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DISPUTE RESOLUTION

Banking and finance arbitration on the rise – a trend to follow?

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Further to a consultation held last year on the use of arbitration, the International Swaps and Derivatives Association (ISDA) is currently preparing five draft model clauses providing for arbitration under the rules of the following institutions: International Chamber of Commerce (ICC), the London Court of International Arbitration (LCIA), the Singapore International Arbitration Centre (SIAC), the Hong Kong International Arbitration Centre (HKIAC), and the American Arbitration Association / International Centre for Dispute Resolution (AAA/ICDR). On 28 January 2013, two draft model arbitration clauses were unveiled by P.R.I.M.E. Finance, an arbitration institution established early last year and dedicated to the resolution of financial disputes. The model clauses provide alternatives for insertion in the ISDA Master Agreements which otherwise provide for disputes to be referred to either the New York or English courts. In the same vein, the Loan Market Association (LMA) has incorporated an option for parties to agree to LCIA arbitration in some of its recently issued standard facility agreements. Inclusion of arbitration clauses in standard form and industry standard financial documentation is the natural result of a trend in the industry which has witnessed a rise in arbitration referrals in the last few years; the LCIA has reported that 17.5 percent of cases arose out of financial agreements, for 2011, as against 11.5 percent in 2010.

The continuing globalisation of the finance market entails that parties from emerging jurisdictions are increasingly involved in cross-border transactions. These parties may refuse to submit future disputes to the courts of London or New York, where a vast majority of financial disputes were historically resolved. A neutral forum, arbitration may be the result of a compromise between parties who do not accept the risks of litigating in the courts of their counterpart's jurisdiction. In addition, financial institutions and other stakeholders have become more alert to the complications associated with the enforcement of court judgments beyond Europe. The rise of arbitration would therefore appear to be largely related to the prospects of obtaining a decision that will be recognised in the places, or places, where the assets are located. However, it should be noted that arbitration is not a panacea for all cross-border enforcement problems, even among New York Convention countries. Notwithstanding their obligations under it, it is not unusual for local courts – in certain jurisdictions in particular – to refuse to uphold an arbitral award on a 'wrong' interpretation of the Convention. Similarly, parties should be aware of the risks associated with the enforcement and interpretation of arbitration agreements, which might be the object of extensive litigation or jurisdiction battles before ▸▸

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the arbitral tribunal. Careful drafting may assist with limiting the risks of preliminary or ancillary disputes over the scope and status of the parties' purported agreement to arbitrate.

The growing complexity of financial transactions and financial products may equally have an impact on the use of arbitration. Although judges' technical knowledge of banking and finance varies from one jurisdiction to another, there is at least a perception that arbitration meets the industry-expressed view that these disputes need to be resolved by experts in the field. Further, more complex transactions tend to generate multi-party or multi-contract disputes, in relation to which arbitration used to fail to provide a satisfactory solution. Many arbitration institutions have attempted to tackle this shortcoming by embarking upon the revision of their rules to address *inter alia* joinder of third parties and consolidation of arbitral proceedings. These new rules do not, however, remove the need for an agreement to arbitrate; and in certain circumstances, the inability to join third parties without their consent may indeed frustrate the global resolution of multi-party disputes. Viewed from another angle, limitations inherent with the consensual nature of arbitration might prove advantageous. For instance, parties have made a tactical use of the fact that third-party disclosure is usually not available in arbitration. Similarly, financial institutions may want to consider agreeing to arbitration in order to avoid class actions, which are generally considered incompatible with arbitration.

Aside from developments in the financial services sector, the rising popularity of arbitration seems to be attributable to the industry's better understanding of the arbitral process and its potential benefits. These include the sometimes overstated portability of awards, confidentiality, finality and flexibility, all of which need to be put into perspective and considered only in light of the available alternatives, the jurisdictions involved and the type of disputes likely to arise, including amount at stake, need for interim relief, types of remedies, etc.

Although not always desirable, the option to 'wash its dirty linen' privately remains one of the main reasons for choosing arbitration over open court litigation. Confidentiality in international arbitration is not a given and depends on the rules and arbitration regimes under which the proceedings are conducted. Further, confidentiality usually goes hand in hand with the absence of precedent, which may have historically explained the industry's reluctance to use arbitration. Having perceived a need for enhanced consistency and certainty, arbitration services providers have started to publish anonymised awards and decisions with a view to facilitate the formation of a financial market jurisprudence. In some instances, non-binding examples might, however, be insufficient. For example, lending institutions who have a propensity to repeatedly litigate over the same terms have traditionally favoured litigation for its binding precedent system, and the example set by published decisions. Further, many industry standard agreements have been drafted under common law systems; the impact of precedent is arguably inherent in those documents and necessary to their understanding. On the other hand, it would appear that the industry now recognises the risks associated with a system of binding precedent. Akin to insurance disputes, financial disputes often involve interpretation questions, in relation to which an 'incorrect' decision may have unfavourable systemic market consequences. In this regard, the flexibility of arbitration may assist. Parties may provide that the tribunal shall render an unreasoned award. Such an unreasoned award would entail the benefit (or risk) of being particularly difficult to challenge. This possibility, coupled with the lack or limited right of appeal on the merits, may be factored in when comparing international arbitration and litigation in a specific jurisdiction, in terms of finality and average length.

Arbitration provides flexibility, although the possibility of tailoring the process to the parties' needs appears considerably underused. For example, the common complaint in relation to documentary overload in both common law style litigation and international arbitration may be addressed by agreeing limited discovery in the arbitration clause or subsequently. Similarly, financial institutions have repeatedly complained about the ▸▸

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alleged lack of procedure in arbitration for disposing of an unmeritorious defence summarily, although such a procedure could be agreed in the arbitration clause (subject to due process compliance checks). Yet, as things stand, along with the prospect of a generally quicker and cheaper process, the availability of summary judgment in certain judicial systems appears to remain an important motive to favour litigation over arbitration. Another advantage of court proceedings is that judges have judicial powers and generally have jurisdiction to deal with all issues relevant to the dispute, including insolvency, competition matters, statutory claims, fraud allegations and corporate disputes, which are still not considered arbitrable in some jurisdictions (including emerging jurisdictions where enforcement may be sought and therefore jeopardised due to arbitrability issues).

In order to keep their powder dry, it has been common practice for parties with sufficient bargaining power to unilaterally retain the option to choose between arbitration and litigation in the dispute resolution clause. Yet, unilateral jurisdiction or arbitration clauses have recently been found unenforceable under Russian and French law. Despite the uncertainty surrounding their potential unenforceability, such clauses have been, in some jurisdictions, particularly popular among banks. It is anticipated that these new decisions of the Russian Supreme Arbitrazh Court and the French Cour de Cassation will prompt banks that want to avoid, at all costs, the risks of being sued in unfavourable jurisdictions to review these clauses and agree to arbitration exclusively. ■

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