

Institutional and Ad hoc Arbitrations: Advantages and Disadvantages

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Introduction

The object of arbitration is to provide fair and impartial resolution of disputes without causing unnecessary delay or expense. Parties are entitled to choose the form of arbitration which they deem appropriate in the facts and circumstances of their dispute.

In international business, a party contemplating concluding an arbitration agreement in a contract for the resolution of disputes or differences may be faced with a choice of the various types of arbitrations which can be conducted under either self-administered ad hoc or institutional rules or procedures.

Most branches of trade or industry have established arbitration procedures within professional bodies. Contemporary arbitration gives the parties wide latitude to establish whatever rules of procedure they deem appropriate.

There are structural contrasts between the types of arbitrations as is reflected in the manner by which cases are generally presented by the parties and apprehended by the arbitral tribunal.

However, in most situations, the type of arbitration is chosen by the parties not so much because they like it but rather because they have no other choice. While there are intrinsic merits in each type of arbitration, more often than not, the option evaporates and the chosen method normally prevails by default.

I deal with only two types of arbitration namely, ad hoc arbitration and institutional arbitration, their advantages and disadvantages over each other.

Ad hoc arbitration

While there is generally an agreement on how things should be done in terms of resolving disputes in arbitration, the differences between the parties can sometimes be a stumbling block.

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There may be differing expectations and possible misunderstandings as parties of different nationalities come together seeking to resolve disputes before an arbitral tribunal of also different nationalities.

The choice of an institutional arbitration may ameliorate such misunderstandings as parties agree to submit their dispute to the administration and, to some extent, the procedural rules of a permanently established arbitration forum or centre.

If an arbitration agreement stipulates that the arbitration shall be administered by an arbitral institution, it is an institutional arbitration. Ad hoc arbitration may best be understood by reference to institutional arbitration. There are distinct differences between the two types of arbitration.

In fact, Article 2(a) of the UNCITRAL Model Law on International Commercial Arbitration recognises both ad hoc and institutional arbitrations as it defines arbitration as:

Any arbitration whether or not administered by a permanent arbitral institution.

The arbitration will be ad hoc if it is one is not administered by an institution as the arbitration agreement does not specify an institutional arbitration. Just like institutional arbitration, ad hoc arbitration may encompass domestic or international commercial arbitration.

An ad hoc arbitration agreement may just provide that:

Disputes between the parties shall be arbitrated in Mauritius.

Such an abbreviated arbitration agreement will only work if the jurisdiction selected has established arbitration law.

The parties then have to determine all aspects of the arbitration like the selection and manner of appointment of the arbitral tribunal, applicable law, procedure for conducting the arbitration and administrative support without assistance from or recourse to an arbitral institution.

The arbitral mechanism is therefore structured specifically for the particular agreement or dispute. If the parties cannot agree on such arbitral detail or, in default of agreement, laid down by the arbitral tribunal at a preliminary meeting once the arbitration has begun, it will be resolved by the law of the seat of arbitration.

If the parties cooperate and facilitate the arbitration, ad hoc proceedings can be more flexible, cheaper and faster than an administered proceeding. It is a popular choice because the parties do not have to pay administrative fees to the arbitral institution.

Parties may have difficulty in negotiating a complete set of rules and agreeing on arbitral procedures which fit precisely their particular needs. It may entail considerable time, attention and expense without the assurance that the agreed terms will address all eventualities.

This is not the only way of proceeding. Parties can adapt of the rules of an arbitral institution but amend provisions for the selection of the arbitral tribunal and remove provisions for administration of the arbitration by the institution.

Parties must be careful not to create ambiguities when incorporating such institutional rules or amending provisions for appointment of the arbitral tribunal or removing provisions for administration of the arbitration by the institution as it may inadvertently create an incomplete institutional process.

Therefore, an ad hoc arbitration proceeding need not be entirely divorced from its institutional counterpart. There are many sets of arbitration rules available to parties who contemplate ad hoc arbitration including where appropriate, incorporating the rules of their own trade associations.

It is open to the parties to adopt the rules framed by a particular arbitral institution without submitting its disputes to such institution. Parties may when they cannot agree on the arbitral tribunal may agree to designate an arbitral institutional as the appointing authority.

Parties can also incorporate statutory procedures such as applicable arbitral law or adopt the UNCITRAL Arbitration Rules which are specifically designed for ad hoc arbitral proceedings.

Institutional arbitration

In an institutional arbitration, the arbitration agreement designates an arbitral institution to administer the arbitration. The parties then submit their disputes to the institution that intervenes and administers the arbitral process as provided by the rules of that institution. The institution does not arbitrate the dispute. It is the arbitral panel which arbitrates the dispute.

The parties may stipulate, in the arbitration agreement, to refer a dispute between them for resolution to a regional institution, for example, *Cairo Regional Centre for International Commercial (CRCICA)*, *Singapore International Arbitration Centre (SIAC)* or *Hong Kong International Arbitration Centre (HKIAC)* or the *Japanese Commercial Arbitration Association (JCAA)* or the *Regional Centre for Arbitration Kuala Lumpur (KLRCA)*.

The arbitration agreement may even refer a dispute to specialised arbitration institutions which are associated with a trade association for example, the *Palm Oil Refineries Association of Malaysia (PORAM)*, *Grain and Feed Trade Association (GAFTA)*, or the *Malaysian Rubber Exchange*. Such institutions specialise in

types of disputes arising between their members with special rules to meet specific requirements for the conduct of arbitration in their specialised areas.

Other leading international institutions are the *International Chamber of Commerce (ICC)*, *London Court of International Arbitration (LCIA)*, the *American Arbitration Association (AAA)*, *International Centre for Settlement of Investment Disputes (ICSID)*, *China International Economic and Trade Arbitration Commission (CIETAC)*, *American Arbitration Association (AAA)*, *World Intellectual Property Organisation (WIPO)*. These institutions provide a framework, although of varying degrees of inadequacy, of rules and procedures for the entire arbitral hearing.

Institutional arbitration may be preferred if the parties do not mind the administrative charges levied by the institution. However, there could be some concern if the amount in dispute is substantial as it would necessarily mean that the administrative fees will be also high as they are calculated based on the amount in dispute.

Also, the institution's administrative structure may lead to added time and costs which, in turn, may affect the efficacy of the arbitral process. The rules may also require parties to respond within unrealistic time frames. Such rules may be applicable to a particular trade or industry, but not to the existing or prospective needs of one or more of the parties.

There are a large number of institutions of different kinds worldwide offering institutional arbitral services. Some are excellent. Some are mediocre. Some are bad. These institutions aim to provide an arbitration service specifically, or within the context of their overall activities and objectives, and due to their infrastructure will in some cases assist with the running of the arbitration. By and large the rules of these institutions follow a similar pattern although they are expressly formulated for arbitrations that are to be administered by the institution concerned.

Parties should take care in selecting and deciding which institution to designate in their arbitration agreement. They should consider the nature and value of the dispute, rules of the institution as these rules differ, and past record and reputation of the institution and also that the institutional rules are in tune with the latest developments in international commercial arbitration practice.

There is a possibility that the arbitral institution is not able to deliver what motivated the parties to select institutional arbitration over ad hoc proceedings, namely, the proper degree of supervision, which often is the lodestone to whether the arbitration process is successful or not.

Advantages of ad hoc arbitration

Suitable for all types of claims

Ad hoc arbitration if properly structured should be less expensive than institutional arbitration. It is suitable for use with for all types of claims, large or small.

Bigger corporations may prefer ad hoc arbitration as they often have large and sophisticated in-house legal departments and have accrued experience in managing arbitration proceedings.

Ad hoc arbitration may be designed according to the requirements of the parties, particularly where the stakes are large or where a state or government agency is involved.

The parties are in a position to devise a procedure fair and suitable to both sides by adopting or adapting to suitable arbitration rules.

Control of the process

Parties are in control of the process. They can write their own rules, set their own timelines and move the arbitration along their own pace. The arbitral tribunal and to a lesser extent the parties have to shoulder the burden of organising and administering the arbitration proceedings.

Agreed procedures

The effectiveness of ad hoc arbitration depends upon the parties' willingness to agree upon procedures at the time when they are already in dispute. If the parties do not cooperate in facilitating the arbitration, there could be loss of time in resolving the issues. There may be repeated recourse to the courts to determine contested interlocutory issues which may delay the arbitration proceedings.

Flexibility

Ad hoc arbitration is flexible in allowing the parties to cooperate and decide upon the dispute resolution procedure. It is only natural that once a dispute arises, parties tend to disagree even on the most basic of things. For example, parties of different nationalities and jurisdiction may misunderstand each other. They may find it difficult to agree and cooperate, which can delay the arbitration and frustrate the resolution of the dispute.

Ready-made arbitration rules

Parties can avoid such disagreement and avoid delays if they agree to conduct the arbitration under for example, UNCITRAL selected arbitration rules. The

result is less time and legal expense spent in determining complex arbitration rules to be used in the arbitration.

Sovereignty issues

State parties may prefer ad hoc arbitration if they are concerned that a submission to institutional arbitration devalues their sovereignty particularly when the disputes involve public interest and large sums of public monies. They would want the flexibility to define issues quickly and also adopt acceptable procedures; for example, they may wish to file simultaneous pleadings as neither party would want to be a respondent as they both believe they have justifiable claims against each other.

Cost-effectiveness

Ad hoc arbitration is less expensive than institutional arbitration. The parties only pay fees of the arbitral tribunal, lawyers or representatives, and the costs incurred for conducting the arbitration, i.e. expenses of the venue charges, etc. They do not have to pay the arbitration institution's administration fees which, if the amount in dispute is considerable, can be prohibitively expensive. The parties also have the flexibility of holding the hearings at any venue. Normally, an institutional arbitration will be held in the institution premises.

Remuneration of arbitral tribunal

In ad hoc arbitrations, the parties will have to agree the scale of remuneration with the arbitral panel and agree fees directly with the arbitral tribunal who will have to collect the money directly from the parties. Although most arbitrators are detached in dealing with these matters, there will inevitably be some degree of distraction which may lead to awkwardness for all concerned. There is no opportunity for negotiation of the fees in institutional arbitration, which requires the parties pay arbitral tribunal fees as stipulated by the institution.

Disadvantages of ad hoc arbitration

There may be situations where ad hoc arbitrations may not be more advantageous than institutional arbitration.

Selection of the arbitral panel

Parties in ad hoc arbitrations normally have to rely on their own good judgment as to the identity and quality of the individual arbitrator. This may be particularly difficult, in the context of international arbitration, as a party may not be able to choose a well known arbitrator from his country due to objections of national bias and would have little, or no, knowledge of arbitrators outside his country.

Lack of expertise

It is an accepted fact that the arbitration clause is the last thing in a particular contract which the draftsman looks at or even pays attention to. As a result it may be lacking in various respects.

Parties when represented by lay persons may lack the necessary knowledge and expertise to set up the arrangements to conduct an ad hoc arbitration. Such parties, especially if of different nationalities, may make misinformed decisions which may affect the arbitration proceedings.

Arbitration may be subject to national laws which provide for default provisions in the absence of agreement. Parties may be unfamiliar with these default provisions and may in fact not want them to apply.

Failure to cooperate

A disadvantage of ad hoc arbitration is that it depends for its full effectiveness upon the spirit of cooperation between the parties and their lawyers backed up an adequate legal system in the place of arbitration. This may not necessarily exist. Parties will have to anticipate all eventualities and provide for them. Parties may have differing views on how these eventualities are to be dealt with and will find it difficult to reach agreement.

In ad hoc arbitrations, the parties will have to agree their own timing provisions from the outset. This is fine to the extent that the parties cooperate properly and are agreed on the overall speed of the proceedings and the timing of the individual steps in the arbitration. Non-cooperation, however, can all too easily result in procedural stalemate.

Internationally, this can prove particularly troublesome, as the parties would have initially met at the venue of the arbitration, often another country, then returned and would only expect to come back to the venue for the hearing proper with pleadings and documents filed by post or electronically.

Having to meet again before the hearing to resolve procedural stalemate will involve unnecessary time and expense.

The arbitral proceedings can be easily delayed by the refusal by either party to appoint an arbitrator, or raising a challenge to either the jurisdiction or the impartiality of the arbitral tribunal. In such a situation, the provisions of the arbitration law become crucial in terms of offering necessary support.

Parties may seek court intervention especially if they are not cooperating to progress the arbitration. Such action in seeking the intercession of the courts will normally increase litigation costs, which negates the cost-effectiveness of ad hoc arbitration but also militates against the intention to resolve the dispute. If all eventualities are not provided for, either due to parties failing to reach

an agreement or to anticipate such eventualities, there will be uncertainty in the conduct of the arbitration.

The tribunal secretary

In complex cases, the arbitral tribunal may appoint a tribunal secretary to administer the arbitration, especially where it entails considerable administrative work. The parties have to bear such fees, which will be added on as the costs of the arbitration.

Default

In ad hoc arbitrations, progressing with the proceedings in the absence of one of the parties may be somewhat riskier, given that the absent party may later challenge the award on the grounds that the arbitral tribunal has not given him a fair opportunity to be heard.

Advantages of institutional arbitration

Reputation

A perceived advantage of institutional arbitration is the reputation and prestige of the institution. It is widely perceived that an arbitral award issued under the name of a well known institution for example, ICC, is helpful in terms of enforcement. It is only natural for courts faced with the enforcement of an award from a reputed institutional arbitration to be more accommodating considering the institution's reputation in running a well administered and supervised arbitration.

It is usual for established arbitration institutions to have a continuing number of new arbitrations. The parties have the comfort of knowing that such arbitration institutions have the experience in ensuring the constitution of the arbitral tribunal, the hearing and publication of the award. Parties can conveniently turn for assistance to someone in the institution with regard to the arbitration. The institution in turn can ensure that the arbitral tribunal is aware of the requirements of the arbitration. Parties and the arbitral tribunal may be more disciplined.

Arbitration rules

Institutional arbitration, rules are normally set out in a booklet. Parties who agree to submit any dispute to arbitration in accordance with the rules of a named institution effectively incorporate that institution's book of rules into their arbitration agreement.

Automatic incorporation of a book of rules is one of the principal advantages of institutional arbitration. They generally arise under the institutional arbitration clause in the agreement between the parties.

The bare-bones clause recommended by the *KLRC*A, for instance, states:

Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity thereof, shall be decided by arbitration in accordance with the Rules for Arbitration of the Regional Centre for Arbitration Kuala Lumpur.

Such a clause provides the minimal essential elements for an enforceable arbitration clause in almost all jurisdictions and is useful if the parties are unable to get specialist advice.

The clause is evidently advantageous, because even if, at some future stage, one party starts dragging its feet to proceed further with arbitration proceedings, it will nevertheless be possible to arbitrate effectively, because a set of rules exists to regulate the way in which the arbitral tribunal is to be appointed and the arbitration is to be administered and conducted. Parties who agree to submit their dispute to arbitration in accordance with those rules effectively incorporate those rules into the arbitration agreement.

The parties under an institutional arbitration have available to them a well-trying and tested set of arbitral rules. The arbitration rules provide for the various factual situations which may arise in arbitration. This is clearly an advantage.

There is a mechanism in the rules to challenge and, if necessary, remove arbitrators. Suppose for instance, that there is a challenge to an arbitrator, on the grounds of lack of independence and impartiality; or suppose that the arbitration is to take place before an arbitral tribunal of three arbitrators and the defending party is unwilling to arbitrate and fails or refuses to appoint an arbitrator. The book of rules will provide for this situation.

Administration

Another important advantage of institutional arbitration is that most arbitral institutions provide trained staff to administer the arbitration. The arbitral institution's staff will ensure that the arbitral tribunal is appointed, that advance payments are made in respect of the fees and expenses of the arbitrators, that time limits are kept in mind and, generally, that the arbitration is run as smoothly as possible.

If the arbitration is not administered in this way, the work of administering it will have to be undertaken by the arbitral tribunal itself. In an international arbitration, especially where the arbitrator is not resident in the country of arbitration, the arbitral tribunal may experience difficulty in administering the arbitration. Also, this administrative work may detract from their primary responsibility of resolving the disputes between the parties.

Supervision

In addition to administration, certain arbitral institutions, like the International Chamber of Commerce (ICC), and the International Court of Arbitration (ICC Court) in Paris, scrutinise an award before it is published to the parties, thus ensuring that the reasoning and content of the award deal with all claims and counterclaims made by the parties and that the principles of due process have been adhered to throughout the course of the proceedings.

The ICC Court is not mandated to review the award on the merits but only on procedural grounds in order not to interfere with the arbitral tribunal's exclusive power to decide the dispute in the final instance. No such quality control exists in ad hoc arbitration.

Quality of the arbitral panel

International arbitration institutions usually benefit from vast databases of arbitrators in order to assist parties in appointing appropriate arbitrators for the resolution of their disputes. The institutions have panels of experienced arbitrators specialising in various areas like construction, maritime, contract, trade, commodities, etc available to them.

Institutions like the ICC even have at their disposal an extensive network of national committees that can be consulted by the ICC headquarters in Paris to help in the identification of arbitrators with no national bias and some measure of experience or expertise in particular industry sectors.

Furthermore, institutions like the ICC will ensure that the appointment of an arbitrator is only confirmed if he is independent and impartial and has sufficient time to fulfil his mandate with due care and efficiency.

Remuneration of arbitral tribunal

An important advantage of institutional arbitration is that it avoids the discomfort of the parties and the arbitral tribunal discussing, agreeing and fixing their remuneration.

Most institutions have a mechanism for determining the scale of remuneration and collecting from the parties the money from which the arbitral tribunal will be paid without directly involving the arbitrators.

This means that the arbitral tribunal are able to maintain a certain level of material detachment. This has the very definite advantage of allowing the arbitral tribunal to focus solely on the substance of the case rather than discuss with the parties a matter that is personal to them.

Speed

In all arbitrations, whether institutional or ad hoc, speed is of the essence. Where an arbitral institution is involved, there will be tight time limits for the exchange of the parties' pleadings, the main hearing and the publication of the final award. These time limits will guide the tribunal and the parties to resolve the dispute swiftly, even though non-compliance with a given deadline will not be fatal and the parties are free to agree a more flexible timetable.

Default procedures

Some institutional arbitration rules expressly provide for the continuation of arbitration proceedings to prevent the proceedings from stopping short in its tracks, even where one of the parties defaults during the course of the arbitration. For example, Article 21(2) of the ICC Rules provides that *"If any of the parties, although duly summoned, fails to appear without valid excuse, the Arbitral Tribunal shall have the power to proceed with the hearing"*.

Disadvantages of institutional arbitration

Administration fees

Parties to arbitration bear the costs of the arbitrator and their lawyers or other representatives. Institutional arbitration is sometimes viewed negatively, as it involves additional fees payable to yet another party—the institution.

As such, institutional arbitration is believed by many to be itself a cause of both increasing expense and increasing time consumption. Among the causes of the increasing expense of are the administrative costs and costs of arbitrators' fees involved in arbitration.

Unnecessary red tape

Procedural requirements of certain arbitration institutions are also viewed by parties as introducing unnecessary red tape in what is meant to be an informal means of dispute resolution. In light of the many advantages of institutional arbitration mentioned above, especially in the international context, the fee of the arbitral institution is literally a small price to pay for an organised and smooth arbitration. And some red tape at the start generally reduces uncertainty and procedural disputes mid way through the proceedings.

Sovereignty issues

Institutional arbitration is seen to be inappropriate where one party is a state. Sovereign entities are often reluctant as a matter of politics to submit to the authority of any institution, regardless of its standing; to do so would be to devalue or deny its sovereignty.

Conclusion

As I mentioned earlier, international arbitration brings together parties from different countries in an organised manner to resolve disputes before an impartial arbitral tribunal. The parties have a choice between of the type of which suits their purpose and objective.

Ad hoc arbitration is suitable if parties want to be masters of the arbitration whereas institutional arbitration is suitable if parties want a proper degree of supervision. It is difficult to say which of these two types of arbitration is superior as it relates more to choice and needs of the parties.

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