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Arbitration in the Financial Services Sector – Camilla Macpherson

As Head of Secretariat for PRIME Finance, an organisation set up amongst other things to encourage the use of arbitration to resolve complex financial disputes, I am particularly pleased to speak on this panel.

Traditionally, disputes in the world of finance have been settled in the national courts of the major financial centres, with the English courts perhaps leading the way. Is this now changing? Is there a real shift towards arbitration? I am going to spend my time looking at the following:

- Does the data evidence a shift?
- Why the change in approach?
- What are the remaining barriers?
- The impact of Brexit.

Data – what does this tell us?

Starting with the data.

There is quite a lot of number-crunching in the world of arbitration. Statistics on cases are collected by many arbitral institutions. Queen Mary University also produces a highly regarded annual survey which seeks to pick up trends.

Take the Queen Mary 2013 International Arbitration survey. In this survey, litigation ranked as first choice for banks, with 82% of respondents saying they would usually opt for the courts. That said, 69% of respondents considered arbitration well-suited to the sector – there was no great in principle objection.

When we come to their 2018 survey, we see rather more enthusiasm, with over half of respondents predicting the increased use of arbitration in the banking and finance sector.

But surveys are one thing. They do not always reflect reality. They can only tell us what a particular group of respondents think (who is in that group?) about a particular question (which was no doubt carefully phrased).

Perhaps more striking therefore are statistics from the LCIA – the London Court of International Arbitration:



- In 2017, the LCIA reported that 24% of its cases came from the banking and finance sector, and 24% of contracts (indeed the **majority** of contracts) under dispute were loans or other facility agreements.
- The numbers increased in 2018, with 29% of cases coming from the banking and finance sector, and loan and other facility agreements being the most common agreements to be disputed.

This looks like more promising evidence of the growth of arbitration in the FS sector. Data from the Hong Kong International Arbitration Centre, the ICC and the Singapore International Arbitration Centre shows more modest growth, but growth all the same.¹

The LCIA's success rests in part on the following:

- London is a well-established financial hub with many banks based in the City;
- many finance documents are governed by English law because it is seen as being practical, commercial and fairly predictable; and
- English-seated arbitration is often a convenient choice.

It is a small leap from this to choosing the LCIA Rules.

If we are to believe the numbers, it does seem to be the case that, whilst litigation is perhaps still the preferred option in the financial services industry, the benefits of arbitration are increasingly being recognised. I leave it to subsequent speakers to contradict me.

Why the change in approach?

There are a lot of reasons for the shift. Some relate to the type of business being done in the financial markets. Some are a simple function of increased understanding in the sector about how arbitration works and what the benefits are. There is an overlap between the two. For example:

- 1. Claims involving financial products can be very complex. In derivatives disputes in particular, there is a real need for arbitrators with a high level of understanding of the documents and practices of the market. Parties to an arbitration generally have some say in who hears their dispute and will therefore be able to choose someone with appropriate

¹ HKIAC: 2017 - 6%; 2018 – 12%; ICC: accounts for 5% to 8% of cases; SIAC: 2017 – 4%; 2018 – 10%.



expertise. This is not generally the case in the court system. The 2013 Queen Mary survey found expertise of the decision-maker to be the number one benefit of arbitration. This

was particularly the case in the FS sector, because of the technical nature of many of the cases. I can't let this moment pass by without noting that of course it was with this very much in mind that PRIME, with its panel of experts in just these types of claim, was established in 2012.

- 2. Enforcement. One of the major advantages of arbitration is the relative ease of enforcement of arbitral awards. The New York Convention is the instrument by which arbitral awards are enforced in foreign jurisdictions. The process under the New York Convention – and the large number of signatories to the Convention – can make enforcement of an arbitral award easier in many jurisdictions than enforcement of a court judgment. Particularly where counterparties are in emerging markets, arbitration therefore provides greater certainty of enforcement for banks as well as a neutral forum – banks do not have to litigate in local courts.
- 3. Education within the market. In 2016, a report from the ICC task force on financial institutions and international arbitration flagged an overall lack of awareness of the benefits of arbitration as well as misconceptions about the process. That had in fact already started to change with the publication of ISDA's 2013 arbitration guide. This was an important step both in educating market participants in the advantages of arbitration and in providing model arbitration clauses to be used (11 clauses at that time – 3 of which provide for arbitration in accordance with the PRIME Finance Arbitration Rules – the difference being in the choice of seat – London, NY or here in The Hague). In 2018, ISDAS expanded its roster of arbitration clauses to cover 16 different arbitration centres. The arbitration industry generally and arbitration practitioners have also done their part in promoting arbitration as an appropriate means of dispute resolution in the area.

What are the remaining barriers?

Again, some of these relate to the industry, and some to the process.



As to the industry:

1. Some cases are quite straightforward and are probably better left to the courts - simple debt collection is a good example.
- 2, Arbitral awards do not have precedent value in the same way as court judgments. Sometimes, banks want a precedent (for better or worse), in order to provide certainty on an issue and shut down future identical or almost identical cases.
3. In some cases, arbitration is just not viable, because the nature of the dispute is not arbitrable – insolvency proceedings are a good example, but also some types of regulatory case.

As to the process:

- One of the attractions of the English courts is the ability to obtain summary or default judgement where a case either has no merit or the other party does not engage in the proceedings. Arbitration does not have a perfect equivalent. However it is a creature of contract and the parties can agree to something fairly similar in effect. Arbitral institutions are also working hard to introduce expedited procedures or quasi summary processes to plug this gap.
- Multiple parties, multiple contracts. There is no doubt that arbitrations with multiple parties and under multiple contracts can be more difficult in arbitration than in the courts. Arbitrators don't have the same case management powers as courts when it comes to consolidating related proceedings and joining parties. Although this can be dealt with in the drafting phase, this is extra hassle compared to just dropping in a court jurisdiction clause. Again, some institutions are introducing rules to simplify matters, but this can still be a problem.

The impact of Brexit

Finally, a word on the impact of Brexit. As with most Brexit-related discussion, there is an element of speculation in what follows.

There is already some data (Practical Law surveys) to suggest that Brexit is causing lawyers and their clients to reconsider their approach to drafting dispute resolution clauses, with some edging



more towards arbitration than might previously have been the case. I don't think this is very surprising.

Much of the concern turns on enforcement of English court judgments within Europe. Currently, English court judgments are recognised and enforced on a predictable basis across the EU in accordance with EU-wide regulations. The post-Brexit regime is less clear and offers less certainty (although it is quite possible that the issues presented by Brexit in this area at least will be resolved in time).

Against this backdrop, arbitration generally – with its enforcement regime, the New York Convention, unaffected by Brexit - begins to look more appealing. But it is not the only option, and a number of commercial courts in mainland Europe see Brexit as an opportunity to take business away from London. It will take time to be sure if Brexit causes a sizeable change in approach – and whether arbitration or something else is the beneficiary – so as with so many things in this area, for the time being it remains a case of 'wait and see'.