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PITFALLS IN THE DRAFTING OF ARBITRATION
AGREEMENTS

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DECLARATION

I hereby declare that this thesis represents my own work, except where due acknowledgement is made, and that it has not been previously included in a thesis, dissertation or report submitted to this University or to any other institution for a degree, diploma or other qualification.

Signed.....

Thuo Caroline Wambui

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ABBREVIATIONS

AAA	American Arbitration Association
ADR	Alternative Dispute Resolution
CIArb	Chartered Institute of Arbitrators
CISG	Convention on International Sales of Goods
CLOUT	Case Law on UNCITRAL Text
ICC	International Chamber of Commerce
ICSID	International Centre for the Settlement of Investment Disputes
LCIA	London Court of International Arbitration
UNCITRAL	United Nations Commission on International Trade Law
Unrp	Unreported case
WIPO	World Intellectual Property Organization

TABLE OF CASES

- Ashville Investments Ltd-vs- Elmer Contractors (1988) Lloyds Rep.
- Chambers –vs- Goldthorpe (1901) 1 KB 624
- Ethiopian Oilseeds and Pulses Export Corp –vs- Rio del Mar Foods Inc. (1990) 1 Lloyds Rep
- Fairacres Development Ltd –vs- Margaret Apondi Olotch t/a M.A. Kiosk [2005] eKLR
- Fillite (Runcorn) Ltd-vs- Agun-lift (a firm) 45 BLR
- Home Insurance –vs- Meator Insurance [1989] All E.R.
- HFCK –vs- Gitutho Associates Misc Civil Application No. 76 of 2000 (OS) unrp
- ICC Case No. 9480/AC (July 1998)
- Jupitar Chit Fund P. Ltd –vs- Dwarka Dinesh Dayal, (1981) ALL ER
- Kaverit Steel & Crane Ltd-vs- Kone Corporation (1994), Vol. XVII Yearbook Commercial Arbitration
- Kirii –vs- Ngari Kirii Nyeri Civil Appeal No. 12 of 1985 unrp
- London and North Western and Great Western Joint Rly Cos. –vs- JH Billington Limited (1899) AC
- Madan Mohan Rajgarhia –vs- Mahendra R. Shah & Bros (2003) 7 SCC
- Mitsubishi Motors Corp –vs- Soler Chrysler Plymouth Inc (1985) 473 U.S
- Nakuru Civil Appeal No. 6 of 1983
- Ram Chandra Ram Nag Ram Rice & Oil Mills Ltd –vs- Howarah Oil Mills Ltd (1958) AIR
- Re Carus-Wilson & Greene (1886) 18 QBD
- Sankar Sealing Systems (P) Ltd –vs- Jain Motor Trading Co (2004) AIR
- Union of India -vs- Ralli Ram (1964) 3 SCR

CHAPTER ONE

RESEARCH REPORT

1. Pitfalls in the drafting of Arbitration Agreements

1.1 Introduction

Arbitration has been defined as a method of dispute resolution involving one or more neutral third parties who are usually agreed to by the disputing parties and whose decision is binding.¹

It is a process by which parties voluntarily refer their dispute to an impartial third person, an arbitrator, selected by them or through a process agreed by them or by an appointing authority for a decision based on evidence and argument to be presented before the arbitration tribunal.

An agreement by the parties to submit to arbitration any disputes or difference between them is the foundation stone of modern international commercial arbitration. If there is to be a valid arbitration, there must first be a valid agreement to arbitrate.² The arbitration agreement fulfils several important functions. It is the arbitration agreement which shows that the parties have consented to resolve their disputes by arbitration.

Whereas litigation proceeds under the laws and judges assigned by the court, arbitration is formed and preceded by the agreement of the parties concerned. The arbitration agreement or clause is therefore significant in this respect. In this sense, the core concept of the arbitration is party autonomy³; the parties may in the arbitration agreement or

¹ Garner Bryan et al (1999), *Black's Law Dictionary* 8th Edition , Sweet and Maxwell, London

² Redfern A & Hunter M, (1999), *Law and Practice of International Commercial Arbitration*, 3rd edition, Sweet & Maxwell, London, page 4

³ Party autonomy refers to the freedom conferred on the parties to decide how any dispute arising between them maybe settled. This is usually encompassed in the arbitration agreement. The concept of party autonomy is enshrined under Article 19(1) of the UNCITRAL Model Law (Model Law) which provides as follows:-

"Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings".

The same language has been adopted under Section 20 of the Arbitration Act.

clause decide the scheme of the arbitration, choose and determine either institutional arbitration or *ad hoc* arbitration⁴, place of arbitration, appointment of arbitrators, arbitration procedure, the authority of arbitrators, and the governing law.

The parties may agree on the governing law applicable to the substance of the dispute which is an important aspect especially where the parties are of different nationalities, to procedure of arbitration or to the arbitral award. In this respect therefore, the arbitration agreement or clause is significant. Despite their significance, arbitration agreements and clauses are often dealt with at the end of negotiations, when the negotiators are tired and the drafters lay little emphasis on the arbitration agreement.

In most cases, parties and negotiators do not give any great emphasis on the arbitration agreement. According to Born, International arbitration agreements are deceptive creatures. Although often brief and superficially simple, they can raise complex legal issues.⁵

There is therefore requirement for greater care and attention when drafting the arbitration agreement. In so doing, drafters can steer clear of such problems as over-specificity, ambiguity, conflicting clauses, and other problems.

Most international and national laws on arbitration do not place greater emphasis on the proper drafting of the arbitration agreement. The only emphasis given is that it must be in writing.

Under the Kenyan Arbitration Act⁶ and the United Nations Commission on International Trade (UNCITRAL) Model Law on International Commercial Arbitration, an arbitration

⁴ *ad hoc* arbitration refers to an arbitration process where parties create their own rules for a particular case, or incorporate in their agreement one of the pre-existing set of rules of a well-known arbitral institution, or adopt a combination of such pre-drafted rules, but without submitting the proceeding to any pre-established institution. Institutional arbitration on the other hand refers to an arbitration process where parties refer any dispute arising between them to an arbitral institution such as the London Court of Arbitration.

⁵ Gary Born, (2001), *International Commercial Arbitration, Commentary and Materials*, 2nd edition, Kluwer Law International, page 55

⁶ Act No. 4 of 1995 see Section 4 thereof.

agreement must be in writing. ⁷No other requirement is needed or emphasized upon. This results in the “*casual*” drafting of the same.

It is therefore paramount to make a case for the call for greater emphasis and attention to ensure that arbitration agreements are properly drafted, are certain, enforceable and provide for all pertinent issues on settlement of disputes through arbitration.

1.2 **PROBLEM STATEMENT**

Arbitration agreements are the cornerstone of the arbitral process, when poorly drafted they result in problems which undermine the entire arbitral process.

1.3 **MAIN RESEARCH OBJECTIVE**

The main research objective of this project paper is to examine the functions of the arbitration agreement, provide for the requirements for a valid and effective arbitration agreement, consider the pertinent factors and choices in drafting an arbitration agreement and the dangers attendant to the lack of a proper arbitration agreement with a view to offering a guide for the emphasis on proper drafting of an arbitration agreement.

1.4 **SPECIFIC OBJECTIVES**

1.4.1 To provide for the vital functions of the arbitration agreement as a basis and cornerstone of every arbitration.

1.4.2 To analyze the formal and substantive requirements for a valid and effective arbitration agreement.

⁷ Article 7(1) of the UNICITRAL Model Law provides that an 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 form of an arbitration clause in a contract or in the form of a separate agreement. Sub-clause 2 provides that the Arbitration Agreement shall be in writing and it 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.

1.4.3 To consider the pertinent factors and choices in drafting an arbitration agreement and the dangers attendant thereto.

1.4.4 To suggest areas for reform to ensure that the arbitral process is not hampered by recommending necessary considerations and emphasis on the arbitration agreements.

1.5 **HYPOTHESIS**

1.5.1 Arbitration is an efficient tool for resolution of commercial disputes.

1.5.2 Arbitration agreements play a vital role and function in determining the manner in which a dispute will be resolved.

1.5.3 There is general lack of emphasis and consideration in the drafting of arbitration agreements.

1.5.4 Lack of proper considerations in drafting of the arbitration agreement hampers the effective resolution of disputes.

1.5.5 If greater emphasis is placed when drafting the arbitration agreement, the process of resolution of disputes through arbitration would be greatly improved and enhanced.

1.6 JUSTIFICATION AND SIGNIFICANCE

The value of this thesis is: -

- 1.6.1 It provides for the role and value of arbitration agreements in ensuring that disputes are properly referred to arbitration in the resolution of commercial disputes and in so doing provide for a case for the upholding of commercial arbitration.
- 1.6.2 Since commercial arbitration is useful for the resolution of commercial disputes in a most efficient and advantageous manner, this should be promulgated and encouraged and therefore any study aimed at illustrating how to achieve the ends of commercial arbitration through proper drafting of the arbitration agreements is justifiable.
- 1.6.3 The thesis provides a positive guide to the proper drafting of arbitration agreements for reference of commercial disputes to arbitration in order to ensure that arbitration as a means of settling commercial disputes is maintained and valued.
- 1.6.4 The thesis also identifies and explores the problems attendant to the poor drafting of arbitration agreements and makes a case for proper emphasis on the arbitration agreement.

1.7 CENTRAL RESEARCH QUESTION

Does the lack of a proper and effective arbitration agreement hamper the resolution of commercial arbitral disputes?

1.8 **RESEARCH QUESTIONS**

- 1.8.1 What is the role of arbitration in the resolution of commercial disputes?
- 1.8.2 What are the functions of the arbitration agreements in the resolution of commercial disputes?
- 1.8.3 What factors need to be considered in drafting an effective and valid arbitration agreement?
- 1.8.4 What are the consequences of an improperly drafted arbitration agreement?
- 1.8.5 What measures are necessary to ensure that arbitration agreements are properly drafted?

1.9 **CONCEPTUAL FRAMEWORK**

When parties need to resolve a dispute, they may often turn not only to the Courts as a method of dispute resolution but also to other alternatives such as arbitration and alternative dispute resolution.

Arbitration has grown over the years because of its obvious economic advantages to the parties and to the society. Parties usually take rational account of the effects of arbitration on the likely disposition of their disputes. Parties usually adopt arbitration because it is to the mutual benefit of the parties to a contract.

Arbitration is based on the contractual concept. According to Bonn Robert, among the devices developed to help parties maintain their contractual obligation is the adjudicatory system of arbitration. Such systems are replacing the courts since their reliance on custom permits greater flexibility in decision making and they are considered to be more private, economic, rapid, certain and conducive to business relationships.⁸

⁸ Bonn Robert (1972), *Arbitration: An alternative system for handling contract related disputes*, Administrative Science Quarterly, Volume 17.

Freedom of contract has been regarded by philosophers, economists and judges as a justification to the will theory of contract and its economic justification in the laissez faire liberalism. Here parties are the best judges of their own interests, and if they freely and voluntarily entered into a contract, the only function of the law was to enforce it.⁹

In numerous judicial cases, the courts have considerably supported the doctrine of freedom of contract, Lord Diplock in *Photo Production Limited vs. Securicor Transport Limited*¹⁰ observed that the basic principle of the common law of contract is that parties to a contract are free to determine for themselves what primary obligations they will accept.

An arbitration agreement is for all purposes a contract between the parties as to the manner in which disputes arising between them may be resolved. Under the concept of the freedom to contract, there is little regulation and parties are allowed to determine how their contract will be governed. This concept is central in the arbitration agreement since parties are free to determine, which disputes will be arbitrated, who the arbitrator will be, the seat of arbitration and the law to be applied to the arbitration amongst all other choices regarding the manner of resolution of disputes that may arise between them.

Since the courts are reluctant to interfere with the agreement of the parties, it is imperative that parties or their Advocates take due care when drafting the arbitration agreement. The freedom to contract should be maximized in the arbitration agreement with the parties agreeing virtually on all matters touching on any disputes between them.

In arbitration, this concept of freedom to contract is also referred to as *party autonomy*¹¹ this doctrine of party autonomy is embodied in national and international laws on

⁹ Chitty on Contracts (1826-1999) Beale H.G et al (eds), Volume 1, 28th Edition, Sweet & Maxwell, London.

¹⁰ (1980) A.C 827

¹¹ Redfern and Hunter *Law and Practice of International Commercial Arbitration*, 4th Edition, 2004 at page 315 provide as follows:-

“Party autonomy is the guiding principle in determining the procedure to be followed in an international commercial arbitration. It is a principle that has been endorsed not only in national laws, but by international arbitral institutions and organizations. The

arbitration which usually call for the enforcement of the intention of parties to an arbitration agreement and which provide for minimum intervention by the court in the arbitral process.

The other concept is the “separability doctrine” which was articulated by the United States Supreme Court in *Prima Paint Corporation vs. Flood & Conklin Manufacturing Co.*¹², wherein the Court ruled that arbitration clauses can be “separable” from the contracts in which they are included. The concept of the separability of the arbitration clause,¹³ means that the arbitration clause in a contract is considered to be separate from the main contract of which it forms part and, as such, survives the termination of that contract.

Separability thus ensures that if, for example, one party claims that there has been a total breach of contract by the other, the contract is not destroyed for all purposes. Instead:

*“It survives for the purposes of measuring the claims arising out of the breach, and the arbitration clause survives for determining the mode of their settlement. The purposes of the contract have failed, but the arbitration clause is not one of the purposes of the contract.”*¹⁴

Parties and their Advocates should thus bear in mind this concept of separability when drafting the arbitration agreement. The same emphasis which parties and their Advocates place on the container or main agreement should be placed on the arbitration agreement.

The primary or main contract concerns the commercial obligations of the parties; the secondary or collateral contract contains the obligation to resolve any disputes arising from the commercial relationship by arbitration. This secondary contract may never

legislative history of the Model Law shows that the principle was adopted without opposition”
¹² 388 U.S. 395 (1967)
¹³ This concept is known in some systems of law as the autonomy of the arbitration clause – *l'autonomie de la clause compromissoire*
¹⁴ per Lord MacMillan in *Heyman -v- Darwins Ltd* [1942] A.C. 356 at 374

come into operation; but if it does, it will form the basis for the appointment of an arbitral tribunal and for the resolution of any dispute arising out of the main contract.

This secondary contract should be treated with as much diligence and emphasis as the primary contract. This however is often not the case. Parties and their Advocates rarely place as much emphasis on the arbitration agreement as they do the main contract; this often inevitably leads to disastrous consequences including having such an arbitration agreement declared invalid.

This thesis argues for greater emphasis and care to be placed by parties while drafting the arbitration agreement to ensure that the parties' intention and desires in having their disputes resolved by arbitration is upheld.

1.10 **RESEARCH METHODOLOGY**

The research methodology adopted is both qualitative¹⁵ and desk based. Qualitative research involves interviewing key informants in the field of arbitration to establish the various issues they have encountered as regards arbitration agreements. In Kenya, the main body is the Chartered Institute of Arbitrators of the United Kingdom, Kenya Branch with key informants being the Chartered Arbitrators. Chartered Arbitrators are at the highest hierarchy of arbitrators in Kenya. These are people who have undertaken various courses in arbitration and who have also conducted arbitrations of varying degrees and of different nature. They are therefore useful in illuminating how the arbitration process works, including how important the arbitration agreement is to the process and the challenges arising from improperly drafted arbitration agreements.

The other research methodology adopted is desk-based. This involves the study of literature and available data on the research problem and topic. Such literature includes: international instruments such as Treaties and model laws, regional instruments and

¹⁵ Qualitative research refers to a method of inquiry which is exploratory in nature and which employs different data collection methods such as interviews, group discussions and focus group discussions. It is a purposeful research methodology aimed at collecting informed data on a specified issue or topic.

regional arbitration bodies' instruments such as the Rules of Arbitration developed by the Chartered Institute of the United Kingdom and those of the International Chamber of Commerce. The other data includes statutes, arbitral rules and cases. Other literature includes textbooks on the field of research and internet sources. This is useful in the generation of ideas and themes relevant to the research problem.

1.11 **LITERATURE REVIEW**

Since arbitration became the preferred dispute resolution method in the business relations in most countries, an impressive amount of specialized literature came to the light. Besides the impressive wave of honorable mentions, the books and articles slowly started to also reveal the defects and problematic elements of the arbitral proceedings. Such a potential problem is the one analyzed in the research. Although the existing literature indirectly touches upon the different points of the topic, there is yet no comprehensive analysis available on the research problem.

Treaties, Statutes and Rules relating to recognition and enforcement of arbitral awards

The main Treaty is the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958 (the New York Convention) it is the main international source of law for arbitration and it was enacted to address the issue of recognition and enforcement of foreign arbitral Agreements and Awards. The New York Convention however, does not lay emphasis on the substance of the arbitration agreement. This defect has contributed to many drafters of arbitration agreements failing to lay emphasis on the content of the arbitration agreement.

The other international instruments which are considered include the UNCITRAL Model law on International Commercial Arbitration which adopts the language of the New York Convention and which save for providing that the arbitration agreement shall be in writing does not proceed any further to state what the content of such an agreement would entail. Other international treaties include the London Court of International

Arbitration Rules and the Washington Convention on the Settlement of Investment Disputes between States all of which do not have provisions on the arbitration agreement.

Books, Articles, Journals and other literature

The books significant to the research include:

International Commercial Arbitration and African States;¹⁶ the author of the book argues for the establishment of an arbitration structure and institutions for Africa which would satisfy the legitimate expectations of local investors and traders. The book does not however focus on the Arbitration agreement and its importance which is the central argument in this thesis.

Just Do It- Drafting the Arbitration Clause in an International Agreement;¹⁷ this article is extremely useful in this research as its focus is also on how arbitration agreements are drafted to ensure that they cover all the main areas. The article also proposes a model arbitration agreement which would be a good recommendation to the issue discussed in this project. However, the article does not delve into the problems which result from a poorly drafted arbitration agreement. This is a major area that is covered in this thesis.

International Commercial Arbitration and Conciliation in UNCITRAL Model Law Jurisdictions;¹⁸ this book discusses arbitration generally. It offers a good insight on the general topic although its main focus is not on the Arbitration agreement which is the focus of this thesis.

¹⁶ Amazu. A (2001) *International Commercial Arbitration and African States*¹⁶, London, Cambridge University Press

¹⁷ Ball Markham (1993) 'Just Do It- Drafting the Arbitration Clause in an International Agreement' Journal of International Arbitration at page 29

¹⁸ Binder Peter, (2005); *International Commercial Arbitration and Conciliation in UNCITRAL Model Law Jurisdictions*; 2nd Edition, Sweet & Maxwell

*International Commercial Arbitration; Commentary and Materials;*¹⁹ the book provides analysis of cases on different aspects of the arbitration including the arbitration agreement. To this extent it is useful especially in providing for practical examples of cases in which the arbitration agreement were improperly drafted. However, as the book focuses on cases only, it is limited in providing the information on arbitration agreement and the effect of the poorly drafted arbitration agreements on the arbitral process which is the central theme of this thesis.

*Effective Dispute Resolution for the International Commercial Lawyer;*²⁰ the book is written in the context of the American jurisdiction examining the evolution of arbitration there with the main focus being the principle of reciprocity. It is noteworthy that Kenya is a signatory to the New York Convention on recognition and enforcement of foreign arbitral Agreements and Awards which does not require reciprocity as argued in the book. In any case, the book does not dwell on the arbitration agreement which is the central theme in this thesis.

*International Arbitration: A Hand Book;*²¹ the book deals with matters of arbitration generally from its history, the importance of the arbitration agreement, appointment of arbitrators, their function up to the entire arbitral process. It does not however focus on the issue of the arbitration agreement which is the focus of this thesis.

*International Chamber of Commerce Arbitration;*²² the book discusses the process of resolution of disputes under the International Chamber of Commerce (ICC) which is an arbitral institution. It emphasizes that the arbitration under the ICC must be premised upon a valid arbitration agreement which is scrutinized by ICC however it does not

¹⁹ Born Gary, (2001) *International Commercial Arbitration; Commentary and Materials*, Transnational Publishers New York

²⁰ Campell D & Summerfield Peter (1989) *Effective Dispute Resolution for the International Commercial Lawyer*, Boston Kluwer Law and Taxation Publishers.

²¹ Capper P. (2004) *International Arbitration: A Hand Book*, 3rd Edition LLP. London Singapore

²² Craig Laurence W., Park William W. Paulsson Jan (1985) *International Chamber of Commerce Arbitration*, Oceana Publications, Inc. New York, London, Rome

define what a valid arbitration agreement is or the effect of an improperly drafted arbitration agreement which is the main focus of this thesis.

The Law of Arbitration;²³ the book is based on the United Kingdom Arbitration Act of 1996 which is more elaborate and extensive as compared to the Kenyan Arbitration Act and to this extent it is useful in highlighting key changes in the Act that could place better emphasis on the drafting of the arbitration agreement.

Rethinking conflict of laws in international arbitration vis-à-vis Kenya's public interest;²⁴ the author of the thesis argues that the UNICITRAL Model law sought to bring harmonization of arbitration laws of different states and to give a uniform approach to conflict of laws with specific emphasis being on public interest. It does not however delve into the issue of the effect of the arbitration agreement on the arbitral process and the effect of a poorly drafted arbitration agreement on the entire process which is the main focus of this thesis.

Final Report of the Commission on International Arbitration (ICC Publication, 1997);²⁵ the article focuses on arbitration of Intellectual Property Disputes through arbitration. It however does not cover the issues addressed in this thesis.

Process of Dispute Resolution: The role of Lawyers;²⁶ this book deals with alternative dispute resolution methods and arbitration, it however does not focus on the arbitration agreement which is the focus of this thesis.

Separability-The Indestructible Arbitration Clause;²⁷ this article covers only one area in arbitration, the doctrine of separability of the arbitration agreement from the main contract. This article therefore does not address the central problem in this thesis.

²³ Gill William Henry (1965:2001) *The Law of Arbitration* 4th Edition, London, Sweet & Maxwell

²⁴ Githara William, (2006) 'rethinking conflict of laws in international arbitration vis-à-vis Kenya's public interest', unpublished LLM Thesis, University of Nairobi, Kenya

²⁵ J. Lew, *Intellectual Property Disputes and Arbitration*, Final Report of the Commission on International Arbitration (ICC Publication, 1997).

²⁶ Murray, J et al (19988) *Process of Dispute Resolution: The role of Lawyers* New York, Foundation Press

*Rusell on Arbitration*²⁸ the book deals with the United Kingdom Arbitration Act of 1996, it does not however focus on the arbitration agreement which is the main focus in this thesis.

Bernstein's Handbook of Arbitration and Dispute Resolution Practice;²⁹ the book consists of appendices of international instruments on arbitration and Rules of internationally acclaimed arbitration bodies such as the International Chamber of Commerce. It does not indicate the consequences of poorly drafted arbitration agreements which is the focus of this thesis.

1.12 **CHAPTER BREAKDOWN**

This thesis consists of five chapters made up as follows:

CHAPTER ONE

This chapter entails the research proposal providing an introduction to the research problem, the problem statement, research objectives, hypothesis, justification and significance of the research, research questions, conceptual framework, research methodology, literature review and chapter breakdown.

CHAPTER TWO

It introduces the topic of arbitration, the process of arbitration and the need for arbitration. It also sets out the history of arbitration in Kenya and how it has evolved to-date.

²⁷ Rogers & Launders, '*Separability-The Indestructible Arbitration Clause*' (1994) 10 *Arbitration International* 71 Svernlou "What Isn't, Ain't: The Current Status of the Doctrine of Separability" (1991) 8 *Journal of International Arbitration* 37

²⁸ Sutton .D et al (2007) *Rusell on Arbitration*, London, Sweet & Maxwell

²⁹ Tackaberry John & Marriott Arthur (2003) *Bernstein's Handbook of Arbitration and Dispute Resolution Practice*, London, Sweet & Maxwell

CHAPTER THREE

It defines the arbitration agreement, it sets out the functions of the arbitration agreement and the factors to consider when drafting a proper arbitration agreement. It also considers the law both international and national and their provisions on arbitration agreements.

CHAPTER FOUR

It discusses the validity of an arbitration agreement and the consequences of an improperly drafted arbitration agreement through analysis of case law on the effects of an improperly drafted arbitration clause.

CHAPTER FIVE

Having identified the issues affecting the arbitration agreement and the impacts of arbitration agreements on the arbitral process, this chapter proposes recommendations for the problems and issues identified in the preceding chapter.

CHAPTER TWO

2.1 Introduction

Arbitration may be described in general terms as a consensual, private process for the submission of a dispute for a decision of a tribunal, comprising one or more independent third persons.³⁰

It is a means by which disputes can be definitely resolved, pursuant to the parties' agreement by independent, non-governmental decision makers.³¹ Thus arbitration can be described as the process where two or more parties, faced with a dispute which they cannot resolve for themselves, agree that some private individual will resolve it for them.

The arbitration process is a branch of the law of procedure that is based on contract rather than legal norms established by states for the creation of judicial settlement of disputes and its definition which is accepted in both common law and civil law systems is that it a mode of resolving disputes by one or more third persons who derive their powers from agreement of the parties and whose decision is binding upon them.³²

The gist of the notion of arbitration as regulated by most of the laws on arbitration is that it is conceived as a substitute for court litigation.

The resolution of disputes by peer experts suits businessmen who hope to continue doing business with each other and who seek to keep their differences "in the family." This was the reason for the businessman's general preference for the arbitral process. This was the pattern for the propagation of the now widespread belief in arbitration as a panacea for the ills of court procedural delays, uncertainties, expense and publicity.³³

³⁰ Capper (2004) *International Arbitration: A Handbook*, 3rd edition, Lovells, London.

³¹ Born (2001) *International Commercial Arbitration; Commentaries and Materials*, 2nd ed, Kluwer Law International.

³² Vries (1982) *International Commercial Arbitration: A Contractual substitute for national courts* Tulane Law Review, Volume 57

³³ *Ibid* at page 43

The origin of the concept of arbitration as a method of resolving disputes was simple³⁴:

“the practice of arbitration therefore, comes, so to speak, naturally to primitive bodies of law and after courts have been established by the state and a recourse to them has become the natural method of settling disputes, the practice continues because the parties to a dispute want to settle them with less formality and expense than is involved in a recourse to the courts.”

In its early stages of development, arbitration was viewed³⁵ as an apparently rudimentary method of settling disputes, since it consists of submitting them to ordinary individuals whose only qualification is that of being chosen by the parties.

This rudimentary nature of the arbitral process has evolved with time and the modern arbitral process has lost its early simplicity. It has become more complex, more legalistic and more institutionalized, yet in its essentials it has not changed. There is still the original element of two or more parties, faced with a dispute that they cannot resolve for themselves, agreeing that one or more private individuals will resolve it for them.³⁶

As regards definition of arbitration in the laws, it is noteworthy that the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958 (“The New York Convention”) does not provide for a definition of arbitration.

On its part the UNCITRAL Model Law on International Commercial Arbitration at **Article II** thereof defines arbitration as: “arbitration means any arbitration whether or not administered by a permanent arbitral institution.” This is not a comprehensive definition

³⁴ Redfern A & Hunter M, (1999), *Law and Practice of International Commercial Arbitration*, 3rd edition, Sweet & Maxwell, London 3

³⁵ Fouchard, Gaillard, Goldman, (1999), *On International Commercial Arbitration* (Emmanuel Gaillard and John Savage eds., Kluwer Law International

³⁶ *Supra* Note 34 at page 4

and it is inadequate and it uses the word 'arbitration' in defining the same word. The same definition has been adopted under Section 3 (1) of the Kenyan Arbitration Act.³⁷

2.2 Elements of Arbitration

There are basic elements of arbitration that sets it apart from other processes of resolution of disputes.³⁸ These are:-

2.2.1 Arbitration is a consensual process; a party cannot be compelled to arbitrate a dispute unless it has agreed to arbitration. This is usually signified by the arbitration agreement in the contract between the parties or parties may agree to arbitration after a dispute has arisen. The power to arbitrate must be derived from the consent of the parties themselves and not from some external force.³⁹ Thus

³⁷ Act No. 4 of 1995. The main focus has been the definition of domestic and international arbitration. Under the Act, an arbitration is domestic if the arbitration agreement provides expressly or by implication for arbitration in Kenya; and at the time when the proceedings are commenced or the arbitration is entered into:-

- a) The parties are nationals of Kenya or are habitually resident in Kenya;
- b) In the case of a body corporate, that body is incorporated in or its central management and control is exercised in Kenya; or
- c) The place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject matter of the dispute is most closely connected is Kenya.

An arbitration is international if:-

- a) The parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different states;
- b) One of the following places is situated outside the state in which the parties have their places of business:
 - a. The place of arbitration if determined, or pursuant to, the arbitration agreement, or
 - b. Any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject matter of the dispute is most closely connected
- c) The parties have expressly agreed that the subject matter of the arbitration agreement relates to more than one state.

³⁸ Section 1 of the English Arbitration Act (1996) provides that the general principles of arbitration are:-

- a) The object of arbitration is to obtain the fair resolution of disputes by an impartial tribunal without unnecessary delay or expense;
- b) The parties should be free to agree how their disputes are resolved, subject only to such safeguards as are necessary in the public interest;
- c) In matters governed under this part of the Act, the court should not intervene except as provided.

³⁹ In the case of *Dallal –vs- Bank Mellat (1986) QB 441* it was held that the Iranian claims tribunal was not private law arbitration because its competence to rule on claims derived from international treaty and not from the will of the parties. In every other aspect it resembled arbitration but could not be recognized as such because the consent to arbitrate resulted in an agreement which was a nullity under its proper law.

arbitration is “designer justice” in the sense that parties have the freedom to decide how and in what manner their dispute will be resolved. If the parties do not agree to arbitration, they have elected to leave the resolution of any dispute that may arise unless they agree otherwise to litigation.⁴⁰

2.2.2 Arbitration is private and under many systems of the law, it is a confidential⁴¹ process in relation to the submissions, evidentiary hearings and final awards. This protects business and commercial confidences and can facilitate settlement by reducing opportunities and incentives for public posturing.⁴² In the English case of *Hassneh Insurance –vs- Mew*⁴³ Justice Colman held as follows:

“If the parties to an English contract refer their dispute to arbitration they are entitled to assume at the least that the hearing will be conducted in private. That assumption arises from a practice which has been universal in London for hundreds of years and is I believe undisputed. It is a practice which represents an important advantage of arbitration over the courts as a means of dispute resolution. The informality attaching to a hearing held in private and the candor to which it may give rise is an essential ingredient of arbitration.....if the hearing itself is private and confidential, then it would seem logical to regard documents created for the purpose of that hearing such as witness statements, experts’ reports and so on as equally private and confidential. It would also seem logical to extend the same description to a note or transcript of what took place at the hearing. To do otherwise

⁴⁰ International Arbitration: The Fundamentals, Washington Publications (June 2005)

⁴¹ The American Arbitration Association (AAA) also provides for “privacy of the hearing” Article 24 of the AAA provides as follows:-

“The Arbitrator shall maintain the privacy of the hearings unless the law provides for the contrary...the Arbitrator shall have the power to require the exclusion of any witness other than a party or other essential person during the testimony of any other witness”

⁴² See for example Article 6 of Appendix 1 of the Statute of the International Court of Arbitration of the ICC which provides that the work of the Court is of a confidential nature which must be respected by everyone who participates in that work whatever the capacity. The Court lays down the rules regarding the persons who can attend the meetings of the Court and its Committees and who are entitled to have access to the materials submitted to the Court and its Secretariat. See also Article 19 (4) the London Court of International Arbitration (LCIA) provides that all meetings and hearings shall be in private unless the parties agree otherwise in writing or the tribunal directs otherwise.

⁴³ (1993) 2 Lloyd’s Rep 243

‘would be almost equivalent to opening the door of the arbitration room to a third party’

In the case of *Dolling-Baker –vs- Merrett*⁴⁴ Lord Justice Parker held as follows:

“as between parties to an arbitration, although the proceedings are consensual and may thus be wholly voluntary, their very nature is such that there must in my judgment be some implied obligation on both parties not to disclose or use for any other purpose any documents prepared for and used in the arbitration, or disclosed or produced in the course of the arbitration, or transcripts of notes of the evidence in the arbitration or the award-an indeed not to disclose in any other way what evidence had been given by any witness in the arbitration save with the consent of the other party or pursuant to an order or leave of the court. That qualification is necessary just as it is in the case of the implied obligation of secrecy between banker and customer.”

There are however circumstances in which confidential documents have to be disclosed, for example where disclosure is ordered by the court. For example in the case of *Esso/BHP –vs- Plowman*⁴⁵ in which the claimants sought an increase in the price of natural gas which they were supplying to two Australian public utilities. The utilities refused to pay and the dispute was referred to arbitration. The Australian Minister for Energy and Minerals then brought a court action against the parties to the arbitration and sought a declaration that any and all information disclosed in the arbitration was not subject to any obligation of confidence. It was held that any obligation of confidentiality was subject to the public’s legitimate interest about the affairs of public authorities and that even if the parties had expressly agreed that everything that occurred in the arbitration would be confidential, the Minister would be entitled to the information he sought, for clearly the parties could not by private agreement displace a duty imposed by statute.

⁴⁴ (1990) 1 WLR 1205

⁴⁵ (1995) CLR 10

2.2.3 Arbitrations are resolved by non-governmental decision makers since the Arbitrators do not act as state judges or government agents, but are private persons ordinarily selected by the parties. These non-governmental decision makers are appointed as a result of the agreement between the parties and they must act impartially and fairly.

2.2.4 Arbitration produces a binding award which is capable of enforcement through national courts. This is unlike mediation and conciliation whose recommendations are non-binding and which are generally not enforceable. The essence of a submission to arbitration is that it comprises a contract to honour the decision of the Arbitrator, and a mandate to the Arbitrator to make a binding determination of the legal rights of the parties. The converse proposition is also true, a procedure which is not intended to result in a decision, or which is intended to yield an opinion, or a recommendation as to future action or a summary of the facts relevant to a disputed issue, are not arbitrations.⁴⁶

In arbitration, the parties have the power and the freedom to:

- 2.2.4.1 Select the tribunal (or agree the method of selection) and can therefore appoint a tribunal with the qualifications and experience to decide the dispute;
- 2.2.4.2 Choose the rules that will apply to the proceedings
- 2.2.4.3 Choose the language of the arbitration
- 2.2.4.4 Choose the place or sit of arbitration

In arbitration, the procedures are less formal and rigid than in litigation and as a result, the parties have greater freedom to agree on neutral and appropriate procedural rules, set realistic timetables, select technical experts and involve corporate management in dispute resolution. The cooperative elements can sometimes help foster a climate conducive to settlement.

⁴⁶ Mustill & Boyd, (1989) Commercial Arbitration, 2nd edn, Butterworths, London

2.3 Significant Features of Arbitration

There are five significant features of the process of arbitration. These are:-

- a) The agreement to arbitrate;
- b) Existence of a dispute;
- c) The choice of arbitrators;
- d) The decision of the arbitral tribunal;
- e) The enforcement of the award

An agreement by the parties to submit to arbitration any disputes or differences between them are the foundation of arbitration.⁴⁷ An arbitration agreement may be spelt out in the main contract as an arbitration clause or it may be set down in a separate submission to arbitration. The main requirement is that the agreement must be in writing.

Another element of arbitration is that there must be a dispute. Thus where one party claims to have an “open and shut” case, to which there is no defence, then the matter cannot go to arbitration. For example; a party who is faced with an unpaid cheque or Bill of Exchange may take the view that there cannot be any genuine dispute about liability and that if legal action has to be taken, they are entitled to go to court for summary judgment. This is also the case where there is an undisputed claim.

Arbitration clauses usually define the jurisdiction in terms of “disputes” and “differences” and existence of a dispute or difference is a condition precedent to the right to arbitrate.

As regards the choice of arbitrators, parties are free to choose their own tribunal although they may delegate this to another third party such as an arbitral institution or the chairperson of a certain professional body. The choice of arbitrators must be a deliberate and conscious decision by the parties since the choice of the persons who compose the arbitral tribunal is

⁴⁷ Supra Note 34 at page 75

vital and often the most decisive step in an arbitration. It has rightly been said that arbitration is only as good as the arbitrator.⁴⁸

As such choosing the right arbitrator for a particular dispute is a matter of great importance. One or more of the arbitrators may be chosen for their special skill and expertise in commercial law, intellectual property, civil engineering or any other relevant field. An experienced arbitral tribunal of this kind would be able to grasp quickly the salient features of fact or law in dispute, and thus offer them the prospects of a sensible award.

As regards the decision of the arbitral tribunal, the task of the arbitral tribunal is to resolve the dispute for the parties by making a decision in the form of a written award. The power to make a binding award is fundamental though the procedure to be adopted in arriving at a binding award may vary depending on the procedure adopted by the parties. For example, parties may in the course of the arbitral proceedings reach a settlement in which case an arbitral tribunal shall record the settlement in the form of an arbitral award on agreed terms.

Once an arbitral tribunal makes the award, it would have fulfilled its mandate and it becomes *functus officio*. However if the award is not carried out voluntarily, it is enforced by legal proceedings in the national courts. In this regard, international, regional and national arbitration laws are important in providing a guideline as to the process of recognition and enforcement of arbitral awards or the mechanism for challenging an award. The most important of these international instruments is the New York Convention which sets out the procedure to be followed for recognition and enforcement of foreign arbitral awards and specifies the limited grounds upon which recognition and enforcement may be refused or challenged.

⁴⁸ Lalive (1989) “Melanges en l’honneur de Nicolas Valticos” Droit et justice

2.4 Advantages and Disadvantages of Arbitration

The popularity of arbitration as a means for resolving commercial disputes has increased significantly over the past several decades. This popularity reflects important advantages of arbitration as a means of resolving commercial disputes. Despite these advantages, however, there are also certain challenges or shortcomings of arbitration.

Arbitration is often perceived as ensuring a genuinely neutral decision-maker in disputes between the parties especially in international arbitration where there are parties of different nationalities. This is because international disputes inevitably involve the risk of litigation before a national court of one of the parties which may be biased, parochial, or unattractive for some other reason.⁴⁹ This is possible because some courts in some jurisdictions lack competence, experience, resources and traditions of evenhandedness satisfactorily to resolve international commercial disputes.

The other advantage of arbitration is that arbitral awards are generally more easily and reliably enforced in foreign states than foreign judgments especially because the New York Convention has abolished the problem of “*double-exequatur*”. Before the New York Convention came into force, a party seeking enforcement of an award in a foreign state, had to show that an award had become final in its country of origin, a party was obliged to seek a declaration in the courts of the country where the arbitration took place in order to show that the award was enforceable in that country before the award could be enforced in the courts of the place of enforcement. This is no longer the case.

In *Parsons & Whittemore Overseas Co. –vs-. Societe Generale de L’Industrie Du Papier (Rakta) and Bank of America*⁵⁰ the court made the following findings with respect to the New York Convention:

- (i) The Convention’s basic thrust was to liberalize procedures for enforcing foreign arbitral awards;

⁴⁹ Supra Note 34 at page 7

⁵⁰ United States Courts of Appeals, 74-1642 and 74-1676, University of Nairobi LLM 2008/2009 Materials on International Commercial Arbitration

- (ii) Unlike the **Geneva Convention of 1927** which placed the burden of proof on the party seeking enforcement and did not circumscribe the range of available defenses to those enumerated in the convention, **the New York Convention** shifted the burden of proof to the party defending against enforcement and limited his defenses to those set forth in **Article V** of the Convention;
- (iii) **The New York Convention** has a pro-enforcement bias; and
- (iv) The defence of public policy under **Article V (2)(b)** is to be narrowly construed as an expansive construction of this defence would vitiate the Convention's basic effort to remove pre-existing obstacles to enforcement. Enforcement of foreign arbitral awards may be denied on this ground only where enforcement would violate the forum state's most basic notions of morality and justice.

The other advantage of arbitration is that it tends to be procedurally less formal and less rigid than litigation in national courts. And as such, parties have greater freedom to agree on neutral and appropriate procedural rules, set realistic timetables, select technical experts and neutral decision makers.⁵¹

The other advantage of arbitration is that it is confidential which protects business and commercial confidences and which facilitates settlement by reducing incentives for public posturing.

The disadvantages of arbitration on the other hand is that it is expensive since the parties must pay the arbitrator (s) costs unlike in litigation where parties do not pay the costs of the judge.

The other disadvantage of arbitration is that an arbitral tribunal must depend for its full effectiveness upon the underlying national system of law which in most cases is limited

⁵¹ Supra Note 34 at page 9

as compared to court judges for example, penal notices to require witness attendance, or to order coercive actions.

The other disadvantage of arbitration is that arbitration is limited to the parties to the arbitration agreement and cannot include other parties. An arbitral tribunal unlike a national court has no power to order for consolidation of actions.

2.5 The Arbitration Process

The arbitration process is normally commenced with an arbitration notice by the Claimant to the Respondent containing the proper particulars of the dispute in respect of which the arbitration is being commenced.⁵² Thereafter the parties proceed to the appointment of the arbitral tribunal. There are several types of arbitral tribunals and many methods of bringing them into existence. The principal types of tribunals are:

- (i) Sole arbitrator;
- (ii) A tribunal of two arbitrators;
- (iii) A tribunal of three arbitrators
- (iv) A tribunal of more than three arbitrators
- (v) An umpire.

The various modes of appointment include:-

(i) Appointment by agreement of the parties to the dispute;

This is the most common method of appointing arbitrators, here the parties must agree upon their choice and the person chosen by the parties must accept the appointment. Such acceptance may be informal or formal. Some jurisdictions require that the acceptance must be in writing.⁵³

⁵² According to Mustill & Boyd (1989) Commercial Arbitration, the expression 'the commencement of the arbitration' must have different meanings in various contexts. For example, the giving of a notice to concur in the appointment of a sole arbitrator is sufficient to prevent time from running under the Limitation Act, and is also an essential first step towards the making of a default appointment. But the arbitration has not at this stage 'commenced' in any practical sense, since there is no person or group of persons charged with any authority to determine the matters in dispute.

⁵³ The Netherlands Arbitration Act Article 1029 (1) requires the acceptance to be in writing.

(ii) Appointment by a trade or other association;

An arbitration clause may provide that the appointment of an arbitrator is to be made by a trade association or club. For example many groups or associations of merchants and traders throughout the world, whether diamond merchants in New York or commodity traders in London prefer to resolve disputes by arbitration amongst themselves which ensures that the disputes are dealt with by experienced practitioners in the relevant trade.⁵⁴

(iii) Appointment by a professional institution;

Sometimes parties provide in the arbitration agreement that the president, chairperson or other senior official of a professional institution shall be the person who is to appoint the arbitrator, this may include for example providing that the appointment shall be made by the Chairperson for the time being of the Law Society of Kenya, or of the Institute of Certified Public Accountants of Kenya or any other such professional body.

(iv) Appointment by an Arbitral Institution;

Arbitration Institutions usually have a mechanism for the appointment of arbitrators. Such institutions include the International Chamber of Commerce (ICC), the American Arbitration Association (AAA), the London Court of International Arbitration (LCIA), the International Convention on Settlement of Investment Disputes (ICSID) and the Kenyan chapter of the Chartered Institute of Arbitrators (CIARB).

(v) Appointment by a list system;

In a list system, each party compiles a list of three or four persons they consider to be acceptable arbitrators, the list is then exchanged in an attempt to reach an agreement.

(vi) Appointment by existing arbitrators;

Where an arbitral tribunal of three arbitrators is to be constituted, the arbitration clause will normally provide that each party is to appoint one arbitrator and that the two arbitrators shall appoint the third who acts as the presiding arbitrator.

⁵⁴ Supra Note 34 at page 197

(vii) *Appointment by a National Court.*

An arbitrator (s) may be appointed by the Courts in the following circumstances:-

- i. Appointment by the Court in default of agreement- where parties cannot agree upon a choice, the Court has the power to do so.
- ii. Appointment by the Court upon revocation or removal of an arbitrator-where an existing tribunal is removed, the Court may appoint an arbitrator in place of the removed tribunal.
- iii. Appointment by the Court to fill a vacancy-if a sole arbitrator refuses to act, is incapable of acting or if he dies and the parties do not agree on another arbitrator, then the Court will appoint the arbitrator.

After the appointment of the arbitral tribunal, the tribunal will proceed in accordance with the agreement of the parties and there is no uniform procedure of conducting the arbitration. Some Institutional Rules of arbitration such as those of the ICC provide a procedure such as the time frame within which each party may present its claim or defence, the conduct of the proceedings and the time limits for publication of the Award.

The parties generally have the autonomy to decide how the arbitration is to be conducted. They may agree also on the type of arbitration such as whether it shall be a documents only arbitration, one requiring a reasoned award or one with witnesses' statements that would be regarded as the evidence in chief and thereby save on time. Ultimately it is upon the parties and the tribunal to decide on the procedure to be followed.

2.6 History and Development of Arbitration in Kenya

In Kenya, the history of arbitration originates from English law. Under the English law, there was the influence continually imposed on voluntary arbitration by the existence of the parallel system of arbitration pursuant to an order of the court. In this procedure, the

reference to arbitration sprang from an action in court.⁵⁵The court therefore retained throughout the reference those inherent powers of control and sanction which it possessed in relation to its own proceedings. With time, arbitration became recognized as a separate mode of resolution of disputes other than by courts. The English Arbitration Act of 1950, then consolidated the Arbitration Acts of 1889 and 1934 and increased the scope of jurisdiction of Arbitrators with instances of court intervention being reduced although the court continued to retain a lot of powers with regard to arbitration.

The Kenyan Arbitration Act⁵⁶ was a replica of the English Arbitration Act of 1950. This Act was then repealed and replaced by the Arbitration Act (1995) Act No. 4 of 1995. This statute commenced on the 2nd of January 1996 by virtue of Legal Notice No. 394 of 1995.

The current Arbitration Act is based on the Model of the United Nations Commission on International Trade Law (UNCITRAL) which was adopted in 1985 with a view to encouraging arbitration and processes that would have global recognition. The United Nations came up with a model of a statute that has been adopted by many countries. The essence of the Act is that it provides for very broad party autonomy in fashioning the arbitration process. This means that parties who enter into an arbitration agreement are to a large extent at liberty to determine the process of adjudication of the disputes that will go to arbitration. Autonomy, for example in deciding who the arbitrator will be, the venue of arbitration, the substantive law that will apply to that agreement or arbitration. Once a dispute has arisen, they also have autonomy with regards to how the arbitral process itself will be conducted.

⁵⁵ Mustill & Boyd (1989) Commercial Arbitration, Butterworths, London

⁵⁶ Chapter 49 of the Laws of Kenya

2.7 Conclusion

Since its evolution, arbitration as a means of settling disputes between parties has considerably gained momentum and its advantages far outweigh its disadvantages. As the parties are offered the option to choose for themselves beforehand, or upon the occurrence of a dispute, by whom the dispute is to be resolved, where, the language and the procedure, they have a greater comfort as compared to leaving the resolution of the dispute to state machinery through the judicial system.

CHAPTER THREE

Introduction

Since arbitration is based upon a valid arbitration agreement it is important to understand what an arbitration agreement is, what it entails, its functions and importance. This chapter will focus on the arbitration agreement and will examine the meaning of an arbitration agreement and the functions of an arbitration agreement.

3.1 Definition of Arbitration Agreement

Section 3 of the Arbitration Act No. 4 of 1995 defines an arbitration agreement as:

“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”

Bernstein and Wood⁵⁷ have also defined “arbitration agreement” succinctly without including the word “arbitration” in the definition:

“Where two or more persons agree that a dispute or potential dispute between them shall be decided in a legally binding way by one or more impartial persons in a judicial manner, that is upon evidence put before him or them, the agreement is called an arbitration agreement or a submission to arbitration”.

An arbitration agreement therefore is a consensus between parties to have current or future disputes between them determined by a person other than the court.

Thus it can be said that an arbitration agreement covers both (i) an arbitration clause in a contract by which the parties agree that disputes between them in the future arising out of the contract will be referred to arbitration and (ii) a separate agreement not forming part

⁵⁷ Ronald Bernstein & Adam Wood, *Handbook on Arbitration Practice* (2nd Edition, Sweet & Maxwell in conjunction with The Chartered Institute of Arbitrators) 9

of another contract to refer an existing dispute to arbitration. In some jurisdictions, this separate agreement is known as a ‘submission agreement’⁵⁸ or an ‘ad hoc agreement’⁵⁹

A clause qualifies as an arbitration agreement even though it does not provide for immediate reference to arbitration following the emergence of a dispute. In the case of *Channel Tunnel Group Limited –vs- Balfour Beatty Construction Limited*⁶⁰ in which the relevant clause provided that, in the event of a dispute between the employer and the contractor, the matter was to be referred in the first instance to a panel of three independent experts who were specifically stated to be acting as experts and not arbitrators. There was however, an appeal from the panel’s decision to three arbitrators appointed under the ICC Rules. The House of Lords held that this type of clause constituted an arbitration agreement within the meaning of the Act.

3.2 Implied Arbitration Agreements

Although the Arbitration Act clearly states that an arbitration agreement must be in writing, an agreement to refer disputes to arbitration may be implied from the conduct of the parties. In the case of *Athletic Union of Constantinople –vs- National Basketball Association*⁶¹ in which a claimant argued that it had not entered into an agreement to arbitrate. The court considered that, whether the claimant had entered into an arbitration agreement or not, would depend upon ‘whether a reasonable person, knowing the relevant background and observing matters in the place of the claimants would conclude from the respondents’ conduct that the respondents were agreeing to participate in the proposed arbitration. In this case, the court concluded that a reasonable person would have so concluded and as such an arbitration agreement was inferred from the conduct of the parties.

⁵⁸ See for example Article 7.1 of the Uncitral Model Law

⁵⁹ The term ‘ad hoc arbitration’ and ‘ad hoc agreement’ were defined in the case of *LG Caltex Gas Company Limited –vs- China National Petroleum Corporation* (2001) 1 WLR 1892 in which the Court of Appeal held that the expression ‘ad hoc arbitration’ and ‘ad hoc submission’ are used in two different senses. Firstly, it is used to describe an agreement to refer an existing dispute and secondly it is used to mean an agreement to refer either future or existing disputes to arbitration without an arbitration institution being specified to administer the proceedings, or at least to supply the procedural rules for the arbitration.

⁶⁰ *Channel Tunnel Group Limited –vs- Balfour Beatty Construction Limited* (1993) 1 ALL E.R 664

⁶¹ *Athletic Union of Constantinople –vs- National Basketball Association* (2002) 1 All E.R 70

3.3 Survival of the Arbitration Agreement upon Termination of the Underlying Contract

An arbitration agreement specifies the means whereby some or all the disputes under the contract in which it is contained are to be resolved. It is however both separate and different from the contract in which it is contained. An arbitration agreement in a commercial contract is ‘an agreement inside an agreement.’ The parties make their commercial bargain but in addition agree on a private tribunal to resolve any issues that may arise between them.⁶²

The question then arises as to what happens to the arbitration agreement in the event that the underlying contract is brought to an end, for example on account of breach by one party. It would be an absurdity if the arbitration agreement were also to be held to come to an end since the agreement by the parties is that the arbitration agreement is meant to provide the means by which disputes about the contract, including the existence and consequences of breach would be determined.

Accordingly, the arbitration agreement is treated as a separate and independent agreement which survives the termination of the underlying contract.⁶³

3.4 Functions of the Arbitration Agreement

The foremost importance of the arbitration agreement is that there can be no arbitration proceedings without an arbitration agreement. Parties must consent to arbitration before they can be subject thereto.

⁶² Sutton and Gill; Russell on Arbitration, 22nd edition, Sweet and Maxwell (2003), 29

⁶³ For example, Section 7 of the English Arbitration Act, 1996 which provides as follows:-
“unless otherwise agreed by the parties, an arbitration agreement which forms or was intended to form part of another agreement (whether or not in writing) shall not be regarded as invalid, non-existent or ineffective because that other agreement is invalid, or did not come into existence or has become ineffective and it shall for that purpose be treated as a distinct agreement.

The foundational importance of the existence of the arbitration agreement was outlined in *Fairacres Development Ltd –vs- Margaret Apondi*,⁶⁴ where the court held that:

“It is trite law that arbitration clauses apply only where there is a dispute between the parties, on a matter covered in the agreement and by the arbitration clause. But all these pre-suppose such a dispute arising during the subsistence of the agreement...there must be a dispute and there cannot be a dispute if there is no contract within which the arbitral clause is but a part and parcel of.” (Emphasis provided)

The need for consensus of parties in pursuing arbitral proceedings was also underscored in the case of *Wasike –vs- Swala*,⁶⁵ Hancox JA stated that:

“Even in the case of an arbitration clause in an agreement, bilateral rights of reference by both parties must be given, otherwise the clause is invalid...”

The arbitration agreement functions to allow parties to agree on various matters in relation to the disputes that may arise between them, including the disputes to submit to arbitration, place of arbitration, number of arbitrators, qualifications of arbitrators and so forth.

The Court has residual and original power to resolve civil disputes in Kenya and this is the case in most states. Any attempt to oust the jurisdiction of the court must be done within the precincts of the law.

Arbitration provides for a means for parties to resolve their disputes outside the forum of the court but still have the procedures and awards of arbitration be backed by the law and enforced by courts.⁶⁶

⁶⁴ *Fairacres Development Ltd –vs- Margaret Apondi Olotch t/a M.A. Kiosk* [2005] eKLR

⁶⁵ Nakuru Civil Appeal No. 6 of 1983, (Hancox, Nyarangi JJA & Platt Ag JA)

⁶⁶ Sir Michael J. Mostill and Stewart C. Boyd, *Commercial Arbitration* (2nd Edition, Butterworths, London Edinburgh, 1989) argue that a modern state must in some way provide backing to arbitration to make it an effective dispute resolution mechanism and at page 4 they state that, “*Arbitration is an important part of commercial life, and any legal system must in some degree be concerned with it.*”

Arbitration has certain specific advantages that parties resorting thereto would like to take advantage of rather than going to court or going to a dispute resolution mechanism whose award cannot be enforced by the court.

For parties to utilize the process of arbitration however, they must agree to do so in order to escape the net of Section 10 of the Act which ousts the jurisdiction of the court in matters governed by the Arbitration Act. The Section provides that:

“Except as provided in this Act, no court shall intervene in matters governed by this Act.”

For parties to be governed by the Arbitration Act therefore, they must have an arbitration agreement. The arbitration clause also functions to commit the parties to resolve their disputes by arbitration, even if the contract has come to an end.⁶⁷

Another function of the arbitration agreement is to allow parties to “design justice”. The arbitration agreement is the set of tools by which parties can design justice.

The Arbitration Act allows parties to determine many aspects of the dispute resolution mechanism availed by arbitration.⁶⁸ In most of the provisions in the Act, there are oft repeated phrases for instance: “*unless otherwise agreed by the parties ...*”,⁶⁹ “*except as otherwise agreed by the parties...*”,⁷⁰ “*parties are free to agree....*”⁷¹ The words themselves give the feeling that parties are first given liberty to determine the matter for themselves before the default provision of the Act can come into play.

⁶⁷ Ian Archibald (Barrister), International Commercial Arbitration – A Roadmap (Drafting the Midnight Clause) Australian Law Society Journal, September 2002, Volume 40 No. 8 page 74

⁶⁹ Section 26

⁷⁰ Section 24 (3)

⁷¹ Section 23 (1)

It is by an arbitration agreement that parties can exercise this freedom that is theirs to determine almost every aspect of the resolution of any present or future dispute between them.

Markham Ball⁷² shows the foundational importance and effect of agreement and autonomy of parties to arbitration in the following words:

“The principle of party autonomy is the foundation of arbitration...The parties’ decisions will shape the style, length, complexity, fairness and cost of their dispute resolution proceedings, and will largely determine whether the proceedings ultimately produce a final, enforceable solution.”

This quote appropriately displays the broad influence that parties have on the arbitration process and if the parties properly exercise their autonomy, they can use this influence to design a dispute resolution procedure that is useful and suitable to their circumstances. The Arbitration Act stipulates the matters concerning which parties may agree in an arbitration agreement.

3.5 Effect of death of a Contracting Party to an Arbitration Agreement

At common law, the death of a party to an arbitration agreement had the effect of discharging the arbitration agreement and also the cause of action to which the agreement related.⁷³

However, this position has now changed. Section 8 of the Arbitration Act provides that the death of a party does not discharge the arbitration agreement or the proceedings under

⁷² Markham Ball, Just Do It – Drafting the Arbitration Clause in an International Agreement, Off-prints of the Journal of International Arbitration, Geneva, December 1993, Vol. 10 No. 4 at 29 See also Kariuki Muigua, Preliminary Proceedings and Interlocutories: The Birth, Teething, Immunization and Weaning of Arbitration Proceedings, unpublished, Chartered Institute of Arbitrators (Kenya Branch) teaching materials (2008) at page 17 where he states that, “importantly, party’s autonomy” permits parties to agree on any matter.”

⁷³ Robert Merkin, Arbitration Law (2004) LLP at page 87

the arbitration agreement. The rights and liabilities of the deceased party are passed on to that party's personal representatives or assigns.⁷⁴

Accordingly, on the death of a person, any cause of action which survives his/her death and which vests in his/her personal representatives may be referred to arbitration by them even in the absence of an arbitration agreement in the original agreement.

3.6 Effect of Bankruptcy of a Contracting Party on existing Arbitration Agreement

The bankruptcy of a person who had earlier entered into an arbitration agreement does not have an automatic discharging effect upon the contract to which the arbitration agreement relates or upon the arbitration agreement itself.⁷⁵

⁷⁴ Section 8 of the Arbitration Act provides as follows:-

- 8 (1) An arbitration agreement is not discharged by the death of any party thereto, either as respects the deceased or any other party, but in such event is enforceable by or against the personal representative of the deceased.
- 8 (2) The authority of an arbitrator is not revoked by the death of any party by whom he was appointed.
- 8 (3) Nothing in this section affects the operation of any law by virtue of which any right of action is extinguished by the death of a person.

⁷⁵ Section 38 of the Arbitration Act provides as follows relating to bankruptcy of a party:-

- 38 (1) Where it is provided by a term in a contract to which a bankrupt is a party that any differences arising out of or in connection with the contract shall be referred to arbitration, then if the trustee in bankruptcy adopts the contract, that term is enforceable by or against him so far as relates to those differences.
- 38 (2) Where a person who has been adjudged bankrupt had, before the commencement of the bankruptcy, becomes a party to an arbitration agreement, and any matter to which the agreement applies requires to be determined in connection with or for the purposes of the bankruptcy proceedings, then if the case is one to which subsection (1) does not apply:-
 - (a) any other party to the agreement or, with the consent of the committee of inspection, the trustee in bankruptcy may apply to the court having jurisdiction in the bankruptcy proceedings for an order directing that the matter in question shall be referred to arbitration in accordance with the agreement; and
 - (b) the court, if it is of the opinion that, having regard to all the circumstances of the case, the matter ought to be determined by arbitration, may make an order accordingly.
- 38 (3) This section shall apply in domestic arbitration or if the bankrupt person is a Kenyan or if the law of Kenya is applicable according to the rule of conflict of laws.

However, the power of the trustee to proceed with the arbitral proceedings or to commence the arbitration proceedings pursuant to the arbitration agreement is only limited to domestic arbitration and Section 38 of the Act does not apply to International Arbitrations.

However, it should be noted that Section 38 of the Act does not apply where the arbitration agreement is made after the bankruptcy of the party in question. Once the bankruptcy proceedings have commenced, the bankrupt's property are frozen as far as the bankrupt is concerned and he has no power to make agreements affecting it; by contrast, the trustee in the bankruptcy may, with the leave of the court or the creditors' committee enter into an arbitration agreement concerning outstanding claims against the bankrupt.

Further where proceedings on a bankruptcy petition are pending, or where a bankruptcy order has been made, the court is entitled to stay any outstanding proceedings against the bankrupt, including arbitration proceedings.

3.7 Assignment of Arbitration Agreements

Under the common law, it was considered that the provisions of arbitration of an assignable contract were not themselves assignable, as an arbitration agreement was considered to be a personal covenant. In the case of *Cottage Club Estates Limited –vs- Woodside Estates Company Limited*⁷⁶; in which the assignee sought to set aside an arbitration award against a third party in favour of the assignor on the basis that following the assignment the arbitrator had no jurisdiction to make an award. The court held that following the assignment, the assignor no longer had a cause of action to be referred to arbitration. However, it was subsequently determined in the case of *Shayler –vs- Woolf*⁷⁷ that the presence of an arbitration agreement in a contract which is by its nature assignable will not prevent assignment of the entire contract, including its arbitration provisions as an arbitration agreement is by its nature assignable.

⁷⁶ *Cottage Club Estates Limited-vs- Woodside Estates Company Limited* (1928) 2 KB 463

⁷⁷ *Shayler –vs- Woolf* (1946) Ch 320

Conclusion

An arbitration agreement is a contractual clause evidencing agreement to refer disputes to arbitration. The nature and function of the arbitration agreement can thus not be understated as it is the cornerstone and foundation of arbitration.

CHAPTER FOUR

4.1 Introduction

Having considered the function and importance of the arbitration agreement in the preceding chapter, this chapter will now consider issues concerning validity of the arbitration agreement. This will be considered in several ways; the form of the arbitration agreement, construction and scope of the arbitration agreement.

Validity of the arbitration agreement.

As arbitration is premised and rooted upon an arbitration agreement, an arbitration agreement must in all effect be valid. The effect of an invalid arbitration agreement would most likely either result in the parties failing to go to arbitration or the setting aside of an award premised on the invalid agreement.

The arbitration agreement in a commercial contract is often a ‘midnight clause’. It is the last clause in the contract to be considered, sometimes late at night or in the early hours of the morning, after long negotiations. Insufficient thought is given as to how disputes are to be resolved (possibly because the parties are reluctant to contemplate falling into disputes) and an inappropriate and unwieldy compromise is often adopted. If a dispute arises, and arbitration proceedings begin, these matters must be dealt with first before any progress can be made with the real dispute or issue. It is thus paramount that proper care be given when drafting the arbitration agreement to avoid such issues.⁷⁸

4.2 Requirement as to form of arbitration agreement

An arbitration agreement that provides for international commercial arbitration must take into account the international requirements of a valid agreement as set out in the Conventions or Treaties on arbitration. If it fails to do so, the arbitration agreement and any award made thereunder would not qualify for international recognition and enforcement.⁷⁹

⁷⁸ Supra Note 34 at page 136

⁷⁹ Wetter (1990), The present status of the International Court of Arbitration of the ICC: an Appraisal, Vol 1, *American Review of International Arbitration* 91 at page 93

The New York Convention sets out the formal requirements for a valid agreement under Article II which provides that each contracting state undertakes to recognize and give effect to an arbitration agreement when the following requirements are fulfilled:-

- (i) The agreement is in writing;
- (ii) It deals with existing or future disputes;
- (iii) The disputes arise in respect of a defined legal relationship, whether contractual or not; and
- (iv) They concern a subject matter capable of settlement by arbitration.

These are the four positive requirements of a valid arbitration agreement.⁸⁰ The New York Convention further provides for other requirements for a valid arbitration agreement at Article V.I (a)⁸¹. Under this provision, recognition and enforcement of an award may be refused if the party requesting the refusal is able to prove that the arbitration agreement was invalid under the applicable law and as such:

- (i) The parties to the arbitration agreement must have the legal capacity under the applicable law;
- (ii) The arbitration agreement must be valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made.

⁸⁰ Ibid at page 93

⁸¹ Article V.I New York Convention: “Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that: (a) the parties to the agreement referred to in Article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected or, failing any indication thereon, under the law of the country where the award was made.

4.2.1 **Requirement that the arbitration agreement be in writing**

The requirement that the arbitration agreement be in writing is found in all international conventions on arbitration, and most national laws, for example the Kenyan and English Acts.⁸²

The rationale for this imposition is because a valid arbitration agreement⁸³ excludes the jurisdiction of national courts and means that any dispute between the parties be resolved by a private method of dispute resolution.⁸⁴

The jurisdiction of an arbitral tribunal is usually considered from the perspective of whether or not the arbitral tribunal has any jurisdiction at all. An arbitral tribunal will lack jurisdiction altogether if there is no enforceable arbitration agreement.

Although there is a requirement that the arbitration agreement be in writing, it is not necessary that the agreement be in a formal document, nor is it necessary that the agreement should be signed by both parties. It is sufficient that the agreement has been orally accepted by the parties or that one has signed and the other has accepted.⁸⁵

⁸² Section 4 (1) Kenyan Arbitration Act and Section 5 (1) English Arbitration Act

⁸³ In the Kenyan case of *Kenya Amateur Athletics Association –vs- Keter*, (1983) LLR 163 where the applicants had applied for stay of proceedings in the High Court after a suit by the Respondent on the grounds that there was an arbitration agreement between the parties and that the matter be referred to arbitration. The application had been dismissed whereupon the Applicant filed an appeal. It was held that there was no arbitration agreement in writing and that the clause which the applicants relied upon which was a clause in a constitution was contrary to the principles of natural justice as it made the applicant both the prosecutor and the judge of the proceedings. The applicants' appeal was thus dismissed.

⁸⁴ *Supra* Note 34 at page 141

⁸⁵ *Union of India vs- Ralli Ram* (1964) 3 SCR, 164 in which it was held that the only requirement is that the agreement be in writing and not on the signature of the parties. A similar view was held in *Jupitar Chit Fund P. Ltd –vs- Dwarka Dinesh Dayal*, (1981) ALL ER 251 in which it was held that the agreement may be in the form of a signed document by one party consisting of the terms and plain acceptance either signed or orally accepted by the other party or an unsigned document consisting of the terms of submission to arbitration agreed orally by both parties. In *Ram Chandra Ram Nag Ram Rice & Oil Mills Ltd –vs- Howarah Oil Mills Ltd* (1958) AIR, 620 the court emphasized that the conduct of the parties is also relevant in determining as to whether both parties agreed to refer the dispute to arbitration.

It is also noteworthy that there is no requirement that the arbitration agreement must be in a prescribed format. In the Indian case of *Rukmanibai Gupta –vs- Collector, Jabalpur*⁸⁶ the Supreme Court held that an arbitration clause is not required to be stated in any particular form. If the intention of the parties to refer the dispute to arbitration can be clearly ascertained from the terms of the agreement, it is immaterial whether or not the expression ‘arbitration’ or ‘arbitrator’ has been used. Nor is it necessary that it should be contained in the same contract document.

4.2.2 **Requirement on existence of a “dispute”**

As regards existing or future disputes it is noteworthy that if the agreement between the parties is in effect an agreement to prevent disputes from arising and not an agreement as to how they are to be settled, then it is not an agreement to arbitrate.⁸⁷ In the case of *Chambers –vs- Goldthorpe*⁸⁸ Smith M.R held as follows:-

“it was argued that there was no dispute between the parties prior to the plaintiff giving his certificate, and that unless there was a dispute the plaintiff could not be in a position of an arbitrator. I do not see why there should not be an arbitration to settle matters, as to which, even if there was no actual dispute, there would probably be a dispute unless they were so settled.”

4.2.3 **Defined Legal relationship**

As regards the requirement that a dispute should arise from a defined legal relationship whether contractual or not, it should be noted that almost all international commercial arbitrations arise out of a contractual relationship between the parties. The dispute submitted to arbitration may be governed by

⁸⁶ (1980) 4 SCC 556

⁸⁷ *Re Carus-Wilson & Greene* (1886) 18 QBD 7

⁸⁸ (1901) 1 KB 624 page 635

principles of delictual or tortious liability rather than by the law of contract.⁸⁹ In the case of *Kaverit Steel & Crane Ltd-vs- Kone Corporation*⁹⁰ in which the plaintiff commenced court proceedings alleging that the defendant had breached certain licence distribution agreements. The defendant sought a stay of proceedings and a reference to arbitration pursuant to an arbitration clause in the agreement. The clause stated that all disputes “arising out of or in connection with this contract” would be referred to arbitration. The court refused to grant the stay on grounds that some of the claims by the Plaintiff contained allegations that went beyond breach of contract such as conspiracy and inducing breach of contract which were tort-based claims not covered by the scope of the arbitration clause. However on appeal, it was held that the wording of the arbitration clause was wide enough to bring within its scope any claim that relied on the existence of a contractual relationship, even if the claim itself was a claim in tort. The court held that:-

“a dispute ‘arises out of or in connection with a contract’ if the ‘existence of the contract is germane either to the claim or the defence.”

In the English case of *Ashville Investments Ltd-vs- Elmer Contractors*⁹¹ an arbitration clause which referred to ‘any matter or thing of whatsoever nature arising thereunder or in connection therewith’ was sufficiently wide to cover claims based on alleged mistake and misrepresentation.⁹²

Thus, subject to any provisions of the relevant applicable law, the terms of an arbitrator’s jurisdiction and powers in any particular case depends on a proper construction of the arbitration agreement. The arbitral tribunal must consider the dispute in question and then elicit from the arbitration agreement whether or not

⁸⁹ Supra Note 9 at page 140

⁹⁰ (1994), Vol. XVII Yearbook Commercial Arbitration, 346

⁹¹ (1988) Lloyds Rep. 73

⁹² In *Ethiopian Oilseeds and Pulses Export Corp –vs- Rio del Mar Foods Inc. (1990) 1 Lloyds Rep 86* the words ‘arising out of’ were held to cover disputes concerning rectification. However, in the case of *Fillite (Runcorn) Ltd-vs- Agun-lift (a firm) 45 BLR 27* it was held that disputes arising under a contract were not wide enough to include disputes as to misrepresentation or negligent misstatements since it referred exclusively to obligations created by or incorporated into that contract.

the parties intended a dispute of the kind in question to be resolved by arbitration.⁹³

4.2.4 **Subject matter capable of settlement by arbitration**⁹⁴

As regards the requirement that the subject matter be capable of settlement by arbitration, an arbitration agreement in respect of disputes relating to:-

- (i) Insolvency proceedings;
- (ii) Probate matters;
- (iii) Matrimonial causes;
- (iv) Criminal matters
- (v) Industrial disputes; and
- (vi) Proceedings for appointment of a guardian

would not be capable of settlement by arbitration as the law has given jurisdiction to determine such matters to specified institutions such as the court exclusive jurisdiction to hear and determine such matters. If the issue of arbitrability were to arise, one would have to have regard to the relevant laws of the different states that are or may be concerned. Whether or not a certain dispute is arbitrable or not is in essence a matter of public policy of a particular state. This may also be a matter for the Courts to decide whether a dispute is arbitrable or not.⁹⁵

⁹³ Supra Note 34 at page 140

⁹⁴ It is noteworthy that the Article VII of the UNICITRAL Model Law does not have the requirement that the subject matter of the arbitration agreement be arbitrable. The Working Committee felt that there was no need to refer to national law in this context.

⁹⁵ In the American case of *Mitsubishi Motors Corp –vs- Soler Chrysler Plymouth Inc (1985) 473 U.S 614* it was held that antitrust issues arising out of international contracts were arbitrable under the Federal Arbitration Act. This was so despite:-

- (i) The public importance of the antitrust laws;
- (ii) The significance of private parties seeking treble damages as a disincentive to violation of those laws; and
- (iii) The complexity of such cases

In its judgement the court held that “we conclude that concerns of international comity, respect for the capacity of foreign and transnational tribunals and sensitivity to the need of the international commercial system for predictability in the resolution of disputes require that we enforce the parties’ agreement, even assuming that a contrary result would be forthcoming in a domestic context.”

Generally most differences or disputes arising between parties and which affect their civil rights may be referred to arbitration. A dispute which affects the rights of another person other than the parties may also not be arbitrable. It is open for the parties to agree to refer any private dispute to arbitration and such agreement may be made to cover disputes which have not arisen, or which in fact may never arise. Disputes as to facts, or liability or the adjustment of monetary disputes are arbitrable.

The arbitration agreement must relate to some disputes or differences between the parties, either present or future. If disputes have actually arisen, the arbitration agreement will usually be an agreement specially relating to such disputes. It may be confined to such disputes, or may be so drawn as to cover other disputes.

The arbitration agreement must however not relate to anything which is illegal, immoral or contrary to public policy and must apply a fixed and recognizable system of law.⁹⁶

4.3 Content of arbitration agreements

The essential validity of the arbitration agreement is concerned with the substance of the arbitration agreement in determining whether the arbitration agreement is valid or not.

In this regard, the first question in considering whether or not an arbitration agreement is valid as regards substance, is whether the parties intended to refer the dispute between them to arbitration. If they did, then an arbitral tribunal or the court should strive to give effect to their agreement.⁹⁷

Thus if it appears from the terms of the agreement by which a matter is submitted to a person's decision that the intention of the parties was that he should hold an inquiry in the nature of a judicial inquiry and hear the respective cases of the parties and decide upon the evidence laid before him, then the case is one of an arbitration.⁹⁸

⁹⁶ Orion Compania Espanola –vs- Belfort (1962) 2 L.I.R 257

⁹⁷ Supra Note 16 at page 143

⁹⁸ Walton (1970) Russell on the Law of Arbitration, 18th edn Stephens & Sons Ltd, London

On the other hand there may be cases in which a person is appointed to ascertain some matter for the purposes of preventing a dispute from arising and not for settling of a dispute and in such cases, an arbitration agreement would not be envisaged by the parties. There may be cases of an intermediate kind, where, though a person is appointed to settle disputes that have arisen, still it is not intended that he shall be bound to hear evidence and arguments. In such cases, it may be difficult to say whether he is intended to be an arbitrator or to exercise some function other than that of an arbitrator. Such cases must be determined each according to its nature.⁹⁹

Difficulties may also arise where the agreement is drafted in such a way that the intention to submit to arbitration is not clear. In an ICC case¹⁰⁰ where the clause stated as follows: “this agreement remains subject to English law and that disputes be submitted to the ICC” it was not clear either from the wording or from previous exchanges between the parties, whether the intention was to refer to arbitration or to conciliation or to some other method of dispute resolution by “the ICC”; accordingly, the arbitrator to whom the file had been passed by the ICC in Paris decided that he had no jurisdiction.

Thus the arbitration agreement must clearly state the intention of the parties to avoid any ambiguity. In the Indian case of *Sankar Sealing Systems (P) Ltd –vs- Jain Motor Trading Co.*¹⁰¹ in which a clause in an agreement for supply of goods provided that ‘any dispute arising in relation to this agreement will be settled by arbitration of a neutral person agreed to by both parties’ was held by the court to be vague and uncertain as the expression ‘neutral person agreed by both’ was not very clear because identification of a neutral person and how the parties were to develop a consensus on him was not made clear. It might not have been the intention of the parties that resort to arbitration was the sole remedy. It only suggested that they could resort to arbitration if they so wished.

⁹⁹ Ibid at page 49

¹⁰⁰ ICC Case No. 9480/AC (July 1998)

¹⁰¹ (2004) AIR 127

4.4 Capacity

As a general rule every reference to arbitration arises from the agreement of the parties to have their differences settled by arbitration. Therefore, anyone who is capable of making a binding contract or agreement is also capable of entering into an arbitration agreement.

The persons who make the agreement to refer may be merely the agents of the parties whose interests are involved in the dispute, and therefore need not necessarily be the persons whose interests are involved in the dispute, and therefore need not necessarily be the parties in the reference.¹⁰²

Capacity to contract is the test for capacity to submit to arbitration and as such any person, sui juris, can make a binding arbitration agreement. An infant may be a party to an arbitration agreement, but he may avoid it before coming of age unless it relates to contracts for the supply of necessaries, a contract of service, or other contract clearly for the infant's benefit.

If an infant is a party to a contract containing an arbitration clause, he is bound by the arbitration clause if the contract as a whole is for his benefit and the arbitration clause cannot be treated as a separate agreement from the main contract.¹⁰³

A bankrupt can only bind himself personally to a reference; his estate will not be affected unless his trustee is made a party to the reference, with the consent of the committee of inspection. If a trustee in bankruptcy adopts a contract to which the bankrupt is a party containing a clause for the reference of all disputes arising out of it to arbitration, the arbitration clause will be enforceable by or against the trustee.

¹⁰² Lawrence David (1968), *A Treatise on the Law and Practice of Arbitrations & Awards*, the Estates Gazette Ltd, London

¹⁰³ See the case of *Slade -vs- Metrodent Ltd* (1953) 2 QB 112

4.5 Factors to Consider When Drafting a Proper Arbitration Agreement

The elements being that arbitration is consensual, private, resolved by non-governmental decision makers, produces a binding award enforceable by national courts, freedom of choice and has a co-operative climate. The features of arbitration discussed are: the agreement to arbitrate; existence of a dispute; the choice of arbitrators; the decision of the arbitral tribunal and the enforcement of the award.

In drafting an arbitration agreement, parties must have this holistic perspective of arbitration in mind and they must especially be aware of the vast responsibility and consequence that is upon them in determining the course of arbitration and the power of choice granted to them.

Whether parties choose to expressly make provision or to make reference to rules, they must make sure that they address at least the following core matters either expressly or by cross-checking to see that they are satisfactorily covered in whatever set of rules that they incorporate into the agreement by reference.

The main factors of consideration in drafting an Arbitration Agreement are:

1. The arbitration agreement must be in writing.
2. Where should the arbitration be held?
3. Will disputes be arbitrable?
4. Which Disputes should be submitted to Arbitration?
5. Will the local Courts assist the Arbitration?
6. Will an Arbitral Award be subject to Appeal in the local Courts?
7. Will the Arbitral Award be enforceable in the Courts of other Nations?
8. How many Arbitrators should there be?
9. What should be the qualifications of the Arbitrator?
10. Will the Arbitration Proceedings be confidential?
11. Can multiple Arbitrations be combined into a single Proceeding?

12. What will be the language of the Arbitration?
13. What substantive Law will apply to the Arbitration?
14. Choice of Rules.
15. Other Clauses.

4.5.1 The arbitration agreement must be in writing¹⁰⁴

When drafting an arbitration agreement one must bear in mind the requirement that it must be in writing as prescribed by Section 4 (2) of the Arbitration Act.

Should a dispute however arise and parties do not have an arbitration agreement in place and they decide to refer their dispute to arbitration, then the first step will be for them to write-up an arbitration agreement.¹⁰⁵

It is however not necessary that an arbitration meet all the formalities of a contract. Section 4 (3) of the Act provides that the agreement shall be in writing by meeting any of a minimum set of standards including being contained in a document signed by the parties; an exchange of letters, telex, telegram, facsimile, electronic mail or other means of telecommunications which provide a record of the agreement; or an exchange of statements of claim and defence in which the existence of an agreement is alleged by one party and not denied by the other party.¹⁰⁶

The provision tries to make it easier to refer a dispute to arbitration to the extent of finding the existence of an arbitration agreement in a statement of claim where the allegation of the existence of the agreement is uncontroverted.¹⁰⁷

¹⁰⁴ See also, Kariuki Muigua, Preliminary Proceedings and Interlocutories: The Birth, Teething, Immunization and Weaning of Arbitration Proceedings, unpublished material, Chartered Institute of Arbitrators (Kenya Branch) teaching materials, 2008 at page 4 where he states that the rationale for having an arbitration agreement in writing, “is that arbitration is mainly a private and contractual arrangement between the parties for resolution of a given dispute or potential dispute(s).”

¹⁰⁵ See Ronald Bernstein & Adam Wood, Handbook on Arbitration Practice, 2nd Edition, Sweet & Maxwell in conjunction with The Chartered Institute of Arbitrators at Page 21-22

¹⁰⁶ Supra Note 102 at page 5

¹⁰⁷ Section 4 (3) (c) of the Arbitration Act

The Court has even found an arbitration agreement to subsist where a Plaintiff produced a contract signed only by itself and not by the Defendant.¹⁰⁸ The argument of Justice Nyamu was that the contract had not been denied by the Defendant and stated:

“I am satisfied that there is an arbitration agreement between the Plaintiff and the Defendant to refer any dispute or difference to arbitration pursuant to Clause 31, that Agreement has been exhibited and not denied. It is in writing as required by the ‘Section 4 of the Arbitration Act.’”

The agreement can also be, and most commonly is, a clause in a contract or a separate agreement.¹⁰⁹

Oral arbitration agreements are however acceptable in certain jurisdictions and in England, oral agreements to submit present or future differences to arbitration may be valid and enforceable at common law.¹¹⁰

To avoid disappointment however, parties should ensure that their arbitration agreement is in writing and if they wish to refer a current dispute to arbitration, they should immediately draft an arbitration agreement.

4.5.2 Where should the arbitration be held?¹¹¹

Failure to decide on this early will lead to disputes in deciding on a place later and could limit the freedom offered by arbitration as the choice may have to be made by the arbitrator or the institution appointing the arbitrator.¹¹²

¹⁰⁸ HCCC No. 32 of 2005(Nyamu J), Pan Africa Builders & Contractors Ltd vs National Social Security Fund Board of Trustees¹⁰⁸ See also Ronald Bernstein & Adam Wood, Handbook on Arbitration Practice, 2nd Edition, Sweet & Maxwell in conjunction with The Chartered Institute of Arbitrators at page 21 where he states that the agreement does not need to be signed by either party.

¹⁰⁹ Section 4 (1) of the Arbitration Act

¹¹⁰ Ronald Bernstein & Derek Wood, Handbook of Arbitration Practice, 2nd Edition, Sweet & Maxwell in Conjunction with The Chartered Institute of Arbitrators at page 21

¹¹¹Markham Ball, Just Do It – Drafting the Arbitration Clause in an International Agreement, Off-prints of the Journal of International Arbitration, Geneva, December 1993, Vol. 10 No. 4 at 35

¹¹² See Section 21 of the Act which provides for the choice of the place of arbitration

In deciding on the place where the arbitration is to take place, the parties will be having several pragmatic questions in mind including accessibility of the place; costs of hiring premises and maybe boarding should there be need to spend a considerable amount of time there; whether the courts of that place can easily support the arbitration proceedings.

It would be unwise for instance for parties to choose a volatile place like Somalia as the place of arbitration. There would be challenges of travelling there, local courts to support the arbitration, a local arbitration act and so on.

Parties might also consider the costs of travel, accommodation and hiring premises to settle a dispute in a certain town or place.

4.5.3 Will disputes be arbitrable?

Some countries have more advanced arbitration jurisprudence as compared to others and it might be that there are certain disputes that may be arbitrable in certain countries but not in others. For example in Kenya, you cannot arbitrate over the winding up of a company or bankruptcy proceedings. Allegations of fraud may in some cases also call for the intervention of the Court in certain jurisdictions.

4.5.4 Which disputes should be submitted to arbitration?¹¹³

The parties should separate, if need be, which disputes are to be submitted to arbitration and which ones are to go to litigation.

Parties cannot therefore arbitrarily claim a right to arbitration without the foundation of an arbitrable dispute. In *London Joint Rly Cos. Vs JH Billington Limited*,¹¹⁴ Lord Halsbury (LC) stated that:

“...a condition precedent to the invocation of the arbitrator on whatever grounds is that a difference between the parties should have arisen; and I

¹¹³ Markham Ball, Just Do It – Drafting the Arbitration Clause in an International Agreement, Off-prints of the Journal of International Arbitration, Geneva, December 1993, Vol. 10 No. 4 at 42

¹¹⁴ *London and North Western and Great Western Joint Rly Cos. –vs- JH Billington Limited* (1899) AC 79 at page 81

think that must mean a difference of opinion before the action is launched ... Any contention that parties could, when they are sued for the price of services, raise then for the first time the question whether or not the charges were reasonable and that therefore they have a right to go to an arbitrator, seems to me to be absolutely untenable.”

Parties need then to ensure that the arbitration agreement adequately covers the kind of disputes that they would like to refer to arbitration rather than trying to claim a dispute is arbitrable simply because it has arisen.

Often, routine disputes like the price of goods might not need to be settled by arbitration but might be more speedily settled by for example a valuer. However, more pertinent questions like breach of contract are worthy of being referable to arbitration.

4.5.5 Will the local courts assist the arbitration?

Parties will also consider whether the local courts will assist in the arbitration. It is almost a foregone conclusion that for countries signatory to the New York Convention,¹¹⁵ the courts must assist the arbitration.

On the other hand however, various jurisdictions, in order to make arbitration meaningful and dependable limit the capacity of courts to intervene in arbitration processes. Locally for example, Section 10 of the Act limits the intervention of the Court in arbitral disputes to that outlined in the Act and there is no automatic right of Appeal to the Courts in arbitration unless the parties agree. This consideration is also important because arbitration without the backing of the law and courts to enforce the award, prevent injustice and ensure compliance with procedure would be a waste of effort. However, most modern states provide sanctions necessary to ensure compliance with arbitration requirements.¹¹⁶

¹¹⁵ Convention on the Recognition and Enforcement of Foreign Arbitral Awards adopted by the United Nations General Assembly in New York on the 10th June, 1958, and acceded to by Kenya on the 10th February, 1989, with a reciprocity reservation.

¹¹⁶ Sir Michael J. Mostill and Stewart C. Boyd, Commercial Arbitration, 2nd Edition, Butterworths (London Edinburgh) 1989 at page 4 state that, “Arbitration is an important part of commercial life, and any legal system must in some degree be concerned with it.”

Local courts may also compel a party to an arbitration agreement to go to arbitration as opposed to pursuing litigation. In Kenya for example, courts may force an unwilling party to go to arbitration should it be so provided in the parties' agreement.¹¹⁷ The courts may also make interim orders either before or during the arbitration proceedings and can also assist to subpoena witnesses and to order production of evidence.

4.5.6 Will an arbitral award be enforceable in the courts of other nations?

Here as well, the provisions of the New York Convention¹¹⁸ are comforting as the Convention compels signatory states to enforce the arbitral awards made in other countries signatory thereto.

This Convention, to which Kenya is a party, has been very successful and has ensured enforceability of at least 90 % of all foreign awards involving persons from its more than 140 signatories and it has even been described as the most successful treaty in private international law.¹¹⁹

Rules of comity may also support the enforcement of foreign arbitral awards where they are in place.¹²⁰

4.5.7 Will an arbitral award be subject to appeal in the local courts?

Arbitration generally limits the recourse to appeal in court against an arbitral award. The most a party can do is seek for the setting aside of the entire or part of the award by the High Court.

A party to an arbitration agreement has need to be aware of this limited means of challenging the award of the arbitrator as the process of appeals is crucial in the

¹¹⁷ Section 6 of the Arbitration Act

¹¹⁸ New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 10 June 1958, Article II, 330 U.N.T.S. 38 (1959)

¹¹⁹ Albert Jan van den Berg Hanotiau (ed); *Convention On The Recognition And Enforcement Of Foreign Arbitral Awards* , ICCA Congress Series No. 9 (The Hague: Kluwer Law International, 1996)

¹²⁰ Markham Ball, Just Do It – Drafting the Arbitration Clause in an International Agreement, Off-prints of the Journal of International Arbitration, Geneva, December 1993, Vol. 10 No. 4 at 31

administration of justice as it is one of the principal means of ensuring accountability on the parts of lower tribunals whereas an appeal is now almost an entitlement given in the courts for most decisions arising from lower tribunals.

It is recognized that if an arbitration is carried out poorly resulting in injustice, arbitration may not offer similar, equivalent or satisfactory remedies similar to those provided by courts one of those remedies being the appeals process.¹²¹

This limitation on the intervention of the court in arbitration should be in the minds of the parties as they draft their arbitration agreement.

The responsibility that parties place upon themselves in opting to have their disputes settled by arbitration rather than courts was well stated in *Kirii -vs- Ngari Kirii*,¹²² where Platt Ag JA stated that:

“...what is less well-known is that by entering into arbitration, the parties have chosen arbitrators to decide their dispute rather than the court, with the consequence that except in limited circumstances there is no appeal... If the process of setting aside the arbitrator’s award is not available or not resorted to, then the only help the court can give the parties is to make sure that the judgment given by the court is in exact accord with the terms of the award. This is based on the free consent and choice of the parties to prefer their dispute to be settled by arbitration.”

4.5.8 How many arbitrators should there be?¹²³

Deciding on the number of arbitrators is important especially in complex matters as having more than one arbitrator will have the advantage of ensuring that the dispute is analyzed from a variety of angles and chances of bias in deliberation are minimized. Although a high number of arbitrators would also result in higher costs on the parties, if

¹²¹ Ronald Bernstein & Derek Wood, Handbook of Arbitration Practice, 2nd Edition, Sweet & Maxwell in Conjunction with The Chartered Institute of Arbitrators at page 5

¹²² Nyeri Civil Appeal No. 12 of 1985 unrp (Coram: Hancox JA, Platt & Gachuhi Ag JJA)

¹²³ Markham Ball, Just Do It – Drafting the Arbitration Clause in an International Agreement, Off-prints of the Journal of International Arbitration, Geneva, December 1993, Vol. 10 No. 4 at 38; see also Ronald Bernstein & Adam Wood, Handbook on Arbitration Practice, 2nd Edition, Sweet & Maxwell, in conjunction with The Chartered Institute of Arbitrators at page 24

the dispute is a complex one, then the benefit of having more than one arbitrator would far outweigh the cost attributable to having more arbitrators.

4.5.9 What should be the qualifications of the arbitrator?

It has been earlier observed that arbitration is as good as the arbitrator.¹²⁴

An important qualification of an arbitrator is neutrality. Neutrality however does not limit an arbitrator from sharing a party's point of view or legal philosophy or view. What is more important is that he should not have a personal, financial or some other substantial interest in the outcome of the arbitration or be under the extra-arbitral control or influence by a party.

4.5.10 Will the arbitration proceedings be confidential?

Unless confidentiality is expressly and satisfactorily provided for in the rules chosen, parties should provide for this in their arbitration clause to avoid unilateral publicizing of their dispute.

4.5.11 Can multiple arbitrations be combined into a single proceeding?

This is an arbitral parallel to consolidation of suits in the court process. It is wise to provide for multiple arbitrations as it will avoid repetition and the risk of discordance if multiple awards were given.

4.5.12 What will be the language of the arbitration?¹²⁵

This is important especially in an international arbitration agreement. Parties may be of differing language and waiting till the occurrence of a dispute to determine the language to use in arbitration would be risking delays and the intervention of the court.

Parties need to consciously determine what language or multiple languages will be used in the deliberation of their dispute.

¹²⁴ Supra Note 18 at page 8

¹²⁵ Supra Note 123 at page 42

4.5.13 What substantive law will apply to the arbitration?

The choice of substantive law is of paramount importance in drafting an arbitration agreement and especially where the agreement involves parties of different nationalities. This is the law that will set out the rights and liabilities of the parties in regard to the matters in dispute.

Parties need to make this determination in their agreement to avoid having to go to court to have the applicable substantive law be determined under protracted conflict of laws proceedings which yields delay and heightened costs.

Parties also have power to expressly authorize the tribunal to determine the dispute in ‘accordance with considerations of justice and fairness without being bound by the rules of law’.¹²⁶

This would therefore allow parties to do away with national systems of law where they might not be useful to them.

This application of a self styled system of law was recognized in the case of *Home Insurance v Meator Insurance*,¹²⁷ where the court stated:

“... this is especially in international commercial contracts that an arbitrator is not to apply a particular system of law but is to act as ‘amiable compositeur’ or is to decide ‘according to’ equity and good conscience or “according to the custom and usages of trade” or “so as to interpret this Reinsurance as an honourable agreement, and with a view to effecting the general purpose in a reasonable manner rather than in accordance with a literal interpretation of the language.”

The above ruling indicates that parties have room to also to apply customs and usages of trade as their substantive law.

With such a wide discretion, parties have an opportunity of choosing a very fitting substantive law to apply to their dispute.

¹²⁶ Section 29 (4)

¹²⁷ [1989] All E.R. 74

4.5.14 Choice of rules

This is a decision on which procedural rules are to be incorporated into the arbitration agreement. In looking at the rules, a party will confirm that the rules make provision for the arbitration in a manner acceptable to themselves. The parties can then expressly exclude the undesirable rules or modify them accordingly. Choice of rules also enables parties to shop for rules that have been tried and tested and even to experiment with new rules. The choice should not be made hurriedly or without proper assessment to consider whether the rules are the best for the current dispute.

Some of the considerations to make in drafting the rules include:

- a) Will there be institutional or *ad hoc* arbitration?
- b) How will the arbitrators be chosen? This is an important consideration as parties must ensure that they choose arbitrators in a method satisfactory to them. Should parties fail to have a method of appointing an arbitrator, then the court will appoint one for them leading to substantial costs and delay.¹²⁸
- c) Will any special procedural rules apply? - failure to do this at time of drafting will risk extra costs and delay.
- d) The arbitration cost?

4.5.15 Other Clauses¹²⁹

These would cover inter alia the following matters:-

- a) evidence,
- b) governing substantive law,
- c) language of the arbitration,

¹²⁸ Ronald Bernstein & Adam Wood, Handbook on Arbitration Practice, 2nd Edition, Sweet & Maxwell, in conjunction with The Chartered Institute of Arbitrators at 24

¹²⁹ Markham Ball, Just Do It – Drafting the Arbitration Clause in an International Agreement, Off-prints of the Journal of International Arbitration, Geneva, December 1993, Vol. 10 No. 4 at 42

- d) What discoveries (production of documents, interrogatories, depositions) will be possible?
- e) What statute of limitations, if any, applies?
- f) May damages include pre-award interest?
- g) What relief may the arbitrators award?
- h) Do the parties want to limit the powers of the courts to review the awards? ..
- i) Must arbitrators have any special qualifications, should parties attempt ADR before resorting to arbitration?
- j) Must the award contain a statement of reasons?
- k) How will the costs of arbitration be apportioned?
- l) In what currency will an award be paid? and;
- m) Should there be a time limit to the arbitration?

However when including these clauses one should be careful to ensure that such clauses do not oust statutes which may result in having the clause declared null and void in the event that they are challenged in a court of law.

Conclusion

A valid arbitration agreement must at the least meet the statutory requirements set out under the Arbitration Act. In essence an arbitration agreement must be in writing and it must refer certain or all disputes to arbitration. Besides, the requirements as to form, the scope of the arbitration agreement must cover disputes which are arbitrable.

CHAPTER FIVE

Introduction

This chapter will consider the problems that are associated with the arbitration agreement and especially where the validity of the arbitration agreement is in question.

This chapter will also propose ways in which the problems can be dealt with and including recommending that the drafters of arbitration agreement be keen when drafting such agreements. Such keenness can be achieved, for example through the use of a checklist to ensure that essential matters are covered by the arbitration agreement.

5.1. Major problems associated with arbitration clauses and Recommendations

From time to time, someone tries to define what a perfect arbitration clause would look like. Efforts to do so usually founder on one of the strengths of arbitration, which is its adaptability to the particular circumstances of the parties and the dispute. Therefore, while it is difficult to generalize about what would make a “perfect” clause, it is not nearly as difficult to identify some of the features that make for a bad one.¹³⁰

The following are the major problems arising from poorly drafted arbitration agreements:-

5.2 Equivocation

Equivocation arises when drafters of the arbitration clause fail to state clearly that the parties have agreed to binding arbitration. It is associated with the requirement that an arbitration agreement need to be in writing, since if there is no agreement then there is no arbitration.¹³¹

If an arbitration clause makes it clear that any dispute “must” or “will” be referred to arbitration, the position is straightforward. However, where the clause is on its face purely permissive and merely allows a dispute to be referred to arbitration, greater

¹³⁰ Townsend (2003), *Drafting Arbitration Clauses: Avoiding the 7 deadly sins*, American Arbitration Association Dispute Resolution Journal Vol. 58, No. 1, 335

¹³¹ Craig et al (1993) *International Chamber of Commercial Arbitration Publication*, Oceania Publication

difficulty would arise in giving effect to such a clause. It is doubtful whether a clause which is purely optional in its terms, in that either party is empowered but not required to commence arbitration proceedings can be regarded as one which constitutes a binding obligation to go to arbitration from the outset even though it may in some instances qualify as an arbitration clause. A clause which provides for arbitration only if both parties are willing to go to arbitration cannot be an arbitration clause, as it is no more than an agreement to agree.¹³²

For example an equivocal clause may be worded as follows:-

“in case of dispute, the parties undertake to submit to arbitration, but in case of litigation the English Courts shall have exclusive jurisdiction”

In the case of *King –vs- Brandywine Reinsurance Co. (UK) Ltd*¹³³ it was held that the arbitration agreement could not be enforced and the application to stay the Court proceedings was dismissed. In this case, the arbitration clause provided that any dispute could be referred to arbitration “upon the agreement of the parties.”

However, and having due regard to the provisions of Section 10 of the Act, the tendency of the Court has been to construe the clause as a binding arbitration clause. In *Lobb Partnership Ltd –vs- Aintree Racecourse Co. Ltd*¹³⁴ the Applicants who were architects sought to overturn an award of an arbitrator in which he had ruled that there was in existence an arbitration agreement between the parties. The relevant clause in the agreement provided that “disputes may be dealt with as provided in paragraph 1.8 of the RIBA Conditions but shall otherwise be referred to the English courts.” Paragraph 1.8 of RIBA contained an arbitration clause. Colman J, held that there was a binding agreement.

The courts of most countries will generally try to uphold an arbitration agreement unless the uncertainty is such that it is difficult to make sense of it. Such clauses include:- *“in case of any unresolved dispute, the matter shall be referred to the International Chamber*

¹³² Merkin Robert, (2004), Arbitration Law, Lloyd’s Commercial Law, London

¹³³ (2004) EWHC 1033 (Comm)

¹³⁴ (2000) BLR 65

of Commerce.”¹³⁵ The problem with this clause is that although there is a broad reference to the International Chamber of Commerce, the clause does not stipulate whether the unresolved dispute is to be settled by arbitration or by conciliation or by some other procedure.

5.3 Inattention

One of the reasons why arbitration clauses have often been referred to as the “midnight clauses” is the fact that no one really pays attention to them as they are often not discussed in as great a detail as the main contract and often than not, most drafters usually “copy paste” arbitration clauses into a contract.¹³⁶

One of the issues to consider when drafting an arbitration clause is the suitability of the clause to the deal between the parties. When drafting the arbitration clause, one should consider the following:-

5.3.1 What type of dispute resolution process is best suited to the client and the transaction?

In answering this question, one should bear in mind the fact that arbitration is not the only option. There are many alternative dispute resolution processes and there is also litigation. In particular cases, it might be more prudent for the parties to litigate than to go to arbitration. However, in international commercial transactions, arbitration may be a more suited option than any other mode of dispute resolution.

5.3.2 If arbitration is selected, does the client understand that the arbitration clause will commit the client to a binding process that involves certain trade-offs?

Arbitration has advantages, prominent among them being confidentiality and privacy, as well as the possibility of crafting a process that will be speedier

¹³⁵ Supra Note 34 at page 172

¹³⁶ Supra Note 34 at page 173

and more economical than litigation. It also provides the opportunity for the parties to choose a fair and neutral forum and to participate in the selection of the decision maker and the rules to be applied. On the other hand, by choosing arbitration, a party would in fact be giving away their rights that in law are usually available to litigants. These may include the right to appeal.

5.3.3 Have the parties considered providing for steps preceding arbitration, especially if the relationship between the parties is an ongoing one?

When drafting an arbitration agreement one needs to consider whether it would be beneficial to provide that parties shall first refer such a dispute to an internal dispute resolution mechanism between the parties failure to which the dispute may then be referred to arbitration.

5.3.4 Have the parties considered where they may want to enforce an award?

This is particularly critical in an international contract. One needs to consider whether the country to which enforcement may be sought is a signatory to the New York Convention. One should consider in what country the client is most likely to need to enforce an eventual award. This would include for example, ascertaining the place where the assets of the adversary are located and determining whether that country is a signatory to the New York Convention on the enforcement of foreign arbitral awards.

5.4 Omission

Another pitfall to avoid when drafting an arbitration clause is omission. In drafting the clause, there are a few mandatory requirements that must be met, and a few provisions that must be included. Omission can result in a clause that expresses an agreement to arbitrate, but fails to provide guidance as to how or where it is to be conducted. For example a clause may provide as follows:-

‘any dispute arising out of this agreement will be finally resolved by arbitration’

The clause would be enforceable as it is clear that disputes are to be resolved by arbitration, however, it does not achieve the goal of arbitration clauses, which is to allow parties to have the autonomy of deciding where and how disputes are to be resolved and to stay away from the courts.

In the case of *Tritonia Shipping Inc –vs- South Nelson Forest Products Corporation*¹³⁷ a charterparty provided merely ‘arbitration to be settled in London.’ The Court of Appeal held that disputes under the charterparty should be arbitrated in London in accordance with the agreement of the parties. In the case of *London-Goldstar International (HK) Ltd-vs- Ng Moo Kee Engineering Ltd*¹³⁸ the arbitration clause provided that arbitration would be ‘in a third country.....in accordance with the rules of procedure of the International Commercial Arbitration Association.’ No third country was nominated and no such association existed. The Supreme Court of Hong Kong held that the parties had nevertheless agreed to go to arbitration: the term ‘third country’ meant any country other than those of which the parties were nationals and the reference to a non-existence association could be deleted as meaningless.¹³⁹ Thus to avoid the pitfall of omission, the drafter of an arbitration clause would best be suited to either use a model clause or make use of a checklist which would indicate what the essential matters are. The ten most important provisions are:-

- (a) Agreement to arbitrate;
- (b) What disputes will be arbitrated;
- (c) Rules that will govern the arbitration;
- (d) The institution if any, that will administer the arbitration;
- (e) The place of arbitration;

¹³⁷ (1996) 1 Lloyd’s Rep 114

¹³⁸ (1994) ADRLJ 49

¹³⁹ In the case of *Hobbs Padgett & Co. (Reinsurance) Ltd –vs- J C Kirkland Ltd* (1969) 2 Lloyd’s Rep. 547 an agreement for the dissolution of a reinsurance brokerage contained the heading ‘suitable arbitration clause’ although nothing further had been inserted. The English Court of Appeal held that the parties had agreed to arbitrate: the question of suitability was an objective one which could be determined by the courts and the missing details could be provided by the general provisions of the Arbitration Act. In the case of *Mangistaumunaigaz Oil Production Association –vs- United World Trading Inc* (1995) 1 Lloyd’s Rep. 617 in which the arbitration clause provided that arbitration if any, by ICC rules in London. Potter J held that this was a valid arbitration agreement and the words ‘if any’ were dismissed either as being more surplusage or as a shorthand for ‘if any dispute’ rather than indicating that there was no final agreement to arbitrate.

- (f) The language of arbitration (especially in an international contract);
- (g) The applicable law;
- (h) The procedural law; and
- (i) The number of arbitrators and the mode of selection.

5.5 Over-specificity

Sometimes a drafter of an arbitration clause may be too over-zealous and thus come up with an arbitration clause with either too many terms or one that may be difficult to implement. For example a clause may provide as follows:

*‘the arbitration shall be conducted by three arbitrators, each of whom shall be fluent in Hungarian and shall have twenty or more years of experience in the design of computer chips and one of whom shall act as chairman, shall be an expert on the law of the Hapsburg Empire’.*¹⁴⁰

When an arbitration clause is over-detailed, those layers of details can make it difficult or impossible to arbitrate when a dispute arises. The over-detailed clause may also result in a clause that may be unrealistic. For example a clause may provide as follows:-

*“the claimant will name its arbitrator when it commences the proceeding. The respondent will then name its arbitrator within seven (7) days and the two so named will name the third arbitrator, who will act as chair, within seven (7) days of the selection of the second arbitrator. Hearings will commence within fifteen (15) days of the selection of the third arbitrator and will conclude not more than three (3) days later. The arbitrators will issue their award within seven (7) days of the conclusion of the hearing”.*¹⁴¹

¹⁴⁰ Supra Note 22 at page 23

¹⁴¹ Supra Note 22 at page 31

Although there are circumstances that may justify the inclusion of tight time limits, in certain specific circumstances, most commercial arbitration would require to proceed in a stately speed.¹⁴²

The other issue is where the drafter in a bid to please the client drafts an arbitration clause which tilts in favour of his client. In the American case of *Hooters of America, Inc –vs- Phillips*¹⁴³ the applicant made an application in court to have the dispute between it and the respondent, its former employee referred to arbitration. The application was dismissed as the court noted that the arbitration agreement contained several overreaching elements which were unconscionable such as:-

- (a) The employee and the employer were each to select an arbitrator and the two arbitrators were to pick the third arbitrator, but all three had to be chosen from a list created by the employer which had exclusive and unrestricted control over who was on the list;
- (b) Nothing in the arbitration clause required the arbitrators to be impartial or independent of the employer;
- (c) The employee was required to file with her claim a list of all witnesses specifying the facts known to each, but the employer was not required to file any with its defence;
- (d) The employer was permitted to move for summary disposition but the employee was not;
- (e) The employer could amend its position but the employee could not;
- (f) The employer could record the proceedings but the employee could not;
- (g) The employer could modify the arbitration rules at will and without notice to the employee; and

¹⁴² See for example the American case of *Re Arbitration No. AAA13-161-0511-85 under Grain Arbitration Rules (1989)* 2nd Cir. 867 in which it was held that failure to meet a deadline in arbitration agreement deprives an arbitrator of jurisdiction to proceed with the arbitration.

¹⁴³ (1999) 4th Cir 173

(h) The employer had the option to cancel the agreement to arbitrate but not the employee.

The court further held:-

“the parties agreed to submit their claims to arbitration-a system whereby disputes are fairly resolved by an impartial third party. Hooters by contract took on the obligation of establishing such a system. By creating a sham system unworthy of the name of arbitration, Hooters completely failed in performing its contractual duty.....and also violated the contractual obligation of good faith. Hooters’ performance under the contract was so egregious that the result was hardly recognizable as arbitration at all.”

5.6 Inconsistency with other contractual terms

An arbitration agreement while it may be clear itself may be inconsistent with the remainder of the contract.¹⁴⁴ This may be a problem where the inconsistency arises because conflicting provisions have been incorporated by reference into the contract. In the case of *Paul Smith Ltd –vs- H & S International Holding Inc*¹⁴⁵ clause 13 of the contract between the parties provided that any dispute between the parties “shall be adjudicated upon” under the ICC rules, while clause 14 stated that the “Courts of England shall have exclusive jurisdiction” over any dispute. Steyn J rejected the argument that the clauses were self cancelling as such a conclusion would involve “the total failure of the agreed method of dispute resolution in an international commercial contract.” Striving to uphold the obligation to arbitrate, the learned judge resolved the ambiguity by a plausible artificial construction of clause 14. The judge held that the jurisdiction provision on clause 14 referred not to the dispute but to the arbitration itself, with the result that English courts were the curial courts in relation to it. Thus while the arbitration was to be governed by the ICC Rules, the residual curial powers of appointment, judicial assistance and review fell within the exclusive jurisdiction of the English courts.

¹⁴⁴ Supra Note 34 at page 24

¹⁴⁵ (1991) 2 Lloyd’s Rep 127

In *Shell International Petroleum Co. Ltd-vs- Coral Oil Co. Ltd*¹⁴⁶ in which the agreement between the parties provided that it was to be governed by English law and was subject to the exclusive jurisdiction of the English courts and any dispute was to be resolved by arbitration in London. The Court of Appeal held that the agreement was to be construed as meaning that the applicable law was English law, and that only disputes as to the applicable law were to be resolved by the English courts, any other dispute was to be resolved by arbitration. This analysis has in effect given supremacy to the arbitration agreement over the jurisdictional clause. This interpretation has found its way in statutes. For example Section 10 of the Arbitration Act which limits interventions by the Court in arbitrations governed by the Act.¹⁴⁷

Although the general principle remains that arbitration clauses will be given priority where there are conflicting contract terms, there may be some situations in which the arbitration clause cannot be regarded as forming part of the dispute resolution process agreed to by the parties. In *MH Alshaya Co. WLL –vs- Retek Information Systems Inc*¹⁴⁸ the claimant a Kuwaiti Company agreed to buy a software system from the respondent, an American company although the negotiations were conducted by its English subsidiary. There were two contracts between the parties, a software licence and a maintenance agreement and a separate confidentiality agreement between the Kuwaiti company and the English subsidiary. The software licence contained both an exclusive jurisdiction clause nominating the English courts and an arbitration clause requiring all disputes to be submitted to arbitration under the rules of the AAA but subject to the right of either party to apply for injunctive relief. The maintenance contract contained only a choice of law and exclusive jurisdiction clause nominating the English courts. The confidentiality agreement in much the same way as the software agreement contained both an exclusive jurisdiction clause and an arbitration agreement. Disputes arose as to the performance of the contract and the claimant

¹⁴⁶ (1999) 1 Lloyd's Rep 72. Cf *National Power Plc –vs- National Grid Co. Plc*, 1998

¹⁴⁷ Cf with the Hong Kong Case of *William Co. –vs- Chu Kong Agency Co. Ltd and Guangzhou Ocean Shipping Co.* (1993) and in which although a similar conclusion was arrived at, the Court held that conflicting arbitration and exclusive jurisdiction clauses gave the claimant the option either to go to arbitration or commence judicial proceedings in the agreed jurisdiction.

¹⁴⁸ (2001), MCLR, 99

commenced judicial proceedings in England seeking damages. The English subsidiary purported to initiate arbitral proceedings and the claimant sought an injunction against it. In granting the injunction, Garland J, held that the arbitration clause in the software agreement could not be given effect. Any dispute between the parties was likely to arise both under the software and maintenance agreements but only the former contained an arbitration clause. That clause could not be implied into the maintenance as it contained a “four corners” or “entire contract” provision under which only the written terms were to be treated as part of the agreement.

Where there is an apparent inconsistency in the clause, most national courts will try to give meaning to it in order to give effect to the general intention of the parties, which was to submit disputes to arbitration. Generally the arbitration agreement would be read as a whole for its proper interpretation. In the case of *Madan Mohan Rajgarhia –vs- Mahendra R. Shah & Bros*¹⁴⁹ the arbitration clause of a Stock Exchange provided that disputes between members and non-members would be resolved by arbitration. The term non-member was defined as including a remisier, authorized clerk or employee or any other person with whom the member shared brokerage. Reading the clause as a whole, the court held that it covered a share dealer utilizing the services of a broker at the Stock Exchange for its business.

5.7 Unconscionable arbitration clauses

A party may seek to avoid an arbitration agreement on the ground that it is unconscionable. In the United States of America there have been recent cases in which parties have attacked the selection of the ICC Arbitration Rules in contracts on the ground that the ICC’s administrative costs are excessive and thus that the arbitration clause is unconscionable. This was the case in *Brower –vs- Gateway 2000, Inc*¹⁵⁰ in which a computer manufacturer’s standard terms and conditions agreement included in the box of the computer, provided for arbitration of any dispute in accordance with the ICC Arbitration Rules. The agreement also stated that by keeping the computer for more than thirty days, the consumer accepted the terms and conditions. The New York

¹⁴⁹ (2003) 7 SCC 138

¹⁵⁰ (1998) WL 481066

court noted that the ICC advance fee of \$ 4000 (for a claim of less than \$ 50,000) is more than the cost of most of the defendant's products. The court held that the excessive cost of the ICC fees would effectively deter and bar consumers from arbitration, leaving them no forum for their disputes. The ICC fees were held unreasonable and the arbitration clause unconscionable and unenforceable.

5.8 Derogation from Institutional Rules

In drafting the arbitration clause, the parties should consider whether they can modify the institutional rules adopted. Most of the institutional rules allow parties to modify their applicability. However in some cases the ICC has on its part refused to administer arbitration because of alterations made by the parties' agreement to particular rules deemed by the ICC to be fundamental to its arbitral procedure.¹⁵¹ For example the ICC has refused to administer arbitrations in situations in which the parties provided for non-binding arbitration, in which the parties' agreement both called for an umpire procedure and adopted the ICC Rules and in which the parties provided that the chairman of a tripartite panel could not alone decide the case in the absence of a majority although the ICC Rules permit him to do so.¹⁵² The ICC has also refused to set into motion arbitration proceedings when arbitral clauses provided that the ICC Court could not confirm arbitrators, handle challenges to arbitrators, replace arbitrators, determine arbitrator's fees or scrutinize the draft award.

Accordingly, if a party wishes to adopt the ICC Rules but to alter them, it should consider including a clause either providing that any alteration of the ICC Rules may be disregarded if the ICC will otherwise refuse to administer the arbitration or adopting back up rules such as the UNICITRAL Rules for the ad hoc arbitration or another institution's rules such as those of the AAA.¹⁵³

¹⁵¹ Takla Youssef, (1996) Non-ICC Arbitration Clauses and Clauses Derogating from the ICC Rules, 7 ICC Int'l Ct. Arb. Bull. 7 at page 11

¹⁵² Schwartz Eric (1998) Comments on choosing between broad and detailed blueprints, ICCA Working Papers, May 3-6, 1998, Paris

¹⁵³ See for example Article 1 (1) of the AAA which provides that the Rules are applicable "subject to whatever modifications the parties may adopt in writing. This language indicates that any of the AAA Rules may be altered by the parties.

5.9 Pathological Arbitration clauses¹⁵⁴

Pathological arbitration clauses might be defined as those drafted in such a way that they may lead to disputes over the interpretation of the arbitration agreement, may result in the failure of the arbitral clause or may result in the unenforceability of an award.¹⁵⁵ examples of pathological arbitration clauses include; naming a specific person as arbitrator who is now deceased or who refuses to act,¹⁵⁶ naming an institution to administer the arbitration proceedings or to appoint the arbitrators if the institution never existed, is misnamed in the clause or refuses to act¹⁵⁷

5.10 Different versions of Arbitration Rules

Since the major arbitral institutions have amended their arbitration rules from time to time, an issue may arise as to which version of the rules the parties intended to govern

¹⁵⁴ Bernstein, Tackaberry et al (1998), Handbook of Arbitration Practice, 3rd edn, Sweet & Maxwell, London at page 551 provides as follows:-

“one might imagine a fourth series of considerations relating to *pathological elements* of the arbitration clause. Here are five types of sins to be avoided:

- (i) Uninformed tinkering with model clauses- the ICC has a model clause comprised of one simple declarative sentence. It has been drafted and refined by experts and appears in widely disseminated ICC brochures. Yet, when a study was conducted in 1987 of 400 pending ICC arbitrations, only one instance was found in which the parties had managed to copy the Model Clause perfectly. Draftsmen who are tempted to improve model clauses often achieve the opposite effect. The deceptively simple language of the ICC Model Clause (all disputes arising out of or in connection with the present contract) covers issues of formation, termination or quasi-contractual torts, attempts at ostensible sophistication may be interpreted as restrictive and lead to arguments about the jurisdiction of the arbitrator;
- (ii) Equivocation-which indicates indecisiveness on the part of the drafter as to the arbitrators or forum;
- (iii) Insufficient specification of the arbitral institution;
- (iv) Designation of authorities intended to appoint arbitrators without verifying whether they are in fact willing to accept such responsibility;
- (v) Combining irreconcilable procedural laws”

¹⁵⁵ Defective arbitration clauses were first denominated as “pathological” in 1974 by Frederick Eisemann, who served at the time as the Secretary General of the ICC International Court of Arbitration. See also use of the by Craig, Park & Paulsson, (1990) International Chamber of Commerce Arbitration, 2nd edn at 94

¹⁵⁶ See *Marcus –vs- Meyerson* (1958) NYS 170 in which it was held that the Court did not have authority to name a substitute for a resigning arbitrator who is specifically named in the parties’ contract. see also Section 9 of the Swedish Arbitration Act of 1929, which provided that :if a person who is designated as arbitrator in an arbitration agreement dies, the agreement shall lapse unless otherwise agreed between the parties.”

¹⁵⁷ The Hamm Court of Appeal in Germany held that an arbitration clause was fatally ambiguous and void in a case in which the clause read “the parties shall proceed to litigate before the Arbitration Court of the International Chamber of Commerce in Paris with the seat in Zurich” the court held that it could not determine whether the parties intended to submit to the ICC in Paris or to the Zurich Chamber of Commerce both of which maintained permanent arbitral tribunals.

their arbitration-the version in effect at the time the parties signed their agreement or the version in effect when the arbitral proceedings were commenced.¹⁵⁸

The parties can ensure that this pitfall does not arise by providing in their clause either that the adopted rules “then in force” on the date of the agreement or the rules “as modified or amended from time to time” shall be applied.¹⁵⁹

In this respect, the parties may wish to adopt the rules in existence at the time of contracting because these are the rules they know and future rules changes may have unpredictable effects. On the other hand, the parties may wish to take advantage of future rule amendments, assuming the institution will only adopt changes that will better the arbitral process.

While allowing the parties expressly to choose which version of the rules they prefer, some of the institutions include a default provision stating which version will be applied in the absence of an agreement. For example, the rules of the ICC, AAA and LCIA all provide that in the absence of an agreement to the contrary, the arbitration shall be conducted according to the rules in effect on the date of the commencement of the arbitral proceedings.¹⁶⁰

5.11 High-Low or Baseball-Style Arbitration¹⁶¹

This is an unusual form of arbitration in which the drafter provides that each party will propose a monetary figure for resolving any dispute over damages and the arbitrator is required to choose one party’s proposal as the award. Some clauses provide that the arbitrator shall select the proposal that is judged to be the more equitable.¹⁶²

¹⁵⁸ Bishop, Hughes & Luce, (2000); A practical Guide for Drafting International Arbitration Clauses, Dallas, Texas.

¹⁵⁹ Bond Stephen, (1990), How to Draft an Arbitration Clause (Revisited), 1 ICC Int’l Crt Arb Bull at page 14

¹⁶⁰ ICC Rules Article 6 (1), AAA International Rules Article 1 (1), LCIA Rules Introductory Paragraph.

¹⁶¹ This term has been adopted in some arbitration texts and materials including Contract Law , 2008 edn, IICLE Press

¹⁶² Supra Note 26 at page 132

This technique limits the discretion of the arbitrator and prevents a compromise award. It also pressures the parties to make realistic proposals rather than seeking outrageous sums or offering unreasonably low amounts. When this technique is employed, its use is typically limited to damage claims. It is also open to challenge as it is not clear whether it is some form of mediation as the solution is suggested by the parties or whether it is arbitration per se.

5.12 Inoperable arbitration agreements

This occurs in cases where parties fail to make a clear, unambiguous and mandatory arbitration agreement. For example, a clause which provides that “disputes arising out of this agreement may be referred to arbitration” is not worded in mandatory form and it might not prevent one party going to court to have the dispute resolved there.¹⁶³

The New York Convention at Article II.3 provides that:

“The Court of a Contracting State, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall, at the request of one of the parties, refer the parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed. (Emphasis provided)

An arbitration agreement is inoperative where it has ceased to have effect as a result, for example, of a failure by the parties to comply with a time limit, or where the parties have by their conduct impliedly revoked the arbitration agreement.¹⁶⁴

Where an arbitration agreement is stated to be incapable of being performed, it would appear that such circumstances would arise in the practical aspects of the prospective arbitral proceedings, for example where it may be impossible to establish an arbitral tribunal.

¹⁶³ Supra Note 30 at page 27

¹⁶⁴ Supra Note 34 at page 174

5.13 Online Arbitration

With technological advancements, parties are now moving towards embracing technology and in having their disputes resolved online. For example, the AAA and the Cyberspace Law Institute have jointly initiated the Virtual Magistrate Project, which administers arbitrations between system operators and online users involving allegedly wrongful messages.¹⁶⁵ These arbitrations decide whether a message should be deleted or access to it restricted, but they do not rule on damage claims.

As this is a recent development, a drafter who wants certain categories of disputes handled online needs to indicate so in the arbitration agreement. If this technique is used, it is critical to designate the situs of the arbitration or the procedural law to apply since there is no single place of an online arbitration and therefore, no clear applicable procedural law. It is also important for the parties to consider issues of confidentiality when using the internet, even if the arbitration is encrypted. Parties should also provide for the procedure to be used, for example the parties may provide that any hearings be held through chat rooms in which dialogue occurs in real time through typed transcripts or that oral hearings be held by video-conference or by conference call.

5.14 Use of Model Clauses to avoid the Pitfalls

Parties normally insert a simple arbitration clause in the primary contract as they believe that the possibility of disputes arising between them is remote. They therefore make innocuous arbitration clauses and move on to the “important” parts of their negotiations and avoid haggling over the details of proceedings which they are optimistic will never occur.¹⁶⁶

¹⁶⁵ Gabrielle Kaufman-Kohler (1998) Identifying and Applying the Law Governing the Arbitration Procedure-The Role of the Law of the Place of Arbitration, Second Working Paper of the ICCA Congress in Paris

¹⁶⁶ Francis J. Higgins and William G. Brown with Patrick J. Roach, Pitfalls in International Commercial Arbitration, 2. 1B 1 - 2. 1B 2

It has even been suggested that it is enough, for an arbitration agreement to be effective for parties to simply state that: “*disputes to be settled by arbitration’ and leave defects of omission to be cured by the court if necessary.*”¹⁶⁷

However, this oversimplification of the arbitration agreement would be a catalyst for delay in determining the various other elements and features of the arbitration agreement as and when disputes arise.¹⁶⁸ This heightening of costs and delay is undesirable as it may result in delays and costs similar to those in court litigation without the benefits of the safeguards offered in the public forum.

Further, when advocates get involved in the dispute and where there is much room for debate as to the nature of the prospective arbitral proceedings, they might complicate the process further by using legal arguments to protect their client’s interests.

Arbitration can therefore pose problems that are unforeseen until a dispute arises between the parties. Such problems can be avoided by the making of provisions in the arbitration clause at the time the contract is being negotiated.

In spite of the foregoing, it is also recognized that making rules and provisions for especially an ad hoc arbitration is a challenging task involving having to grapple with the possibility of hypothetical eventualities and at the same time having to negotiate the main contract. Parties in practice therefore do not provide for every aspect of arbitration in drafting an arbitration agreement.

Nevertheless, parties should endeavor to iron out such issues in the negotiation of the main contract as trying to do it in the context of an existing dispute might not yield desirable results as parties are already seeking to protect their own interests and gain tactical advantage. This is more likely than not a pre-cursor to court proceedings and they

¹⁶⁷ Ronald Bernstein & Adam Wood, Handbook on Arbitration Practice, 2nd Edition, Sweet & Maxwell in conjunction with The Chartered Institute of Arbitrators at 23

¹⁶⁸ Supra Note 165 at page 4 where it is stated that: “*In fact, a bare bones arbitration clause almost inevitably fails to confront the problems which arise in subsequent disputes.*”

should therefore note to provide early for all possible eventualities in their arbitration proceedings.

Parties usually easily discharge the burden of drafting a detailed arbitration clause by making reference to a set of rules to be the governing rules of an arbitration between them when it arises.¹⁶⁹ Incorporating rules of trade or institutional bodies as the governing rules in an arbitration agreement is common practice.

Alternatively, parties may refer their disputes to be resolved by a certain arbitral institution then the institute chosen to be the arbiter of disputes between the parties will apply its own rules to the dispute.¹⁷⁰

These should however not be a ground for indolence on the part of the parties so as to assume that the rules are watertight and will adequately cover the dispute between the parties. As we have seen earlier, institutional rules of procedure are not always satisfactory and may leave uncertainty over important questions such as discovery, admissible evidence, whether hearing should be oral or not and so forth.

There is therefore need for parties to be vigilant and to scrutinize the adopted rules so that they exclude what is not useful for them and to add what is not included in the rules that they might want to have as part of their agreement.

Each of the leading arbitral organizations provides a sample arbitration clause for inclusion in international contracts. For example, the ICC suggests the following clause:

¹⁶⁹ Supra Note 68 at page 73

¹⁷⁰ Examples of such institutions are the International Court of Arbitration of the International Chamber of Commerce (ICC) headquartered in Paris; London Court of International Arbitration (LCIA); International Centre for the Settlement of Investment Disputes and the Permanent Court of Arbitration at The Hague (for disputes between states or state agencies and nationals of other states); World Intellectual Property Organization (WIPO); American Arbitration Association; Chambers of Commerce in Zurich, Stockholm and elsewhere; Union of Chambers of Commerce of the Arab Countries

“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.”¹⁷¹

This clause has been said to contain the three “key expressions” for an arbitral clause – “All disputes”. . . “in connection with”. . . “finally settled”.¹⁷² The term “all disputes” encompasses all types of controversies, without exception. The language, “in connection with”, creates a broad form clause that will cover non-contractual claims such as tort and fraud, while “finally settled” indicates the parties intend the arbitrator’s ruling to be final so a court will not try the case de novo.

The London Court of International Arbitration’s suggested clause states:

*“Any dispute arising out of or in connection with this contract, including any question regarding its existence, validity or termination, shall be referred to and finally resolved by arbitration under the London Court of International Arbitration Rules, which Rules are deemed to be incorporated by reference into this clause.”*¹⁷³

The AAA suggests the following clause:

*“Any controversy or claim arising out of or relating to this contract shall be determined by arbitration in accordance with the International Arbitration Rules of the American Arbitration Association”.*¹⁷⁴

It should be noted that the clauses quoted are all broad-form clauses designed to encompass all disputes relating to the parties’ contract. While almost certainly enforceable, these clauses provide the bare minimum in an arbitration clause.

¹⁷¹ Rules of the ICC (as in force from 1st January, 1998)

¹⁷² Craig, Park & Paulsson (1990), International Chamber of Commerce Arbitration, 2nd edn at page 94

¹⁷³ LCIA Recommended Arbitration Clauses

¹⁷⁴ AAA International Rules whose model clause also gives the parties the option of specifying the number of arbitrators, and the place and language of the arbitration.

The ultimate goal of a model clause would be to facilitate commercial arbitration and to ensure its proper functioning and recognition. Its practical value would, in particular, depend on the extent to which it provides answers to the manifold problems and difficulties encountered in practice. Thus, in preparing a model arbitration clause an attempt should be made by the institution drafting it to meet the concerns which have repeatedly been expressed in recent years, sometimes labeled as “defects” or “pitfalls” in international commercial arbitration.¹⁷⁵

5.15 Use of a checklist in drafting an arbitration agreement to avoid the pitfalls.

Several writers have suggested that it would be advisable in drafting an arbitration clause, to start by borrowing from a precedent usually a model clause from one of the major arbitration institutions.¹⁷⁶ It is generally accepted that there is no arbitration clause that fits into all circumstance and adaptation must be realized by exercising proper draftsman judgment and skill.

Parties could be spared the effort of groping in the dark by there being a model clause that is comprehensive and that adequately provides for the important and apprehensible aspects of arbitration which are:

1. The Arbitration Agreement to be in writing.
2. Where should the Arbitration be held?
3. Will disputes be arbitrable?
4. Which Disputes should be submitted to Arbitration?
5. Will the local Courts assist the Arbitration?
6. Will an Arbitral Award be subject to Appeal in the local Courts?
7. Will the Arbitral Award be enforceable in the Courts of other Nations?

¹⁷⁵ Holtzmann & Neuhaus Joseph (1994), A Guide To the UNICITRAL Model Law on International Commercial Arbitration, Legislative History and Commentary, Kluwer Law and Taxation Publishers, Boston

¹⁷⁶ Supra Note 68 at page 2

8. How many Arbitrators should there be?
9. What should be the qualifications of the Arbitrator?
10. Will the Arbitration Proceedings be confidential?
11. Can multiple Arbitrations be combined into a single Proceeding?
12. What will be the language of the Arbitration?
13. What substantive Law will apply to the Arbitration?
14. Choice of Rules.
15. Other Clauses.

The above list can also be a checklist for parties who opt to adopt rules or to refer their disputes to arbitration as it can be used to confirm whether the rules adopted are sufficient to meet the needs of the parties in the context of a dispute.

Further, the Arbitration Act could be helpful in drafting as it provides for the default position if parties have failed to agree on any point. Parties could therefore draft an agreement to cover each or certain selected positions covered by the Arbitration Act whenever they are of the opinion that the default position is not sufficient.

5.16 Conclusion

In drafting the clause, there are a few mandatory requirements that must be met, and a few provisions that must be included. These provisions should be clear and unequivocal. In addition to these provisions, however, a clause may be ornamented in virtually endless combinations with a cornucopia of provisions covering topics as important as the situs of the arbitration and as esoteric as class action arbitrations.

A word of caution is in order. There is no such thing as a single “model”, “miracle” or “all purpose” clause appropriate for all occasions. Each clause should be carefully tailored to the exigencies of a given situation, taking into account the likely types of disputes, the needs of the parties’ relationship and the applicable laws. Because the arbitration clause is typically one of the last contractual provisions negotiated – after the parties have agreed on the essential terms – often the parties merely insert form clauses or

allow the party with the greatest bargaining strength to dictate the contents of the clause. In the latter case, a negotiator must know which provisions are essential and which are not.

Beyond merely including arbitration clauses in individual agreements, however, companies may wish to consider the desirability of establishing arbitration and alternative dispute resolution (ADR) programs. Most companies have numerous types of contracts – consumer contracts (often standard-form agreements with thousands of people), distribution agreements, franchise agreements, supplier contracts, sales agreements, commercial agreements of various sorts (sometimes with competitors), and unusual agreements such as those involving large projects and sales or purchases of substantial assets. Each of these agreements involves different considerations for dispute resolution clauses, and different arbitration clauses should be crafted for each. In addition, a multi-tiered ADR clause may be appropriate for major projects.

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