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Daesang V. NutraSweet Reaffirms NY's Pro-Arbitration Attitude

By **Stephen Younger and Michael Farinacci** (October 11, 2018, 6:19 PM EDT)

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On Sept. 27, 2018, in a widely followed arbitration case, a unanimous panel of the New York Supreme Court Appellate Division, First Department, concluded that the New York County, Commercial Division, erred when it partially vacated an arbitration award on the ground that the arbitrators manifestly disregarded the law. As a result, the Appellate Division confirmed the arbitration award.[1]

Background

The case arose from an international commercial dispute between two artificial sweetener producers.[2] NutraSweet Co. had entered into an agreement with Daesang Corp. to purchase Daesang's aspartame business. The agreement provided that disputes were to be "resolved through arbitration by a three-member tribunal in New York under the rules of the International Chamber of Commerce."[3] Daesang commenced an arbitration proceeding against NutraSweet for breach of contract because, nearly four years after the closing of the transaction, NutraSweet had sought to rescind the agreement.[4]

After an evidentiary hearing, a three-member tribunal unanimously ruled in favor of Daesang and dismissed all of NutraSweet's defenses and counterclaims.[5] Thereafter, Daesang petitioned the Commercial Division to confirm the arbitration award. NutraSweet moved to vacate the award, asserting "that the arbitrators manifestly disregarded the law and evidence, violated public policy, and utterly failed to discharge their duties in accordance with the law and the Terms of Reference governing the arbitration."[6]

Justice Charles E. Ramos[7] of the Commercial Division "reluctant[ly]" ruled in favor of NutraSweet, holding that the arbitrators had "manifestly disregarded the law and had misconstrued the procedural record."[8] In its decision, the lower court remanded a substantial portion of the claims to the arbitrators for redetermination. Daesang appealed.[9]

Discussion

According to the First Department, in New York, it is well-settled "that judicial review of arbitration awards is extremely limited[,]" and courts must give "extreme deference to arbitrators."[10] Therefore,

"[a]n arbitration award must be upheld when the arbitrator offers even a barely colorable justification for the outcome reached."[11] Moreover, "[u]nder the [Federal Arbitration Act (9 USC § 1 et seq., the "FAA")], even if an arbitral tribunal's legal and procedural rulings might reasonably be criticized on the merits, an award is not subject to vacatur for ordinary errors[.]"[12]

First, the Appellate Division reviewed the arbitrators' finding that Daesang's false representations in the agreement were purely contractual and thus could not be pursued based on a fraud theory.[13] NutraSweet alleged that the tribunal had manifestly disregarded the law in dismissing its fraud counterclaims. According to the New York Court of Appeals, the manifest disregard doctrine is only to be used in the "rare occurrences of apparent egregious impropriety on the part of the arbitrators, where none of the provisions of the FAA apply."[14] An arbitration award can be vacated only if: "(1) the arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether, and (2) the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case."[15] The Appellate Division found that the tribunal had not ignored the law; in fact, the tribunal accepted the authority put forth by NutraSweet and "made a good-faith effort to apply" the legal standard proffered by NutraSweet.[16] Even if the tribunal had misapplied the law, the First Department held that such a decision was a mere error of law and did not rise to the level of manifest disregard.[17]

Second, the First Department reviewed the tribunal's determination that NutraSweet had waived its freestanding claim to recover damages for breach of contract.[18] NutraSweet argued that the tribunal's utter failure to discharge its duties was within one of the four statutory grounds under the FAA to vacate an arbitration award.[19] The Appellate Division, however, explained that the arbitrators' asserted misunderstanding of NutraSweet's oral arguments and written submissions would not result in a dereliction of duty by the tribunal. "A court is not empowered by the FAA to review the arbitrators' procedural findings, any more than it is empowered to review the arbitrators' determinations of law or fact."[20] The First Department concluded that as long as the tribunal was construing the procedural record, as it was here, then the FAA[21] does not give courts the power to correct their mistakes.[22]

Finally, NutraSweet argued, in the alternative, that the lower court's decision should be affirmed on independent public policy grounds — grounds not reached by the Commercial Division.[23] NutraSweet claimed that allowing Daesang to profit from its wrongdoing — i.e., fraudulently inducing NutraSweet into the agreement — would be against public policy. While the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958, also known as the New York Convention, permits a country to deny an arbitration award for public policy reasons, the First Department ruled that no such policy basis was present here. The Appellate Division cautioned that "the Convention's public policy defense to enforcement of an award 'should be construed narrowly' and 'should apply only where enforcement would violate our most basic notions of morality and justice.'"[24]

Takeaways

The First Department's ruling quells concerns that resulted from the Commercial Division's decision and reaffirms New York's pro-arbitration perspective. The decision was set to disrupt the "emphatic federal policy in favor of arbitral dispute resolution"[25] and the New York Convention's goal to "encourage the recognition and enforcement of commercial arbitration agreements in international contracts and to unify the standards by which agreements to arbitrate are observed[.]"[26] Notably, the New York City Bar Association's International Commercial Disputes Committee filed an amicus brief in support of Daesang, arguing that the decision's expansive interpretation of the manifest disregard doctrine would overburden New York courts and discourage parties from choosing New York as their arbitral seat.[27]

Daesang is an important decision for the New York courts given that it helps reaffirm New York's role as "one of the world's preeminent international arbitration centers."[28] Sophisticated parties desire predictability in the enforcement of arbitration awards, which is a key reason why the manifest disregard doctrine is applied narrowly. Accordingly, parties should not expect New York courts to undertake a substantive review of an arbitrator's decisions — as opposed to an assessment of whether the tribunal exceeded its powers as specified in the agreement. If courts were to apply a more rigorous standard of review, the purpose of agreeing to arbitrate would be undermined. Instead of being considered a final decision, the arbitration award would become the first step in a time-consuming judicial review process — a process that the parties chose to avoid by selecting arbitration.

As more and more clients engage in international commercial activities, arbitration is becoming a crucial tool to facilitate international commerce. When parties agree to arbitrate, they choose to opt out of the court system and thereby avoid the potential unpredictability of litigating in foreign courts. In exchange for the expediency and confidentiality of arbitration, parties assume the risk that an arbitration tribunal will interpret the facts or apply the law against them. Therefore, when agreeing to arbitration, parties must understand the implications of their agreement. Moreover, when a dispute arises, parties should thoroughly research potential arbitrators before choosing their panel.

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[1] Matter of Daesang Corp. v. The NutraSweet Co. et al., 655019/2016, 2018 NY slip op. 06331, at *2 (App. Div. 1st Dep't Sept. 27, 2018).

[2] A more detailed recitation of the facts can be found here.

[3] Id. at *3.

[4] Section 10 of the Joint Defense and Confidentiality Agreement provides that "NutraSweet is entitled to rescind any transaction ultimately agreed upon in the event legal proceedings challenging the deal as an antitrust violation are instituted 'by any customer with annual worldwide aspartame requirements in excess of 1,000,000 pound[.]'" Id. at *3.

[5] Id. at *4.

[6] Id. at *6.

[7] Justice Ramos is currently the Commercial Division Justice assigned to hear international arbitration matters.

[8] Id. at *2.

[9] Id. at *6.

[10] Id. at *7.

[11] Id. (quoting Wien & Malkin LLP v Helmsley-Spear, Inc., 6 N.Y.3d 471, 479-80 (2006)).

[12] Matter of Daesang, at *2 (quoting Wien & Malkin, 6 N.Y.3d at 481 (internal quotation marks omitted)).

[13] Matter of Daesang, at *8.

[14] Id. at *7 (quoting Wien & Malkin, 6 N.Y.3d at 480-481 (internal quotation and citations omitted)).

[15] Id.*7-8 (quoting Wien & Malkin, 6 N.Y.3d at 480-481 (internal quotation and citations omitted)).

[16] Matter of Daesang, at *8.

[17] Id.

[18] Id. at *9.

[19] Id. at*7; "[W]here the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made." Id. (quoting 9 USC § 10[a]).

[20] Matter of Daesang, at *10.

[21] "While … this matter is governed by the FAA, we observe that similar conclusions have been reached by courts applying the analogue of 9 USC § 10(a)(4) in CPLR article 75, which authorizes vacatur where an arbitrator 'exceeded his [or her] power or so imperfectly executed it that a final and definite award upon the subject matter submitted was not made'(CPLR 7511[b][iii])." Matter of Daesang, at *9-10.

[22] Id. at *11 (quoting Oxford Health Plans LLC v. Sutter, 569 U.S. 564, 572-573 (2013)).

[23] Matter of Daesang, at *11.

[24] Id. at *11 (quoting Waterside Ocean Navigation Co.v. Int'l Navigation Ltd., 737 F.2d 150, 152 (2d Cir. 1984) (internal quotation marks omitted)).

[25] Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 631 (1985).

[26] Scherk v. Alberto-Culver Co., 417 U.S. 506, 534 n.15 (1974).

[27] Brief for the Association of the Bar of the City of New York as Amicus Curiae In Support of Appellant and Reversal, pages 15-16.

[28] Id. at page 2.