ISDA adopts model arbitration clauses for use with ISDA Master Agreements

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Compliance, risk and legal professionals working with the International Swaps and Derivatives Association's 2002 Master Agreement and 1992 Master Agreement (multicurrency-cross border) will note ISDA's recent publication of a range of optional arbitration clauses (the model arbitration clauses), which are intended to form part of the schedule to a Master Agreement.


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Planning for disputes: the importance of forum selection clauses for compliance, risk and legal professionals working with ISDA Master Agreements

Planning for disputes is a critically important component of managing the risks associated with any contract or transaction. That is particularly so in contracts with an international dimension, which raise important questions as to where, by whom and by which legal rules any disputes arising out of the contract will be resolved. The answers to those questions will have a critical impact on the merits and enforceability of any judgment or award, the cost and speed of resolving any disputes and, ultimately, the risk that a contract will be performed according to its terms.

ISDA's Master Agreements are no different, and in an increasingly globalised market for swaps and derivatives it is equally important for compliance, risk and legal professionals working with the Master Agreements to focus on how disputes arising out of them will be resolved. Between 2011 and 2013 ISDA therefore conducted a consultation regarding the use of arbitration for disputes arising out of its Master Agreements. It was evident from ISDA's consultation process that there was strong demand for an arbitration option for use with the Master Agreements.

Demand for the ISDA Model Arbitration Clauses

Why was there strong demand for an arbitration option for use with the Master Agreements from ISDA's members? ISDA noted the following reasons why arbitration, rather than the historically preferred English or New York court litigation, of swaps and derivatives disputes is likely to continue to increase:

> In recent years, there has been a surge in the frequency with which arbitration clauses are included in a range of financial contracts, and in the number of financial disputes referred to arbitration.

Arbitration is being increasingly used in relation to privately negotiated or over-the-counter (OTC) derivative transactions entered into under master netting agreements, such as the Master Agreements.

Arbitration is increasingly popular in Master Agreements involving parties established or operating in emerging market jurisdictions.

Arbitration benefits from a much more comprehensive regime for the cross-border enforcement of arbitral awards than exists for court judgments. As ISDA noted, "[s]ucceeding on the merits of a dispute may prove to be a pyrrhic victory if it is not possible to enforce the resulting judgment."

Because many counterparties in emerging jurisdictions are increasingly reluctant for disputes to be resolved in the English or New York courts, arbitration is often a more (or the only) acceptable alternative.

Regulatory pressure for the development of clearing mechanisms for OTC derivatives may also encourage the use of arbitration. The clearing rules of most of the world's clearing houses (for securities and commodities trading, exchange-traded futures and options, and now many OTC derivatives) provide for disputes to be resolved by arbitration.

As ISDA has noted, critically, court judgments — even those from London and New York — are not enforceable everywhere (or at least not easily). The "enforcement premium" offered by arbitration is that more than 140 countries have ratified the 1958 UN Convention on Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention), which provides for the streamlined recognition and enforcement of arbitral awards in those jurisdictions (subject to limited exceptions).

Moreover, more U.S. and non-U.S. counterparties (such as public pension plans and state-owned or controlled enterprises) — perhaps with more bargaining power than ever — may simply reject English or New York litigation. Confidentiality and the procedural advantages of arbitration, such as forum neutrality and the finality of arbitral awards, are also increasingly favoured. As a result, the use (and in some cases, necessity) of arbitration as a dispute resolution mechanism in financial transactions has increased markedly (particularly in the international arena).

ISDA's Model Arbitration Clauses

These realities are reflected in ISDA's recent publication of a range of optional arbitration clauses, which are intended to form part of the Schedule to a Master Agreement. The Model Arbitration Clauses can be found in the

2013 ISDA Arbitration Guide (the Arbitration Guide) which supplements and amends the corresponding guidance in the ISDA User's Guides. Key preliminary features of each of the Model Arbitration Clauses include the following:

The clause contains a "governing law" provision specifying the governing law of the Master Agreement and the Model Arbitration Clause. The clause implements the Governing Law clause in the Master Agreements (Section 13 (a)) and the Schedules thereto.

The clause eliminates the Jurisdiction clause of the Master Agreement (Section 13(b)) and replaces it with the Model Arbitration Clause. As the Arbitration Guide notes, the jurisdiction clauses in Section 13 (b) of the Master Agreement must be removed; otherwise the Master Agreement will contain both jurisdiction and arbitration clauses — which can risk making ineffective the arbitration clause.

To reflect the choice of arbitration, the clause amends the Process Agent (Section 13(c)) and Waiver of Immunities (Section 13(d)) clauses and definition of "Proceedings" (Section 13 (b)).

The Model Arbitration Clauses provide for use of the leading institutional arbitration rules, offering the following combinations of arbitral rules, governing law, and seat (Arbitration Guide, Appendices A-G):

1. Rules of Arbitration of the International Chamber of Commerce (ICC)

   Governing law: English; Seat: London

   Governing law: New York; Seat: New York

   Governing law: English or New York; Seat: Paris

2. Arbitration Rules of the London Court of International Arbitration (LCIA)

3. Governing law: English; Seat: London

4. International Arbitration Rules of the American Arbitration Association — International Centre for Dispute Resolution (AAA-ICDR)

Governing law: New York; Seat: New York

5. Administered Arbitration Rules of the Hong Kong International Arbitration Centre (HKIAC)

   Governing law: English or New York (arbitration clause expressly governed by Hong Kong law); Seat: Hong Kong

6. Arbitration Rules of the Singapore International Arbitration Centre (SIAC)

   Governing: English or New York (arbitration clause expressly governed by Singapore law); Seat: Singapore

7. Swiss Rules of International Arbitration (Swiss Arbitration)

   Governing law: English or New York; Seat: Zurich or Geneva

8. Panel of Recognised International Market Experts in Finance Arbitration Rules (P.R.I.M.E. Finance)

   Governing law: English; Seat: London

   Governing law: New York; Seat: New York

   Governing law: English or New York (arbitration clause expressly governed by Dutch law); Seat: The Hague

Drafting the right clause

ISDA is careful to note that the Model Arbitration Clauses were a response to member feedback, and inclusion in the Arbitration Guide is not an endorsement of the clauses (or combinations of rules, governing law, and seats). The Model Arbitration Clauses are to provide guidance only and parties are free to modify the Model Arbitration Clauses as they devise and negotiate. As the Arbitration Guide notes, whether the Model Arbitration Clauses are adopted or market participants negotiate their own terms, in all cases parties should seek appropriate legal advice to select the appropriate dispute resolution mechanisms for their circumstances.

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