Drafting an Arbitration Agreement

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A clear and effective arbitration agreement is essential to the success of any arbitral proceedings; it is the source of the tribunal's authority and a pre-requisite to the enforcement of an award under the New York Convention.

A well-drafted arbitration clause is no guarantee of a successful arbitration, but a badly-drafted clause may be the cause of years of proceedings, wasted costs and an award that is unenforceable. What then constitutes an effective arbitration agreement?

Arbitration clauses can be as short as "Arbitration to be settled in London" or run to several pages seeking to cover every possible eventuality. Both extremes should be avoided. The former leaves too many issues uncertain, not least of which is the validity of the clause itself, while the latter runs the risks of being unworkable in practice and of unduly restricting the tribunal's power to adopt suitable procedures.

Rather than attempt the impossible by trying to anticipate the type of disputes that may arise, the drafter of the arbitration agreement should concentrate on using wording that gives the tribunal the flexibility to conduct the proceedings effectively and efficiently. And, bearing in mind that the validity of the clause may have to be tested by arbitrators or in national courts, whose first language is not English, the wording must above all be clear.

This article reviews the provisions that an effective arbitration agreement ought to cover with reference the relevant provisions of the Arbitration Act 1996 (the 1996 Act) and the Arbitration Rules of UNCITRAL, of the London Court of International Arbitration and of the International Chamber of Commerce. It also considers some special situations that require particular attention.

The article is written from the perspective of an English lawyer, but many of the comments apply regardless of the nationalities of the parties, the law of the contract or the place of arbitration; subject only to the caveat that the provisions of any agreement must be checked for effectiveness under the applicable law.

The Arbitration Agreement
Below is a checklist of provisions to be included in an international commercial agreement followed by a brief commentary with reference to the relevant rules of some of the main international arbitral institutions:

1. All and any disputes or differences arising out of or in connection with this Agreement, or the breach, termination or invalidity thereof shall be finally settled by arbitration.
2. In accordance with the [UNCITRAL] Arbitration Rules.
3. The number of arbitrators shall be [one/three].
4. The appointing authority for the purpose of the UNCITRAL Rules shall be [the London Court of International Arbitration].
5. The seat of the arbitration shall be [London].
6. The language of the arbitral proceedings shall be [English].
7. All and any awards of the Arbitrators shall be final and binding.
8. The parties expressly exclude all and any rights of appeal from all and any awards.
9. The final award shall be made within six months from the appointment of the third arbitrator, but insofar as it is impractical to do so, it shall be made as soon as possible thereafter.

1.The Scope of the Clause

This section of the clause is critical; it sets the boundaries for which disputes the tribunal is authorised to determine. Clarity is essential since an award made on issues that fall outside the scope of the clause will be unenforceable. It is usually desirable to cast the net widely to ensure that the clause encompasses the broadest possible range of disputes.

It is possible to draft the clause so that certain categories of dispute are hived-off for resolution by, for example, expert determination. This can be useful where the contract contains terms of a highly technical nature. Such arrangements can be effective, although when a dispute first arises, they may lead to a time consuming wrangle over the appropriate method of resolution for that particular dispute. One solution is to make express provision for how any such preliminary issue itself should be resolved.

2.Choice of Rules

Under English law, there is no need to subject the arbitration to any particular rules; the Arbitration Act 1996 sets out "default rules", which regulate the powers of the tribunal and other procedural matters in the absence of the agreement by the parties. Generally, however, it is preferable expressly to incorporate an established set of rules. This is particularly true if the chosen venue is in a jurisdiction which has no established law of arbitration.

By Section 4(3) of the 1996 Act, the provisions of any rules that the parties have agreed to apply may be effective to exclude the operation of the default provisions in the 1996 Act.

There are a number of arbitral institutions that offer an arbitration service and a set of rules. These include the London Court of International Arbitration (LCIA) and the Court of Arbitration of the International Chamber of Commerce (ICC). Both have a secretariat which has an administrative role in the conduct of the proceedings, including the appointment of the tribunal and, in the case of the ICC, scrutiny of the award.

The leading non-institutional rules are the UNCITRAL Arbitration Rules. UNCITRAL itself plays no part in the proceedings, the conduct of which is left to the tribunal.

There is no simple answer to which rules should be used, although with non-institutional rules, the parties do not have to meet the expenses of a secretariat and, arguably, the arbitrators have a greater flexibility to conduct the proceedings in the most efficient manner.

The UNCITRAL Rules have been in use since 1976 and are tried and tested. The ICC and the LCIA Rules have a longer history and have introduced extensive revisions that apply to all arbitrations that start after 1st January 1998.

3.The Number of Arbitrators

The larger the sum in dispute, the more likely it is that a tribunal of three will be appropriate. For obvious reasons, there should always be an uneven number.

The advantages of a sole arbitrator are speed of appointment and of decision-making, greater flexibility in fixing hearing dates and lower fees. On the other hand, the parties are likely to have a greater say in appointing a tribunal of three and this may be valuable where the parties come from differing legal and cultural backgrounds. In principle, at least, the fact that three different arbitrators will contribute to making the award reduces the risk of mistakes and misunderstandings, even if it does not guarantee a higher quality of decision making.

4.Appointing Authority

The role of the appointing authority is to appoint and/or replace members of the tribunal where one party defaults in appointment or in the event of death, incapacity, removal, etc of an arbitrator.

No separate appointing authority is needed under the LCIA or ICC Rules. Under the UNCITRAL Rules,

the Secretary-General of the Permanent Court of Arbitration at The Hague is empowered to designate an appointing authority if the parties have failed to agree, but this procedure takes time and could result in an unexpected institution being nominated. Where an appointing authority is named in the arbitration agreement, it is prudent to check that the organisation is willing and able to undertake the role and ensure that its correct title is used.

5.Choice of Venue
This is possibly the most important provision of all. It dictates not only where the proceedings will be held geographically, but also the law of the proceedings. Although the seat of the arbitration is usually where the proceedings are held, most institutional rules enable the tribunal to hold hearings at any other location without prejudice to the selection of the legal seat. However, since the award itself will usually be published in the state which the parties have chosen as the seat (wherever the arbitration may be heard) it is important to select a venue in a country that has ratified the New York Convention to facilitate the enforcement of any award. For this reason, at least, care must be taken by parties if invited by the arbitrators to change their chosen seat after the arbitration has commenced.

The unsatisfactory decision in Hiscox v Outhwaite, in which it was held that an award was made in the country where it was signed, was overturned by Section 53 of the 1996 Act. This clarifies that where the seat of the proceedings is in England and Wales the award shall be treated as made there regardless of where it was signed. A similar provision may be found in the ICC Rules (Article 25(3)).

The UNCITRAL Rules (Article 32(4)) and those of the LCIA (Article 26.1) require the award to state the place in which it was made.

The seat of the arbitration is also relevant to the enforceability of an award under the New York Convention, under which enforcement may be refused if:

- the arbitration agreement is not valid under the law of the country where the award was made, or;
- the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the law of the country where the arbitration took place, or;
- the award has been set aside and suspended under the law of the country in which it was made.

6. The language of the proceedings

Most rules enable the tribunal to determine the language of the proceedings, but, in the interests of certainty, it is advisable to make an express choice taking into account the language(s) of the parties, their advisers, the contract, the contractual correspondence and other documents and the venue of the proceedings.

7.Finality
Is it wise to include a provision stipulating that the award shall be final. This does not preclude the possibility of an appeal, but it does clarify that the parties intend that the award should be satisfied, or enforceable through the courts, forthwith.

8.Exclusion of the right of appeal
The arbitration laws of most jurisdictions now exclude the possibility of appeal, but there are some, notably England, where it still exists. Some parties may like the comfort of having a possible recourse to the courts, but excluding the right of appeal has the distinct advantage of putting a cap on the length of time, and therefore the costs, of bringing a dispute to final conclusion.

The UNCITRAL Rules do not exclude the right of the appeal. Whether such a right exists depends on the law of the seat of the arbitration and if the parties wish to exclude the right they must say so

expressly in their clause. Article 26.9 of the LCIA Rules and Article 28(6) of the ICC Rules do exclude any form of appeal or recourse to the courts.

9.Time limit for making the award

A useful provision in an arbitration clause is one which requires the arbitrators to produce their award within, say, six months of being appointed. However, if such a provision is included, care must be taken to ensure that the time can be extended since, if the proceedings run into unavoidable delay, the tribunal may find itself functus officio if it does not deliver its award within the specified time limit.

Section 50 of the 1996 Act requires an application for an extension of any agreed time limit to be made to the court unless otherwise agreed. Article 24 of the ICC Rules requires an award to be made within 6 months of the Terms of Reference, but gives the ICC Court power to extend. The LCIA and the UNCITRAL Rules do not require the award to be made within any specific time.

Other provisions

Multi-tier dispute resolution

Some parties like to include a provision in the arbitration agreement requiring the parties to attempt to resolve a dispute by amicable negotiations before any proceedings are commenced; they may also build in a requirement to refer disputes initially to ADR. Such provisions are perfectly acceptable, although they can be a nuisance when the claimant wishes to start proceedings promptly.

Qualifications of the arbitrators

In contracts relating to particular industries, or of a technical nature, consideration may be given to stipulating that the arbitrators should have specified academic, professional or commercial experience and/or qualifications. It is, however, important not to introduce too many requirements since this will limit the choice of whom can be appointed.

Governing law

It is important to be clear what the governing law of the arbitration agreement is since this will determine its validity and effect. The main contract should have a governing law clause in any event and this will usually apply also to the arbitration agreement. But where the proceedings are to be conducted in a country other than the country whose laws govern the contract as a whole, it is advisable to specify expressly that the governing law of the contract applies equally to the arbitration agreement (or to make some other express provision). If this is not done, it may be argued, under some national laws, e.g. France, that the proper law of the arbitration agreement is not that of the main contract, but that of the chosen venue.

Special Situations

Multi-party contracts

The first question that the drafter of an arbitration agreement should ask is how many parties there are to the contract. If the answer is more than two, he will need to consider very carefully how the tribunal is to be appointed, bearing in mind the fundamental requirement that each party to the proceedings be treated equally. It is not acceptable, for example, for one party to be allowed to nominate its own arbitrator, with the remaining parties being forced to accept a joint appointment by the appointing authority even if that is what they agreed in the arbitration clause.

The arbitration agreement may make provision for groups of parties to make joint appointments, but the Dutco decision says such an agreement is not binding. The safer solution is to provide for the appointing authority to nominate and appoint either the sole or all three arbitrators. This involves abandoning the principle of party-appointment, but ensures, at least, that all parties are treated equally. This is the solution adopted by the ICC in Article 10 of its new rules.

The LCIA Rules approach the problem less directly. Article 5.5 provides that the LCIA alone is empowered to appoint arbitrators and states that it shall have regard to, inter alia, the number of parties, if more than two.

The UNCITRAL Rules do not deal with the issue at all, which is left to the appointing authority to grapple with.

None of these solutions is entirely satisfactory and the inexperienced contract drafter would be well-advised to seek specialist advice.

Consolidation of Proceedings

An even more complex situation arises where there are a number contracts relating to a single project. In such a situation, a dispute may arise which bears on several of the different project contracts and on any number of parties. If each contract contains a separate arbitration agreement between the parties to it, separate proceedings will have to be commenced in respect of each contract. This is likely to be seriously unsatisfactory causing delays, unnecessary expense and may result in inconsistent decisions between different sets of parties in different arbitrations based on the same set of facts.

Under the 1950 Arbitraton Act, the court had a discretion, in relation to domestic arbitration agreements, to refuse to stay its proceedings precisely on these grounds. But, under the 1996 Act, which abolished the distinction between domestic and non-domestic arbitration agreements, the court no longer has such a discretion.

The apparently obvious solution to this problem would be to consolidate the various proceedings and bring all parties before one tribunal as with court proceedings. With arbitration proceedings, however, agreement of all parties is required if there is to be consolidation. This is now spelled out in section 35 of the 1996 Act, which specifically states that the tribunal has no power to consolidate in the absence of agreement.

In practice such agreement will almost never be reached after a dispute has arisen since any party whose role is peripheral is likely to want to avoid being dragged into a large multi-party dispute which may last for years and involve him in wasted time and expense.

Such agreement to consolidate can be set out in the arbitration agreement itself, but the practical difficulties are considerable. Points that need to be covered include:

- how to appoint the tribunal while maintaining equality of treatment of the parties;
- enforceability of an award against a party who did not take part in the proceedings;
- is an award - as to the interpretation of a clause in the contract - binding on a party who has not taken part in the proceedings?;
- is a waiver of confidentiality required?

While these issues can be catered for, the arbitration agreement is likely to become overly complex and lengthy and, when it comes to be put into practice, may prove to be unworkable.

The ICC and the LCIA fought shy of introducing any form of compulsory consolidation into their rules because of these very problems. The construction industry, which is perhaps most directly affected by this issue, has been bolder and has produced a draft set of Rules, the Construction Industry Model Arbitraction Rules (CIMAR). It will be interesting to see how these fare in practice.

For those responsible for drafting arbitration agreements involving a series of contracts, perhaps the best they can hope for is to create an environment which forces the parties to give consideration to the possibility of consolidation and creates a framework for it without actually seeking to make it compulsory.

The alternative, of course, is to recognise and in some instances it may be better not to agree to arbitration at all, but to accept that the courts may be the more effective forum.

Optional Clauses

In their loan agreements, banks have traditionally included jurisdiction clauses that give them the right to begin proceedings against the borrower in the widest range of jurisdictions while forcing the borrower, should he wish to sue, to bring proceedings only in the courts of one state, often that of the bank's domicile.

These provisions are generally effective and banks are able to pursuade borrowers to agree to them because of their dominant bargaining position. Recent years have seen a number of international banks extending this concept to give them (but not the borrower) the option to bring proceedings either in the courts or by way of arbitration. This enables the bank to take advantage of the New York Convention if it so wishes.

Conclusion

As L Yves Fortier C.C., Q.C. said in the opinion column in the first issue of the International Arbitration Law Review, arbitration is progressively becoming the forum of choice for dispute resolution in the international business community. With the growing complexity of international transactions, there is an increasing number of issues for the drafter of the arbitration agreement to address. For certain of these issues, solutions are likely to remain elusive, but the best way to achieve an effective arbitration agreement is to ensure clarity and avoid unnecessary complex provisions.

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