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ARBITRATION WITHOUT LAW: CHOICE OF LAW IN FRAND DISPUTES

*Eli Greenbaum**

INTRODUCTION

Recent arbitration between InterDigital and Huawei seems to demonstrate the purported advantages of arbitration as a means of dispute resolution.¹ The warring parties subsumed their multiple suits across different jurisdictions and forums into a single binding arbitral process. By virtue of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards² (“the New York Convention”), the arbitral award would be enforceable across jurisdictions. But even an agreement to arbitrate requires agreement on certain basic matters. On the most fundamental level, it requires agreement on the substantive and procedural laws governing the dispute, as well as the situs—or location—of the arbitration.³ The InterDigital arbitration shows the unfortunate difficulty of bridging even these basic gaps, and the recent Southern District of New York decision in *InterDigital Communications, Inc. v. Huawei Investment & Holding Co.*,⁴ concerning the arbitral award, may make such agreement even harder. At the same time, however, *InterDigital* provides unexpected insight into when proceeding without such agreement can facilitate dispute resolution. An agreement on substantive law may not necessarily provide legal clarity, and arbitrating parties should weigh the difficulty of obtaining consensus on such basic matters against the certainty that substantive law can, in practice, bring to the arbitration.

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1. *See InterDigital Commc'ns, Inc. v. Huawei Inv. & Holding Co.*, 166 F. Supp. 3d 463, 466 (S.D.N.Y. 2016).

2. *See* Convention on the Recognition and Enforcement of Foreign Arbitral Awards art. 1, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38 [hereinafter New York Convention].

3. *See* ALAN REDFERN ET AL., LAW & PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION 119, 159 (4th ed. 2004) (noting that parties should choose governing law “with proper care and consideration” and describing the place of arbitration as a “decision of major importance”). Of course, disputants must make other significant decisions concerning the scope and procedures of the arbitration. *See generally* Jorge L. Contreras & David L. Newman, *Developing a Framework for Arbitrating Standards-Essential Patent Disputes*, 2014 J. DISP. RESOL. 23 (discussing choices for the scope and proceedings of a FRAND arbitration).

4. 166 F. Supp. 3d 463 (S.D.N.Y. 2016).

I. ARBITRATION WITHOUT LAW

InterDigital owned several patents covering technical standards for 3G and 4G wireless technology, and had committed to license these patents under “fair, reasonable and non-discriminatory” (FRAND) terms.⁵ Companies often dispute what constitutes “reasonable” compensation, and InterDigital spent a number of years in litigation with Huawei over the meaning of these FRAND commitments. The dispute with Huawei involved actions in China, an antitrust complaint before the European Commission, hearings before the U.S. International Trade Commission, and suits in the District of Delaware.⁶ Eventually, in December 2013, the parties signed an arbitration agreement, which provided that these disputes would be submitted to arbitration before the International Chamber of Commerce (ICC).⁷

In a relatively common move, the arbitration agreement cleaved the governing law of the arbitration from the situs of the arbitration proceeding.⁸ The arbitration was to take place in Paris, the headquarters of the ICC.⁹ The arbitration agreement itself, however, was governed by New York law, and further provided that disputes that were not within the scope of arbitration could be brought before “state and federal courts in the State of New York.”¹⁰ Unusually, the arbitration agreement expressly provided that no specific law would govern the question at the heart of the arbitration—the parties were allowed to “cite law from any jurisdiction” in arguing what patent license terms would constitute “fair, reasonable and non-discriminatory” compensation.¹¹ In other words, the arbitration agreement provided the arbitrators with no standard or rules for determining what constituted FRAND licensing terms.¹²

The arbitral panel rendered an award in May 2015, which included a determination of the terms of a patent license agreement.¹³ Huawei, unhappy with the decision, filed a motion for vacatur before the Paris

5. *Id.* at 466.

6. *See* InterDigital, Inc., Quarterly Report 8–16 (Form 10-Q) (May 1, 2014) (describing the various proceedings between InterDigital and Huawei).

7. *See* InterDigital, 166 F. Supp. 3d at 467. Pursuant to the settlement agreement, InterDigital retained the right to appeal a Chinese court decision. *See* InterDigital, Inc. Quarterly Report, *supra* note 6, at 10.

8. *See* InterDigital, 166 F. Supp. 3d at 467–68.

9. *See id.* at 467.

10. *Id.* at 468.

11. *Id.*

12. In other situations where the disputants to an international arbitration have not specified any national law to resolve the dispute, but rather stated that arbitrators may issue a decision under a nonnational standard, arbitrators sometimes have employed a conflict of laws analysis to determine applicable national law or have determined that they are empowered to make an award based on “general principles of law,” occasionally referred to as a “*lex mercatoria*.” *See* David W. Rivkin, *Enforceability of Arbitral Awards Based on Lex Mercatoria*, 9 *ARB. INT’L* 67, 68–69 (1993); *see also* Carlo Croff, *The Applicable Law in an International Commercial Arbitration: Is It Still a Conflict of Laws Problem?*, 16 *INT’L LAW* 613, 623–35 (1982).

13. *See* InterDigital, 166 F. Supp. 3d at 466.

courts.¹⁴ InterDigital countered with a petition in the Southern District of New York to confirm and enforce the award, pointing to the provision of the agreement that granted jurisdiction to the New York courts. The Southern District of New York was called upon to decide whether the enforcement proceeding should be stayed pending the outcome of the proceeding in Paris.

The district court, spotlighting the failure of the arbitration agreement to specify substantive law for the central question of the dispute, stayed InterDigital's enforcement petition.¹⁵ The decision relied on the court's interpretation of the New York Convention, a widely adopted convention that governs the enforcement of international arbitral awards.¹⁶ The court noted that the New York Convention divides jurisdictions into "primary" and "secondary" jurisdictions.¹⁷ A court has "primary jurisdiction" if it is in "the country in which, or under the [arbitration] law of which, [an] award was made."¹⁸ Such courts have broad discretion to set aside arbitral decisions. In contrast, a court with "secondary jurisdiction" may only decline to enforce an award for a limited set of enumerated reasons.¹⁹ The *InterDigital* court reasoned that it had only secondary jurisdiction—the situs of the arbitration was in France and, even though the arbitration agreement was governed by New York law, the parties did not specify any governing law for the key issue of what constituted FRAND licensing terms.²⁰ In other words, New York was neither the law of the country "in which" the arbitration took place, nor did it provide the law "under" which the award was made. Given that New York had only secondary jurisdiction under the New York Convention, the court exercised its discretion to stay InterDigital's enforcement action.²¹ Unfortunately, while *InterDigital* seems to follow closely the New York Convention, it in fact seriously misinterprets the treaty. Moreover, such misinterpretation could undercut the sometimes important strategy of agreeing to resolve disputes through arbitration, despite disagreement concerning the law applicable to the dispute.

II. WHAT LAW FOR FRAND?

InterDigital involved FRAND claims—a dispute over InterDigital's commitment to license patents under "fair, reasonable and non-discriminatory" conditions.²² InterDigital made this commitment when it participated in setting the technical standards for 3G and 4G wireless

14. *See id.* at 468.

15. *See id.* at 473.

16. *See id.* at 470; *see also* New York Convention, *supra* note 2.

17. *InterDigital*, 166 F. Supp. 3d at 469.

18. *Id.* (alterations in original) (quoting *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 335 F.3d 357, 364 (5th Cir. 2003)).

19. *Id.*

20. *See id.*

21. *See id.* at 469–70, 472 n.3.

22. *Id.* at 466.

technology, and provided the standard-setting body with patented technology that became “essential” to those standards.²³ Participants in the standard-setting process are typically required by standards organizations to commit to licensing their “standard-essential patents” on FRAND terms.²⁴ FRAND commitments encourage adoption of the standard by providing assurance that proprietary technology in the standard will be available for licensing on reasonable terms.

The FRAND standard, however, can often seem vague and ambiguous, and disputes arise when firms cannot reach an agreement on what constitutes FRAND licensing terms.²⁵ Scholars have long disputed the mechanics for calculating a FRAND royalty,²⁶ and only a limited number of judicial decisions address the matter.²⁷ Moreover, different jurisdictions can view FRAND commitments from starkly diverging perspectives. Some jurisdictions may be solicitous of the rights of patent holders, while others may require patent holders to license their technologies for only minimal compensation. Indeed, the *InterDigital* parties had previously jostled in China, where a court set a FRAND rate that some American scholars believed was “orders of magnitude lower” than ordinary industry demands.²⁸ In other words, what constitutes a FRAND royalty can be characterized by acute legal uncertainty, and this uncertainty is only magnified when the disputing parties come from jurisdictions with different ideas about how to compensate owners of intellectual property rights.

These acute differences explain *InterDigital* and Huawei’s unorthodox choice to resolve their FRAND dispute through arbitration, while also

23. *See* *Certain Wireless Devices with 3G Capabilities and Components Thereof*, Inv. No. 337-TA-800, slip op. at 418–22 (ALJ June 28, 2013) (Initial Determination).

24. Mark A. Lemley & Carl Shapiro, *A Simple Approach to Setting Reasonable Royalties for Standard-Essential Patents*, 28 *BERKELEY TECH. L.J.* 1135, 1136 (2013).

25. Most standard-setting organizations disclaim any role in determining the details of a FRAND license. *See id.* at 1137–38 (2013) (arguing that litigation over FRAND royalties demonstrates the “ambiguities and omissions in the FRAND system”); *see also* Mark A. Lemley, *Intellectual Property Rights and Standard-Setting Organizations*, 90 *CALIF. L. REV.* 1889, 1906 (2002).

26. *Compare* Mark A. Lemley & Carl Shapiro, *Patent Holdup and Royalty Stacking*, 85 *TEX. L. REV.* 1991, 1991 (2007) (proposing methodologies for calculation of FRAND rates), *with* Damien Geradin, *The Meaning of “Fair and Reasonable” in the Context of Third-Party Determination of FRAND Terms*, 21 *GEO. MASON L. REV.* 919, 923–27 (2014) (criticizing the methodology proposed by Lemley & Shapiro).

27. In December 2013, when the *InterDigital* arbitration agreement was signed, only two U.S. courts had addressed the calculation of FRAND rates. *See* *Microsoft Corp. v. Motorola, Inc.*, No. C10-1823JLR, 2013 U.S. Dist. LEXIS 60233, at *1 (W.D. Wash. Apr. 25, 2013); *In re Innovatio IP Ventures, LLC*, No. 11 C 9308, 2013 U.S. Dist. LEXIS 144061, at *1 (N.D. Ill. Sept. 27, 2013).

28. Leon B. Greenfield et al., *SEP Enforcement Disputes Beyond the Water’s Edge: A Survey of Recent Non-U.S. Decisions*, 27 *ANTITRUST* 50, 53 (2013). The Chinese decision also took into account factors that U.S. courts would not have considered, and may have been influenced by government pressure. *See* D. Daniel Sokol & Wentong Zheng, *FRAND in China*, 22 *TEX. INTELL. PROP. L.J.* 71, 90 (2013).

declining to specify the national law applicable to the dispute.²⁹ A growing consensus of scholars and regulators regard arbitration as an efficient means of resolving FRAND disputes.³⁰ These advocates assert that arbitration results in substantial cost savings when compared to the cost of litigating complex patent disputes across several jurisdictions. At the same time, given the potential stark differences between royalty rates set by differing jurisdictions (e.g., the expected divergence between the royalty rates in Chinese and U.S. courts in the *InterDigital* litigation), parties may not be able to agree on an appropriate governing law. While not specifying applicable law can increase legal uncertainty,³¹ this may be less relevant to disputes (such as FRAND) where the appropriate resolution requires empirical comparison to, and detailed economic analysis of, similar licensing agreements.³² Here, the parties may have decided that the costs of failing to agree on governing law were not high in a dispute focused on such specific economic terms and where the substantive law of no jurisdiction could provide clear legal guidance as to the details of such terms.

29. The *InterDigital* arbitration involved technical standards administered by at least three standards organizations—the European Telecommunications Standards Institute (ETSI), the Telecommunications Industry Association (TIA), and the International Telecommunications Union (ITU). See *Certain Wireless Devices with 3G Capabilities and Components Thereof*, Inv. No. 337-TA-800, slip op. at 418–19 (ALJ June 28, 2013) (Initial Determination). The FRAND commitment to ETSI expressly provided that it would be governed by French law. See *id.* at 422. In contrast, the Chinese decision setting FRAND rates asserted that the dispute should be governed by Chinese law. See Sokol & Zheng, *supra* note 28, at 90; see also *supra* note 28 and accompanying text (discussing generally the Chinese decision). The policies of the TIA and ITU do not specify any governing law. See TIA, TIA INTELLECTUAL PROPERTY RIGHTS POLICY (IPR POLICY) (1st ed. 2014), http://www.tiaonline.org/sites/default/files/pages/IPRP-2014May01_0.pdf [<https://perma.cc/WZZ2-73T9>]; *Common Patent Policy for ITU-T/ITU-R/ISO/IEC*, ITU, <http://www.itu.int/en/ITU-T/ipr/Pages/policy.aspx> (last visited Nov. 10, 2016) [<https://perma.cc/RDD9-STQH>].

30. See, e.g., Lemley & Shapiro, *supra* note 24; Kai-Uwe Kühn et al., *Standard Setting Organizations Can Help Solve the Standard Essential Patents Licensing Problem*, CPI ANTITRUST CHRON., Mar. 2013, at 1, 4.

31. See Note, *General Principles of Law in International Commercial Arbitration*, 101 HARV. L. REV. 1816, 1819 (1988) (asserting that when parties specify arbitration by general principles of law, the “results become unpredictable, and parties to agreements have little ground on which to base their expectations”); see also Christopher R. Drahozal, *Contracting out of National Law: An Empirical Look at the New Law Merchant*, 80 NOTRE DAME L. REV. 523, 533 (2005) (asserting that “contractual choice of law avoids uncertainty”).

32. Both Chinese and American approaches to determining FRAND rates rely on comparisons to similar licensing agreements. U.S. courts typically use a list of fifteen so-called *Georgia-Pacific* factors to determine royalty rates for patented technology. *Georgia-Pacific Corp. v. U.S. Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970); see also Lemley, *supra* note 25, at 1914 n.84 (stating that “the fifteen *Georgia-Pacific* factors have become a standard measure of reasonable royalties in patent cases”). Factor one involves examination of royalties previously paid for the patent in suit and factor two involves comparison to licensing rates paid for comparable patents. See *Microsoft*, 2013 U.S. Dist. LEXIS 60233, at *54. For a summary of how Chinese courts have also used comparison methodologies to set FRAND rates, see Fei Deng & Su Sun, *Determining the FRAND Rate: U.S. Perspectives on Huawei v. InterDigital*, CPI ANTITRUST CHRON., Feb. 2014, at 1.

III. ENFORCEMENT WITHOUT LAW

The New York Convention is the foundational treaty concerning international commercial arbitration.³³ The purpose of the New York Convention is to ensure certainty in the recognition and enforcement of international arbitral awards.³⁴ *InterDigital* seems at first blush to further these purposes—the court declines to conduct a superfluous review of the arbitral award and defers to the determination of the courts at the arbitration situs. But *InterDigital* badly misinterprets the New York Convention, and the decision could increase concerns about the integrity and enforceability of international arbitration where the parties have not agreed on applicable governing law.

To the extent arbitrating parties have concerns about the integrity of the arbitral process, *InterDigital* magnifies those concerns by implying that disputants that forgo specific national law have limited their rights to judicial review of the arbitral decision. As per *InterDigital*, New York courts cannot review arbitral awards that are not made under New York substantive law, and as such the Southern District of New York could not review the FRAND award made under general principles of law.³⁵ This, however, represents a misunderstanding of the New York Convention. The New York Convention indeed allows for judicial review of arbitral decisions by the jurisdiction “under the law of which” the decision was made, but this refers to the procedural law of the arbitration situs rather than the substantive law governing the dispute.³⁶ In other words, the choice of substantive law does not affect the parties’ rights to judicial review under the New York Convention, and the court’s power to review the award would have been limited even if the parties had specified that the arbitration would be governed by New York substantive law. Nevertheless,

33. See REDFERN ET AL., *supra* note 3, at 69 (characterizing the New York Convention as “the most important international treaty relating to international commercial arbitration” and a “major factor in the development of arbitration” as a means of international dispute resolution).

34. See generally New York Convention, *supra* note 2.

35. See *InterDigital Commc’ns, Inc. v. Huawei Inv. & Holding Co.*, 166 F. Supp. 3d 463, 470 (S.D.N.Y. 2016).

36. See, e.g., *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 364 F.3d 274, 289–90 (5th Cir. 2004); *M & C Corp. v. Erwin Behr GmbH & Co.*, 87 F.3d 844, 848 (6th Cir. 1996); see also *Steel Corp. of the Phil. v. Int’l Steel Servs., Inc.*, 354 F. App’x 689, 693 (3d Cir. 2009). The arbitration agreement at issue in *InterDigital* was governed by New York law. *InterDigital*, 166 F. Supp. 3d at 468. Unless arbitration agreements expressly specify otherwise, however, courts will ordinarily interpret such provisions as referring to the substantive law governing the contract rather than the procedural law governing the international arbitration. See *Karaha Bodas*, 364 F.3d at 290. The rules governing the interpretation of agreements for domestic arbitration may be somewhat muddier. Compare *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 64 (1995) (holding that an agreement specifying New York law refers to “substantive principles that New York courts would apply, but not to include special rules limiting the authority of arbitrators”), with *Volt Info. Scis., Inc. v. Bd. of Trs. of the Leland Stanford Junior Univ.*, 489 U.S. 468, 470, 479 (1989) (finding that a contract containing a choice of law provision incorporated the California rules of arbitration).

InterDigital incorrectly states that the parties' decision to not specify governing law—a decision without which they may have found insufficient common ground to agree to arbitration—results in a waiver of their right to judicial review of the arbitral award.

Second, for parties concerned about the possibility of enforcing arbitral determinations, *InterDigital*'s misinterpretation suggests that awards under substantive general principles of law may be treated differently under the New York Convention, as opposed to awards made under national law. This suggestion resurrects old debates over whether courts will enforce arbitral decisions not made under specific national law. Early English courts and commentators voiced a traditional hostility toward arbitration agreements not governed by the law of a specific jurisdiction, such as agreements to arbitrate under general principles of law or equity.³⁷ Later judicial decisions evolved toward the enforcement of such arbitral decisions.³⁸ In *Ministry of Defense of the Islamic Republic of Iran v. Gould Inc.*,³⁹ for example, the defendant, Gould, resisted the enforcement of an award made by the Iran-United States Claims Tribunal.⁴⁰ Gould pointed to the same language cited by *InterDigital*, arguing that article V(1)(e) of the New York Convention refers to the enforcement of arbitral decisions made “under the law” of a country and thus did not include the enforcement of decisions not made under national law.⁴¹ The Ninth Circuit rejected this argument, holding that courts had jurisdiction to enforce arbitral awards regardless of whether they were made under the law of a state.⁴² Gould's discredited arguments, however, live on in *InterDigital*, which also reads out nonnational substantive law from article V(1)(e) of the New York Convention.⁴³

CONCLUSION

Most contracting parties prefer to have their agreement governed by a specific national law, and it is rare for parties to stipulate that nonnational legal principles will govern their relationship.⁴⁴ International FRAND disputes, however, may present a situation that calls for the application of such “general principles of law.” Scholars have disparaged nonnational law as frequently vague and as not providing sufficient clarity or certainty for

37. See Rivkin, *supra* note 12, at 73.

38. See *id.* at 74.

39. 887 F.2d 1357 (9th Cir. 1989).

40. See *id.* at 1358.

41. See *id.* at 1364.

42. See *id.* at 1365.

43. In a similar vein, some commentators have asserted that the phrase “under the law of which,” in referring to the procedural law of the arbitration, means the New York Convention should only apply to awards made under the procedural safeguards of another contracting party, and should not apply to arbitrations not subject to any national procedural law. See Rivkin, *supra* note 12, at 80–81.

44. See Drahozal, *supra* note 31, at 549 (“The available empirical evidence indicates that parties only rarely contract for application of transnational commercial law.”).

international legal disputes.⁴⁵ At the same time, however, national courts have issued few FRAND decisions, making it unapparent whether national law provides a clear basis for determining “fair and reasonable” royalty rates. Moreover, determinations of FRAND can be technocratic exercises of comparing similar licensing transactions,⁴⁶ and the substantive foundations of national law may not be necessary to support such economic assessments. As such, given the difficulty of agreeing on a body of national law to govern FRAND disputes, some parties may find it appropriate to escape the system of national laws altogether.

Given their heterogeneous membership and diverse interests, standards organizations have found it difficult to agree on detailed standards and procedures for determining FRAND licensing terms.⁴⁷ It is unlikely that disputing parties, having failed to find common ground during the collaborative standards process, will suddenly discover consensus during a contentious arbitral proceeding.⁴⁸ As such, parties to an international FRAND arbitration may often find it productive to avoid the question of governing law by making reference to neutral nonnational standards. In misinterpreting the New York Convention, however, *InterDigital* may make it less likely that parties will agree to use such neutral general principles for an arbitral proceeding. Specifying governing law may not always provide clarity and efficiency for dispute resolution, but *InterDigital* may raise the costs of failing to find agreement on such matters.

45. See, e.g., *id.* at 546.

46. See *supra* note 32 and accompanying text.

47. See Geradin, *supra* note 26, at 932–33; see also Joshua D. Wright, *SSOs, FRAND, and Antitrust: Lessons from the Economics of Incomplete Contracts*, 21 GEO. MASON L. REV. 791, 806 (2014) (stating that standards organizations “typically specify very little as to the meaning of ‘fair’ or ‘reasonable,’ at least in part because there is significant heterogeneity among the firms, technologies, and products”).

48. Eli Greenbaum, *Forgetting FRAND: The WIPO Model Submission Agreement*, LES NOUVELLES, July 2015, at 81, 86.