ARBITRATING BANKING AND FINANCE DISPUTES - WHAT ARE THE BENEFITS?

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While there has been some growth in the use of arbitration as a means of resolving disputes in the finance sector, court litigation is still by far the preferred-choice of financial institutions in Switzerland. At the SCAI Conference "Arbitrating banking disputes – Are there tangible benefits?" it was discussed how the wider use of arbitration in the finance sector can be promoted and encouraged. This blog post provides a short overview which kind of banking disputes may be suitable and what advantages choosing arbitration may have.

Which types of banking disputes are suitable for arbitration?

First, it is to be addressed for which areas of banking, arbitration could be a suitable alternative.

For a number of reasons, arbitration seems not a suitable choice for disputes with retail customers ("consumer disputes"). On the one hand, the amount in dispute often will be disproportionate to the costs of the proceedings. On the other hand, arbitral awards in such disputes may not be enforceable at the domicile of the customer due to national law providing for the mandatory jurisdiction of its courts. While Swiss law considers such disputes in an international context arbitrable, this does not hold true for some countries. For example, certain banking contracts with consumers such as future trades are not arbitrable under German law (§101 WpHG).

Moreover, there could be difficulties with satisfying the form requirements for an arbitration agreement. For example, including an arbitration clause in the general terms and conditions may raise issues of formal and substantive validity.

These concerns do not apply to contracts with institutional investors or high-net worth individuals providing for investment advisory services or asset/wealth management, agreements with outsourcing providers and vendors, interbank agreements and contracts with states or state-controlled parties. Accordingly, agreeing to submit disputes arising out of these contracts to arbitration could be a viable alternative.

What advantages does arbitration offer?

Arbitration may have significant advantages for Swiss financial institutions. This holds, in particular, true with customers, partners and providers in an international context.

First, an arbitral award is better enforceable than a Swiss court decision. 156 of 193 nations worldwide are member states of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Recognition and enforcement in these states may only be refused based on the limited grounds specified in the Convention. This is an important factor to consider if enforcement potentially would have to be sought in a state outside the EU with a restrictive approach or practice of recognizing and enforcing foreign court decisions.

Second, arbitration provides a higher degree of confidentiality. In contrast to court proceedings, the public and press are not entitled to be present at hearings. This significantly reduces the risk that the press becomes aware of the case. Considering the reputational damage negative or biased press coverage may have, this is a factor speaking strongly in favor of arbitration.

Third, arbitration may be the preferred choice for Swiss financial institutions if the customer or

business partner is not willing to agree to litigation in Switzerland. Arbitration can be invoked as neutral alternative to agreeing to the jurisdiction of foreign courts. Not only can the risk of a biased court be avoided but also proceedings with a very long duration. Even in jurisdiction with a court system known to be efficient, the possibility of several instances of appeal renders arbitration with its very limited opportunities to appeal the award more attractive.

Other advantages of arbitration are that arbitrators with specific expertise and experience in banking law and/or with finance disputes may be chosen and that the proceedings can be conducted in English.

Are the usual concerns still justified?

The availability of interim relief is still perceived as argument in favor of litigation (and against arbitration). This perception is, however, unjustified and outdated considering that the rules of the major arbitration institutions today provide the possibility to request interim relief from an emergency arbitrator. As a consequence, interim relief against a contractual party can also be obtained swiftly before the constitution of the arbitral tribunal. Likewise, if arbitral proceedings have already been initiated and the arbitral tribunal constituted, interim relief can be obtained from the arbitral tribunal. While in case of non-compliance, state courts need to be involved to enforce the interim relief granted, parties have an incentive to comply voluntarily in order not to displease the arbitral tribunal.

Alternatively, interim relief can be requested directly from a state court. The arbitration clause does not bar the parties to do so.

Further concerns raised include the proper application of Swiss law. These concerns stem from the fact that the arbitrators may not be Swiss qualified lawyers and that awards cannot be challenged based on the improper application or wrong interpretation of Swiss law before the Swiss Federal Court. These concerns can be addressed by including an arbitration clause requiring all or the presiding arbitrator to have certain qualifications in Swiss law. In addition, arbitral tribunals tend to consider the relevant literature and case law much like state court judges.

Conclusion

In conclusion, it seems that the financial industry's strong preference of state court litigation is no longer justified. For certain contractual relationships financial institutions regularly are parties to, arbitration offers significant advantages compared to state court litigation in Switzerland.

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