Mikhail Kartuzov, PhD in Law, Attorney at Law
National University "Odesa Law Academy", Ukraine

ADVANTAGES AND DISADVANTAGES OF INTERNATIONAL COMMERCIAL ARBITRATION IN COMPARISON TO LITIGATION AND OTHER MEANS OF DISPUTE RESOLUTION

The Article is devoted to a research of the advantages and disadvantages of the International Commercial Arbitration in comparison to litigation and other methods of alternative dispute resolution. In the Work is researched the history of International Commercial Arbitration, the fundamental features of the International Commercial Arbitration, the essence of advantages of the International Commercial Arbitration and its disadvantages, the peculiarities of regulation and procedures of the International Commercial Arbitration in comparison with the procedures of the national courts. Despite the potential disadvantages associated with the International Commercial Arbitration, it remains a popular choice of dispute resolution for parties. The various advantages and disadvantages identify that whether the International Commercial Arbitration is a practical route in comparison to litigation or other Methods of Alternative Dispute Resolution will largely depend on the facts and circumstances of each dispute.

Key words: International Commercial Arbitration, Litigation, Alternative Dispute Resolution, Advantages, Disadvantages, Arbitration award, Enforcement, Procedure, Interim measures, *Res judicata*.

Arbitration, as a method of dispute resolution, was well established under Roman Law by the first century BC. Under Roman Law the parties of a dispute entered into an agreement, called a *compromissum*, to submit to arbitration and abide by the arbitration award[1]. One of the famous Roman author - Cicero - considered arbitration as "mild and moderate" as against litigation, which he considered to be "exact, clear-cut and explicit"[2].

In England, for several centuries, the prominent view is that the disputes get in the way of trade and the swift resolution of disputes benefits trade. In 1475 the Chancellor of the Star Chamber said[3]: "*This dispute is brought by an alien merchant… who has come to conduct his case here, and he ought not to be held to await trial by twelve men and other solemnities of the law of the land but ought to be able to sue here from hour to hour and day to day for the benefit of the merchants*". In the preamble of the first English Arbitration Act of 1698 is to be found the confirmation that the arbitration is specifically enacted for the benefit of trade[4]: "*Now for* ***promoting trade*** *and* ***rendering the award of arbitrators more effectual in all cases****, for the* ***final determination of controversies referred to them****, by merchants and traders, or others, concerning matters of account or trade, or other matters*". These three objectives have remained the core of the International Commercial Arbitration[5], which distinguish the International Commercial Arbitration from Litigation and other Means of Dispute Resolution.

Analysing the core objectives of the International Commercial Arbitration it is absolutely necessary to specify the fundamental features of the International Commercial Arbitration, which help us to define its advantages and disadvantages. Lew, Mistelis and Kroll defined four fundamental features of the

[1] Lord Hacking, D. (2000). Dispute Resolution in London. *The Journal of the Chartered Institute of Arbitrators, vol. 66, 3*.
[2] Barrett, J.T., Barrett, J.P. (2004). *A History of Alternative Dispute Resolution: The Story of Political, Cultural, and Social Movement.* San Francisco: Jossey-Bass.
[3] Potter, H. (1943). *An Historical Introduction to English Law and its Institution*. 2nd edition, London: Sweet & Maxwell, 160.
[4] Lord Hacking, David (1997). Arbitration Law Reform: The Impact of the UNCITRAL Model Law on the English Arbitration Act 1996. *The Journal of the Chartered Institute of Arbitrators, Vol. 63, 4*.
[5] Lord David Hacking. (1999). Arbitration Law Reform in Europe. *The Journal of the Chartered Institute of Arbitrations, vol. 65, 3, 1/6.*

International Commercial Arbitration[1]:

1. An alternative to national courts;
2. A private mechanism for dispute resolution;
3. Selected and controlled by the parties;
4. Final and binding determination of parties' rights and obligations.

1. An alternative to national courts

The most obvious forum for all disputes is system of national courts, which exist and are maintained by the state to defend the parties' rights and interests. It is a responsibility of the state to ensure that national courts work properly, that there are procedural rules to regulate the basis of jurisdiction and the conduct of cases before the court.

The International Commercial Arbitration is not part of the national court system. It is a quasi-judicial institution, special device, which derive its power from a private agreement of the parties, who remove their dispute from the jurisdiction of national courts.

2. A private mechanism for dispute resolution

If the national courts are public, the International Commercial Arbitration is generally private, as every contract between parties. Nevertheless, the enforcement of the arbitration award as the enforcement of the decision of the national court was ensured by the state power.

3. Selected and controlled by the parties

The principal characteristic of the International Commercial Arbitration is that it is chosen and controlled by the parties. Party autonomy is the ultimate power determining the form, structure, system and other details of the arbitration.

4. Final and binding determination of parties' rights and obligations

In the arbitration agreement the parties of the dispute should agree that the arbitrators should resolve the dispute finally. The parties have accepted that not only will arbitration be the form of dispute settlement, but also that they will accept and give effect to the arbitration award. Implied with the agreement to arbitrate is the acceptance that the strict rules of procedure and rights of appeal of a national court are excluded, subject to very limited, but essential, protections. The arbitration award is final and binding on the parties. This is both a contractual commitment of the parties and the effect of the applicable law.

These fundamental features of the International Ccommercial Arbitration highlighted its advantages and disadvantages in comparance with the National Courts and other mechanisms of Alnernative Dispute Resolution.

According to the statement which was made at inauguration of "the City of London Chamber of Arbitration" (the predecessor of the London Court of International Arbitration) on 23.11.1882 the Speaker defined the main ideas about wanted advantages of the International Commercial Arbitration in comparison with litigation: "*This Chamber is to have all the virtues which the law lacks. It is to be expeditious where the law is slow, cheap where the law is costly, simple where the law is technical, a peacemaker instead of stirrer-up of strife*"[2].

For the Ukrainian companies the main advantage of the International Commercial Arbitration is *Easy enforcement of the Arbitration Award:* Both domestic and international arbitration awards should be easily enforceable - in the same way and as simply as a national court judgment. The legal system recognizes that the parties have decided that arbitrators should make the final determination of their dispute as an alternative to the national court. The law therefore gives effect to the intention of the parties and enforces the award just as it would a national judgment. In the international arena arbitration awards are more easily enforceable than national court judgments. As a result of the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards 1958 there are now more than 140 countries which have accepted the obligation to give effect to arbitration awards made in other countries which are party to the New York Convention. There are limited grounds to refuse enforcement. This is far more effective than the enforcement of foreign judgments which are dependent on bilateral conventions (for Ukraine, with limited exceptions, only Convention with CIS countries could be applied).

Suitability for international transactions: Contracting parties from one country are generally

[1] Lew, J.D.M., Mistelis, L.A., Kroll, S.M. (2003). *Comparative International Commercial Arbitration*. The Hague/London/New York: Kluwer Law International, 7.

[2] Lord David Hacking (2000). Dispute Resolution in London. *The Journal of the Chartered Institute of Arbitrators, vol. 66, 3.*

unwilling to submit a claim to the national courts of the other party. The neutrality and independence of the arbitration process, established within the context of a neutral venue, and not belonging to any national system, is a real attraction for the parties for the International Commercial Arbitration as a system to resolve disputes arising from international transactions. As parties are drawn from jurisdictions across the world, with very different legal, political, cultural and ethical systems, International Commercial Arbitration provides a forum in which all of these interests can be protected and respected. In the Resolution of United Nations, adopting the UNCITRAL Arbitration Rules is to be found: "*The General Assembly…being convinced that the establishment of rules for…arbitration, that are acceptable in countries with different legal, social and economic systems, would significantly contribute to the development of harmonious international economic relations…*".[1]

Flexible procedure: A principal factor differentiating a national court from the International Commercial Arbitration is the rigidity of national court procedures. The procedural rules lay down the basis for the courts' jurisdiction, the circumstances in which an action can be brought, how to initiate proceedings, what documents must be filed, the rights of reply and how the case, generally, should be conducted. There are little or no areas on which the judge can, in his discretion, even with the agreement of the parties, move away from the norms of the procedural rules.

By contrast, the form, structure applicable law and procedure of every International Commercial Arbitration is different and will vary according to the characteristics of the case. The arbitrations may be under different rules, with different national or international laws applying, with one or three arbitrators and one or more claimants or respondents. Due to the private nature of the International Commercial Arbitration and that it is established by agreement of the parties, the procedure can be fixed by the parties in the arbitration agreement and arbitrators should to meet the characteristics of each case.

Also, it is necessary to highlight, that all of the major international arbitration rules give authority and power to the arbitrators to determine the procedure that they consider appropriate, subject always to party autonomy. For example, Article 15 of ICC Rules provides:

"*The proceedings before the Arbitral Tribunal shall be governed by these Rules, and, where these Rules are silent, by any rules which the parties or, failing them, the Arbitral Tribunal may settle on, whether or not reference is thereby made to the rules of procedure of a national law to be applied to the arbitration*" (the same rules are to be found in AAA ICDR Rules Article 16(1); LCIA Article 14(2); NAI Arbitration Rules Article 23(2); UNCITRAL Arbitration Rules Article 15(1); WIPO Arbitration Rules Article 38(a))[2].

It is for these reasons that for many types of international commercial arrangements, the International Commercial Arbitration is the preferred mechanism for dispute resolution.

Final and binding: As a general rule the arbitration awards have an effect of *res judicata* and are final and binding. There are no or very limited grounds on which arbitrators' awards can be appealed to the national courts on the basis that the arbitrators' conclusions are wrong. Equally, the grounds upon which the decisions of arbitrators can be challenged and set aside are limited to where the arbitrators have either exceeded the jurisdictional authority in the arbitration agreement or have committed some serious breach of natural justice.

Neutrality: National courts have, or are at least perceived to have, an inherent national prejudice. Judges are drawn from that nationality. They do not necessarily have the knowledge of, or ability to handle, disputes arising from international business transactions or even disputes between parties from different countries, *i.e.* with conflicting legal, cultural, political and ethical systems. The procedure followed in national courts is in accordance with the laws set down by that state. By contrast to the perceived partiality of a national court, an arbitration tribunal is thought to be neutral. It can be established with its seat in a country with which neither party has any connection; arbitrators can be selected from different countries and with different nationalities, and the tribunal is independent of direct national influence. This neutrality gives arbitration independence and a loyalty primarily to the parties.

Expert arbitrators: Particularly for disputes that arise of some special areas (shipping, international carriage of goods, insurance, etc.) or where there is a particular characteristic of the dispute, parties are able to select arbitrators with expert knowledge (lawyer, which specialized in the shipping Law; former captain;

[1] Resolution 31/98 adopted by the General Assembly, on 15 December 1976. http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf (2015, May, 5).

[2] Lew, J.D.M., Mistelis, L.A., Kroll, S.M. (2003). *Comparative International Commercial Arbitration*. The Hague/London/New York: Kluwer Law International, 7

auditor, etc). Whilst, generally, arbitrators are not expected to use their relevant background experience for the purpose of making decisions (that is a function for an expert determination), having specific knowledge and an understanding of the subject-matter will often give increased confidence in the arbitration process.

Confidentiality: Due to the private nature of the International Commercial Arbitration, it is a confidential process. As a result, what proceeds in the arbitration will not only be kept private between the parties but will remain absolutely confidential. This means that the existence of the arbitration, the subject matter, the evidence, the documents that are prepared for and exchanged in the arbitration, and the arbitrators' awards cannot be divulged to third parties. It also means that only parties to the arbitration, their legal representatives and those who are specifically authorized by each party can attend the arbitration hearing.

Time: It is often assumed that arbitration is, or at least should be, quicker than national courts. In theory and in many cases this is absolutely right. In many countries, the national courts have a "reasonable" time-limit, which can lead to such a delay that it can be years before a judgment can be obtained. If the parties are agreed, they can seek the involvement of an arbitrator at very short notice; if they are able to present their cases to the arbitrator within a short period, the whole matter can be resolved with great expedition.

Cost: Due to the inherent advantages discussed above, in principle the International Commercial Arbitration should be less expensive than the national courts. Again, in practice it is not always so. Where arbitrations can be held quickly and the arbitration awards issued with little or no delay, the costs may be significantly reduced in contrast to those of a lengthy court procedure. However, for complicated international commercial arbitrations, particularly before three or more arbitrators, this may not always be the case as in addition to the costs of the lawyers, the parties will also have to pay the significant fees of the arbitrators.

In the same time the International Commercial Arbitration has some disadvantages in comparison with litigation and Alternative Dispute Resolution:

Limits to challenge the arbitration award: Because of the existence of the effect of *res judicata*, there is no right of appeal of arbitration award even if the arbitrator makes a mistake of fact or law. However, there are some limitations on that rule, the exact limitations are difficult to define, except in general terms, and are fact driven.

Limits on tribunal's power to grant preventative or provisional remedies: While the parties can give a tribunal most of the powers enjoyed by the courts, a tribunal does not have the power to grant penal sanctions, for example, for contempt of court. Even if a tribunal has the power to grant a preventative or provisional remedy, such as the power to freeze assets, there may well be merit in an application to a national court if the applicant believes that the tribunal's order would be ignored unless backed up by a penal sanction. There may also be a period of time immediately after the commencement of the arbitration proceedings where no relief is available from the tribunal at all because the tribunal has not yet been appointed. A party seeking pre-emptive remedies will again need to make an application to the national court.

Limit on tribunal's power to join parties and consolidate proceedings in multi-party disputes: Only those parties which enter into an arbitration agreement may be made parties to any resulting arbitration. It is not generally possible to join non-parties to arbitral proceedings or to consolidate two arbitrations (i.e. to hear them together) without the consent of all parties, including the new party joining the arbitration. In cases where consideration to the issue of multi-party disputes is given at the time the contract is drafted, the tribunal can be given powers to consolidate and join related disputes by obtaining advance consent from all the parties involved.

Limits on tribunal's power to speed up the arbitration proceedings: It is rare for a party to obtain an arbitration award on the substance of a claim in the International Commercial Arbitration in the absence of a full hearing at which each party orally argues its case, presents its witnesses and cross-examines the other party's witnesses. A hearing can generally be requested by either party. Fast-track procedures in the International Commercial Arbitration without a hearing are rare. However, where the parties agree at the outset that a very quick resolution of the case may be appropriate where the dispute is clear-cut, they can draft a clause empowering the tribunal to make rulings on preliminary issues. For example, many lenders consider that the issue most likely to arise in a dispute under a loan agreement is whether or not the borrower has defaulted in its loan repayments, and lenders can have a clause included empowering the tribunal to deal with this issue in an accelerated procedure based on the parties limited written submissions

only and without a hearing.

Time: The arbitration process may not be fast, particularly when there is a panel of arbitrators. As an example should be provided the arbitration award from May 2014; this arbitration proceedings have been pending for nearly **eight years** involving a patent license agreement between the technology companies Amkor Technology and Tessera Technologies[1].

Cost: It is routinely argued that arbitration is cheaper than litigation. Although litigation can be costly, many of the costs incurred in litigation are also incurred in arbitration, and additional costs are incurred during the course of a typical arbitration to pay for what is essentially a private judicial system. In 2013 jeweler Tiffany lost $449.5 million, plus interest, costs and attorney fees, in an arbitral proceeding to Swatch SA concerning a failed partnership in which Swatch was to develop watches for Tiffany's brand. The amount of legal fees that Swatch incurred in arbitration - a supposedly cost-effective venue - was more than twice that of the average total fees for patent litigation in federal court, again showing that the common contention that arbitration is inexpensive is often plain false[2].

Despite the potential disadvantages associated with the International Commercial Arbitration, it remains a popular choice of dispute resolution for parties. The various advantages and disadvantages identify that whether the International Commercial Arbitration is a practical route in comparison to litigation or other Methods of Alternative Dispute Resolution will largely depend on the facts and circumstances of each dispute. This includes (but is not limited to):

- jurisdiction governing the dispute;
- the number of parties involved;
- complexity;
- merits of a party's case;
- need for privacy;
- location of other parties' assets.

Parties can either mutually agree upon arbitration after a dispute has arisen, or more commonly, at the time of entering into a particular contract agree to refer all future disputes arising out of that contract to arbitration. Either way, a party should always attempt to assess whether arbitration would be appropriate given the facts and circumstances of the dispute that has arisen or of the types of disputes that could arise. Only on that basis can a party ensure that such dispute will be determined in the most fair, effective and efficient way.

References

1. Barrett, J. T., Barrett, J. P. (2004). *A History of Alternative Dispute Resolution: The Story of Political, Cultural, and Social Movement*. San Francisco: Jossey-Bass.
2. Foldenauer, A. (2014). Big Risks and Disadvantages of Arbitration vs. Litigation. <http://www.injurylawyerofatlanta.com/wp-content/uploads/2014/12/ARBITRATION.Big-Risks-and-Disadvantages-of-Arbitration-vs.-Litigation.CORPORATE-COUNSEL.072914.pdf> (2015, May, 5).
3. Lew, J.D.M., Mistelis, L. A., Kroll, S. M. (2003). *Comparative International Commercial Arbitration*. The Hague/London/New York: Kluwer Law International.
4. Lord David Hacking (1997). Arbitration Law Reform: The Impact of the UNCITRAL Model Law on the English Arbitration Act 1996. *The Journal of the Chartered Institute of Arbitrators, vol. 63, 4.*
5. Lord David Hacking (1999). Arbitration Law Reform in Europe. *The Journal of the Chartered Institute of Arbitrations, vol. 65, 3.*
6. Lord David Hacking (2000). Dispute Resolution in London. *The Journal of the Chartered Institute of Arbitrators, vol. 66, 3.*
7. Potter, H. (1943). *An Historical Introduction to English Law and its Institution*. 2nd edition. London: Sweet & Maxwell.
8. Resolution 31/98 adopted by the General Assembly, on 15 December 1976. <http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf> (2015, May, 5).

[1] Foldenauer, A. (2014). Big Risks and Disadvantages of Arbitration vs. Litigation http://www.injurylawyerofatlanta.com/wp-content/uploads/2014/12/ARBITRATION.Big-Risks-and-Disadvantages-of-Arbitration-vs.-Litigation.CORPORATE-COUNSEL.072914.pdf (2015, May, 5).
[2] Foldenauer, A. (2014). Big Risks and Disadvantages of Arbitration vs. Litigation http://www.injurylawyerofatlanta.com/wp-content/uploads/2014/12/ARBITRATION.Big-Risks-and-Disadvantages-of-Arbitration-vs.-Litigation.CORPORATE-COUNSEL.072914.pdf (2015, May, 5).