A SUMMARY AND COMMENTARY ON THE IBA GUIDELINES ON DRAFTING THE INTERNATIONAL COMMERCIAL ARBITRATION CLAUSE

Prepared by Richard A. Glaser, Esq.
Member, Dickinson Wright PLLC; Adjunct Professor of International Commercial Arbitration, Thomas M. Cooley Law School

The *Guidelines on Drafting the International Commercial Arbitration Clause*, developed by a distinguished committee selected by the International Bar Association (IBA), provides a convenient and thoughtful resource for the creation of an arbitration agreement between transnational parties that optimizes enforcement of the desired arbitral proceeding and its resulting award.

The first Eight Guidelines address the most essential elements of an enforceable arbitration agreement. They are followed by optional contractual considerations (*i.e.*, allocation of costs, time limits, discovery considerations). The IBA Guidelines also address more customized applications that arise when multiple parties or contracts complicate the bi-lateral transaction. The Guidelines further provide recommendations when parties are intent upon integrating preliminary dispute resolution procedures.

This summary examines the Eight Basic Drafting Guidelines, and offers the practitioner specific recommendations to each.

Before starting, it is critical to understand the core objective of international arbitration - making sure that the resulting award can be efficiently enforced. Second, as your client's counselor, you want to do all you can to align your client's expectations of arbitration compared to American litigation (more efficient and confidential, less discovery or opportunity for appeal) with reality. While international arbitration can provide benefits of expediency relative to civil litigation, it assuredly will not be as cost efficient or streamlined as desired. However, its greatest benefit cannot be taken for granted -- when structured and conducted correctly, the resulting arbitral award may be uniformly enforced or recognized on nearly a global basis.

That process starts with the drafting of a proper arbitration clause.

Guideline 1: The parties should select between *ad hoc* or *institutional* arbitration.

Ad hoc must be selected and designed by the parties in their agreement, which means it will not be administered by a recognized institutional body, but by the arbitration panel (or individual arbitrator), once it/he/she is appointed. International parties may view the *ad hoc* option to allow more flexibility with less interference and expense. However, the *ad hoc* procedure can lead to awkward situations that may threaten the process when questions about an arbitrator's fitness, potential conflicts or the adequacy of his/her previous disclosures arise. The recognized institutions (ICC or AAA (ICDR)) are experienced in dealing with these thorny issues and can provide a welcomed buffer between parties and the arbitrator. Of course, that does come at a price which can be substantial.

In *ad hoc* arbitration, the parties may incorporate by reference the procedural rules of an institutional body without involving the institution itself, but that still leaves the arbitrator to administer (or police) himself.

Most importantly, the parties must examine whether an *ad hoc* arbitration may not be recognized in the jurisdictions most likely petitioned to enforce the resulting award. While this may not be commonplace, the risk is too great not to be evaluated in the drafting stage.

Recommendation: *In the international arena, the parties are well-advised to opt for institutional, but take care to make sure that the courts of the nation where enforcement or recognition of the award most likely will be sought will respect the selected institution. The courts of some nations may regard with suspicion ad hoc procedures and even some institutions foreign to them (e.g., for purposes of securing recognition in China, selection of CIETAC is recommended). Also, when foreign nations are asked to assist with discovery needs within their borders, they may be more receptive when a recognized institution is administering the arbitration and approves the request for assistance.*

Guideline 2: Parties should select a set of Arbitration Rules and use the model clause recommended by the arbitration rules as a starting point. This Guideline includes sample elements of a model arbitration clause, with many additional provisions that must be considered if the parties choose *ad hoc* over institutional.

Recommendation: *The Guidelines caution that ad hoc arbitration requires additional layers of language to assure the inclusion of important elements that are automatically integrated when an institution and its rules are incorporated by reference into the agreement. At the negotiation stage, the parties are focused on a transaction that promises mutual benefits; they do not want the dispute resolution negotiation to subsume their most hopeful plans. Your job is to show them the importance of spending time and careful thought on dispute resolution provisions, so don't overwhelm them by reinventing the internal rules of arbitration in the agreement. The key is to select the institution (and, in turn, its rules) that will be accepted by those nations where enforcement and recognition are most likely to be pursued. Check in advance whether your "target" nation requires special language in the arbitration clause for recognition or enforcement.*

Guideline 3: Generally, parties should define arbitral jurisdiction broadly and not attempt to limit the scope of issues subject to arbitration. The parsing of issues is discouraged, and more inclusive language -- "any and all issues," "in connection with," or "relating to" -- may be less problematic than simply to say "all disputes arising out of this agreement."

Recommendation: *In general, this is sound advice. It can avoid after-the-fact controversy over what issues the parties intended to include or exclude from the arbitral decision. While the drafters recognize there may be need for exceptions, it cannot be over-emphasized that the parties should always consider carving out situations requiring immediate injunctive relief or temporary restraining orders, particularly in intellectual property, wrongful competition, and trade secret settings. Arbitration is not a suitable forum for the adjudication and enforcement of emergency orders, the need for which may arise even before the arbitrators have been selected.*

Guideline 4: The parties should select the place (seat) of arbitration.

In domestic arbitrations, this step is largely a matter of convenience, particularly where the Federal Arbitration Act has application in both state and federal courts. The selection of seat becomes more substantive if a particular local court, which may be petitioned for supervisory control, has exhibited hostility or blind deference to private arbitration in the past.

In international arbitration, selection of seat is critical because it presumptively determines the *lex arbitri*, the procedural law which the host nation's courts will apply to supervise the arbitral proceedings and to review the award(s). Under the New York Convention, which has gained nearly universal approval, *only* competent courts of the *lex arbitri* nation can set aside or suspend the arbitral award.

Recommendation: *Assume that where the arbitration is held will dictate the national law which governs the criteria for vacatur, or the setting aside of the award. The parties theoretically can select one site as a convenient or compromise location to conduct the arbitration, and contractually designate a separate national law to supply the lex arbitri. This can lead to confusion and frustrate the parties' intent. For good reason, it is discouraged.*

It may be helpful to stipulate that the designated seat of the arbitration shall also be treated as the "place where the arbitration award is made." This avoids confusion if, for example, the arbitrator(s) sign(s) the award in a different country.

Guideline 5: Parties should specify the number of arbitrators.

Typically, the choice is between one or three. Three (3) obviously multiplies cost, can complicate scheduling and encourage delay as awards are drafted and exchanged for comment. On the other hand, three may offer a more balanced range of perspectives and collective wisdom than a single arbitrator. An appealing argument can be made that the number of decision-makers should await fruition of the dispute, at which time the appropriate number can be selected. However, when the parties get into a full blown dispute, it may be doubtful whether any consensus can be reliably reached.

In many cases with two party-appointed arbitrators and a third neutrally selected arbitrator, the decisive vote is cast by the latter, so each party winds up bearing the extra expense of a three person panel when ultimately only a single arbitrator decides the case.

Even though the *IBA Guidelines* do not address it, the parties should stipulate how the award will be made among three arbitrators, or make sure the selected institutional rules address this point to the parties' satisfaction. Is it majority rule, or will the third or neutral arbitrator always be the tie-breaker or decisive vote? In multi-issue cases, majority rule can lead to as many possible outcomes as there are combination of issues. Having a single arbitrator avoids this potential confusion.

Recommendation: *If technical, cultural, or financial complexities demand more abilities than a single arbitrator can provide, then those criteria should be considered early in the contract drafting stage, and legitimately may justify more than one arbitrator. If, however, the argument for three is based on the perception that the case is complicated, then consider whether the extra bodies will provide value commensurate with their added expense. In most cases, one arbitrator should suffice and will minimize delays.*

Guideline 6: The parties shall specify the method of selection and replacement of arbitrators and, in an *ad hoc* arbitration, should select an appointing authority.

The most salient point here, as noted earlier, is to opt for institutional over *ad hoc* arbitration. The parties are free to establish their own procedure, but in the event of a communication breakdown, the institution's rules will provide an automatic backstop. Institutional rules typically provide for corrective procedures in the event a party or party-appointed arbitrator ceases to cooperate in the process or the latter can no longer serve for any reason. Reputable arbitral institutions typically are prepared to deal with these disruptive situations. Some institutional rules even provide for continuation of a truncated proceeding so that an award may still be rendered even when the disruption occurs so late in the process that a replacement arbitrator would not be practical.

Recommendation: Opt for institutional as opposed to *ad hoc*, explore implementing the selection process with which the parties are most comfortable, but reserve the institutional body of rules as the fall back position in case the "best laid plans" go awry.

Guideline 7: The parties should specify the language of arbitration.

Obviously, the arbitrators need to understand the witnesses, the exhibits and one another. If not established in the contract, then the arbitrators will select the language of the proceedings, which may seem a sensible approach after the issues, fluency of the witnesses, and language of key exhibits are known. However, in international contracts, each party may want assurances that at least one arbitrator understands its language and business culture, which would have to be pre-ordained by the Agreement.

Recommendation: *Select in the Agreement the language that will control the arbitration and determine with the client whether any special needs require accommodation. Consideration should also be given to investing the arbitrators with discretion to appoint translators as circumstances may warrant.*

Guideline 8: The parties should ordinarily specify the rules of law governing the contract and any subsequent disputes.

Too often, international commercial arbitration can get bogged down in debating what law governs the contract compared to the arbitral procedure and, in turn, what is meant by "procedure." The "lex contractus," or substantive law, is the law that applies to the commercial issues and contract interpretation. On the international stage, some parties have opted for a more commercial, market-centered (lex mercantoria) or fair and equitable (amiable compositeur/*ex aequo et bono*) basis for decision. While some parties may view this as a suitable alternative to a single nation's rule of law, there can be uncertain and costly consequences for commercial parties to abandon a known rule of law and an identifiable body of precedent.

As noted earlier, the seat (or place) of the arbitration dictates the national law that the courts will apply to supervise or judicially review (set aside or vacate) the arbitral proceedings. In some cases where the parties have designated a place for arbitration but then specify another nation's laws to govern "procedural" issues, courts have endeavored to maintain consistency between external procedural law (*lex arbitri*) and the arbitral seat by interpreting the selection of a different "procedural" law to refer to the procedures that are *internal* to the arbitration (*i.e.,* evidentiary rulings, order and timing of proofs, etc.).

Recommendation: *Avoid confusion. Make a clear selection of controlling substantive law in a clause apart from the dispute resolution or arbitration sections. Within the arbitration clause, identify the seat and, if desired, directly tie the national law of the "seat" to govern the procedural issues. For example: "The seat of the arbitration, which will be deemed the place where the arbitral award is made, shall be New York City, and the courts shall apply the statutory and common laws of the United States, including but not limited to the U.S. Federal Arbitration Act, to decide procedural issues."*

With these foundations in place, you can consult the remaining sections of the *IBA Guidelines* to identify with your client which optional features make the most sense for your transaction.

FOR MORE INFORMATION, PLEASE CONTACT:

Richard A. Glaser is a member in Dickinson Wright's Grand Rapids office and can be reached at 616.336.1043 or rglaser@dickinsonwright.com.