

A Lawyer's Primer in Drafting Arbitration Clauses for a Domestic Arbitration

By Kenneth Glasner, Q.C.

The relationship between arbitration and litigation forms part of the subject matter addressed by Newbury, JA in *MacKinnon v. National Money Mart Company*,¹ when she cited Deschamps J. at paragraph 26 in *Dell Computer Corp. v. Union des consommateurs*²:

The neutrality of arbitration as an institution is one of the fundamental characteristics of this alternative dispute resolution mechanism. Unlike the foreign element, which suggests a possible connection with a foreign state, arbitration is an institution without a forum and without a geographic basis ... Arbitration is part of a no state's judicial system ... the arbitrator has no allegiance or connection to any single country ... In short, arbitration is a creature that owes its existence to the will of the parties alone ...

To say that the choice of arbitration as a dispute resolution mechanism gives rise to a foreign element would be tantamount to saying that arbitration itself establishes a connection to a given territory, and this would be in outright contradiction to the very essence of the institution of arbitration: its neutrality. This institution is territorially neutral; it contains no foreign element. Furthermore, the parties to an arbitration agreement are free, subject to any mandatory provisions by which they are bound, to choose any place, form and procedures they consider appropriate. They can choose cyberspace and establish their own rules.

While arbitration offers significant advantages over litigation, poorly drafted clauses lead to costly and time consuming delays and fail to meet the intentions and expectations of the parties - in particular the businessmen who have entered into contracts to achieve some rational commercial purpose. Lawyers should devote the same attention to a dispute resolution clause as they do in any other fundamental term of the agreement.

Agreements to arbitrate are formed:

1. during negotiating a contract, or
2. after a dispute has arisen.

Frédéric Eisemann, former Secretary-General of the ICC International Court of Arbitration, established four essential functions of an arbitration clause. They are³:

1. **An arbitration clause must produce mandatory consequences for the parties;**
2. **It must exclude the intervention of state courts in the settlement of the conflict, at least before an award is issued;**
3. **It must empower the arbitrator to settle the dispute likely to arise between the parties;**
4. **It must allow for the most efficient and rapid procedure leading to an award that is judicially enforceable.**

The preferred system is to negotiate a process prior to entering the main contract and not after acrimony has developed. The arbitration clauses stand separate and apart from the main agreement.⁴

Considerations in domestic arbitration may be different from considerations in international arbitration. The starting point would be to carefully review the statutes which will be applicable in your client's case. Clauses dealing with costs, confidentiality, restrictions to the court and a plethora of other matters must be considered in each case. There are few cases in which one can apply a standard arbitration clause that meets the needs and commercial expectations of the client. In addition, consideration must be given to a set of rules (such as institutional rules) dealing with the process which will govern or whether rules will be decided on ad hoc basis using a bespoke clause, or blending of the two. These are usually referred to as non-institutional arbitration versus institutional arbitration.

I have provided a checklist which includes some of the dos and don'ts in considering arbitration provisions. Some of these points are set out in an article written by Karen Birch of Allen & Overy LLP in the United Kingdom – some have been gleaned as a neutral.

Do

1. have a clear, unequivocal agreement to arbitrate.
2. consider the dispute resolution clauses early in negotiations.
3. consider whether to include a formal pre-arbitration procedure, eg mediation.

4. make an informed choice between institutional and ad hoc arbitration and read any relevant rules. In British Columbia direct your attention to section 22 of the *Commercial Arbitration Act* (“Domestic Act”). These make the BCICAC rules applicable unless otherwise agreed or inconsistent with an enactment.
5. specify the “seat” or formal place of arbitration – sometimes referred to as “the place” or “the forum”.
6. specify an odd number of arbitrators, the manner of appointment, and if it’s an ad hoc arbitration the appointing authority.
7. specify the language of arbitration.
8. consider the scope of the agreement to arbitrate.
9. specify the governing law.
10. consider whether a waiver of appeal of decisions of the tribunal is desirable and enforceable. Subject to the applicable arbitration legislation (See sections 23, 31, and 35 of our Domestic Act) the parties should clearly state their intentions with respect to appeals. The joint intention may include that the decision of the arbitrator shall be final and binding and shall not be subject to appeal on a question of fact, law or mixed fact and law. The words, “final and binding” will probably not be sufficient to limit the court’s intervention.
11. consider providing for joinder or consolidation of disputes if it is a multi-party or multi-contract situation as in a construction dispute. This will require the parties who are not party to the agreement to “buy in” and subject to the other parties consent. But also see *Xerox Canada Ltd. and Xerox Corporation v. MPI Technologies Inc. and MPI Tech S.A.*^A.
12. obtain an understanding of your client’s business including whether or not products or services sold are within the province, the country, or a foreign state. Is this a situation where the dispute involves intellectual property (“IP”) where speed for resolution may be paramount.

13. consider the nature of relief an arbitrator may impose having regard to the law in a particular jurisdiction and where possible expand the arbitrator's powers.⁵
14. what is the effect of an arbitration clause in one agreement where the parties have other agreements that may exist between the parties.⁶
15. read and understand the relevant legislation and the institutional rules.
16. understand how the issue of costs is dealt with by the Domestic Act and the agreement with respect to costs contained in the contract.⁷
17. consider including a time limitation clause for giving or filing a notice to arbitrate

DO NOT

1. assume that dispute resolution provisions do not really matter.
2. assume that arbitration is the best option for all disputes.
3. assume that all jurisdictions are supportive of arbitration.
4. blindly adopt an arbitration clause from another agreement.
5. draft an arbitration clause without examining the rest of the agreement and related agreements. Ensure that if your clauses amend or expand the institutional rules that there is no ambiguity or inconsistency.
6. choose more than one governing law or seat. It is important to remember that the substantial rights may be different from the procedural law ("lex loci arbitri"). Generally the seat of the arbitration will be the lex loci arbitri. This is one of the reasons why Canada is most suited for international arbitration.
7. choose arbitration rules that are inconsistent with the arbitration clause without specifying that such rules are being amended by agreement.
8. assume that "split clauses" (which provide for one party to have the option to arbitrate or litigate while the other party can only litigate) are valid in all jurisdictions.
9. include restrictive criteria for the qualifications of arbitrators that may make it difficult or impossible to appoint suitable arbitrators.

10. specify as an appointing authority a person, position or institution unless you are sure that it exists and will be willing to make the appointment. Do not misname the institution.
11. assume that arbitration will be confidential. If the parties want confidentiality, provide for it expressly.
12. use “may” when you mean “shall”.
13. use a med/arb clause unless you carefully consider the problem solving techniques which may be used by the mediator who will then be your arbitrator if the mediation is unsuccessful.

In Canada, the alpha and omega on drafting ADR clauses can be found in the Carswell Publication entitled “Drafting Arbitration Clauses for Commercial Contracts”, prepared and edited by Wendy Earle of BLG in Toronto.

Another excellent arbitration clause checklist may be found at, *The Advocates’ E-Brief*, Vol. 19, No. 3, Spring 2008, written by Barry Leon and Jana Slettnee, of Torys LLP. See <http://www.torys.com/Publications/Documents/Publication%20PDFs/AR2008-43.pdf>.

CONFIDENTIALITY OF ARBITRATION AWARDS

One of the benefits of private arbitration is the possibility that not only the process attendant upon the arbitration is confidential but also the award. In cases where the award is being reviewed by the court a request may be made to the presiding judge that the award be sealed. Clearly the presiding the judge in his or her reasons would be careful on how they express their views on the contents of that award.⁸

The importance of confidentiality was raised recently in *John Forster Emmett v. Michael Wilson & Partners Limited*.⁹

In drafting a confidentiality clause consideration should be given:

1. On whether the issue of confidentiality is recognized by the law of the venue of the arbitration.
2. If the governing arbitral body has a confidentiality provision included in their rules.
3. To include a provision that the award is not subject to an appeal on a question of fact, law or mixed fact and law.

There are other circumstances in which an award may lose its cloak of confidentiality.

Some of those are:

1. The subject matter in dispute must be reported as material to the financial condition of a public company.
2. Disclosure may be required by shareholders, partners, creditors and others having a legitimate business interest.
3. One or more parties may be subject to a fiduciary duty to disclose.
4. Parties may have a duty of disclosure to their insurers.
5. Parties may be obliged to disclose evidence from the arbitration in a subsequent proceeding.

Consideration of these factors will help you design the most appropriate confidentiality clause as it relates not only to process but also to the award.

UNCONSCIONABILITY

Arbitration clauses have become common place in national and international consumer contracts – contracts of adhesion (take a look at your credit card contract). Coupled with this proliferation of “standard contracts” is that many arbitration clauses are very favourable to issuer of the card. A number of these arbitration clauses have been considered by the American courts as unconscionable. Paul Marrow, in his article *Policing Contracts for Unconscionability: Guidelines for International Arbitrators Subject to the Scrutiny of US Courts*,¹⁰ sets out criteria dealing with procedural and substantive unconscionability.

Under the heading of procedural unconscionability factors to be considered are:

- 1. Is the contract standard form?**
- 2. Is the suspect clause boilerplate?**
- 3. Was the clause hidden or made non-conspicuous?**
- 4. Is the language used incomprehensible to a lay person?**
- 5. Was there gross inequality in bargaining power?**
- 6. Was there exploitation of a weakness such as lack of sophistication or education?**

Under the heading of substantive unconscionability, the factors are:

1. **significant price disparity;**
2. **private penalties;**
3. **a denial of a basic right or remedy;**
4. **liquidated damages;**
5. **disclaimers;**
6. **covenants not to compete;**
7. **limitations on remedies;**
8. **absence of mutuality concerning access to the judicial system;**
9. **pre-dispute mandatory arbitration.**

CAVEAT

In July 2009, in the decision of *Bell Canada v The Plan Group et al*, the Ontario Court of Appeal¹¹ had the opportunity to deal with the failure by one party to an arbitration to follow the then current rules of the Arbitration and Mediation Institute of Ontario by failing to commence the arbitration process pursuant to those rules, including payment of the Institutes' fees.

The Court found that under the agreement, Plan Group failed to follow the process agreed to by the parties, with the result that they were barred from claiming by arbitration a substantial sum of money from Bell Canada. The Plan Group case cited an earlier decision of the Ontario Superior Court of Justice between *Spectra Innovations v Mitel Corporation*¹² where that court found that a party could not pick and choose which rules of the ICC to follow.

In British Columbia in the absence of specifically drafted rules and protocols contained within a contract the parties are obliged to follow section 22 of the *Commercial Arbitration Act*. Notwithstanding those rules the parties may, by consent, amend those rules to meet the particular situation, provided firstly that they commence the proceedings and follow the initial protocols set out in section 8 of the rules, which include submitting an arbitration notice and paying the commencement fee.

BRITISH COLUMBIA INTERNATIONAL COMMERCIAL ARBITRATION CENTRE (BCIAC)

BCIAC was established by the Provincial Government in 1986. BCICAC rules govern domestic arbitration pursuant to section 22 of the Domestic Act. The entity is also referred to in the *International Commercial Arbitration Act of British Columbia* and in numerous national and international articles which refer to regional arbitration institutions.

The advantages of using BCICAC include:

1. Pre-establish rules and procedure
2. Administrative assistance, including the handling of arbitrators fees and disbursements
3. Lists of experienced arbitrators
4. The appointment of arbitrators

Part of the history of BCICAC can be found in the comments regarding the development of arbitration in British Columbia in *Commercial Arbitration in Canada: A Guide to Domestic International Arbitration (2007)* by J.K. McEwan and Ludmila Herbst as cited in *Mackinnon (Supra)*:

British Columbia was the first jurisdiction to adopt the Model Law anywhere in the world. British Columbia was particularly interested in attracting arbitration business as is reflected in the preamble to its International Commercial Arbitration Act, which was essentially a reworked version of the Model Law.

...

British Columbia took a leadership role in enacting new domestic commercial arbitration legislation as well. In this regard, the Law Reform Commission of British Columbia issued a Report on Arbitration in 1982 recommending the adoption of modernized legislation. The report has been described as the first proposal for modernizing the legislative regime then in place throughout common law Canada. Legislation influenced in part by the Model Law was drafted and enacted

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INTERNATIONAL ARBITRATION

The International Arbitration arena differs significantly from that of the Domestic arena and as such could occupy an article on drafting at least twice the length of this one.

International Arbitration agreements are different¹³:

- different laws
- different courts
- different legal cultures
- long distance logistics
- danger of duplicating process
- treaty in international convention
- state controlled issues
- enforcement

CONCLUSION

There are a number of publications available to the drafter; the following three which I suggest would form the foundation of essential reference material. They are:

1. *Drafting ADR and Arbitration Clauses for Commercial Contracts*, by Wendy Earle, Carswell
2. *Commercial Arbitration in Canada (A Guide to Domestic and International Arbitration)* by McEwan and Herbst, Canada Law Book
3. *Arbitration Law of Canada: Practice and Procedure*, BY J. Brian Casey, Juris Publishing Inc.

ENDNOTES

1. *2009 BCCA 103*
 2. *2007 SCC 34*
 3. *Gowlings Guide to International and Domestic Arbitration and ADR, 2006 by Robert Nelson*
 4. *Premium Nafta Products Limited v. Fili Shipping Company Limited*, [2007] UKHL 40
 5. *Premium Brands Operating GP Inc. v. Turner Distribution System Ltd.*, S097601, Van. Registry; May 26, 2010, Russell J.; also March 1, 2010, Pearlman J.
 6. *Dancap Productions Inc. et al v. Key Brand Entertainment Inc. et al and Ed Mirvish Enterprises Limited* 2009 ONCA 135
 7. *Four Seasons Hotels Ltd. v. Pacific Centre Ltd.*, 2002 BCSC 148; January 31, 2002, Neilson J.
 8. *Telesat Canada v. Boeing Satellite Systems International Inc.* [2010] O.J. No. 35, Hackland J.
 9. [2008] EWCA Civ 184
 10. *Arbitration, Vol. 73, No. 4, November 2007*
 11. 2009 ON CA 548
 12. [1999] O.J. No. 1870
 13. *Arbitration Agreements*, Federated Press Conference, October 15, 2008 William G. Horton
- ^A 2006 Can LII 41006 (ON S.C.)