

ICC Examines the Use of International Arbitration by Financial Institutions

An extensive report [issued](#) recently by the International Chamber of Commerce (ICC) confirms that arbitration is appropriate for resolving disputes in many fields of banking and finance activity, dispelling previously held conceptions that it is not. Taking an empirically based approach to its analysis, the report examines the use of arbitration across the industry and provides users with guidance as to how they can effectively tailor arbitration to their specific needs.

The use of arbitration in the finance sector has historically lagged behind its use in many sectors, with the general perception that litigation is better suited for the resolution of banking and finance disputes. This notwithstanding that in 2013, 69% of in-house counsel considered arbitration to be "well-suited" to the industry indicating a mismatch between perception and reality.¹

The Task Force

The ICC Task Force on Financial Institutions and International Arbitration (the Task Force) was set up "to study the use, perception and experience of international arbitration by financial institutions, as well as to identify and propose recommendations to increase the attractiveness of international arbitration to financial institutions."² During the two year long research process, the Task Force (which included Clifford Chance's London Partner Marie Berard) conducted interviews with over 50 financial institutions from across the globe, and analysed hundreds of internal policies, arbitral awards, and relevant articles as well as data from 13 participating arbitral institutions. The ICC Commission's Report, 'Financial Institutions and International Arbitration' (the Report) confirms that international arbitration is used in the banking and finance

sectors, albeit not to its "full potential",³ despite recent industry-specific initiatives that facilitate and support arbitration. There remains a lack of awareness across the industry of the benefits of international arbitration, coupled with an overstated perception that there are limitations to using arbitration in banking and financial disputes.

The Report considers the use of arbitration in specialist banking and finance areas, makes general recommendations and provides guidance on the use of arbitration in the industry.

Sector-specific analysis

Financial institutions enter into commercial transactions like any other corporate entity. These might include the purchase of products, services, or investments in equity stakes in other companies all of which may give rise to disputes that can be resolved by arbitration. The industry also encompasses many specific types of transactions and areas of financial activity. The Report examines the current – and possible future – use of arbitration in specific specialist areas. A few salient points are set out below.

1. **Arbitration of derivatives disputes:** The framework for the resolution of derivatives disputes through arbitration has evolved in recent years. Notably, optional arbitration clauses were introduced into the ISDA Master Agreement in 2013 (see [here](#) for our previous briefing). Knowledge of arbitration is growing in the sector as "arbitration has increasingly been

¹ Corporate Choices in International Arbitration: Industry Perspectives', Queen Mary, University of London, PwC, 2013, <http://www.arbitration.qmul.ac.uk/docs/123282.pdf>.

² See <http://www.iccwbo.org/About-ICC/Policy-Commissions/Arbitration/Task-forces/Task-Force-on-Financial-Institutions-and-International-Arbitration/>.

³ The Report, para 32.

presented as a viable alternative to litigation".⁴ This is particularly the case when dealing with counterparties from emerging markets where the strong system surrounding the enforcement of arbitral awards can be particularly attractive. In this sector, the expertise of decision makers is important, and arbitration may prove attractive to financial parties who can select arbitrators with specific derivatives expertise.

2. **Sovereign finance disputes:** The Task Force carried out a detailed review of sovereign bonds and capital markets documentation issued by 92 governments and found that 20% of sovereign bonds included arbitration as a dispute resolution mechanism. When contracting with a sovereign counterparty, there is a strong preference for arbitration (immunities from suit typically enjoyed by a State can be waived by agreements to arbitrate). Non-payment is the most common issue in the context of sovereign finance. For these sorts of disputes, arbitration may not prove a particular advantage (for example, there is no need for arbitrators with specific finance expertise). However, more complex sovereign finance disputes such as sovereign debt restructuring may well engage a state's liability under investment treaties, which invariably provide for arbitration (see further below).
3. **Investment arbitration and Banking & Finance:** The Report includes interesting observations regarding the use of Investor-State Dispute Settlement (ISDS) by financial institutions through investment treaties. Whilst there are some notable exceptions, investments relating to the oil & gas, mining and other sectors traditionally associated with long-term foreign direct investment are often protected by such treaties. In relation to financial instruments, the Report notes that depending on the type of instrument, and depending on where it can be said that the investment has been "made", it may be difficult to establish protection for the instrument under an investment treaty. That said, the Task Force predicts that the landscape in this area will change as more case law considers these issues closely and as investment treaties provide more specific reference to the type of financial instruments that qualify for protection.
4. **Arbitration of disputes relating to regulatory matters:** Arbitration is far less common in relation to regulatory matters. This is hardly surprising as regulatory issues also often involve questions of public policy and are dealt with by the courts and special

⁴ The Report, para 68.

The Report considers the use of arbitration in the following areas:

- derivatives
- sovereign finance
- international financing
- Islamic finance
- international financial institutions (IFIs), development finance institutions (DFIs) and export credit agencies (ECAs)
- advisory matters (including M&A and equity markets)
- asset management
- investment arbitration and financial institutions
- arbitration of disputes relating to regulatory matters

administrative tribunals. Nevertheless, respondees to the Task Force were receptive to using arbitration to settle the civil consequences of regulatory breaches. Indeed arbitration has proved successful in the context of disputes between financial institutions and their customers (e.g. through arbitration proceedings administered by the Financial Industry Regulatory Authority in the United States, or the Financial Dispute Resolution Centre in Hong Kong).

5. **Arbitration of international financing disputes:** The Task Force noted a "reticence"⁵ in the use of arbitration in international financing transactions, particularly in relation to syndicated lending and asset finance where litigation is considered preferable. However, arbitration is prevalent in international project finance and general loans. In relation to trade finance (an area where disputes have traditionally been resolved through litigation), there is a general recognition that litigation may not always be the best option. Taking into account the diversity of the international financing sector, the Task Force concludes that "[w]hether arbitration is attractive in any given transaction will depend on the specific circumstances",⁶ including the quality of the courts available and potential arbitrability issues (enforcement of certain security provisions or insolvency matters).

⁵ The Report, para 101.

⁶ The Report, para 107.

6. **Arbitration of Islamic finance disputes:** The potential of international arbitration in the context of Islamic finance remains "completely untapped."⁷ Arbitral tribunals are free to apply Shari'a law if the parties have chosen it (subject to any restrictions regarding applicable law in the law of the seat). According to the Task Force, this should encourage parties who wish to see Shari'a law applied to their disputes to choose arbitration in preference to litigation before certain courts whose approach to clauses referring to Shari'a law is unclear.
7. **Arbitration of disputes involving IFIs, DFIs and ECAs:** IFIs, DFIs as well as ECAs are familiar with and are regular users of international arbitration, having set out their preferences (e.g. institutional arbitration rather than ad hoc arbitration) in standard dispute resolution clauses. This is driven by the high prevalence of major transactions with State-owned entities in emerging countries. Arbitration is often seen as a more neutral process than court litigation, and arbitral awards are likely to be more easily enforceable than a court judgment in certain jurisdictions.
8. **Arbitration of disputes relating to advisory matters:** Financial institutions have limited experience of arbitration in the context of M&A and advisory work more generally despite the fact that arbitration appears to be "ideally suited"⁸ to these types of work given the complexity of the issues typically raised and the need for confidentiality in this field.
9. **Arbitration of disputes relating to asset management:** Arbitration is well suited to the resolution of the potentially complex disputes relating to asset management activities (with the added benefits of confidentiality), and remains underutilised in this sector.

General recommendations

The Task Force makes several general recommendations that address the perceived limitations of arbitration expressed by those interviewed. The Report emphasises that in most cases it is possible to tailor "the arbitration procedure to suit the needs of the banking and financing sector."⁹

The Report also emphasises various case management / time and cost-reduction techniques recommended in

arbitration proceedings, and sets out the drafting and procedural options available to banks and other financial institutions - ranging from requirements regarding the arbitrators' expertise to the possibility to opt out of appellate procedures, or to expressly permit appeals.

For example parties can, through drafting, empower the arbitral tribunal to consider claims or defences on a summary basis or summarily dismiss claims or defences that are manifestly without legal merit. The Task Force recommends that financial institutions develop policies guiding their teams as to when arbitration is or is not appropriate so that bespoke arbitration agreements can be drawn up. Trade associations, such as the Loan Market Association, might play a role in standardising arbitration clauses for use in specialist sectors.

Arbitration as a flexible tool

The extensive empirical research conducted by the Task Force provides a welcome understanding of how arbitration is currently being used by the financial sector and how the mechanism can be tailored to the specific needs of different specialist sub-sectors of the industry. Whether arbitration or litigation is appropriate for a particular type of transaction is driven by a number of transaction-specific factors, these include:

- the location of parties and the assets – if they are located in a jurisdiction where the recognition of foreign judgments is problematic, parties may wish to opt for arbitration to benefit from easier enforcement of the arbitral award under the New York Convention;
- the type of legal questions in dispute;
- whether a long or short process is practical or desirable;
- whether industry expertise will be relevant;
- whether the parties wish to be protected by confidentiality;
- whether, and if so to what extent, is document production desirable;
- whether a summary or expedited form of proceedings is required; and
- whether they would prefer a decision that has precedential value.

Where arbitration is preferable to litigation it can be used in a way which addresses concerns about its efficacy, given its inherent flexibility. The vast majority of the concerns expressed by financial institutions surveyed by the Task Force can be addressed in carefully drafted, bespoke arbitration agreements.

⁷ The Report, para 108.

⁸ The Report, para 135.

⁹ The Report, para 8.

Clifford Chance has many years of experience representing financial institutions in the ever increasing number of disputes being arbitrated. Examples include:

European Bank vs. Russian guarantor in loan guarantee enforcement dispute	Middle East sovereign wealth fund vs. South-East Asian state investment company	International Bank re: enforcement of Indian investment
<p>Our London, Moscow and New York teams acted for a major European bank in connection with a US\$1.2 billion loan guarantee dispute against a Russian guarantor. The main dispute was successfully resolved by arbitration in London under the LCIA Rules. We also successfully defended the bank against parallel Russian proceedings started by minority shareholders of the Russian guarantor; obtained anti-suit relief in the English courts to restrain the Russian proceedings; and secured the dismissal of the borrower's claim in the New York courts.</p>	<p>Our London, Dubai and Abu Dhabi teams are currently advising a Middle East sovereign wealth fund on a high profile LCIA arbitration in London against a South-East Asian state investment company in relation to a binding term sheet for the provision of debt financing through an asset swap agreement.</p>	<p>Our Hong Kong and Singapore offices represented the investment banking division of a multinational banking and financial services organisations in two parallel arbitrations arising out of its investment in a film post production company in India and Dubai. We obtained Interim Awards from the SIAC Emergency Arbitrator requiring the Respondents to stop further dissipation of assets, freezing their bank accounts and to disclose information. The Emergency Awards were then utilised to freeze funds in India. We went on to prevail in the substantive actions and, through local counsel, are presently enforcing the awards against the frozen funds.</p>
International Financial Institution vs. Industrial contractor regarding drawdown of letter of credit	British Bank relating to escrow arrangements	Nigerian bank re: consultancy services claim
<p>Our London and Paris teams represented an international financial institution in an ICC arbitration, successfully defeating the claims by a Eastern European steel mill contractor which alleged tortious interference in the drawdown of a letter of credit and unjust enrichment.</p>	<p>Our London team advised a British multinational banking and financial services company in a dispute concerning the operation of an escrow agreement and alleged breaches of Reserve Bank of India regulations in AAA arbitration proceedings seated in New York.</p>	<p>Our London office successfully defended a major Nigerian bank in a US\$855 million claim brought by a dissatisfied service provider arising out of a failed pre-paid credit card programme in <i>ad hoc</i> arbitration based in London pursuant to the Arbitration Act 1996.</p>
South African Bank re: non-payment of loans in Mongolia	Western European Bank vs. Greek Bank in post M&A dispute	European bank re: insurance policy
<p>Our London team represented a South African Bank (and syndicated lenders) in three London-seated LCIA arbitration proceedings (and associated court applications) against a Mongolian and Russian State-owned mining company arising out of several trade finance agreements.</p>	<p>Our Paris team advised a Western-European bank in post M&A arbitration proceedings arising out of a sale of a subsidiary to a Greek bank. The dispute concerned alleged breaches under a share purchase agreement, Greek debt refinancing and banking regulatory issues.</p>	<p>Our Dubai office is acting for a European state-owned bank in parallel ICC Arbitration and Dubai International Financial Centre (DIFC) Court proceedings defending claims by an insurer for a declaration of non-liability under an insurance policy. The dispute involves complex questions of jurisdiction and allegations of non-disclosure, misrepresentation, deceit and bad faith brought by the insurer against eight defendants.</p>

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