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Exploring California's reputation: From wild West to arbitration destination

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California is well positioned as an arbitration venue, particularly for U.S. to Asia disputes, due to its geography, leading universities, experienced arbitrators, and capable judiciary.

1. California's reputation and how to improve it. You have mentioned that California was, and in some quarters still is, viewed by the Europeans as the wild, wild West with out-of-control juries and courts, and insufficient appreciation for international arbitration. Later on, you add that nothing is forever, and geopolitical and global economic trends have a way of upending one's assumptions. In the past year, have you seen the erosion of some of those negative assumptions? How could California improve its reputation?

Answer: This is a complicated question, involving some real and some mostly imaginary issues.

The most important "real" issue, not unique to California, is the U.S. court system which features two uniquely risky characteristics as compared with foreign jurisdictions: juries and punitive damages. The U.S. court system typically resolves business-to-business contract and tort disputes with juries as the fact finders and judges instructing on the law. Juries are unheard of outside the U.S. in business disputes.

Our second unique characteristic is punitive damages, which are an available remedy for business torts, for example, fraud, breach of fiduciary duty, or interference with contract. Any plaintiff's lawyer worth their salt will plead a business tort where feasible for the purpose of injecting punitive damages. Again, this is unheard of outside the U.S.

Within the United States, California is perceived to be marginally more favorable to the plaintiff's bar than in some other jurisdictions that market themselves as more business-friendly, such as Delaware or New York. The biggest threat is the presence of an excellent plaintiff's bar in California.

The availability of juries and punitive damages are two "real" issues. The only way for a foreign company contracting with a California company to avoid these issues is to negotiate for arbitration.

How does California compare with other states within the U.S. as a favorable arbitration venue? California is well positioned to capture international arbitrations, particularly U.S. to Asia disputes, due to geography, its leading universities who have increasingly focused on international arbitration, its growing pool of experienced arbitrators, and its capable judiciary which defers to arbitration.

How can California shake the reputation of being the "wild, wild, West?" First, the audience must distinguish between juries and punitive damages, which are American devices on the one hand, and California as being a more plaintiff-oriented venue on the other hand. The first perception is not a California issue, and the second can be avoided by arbitration. There is no magic pill and reputation is built up or torn down over a matter of years. The arbitration bar must be introduced to California as a welcome venue.

The California Lawyers Association and California Arbitration, Inc. just hosted the third annual California Internation Arbitration Week, bringing together arbitrators and advocates for a week of programs. In addition, Global Arbitration Review (GAR) simultaneously held its first GAR Live! day focused on technology, in San Francisco. These two events were well-programmed and well-attended and are adding to California's reputation for international arbitration.

2. Technology sector's growing acceptance. You mentioned that many officers, particularly in the technology sector, were skeptical of arbitration - in part due to previous bad results by their peers, or lack of familiarity with the process. Could you expand on what the arbitration environment was like during those days of bad results, and how the environment differs today?

Answer: In the decade roughly between 2000 through 2010, I would hear technology corporate counsel discuss how dangerous arbitration is and how they prohibit arbitration clauses in their

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contracts. When I asked why, the response came back to the bad experiences of other large technology companies where arbitrators had ruled adversely to the technology company and there was no right of appeal.

I distinctly recall being invited to provide an introduction to arbitration, to the commercial law department of a large technology company, sometime during that decade. I had just sat down before an audience of twenty lawyers and paralegals. Before I could begin, a deputy general counsel who obviously had seniority came in, sat down, and said, "Cedric, you will have to convince me of arbitration, because right now I don't believe in it. We just came through an arbitration, where we lost, and now we have no right of appeal for the arbitrator's errors."

I took this as an opportunity to explain the upsides and downsides of arbitration. I started by saying that since I was not his litigator, I could not speak to their selection of arbitrator, which is probably the most important decision to be made. Nor could I comment on the many judgment calls in the arbitration. I then said that I fully appreciated that technology disputes can be resolved before our local court - the Northern District of California - where the judges are adept at complex technology issues and where the losing party retains the right of automatic appeal. I added that as to domestic arbitration between two U.S. technology companies, I was agnostic as between court litigation and arbitration. However, when the company went overseas for a supply contract or a joint research and development contract, or a joint venture to construct a new facility, it was an entirely different issue. In that case, did he want his client's dispute resolved in the courts of China or India or in any other country in Asia? Even if his counter-party was in a Western European country, did he have confidence that the company would not be on the losing end of the counter-party's home court advantage? And it was unlikely that his counter-party would accept resolution in a U.S. court. Thus, arbitration for a cross-border dispute provided no home court advantage for either side. Moreover, since there is an international treaty for the enforcement of international arbitration awards (the New York Convention), but no analogous multilateral treaty for enforcement of court judgments, he might have no recourse if he prevailed in a U.S. court but the foreign counter-party had no

assets in the U.S. Some countries such as China simply do not recognize U.S. court judgments.

Today, sophisticated corporate counsel, educated on the pro's and con's of arbitration, discuss potential arrangements where two technology companies, at the time of negotiating their contract, might come to an agreement on the use of arbitration. During the recent 2024 California International Arbitration Week, I listened to an experienced corporate counsel discuss how she and her colleagues explore arbitration within limits, i.e., the parties put parameters around the arbitration result by capping the upside and downside of their potential dispute. For example, the parties might negotiate an arbitration clause that provides that the issues of patent ownership and infringement are beyond the authority of the arbitrator. And as to damages, they limit in advance damages in a patent licensing dispute to a band between a floor of $X and a ceiling of $Y. In this fashion, the parties get the advantages of arbitration, such as speed, lower cost and confidentiality while minimizing the downside risk of lack of appellate review.

3. Centers of arbitration activity. You mentioned that San Francisco, LA, and Silicon Valley are actively seeking to become centers of arbitration activity. How is that going? What are your predictions for the next five years?

Answer: The process of becoming a global center of arbitration activity has several necessary components and should be measured in half-decades, not in single years. What are the necessary components?

First, legislative roadblocks to international arbitration should be removed. In 2013, I co-authored with a lawyer from a competing firm, Steve Smith, a Daily Journal article titled "Achieving California's Potential as an International Arbitration Center," calling for legislation to clarify that for international arbitration matters, foreign lawyers and arbitrators need not be a member of the California bar. Several years later, this effort resulted in the Chief Justice of the California Supreme Court appointing a blue-ribbon committee that after study recommended that foreign-qualified lawyers be allowed to appear in international arbitrations in California without being barred here. After legislative action, California's practice rules were brought into line with the rules of New York and other states, removing one of our competitive disadvantages in international arbitration.

Second, one needs a judiciary supportive of the arbitral process that evaluates arbitral awards under international norms and that does not overturn awards where not warranted. Although California is perceived as liberal and plaintiff-oriented, its judiciary does not vacate (overturn) arbitral awards at a disproportionately higher rate than the judiciaries from other U.S. states.

Third, one needs a pool of capable arbitrators and lawyers available to sit as decision-makers or to advocate as counsel in complex arbitrations. California has long had a very capable, albeit small, arbitration bar. Today, more law firms are setting up arbitration groups based in California and more young lawyers are coming into the workforce. It is a virtuous circle - more arbitrations beget more practitioners which begets more arbitrations.

Fourth, having a large and receptive client base based in your venue is very helpful. This is a key competitive advantage that California has over most other venues. If California were a country, its GDP would rank it as the 4th largest country, behind the U.S., China, and Japan. California is undeniably the global technology center, in addition to its primacy in entertainment and agriculture. Of the seven most valuable technology companies (called the "magnificent Seven" in the investment world), four are headquartered here - Apple, Google, Facebook (Meta), and Nvidia. A fifth, Tesla, was founded and had its great success here but recently relocated to Texas. The venture capital, private equity, and the entire start-up ecosystem are also centered here. As a consequence, many foreign and out-of-state law firms have set up Northern California branches to take advantage of client opportunities.

The fifth requirement is geographical desirability including easy flight connections to the commercial centers in both the U.S. and the world, as well as having comfortable hotel and restaurant facilities to accommodate the legal teams and the arbitrators. California shines for U.S. to Asia disputes, as it takes five-hours less time to travel from Asia compared to the East Coast.

Next, what is the timeline? Long-standing patterns don't dissipate quickly. But over a half-decade timeline, I anticipate that we will see substantially more arbitrations specifying a California arbitral seat. If only 20%-30% of California companies insert a California arbitration clause into their cross-border contracts, instead of relying on the courts or inserting an arbitration clause specifying another venue, that by itself would represent a major paradigm shift and the number of arbitrations based here would increase substantially.

4. Artificial Intelligence: In a May 2021 interview with the Daily Journal you noted that videoconference technology has improved, creating greater efficiency through virtual hearings. Not quite three years later, AI has dramatically impacted all areas of law. What

do you consider to be the positives, and negatives, of AI in the realm of international arbitration?

Answer: The legal profession actually has had a rudimentary form of artificial intelligence (AI) for a number of years, namely, in document collection and word-based legal research. If you are searching a client's voluminous electronically stored information (ESI) for responsive documents in answer to document requests, or at a later stage are searching through your collected document database for relevant documents to use in trial preparation, you already use document search techniques that employ AI. This has spawned litigation support companies that can assist with document organization and searches. The better your predictive code words, the better your output. Similarly, if you are looking for cases that relate to the topics in your litigation, you can launch a Lexis case search that is focused on your identified words.

The next step for AI in legal work is the application of reasoning to assist in pulling up documents and cases for lawyer review.

The final step is drafting legal memoranda that make reasoned arguments. Frankly, I am skeptical about how far AI can reliably go. For example, you could ask the AI program to locate all cases in a given jurisdiction that discuss topic X. And you can then ask AI to identify the cases that not only discuss topic X, but also rule for your client's position. But does AI understand why the rulings went in a given direction? Can AI understand the nuances and fine distinctions that underlie different rulings? If you ask AI to draft a legal argument based on the cases it has pulled together, how much can you rely on that?

It remains to be seen how far generative AI can go. Legal reasoning and the application of judgment are reserved for the professional.

5. Presidential election. What impact, if any, may the next presidential election have on international arbitration?

Answer: 2024 will be wild and unprecedented in U.S. politics, a period unlike any that we have seen in our lifetimes. Although there are many clear differences between Joe Biden and Donald Trump, neither has spoken about international arbitration procedures. However, Trump in his first term raised tariffs on certain products, such as steel, which impacted trade flows and ultimately raised costs to the U.S. consumer. Recently, Trump has threatened to impose a 100 percent tariff on Chinese electric vehicles, presumably to protect U.S. vehicle makers from foreign competition.

Currently, the most that can be said is that President Biden will continue on today's geopolitical and economic path and candidate Trump will usher in four years of unpredictability based on a transaction-based "what can you do for me" philosophy, on the positions he takes in pending litigation that undermine confidence in the judicial system, and on a U.S. retreat from the world stage. I do not foresee either a Biden or a Trump administration launching attacks on the international arbitration system because our country's corporations depend on a predictable business environment, which means upholding the sanctity of cross-border contracts. To the extent that Trump's policies lead to abridgment of contracts, that will mean an increase in contractual disputes and thus an increase in arbitration caseloads.

6. Main difference between arbitration and litigation. Do observers miss any differences between court litigation and arbitration?

Answer: I am always surprised that in the discussions over the relative cost differences between court litigation and arbitration, observers traditionally overlook one factor. Only 1%-2% of US court civil disputes go to trial, whereas about 25% to 40% of arbitration cases go to trial. Why? Because in court litigation, there is enormous money spent on discovery (depositions, written interrogatories, document requests), after which the court litigants know more about their cases, are exhausted, and then settle. By contrast, in a complex cross-border arbitration, there is much less money spent on discovery and thus there are cost savings. However, since the parties know considerably less about their case and go to trial (called "merits hearing" in arbitration circles) much more frequently, the costs associated with the higher fees of trial should be ascribed to arbitration.

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