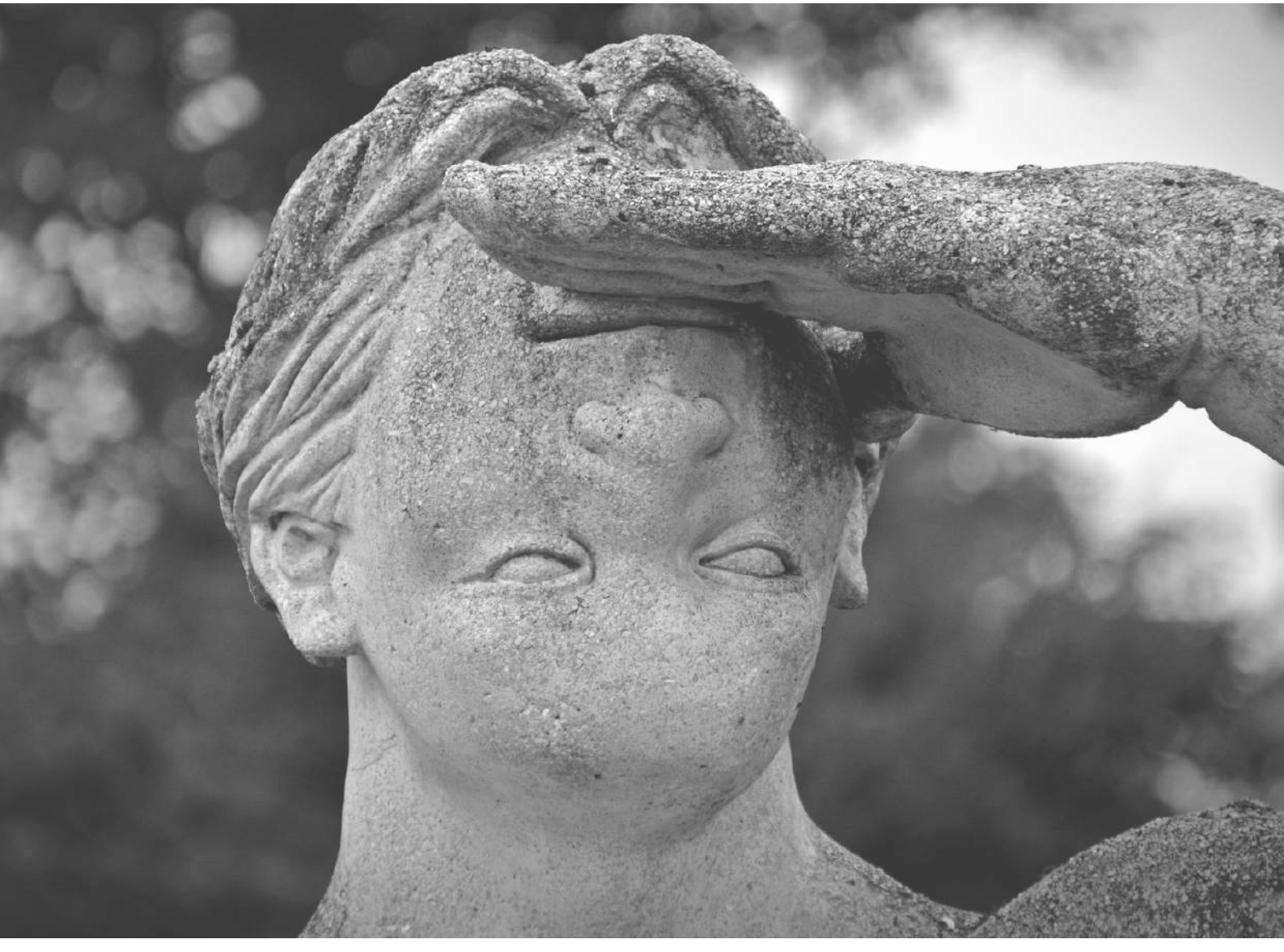
Arbitration Agreement Going Wrong

No one wants to see a dispute go sideways. Neither do we, hence the warning: no recourse to arbitration is possible without a properly constituted arbitration agreement. In practice, we have seen various companies use similar arbitration clauses that do not disclose the most essential terms of the arbitration proceedings. A wrongly drafted arbitration clause may cause a dispute to become unresolvable in arbitration. In this article, we have tried to point out the most common mistakes made when drafting an arbitration agreement.



ARBITRATION AGREEMENT MISTAKES

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Arbitration, as an effective alternative dispute resolution mean, is actively used by parties to legal relations, in particular by foreign investors. An arbitration agreement is a prerequisite for arbitration and is essential for arbitration to take place. The content and correctness of the agreement largely determines arbitrability of a dispute. Therefore, a proper arbitration agreement draft is a crucial task at the contractual or separate document stage when a dispute is to be submitted to arbitration.

In practice, many problems with arbitration are due to the lack of awareness of the nature, role, and operation of arbitration.

In the Republic of Kazakhstan, arbitrations may exist in the form of arbitrations formed specifically to deal with a particular dispute ("ad hoc arbitrations") or as permanent institutional arbitrations.

The International Arbitration Centre under the Astana International Financial Centre is of particular interest, which is not subject to national arbitration law and which is governed by the Arbitration and Mediation Rules, AIFC-approved. Regardless of arbitration type, an appeal is only possible if there is a duly drafted arbitration agreement between the parties to the proceedings.

Pursuant to Article 2(8) of the Law of the Republic of Kazakhstan "On Arbitration" of 8 April 2016, an arbitration agreement is a written agreement between the parties to submit a dispute which has arisen or may arise from civil law relations.

Entering into an arbitration agreement, the parties themselves waive the right to apply to a state court, undertake to comply voluntarily and bindingly with the terms of the arbitral award, and agree on its finality. When concluding an arbitration agreement, the parties must agree on the arbitration terms, such as arbitral tribunal (its title in the case of a permanent arbitration), place, language, applicable law, constitution, and the rules of the arbitral proceedings.

Normally, all permanent arbitrators recommend using their own arbitration clause. By their clauses and unless otherwise agreed by the parties, permanent arbitrators submit the terms of the arbitral proceedings to their own rules, which specify all necessary procedural details.

THE FORM OF THE ARBITRATION AGREEMENT

From the definition of an arbitration agreement comes the form it should take. As agreed by the parties, an arbitration agreement may be contained in a separate clause in a contract (the so-called "arbitration clause") or it may be entered into as a separate agreement independent of the main contract. An arbitration agreement shall also be deemed to be in writing if (1) it is entered into, including by means of an exchange of letters, telegrams, telephonograms, faxes, electronic documents or other documents which identify the parties and evidences their will to submit the dispute to arbitration or (2) it is entered into through an exchange of statement of claim and statement of defense in which one party states that there is an agreement and the other does not object. In our experience, the most common form of an arbitration agreement is a separate clause in a contract signed by both parties.

However, in practice, we have dealt with the use of identical arbitration clauses by different entities, which do not contain all the terms of the arbitration and therefore do not work. The fact that one and the same clause taken from the internet is used indicates negligence in the drafting of the arbitration agreement. In the meantime, such arbitration clauses cause problems later on that significantly slow down the arbitral process and sometimes make it impossible to arbitrate the dispute at all.

THE MOST COMMON MISTAKES IN DRAFTING AN ARBITRATION AGREEMENT IN PRACTICE

I. The arbitration agreement does not refer to a particular arbitration or refers to a non-existent arbitration.

Often, intentionally or unknowingly, parties choose a non-existent arbitration or fail to name a particular arbitration with the authority to resolve potential disputes. This also applies when parties indicate the name of an arbitration in a wrong way or when the names of different arbitrations are confusingly similar. As a result, the parties are unable to apply to either the arbitral tribunal or a state court for the resolution of the dispute. However, there is a way out of this situation and it is as follows:

1) if the parties to the arbitration are located in a country party to the European Convention on International Commercial Arbitration of 21 April 1961 (hereinafter the "European Convention"), the claimant must apply to the President of the competent chamber of commerce of the respondent country or to a special committee, whose composition and nature of activities are defined in the Annex to the European Convention, with a request to appoint arbitration to decide the dispute.

2) where the parties to the proceedings are not parties to the European Convention, the claimant shall request the respondent to conclude a supplementary agreement on the terms of the arbitration not regulated by the current arbitration agreement. If the respondent does not agree to or ignores the request to settle the terms of the arbitration, the claimant shall be advised to apply to a national court. This right derives from the provision of Article 10 of the Law on arbitration: "the court before which an action in the subject matter of the arbitration is brought shall, if either party so requests, refer the parties to arbitration not later than the submission of its first statement on the merits, unless it finds that the arbitration agreement is invalid, inoperative or unenforceable". That is, in order to subject potential disputes with an arbitration clause to the jurisdiction of a state court, the court must prove the invalidity and unenforceability of the arbitration agreement due to the lack of an arbitral body specified in the arbitration agreement.

II. Expanded interpretation of the scope of the arbitration clause.

Expanded interpretation of the scope of the arbitration clause.

The Law on arbitration's definition of an arbitration agreement provides for the submission to arbitration of a dispute which has arisen or may arise out of a civil-law relationship. However, not all disputes arising from civil law relations are competent for arbitration. The term "civil relations" itself is quite broad and includes non-contractual disputes that may arise outside of the contract in which the arbitration clause is included. By entering into an arbitration agreement, however, the parties usually refer to arbitration jurisdiction to resolve disputes that may arise directly in connection with the performance, breach, invalidity or termination of a contract, rather than to civil law relations in general. Pursuant to Article 20 of the Law on arbitration, it is up to the arbitral tribunal to decide whether or not it has jurisdiction to hear the dispute submitted to it. If the scope of the arbitration clause is interpreted broadly, there is a risk that the claim will be returned if the arbitral tribunal decides that it is not competent to resolve the dispute.

Moreover, in the event it becomes necessary to apply to a state court for enforcement of an arbitral award, the court may refuse to issue a writ of execution on the grounds that "the award was made on a dispute not provided for in or not covered by the arbitration agreement, or contains rulings on matters outside the scope of the arbitration agreement, and because the dispute is not within the jurisdiction of the arbitral tribunal". It is therefore recommended that the arbitration clause be extended directly to the contract and to disputes that may arise under the contract.

III. Failure to state the applicable law in the arbitration agreement

Expanded interpretation of the scope of the arbitration clause

The applicable law is also an important condition of the arbitration agreement. As a general rule, where a Kazakhstani permanent arbitration tribunal is chosen and the arbitration is subject to its rules, the applicable law is that of the Republic of Kazakhstan. .

However, in the absence of a reference to this condition of the arbitration process, the European Convention solves this problem in the following way: "the law chosen by the parties and, in the absence thereof, the law of the country where the award is to be made shall apply to the arbitration agreement.

However, if the parties have not specified the law applicable to the arbitration agreement and it cannot be ascertained in which country the award is to be made, the court shall determine the applicable law by reference to the conflict-of-laws rule of the country where the case is brought.

The International Arbitration Centre, for example, regulates the matter in such a way that, in the absence of an agreement on the applicable law, the Arbitral Tribunal shall apply the law that it considers most appropriate to the circumstances of the case and the main purpose. Also, the International Arbitration Centre follows the rule that any designation by the parties of the law of a given state shall be deemed to refer to the substantive law of that state and not to its conflict-of-laws rules. Notably, in Kazakhstani practice, the issue of applicable law still needs to be regulated.

In order to avoid these and other problems, we recommend researching the experience and rules of permanent arbitrations before entering into an arbitration agreement, choosing an arbitral body with an impeccable reputation, agreeing on the essential terms of the arbitration process, and becoming familiar with the list of arbitrators. When adopting its own rules, each arbitral tribunal shall specify all necessary procedural matters. Therefore, to minimise the risks that may arise from omissions in the arbitration agreement, it is advisable to choose specific rules, and to submit the arbitration to the rules of those rules. Arbitration has many advantages and guarantees a fair arbitration award, provided the arbitration agreement is drafted correctly and in full.

We are always happy to assist with the drafting of the arbitration agreement and the representation in the arbitral proceedings.