

NOTE

THREE’S COMPANY: EXAMINING THE THIRD-PARTY PROBLEM THROUGH AN ANALYSIS OF *BRIDAS S.A.P.I.C. V. GOVERNMENT OF TURKMENISTAN**

TABLE OF CONTENTS

- I. INTRODUCTION.....262
- II. OVERVIEW OF INTERNATIONAL ARBITRATION.....264
 - A. *Laying the Statutory Groundwork*.....264
 - B. *Judicial Review of International Arbitration Awards*265
- III. STATEMENT OF THE CASE266
 - A. *Facts and Proceedings*267
 - B. *The Bancec Presumption*272
- IV. ANALYSIS274
 - A. *The Third-Party Problem*.....274
 - B. *The Mists of Metaphor: Veil-Piercing in General*276
 - C. *How the Fifth Circuit Got It Wrong*.....278
- V. CONCLUSION.....284

* This Note received the Hicks, Thomas & Lilienshern LLP Award for the Best Student Note written for the *Houston Law Review*. The Author wishes to thank her family and friends—both endless sources of support and guidance. Thanks also to the editors of the *Houston Law Review* for their tireless work.

I. INTRODUCTION

“[A]rbitration is a creature of contract.”¹ Consent is the cornerstone upon which the temple of private dispute resolution has been built—unlike courts, which derive their power from broadly applicable laws, the authority of an arbitral tribunal flows from the specific agreement between the parties.² Despite the central role of consent in the legitimacy of international arbitration, courts and arbitrators around the world bind nonsignatories to agreements to arbitrate based on a variety of theories.³

This Note proposes that the theories used to bind nonsignatories to international arbitrations are too many, too varied, and too complex. The legitimacy and continued success of international arbitration depend upon the support of a secure and reliable legal framework. This Note suggests that the third-party problem—that is, the various difficulties inherent in binding nonsignatories to what is essentially a consensual process—would be less of a problem if arbitrators were permitted to make jurisdictional decisions regarding nonsignatories and if courts respected those decisions. U.S. courts must heed the parties’ intent to commit jurisdictional decisions to the arbitrator, especially in the context of international business transactions with little or no connection to the United States other than as the situs of the arbitration.⁴ Arbitrators, in turn, should apply a uniform international standard when binding

1. *United Steelworkers v. Am. Mfg. Co.*, 363 U.S. 564, 570 (1960) (Brennan, J., concurring).

2. See James M. Hosking, *The Third Party Non-Signatory’s Ability to Compel International Commercial Arbitration: Doing Justice Without Destroying Consent*, 4 PEPP. DISP. RESOL. L.J. 469, 476 (2004) (“[T]he ‘crucial difference between arbitration and courts lies in the fact that the basis of the jurisdiction of an arbitral tribunal is the will of the parties, while courts owe their competence to procedural norms of a state or of an international convention.” (quoting TIBOR S. VARADAY ET AL., *INTERNATIONAL COMMERCIAL ARBITRATION: A TRANSNATIONAL PERSPECTIVE* 61 (1999))).

3. See generally *id.* at 490–544 (studying the various theories used in England, France, and the United States in order to bind a nonsignatory to an agreement to arbitrate).

4. This is consistent with the Supreme Court allowing an arbitral tribunal to determine its own jurisdiction where the parties have committed that issue to the arbitrator. See *First Options of Chi., Inc. v. Kaplan*, 514 U.S. 938, 943–44 (1995) (concluding that “a court must defer to an arbitrator’s arbitrability decision when the parties submitted that matter to arbitration” as long as there is “clea[r] and unmistakabl[e]’ evidence that they did so” (quoting *AT&T Techs., Inc. v. Commc’ns Workers*, 475 U.S. 643, 649 (1986) (alteration in original))). The International Chamber of Commerce (ICC) rules, incorporated by reference in many international agreements, evince the required intent to allow the arbitrator to define the scope of her own power. See *infra* note 31 (detailing the ICC rules governing arbitration).

nonsignatories to an arbitration agreement.⁵ This Note does not argue that *all* judicial review of international arbitration awards should cease;⁶ rather, only that courts should respect the agreement of the parties and should refrain from delving too deeply into the merits of a case under the guise of a jurisdictional inquiry.

This Note analyzes the third-party problem in the context of *Bridas S.A.P.I.C. v. Government of Turkmenistan*,⁷ a recent Fifth Circuit case binding a nonsignatory government to an agreement to arbitrate. *Bridas* conclusively demonstrates that independent jurisdictional review by courts vitiates at least two of the main forces driving international arbitration: efficiency and the desire for a neutral forum.⁸ *Bridas* also illustrates the need for unique treatment of government instrumentalities in the event a U.S. court examines the question of binding sovereign nonsignatories to an arbitration agreement. If a court must undertake such an inquiry, rules geared toward the special circumstance of government instrumentalities, and ideally rules that have resonance in the international community, should govern the court's inquiry.

By way of introduction, Part II of this Note provides an overview of the concepts and statutes central to international arbitration. Part III examines the two Fifth Circuit opinions issued in *Bridas* and case law relevant to the court's decision. Part IV explores the third-party problem and discusses how the *Bridas* decision exacerbates that problem, especially in the context of international arbitration. Additionally, Part IV considers how government instrumentalities involved in

5. *But see* Hosking, *supra* note 2, at 584–86 (rejecting an international standard for nonsignatory issues and concluding that applying domestic contract law is the best solution to the third-party problem).

6. In fact, such a hands-off approach by courts would probably undermine the legitimacy of international arbitration. *See* William W. Park, *The Specificity of International Arbitration: The Case for FAA Reform*, 36 VAND. J. TRANSNAT'L L. 1241, 1266 (2003) (concluding that completely eliminating judicial review would damage “the health of international arbitration”). The grounds for review, however, should be narrow and should avoid independent jurisdictional review where the parties have committed that issue to the arbitral tribunal.

7. *Bridas S.A.P.I.C. v. Gov't of Turkmenistan (Bridas II)*, 447 F.3d 411 (5th Cir. 2006); *Bridas S.A.P.I.C. v. Gov't of Turkmenistan (Bridas I)*, 345 F.3d 347 (5th Cir. 2003).

8. *See, e.g.*, W. Laurence Craig, *Some Trends and Developments in the Laws and Practice of International Commercial Arbitration*, 30 TEX. INT'L L.J. 1, 2 (1995) (exploring the aims and benefits of international arbitration). The arbitration agreement in *Bridas* was signed in 1993 and repudiated in 1996. *Bridas I*, 345 F.3d at 351–52. The litigation concerning the arbitration proceedings lasted from 1999 until late 2006, leading the Fifth Circuit to comment, “This dispute has been in litigation longer than the agreement that spawned it.” *Bridas II*, 447 F.3d at 414.

international arbitrations present especially delicate problems for U.S. courts. Part V concludes.

II. OVERVIEW OF INTERNATIONAL ARBITRATION

The emergence of the multinational corporation and the concomitant disregard for national boundaries in the context of trade and investment heralded a new era of international dispute resolution.⁹ Although concerns regarding economy and efficiency fuel all forms of commercial arbitration, the search for a neutral forum is the *raison d'être* of international arbitration.¹⁰ National courts are the product of national norms, and parties to international business transactions place a high premium on the ability to avoid costly, biased, and unpredictable litigation in foreign courts.¹¹

A. *Laying the Statutory Groundwork*

Understanding international arbitration implicates a myriad of domestic statutes and international conventions. The Federal Arbitration Act (FAA) is the central authority governing arbitration in the United States.¹² In addition, the United States is a signatory to the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention)—the primary mechanism ensuring the enforcement of international arbitration awards.¹³ Signatories to the New York Convention agree that “[e]ach [c]ontracting [s]tate shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the

9. See Craig, *supra* note 8, at 2 (commenting on the “growth of international commercial arbitration” due to the “explosive growth of international trade and commerce”).

10. See *id.* (“In short, while speed, informality, and economy have had some influence on the growth of international commercial arbitration, the essential driving force has been the desire of each party to avoid having its case determined in a foreign judicial forum.”).

11. *Id.* at 2–3.

12. See Charles Lee Eisen, *What Arbitration Agreement? Compelling Non-Signatories to Arbitrate*, 56 DISP. RESOL. J. 40, 42 (2001) (“The centerpiece of arbitration involving interstate commerce is the Federal Arbitration Act.”). When an arbitration implicates solely intrastate commerce, the various state laws governing arbitration control. *Id.*

13. See Amber A. Ward, Comment, *Circumventing the Supremacy Clause? Understanding the Constitutional Implications of the United States’ Treatment of Treaty Obligations Through an Analysis of the New York Convention*, 7 SAN DIEGO INT’L L.J. 491, 493–94 (2006) (explaining that the New York Convention is “the primary vehicle” for enforcing international arbitration awards). The Convention is widely recognized as instrumental in the growth and continued success of international arbitration. *Id.* at 494.

award is relied upon.”¹⁴ Section 2 of the FAA implements the New York Convention.¹⁵

The FAA establishes a strong federal policy favoring arbitration.¹⁶ Any ambiguities concerning the validity of an arbitration should be resolved in favor of the arbitration.¹⁷ Judicial review of arbitration agreements is necessarily narrow; courts may not review the merits of a case under the guise of a proceeding to confirm or vacate an arbitral award.¹⁸

B. *Judicial Review of International Arbitration Awards*

The FAA governs judicial review of international arbitrations unfolding in the United States.¹⁹ To prevent arbitration from becoming mere foreplay to litigation, judicial review is, and must remain, limited.²⁰ The FAA lays out four statutory grounds for vacating an arbitration award.²¹ In addition

14. United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, art. III, June 10, 1958, 330 U.N.T.S. 3, *available at* http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention.html.

15. *See* 9 U.S.C. §§ 201–08 (2000) (“The Convention on the Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958, shall be enforced in United States courts in accordance with this chapter.”).

16. *See* *Moses H. Cone Mem’l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983) (agreeing with the “healthy regard for the federal policy favoring arbitration”).

17. *See id.* at 24–25 (“[A]s a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration.”); *see also* Anthony M. DiLeo, *The Enforceability of Arbitration Agreements By and Against Non-Signatories*, 2 J. AM. ARB. 31, 35 (2003).

18. *See* Stephen L. Hayford, *A New Paradigm for Commercial Arbitration: Rethinking the Relationship Between Reasoned Awards and the Judicial Standards for Vacatur*, 66 GEO. WASH. L. REV. 443, 452 (1998) (limiting the inquiry to whether arbitrators performed the “the job they were told to do—not whether they did it well, or correctly, or reasonably” (quoting *Remey v. PaineWebber, Inc.*, 32 F.3d 143, 146 (4th Cir. 1994))).

19. *See* *Park*, *supra* note 6, at 1245 (“The Federal Arbitration Act subjects most arbitration in the United States to a single standard for judicial review, regardless of whether the dispute is big or small, domestic or international . . .”). There is a conflict in the circuits as to whether the FAA grounds for vacatur or the somewhat narrower New York Convention grounds apply to an action to vacate a nondomestic award rendered in the United States. Christopher R. Drahozal, *New Experiences of International Arbitration in the United States*, 54 AM. J. COMP. L. 233, 241–42 (2006). Because the Fifth Circuit applied the FAA in the *Bridas* dispute, the New York Convention standards are outside the scope of this Note.

20. *See* *Moseley, Hallgarten, Estabrook & Weeden, Inc. v. Ellis*, 849 F.2d 264, 267 (7th Cir. 1988) (“[A]n extremely low standard of review is necessary to prevent arbitration from becoming merely an added preliminary step to judicial resolution rather than a true alternative” (quoting *E.I. DuPont de Nemours & Co. v. Grasselli Employees Indep. Ass’n*, 790 F.2d 611, 614 (7th Cir. 1986))).

21. 9 U.S.C. § 10 (Supp. IV 2004).

In any of the following cases the [court] . . . may make an order vacating the award . . . (1) where the award was procured by corruption, fraud, or undue

to these statutory grounds, courts have carved out a variety of nonstatutory grounds for vacatur.²²

Courts may also review an arbitrator's decision to exercise jurisdiction over a particular dispute.²³ An arbitrator's ability to determine her own jurisdictional authority is referred to as "compétence-compétence."²⁴ In the United States, courts should defer to an arbitrator's jurisdictional decisions provided that "clear and unmistakable evidence" indicates the parties allocated to the arbitrator the power to interpret the scope of the arbitration agreement.²⁵

Because there is no neutral international forum considering appeals of arbitral decisions, jurisdictional problems have special significance in the international arena. If U.S. courts review the arbitrability of every dispute, sophisticated parties to complex international transactions may find themselves litigating questions of jurisdiction and scope in every dispute they intended to commit to arbitration.

III. STATEMENT OF THE CASE

This section will present the facts of *Bridas* and track the parties' journey up and down the Fifth Circuit. In short, *Bridas* teaches that U.S. courts must avoid the business of ordering

means; (2) where there was evident partiality or corruption in the arbitrators, or either of them; (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or (4) where 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.

22. Every circuit has adopted the nonstatutory "manifest disregard of the law" standard as an additional ground for vacatur. Drahozal, *supra* note 19, at 240. Other courts have refused to enforce an award that "is in direct conflict with public policy[,] . . . arbitrary and capricious[,] . . . completely irrational[, or] . . . fails to draw its essence from the parties' underlying contract." Hayford, *supra* note 18, at 461-62 (internal quotation marks and citations omitted).

23. See *First Options of Chi., Inc. v. Kaplan*, 514 U.S. 938, 942 (1995) (considering the proper standard of review for "an arbitrator's decision about arbitrability"). The Supreme Court defined "arbitrability" as whether or not a party agreed to arbitrate the merits of a case. *Id.* As arbitrators derive their jurisdiction over a proceeding from the agreement of the parties, inquiries concerning "arbitrability" and jurisdiction are identical.

24. William W. Park, *Determining Arbitral Jurisdiction: Allocation of Tasks Between Courts and Arbitrators*, 8 AM. REV. INT'L ARB. 133, 140 (1997). Literally, compétence-compétence means "jurisdiction concerning jurisdiction." *Id.*

25. *First Options of Chi., Inc.*, 514 U.S. at 943-44 (quoting *AT&T Techs., Inc. v. Commc'ns Workers*, 475 U.S. 643, 649 (1986) (alterations omitted)).

foreign governments to honor agreements to which the foreign governments may or may not have consented. When parties have contractually agreed to resolve their disputes through binding arbitration, their decision must be respected.

A. *Facts and Proceedings*

In 1993, Bidas, an Argentinean company, entered into a joint venture agreement (JVA or the agreement) to develop oil and gas located in Turkmenistan, an oil-rich former Soviet state.²⁶ The original parties to the agreement were Bidas and the “Turkmenian Party,” a state-owned enterprise.²⁷ The Government of Turkmenistan was not a signatory to the agreement.²⁸ The JVA contained an arbitration clause requiring that any dispute or controversy arising out of the JVA be settled by binding arbitration proceedings.²⁹ The parties further stipulated that the International Chamber of Commerce’s Rules of Conciliation and Arbitration (ICC rules) would govern any arbitration proceedings.³⁰ The ICC rules incorporated in the JVA provided that the arbitral tribunal would decide any questions of jurisdiction that arose during the proceeding.³¹

Within three years the agreement between the parties crumbled.³² Bidas commenced an ICC arbitration proceeding against Turkmenneft and the Government of Turkmenistan.³³

26. *Bidas S.A.P.I.C. v. Gov’t of Turkmenistan (Bidas I)*, 345 F.3d 347, 351 (5th Cir. 2003). Turkmenistan, a former province of the now defunct Soviet Union, declared its independence in 1991. Roger P. Alford, *Binding Sovereign Non-Signatories*, 4 THE INT’L ARB. NEWS 2, 2 (2003–04). Turkmenistan is estimated to have the fourth largest gas reserves in the world—as high as six billion barrels according to the Government of Turkmenistan. *Id.*

27. *Bidas S.A.P.I.C. v. Gov’t of Turkmenistan (Bidas II)*, 447 F.3d 411, 414 (5th Cir. 2006). The Government of Turkmenistan changed the identity of the Turkmenian Party over the life of the agreement. *Id.* The final entity to comprise the Turkmenian Party was Turkmenneft. *Id.*

28. *Bidas I*, 345 F.3d at 351.

29. *Id.* at 351–52.

30. *Id.* at 352.

31. INT’L CHAMBER OF COMMERCE, RULES OF ARBITRATION art. 6, para. 4 (1998), available at http://www.iccwbo.org/uploadedFiles/Court/Arbitration/other/rules_arb_english.pdf.

[T]he Arbitral Tribunal shall not cease to have jurisdiction by reason of any claim that the contract is null and void or allegation that it is non-existent, provided that that the Arbitral Tribunal upholds the validity of the arbitration agreement. The Arbitral Tribunal shall continue to have jurisdiction to determine the respective rights of the parties and to adjudicate their claims and pleas even though the contract itself may be non-existent or null and void.

Id.

32. See *Bidas II*, 447 F.3d at 414–15.

33. *Id.* at 415.

Bridas claimed that both the state instrumentality and the state itself, a nonsignatory to the agreement, were liable for breach of contract.³⁴ The Government filed an objection to the jurisdiction of the arbitral tribunal on the grounds that it was not a signatory to the agreement to arbitrate and thus was not a proper party to the arbitration.³⁵ After filing the jurisdictional objection, the Government ceased all participation in the arbitral proceedings, which took place in Houston.³⁶

The arbitral panel first considered whether the JVA authorized the panel to determine if jurisdiction existed over the Government of Turkmenistan. It answered this question in the affirmative.³⁷ The panel proceeded to conclude “that ‘the Government was a proper party to the arbitration.’”³⁸ The panel found both Turkmenneft and the Government liable for breaching the JVA, and awarded \$495 million in damages to Bridas.³⁹

After the arbitration award issued, Bridas filed an application for confirmation of the award in the U.S. District Court for the Southern District of Texas.⁴⁰ The Government of Turkmenistan and Turkmenneft filed motions to vacate the award, arguing that the arbitral panel never had jurisdiction over the Government, a nonsignatory to the JVA containing the arbitration clause.⁴¹ Thus, they claimed the Government could

34. *Id.* (discussing the breakdown of the parties’ relationship, the subsequent arbitration proceedings, and the arbitration award in which the tribunal found Turkmenneft and the Government liable for repudiating the agreement); *see also* Petition for a Writ of Certiorari at 2–3, *Gov’t of Turkmenistan v. Bridas S.A.P.I.C.*, No. 06-267, 2006 WL 2459586 (Aug. 21, 2006) (noting that Bridas commenced arbitration proceedings to recover damages for breach of contract).

35. *Bridas I*, 345 F.3d at 352.

36. Petition for a Writ of Certiorari at 3, *Gov’t of Turkmenistan v. Bridas S.A.P.I.C.*, No. 06-267, 2006 WL 2459586 (Aug. 21, 2006).

37. *See Bridas I*, 345 F.3d at 352 (observing that the arbitral tribunal first held that “the arbitrators had jurisdiction to determine whether they had jurisdiction over the Government”). An arbitrator’s authority is derived from the arbitration agreement; he is not permitted to decide matters the agreement does not place before him. *See, e.g.*, *Beaird Indust., Inc. v. Local 2297, Int’l Union*, 404 F.3d 942, 943–44 (5th Cir. 2005) (affirming the conclusion that an arbitrator exceeded his authority when he ignored the unequivocal reservation of certain rights within the arbitration agreement).

38. *Bridas I*, 345 F.3d at 352 (quoting the tribunal’s First Partial Award).

39. *Bridas S.A.P.I.C. v. Gov’t of Turkmenistan (Bridas II)*, 447 F.3d 411, 415 (5th Cir. 2006).

40. *Bridas I*, 345 F.3d at 352. The proper place to review an arbitration award is the site of the arbitration. 9 U.S.C. §§ 9–11 (2000 & Supp. V 2005) (mandating that unless the parties agree otherwise, the U.S. district court “within which such award was made” has jurisdiction to review the award).

41. *Bridas I*, 345 F.3d at 352–53; *see also* Timothy G. Nelson, *BRIDAS v. Government of Turkmenistan: U.S. Courts Uphold an Arbitrator’s Power to Hold A Foreign Sovereign Liable for the Acts of Its State-Owned Enterprise*, 24 ASA BULL. 584,

2008]

THREE'S COMPANY

269

not be bound by the terms of the JVA or by the arbitration award.

The district court disagreed with the Government.⁴² After undertaking an independent review of whether the JVA bound the Government to arbitrate with Bidas, the district court denied the motion to vacate.⁴³ The district court concluded that, although the Government was separate from Turkmenneft as a matter of corporate formality, “principles of agency and equitable estoppel bound the Government to the JVA.”⁴⁴

The Fifth Circuit reversed the district court’s decision to bind the Government to the JVA based on agency and estoppel theories and remanded the case for further consideration.⁴⁵ Affirming the decision to undertake an independent jurisdictional review, the Fifth Circuit concluded that no clear and unmistakable evidence evinced the parties’ intent to give the arbitral tribunal the authority to determine its own jurisdiction.⁴⁶ The Fifth Circuit acknowledged that the express terms of the parties’ agreement did not bind the Government to arbitration.⁴⁷ Recognizing that “[w]ho is actually bound by an arbitration agreement is a function of the intent of the parties,”⁴⁸ the Fifth Circuit then considered whether to bind the Government, a nonsignatory, absent express terms indicating their intent to be bound.⁴⁹

The Fifth Circuit rejected the district court’s conclusion that Turkmenneft signed the JVA as the agent of the Government.⁵⁰ The court reiterated that, as arbitration is a matter of contract, the typical case will not warrant applying an arbitration

593 (2006) (stating the grounds for the motion to vacate included “that the State of Turkmenistan was not a signatory to the JV Agreement and therefore was not bound either by the JVA arbitration clause or the ensuing ICC Awards”).

42. *See Bidas I*, 345 F.3d at 354 (reciting the district court’s holding that the Government was bound to the JVA).

43. *Id.*

44. *Id.*

45. *Id.* at 366.

46. *Id.* at 354–55. The court noted that “[t]his independent review of whether the arbitration panel had jurisdiction over the Government represents a departure from the typically deferential review afforded arbitral decisions pursuant to the federal policy favoring arbitration.” *Id.* at 354 n.4.

47. *See id.* at 355 (“It is apparent that the four corners of the agreement do not bind the Government to arbitrate this dispute.”).

48. *Id.*

49. *See id.* at 356 (“Ordinary principles of contract and agency law may be called upon to bind a nonsignatory to an agreement whose terms have not clearly done so.”).

50. *Id.* (noting that “the district court’s holding that Turkmenneft is an agent of the Government does not withstand our review”).

agreement to a nonsignatory.⁵¹ Central to the court's rejection of the agency theory was the fact that both Bridas and Turkmenneft were sophisticated parties represented by able counsel—if the parties had truly intended Turkmenneft to sign the JVA as an agent of the Government, that fact surely would have been indicated by clearer language.⁵²

The Fifth Circuit also held that the equitable estoppel and third-party beneficiary principles did not apply to the circumstances of the case.⁵³ In so concluding, the court relied on the fact that the Government never sought to enforce the terms of the agreement in an attempt to derive some benefit under the agreement, while at the same time avoiding liability by pointing to their nonsignatory status.⁵⁴ As both the equitable estoppel and third-party beneficiary theories were crafted to avoid allowing a party to “have it both ways,”⁵⁵ the rationale supporting these exceptions to the “fundamental premise that a party cannot be compelled to arbitrate a matter without its agreement”⁵⁶ did not apply. After rejecting every other method of binding the government to the arbitration agreement, the Fifth Circuit remanded the case for a more detailed examination of whether or not the Government could be bound to the JVA based on the alter-ego theory.⁵⁷

On remand, the district court vacated the arbitration award against the Government, holding that the evidence did not demonstrate the level of control required to find alter-ego

51. *See id.* at 358 (“Arbitration agreements apply to nonsignatories only in rare circumstances.”).

52. *Id.*

53. *See id.* at 361–62 (“The district court thus abused its discretion in applying the . . . theory of equitable estoppel to this case. . . . Nor is the third-party beneficiary doctrine availing.”).

54. *See id.* (noting that the Government never sued Bridas under the agreement or otherwise “exploited” the agreement); *see also id.* at 363 (“[W]e are again reluctant to bind the Government to the terms of the JVA on a third-party beneficiary theory because the Government has never filed a claim against Bridas premised upon the agreement, or otherwise sought to enforce its terms.”). This reasoning is similar to that employed by other circuits in upholding the presumption of separate legal status between a government instrumentality and a sovereign absent a manipulation of the courts. *See infra* note 131 (discussing the similar cases among different circuits in which the same presumption applies).

55. *Bridas I*, 345 F.3d at 360 (quoting *Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524, 528 (5th Cir. 2000)).

56. *Id.* at 361 (quoting *J. Douglas Uloth & J. Hamilton Rial III, Equitable Estoppel as a Basis for Compelling Nonsignatories to Arbitrate—A Bridge Too Far?*, 21 REV. LITIG. 593, 632 (2002)).

57. *Id.* at 359–60. As alter-ego determinations are inherently fact sensitive, the district court erred in basing its holding that Turkmenneft and the Government were not alteregos solely on the presence of corporate formalities. *Id.*

status.⁵⁸ A second appeal ensued.⁵⁹ In a 2006 decision, the Fifth Circuit again reversed the district court and confirmed the arbitration award.⁶⁰ The Fifth Circuit held that Turkmenneft was the alter ego of the Government of Turkmenistan.⁶¹ In order to invoke the alter-ego exception to the presumption that a parent corporation is not liable for the conduct of its subsidiary, the Fifth Circuit required that “(1) the owner exercised complete control over the corporation with respect to the transaction at issue and (2) such control was used to commit a fraud or wrong that injured the party seeking to pierce the veil.”⁶² Because of the alter-ego finding, the court was entitled to “pierce the veil”⁶³ dividing Turkmenneft and the Government, and to attribute the actions of one to the other.⁶⁴ The court noted that corporate separateness is a “bedrock principle of corporate law” and that veil-piercing “is reserved for exceptional cases.”⁶⁵

Despite their conclusive holding that no agency relationship existed between Turkmenneft and the Government, the Fifth Circuit concluded that Turkmenneft’s lack of financial independence established the control required to pierce the corporate veil.⁶⁶ In addressing the “fraud or injustice” prong of alter-ego liability, the court concluded that the Government manipulated Turkmenneft in an attempt to avoid liability for breach of contract for either Turkmenneft or the Government.⁶⁷

58. *Bridas S.A.P.I.C. v. Gov’t of Turkmenistan (Bridas II)*, 447 F.3d 411, 415–16 (5th Cir. 2006).

59. *Id.*

60. *Id.* at 420.

61. *Id.*

62. *Id.* at 416 (quoting *Bridas I*, 345 F.3d at 359). Surprisingly, the Fifth Circuit did not even mention *Bancec*, “[t]he leading case on the subject of government liability for actions of government agents and instrumentalities . . .” Alford, *supra* note 26, at 4.

63. As the Supreme Court noted, this area of corporate law is clouded by metaphor. *First Nat’l City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611, 623 (1983). If a parent and subsidiary are alteregos, then a court is entitled to disregard the general rule that a parent is insulated from liability for the actions of its subsidiary. See *infra* section IV.B (discussing the alter-ego theory).

64. See *Bridas II*, 447 F.3d at 420 (ordering enforcement of the arbitration award and concluding “that the Government acted as the alterego of Turkmenneft in regard to this Joint Venture Agreement with Bridas”).

65. *Id.* at 416.

66. See *id.* at 420 (“The fact that a subsidiary maintains what amounts to a ‘zero balance,’ and relies exclusively upon another entity to service its debts, is strong evidence that the subsidiary lacks an independent identity.”). In *Bridas I*, the court explained that agency and alter-ego determinations encompass different inquiries because the laws of agency are contractual in nature, and the alter-ego doctrine is rooted in equity. *Bridas I*, 345 F.3d at 359. “Courts are thus comparatively free from the moorings of the parties’ agreements when considering whether an alter ego finding is warranted.” *Id.*

67. See *Bridas II*, 447 F.3d at 417.

The court based this conclusion on the fact that the Government changed the entity comprising the “Turkmenian Party” under the JVA and undercapitalized the new entity.⁶⁸ According to the court, this action satisfied the “fraud or injustice” standard because it prevented Bidas from recovering a substantial damage award in their breach of contract action.⁶⁹ Together, these control and injustice findings led the Fifth Circuit to hold that *Bidas* presented a quintessential case for piercing the corporate veil and that the arbitration award must be enforced because the Government was bound to the original JVA and, as a result, to the arbitration proceedings.⁷⁰

B. *The Bancec Presumption*

Understanding the Supreme Court’s decision in *First National City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*⁷¹ is central to understanding the import of *Bidas*. In *Bancec*, the Supreme Court faced the question of whether an instrumentality of the Cuban government could be held liable for actions of its sovereign parent that allegedly violated international law.⁷² In formulating an answer to this question, the Court determined that “government instrumentalities established as juridical entities distinct and independent from their sovereign should normally be treated as such.”⁷³

In *Bancec*, the Cuban Government gave the Banco Para el Comercio Exterior de Cuba (Bancec) statutory authority to act as the Cuban Government’s “exclusive agent,” and afforded Bancec full juridical capacity in its own right.⁷⁴ After its establishment, Bancec entered into a commercial transaction facilitated by an irrevocable letter of credit issued by First National City Bank (Citibank).⁷⁵ Bancec then assigned the letter of credit to Cuba’s central bank, Banco Nacional, for collection.⁷⁶ When Banco

68. *Id.*

69. *Id.* at 417; *see also id.* at 420 (“Despite some indicia of separateness, the reality was that when the Government’s export ban forced Bidas out of the joint venture, the Government then exercised its power as a parent entity to deprive Bidas of a contractual remedy.”).

70. *See id.* (summarizing findings and concluding that this was a “rare case” in which piercing the veil was necessary).

71. *First Nat’l City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611 (1983).

72. *Id.* at 613.

73. *Id.* at 626–27.

74. *Id.* at 613–14.

75. *Id.* at 614.

76. *Id.*

Nacional presented the draft to Citibank for payment, Citibank offset the amount owed to Banco Nacional by deducting the value of Citibank's assets seized and nationalized by the Cuban Government.⁷⁷ Bancec brought suit in a U.S. district court to recover the full amount owed to it under the letter of credit.⁷⁸ Bancec claimed that as a separate, distinct instrumentality of a foreign government, it could not be held liable for actions taken by the sovereign.⁷⁹

The Court indicated that, as a general rule, a presumption of separate legal status exists between a government instrumentality and its sovereign.⁸⁰ It grounded this presumption on the distinct nature of government instrumentalities and the special role they play in the international arena.⁸¹ The Court concluded that disregarding the separate status of government instrumentalities would wreak havoc on the international economic community by causing uncertainty and leading to a general disdain of contracting with state instrumentalities.⁸²

The Court went on to address the issue of whether the presumption of independent status could be overcome in certain circumstances, thus allowing a court to "pierce the veil" and hold the instrumentality liable for the actions of the Cuban Government under the alter-ego theory.⁸³ The Court announced two exceptions to the presumption of separateness: first, "where a corporate entity is so extensively controlled by its owner that a

77. *Id.* at 614–15.

78. *Id.* at 613.

79. *Id.* at 619–20.

80. *Id.* at 626–27.

81. *Id.* at 624 ("Increasingly during this century, governments throughout the world have established separately constituted legal entities to perform a variety of tasks."). Quoting a legal scholar, the Court commented that "[s]eparate legal personality has been described as 'an almost indispensable aspect of the public corporation.'" *Id.* at 625 (quoting W. Friedmann, *Government Enterprise: A Comparative Analysis*, in *GOVERNMENT ENTERPRISE: A COMPARATIVE STUDY* 303, 314 (W. Friedmann & J. Garner eds., 1970)).

82. *Id.* at 626 ("Freely ignoring the separate status of government instrumentalities would result in substantial uncertainty over whether an instrumentality's assets would be diverted to satisfy a claim against the sovereign, and might thereby cause third parties to hesitate before extending credit to a government instrumentality without the government's guarantee.").

83. *See id.* at 628–30 (reviewing corporate veil-piercing concepts and concluding that similar principles could be applied to governments and their instrumentalities). The Court reviewed cases discussing private corporate law and noted those cases have "long recognized 'the broader equitable principle that the doctrine of corporate entity, recognized generally and for most purposes, will not be regarded when to do so would work fraud or injustice.'" *Id.* at 629 (quoting *Taylor v. Standard Gas & Elec. Co.*, 306 U.S. 307, 322 (1939)).

relationship of principal and agent is created,”⁸⁴ and second, where recognition of an instrumentality’s separate legal status “would work fraud or injustice.”⁸⁵ The Court supported these exceptions to the general rule by pointing out that holding otherwise would allow Cuba to shield itself from liability by abusing the corporate form.⁸⁶ Thus, the Court permitted Citibank to offset the amount under the letter of credit by the value of Citibank’s nationalized assets.⁸⁷

IV. ANALYSIS

Understanding the nuances of *Bridas* and the problematic implications of the court’s reasoning therein requires further explication of what the third-party problem entails. Thus, this section will further explore that topic by addressing the third-party problem generally and then by examining the alter-ego theory, the method the Fifth Circuit used to bind the Government of Turkmenistan to the arbitration agreement.⁸⁸ Next, this section will illustrate how the Fifth Circuit’s decision in *Bridas* violated the intent of the parties involved, undermined the consensual basis of arbitration, and set a dangerous precedent for future cases involving government instrumentalities.

A. *The Third-Party Problem*

The contractual nature of arbitration requires that each party manifest some indicia of consent to the agreement to arbitrate before being subject to the jurisdiction of an arbitrator.⁸⁹ Thus, a party must generally be a signatory to an arbitration agreement before an arbitrator has the jurisdiction necessary to render an award.⁹⁰ Courts and arbitrators alike, however,

84. *Id.* at 629.

85. *Id.* (quoting *Taylor*, 306 U.S. at 322).

86. *See id.* at 633 (“Cuba cannot escape liability for acts in violation of international law simply by retransferring the assets to separate juridical entities.”). The Court pointed out that because Bancec was dissolved after the nationalization of the banks, the real beneficiary of the letter of credit would be the Government of Cuba. *Id.* at 632. Thus, the Government could not obtain relief in a U.S. district court without waiving its sovereign immunity defense, which would subject the Cuban Government to a counterclaim by Citibank for the value of Citibank’s assets seized in the nationalization. *Id.*

87. *Id.* at 633.

88. *See Bridas S.A.P.I.C. v. Gov’t of Turkmenistan (Bridas II)*, 447 F.3d 411, 416–17, 420 (5th Cir. 2006) (applying the alter-ego theory to bind the Government of Turkmenistan to the arbitration agreement).

89. *See Hosking*, *supra* note 2, at 476–77 (describing such consent as “[t]he threshold question in arbitration”).

90. *See Grigson v. Creative Artists Agency, L.L.C.*, 210 F.3d 524, 528 (5th Cir. 2000) (“[A]rbitration is a matter of contract and cannot, in general, be required for a matter

demonstrate willingness to bind a nonsignatory to an arbitration agreement in the event some other manifestation of consent to the agreement is present.⁹¹ U.S. courts agree that the judiciary should apply domestic principles of contract law in analyzing whether or not an arbitration agreement binds a nonsignatory.⁹² Courts invoke “incorporation by reference, assumption, agency, veil-piercing/alter ego, estoppel,” and third-party beneficiary theories to bind nonsignatories to arbitration agreements.⁹³

According to one commentator, the extension of the arbitration clause of a contract to nonsignatories—the third-party problem—is “one of the most difficult topics in international arbitration.”⁹⁴ Confusion and uncertainty are inherent in the third-party problem.⁹⁵ Because the law of the site of the arbitration determines who is bound by an arbitration clause, judicial review of an arbitration award will vary drastically depending on where the arbitration takes place.⁹⁶ The structure of U.S. law—in which contract law is state law—compounds this problem; fifty different state contract regimes create a vast number of possible resolutions to judicial review of

involving an arbitration agreement non-signatory . . .”).

91. See Carolyn B. Lamm & Jocelyn A. Aqua, *Defining the Party—Who Is a Proper Party in an International Arbitration Before the American Arbitration Association and Other International Institutions*, 34 GEO. WASH. INT’L L. REV. 711, 713 (2003) (“Although consent of the parties remains an underlying consideration foremost in the minds of the arbitrator or judge, decisions rendered by arbitral tribunals . . . and recently by U.S. federal courts, reflect a general trend to extend the arbitrability of many international disputes to non-signatories . . .”).

92. See DiLeo, *supra* note 17, at 36 (“The law of arbitration is essentially contractual, thus the presumption in favor of arbitration means that courts will analyze the scope of such agreements using state contract law principles to answer the question of who is bound.”). A court should only become entangled in the arbitrability question in the absence of clear and unmistakable evidence that the parties intended to commit such questions to the arbitrator; if the parties manifested an intent to allow the arbitral tribunal to determine its own jurisdiction, then courts should respect the decision of the arbitrator. See *supra* notes 5–6 and accompanying text (discussing how courts should react to arbitrability questions).

93. Thomson-CSF, S.A. v. Am. Arbitration Ass’n, 64 F.3d 773, 776 (2d Cir. 1995) (punctuation omitted).

94. Hosking, *supra* note 2, at 473 (quoting Marc Blessing, *The Arbitration Agreement—Its Multifold Critical Aspects*, in THE ARBITRATION AGREEMENT—ITS MULTIFOLD CRITICAL ASPECTS, ASA Special Ser. No. 8, 18 (1994)).

95. For example, one commentator compared legal systems in England, France, and the United States, and their approaches to third parties in arbitration and contract law, and concluded that the third-party problem arises because “there is inconsistency within each jurisdiction’s application of specific legal theories.” Hosking, *supra* note 2, at 490–560. In attempting to organize these theories into a manageable framework, the author noted that categorization is a difficult task. *Id.* at 487.

96. See DiLeo, *supra* note 17, at 36 (noting that the law of the state where an arbitration occurred applies to later judicial review of the arbitration).

an arbitration dispute.⁹⁷ In addition, arbitration disputes are often removed to federal courts, adding the additional complexity created when federal courts attempt to apply state law doctrines.

The confusion created by the inability to categorize the legal theories which will apply to judicial review of an international arbitration illustrates one aspect of the third-party problem. The inability to predict with certainty which legal theories—and of which country—a court will apply is yet another. These uncertainties necessarily impose costs on all international transactions.⁹⁸ International arbitration owes its existence to the fact that arbitration provides a neutral forum to resolve international disputes.⁹⁹ In turn, the availability of a neutral forum fuels the firestorm of international business transactions sweeping the global economy.¹⁰⁰ The coveted neutral forum provided by international arbitration will become nothing more than an illusion if domestic law continues to be the primary source governing judicial review of international arbitrations.

The next section addresses the alter-ego veil-piercing theory, one specific methodology used to bind a nonsignatory to an arbitration agreement.

B. *The Mists of Metaphor*:¹⁰¹ *Veil-Piercing in General*

Courts are commonly asked to bind a nonsignatory to an arbitration agreement in two recurring fact situations: “[1] ‘groups of companies’ situations in which it is claimed that companies in the corporate chain other than just the signatory company are bound by the arbitration agreement and [2] ‘state entity’ disputes in which [a party] seek[s] to bind a state to the arbitration clause entered into by a [government instrumentality].”¹⁰² As evidenced by *Bridas*, U.S. courts use the alter-ego theory to resolve both of these scenarios.¹⁰³ The alter-ego theory developed in response to

97. See, e.g., Stephen K. Huber, *Arbitration and Contracts: What Are the Law Schools Teaching?*, 2 J. AM. ARB. 209, 248 (2003) (stating that “contract law is state law”).

98. See Park, *supra* note 6, at 1257 (“Without predictability about applicable substantive and procedural norms, business managers may . . . charge greater prices to cover the risk of uncertainty in the event of dispute.”).

99. See *supra* notes 9–11 and accompanying text (discussing why businesses use international arbitration).

100. *Id.*

101. *Berkey v. Third Ave. Ry. Co.*, 155 N.E. 58, 61 (N.Y. 1926) (Cardozo, J.) (“The whole problem of the relation between parent and subsidiary corporations is one that is still enveloped in the mists of metaphor.”).

102. See Hosking, *supra* note 2, at 480 (discussing the two scenarios that have “heavily influenced” the doctrine concerning third parties in arbitration).

103. See *Bridas S.A.P.I.C. v. Gov’t of Turkmenistan (Bridas II)*, 447 F.3d 411, 416–17, 420 (5th Cir. 2006) (finding that both corporations and foreign government entities

the limited liability usually enjoyed by a parent corporation with respect to its subsidiaries. Generally speaking, a parent corporation is regarded as a distinct legal entity from its subsidiaries or affiliates, and the parent will not be held directly liable for the actions of its affiliates absent “exceptional circumstances.”¹⁰⁴ This general rule reflects the fact that the corporate vehicle (including limited liability) is the grease that turns the wheel of international commerce.¹⁰⁵ However, courts will “pierce the veil” that insulates a parent corporation from liability for the actions of its subsidiary upon a finding that the two entities are “alter-egos.”¹⁰⁶ The alter-ego doctrine is grounded in equity, and courts generally invoke the doctrine according to the equitable principles of justice and necessity.¹⁰⁷ Thus, before disregarding the general rule of separate legal status, U.S. courts usually require a showing that the corporate form has been used to perpetrate some fraud or injustice, or that the parent has so dominated the affairs of the subsidiary that they are essentially one entity.¹⁰⁸

In the arbitration context, this doctrine means that a parent corporation may be forced to arbitrate based on a contract signed by the subsidiary, but not the parent itself, as long as a court finds that the two entities are alter egos.¹⁰⁹ The same

can be bound to an arbitration using the alter-ego theory).

104. Nelson, *supra* note 41, at 584.

105. See *id.* (noting that “the corporation is a basic building block of the modern economy”). Without this presumption of separate legal status, business transactions would be chilled by the threat of uncertain and unpredictable liability. See *id.* (stating that the doctrine allows courts to “foster an atmosphere of business certainty”).

106. See Eisen, *supra* note 12, at 42–43 (describing the alter-ego theory of third party arbitration). In discussing piercing the veil between a government and its instrumentality, the Supreme Court has cautioned against allowing dramatic imagery to usurp the role reserved for careful analysis: “The whole problem of the relation between parent and subsidiary corporations is one that is still enveloped in the mists of metaphor. Metaphors in law are to be narrowly watched, for starting as devices to liberate thought, they end often by enslaving it.” *First Nat’l City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611, 623 (1983) (quoting *Berkey*, 155 N.E. at 61).

107. See *Bridas S.A.P.I.C. v. Gov’t of Turkmenistan (Bridas I)*, 345 F.3d 347, 359 (5th Cir. 2003) (“[T]he alter ego doctrine can be invoked ‘only where equity requires the action to assist a third party.’” (quoting *McCarthy v. Azure*, 22 F.3d 351, 362–63 (1st Cir. 1994))).

108. See Eisen, *supra* note 12, at 42–43 (explaining that alter-ego liability may be invoked “where a showing of fraud or other legal wrong can be made, or where the affairs of the subsidiary have been so dominated by the parent that the parent is effectively controlling the subsidiary”). The *Bridas I* court required a showing of fraud or wrong and control before piercing the veil. *Bridas I*, 345 F.3d at 359.

109. Eisen, *supra* note 12, at 42–43. In making the alter-ego determination, courts look to the observance of corporate formalities, financial independence of the subsidiary, physical convergence of the two entities, and a host of other variegated factors. See *id.* at 43 (listing business practices which the court should consider); see also *Bridas I*, 345 F.3d

considerations that lead courts to eschew alter-ego liability in domestic litigation are doubly present in international arbitration: not only do the liability-limiting features of the corporate form ease the business of international business, but the preeminent role of consent in arbitration cuts against binding parties to agreements they have not signed. Thus, the alter-ego veil-piercing theory should remain the exception rather than the rule.

C. *How the Fifth Circuit Got It Wrong*

The Fifth Circuit erred in two fundamental respects in *Bridas*. First, the court should not have undertaken an independent jurisdictional review, as there was clear and convincing evidence that the parties to the arbitration intended to submit that issue to the arbitrator.¹¹⁰ Second, having decided to analyze the jurisdictional question, the court should not have applied domestic corporate law to order a sovereign nation to pay damages. This section will discuss both problems.

The Fifth Circuit should have respected the parties' agreement to submit jurisdictional issues to the arbitrator. The JVA containing the agreement to arbitrate incorporated the ICC rules.¹¹¹ These rules delegate the authority to determine the scope of the arbitration agreement to the arbitrator and expressly state that the arbitrator's jurisdiction does not evaporate in the face of claims that no agreement to arbitrate exists.¹¹² In addition to

at 360 n.11 (instructing the district court to consider at least twelve different factors when deciding an alterego issue).

110. The Author recognizes that the clear and convincing evidence doctrine originated in the context of *signatories*. However, there is no reason that the doctrine cannot apply to determine whether nonsignatories consented to allowing the arbitrator to determine whether the nonsignatory is bound to the arbitration agreement. This argument carries special weight in the *Bridas* context because there is such clear evidence that the nonsignatory did consent to the jurisdiction of the arbitrator.

111. *Bridas I*, 345 F.3d at 351–52. The ICC is an international business organization designed to further international trade. See International Chamber of Commerce, *What Is ICC?*, <http://www.iccwbo.org/id93/index.html> (last visited Jan. 15, 2008) (“ICC . . . is the voice of world business championing the global economy as a force for economic growth, job creation and prosperity.”). Dispute resolution is one of the organization's primary functions. *Id.*

112. See INT'L CHAMBER OF COMMERCE, *supra* note 31, art. 6, para. 4.

[T]he Arbitral Tribunal shall not cease to have jurisdiction by reason of any claim that the contract is null and void or allegation that it is non-existent, provided that the Arbitral Tribunal upholds the validity of the arbitration agreement. The Arbitral Tribunal shall continue to have jurisdiction to determine the respective rights of the parties and to adjudicate their claims and pleas even though the contract itself may be non-existent or null and void.

Id.; see also *id.* art. 6, para. 2 (providing that, in the event one party raises claims concerning the scope of the arbitration agreement, “any decision as to the jurisdiction of

incorporating the ICC rules into the JVA, the parties to the arbitration, *including the Government of Turkmenistan*, signed terms of reference prior to the arbitration which explicitly submitted to the arbitrator the jurisdictional issues presented by the case.¹¹³

Arguably, the incorporation of the ICC rules into the arbitration agreement, together with the terms of reference signed by all parties, constitute the required “clear and unmistakable evidence” that all parties—including the nonsignatory Government—agreed to arbitrate the issue of arbitrability.¹¹⁴ By contracting to have all disputes resolved according to the ICC rules, and by signing pre-arbitration terms of reference that incorporated those rules, the participants in the arbitration agreed to be bound by the provisions of those rules. The relevant ICC provisions clearly and unmistakably allow the arbitrator to determine her own jurisdiction.¹¹⁵ The pre-arbitration terms of reference stated that the arbitrator was to consider the issue of whether “the arbitral tribunal ha[d] the jurisdiction to decide whether the Government is a proper party to this arbitration’ and ‘if so, [was] the Government a proper party to this arbitration.”¹¹⁶ The fact that the Government of Turkmenistan signed the terms of reference conclusively resolves any lingering questions regarding whether the Government—a nonsignatory to the JVA incorporating the ICC rules—agreed to submit issues concerning the scope of the agreement to the arbitrator.¹¹⁷

the Arbitral Tribunal shall be taken by the Arbitral Tribunal itself”).

113. See Alford, *supra* note 26, at 3 (stating that the terms of reference—signed by both Bidas and the Government—included the question of whether the arbitral tribunal would have jurisdiction to decide whether the Government was a party to the arbitration).

114. See *First Options of Chi., Inc. v. Kaplan*, 514 U.S. 938, 944 (1995) (“Courts should not assume that the parties agreed to arbitrate arbitrability unless there is ‘clea[r] and unmistakabl[e]’ evidence that they did so.” (quoting *AT&T Techs., Inc. v. Commc’ns Workers*, 475 U.S. 643, 649 (1986) (alteration in original))); see also *supra* notes 5–6 and accompanying text (proffering that courts should use some restraint in judicial review of international arbitration awards). Other courts of appeals have held that incorporating the ICC rules evinces intent to submit questions of arbitrability to arbitration. See *Shaw Group Inc. v. Triplefine Int’l Corp.*, 322 F.3d 115, 122 (2d Cir. 2003) (holding that an agreement to resolve all disputes in accordance with the rules and procedures of the ICC manifested an intent to allow an arbitrator to resolve arbitrability issues); *Apollo Computer, Inc. v. Berg*, 886 F.2d 469, 473 (1st Cir. 1989) (same).

115. See *supra* note 112 and accompanying text (quoting the relevant ICC Rules of Arbitration provisions).

116. See Alford, *supra* note 26, at 3 (quoting Terms of Reference at 11–12, *Bidas S.A.P.I.C. v. Gov’t of Turkmenistan*, No. 9058/FMS (ICC Int’l Ct. of Arb. June 15, 1999), reprinted in Mealy’s Doc. No. 05-011026-011X).

117. According to one commentator, “[i]f there was any doubt as to whether the parties committed the question to the tribunal in the original contract, those doubts

The Fifth Circuit ignored the parties' "clear and unmistakable" intent to allow the arbitrator to determine the scope of the arbitration agreement and concluded that the case warranted an independent jurisdictional review.¹¹⁸ This holding undermines the purpose of international arbitration. The threat of independent jurisdictional review of every arbitration award imposes significant transaction costs on parties to complex international transactions.¹¹⁹ By choosing to resolve their disputes in arbitration, the parties to this dispute manifested the intent to avoid litigating disputes in an unfamiliar and possibly hostile forum, to promote efficiency and economy, and to ensure the confidentiality of the proceedings.¹²⁰ These intentions were thwarted by nearly six years of costly litigation in American courts.

The jurisdictional questions in *Bridas* require a detailed examination of the relationship between the Government of Turkmenistan and its instrumentality, and whether the actions of one can fairly be attributed to the other. These questions go directly to the merits of the case and involve the kind of detailed and careful analysis the parties intended to, and did, submit to the arbitral panel.¹²¹ In undertaking an independent jurisdictional review, the Fifth Circuit ignored the parties' express intentions.

The *Bridas* case is international in every sense of the word. American courts should not squander their limited time and resources solving disputes that have clearly been committed to arbitration. The threat of foreign litigation will dampen international contracting or cause it to become less lucrative.¹²² At the very least, parties familiar with the paternalistic and

should have been eliminated with the signing of the ICC terms of reference." *Id.*

118. *Bridas S.A.P.I.C. v. Gov't of Turkmenistan (Bridas I)*, 345 F.3d 347, 354 & n.4 (5th Cir. 2003) (recalling that the district court found no clear and unmistakable evidence of consent and noting that the district court's independent review was proper under the circumstances).

119. *See Park, supra* note 6, at 1257 ("For many wealth-creating transactions, the prospect of foreign court intervention will chill cross-border economic cooperation, causing productive transactions to falter or become more expensive."). These costs are not only born by the parties; the court itself surely devoted significant time and resources to this dispute.

120. *See Craig, supra* note 8, at 2-3 (discussing why arbitration is more appealing to companies engaged in international business).

121. This is not a case in which the arbitral panel made a cursory or unfounded decision regarding jurisdiction. *See Alford, supra* note 26, at 3-4 ("The arbitral tribunal analysis regarding the question is complex and detailed and suggests a careful parsing of the letter and spirit of the JVA.").

122. *See supra* note 119 and accompanying text (noting that an increase in court intervention will "chill" international transactions).

interventionist tendencies of the Fifth Circuit will avoid Houston as an arbitral situs.¹²³

In addition to the problems caused by the Fifth Circuit's independent jurisdictional review, the court set a dangerous precedent by applying domestic corporate law to the issue of whether a sovereign nation may be bound by the acts of its instrumentality.¹²⁴ Much litigation and legislation illustrate the fact that governments are different.¹²⁵ Courts should not import principles that govern corporate liability in the private sector into suits involving the public sector.¹²⁶

Although the relationship between government instrumentalities and the sovereign mirror that between a parent corporation and a subsidiary in some respects, the special considerations present in the government context warrant a distinct alter-ego analysis. Government instrumentalities are an essential ingredient in the economic progress of developing countries.¹²⁷ The separate legal status of such public enterprises enables third parties to freely contract with government instrumentalities without fear of facing a sovereign immunity defense.¹²⁸ Cavalier disregard of the independence of government instrumentalities will chill economic growth in underdeveloped countries, create uncertainty, and place countries with large

123. See Park, *supra* note 6, at 1253 (“The prospect of such judicial meddling in the arbitral process can only alarm foreign enterprises contemplating arbitration in the United States.”).

124. Moreover, the parties, an Argentinean corporation and a Turkmenian instrumentality, cannot possibly have imagined that U.S. corporate law would govern their dispute. The business transaction at issue had no nexus with U.S. commerce. In addition, the contract stated that the relationship between the parties would be governed by English law. See *Bridas S.A.P.I.C. v. Gov't of Turkmenistan (Bridas II)*, 447 F.3d 411, 416 n.5 (5th Cir. 2006) (admitting an “air of unreality” because the court is deciding a “wholly foreign dispute . . . fortuitously arbitrated in this country”).

125. Under the Foreign Sovereign Immunity Act, a foreign state is immune from suit in the United States unless the state's conduct falls within one of the statutory exceptions. 28 U.S.C. § 1604 (2000). The act of state doctrine limits the ability of American courts to judge the acts of a foreign sovereign. See *Walter Fuller Aircraft Sales, Inc. v. Republic of Philippines*, 965 F.2d 1375, 1387–88 (5th Cir. 1992) (recognizing that the doctrine “prevent[s] courts from judging foreign public acts”).

126. See Alford, *supra* note 26, at 4 (criticizing the *Bridas* court's “wholesale application to the public sector of traditional corporate principles derived from the private sector”).

127. See Friedmann, *supra* note 81, at 333–34 (“[P]ublic enterprise, largely in the form of development corporations, has become an essential instrument of economic development in the economically backward countries which have insufficient private venture capital to develop the utilities and industries which are given priority in the national development plan.”).

128. *First Nat'l City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611, 625–26 (1983).

amounts of state-owned assets at a considerable disadvantage vis-à-vis the rest of the world.¹²⁹

The Supreme Court has clearly determined that government instrumentalities warrant special consideration.¹³⁰ The Fifth Circuit violated this mandate by ignoring the distinct realities presented in the government context, and by applying domestic corporate law to “pierce the veil” between a government instrumentality and its sovereign parent. Courts must employ a different standard in circumstances involving the liability of a sovereign nation.

In recognition of the special status of government instrumentalities, the Fifth Circuit should have looked to *Bancec* for guidance, rather than exclusively to private sector corporation law. An examination of *Bancec* would have revealed the facts of *Bridas* simply do not warrant invocation of the *Bancec* exception. As other circuits have recognized,¹³¹ the *Bancec* Court was primarily concerned with the injustice of allowing the Cuban Government to reap the benefit of the American court system

129. *See id.* at 626 (“Freely ignoring the separate status of government instrumentalities would result in substantial uncertainty over whether an instrumentality’s assets would be diverted to satisfy a claim against the sovereign, and might thereby cause third parties to hesitate before extending credit to a government instrumentality . . .”).

130. *See id.* at 623–28 (discussing the nature of government instrumentalities).

131. In considering cases involving foreign instrumentalities, other circuits have looked to *Bancec* for guidance and have construed the exceptions to the presumption of separate status narrowly, requiring an affirmative misuse of the U.S. court system or a violation of international law before treating a state-owned instrumentality and the state as one entity. *See, e.g.*, *Flatow v. Islamic Republic of Iran*, 308 F.3d 1065, 1071–73 (9th Cir. 2002) (rejecting the argument that the circumstances of the case warrant overcoming the *Bancec* presumption and noting that no party is “attempting to use a United States court to recover on a claim while at the same time trying to avoid being the subject of an adversary proceeding”); *Transamerica Leasing, Inc. v. La Republica de Venezuela*, 200 F.3d 843, 847–48, 852 (D.C. Cir. 2000) (recognizing that the *Bancec* rule was formulated to answer the question of whether a foreign sovereign may be held responsible for the conduct of its instrumentality and holding that, under the *Bancec* rule, an attempt to revive a commercial instrumentality by injecting state funds to cover the instrumentality’s losses did not justify disturbing the presumption of separate legal status); *Alejandre v. Telefonica Larga Distancia de P.R., Inc.*, 183 F.3d 1277, 1286 (11th Cir. 1999) (holding that inability to collect “is not a sufficient basis for overcoming the presumption of separate juridical status”); *Fed. Ins. Co. v. Richard I. Rubin & Co.*, 12 F.3d 1270, 1290 n.16 (3d Cir. 1993) (explaining that the Supreme Court’s *Bancec* opinion, in crafting exceptions to the important principle of separate legal status, was primarily concerned with preventing a foreign state from creating a separate entity and then hiding behind that entity to avoid liability); *Banco Nacional de Cuba v. Chem. Bank N.Y. Trust Co.*, 782 F.2d 377, 380 (2d Cir. 1986) (concluding that the injustice exception to the general presumption of separateness identified in *Bancec* did not apply to a mere breach of loan agreement, in which there was no attempt to manipulate the U.S. courts to avoid liability for a violation of international law). Unlike its sister courts, the Fifth Circuit required neither a violation of international law nor an affirmative misuse of U.S. courts before piercing the veil in *Bridas*.

while simultaneously avoiding liability for its violations of international law.¹³² Those concerns are not implicated in *Bridas*. *Bridas* is not a case in which a government instrumentality initiated suit and then asserted its separate status in order to avoid liability for violations of international law. Rather, *Bridas* involves a dispute between an active government instrumentality and an Argentinean corporation in which the foreign government is seeking no benefit from the U.S. court.¹³³

The wholesale application of domestic corporation law to a dispute involving a government instrumentality is a clear departure from other cases considering the same issue.¹³⁴ Moreover, by invoking the exceptions to the *Bancec* presumption over a mere contract dispute, the Fifth Circuit unnecessarily broadened the circumstances under which a foreign court may adjudicate a foreign government's actions.¹³⁵ Other courts deciding the question have limited the circumstances under which a government instrumentality and its sovereign may be regarded as alter egos to cases presenting affirmative misuse of American courts to duck liability for violations of international law.¹³⁶ Specifically, those courts have squarely rejected a claim that a contract breach—resulting from a government's failure to provide an instrumentality with enough capital to cover its debts—provides grounds for disregarding the *Bancec* presumption of separate legal status.¹³⁷ In ignoring the Supreme Court's mandate that "government instrumentalities established as juridical entities distinct and independent from their sovereign should normally be treated as such,"¹³⁸ and in deviating

132. *Bancec*, 462 U.S. at 632. In support of the holding, the Court compared the case to *National City Bank v. Republic of China*, in which the Court remarked, "We have a foreign government invoking our law but resisting a claim against it which fairly would curtail its recovery." *Id.* (quoting *Nat'l City Bank v. Republic of China*, 348 U.S. 356, 361 (1955)).

133. The motion to vacate does not implicate the kind of inequitable misuse of the courts that concerned the Supreme Court in *Bancec*. See *Bridas S.A.P.I.C. v. Gov't of Turkmenistan (Bridas I)*, 345 F.3d 347, 362 (5th Cir. 2003) ("[T]he Government has not sued *Bridas* under the agreement. The Government has thus not 'exploited' the JVA.").

134. *Id.*

135. This broadening is unnecessary because the court could have affirmed the arbitration award on other, narrower grounds. See *infra* notes 139–143 and accompanying text (proposing that the court could have simply confirmed the award because there were no statutory grounds for vacatur).

136. See *supra* note 131 and accompanying text.

137. *Id.* (noting the holdings of *Transamerica* and *Alejandre*, in which undercapitalization of an instrumentality or uncollectibility of a debt was insufficient to pierce the veil dividing an instrumentality from its sovereign).

138. *First Nat'l City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611, 626–27 (1983).

from other courts' interpretation of the parameters of the *Bancec* exceptions, the Fifth Circuit rendered the *Bancec* presumption devoid of any significance.

In sum, the Fifth Circuit has created uncertainty and disarray in "piercing the veil" between the Turkmenistan Party and the Government of Turkmenistan over a mere breach of contract suit. These consequences could have been avoided by respecting the arbitrator's competency to determine jurisdictional issues in the first place.¹³⁹ Had the Fifth Circuit found the requisite evidence evincing intent to arbitrate the issue of arbitrability, the court could have simply confirmed the award based on the fact that the Government did not establish any of the statutory grounds for vacatur.¹⁴⁰ Such a holding would comport with previous case law¹⁴¹ and further the goals underpinning international arbitration. Instead, the court strayed from the Supreme Court's holding in the *Bancec* case and undermined the process through which many developing countries obtain the financial resources needed to make large-scale national investments.¹⁴² The practical result of the court's holding will be an abandonment of the city of Houston as a situs for international arbitrations.¹⁴³

V. CONCLUSION

Bridas is a cautionary tale illustrating the woes of applying domestic contract law to complex international transactions

139. Such a holding comports with the Supreme Court's decision in *First Options of Chicago v. Kaplan*, allowing arbitrators to determine the scope of their own power provided that "clear and unmistakable evidence" demonstrates that the parties intended to commit arbitrability issues to arbitration. *First Options of Chi., Inc. v. Kaplan*, 514 U.S. 938, 944 (1995) (citing *AT&T Techs., Inc. v. Commc'ns Workers*, 475 U.S. 643, 649 (1986)).

140. The incorporation of the ICC rules, combined with the fact that all parties, including the Government, signed the terms of reference submitting the jurisdictional issues to the arbitrator easily meets the "clear and unmistakable evidence" standard. *See supra* notes 111–17 and accompanying text.

141. *See, e.g., AT&T Techs., Inc.*, 475 U.S. at 649 (establishing the "clear and unmistakable evidence" standard) and cases cited therein.

142. *See* Friedmann, *supra* note 81, at 333–34 (explaining that many public corporations enter into partnerships with foreign private enterprises).

143. Because the law of the situs applies to judicial review of arbitrations, *see* Craig, *supra* note 8, at 11, 38–39, any government instrumentality will be sure to negotiate for a forum in which the risk of the sovereign government being ordered to pay a huge sum by a district court is less drastic. Contrary to the Fifth Circuit's assertion that *Bridas* is a "rare" case, *Bridas S.A.P.I.C. v. Gov't of Turkmenistan (Bridas II)*, 447 F.3d 411, 420 (5th Cir. 2006), the ICC has estimated that 30% of its cases involve at least one party at least partially controlled by the state. Craig, *supra* note 8, at 8. Thus, the Fifth Circuit's precedent enlarging the extent to which a state may be bound by the actions of its instrumentality in an international arbitration is not without significance.

involving foreign nations. National courts thwart the carefully bargained-for neutrality coveted by business managers submitting their disputes to international arbitration when they use domestic contract law to bind nonsignatories to an arbitration agreement.¹⁴⁴ The geographical site of arbitration is often a matter of convenience, and the parties to the arbitration often lack any ties to the place of arbitration.¹⁴⁵ In agreeing to resolve their disputes through binding international arbitration, parties to a complex transaction surely never imagined litigating nuanced domestic contract theories involving detailed investigation into the relationships between the parties in national courts.¹⁴⁶

In order to serve the needs and intentions of the international community, U.S. courts should forego independent review of the jurisdiction of the arbitrator when the parties to an arbitration—including nonsignatories to the underlying agreement—commit that question to arbitration. This could be accomplished by amending the FAA to include rules specific to international arbitration.¹⁴⁷ The new statute could create a presumption that when the parties agree to participate in an international arbitration subject to the ICC rules, courts should not undertake an independent review of the arbitrator's jurisdiction, even if one of the participants to the arbitration was a nonsignatory to the arbitration agreement.

If a new arbitration statute limits a court's ability to review the jurisdiction of the arbitrator, the international community must supply a uniform, accessible standard addressing when a foreign sovereign may be bound to arbitrate vis-à-vis the acts of its instrumentality. Professor Alford, a practitioner and scholar of international arbitration, would look to the International Law Commission (ILC) draft articles on Responsibility of States for Internally Wrongful Acts to determine when to hold a sovereign

144. See Craig, *supra* note 8, at 11 (noting that “the state where arbitration is held has legislative jurisdiction to dictate procedural rules for arbitral proceedings in that state, and that the state's courts have the power to enforce such provisions”). After undertaking a study of the contract law of the United States, England, and France, one commentator concluded that the third-party problem is an issue because “there is inconsistency within each jurisdiction's application of specific legal theories.” Hosking, *supra* note 2, at 560.

145. Park, *supra* note 6, at 1265.

146. See Craig, *supra* note 8, at 2–3 (explaining that the desire to avoid onerous litigation in foreign courts is the key factor driving international arbitration).

147. Professor Park, a frequent commentator on international arbitration, has addressed the need for a new statute and proposed statutory language limiting judicial review of international arbitration awards to narrow grounds. See Park, *supra* note 6, at 1248. *Bridas* provides additional support for his position.

liable for acts of its instrumentality.¹⁴⁸ Under the ILC rules, a sovereign would be responsible for the actions of its instrumentality where (1) “the entity is engaged in a governmental function” or (2) “the State is directing or controlling its non-public acts.”¹⁴⁹ This rule is consonant with the “control” exception to the *Bancec* rule, but would eliminate the vagaries of the “injustice” exception.¹⁵⁰

Such clear international standards would promote certainty in international transactions and clarity in the law of international arbitrations. Clear rules would also allow courts to abdicate the responsibility of deciding arbitrability issues without fear that arbitrators would make arbitrary and capricious decisions binding nonsignatories to arbitration agreements. Such an international standard would preserve the consensual basis of arbitration and better serve the goal of avoiding litigation in a foreign court.

Linda R. Boyle

148. See Alford, *supra* note 26, at 6 (describing International Law Commission rules).

149. *Id.*

150. See *First Nat'l City Bank v. Banco Para el Comercio Exterior de Cuba (Bancec)*, 462 U.S. 611, 629 (1983) (announcing that courts may pierce the veil between a state and its instrumentality upon a finding of control or injustice).