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Article

***277** Drafting an Effective Arbitration Agreement in International Commercial Contracts

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CONTENTS

1 INTRODUCTION

Arbitration has over the years become the preferred method of resolving disputes arising in international commercial transactions. A body of international arbitral jurisprudence and settled procedural rules/laws; international customary practices; and principles recognised by nations involved in major international trade, have been developed. It is therefore of utmost importance that lawyers involved in the negotiation, drafting and interpretation of international commercial contracts should be very familiar with the various terms, and conditions which must be expressly agreed upon and included in the arbitration agreement to make it effective in meeting the needs of the parties in the event of a dispute arising under the particular contract.

This article will discuss some basic or fundamental issues or terms that must be considered by drafters and negotiators of international commercial arbitration agreements. In this article, "international commercial contracts" [FN1] includes all commercial contracts with an international character. This would include transactions between parties from different States; or having their places of business registered under the laws of different States; or the contract is to be performed in a different State from that of the nationality of the parties. [FN2]

2 DEFINITION

Arbitration refers to a method of private dispute resolution authorised by an ***278** agreement to that effect between the parties. It is private and not public. It is not regulated nor conducted under the auspices of a State mechanism like litigation. Arbitration is an alternative to litigation in a State court. This is especially useful in international commercial transactions where the parties involved are from different States or, by its very nature, the contract could be subject to the laws of various States. The parties might not trust the judiciary of their opponent and therefore may not be willing to be subjected to it. The witnesses, site for inspection, and evidence might not be easily accessible to either party's courts without incurring unreasonable expense. The parties might speak different languages. This might disadvantage one of the parties in any litigation before the national courts of the other party. The disadvantaged party might not be familiar with the procedural rules and laws of the foreign court, and might be constrained to use the local lawyers, with whom it is not

familiar. It might not be in a position to project the time and, by direct consequence, the cost of the litigation. It might then be subjected to various levels of appeal. These practical constraints have made litigating in either party's jurisdiction unattractive in international commercial dispute resolution.

Arbitration gives the parties the opportunity of making adequate provisions regarding these issues in their arbitration agreement. The arbitration agreement can be drafted as a dispute resolution clause in the body of the main contract. This agreement is pre- dispute (clause compromissoire). The parties can equally enter into a Submission agreement (compromise) when the dispute arises. In either case, the parties must conclude a valid arbitration agreement. Almost all international conventions and national laws and rules on international arbitration now recognise the efficacy of a pre-dispute arbitration clause embodied in a substantive contract. These laws also recognise the arbitration clause as a separate contract, with a separate existence from the main contract in which it is contained (the principle of separability). [FN3]

3 THE ARBITRATION AGREEMENT

The lawyer involved in negotiating or drafting an arbitration agreement in an international commercial transaction must consider the matters discussed below. These matters cover both the formal and substantive validity issues.

*279 3.1 THE ARBITRATION AGREEMENT MUST BE IN WRITING

Article 7 of the UNCITRAL Model Law defines an arbitration agreement as:

> (1) 'Arbitration agreement' is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.
>
> (2) The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telex, telegrams or other means of telecommunication which provide a record of the agreement, or in an exchange of statements of claim and defence in which the existence of an agreement is alleged by one party and not denied by another. The reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause part of the contract.

The Model Law's definition, which we shall use as a working model, [FN4] provides for pre-dispute arbitration agreements and submission, or post-dispute agreement. These we have discussed above. Subsection (2) details the form of a valid arbitration agreement. The most important of which is that the arbitration agreement must be in writing. [FN5] It then goes on to expound on what "writing" includes. The easiest way to prove an agreement in writing is to produce a written copy of it. The legal adviser must ensure that the arbitration agreement is in writing. It should be set out in clear and unequivocal terms in the main contract or be clearly referred to in a supplementary or separate agreement.

Article II of the New York Convention [FN6] is almost mirrored by Article 7 of the Model Law. Each Instrument provides for the means of communication prevailing at the time it was drafted but with the same aim of ensuring that the existence of the arbitration agreement is provable in evidence in a written form.

Article II.2 of the New York Convention states:

> ***280** The term 'agreement in writing' shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.

The arbitration agreement must be capable of being reproduced in written form to prove its existence. The arbitration agreement itself does not have to be signed separately [FN7] from the main contract. The execution of the main contract in which the arbitration agreement is embodied suffices. [FN8] However, where the parties execute a Submission agreement, then the agreement has to be duly executed by the parties.

It is important to note that if the arbitration agreement does not satisfy this writing requirement, it invalidates any

claims to the existence of a valid arbitration agreement. [FN9] The existence and validity of the arbitration agreement form the jurisdictional basis of any arbitration. It must be produced when recognition or/and enforcement of a final award is sought under the New York Convention. [FN10] The arbitration agreement must contain the names of the parties to be bound by it. The parties must be properly named, their assigns, principals, agents, and other relevant parties (if any) must be properly joined or included as parties. This is especially important where one of the parties is a State agency/department with the relevant State ministry not named in the main contract.

3.2 TYPES OF ARBITRATION

The lawyer must address the issue whether the arbitration would be ad hoc or institutional. The parties can choose to have their arbitration conducted under the Institutional Rules of a particular arbitration institution. Where the parties decide to have their arbitration under the arbitration laws/rules of the place where the arbitral tribunal would sit and not under the rules of any arbitration institution then, their arbitration proceedings is said to be "ad hoc". An ad hoc arbitration can be held in the premises of certain arbitration institutions (for example, the LCIA [FN11] and the LRCICA [FN12]). It is advisable to inquire from the arbitration institutions directly and to find out the terms under which this can be done. In this capacity, the arbitration ***281** institution concerned would offer administrative services and can act as an appointing authority. [FN13] The parties in an ad hoc arbitration can use a hotel room, conference centres, the arbitrators office, wherever would meet their particular needs.

Where the parties decide on an institutional arbitration, then it is advisable to decide on the particular arbitration institution and check out their Rules to ensure that its provisions would meet the needs of the parties. Once a particular arbitration institution has been decided upon, then its recommended arbitration clause should be reproduced as it is stated in its Rules as the arbitration agreement. The arbitration agreement should properly describe the institution, stating its correct name, description and location. This makes for certainty and clarity, and ensures the clause does not become pathological, as to raise doubts, which might make it null and void, inoperable, or incapable of being performed. [FN14] If the parties want to arbitrate under the Rules of the International Chamber of Commerce (ICC), then its arbitration agreement should contain the ICC standard clause:

> All disputes arising out of or in connection with the present contract shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with the said Rules. [FN15]

The version of the Institutions Rules to which the parties wish to be bound can be clearly stated, otherwise most institutions rules provide for the parties to arbitrate under the version of their rules in use at the time the dispute arises and not the version in use when the arbitration agreement was entered into.

3.3 SEAT OF ARBITRATION

The legal adviser must then avert his/her mind to the seat of the arbitration. Most institutional arbitrations can be held in any part of the world while applying the institutions Rules. It is equally now established that an arbitral tribunal can sit anywhere without having to change its legal or juridical seat. This in effect means that the seat of the arbitration can be Paris but the tribunal can meet in Lagos for the convenience of the parties and the arbitral tribunal. The choice of the juridical seat is very crucial. This is because the law of the seat would apply to various aspects of the arbitration as its lex arbitri. Some national courts, for example, English courts, would apply their laws as the substantive law where the main contract is silent on the applicable substantive law and England is the seat of the arbitration. This would have a disastrous effect where the ***282** drafters of the parties had omitted to choose the substantive law, with England as the seat, without any intentions of subjecting their contract to English law. The law of the seat of the arbitration would govern procedural issues such as the validity of the arbitration agreement, the arbitrability of the claim, and the enforceability of the arbitration agreement and award [FN16]

The law of the seat would be invoked where the parties need judicial assistance or any form of judicial intervention. The arbitration laws of the seat would have mandatory provisions from which the parties cannot derogate. It is therefore very important that the legal advisers comb through the arbitration laws of the proposed seat to ensure it will serve their arbitration effectively. It is the law of the seat that would determine if the arbitral tribunal can decide on its jurisdiction,

make interim orders of preservation, protection, freezing orders and injunctions, deal with multi-party, joinder and consolidation issues (some arbitration institution rules now provide for these matters). Arbitration by its very nature of being consensual, frustrates the ability of the arbitral tribunal to make orders binding on third parties. The courts at the seat would have to be asked to make such orders and to order the appearance of witnesses before the arbitral tribunal, to give evidence or to produce documents [FN17]. The need for the parties to choose an arbitration-friendly seat cannot be over emphasised. The arbitral tribunal being able to determine the existence and validity of an arbitration agreement, irrespective of an alleged invalidity of the main contract embodying the arbitration agreement (principle of separability); and determine its own jurisdiction when it is challenged (principle of competence-competence) would save time and cost of the proceedings. The arbitral tribunal should be able to make interim orders of preservation, protection and injunction. The subject matter of the transaction must be one that is capable of settlement by arbitration under the laws of the seat, since an award can be set aside at the seat on this grounds hinged on public policy considerations. [FN18] The arbitration agreement must be valid under the law of the seat and mandatory provisions of the lex arbitri must be complied with, failing which, the award might be disqualified from being recognised and enforced under the New York Convention. [FN19]

There are other practical issues that the legal adviser will have to equally consider in choosing the seat of the arbitration. They include issues of security or personal safety of the parties and arbitrators; access to exhibits and witnesses; political stability; efficient and effective telecommunication services; airports, hotels, restaurants, banks and accessibility and convenience of the seat to all relevant parties. Some laws require the final award to be signed at the chosen or juridical seat of the arbitration. It is good practice to sign the award at the place of arbitration.

***283 3.4 CHOICE OF LAW**

This is choosing the law that would apply to the main contract. It can also be the law that would apply to the arbitration agreement, though not necessarily. This ensures that the law, which the parties have considered and chosen to apply to their agreement would be applied and a different body of laws or rules not contemplated by the parties, and which might be wholly inappropriate, is not imposed on them. It equally would save the arbitral tribunal valuable time and expense in determining the applicable substantive law by applying conflict of law rules. The issue of any additional powers to be conferred on the arbitral tribunal overlaps between the choice of the seat of the arbitration and the applicable substantive law. The law of the place of enforcement might equally be relevant at the stage of enforcement relying on Art. V.2 of the New York Convention. An example is empowering the arbitral tribunal to award punitive damages (treble damages under the Shearman Anti trust law in the United States) where the law of the place of arbitration (or the law of the place where recognition and enforcement is sought under the New York Convention) does not permit such awards.

3.5 COMPOSITION OF THE ARBITRAL TRIBUNAL

It is advisable to agree on the number of arbitrators, any particular expertise, and professional or language requirements. This would have a major bearing on the value, complexity and technicality of the dispute. The parties can provide for a sole arbitrator to be jointly appointed by them or to be appointed by a named appointing authority. In most jurisdictions, the default position is that the national courts at the seat of the arbitration would appoint the arbitrator; [FN20] while under most arbitration institution Rules, the institution's court or secretariat would appoint the arbitrator. In most three-member arbitral tribunals, each party appoints an arbitrator and the two party-appointed arbitrators would then jointly appoint the chairman (presiding arbitrator) of the arbitral tribunal. Where the two party-appointed arbitrators fail to agree on the appointment of the third arbitrator, the arbitration institution, appointing authority or the court would make the appointment. It is not in keeping with modern trends to stipulate nationality, [FN21] gender or race of the arbitrator. This is because of the global drive towards racial and gender equality. Some arbitration institutions when appointing arbitrators on behalf of the parties would strive to appoint arbitrators of independent nationalities. It is equally not advisable to nominate a particular person as the arbitrator in a pre-dispute arbitration clause. This is for practical reasons. The nominee might have become deceased before the dispute arises, the nominee might become dependent on one of the parties, or be burdened with other assignments as not to have the time to dedicate to this particular arbitration, so as to disqualify him or her. This could render the arbitration agreement unenforceable and inoperable. In ad hoc arbitrations, it is important to nominate an ***284** appointing authority. The appointing authority would make default appointment of ar-

bitrators. [FN22]

3.6 LANGUAGE OF THE ARBITRATION

Where the parties are from different States having different languages, it is advisable to agree on the language(s) in which the arbitration proceedings would be conducted and if and translation of documents and proceedings would be necessary. Remember to expressly agree which of the parties would bear the additional costs of the translation and what documents would be translated, agreeing on which (or both) would be the authoritative version. This would also assist with the nomination and appointment of members of the arbitral tribunal. They might need to be fluent in the relevant languages. The default position would be to conduct the arbitration proceedings in the language of the contract.

3.7 SCOPE OF THE ARBITRATION AGREEMENT

The pre-dispute arbitration agreement must be worded very broadly, enough to encompass whatever dispute, no matter the nature, that might arise between the parties regarding the particular contractual transaction. The wording of any arbitration agreement must equally indicate that the proceedings would finally determine the dispute between the parties. This shows the finality of arbitration proceedings and makes for minimal court interference by way of appeals against awards rendered in an arbitration proceeding. Most national laws have limited grounds of appeal against final arbitral awards, which reflect the grounds stated in Art. V of the New York Convention. Some states have more limited grounds, for example, France. [FN23] The finality of arbitration conforms with the need to bring an end to litigation and therefore a final award renders the dispute res judicata, meaning that the issues arbitrated therein cannot be re-litigated between the same parties. The arbitration agreement can be worded to give the arbitral tribunal certain powers that might be necessary to the parties during the proceedings. An example is empowering the arbitral tribunal to make necessary interim orders within its jurisdiction, to award punitive damages as mentioned in Part 4.4 (above), amongst others.

3.8 EXECUTION OF THE ARBITRATION AGREEMENT

Most arbitration laws recognise that the pre-dispute arbitration clause contained in a contract which is duly executed, does not require any other form of execution, be it in the form of the parties appending their signatures to the clause or otherwise. [FN24] However, ***285** in a submission agreement, the arbitration agreement has to be duly executed by the parties. This is because the Submission agreement exists all by itself and does not form part of any other agreement. The arbitration agreement contained in a main contract is said to be a separate agreement, with its own independent existence, and therefore cannot be affected by any illegality or invalidity affecting the main contract. Where, however, the arbitral tribunal or a national court rules that the alleged contract containing the arbitration clause never came into existence, the existence of the arbitration clause then becomes an issue. The arbitration clause cannot exist in isolation from the main contract. This contention is discussed in the Pyramids case quoted above.

3.9 INCORPORATION BY REFERENCE

Where the parties have entered into a series of contracts or sub-contracts, or related contracts, and the relevant contract does not contain an arbitration agreement but refers to another contract containing an arbitration agreement, the relevant contract must make clear reference to the arbitration agreement and to forestall any difficulty of proof in the future, a copy of the arbitration agreement should be brought to the notice of the party to be bound by it. This is especially important in General Conditions of Contracts whose terms are not necessarily negotiated and agreed upon by the parties. A good and viable defence as to the existence and knowledge by the other party is the fact that it was duly notified.

3.10 MULTI-TIERED DISPUTE RESOLUTION CLAUSES

Following the recent trend in dispute resolution, regarding mediation and the use of non-binding alternative dispute resolution methods, lawyers now have to understand the various ADR methods that might be applied in the resolution of disputes in their clients industry. The parties might desire to attempt an amicable settlement of the dispute first, failing which they can commence arbitration. An escalating or multi-tiered dispute resolution clause can then be drafted, with adequate time limits to ensure that one party does not abuse the process by employing various delay tactics to frustrate

the commencement of arbitration or to force the other party into an unreasonable settlement terms. The lawyer can explore the possibility of "med-arb" with the parties. This envisages a process whereby the parties mediate their dispute and, failing a settlement, commence arbitration with the same third party neutral or a different third party neutral as arbitrator.

4 CONCLUSION

The legal adviser, negotiator, or drafter of an arbitration agreement must make out time to consider the legal implications of the terms of the arbitration agreement to be ***286** included as a clause in the main contract. [FN25] The major issues are discussed in this article and some guidelines given as to points to note. Time must be taken to study the arbitration institution Rules or applicable ad hoc or national arbitration laws of the chosen juridical seat - check the mandatory provisions of the relevant law to ensure that it will assist and not frustrate the arbitration proceedings before finalising the choice of seat, rules and substantive laws. A search must be conducted into the various States where your opponent has viable assets; then their arbitration laws must be checked to ensure they are user friendly and can be enforced under the New York Convention. Where a State party is involved, and it is not an ICSID [FN26] arbitration, [FN27] ensure that its consent is obtained from the proper and relevant authority and its identified assets upon which enforcement of the award can be levied, and which does not enjoy any form of immunity.

Legal advisers are encouraged to enlighten their clients involved in international trade on the necessity of including an arbitration agreement in all their contracts. There are arbitration institutions in all major trading cities (and nations) of the world. The courts of most international trading nations are very conversant with international arbitration procedure and render necessary assistance to parties arbitrating within their jurisdiction. [FN28] Arbitration institutions constantly revise their rules to make for better and improved arbitrations under their rules. The adoption and adaptation of the UNCITRAL Model Law by well over 36 nations as at the early 2003 and the availability of decisions rendered there-under by various courts and arbitration tribunals published by the UNCITRAL [FN29] makes for a more internationally recognised and uniform translation and implementation of international commercial arbitration laws.

A well-drafted and valid arbitration agreement ensures that the parties' desire to arbitrate their dispute will be given effect, with minimal interference from national courts, to save time and costs. It further ensures that the arbitral tribunal of the parties' choice is formed to render a validly recognisable and enforceable award in almost any part of the earth. The success of an international commercial arbitration is dependent, to a large extent, on the drafting of the arbitration agreement which evidences the efficacy of party autonomy.

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[FN1]. Article 3 of UNCITRAL Model Law on International Commercial Arbitration, 1985 (The Model Law)

[FN2]. See Art. 1.1 CISG (United Nations Convention on Contracts for the International Sale of Goods, Vienna, 1980); Arts. 1.3 and 1.4 of The Model Law.

[FN3]. See Art. II.2 of the New York Convention (Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958); Art. 7(1) of The Model Law; Art. 3 of the new Brazilian Arbitration Law, 1996; Art. 16 of the Arbitration Law of The People's Republic of China, 1995; s. 6(1) of the Arbitration Act, 1996 of England & Wales; Art. 1442 of the French Code of Civil Procedure 1981; s. 1(1) of the Nigerian Arbitration and Conciliation Act, 1988; Art. 1.1 of the UNCITRAL Arbitration Rules, 1976.

[FN4]. This is because the Arbitration laws of more than 34 States are modelled after the Model Law.

[FN5]. See s. 5 of the English Arbitration Act. It states that the arbitration agreement should be in writing, and goes on to give a comprehensive list of what would be construed as an agreement in writing, including 'agreements otherwise in writing'.

[FN6]. Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958.

[FN7]. See s. 5(2)(a) of the English Arbitration Act, 1996.

[FN8]. See the decision of the Bermuda Court of Appeal in Sojuznefteexport (SNE) (USSR) v Joc Oil Ltd (Bermuda) (1989) 4 IAR B1; Yearbook Comm. Arb. **Vol**. XV (1990) 384.

[FN9]. See: Di Pietro, D. and Platte, M., Enforcement of International Arbitral Awards, 2001 published by Cameron May Ltd, at 67-75. See also Art. V.1(a) of the New York Convention.

[FN10]. Article IV (b). In Yukos Oil Co. vs Dardana Ltd [2002] EWCA Civ. 543; the English Court of Appeal held that an application for enforcement of an award is in two stages- (1) production of the award and an arbitration agreement in writing (s. 102), even if the arbitration agreement is not binding on the respondent; (2) the respondent would then have to show that one of the grounds in s. 103 (2) is made out. This shows the importance of having a written arbitration agreement. It satisfies the first hurdle required in enforcement of award proceedings.

[FN11]. The London Court of International Arbitration.

[FN12]. Lagos Regional Centre for International Commercial Arbitration.

[FN13]. Where this is provided for. An example is the nomination of an Appointing Authority contemplated under The Model Law and the UNCITRAL Rules regarding the appointment and challenge of arbitrators. See Art. 6 of The Model Law and Art. 6.1 UNCITRAL Rules.

[FN14]. See Art. II.3 of the New York Convention.

[FN15]. The standard ICC arbitration clause contained in the 1998 ICC Rules of Arbitration.

[FN16]. McLaren, D.E., 'A Fresh Look at ADR: International Commercial Arbitration'. A Paper delivered at the 2000 American Corporate Counsel Association Annual Meeting, at p. 8. See also Art. V.I(e) of the New York Convention.

[FN17]. See Art. 27 of The Model Law.

[FN18]. See Art. V.I(e) of the New York Convention.

[FN19]. Article V (a)(d)(e) show the relevance of the law of the seat in setting aside proceedings.

[FN20]. An example is s. 18 (2) of the English Arbitration Act, 1996.

[FN21]. See Art. 11 (1) of The Model Law. See also (5) which states that it would be advisable to appoint an arbitrator of a nationality other than those of the parties. Some other arbitration institutions (for example the ICC) adapt the same practice of appointing an arbitrator of a different nationality from the parties.

[FN22]. See Arts. 6.2 and 7.2 (a) of the UNCITRAL Arbitration Rules 1976.

[FN23]. Article 1484 of Book IV of the Code of Civil Procedure Rules, 1981 which does not contain the ground listed in Art. V (l)(e) of the New York Convention.

[FN24]. See SPP (Middle East) Ltd. and Southern Pacific Properties Ltd v. Arab Republic of Egypt and Egyptian General Company for Tourism and Hotels (the 'Pyramids case') (1984) 23 ILM 1048, where the Egyptian Government successfully argued the non-existence of the arbitration agreement which was contained in a contract to which Egypt did not execute and was not a party. The fact that the arbitration agreement is a separate agreement gave the arbitral tribunal jurisdiction to hear the application.

[FN25]. See generally, W. Ray Turner's article in the Practice Teaching Section of the Journal of the Chartered Institute of Arbitrators entitled 'Arbitration Agreements', published in Arb (2000) 66 (3), at pp. 230-236.

[FN26]. Rules of Procedure for Arbitration Proceedings of the International Centre for the Settlement of Investment Dis-

pute, 1965; see also ICSID Additional Facility Rules.

[FN27]. See Asouzu, A.A., International Commercial Arbitration and African States; published by Cambridge University Press, 2001, pp. 215-401.

[FN28]. See Sanders, P., Quo Vadis Arbitration? Sixty Years of Arbitration Practice - A Comparative Study, Kluwer Law Int'l, The Hague (1999).

[FN29]. See CLOUT (Case Law on UNCITRAL Texts) on the UNCITRAL website, available at: <http://www.uncitral.org>.

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