss China Time Ltd (“Eco Swiss”) for breach of a licensing agreement concluded with the latter, on the ground that the award in question was contrary to public policy within the meaning of the Dutch Code of Civil Procedure by virtue of the nullity of the licensing agreement under Article 101 TFEU.<sup>405</sup>

Benetton, a Dutch company, signed an eight-year licensing agreement with Eco Swiss, a Hong Kong company, and Bulova Watch Company, an American corporation.<sup>406</sup>

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399. *Baxter*, 315 F.3d at 831.

400. *Id.* (citing *George Watts & Son, Inc. v. Tiffany & Co.*, 248 F.3d 577 (7th Cir. 2001)).

401. *Id.* at 831–32.

402. *Id.* at 832.

403. Bermann 2012, *supra* note 178, at 411; Liebscher, *supra* note 143, at 790.

404. *Eco Swiss*, 1999 E.C.R. I-3055 (1999). *See also* Joined Cases C-295, C-296, C-297 & C-298/04, *Vincenzo Manfredi v. Lloyd Adriatico Assicurazioni SpA, Antonio Cannito v. Fondiaria Sai SpA, and Nicolò Tricarico, Pasqualina Murgolo v. Assitalia SpA*, 2006 E.C.R. I-6619, ¶ 31 (“Articles [101 and 102 TFEU] are a matter of public policy which must be automatically applied by national courts.”).

405. *Eco Swiss*, 1999 E.C.R. I-3055, ¶ 2. At the time of the *Eco Swiss* decision, TFEU, *supra* note 184, art. 101 was in effect as TEC, *supra* note 184, art. 81. For sake of clarity, Article 101 TFEU is referred to in the text.

406. *Eco Swiss*, 1999 E.C.R. I-3055, ¶ 9.

The agreement granted Eco Swiss the right to manufacture watches bearing the “Benetton by Bulova” label, to be sold by Eco Swiss and Bulova.<sup>407</sup> The agreement provided that all disputes arising between Benetton, Eco Swiss, and Bulova were to be settled by arbitration according to the rules of the Nederlands Arbitrage Instituut and under Dutch law.<sup>408</sup> Benetton terminated the agreement after only five years, giving rise to arbitral proceedings between the parties.<sup>409</sup>

After being ordered to compensate Eco Swiss and Bulova for damages they had suffered as a result of the early termination, Benetton applied for annulment of the award on that ground that it was contrary to public policy by virtue of the nullity of the licensing agreement under Article 101 TFEU.<sup>410</sup> At no point in the arbitral proceedings had Benetton raised the question whether the licensing agreement was void under Article 101 TFEU.<sup>411</sup> When its application for a stay was denied by the Rechtbank, Benetton appealed to the Gerechtshof, which proved more sympathetic, ruling that the final arbitration award could be held contrary to public policy and thus granting the application for a stay.<sup>412</sup> Eco Swiss countered with proceedings in cassation before the Hoge Raad.<sup>413</sup> The Hoge Raad noted that an arbitration award is contrary to public policy under Dutch law only if its enforcement would violate a “mandatory rule so fundamental that no restrictions of a procedural nature should prevent its application.”<sup>414</sup> The “mere fact that, because of the terms or enforcement of an arbitration award, a prohibition laid down in competition law is not applied is *not* generally regarded as being contrary to public policy.”<sup>415</sup> The Hoge Raad reasoned that neither party had raised the Article 101 TFEU issue during the arbitration proceedings and that the arbitrators would have been exceeding their authority, opening their award to possible annulment, had they brought it up on their own.<sup>416</sup> However, it referred a number of questions to the CJEU for preliminary rulings, including, *inter alia*, whether a court must set aside an award that it considers contrary to Article 101 TFEU notwithstanding limits imposed by Member State procedural law.<sup>417</sup>

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407. *Id.*

408. *Id.* ¶ 10.

409. *Id.* ¶ 11.

410. *Id.* ¶¶ 12–13.

411. *Id.* ¶ 26.

412. *Id.* ¶¶ 17–22.

413. *Id.* ¶ 23.

414. *Id.* ¶ 24.

415. *Id.* ¶ 2 (emphasis added).

416. *Id.* ¶ 26.

417. *Id.* ¶ 30.

The CJEU addressed the reference by reiterating its position in *Nordsee* that an arbitration tribunal is not a “court or tribunal of a Member State” within the meaning of Article 267 TFEU and is therefore not able to refer questions to the CJEU.<sup>418</sup> The court stated that, in the interest of efficient arbitration proceedings, review of arbitration awards should be limited and refusal to recognize or enforce award should be occur only in exceptional circumstances.<sup>419</sup>

Those concerns, however, were trumped by the fact that Article 101 TFEU represented “a fundamental provision which is essential for the accomplishment of the task entrusted to the [EU] and, in particular, for the functioning of the internal market.”<sup>420</sup> Because arbitrators are not able to refer questions of law to the CJEU, it is in the interest of the EU that questions concerning Article 101 TFEU be examined by Member State courts and referred to the CJEU where necessary.<sup>421</sup>

The CJEU noted that the purposes of Article 101 TFEU were so vital to the European project that it led the framers of the Treaty to provide expressly in Article 101(2) TFEU that any agreements prohibited pursuant to it would be “automatically void.”<sup>422</sup> Article 101 TFEU, the court reasoned, could be regarded as a matter of public policy under Article V(2)(b) of the New York Convention.<sup>423</sup> The court held that where the procedural law of a Member State required a court to grant an application for annulment on grounds that the award violated national public policy, the Member State was required to also grant an application on grounds that the award failed to comply with Article 101(1) TFEU.<sup>424</sup>

Clearly a disparity exists between arbitration of disputes involving antitrust (competition) laws in the US as in the EU. Scholars, however, have noted that arbitration poses no threat to the enforcement of EU competition policy, just the US Supreme Court found arbitration not to endanger the enforcement of US antitrust laws.<sup>425</sup> In the following section, the treatment of consumer protection laws in the US and the EU in respect of arbitration is discussed.

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418. *Id.* ¶ 34 (citing Case C-102/81, *Nordsee Deutsche Hochseefischerei GmbH v Reederei Hochseefischerei Nordstern AG & Co KG*, 1982 E.C.R. 1095, ¶¶ 10–12)). At the time of the *Eco Swiss* decision, TFEU, *supra* note 184, art. 267 was in effect as TEC, *supra* note 184, art. 234. For sake of clarity, Article 267 TFEU is referred to in the text.

419. *Eco Swiss*, 1999 E.C.R. I-3055, ¶ 35.

420. *Id.* ¶ 36.

421. *Id.* ¶ 40.

422. *Id.* ¶ 36.

423. *Id.* ¶ 39.

424. *Id.* ¶¶ 37, 41.

425. Brozolo, *supra* note 1, at 782.

## **5.2 Whereas US state consumer law does not stand in the way of US federal policy favoring arbitration, EU consumer law does stand in the way of Member State rules compelling such arbitration**

Scholars have noted that the arbitration of disputes involving consumer contracts presents “a very special problem.”<sup>426</sup> Consumer contracts often arise from the day-to-day transactions of consumers, and, if in writing, are usually standard form contracts, or, in more pejorative terms, contracts of adhesion.<sup>427</sup> Such contracts tend to be “extremely one-sided,” favoring sellers and suppliers against consumers.<sup>428</sup> Whether from manifest weakness in bargaining position, ignorance, or indifference, consumers regularly enter into lopsided contracts of adhesion.<sup>429</sup> These contracts are rarely negotiated and may not be fully understood by the consumers agreeing to their terms.<sup>430</sup> A consumer’s only alternative to “complete adherence” to contract of adhesion is often limited to “outright rejection.”<sup>431</sup> The insertion of an arbitration clause into a lengthy consumer contract can effectively limit a consumer’s avenues of relief under the contract.

Whereas a liberal approach to arbitration of consumer contracts has recently dominated in the US, the opposite tact has gained prevalence in the EU. The current jurisprudence of the US is discussed below in subsection 5.2.1, followed by an explanation of the situation in Europe in subsection 5.2.2.

### **5.2.1 US state public policy expressed in consumer protection laws prohibiting mandatory arbitration of consumer contracts is preempted by the federal policy favoring arbitration of contractual disputes**

In paragraph 5.2.1.1, the former treatment of arbitration of contracts of adhesion under California law is explained. *AT&T Mobility*, in which the US Supreme Court held California’s approach to be pre-empted under the FAA, is discussed in paragraph 5.2.1.2.

#### **5.2.1.1 *Pre-empted California State approach***

In the *Discover Bank* decision, the Supreme Court of California held that the mandatory waiver of class arbitration in consumer contracts of adhesion is unconscionable

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426. Otto & Elwan, *supra* note 303, at 360.

427. A contract of adhesion or adhesion contract is a “standard form contract prepared by one party, to be signed by another party in a weaker position, usually a consumer, who adheres to the contract with little choice about the terms.” BLACK’S LAW DICTIONARY 366 (9th ed. 2011).

428. QUINTIN JOHNSTONE & DAN HOPSON JR., *LAWYERS AND THEIR WORK* 329–30 (1967).

429. JOHNSTONE & HOPSON JR., *supra* note 428, at 360.

430. Otto & Elwan, *supra* note 303, at 360.

431. ALLAN FARNSWORTH, *CONTRACTS* § 4.26, at 297 (3d ed. 1999).

under certain circumstances and should not be enforced by California courts.<sup>432</sup> Moreover, the court asserted that the FAA did not preempt the prohibition of class action waivers in arbitration agreements.<sup>433</sup>

At issue in *Discover Bank* was the validity of a provision in an arbitration agreement between Discover Bank and Christopher Boehr, a California resident and credit cardholder, forbidding class arbitration of disputes.<sup>434</sup> Boehr alleged that Discover Bank engaged in a deceptive practice by representing to cardholders that late payment fees were not assessed if payment was received by a particular date, whereas in fact such fees were assessed if payment was received after 1:00 p.m. on that date.<sup>435</sup> Discover Bank's practice thus "[ed] to damages that were small as to individual consumers but large in the aggregate."<sup>436</sup> Boehr claimed for damages and Discover Bank moved to compel arbitration pursuant to the arbitration agreement.<sup>437</sup> Boehr then sought to decide the dispute in a class-wide arbitration, a "well accepted" practice in California.<sup>438</sup>

The arbitration agreement concluded between the parties however contained a clause forbidding class-wide arbitration of disputes.<sup>439</sup> It further stated that Delaware law and the FAA governed the agreement.<sup>440</sup> Discover Bank argued that section 2 of the FAA requires the enforcement of the arbitration clause, including class action waivers.<sup>441</sup> The dispute took a circuitous route through the California courts before ultimately arriving at the Supreme Court of California.<sup>442</sup>

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432. *Discover Bank v. Superior Court*, 30 Cal. Rptr. 3d 76, 94 (Cal. 2005), *abrogated by* AT&T Mobility LLC v. Concepcion, 131 S.Ct. 1740 (2011).

433. *Id.*

434. *Id.* at 80.

435. *Id.*

436. *Id.* at 78.

437. *Id.* at 81.

438. *Id.* at 78.

439. The clause stated that "neither you nor we shall be entitled to join or consolidate claims in arbitration by or against other card members with respect to other accounts, or arbitrate any claim as a representative or member of a class or in a private attorney general capacity." *Id.* at 79.

440. *Id.* at 79–80.

441. *Id.* at 80.

442. Initially the trial court sided with Discover Bank and granted its motion to compel arbitration, under Delaware law. *Id.* at 81. Shortly thereafter, the Fourth District Court of Appeal of California decided that a "virtually identical class action waiver was unconscionable" in *Szetela*. *See Szetela v. Discover Bank*, 118 Cal. Rptr. 2d 862 (Cal. Ct. App. 2002). Boehr sought and was granted reconsideration of his claim in light of the *Szetela* decision. *Discover Bank*, 30 Cal. Rptr. 3d at 81. The trial court found *Szetela* to constitute new and controlling authority and held that enforcing the class action waiver under Delaware law would contravene a fundamental Californian public policy. *Id.* Discover Bank appealed, seeking reinstatement of the trial court's prior order to compel arbitration. The appellate court was sympathetic, holding that the FAA preempted any state law rule prohibiting class action waivers. *Id.* The Supreme Court of California granted review. *Id.*

The Supreme Court of California discussed at length the importance of class action remedies in California law and the development of “the hybrid procedure of class-wide arbitration.”<sup>443</sup> It also noted that appellate courts had answered affirmatively to the question whether “a class action waiver may be unenforceable as contrary to public policy or unconscionable”<sup>444</sup> Considering the same rule applied to class-action waivers in arbitration agreements, the court reasoned that:

[W]hen the waiver is found in a consumer contract of adhesion in a setting in which disputes between the contracting parties predictably involve small amounts of damages, and when it is alleged that the party with the superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money, . . . the waiver becomes in practice the exemption of the party “from responsibility for [its] own fraud, or willful injury to the person or property of another.”<sup>445</sup>

Under such circumstances, the court held, class-action waivers in arbitration agreements were “unconscionable under California law and should not be enforced.”<sup>446</sup>

#### **5.2.1.2 Federal approach favoring efficient, streamlined resolution of disputes**

The US Supreme Court recently decided a challenge to the *Discover Bank* rule.<sup>447</sup> It held that California’s rule compelling class arbitration “[was] not arbitration as envisioned by the FAA, lack[ed] its benefits, and there [could] not be required by state law.”<sup>448</sup>

In 2002, AT&T Mobility LCC (“AT&T”) ran a sales campaign to advertise its services by offering free mobile phones. In 2002, Vincent and Liza Concepcion, residents of California, bought the service and received two free mobile phones. While the Concepcions had not been charged for the phones, they were billed \$30.22 for sales tax on the basis of the phones’ retail value. They filed a complaint against AT&T, which was later merged with other similar complaints in a class action against AT&T, alleging that it had

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443. *Id.* at 82 (citing *Keating v. Superior Court*, 183 Cal. Rptr. 360 (Cal. 1982) (ordering class-wide arbitration of 7-Eleven franchisors’ claims where the arbitration agreement was silent on the matter), *rev’d, appeal dismissed, Southland*, 465 U.S. 1 (1994)).

444. *Id.* at 83. In *Szetela*, the appellate court barred a contract containing a class arbitration waiver, holding the waiver to be both procedurally and substantively unconscionable. *See Szetela*, 118 Cal. Rptr. 2d at 866. The waiver violated fundamental notions of fairness and public policy “by granting Discover a ‘get out of jail free’ card while compromising important consumer rights.” *Id.* at 868. Class action waivers were subsequently found unconscionable other California case. *See, e.g., Cohen v. DirecTV, Inc.*, 48 Cal. Rptr. 3d 813, 819–21 (Cal. Ct. App. 2006); *Aral v. EarthLink, Inc.*, 36 Cal. Rptr. 3d 229, 237–38 (Cal. Ct. App. 2005); *Klussman v. Cross Country Bank*, 36 Cal. Rptr. 3d 728, 739–40 (Cal. Ct. App. 2005).

445. *Discover Bank*, 30 Cal. Rptr. 3d at 85 (quoting CAL. CIV. CODE § 1668 (West 2013)).

446. *Id.* at 87.

447. *AT&T Mobility*, 131 S.Ct. 1740 (2011).

448. *Id.* at 1753.

engaged in false advertising and fraud by charging sales tax on “free” mobile phones.<sup>449</sup> The adhesive contract between AT&T and the Concepcions authorized AT&T to make unilateral changes. It further included an arbitration clause providing for arbitration of all disputes between the parties in their “individual capacity”—i.e., not as members of a representative class.<sup>450</sup>

AT&T moved to compel arbitration under the agreement after the Concepcions failed to pay the charged amount. The Concepcions argued that the arbitration agreement was unconscionable under the *Discover Bank* rule because it included a class-action waiver.<sup>451</sup> The Southern District of California agreed, holding that the arbitration provision was unconscionable,<sup>452</sup> and the Ninth Circuit affirmed, holding that the provision was unconscionable under the *Discover Bank* rule and that the FAA did not preempt the *Discover Bank* rule because the rule was “a refinement of the unconscionability analysis applicable to contracts generally in California.”<sup>453</sup> The FAA permits arbitration agreements to be invalidated by “generally applicable contract defenses, such as fraud, duress, or unconscionability.”<sup>454</sup> The US Supreme Court granted certiorari and overturned the Ninth Circuit decisions, holding that the *Discover Bank* rule was inconsistent with the FAA, class-wide arbitration lacked the advantages of arbitration promoted by the FAA, and US state law could not require class-wide arbitration.<sup>455</sup>

Justice Scalia, writing for the US Supreme Court, reasoned that the purpose of the FAA, as evident from the statutory text, was to ensure the enforcement of arbitration agreements according to their terms “so as to facilitate streamlined proceedings.”<sup>456</sup> In light of that purpose, the Court had previously held that parties might agree to limit the issues subject to arbitration,<sup>457</sup> to arbitrate according to certain rules,<sup>458</sup> and to limit with whom a party will arbitrate.<sup>459</sup> The Court had allowed the parties discretion on these issues

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449. *Id.* at 1744.

450. *Id.*

451. *Id.* at 1745.

452. *Laster v. T-Mobile USA, Inc.*, No. 05CV1167DMS AJB, 2008 WL 5216255, at \*1 (S.D. Cal. Aug. 11, 2008), *aff’d sub nom.* *Laster v. AT & T Mobility LLC*, 584 F.3d 849 (9th Cir. 2009), *rev’d, sub nom.* *AT&T Mobility*, 131 S.Ct. 1740 (2011).

453. *Laster*, 584 F.3d at 856, *rev’d sub nom.* *AT&T Mobility*, 131 S.Ct. 1740 (2011).

454. *See, e.g., Doctor’s Associates*, 517 U.S. 681, 687 (1996); *Allied-Bruce*, 513 U.S. 265, 281 (1995); *Rodriguez de Quijas v. Shearson/Am. Exp., Inc.*, 490 U.S. 477, 483 (1989); *Shearson*, 482 U.S. 220, 226 (1987).

455. *AT&T Mobility*, 131 S.Ct. 1740

456. *Id.* at 1748.

457. *Mitsubishi Motors*, 473 U.S. 614, 628 (1985).

458. *Volt*, 489 U.S. 468, 479 (1989).

459. *Stolt-Nielsen S.A. v. AnimalFeeds Int’l Corp.*, 130 S.Ct. 1758, 1774 (2010).

to encourage “efficient, streamlined procedures tailored to the type of dispute.”<sup>460</sup> In contrast, the *Discover Bank* rule interfered with arbitration: it allowed any party to a consumer contract to demand class-wide arbitration after a dispute had already begun.

Moreover, the rule was unwieldy: it required that damages be small and the consumer to allege a scheme to cheat consumers. However, California courts had already held damages of \$4,000 to be “small,” and the allegation requirement had “no limiting effect” at all.<sup>461</sup> The rule was limited to contracts of adhesions, but as Justice Scalia commented, “[t]he times in which consumer contracts were anything other than adhesive are long past.”<sup>462</sup>

By allowing class-wide arbitration of such a vast swathe of agreements, the *Discover Bank* rule promoted a policy inconsistent with the FAA.<sup>463</sup> Class arbitration is inconsistent with the FAA because, first, it negated the informality of arbitration-- “[its] principal advantage”—by “requir[ing] procedural formality.”<sup>464</sup> Moreover, class arbitration is decidedly disadvantageous to the defendants.<sup>465</sup> Finally, as a method of dispute resolution, “[a]rbitration is poorly suited to the higher stakes of class litigation.”<sup>466</sup> Because the *Discover Bank* rule allowing class-wide arbitration did not have the purpose of enforcing arbitration agreements according to their terms, facilitating the streamlined resolution of disputes, it was pre-empted by the FAA. Class-wide arbitration thus could not be required by California law.

### **5.2.2 Mandatory arbitration provisions are “unfair terms” under EU consumer law and cannot be enforced even where Member State law holds otherwise**

Directive 93/13/EEC on Unfair Terms in Consumer Contracts (the “Unfair Terms Directive”) is a major piece of consumer legislation in the EU.<sup>467</sup> The Unfair Terms Directive purports to accomplish a partial harmonization of consumer law within EU.<sup>468</sup> It sets minimum protection for the weaker party in consumer contracts—typically consumers.

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460. *AT&T Mobility*, 131 S.Ct. at 1749.

461. *Id.* at 1750.

462. *Id.* at 1750 (citing *Carbajal v. H & R Block Tax Servs., Inc.*, 372 F.3d 903, 906 (7th Cir. 2004)).

463. *Id.* at 1751.

464. *Id.*

465. *Id.*

466. *Id.* at 1752.

467. Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts, 1993 O.J. (L 95) 29 [hereinafter Unfair Terms Directive]; see UNDERSTANDING EU CONSUMER LAW 352–53 (Hans-W. Micklitz, N. Reich, P. Rott eds., 2009) [hereinafter EU CONSUMER LAW].

468. EU CONSUMER LAW, *supra* note 467, at 127.



Moreover, the Unfair Terms Directive aims to promote and enhance cross-border trade amongst the Member States and to combat distortions of competition law.

The Unfair Terms Directive applies to “unfair terms” included in contracts of adhesion, pre-formulated terms, and individual terms.<sup>469</sup> As discussed above, contracts of adhesion—referred to as “standard terms” in the Directive—are contracts including standard business conditions that are pre-formulated for repeated use by the offeror against consumers.<sup>470</sup> Pre-formulated terms are those that have not been individually negotiated but which on their own do not exclude the application of the Directive to the rest of the contract if an overall assessment indicates that it is a contract of adhesion.<sup>471</sup> Individual terms are less common. Micklitz has remarked, “[i]t is difficult to understand . . . when such individual terms in consumer contracts exist.”<sup>472</sup> Through case law, the CJEU concluded that it is within the power of a Member State court to, of its own motion, make a preliminary assessment as to whether a contract term is unfair before admitting a claim on that basis.<sup>473</sup> When a Member State court finds that an unfair term renders a consumer contract void, it cannot, however, make that determination subject to the consumer’s observation of a notice period.<sup>474</sup>

The Unfair Terms Directive covers only business-to-consumer transactions. The concept of a “consumer” in the Unfair Terms Directive is similar to that employed in other European Directives: “any natural person who . . . is acting for purposes which are outside his trade, business or profession.”<sup>475</sup> The CJEU has strictly interpreted “consumer” to focus on the Directive’s protective purposes. The term excludes self-employed persons and includes only natural persons.<sup>476</sup> The seller or supplier with whom the consumer contracts may be “any natural or legal person who . . . is acting for purposes relating to his trade, business or profession, whether publicly owned or privately owned.”<sup>477</sup>

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469. See Unfair Terms Directive, *supra* note 467, art. 2(a), art. 3.

470. With regard to contracts of adhesion, the Directive shifts the burden of proof to prove a contract term has been individually negotiated to the seller or supplier. See Unfair Terms Directive, *supra* note 467, art. 3(2). It also requires Member States to introduce special procedures with regard to standard terms so that contractual terms “drawn up for general use” may be removed from the contracts. See *id.* art. 7(2).

471. Unfair Terms Directive, *supra* note 467, art. 3(1).

472. See EU CONSUMER LAW, *supra* note 467, at 129.

473. Joined Cases 240 & 244/98, *Océano Grupo Editorial and Salvat Editores*, 2000 E.C.R. I-4941, at ¶ 29.

474. Case C-474/00, *Cofidis SA v Jean-Louis Fredout*, 2002 E.C.R. I-10875, at ¶ 38.

475. Unfair Terms Directive, *supra* note 467, art. 2(b).

476. See Joined Cases 541 & 542/99, *Cape Snc v. Idealservice Srl and Idealservice MN RE Sas v. OMAI Srl*, 2001 E.C.R. I-9049, at ¶¶ 14–15.

477. Unfair Terms Directive, *supra* note 467, art. 2(c).

Whereas US federal law worked to expand the application of arbitration to areas of consumer law previously thought within the confines of US state law (such as *Discover Bank*), the Unfair Terms Directive—a provision of European “federal” law—specifically limits arbitration in the field of consumer contracts. The Directive classifies a term as “unfair” if “it causes a significant imbalance in the parties’ rights and the obligations arising under the contract, to the detriment of the consumer.”<sup>478</sup> Furthermore, the Annex to Directive contains a non-exhaustive list of terms that may be regarded as unfair, including mandatory arbitration provisions in consumer contracts like those in dispute in *AT&T Mobility*.<sup>479</sup> Such provisions were the subject of the *Mostaza Claro* and *Asturcom* cases.<sup>480</sup> Both cases, discussed in depth below, concern the intersection of arbitration and consumer law in the EU. The cases exemplify “the impact of European law on private law.”<sup>481</sup>

### 5.2.2.1 **Mostaza Claro: EU consumer laws are a defense to enforcement of arbitral awards**

In *Mostaza Claro*, the CJEU held that EU consumer laws may be invoked as a valid defense against an arbitral award.<sup>482</sup> Moreover, the court held that the Unfair Terms Directive provides a defense against arbitral awards in an action for annulment, even when the consumer did not plead the invalidity of the arbitral agreement during the arbitration proceedings.<sup>483</sup>

Not unlikely the dispute in *AT&T Mobility*, the issue in contention in *Mostaza Claro* arose out of a mobile telephone contract. Ms. Mostaza Claro concluded a contract with Móvil, which contained an arbitration clause under which any dispute arising from the contract was to be referred for arbitration to the Asociación Europea de Arbitraje de

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478. *Id.* art. 3.

479. *Id.* annex 1, para. 1(q): “Excluding or hindering the consumer’s right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions.”

480. *Mostaza Claro*, 2006 E.C.R. I-10437; *Asturcom*, 2009 E.C.R. I-9579.

481. Hanna Schebesta, *Does the National Court Know European Law? A Note on Ex Officio Application After Asturcom*, 4 EUR. REV. PRIV. L. 847, 849 (2010).

482. See Bernd U. Graft & Arthur E. Appleton, *Elisa María Mostaza Claro v. Centro Móvil Milenium: EU Consumer Law as a Defence Against Arbitral Awards*, *ECJ Case C-168/05*, 25 ASA BULL. 48, 55 (2007); see also Bernd U. Graf & Arthur E. Appleton, *ECJ Case C-40/08 Asturcom—EU Unfair Terms Law Confirmed as a Matter of Public Policy*, 28 ASA BULL. 413, 413 (2010).

483. *Mostaza Claro*, 2006 E.C.R. I-10437; see also Case Comment, *Case C-234/08, Pannon GSM Zrt. v. Erzsébet Sustikné Györfi, Judgment of the Court (Fourth Chamber) of 4 June 2009, not yet reported and Case C-40/08, Asturcom Telecomunicaciones SL v. Maria Cristiba Rodriguez Nogueira, Judgment of the Court (First Chamber) of 6 October 2009, not yet reported*, 47 COMMON MKT. L. REV. 879, 898 (2010) [hereinafter *Asturcom Case Comment*].

Derecho y Equidad (“AEADE”).<sup>484</sup> Ms. Claro failed to comply with the contractual minimum subscription period, and Móvil initiated arbitration proceedings against her before the AEADE. During the proceedings, Ms. Claro presented arguments on the merits of the dispute but did not claim that the arbitration agreement was void.<sup>485</sup> AEADE issued a decision in favor of Móvil. Ms. Claro then contested the decision before the Audiencia Provincial de Madrid, arguing that the arbitration clause constituted an unfair term under the Unfair Terms Directive, thereby rendering the arbitration agreement null and void.<sup>486</sup>

In its order for reference to the CJEU, the Audiencia Provincial stated that there was no doubt that the arbitration clause was an unfair term rendering the agreement null and void. It wished to receive the CJEU’s opinion, however, as to whether Ms. Claro’s failure to contest the term during the arbitral proceedings precluded her from doing so in an annulment proceeding.<sup>487</sup>

The CJEU invoked its case law to describe the nature of the system of protection introduced by the Unfair Terms Directive: consumers are in a weak position vis-à-vis sellers and suppliers with regard to both bargaining power and level of knowledge; consumers are unable to influence and thus usually accept the terms of consumer contracts which are drawn up in advance by sellers and suppliers; correcting the imbalance in this relationship requires positive action unconnected with contractual parties.<sup>488</sup> To fulfill the Directive’s Article 6 aim of preventing individual consumers from being bound by unfair terms<sup>489</sup> and its Article 7 aim of preventing the continued use of unfair terms in consumer contracts,<sup>490</sup> Member State courts have the power to determine of their own motion whether a term is unfair.<sup>491</sup> The court reasoned that the protection conferred on consumers by the Directive extends to situations in which the consumer fails to raise the unfair nature of term, regardless of whether the consumer is unaware of his or her rights or is prevented

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484. *Mostaza Claro*, 2006 E.C.R. at I-10443, ¶ 16.

485. *Id.* ¶ 17.

486. *Id.* at I-10444, ¶ 18.

487. *Id.* ¶¶ 19–20

488. *Id.* at I-10446, ¶¶ 25–26 (citing *Océano Grupo*, 2000 E.C.R. I-4941, at ¶¶ 25–27).

489. Unfair Terms Directive, *supra* note 467, art. 6(1):

Member States shall lay down that unfair terms used in a contract concluded with a consumer by a seller or supplier shall, as provided for under their national law, not be binding on the consumer and that the contract shall continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair terms.

490. *Id.* art. 7(1):

Member States shall ensure that, in the interests of consumers and of competitors, adequate and effective means exist to prevent the continued use of unfair terms in contracts concluded with consumers by sellers or suppliers.

491. *Mostaza Claro*, 2006 E.C.R. at I-10446, ¶ 27 (citing *Océano Grupo*, 2000 E.C.R. at ¶ 28).

from exercising them due to the costs that would entail.<sup>492</sup> Thus, if the Audiencia Provincial were to prohibit Ms. Claro from arguing the unfair terms defense in the annulment proceedings, the aim of the Directive to prevent individual consumers from being bound by unfair terms would be stymied and “the regime of special protection established by the Directive would be definitively undermined.”<sup>493</sup>

In response to the *Móvil*'s argument that allowing a national court to determine whether an arbitration agreement is void even where the consumer did not make such claim during the arbitration proceeding would “seriously undermine the effectiveness of arbitration awards,” the CJEU conceded that review of arbitration awards must be limited in scope and that annulment of or refusal to recognize an award should be allowed only in exceptional circumstances.<sup>494</sup> The court concluded, however, that the *Eco Swiss* case had established that where, under domestic rules of procedure, a Member State court must grant an application for annulment of an arbitration award on the basis of failure to observe national rules of public policy, it must also grant such an application where it is founded on failure to comply with rules of EU public policy.<sup>495</sup> The CJEU reasoned that Article 6 of the Directive was a mandatory provision, expressing “the nature of importance of the public interest” of consumer protection.<sup>496</sup> Thus, the court held that the Unfair Terms Directive required the Spanish court to determine whether the arbitration agreement was void and to annul the award where the agreement contains an unfair term, even though Ms. Claro had not made such an argument during the arbitral proceedings.<sup>497</sup>

By referring to *Eco Swiss*, the CJEU strongly suggested, without explicitly stating, that consumer protection is part of EU public policy. The European Commission and Advocate General Tizzano presented divergent approaches to applying *Eco Swiss* in *Mostaza Claro*. In *Eco Swiss*, the court had interpreted Article 101 TFEU to be a rule of EU public policy because it constituted a “fundamental” provision which is “essential for the accomplishment of the tasks entrusted to the Community and, in particular, for the functioning of the internal market.”<sup>498</sup> The Commission argued that the provisions of the Unfair Terms Directive could similarly be considered public policy because they were “harmonising provisions approved for the purpose of providing more efficient protection

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492. *Id.* at I-10446, ¶ 29.

493. *Id.* ¶ 30.

494. *Id.* at I-10448, ¶ 33–34 (citing *Eco Swiss*, 1999 E.C.R. I-3055, ¶ 35)).

495. *Id.* ¶ 35 (citing *Eco Swiss*, 1999 E.C.R. at ¶ 37).

496. *Id.* at I-10449, ¶ 38.

497. *Id.* ¶ 39.

498. *Eco Swiss*, 1999 E.C.R. at ¶ 37.

for the consumer within the internal market.”<sup>499</sup> Thus, the provision contributes to the Article 3(1)(b) TFEU<sup>500</sup> aim of “strengthening of consumer protection.”<sup>501</sup> In the Commission’s view, Member State courts were required to ensure that the Directive’s provisions were enforced in actions for the annulment of arbitration awards, regardless of whether the failure to comply with the Directive had been raised during the arbitral proceedings.<sup>502</sup> As discussed above, the CJEU sided with the Commission in its judgment.

It is of significance, however, that the CJEU did not take the advice of Advocate General Tizzano, who favored a more narrow reading of EU public policy in the realm of consumer protection. Advocate General Tizzano worried that applying *Eco Swiss* to the facts in *Mostaza Claro*, as suggested by the Commission, would “give excessively wide scope to a concept, namely that of public policy, which traditionally refers only to rules that are regarded as being of primary and absolute importance in a legal order.”<sup>503</sup> Instead, Advocate General Tizzano had suggested the court rule that failing to allow Ms. Claro to present the unfair term defense would comprise her right to a fair hearing.<sup>504</sup> By rejecting the Advocate General’s narrower approach, the CJEU signaled that EU consumer law was a matter of public policy. Scholars have noted that the CJEU’s objective in *Mostaza Claro* was clear: to prevent the circumvention of EU consumer law provisions through the use of arbitration clauses in consumer contracts.<sup>505</sup> This stands in stark contrast to the holding of the US Supreme Court in *AT&T Mobility*, which prohibited California from regulating the use of mandatory arbitration clauses in consumer contracts.

The facts in *Mostaza Claro* were specific to Spain, but the judgment has relevance for international arbitration. Provided that an arbitral award has an appropriate legal connection with the EU, the CJEU’s reasoning that Member State courts cannot overlook possibly unfair terms because the party seeking annulment failed to raise the claim during the arbitral proceedings is equally applicable to foreign and domestic arbitral awards. Mourre notes that *Mostaza Claro* “shows that the European Court may well be, in the future, willing to require national courts to exert a more stringent control on the way arbitrators apply EU law.”<sup>506</sup> Another commentator stated that *Mostaza Claro*, as well as

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499. *Mostaza Claro*, Opinion of Advocate General Tizzano, 2006 E.C.R. at I-10434, ¶ 55.

500. TEC, *supra* note 184, art. 3(1)(t) (as in effect 2006) (now TFEU, *supra* note 184, art. 3(1)(b)).

501. *Mostaza Claro*, Opinion of Advocate General Tizzano, 2006 E.C.R. at I-10434, ¶ 55.

502. *Id.*

503. *Id.* at I-10434, ¶ 56.

504. *Id.* at I-10435, ¶ 59.

505. See *Asturcom* Case Comment, *supra* note 483.

506. Mourre, *supra* note 124, at 51.

*Eco Swiss*, make possible “revision of arbitral awards on the basis of [EU] law without a solid yardstick as to which [EU] rules constitute public policy.”<sup>507</sup>

**5.2.2.2 In *Asturcom*, the CJEU held that the principle of equivalence may require Member States courts to determine ex officio whether arbitration clauses are contrary to EU consumer law**

A dispute between a telecoms operator and a consumer was at issue in both *Mostaza Claro* and *AT&T Mobility*. The most recent CJEU case concerning EU consumer law and arbitration, *Asturcom*, also arose from a dispute between a telecommunications firm and a consumer.<sup>508</sup> Whereas *Mostaza Claro* concerned the obligation of Member State courts to determine whether an arbitration clause was an unfair term during annulment proceedings, the obligation of Member State courts in award enforcement proceedings was at issue in *Asturcom*. The consumer, Mrs. Rodríguez Nogueira, contracted with Asturcom for a mobile telephone subscription. The contract included an arbitration clause but did not indicate that the seat of the tribunal was in Bilbao (far from Mrs. Nogueira’s home). Asturcom initiated proceedings against Mrs. Nogueira, and the tribunal issued an award in its favor. Mrs. Nogueira failed to initiate proceedings for annulment of the award, and it became final. In 2007, Asturcom brought an action before the Juzgado de Prime Instancia in Bilbao to enforce the award.<sup>509</sup> The court sought a preliminary reference from the CJEU, asking whether:

[T]he [Unfair Terms Directive] must be interpreted as meaning the national court or tribunal hearing an action for enforcement of an arbitration award which has acquired force of *res judicata* and was made in the absence of the consumer is required to determine of its own motion whether an arbitration clause in a contract concluded between a consumer and a seller or supplier is unfair and to annul award.<sup>510</sup>

Judge Tizzano (formerly Advocate General Tizzano, the author of the Advocate General’s Opinion in *Mostaza Claro*) wrote the judgment of the CJEU in *Asturcom*.<sup>511</sup> The CJEU noted that the Unfair Terms Directive created a system of protection for consumers, premised on the idea that consumers are in a weak position vis-à-vis sellers. Article 6(1) of the Directive, providing that unfair terms are not binding on the consumer,

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507. Liebscher, *supra* note 143, at 806.

508. See *Asturcom* Case Comment, *supra* note 483.

509. *Asturcom*, 2009 E.C.R. I-9579, ¶ 24.

510. *Id.* ¶ 28.

511. See Schebesta, *supra* note 481, at 850.

was, the CJEU reasoned, a “mandatory provision.”<sup>512</sup> Furthermore, “positive action” was required to remedy the imbalance between sellers and buyers. In *Mostaza Claro*, the CJEU noted, such positive action had been necessary, and the CJEU thus required that national courts assess of their own motion whether a contractual term was unfair.<sup>513</sup>

However, unlike the claimant in *Mostaza Claro*, Mrs. Nogueira did not involve herself in the arbitral proceedings. By failing to bring an action for annulment, Mrs. Nogueira had allowed the award to become final and acquire the status of *res judicata*. The CJEU reasoned that a Member State court could not be required “to make up fully for the total inertia on the part of the consumer.”<sup>514</sup> The court thus held that the imposition of a time limit during which an award may be challenged was consistent with the principle of effectiveness, as it was “not in itself likely to make it virtually impossible or excessively difficult to exercise any rights which the consumer derives from [the Unfair Terms Directive].”<sup>515</sup>

The CJEU then considered whether the Spanish court was required to determine of its own motion whether the arbitration clause was unfair and to annul the award under the principle of equivalence. The principle of equivalence requires that “the conditions imposed by domestic law under which the courts and tribunals may apply a rule of [EU] law of their own motion must not be less favorable than those governing the application by those bodies of their own motion of rules of domestic law of the same ranking.”<sup>516</sup> The CJEU noted that the Unfair Terms Directive was a mandatory provision and that the Directive was essential to the accomplishment of the tasks [of the EU] . . . in particular to raising the standard of living and the quality of life throughout [the EU].<sup>517</sup> Given the “nature and importance of the public interest” in protecting consumers, the court held, “Article 6 . . . must be regarded as a provision of equal standing to national rules which rank, within the domestic legal systems, as rules of public policy.”<sup>518</sup>

By relying on the principle of equivalence, the CJEU rejected the proposed approach of Advocate General Trstenjak, who argued that the time limit during which an award may

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512. *Asturcom*, 2009 E.C.R. I-9579, ¶ 30.

513. *Id.* ¶ 31.

514. *Id.* ¶ 47.

515. *Id.* ¶ 46.

516. *Id.* ¶ 49 (citing Joined Cases C-430 & C-431/93, *Jeroen van Schijndel and Johannes Nicolaas Cornelis van Veen v Stichting Pensioenfonds voor Fysiotherapeuten*, 1995 E.C.R. I-4705, ¶¶ 13 and 17).

517. *Id.* ¶ 51.

518. *Id.* ¶ 52.

be challenged was not in compliance with the principle of effectiveness.<sup>519</sup> She supported the position that Member State courts have the power to determine of their own motion whether an arbitration clause is unfair and should be annulled by arguing that it “takes best account” of the aim of the Unfair Terms Directive—i.e., protecting consumers.<sup>520</sup> Moreover, she reasoned, the principle of effectiveness was implicated by the wording of Article 7(1) of the Directive, proving that Member States employ “adequate and effective means” to protect consumers from unfair terms.<sup>521</sup> Such means must be “effective”, meaning that where a directive grants rights to individuals, Member States must “effectively . . . guarantee the rights.”<sup>522</sup>

Thus where a Member State court is required by national procedural rules to assess of its own motion during an enforcement proceeding whether an arbitral agreement conflicts with domestic rules of public policy, it is simultaneously obliged to assess of its own motion whether that agreement is unfair under Article 6.<sup>523</sup>

*Asturcom* reinforces the obligation created in *Mostaza Claro* for Member State courts to take into consideration, of their own motion, the Unfair Terms Directive in arbitration enforcement proceedings. Whereas, under US federal arbitration law, US state courts are prevented from considering state public policy when seized of actions for enforcement of awards, European state courts are required to apply federal public policy if state public policy would apply.

## **6 CONCLUSIONS**

Public policy cannot be ignored by parties choosing to submit their disputes to international commercial arbitration. While arbitration is guided by party autonomy, the ultimate sovereignty of States demands that parties adhere to the State public policies. This position is reflected in the public policy exceptions to the recognition and enforcement of foreign arbitral awards included at Article V(2)(b) of the New York Convention and Article 36(1)(b)(ii) of the UNCITRAL Model Law. Moreover, the national legislation of

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519. See Schebesta, *supra* note 481, at 853–54.

520. *Asturcom*, Opinion of Advocate General Trstenjak, 2009 E.C.R. I-9579, ¶ 58–59.

521. *Id.* ¶ 59.

522. *Id.* ¶ 59 (citing Case 48/75, Jean Noël Royer, 1976 E.C.R. 497, ¶ 73 (“The Member States are consequently obliged to choose . . . the most appropriate forms and methods to ensure the effective functioning of the directives, account being taken of their aims.”)).

523. *Asturcom*, 2009 E.C.R. I-9579, ¶ 53 (citing Case C-243/08, Pannon GSM Zrt. v. Erzsébet Sustikné Györfi, 2009 E.C.R. I-04713, ¶ 25).



many States includes a specific exception to the recognition and enforcement of arbitration awards and agreements to arbitrate on grounds of public policy.

In the United States and Europe, significant jurisprudence has developed, detailing the circumstances in which recognition or enforcement may be refused by a State court on public policy grounds. The exception is almost always interpreted narrowly. There is some dispute as to what “public policy” actually entails, but even the most liberal interpretation of the term leads to a narrow application. The best interpretation is to limit the public policy exception of Article V(2)(b) to the public policy of the State in which recognition or enforcement of a foreign arbitral award is sought. In France, the term is limited further to those French public policies that are of fundamental value and universally recognized. Scholars have proposed an ever more strict interpretation that would sever public policy’s connection to the enforcing State and only implicate those values that are recognized and applied by a majority of States.

In Part 4, consideration was given to the practical application of the public policy exception in the courts of the US, the UK, and France. In the US, attempts to equate US foreign policy with US public policy have consistently been rejected. Attempts to equate federal substantive law with US public policy applicable to the recognition or enforcement of foreign arbitral awards have been similarly unsuccessful. Even where federal law would disallow domestic arbitration of some matter—antitrust laws in *Mitsubishi Motors* or claims under the Securities Exchange Act of 1932 in *Scherk*—federal courts have permitted its international arbitration. In a minority of cases, federal courts have used US public policies favoring international comity or disdaining agreements entered into under fraud or duress to refuse enforcement of arbitral awards, but these decisions have not been widely followed. Likewise, in the UK, the default position of courts is to grant recognition and enforcement of arbitral awards. In a number of rare cases, UK courts have refused enforcement where the underlying agreement was contrary to English law. And UK courts have consistently applied a high bar of “reprehensible or unconscionable conduct” to claims that an agreement was the product of fraud and should be refused recognition or enforcement. France, it was detailed, distinguishes between domestic and international public policy. This distinction makes it even harder from award-debtors to have the recognition or enforcement of a foreign arbitral award refused in French courts. Moreover, French courts disregard the doctrine of comity and are uniquely willing to enforce even awards that have been set aside by courts at the place of arbitration.

Finally, in Part 5, the divergent paths taken by the highest courts in the US and in the EU to public policy in arbitration cases were detailed. In the US, the federalization of arbitration law has inhibited the ability of US states to prevent arbitration in matters of consumer law, whereas in the EU the federalization of consumer law has inhibited the ability of Member States to require arbitration in such matters. In the US, the US Supreme Court has rejected the idea that antitrust laws are an expression of US public policy that cannot be adequately enforced through private arbitration. In the EU, it is generally recognized that such laws *are* an expression of EU public policy. Yet, while the position of the US Supreme Court and the CJEU has differed on these issues, the trend across the US and the EU is of the increasing popularity of commercial arbitration.