Pathological Arbitration Clauses: How to Avoid, Recognize, and Deal With "Less-than-perfect" Arbitration Clauses

Guest Speakers: Matthew Kindree and Christina Doria
Moderators: Michael Erdle and Tricia-Jo Lewis

By: Mary Korica

On November 19, 2013, the Commercial section of the ADR Institute of Ontario ("ADRIO") held the live program and webinar "Pathological Arbitration Clauses" with speakers, Matthew Kindree and Christina Doria, from Baker & McKenzie, and Michael Erdle as Moderator.

The seminar discussed recurring problems in arbitration clauses, and how arbitrators might have a role in dealing with pathological clauses. The speakers chiefly referenced the ADR Institute of Canada National Arbitration Rules ("ADR Rules").

Mr. Kindree, a solicitor, began by discussing the purpose and anatomy of the arbitration clause. He noted that parties to contracts usually agree to include provisions for arbitration in commercial agreements based on lawyers' advice that arbitration is a faster, less expensive and more confidential process to deal with disputes rather than litigation. This establishes the parties' expectations in the event of arbitration. However, given that corporate counsel are often unfamiliar with the arbitration process and given people's tendency to begin ventures with careful attention to provisions for goals being achieved rather than things going wrong, arbitration clauses are often included perfunctorily and are not clear, concise and complete. This can lead to difficulties in an eventual arbitration process and in meeting parties' expectations.

Four key questions were outlined for approaching any arbitration: What is the issue to be arbitrated? How is it to be arbitrated (including procedure and timing)? Where should it be arbitrated? and by whom should it be arbitrated? He noted that the arbitrator(s) will likely confront issues of process, timing, and scope.

The arbitrator's role, and what he or she can do to manage the process, was addressed by Ms. Doria, a litigator. She identified the arbitrator's role as: (i) being independent and impartial; (ii) being adjudicative; (iii) establishing and administering the arbitral process; and (iv) possibly having the power to sanction. She described ways of dealing with imperfect arbitration clauses, referencing the arbitrator's role as provided in the ADR Rules.

The ADR Rules require arbitrators to be independent and impartial so as to protect the integrity of the process and provide the parties with a fair decision. Ms. Doria emphasized that it is key to spot problems at the outset, for example, noting whether the arbitration clause provides that the parties "may" or "shall" arbitrate. If the arbitrator's jurisdiction is not clear, her first step should be to decide, in accordance with her adjudicative role, and in consultation with the parties, whether he or she has jurisdiction.

Ms. Doria pointed to Rule 1 of the ADR Rules, which states that:

"The purpose of the Rules is to enable the parties to a dispute to achieve a just, speedy and cost effective determination of matters in dispute, taking into account the values that distinguish arbitration from litigation."

Ms. Doria stated that this rule may be a basis for the arbitrator to take a "muscular" approach in the interest of ensuring that counsel or parties do not abuse the process and that the process runs according to the parties' goal of efficiency (implicit in their agreement to arbitrate under the ADR Rules).

Ms. Doria pointed out that, while opinions differ, one view is that arbitrators – to meet their duty to ensure the fairness of the process and protect an eventual award from annulment – have the power to sanction parties, within limits. She described cases of parties refusing to deliver documents or fabricating documents, as situations where sanctions might be appropriate. Reference was made to rule 23 which allows the Tribunal to conduct the arbitration in the manner it considers appropriate, requires that each party be treated fairly, and requires the Tribunal to strive to achieve a just, speedy and cost effective proceeding, taking into account Rule 1.

Mr. Kindree presented real life examples of "pathological

clauses", demonstrating indeterminate duties, unrealistic timing, unrealistic or unspecified discovery and a vague scope of arbitrable disputes. For example: he addressed clauses that required the completion of "good faith" negotiations before arbitration can commence; the condition that parties "shall in good faith deliver documents"; and a clause where the award had to be made within 45 days after the notice of arbitration. He noted that a party to an arbitration may want to delay the process or challenge the final outcome, and therefore exploit nebulous terminology.

Indeterminate Duties: Mr. Kindree agreed with an audience member who suggested that the arbitrator could have the parties sign a new submission to arbitration that addressed the flaws present in the initial agreement. He also recommended that the arbitrator could suspend the arbitration and order the parties to negotiate in good faith within a set time period. Although this might not ensure parties would return believing that the good faith criterion had been met, it would nonetheless provide the arbitrator with jurisdictional authority.

Unrealistic Timing: The presenters noted that arbitration provisions can set an unreasonable time period for the arbitration process, for example by tying the period for final resolution to the time of dispute notice. This risks the process extending past the allotted time and creating grounds for challenging the final award. Ms. Doria recommended that in such cases the arbitrator meet with the parties to agree to a more reasonable timeframe, and ensure that the lawyers are communicating with the parties on such decisions. She noted that the ADR Rules allow the arbitrator to extend or abridge time limits, except the timeframe for making the award (which under the Rules, must be made within 60 days after the close of hearings). Mr. Kindree cautioned that it is very difficult to anticipate all the issues that might arise within an arbitration or outside of it that might impact on the process, and that timelines are often underestimated.

Unspecified Discovery: Ms. Doria mentioned that if an arbitration clause requires extensive discovery, the arbitrator can return to the intent outlined in ADR Rule 1 which suggests that the process should not be run in the same manner as litigation. She recommended discussing with the parties what should be included, and noted that there can be differing expectations among counsel, especially in international cases. However the arbitration tribunal has the power to decide the scope of disclosure of documents, and arbitrators have tools at their disposal to help guide discovery, including the International Bar Association Rules on the Taking of Evidence, and employing a Redfern Schedule.

Overall, the speakers recommended that arbitrators use the pre-arbitration meeting provided for by the ADR Rules to clear up procedural matters with the parties, including establishing timelines, and identifying issues. The pre-arbitration period can also be used by the arbitrator to issue procedural orders to address problematic matters. The presenters emphasized that it is incumbent on the arbitrator to effectively manage the process.

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