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Supreme Court Set to Resolve Impasse Over US Discovery in International Arbitration

Article

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The future of discovery in private international arbitration is in the Supreme Court's hands following oral argument last month in two consolidated cases concerning the interpretation of 28 U.S.C. § 1782. A relatively arcane provision that has recently attracted headlines, section 1782 authorizes federal district courts to order broad production of documents and testimony from a person or entity within the U.S. "for use in a proceeding in a foreign or international tribunal."

The question at the heart of the dispute is whether private international commercial arbitrations constitute "tribunals" under section 1782, or if that term is meant to include only governmental or quasi-governmental proceedings. The Supreme Court's decision is likely to resolve a circuit split years in the making, and could have significant consequences by opening the floodgates of U.S.-style discovery in international arbitration practice.

The 2nd, 5th, and 7th Circuit Courts of Appeal have opted for a narrow interpretation of section 1782, holding that it only permits a U.S. court to order U.S.-style discovery in connection with foreign proceedings that involve some form of "governmental" or "quasi-governmental" authority.

On the other hand, the 4th and 6th Circuits have held that section 1782 discovery is available in all foreign and international arbitrations, including private proceedings before arbitrators selected by the parties. The two cases now before the Supreme Court are set to resolve the confusion.

The first, *ZF Automotive U.S. Inc. v. Luxshare Inc.*, stems from a private commercial arbitration in Germany between ZF Friedrichshafen AG, a German corporation, and Luxshare, a Hong Kong limited liability company. Luxshare filed an ex parte application in federal district court in Michigan for section 1782 discovery from a U.S. subsidiary of ZF Friedrichshafen AG.

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The application was originally granted and eventually appealed to the 6th Circuit. In an unusual procedural move, the Supreme Court granted certiorari before the 6th Circuit rendered a decision, and consolidated the case with *AlixPartners, LLP, et al. v. The Fund for Protection of Investors' Rights in Foreign States*.

The AlixPartners case arises from a dispute between two foreign parties — the Fund for Protection of Investors Rights in Foreign States ("Fund"), a Russian investment entity, and the Republic of Lithuania — which were engaged in international ad hoc arbitration pursuant to a treaty between Russia and Lithuania. To assist in the merits phase of arbitration, the Fund filed an application under section 1782 for discovery from a New York-based consulting firm, AlixPartners, which spurred the appeal to ascertain whether AlixPartners had to comply given that the underlying arbitration, although resulting from a treaty and involving government parties, was subject to the determination of private, non-government-related arbitrators.

The Supreme Court's consolidation of the cases is interesting because the two cases present slightly different fact patterns. For example, the AlixPartners arbitration was conducted pursuant to international treaty, while the ZF Automotive arbitration was between private parties to a contract requiring arbitration before private arbitrators. The potential impact of these differences was the focus of considerable questioning by the Justices during oral argument as they probed how to interpret the term "foreign tribunal" under section 1782.

If the Supreme Court adopts the approach taken by the 2nd, 5th, and 7th Circuits and holds that private international arbitrations do not qualify as "tribunals" under the statute, then the traditional practice that allows for more limited discovery in international arbitrations will remain intact.

On the other hand, if the Court adopts the more expansive definition of a "tribunal" from the 4th and 6th Circuits, the decision will likely have lasting impacts on not only the expense and efficiency of private international arbitration when documents and witnesses are located in the United States, but also the text of arbitration provisions in parties' agreements and the arbitral rules set by foreign, private arbitral organizations.

Arbitration is often cited as a more cost-effective and expedient alternative to litigation, primarily because the scope of discovery is determined by the parties themselves and can be less extensive than traditional disclosure allowed by the Federal Rules of Civil Procedure. A broad interpretation of "tribunal" under section 1782 would eliminate this perceived advantage by allowing parties in foreign-based arbitration to seek expansive document discovery, including electronically stored information, and take deposition testimony.

In order to avoid the consequences of a broad decision by the Supreme Court, parties worldwide would need to reconsider the arbitration provisions they currently use in order to place contractual guardrails around such a decision. Likewise, foreign, private arbitral organizations may need to amend their rules

in order to permit or deny U.S.-based discovery or impose procedures on when and how it can be used (e.g., only once an arbitration is filed, rather than beforehand; only with arbitrator permission; only if the foreign seat of the arbitration or governing law of the arbitration permit similar style discovery).

In the meantime, the U.S. court system will have to decide these issues on a case-by-case basis, which is likely to lead to different procedures and standards over the permissible timing and scope of discovery. The possible consequences could go even further, with parties to U.S.-based arbitration and governed by U.S. laws attempting to avoid or impose similarly broad discovery through carefully drafted arbitration provisions or by choosing arbitral organizations whose rules allow or prohibit broader discovery.

The case also raises interesting issues of comity, often cited as the primary purpose behind section 1782. Foreign nations may have similar statutes that authorize parties in litigation to conduct discovery within their borders, but the same is not necessarily true for parties engaged in arbitration. As a result, a broad interpretation of section 1782 could disadvantage U.S. companies engaged in private international arbitration with foreign entities that have no connection to the U.S.

While the foreign counterparty could have access to extensive discovery in the United States, the U.S. entity would likely be denied a reciprocal benefit under the laws of the foreign state. It would also leave domestic parties subject to mandatory international arbitration provisions in existing contracts in a far worse position to negotiate in preliminary settlement discussions.

Moreover, as argued to the Supreme Court, a decision expanding the scope of section 1782 could place U.S. courts and U.S.-based entities at the center of otherwise completely foreign disputes, leading to political concerns as well as increasing the burden and expense on the U.S. courts and U.S. entities without reciprocal benefits to parties who wish to take discovery in foreign countries.

Application of section 1782 to purely private arbitration could overwhelm federal district courts with discovery requests for disputes involving wholly foreign parties with no domestic interest. Discovery disputes are common and often lead to the need for judicial intervention, and an influx of foreign parties seeking discovery in the U.S. raises concerns that it will bog down an already overburdened judiciary at the expense of domestic parties engaged in traditional litigation in federal courts.

The Supreme Court is expected to issue a decision by this summer. Until then, practitioners should consider the potential consequences of international arbitration agreements, particularly in contracts with foreign counterparties. A broad interpretation of section 1782 from the Supreme Court could leave clients with little to no recourse over the scope of U.S. discovery in disputes resulting in private international arbitration or perhaps even sound the death knell for private international arbitration as the preferred method of dispute resolution for

parties with U.S. subsidiaries or reliant on U.S. companies in connection with their foreign businesses.

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