How India Inc is coping with ineffective ad-hoc arbitration and paving way for a new trend

The slow pace of justice in domestic courts and the ineffective local trend of ad-hoc arbitration are giving way to a new style of institutional arbitration.

Naren Karunakaran | 09 July 2015, 9:05 AM IST

When a guest signs a reservation form at any of the Taj Hotels and Resorts in India, he or she, unbeknownst, agrees to refer any possible dispute to arbitration.

The parties to a dispute, in choosing arbitration, opt for a private or alternative dispute resolution (ADR) process instead of seeking redress in a court of law. The Taj Hotels' terms and conditions also state arbitration proceedings will be under the rules of the London Court of International Arbitration India (LCIA), an independent subsidiary of the LCIA, UK. Arbitration between a guest and a hotel is rather pedestrian. It, however, acquires a critical nature in large infrastructure contracts.

An arbitration clause is de rigueur in commercial contracts. RIL has a series of ongoing arbitrations against the government related to the KG-D6 block. Lately, multinationals have been hauling India to arbitration under certain clauses of bilateral investment treaties (BITs) signed between countries. Vodafone's dispute with India is an example. High-profile arbitrations are hitting headlines like never before. "At any given time, I have half-a-dozen arbitrations against ONGC," says Hiroo Advani, senior partner at

Advani & Co, a Mumbai-based law firm. The firm has fought numerous arbitrations ranging from $50 million to $1 billion in recent years. The numbers are burgeoning but the approach to the arbitration issue is in transition.

The fact that companies are refining arbitration clauses in contracts, for instance, with clear mentions of institutions, like the LCIA India, or the Singapore-based Singapore International Arbitration Centre (SIAC) and also clarifying the seat of arbitration, is a significant development. It is no longer a 'midnight clause,' says the general counsel of a large power company, included at the last moment in contract negotiations.

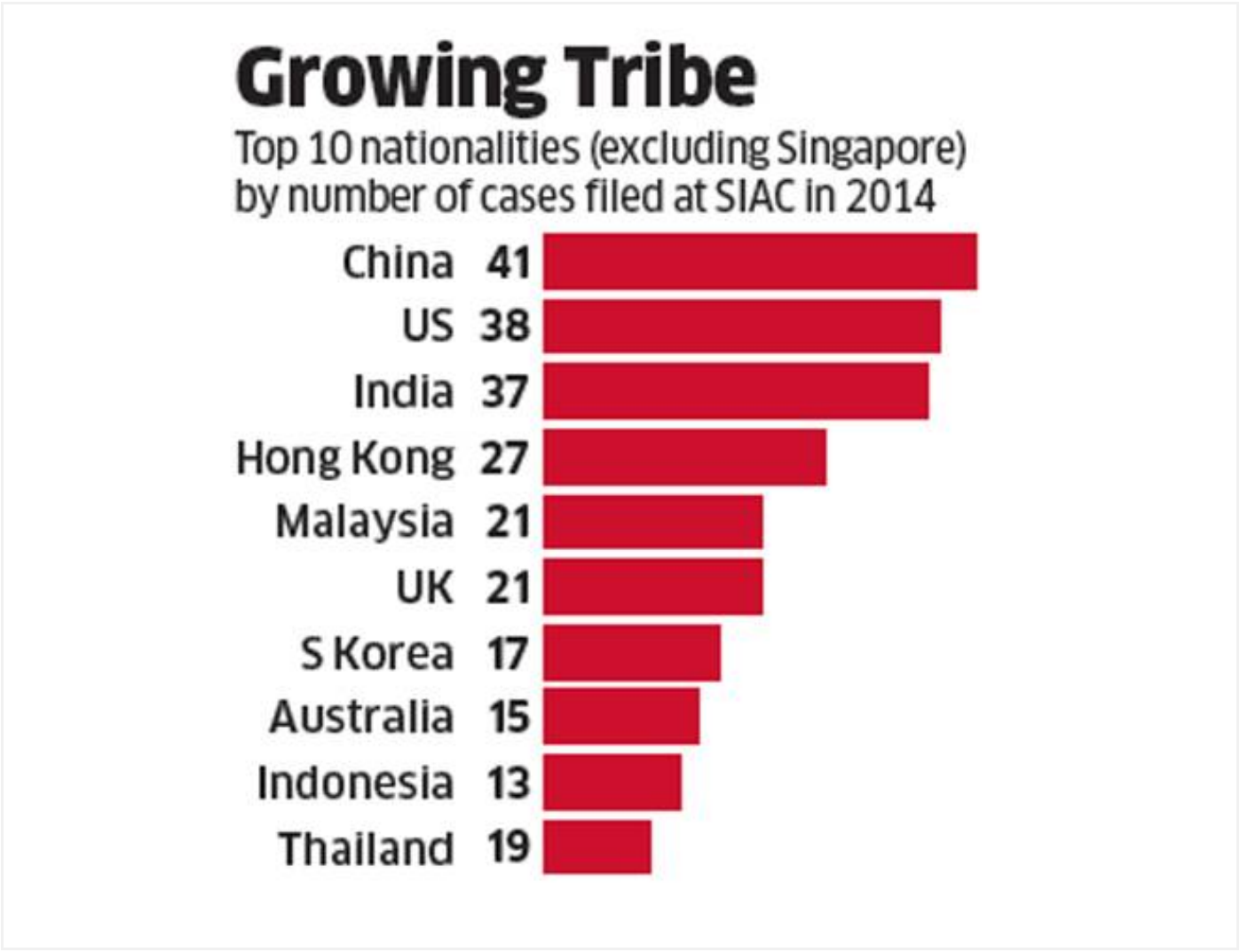
The trend also indicates a move away from 'ad-hoc arbitration' which is the norm in India; over 95% of arbitrations are of this nature. Companies now prefer the discipline and a degree of certainty that a supervisory arbitral institution brings to the table. Such institutions help with the appointment of arbitrators, set timelines, regulate costs, and extend administrative support. That 'institutional arbitration' is gaining in traction is borne out by the fact that LCIA India, which started operations in 2010, is overseeing arbitrations of value exceeding $2.9 billion. "Our biggest is a recent $1 billion claim between Indian parties," reveals Ajay Thomas, Registrar, LCIA India. So, why is Thomas elated about the prospects of doing business in India? The principal reason is arbitration, largely ad-hoc as practised in India, is in a shambles. The attorney general of India recently used stronger words and called it a "joke."

The reason why domestic arbitration is attracting such expletives is because arbitration proceedings are beginning to resemble court proceedings. It's a replica now, even worse, which is ironic as arbitration draws strength from its inherent differences from a convoluted court process.

The languorous Indian court system is weighed down with over 30 million pending cases. A couple of years ago, Bloomberg Businessweek calculated that if the nation's judges worked nonstop, without sleep or break, and cleared 100 cases every hour, it would take 35 years to catch up.

For litigants, the thought of getting into this quagmire was scary and, therefore, arbitration was seen as succour. Its biggest advantages: it's fair, it's cost-effective, and it's quick. The average time taken for an award by the LCIA is 12 months. Advani lauds the SIAC, where awards can be expected in less than six months if the amount in dispute is less than $ 5 million. Little wonder then Indians are among the top nationalities who submitted their disputes to arbitration at the SIAC in 2014 (see chart). Singapore is a favoured neutral destination for international commercial arbitration

where one of the parties to the dispute is a foreign entity.



"In regular courts, you also run the risks of appeals," explains Vyapak Desai, partner, Nishith Desai Associates. "Arbitration gives finality." Arbitral awards can be challenged on very limited grounds.

The problem with ad-hoc arbitration, therefore, begins with the replica bit. Most arbitrators in India are retired high court and Supreme Court (SC) judges and the pace at which they function is frustrating. Subject experts as arbitrators are rare here. It could take years for a dispute to reach an awards stage.

Many of these retired judges charge anything from Rs1 lakh to even Rs5 lakh per day plus expenses; in Mumbai they have now started charging on a sitting basis, separately for a morning and evening sitting. Fees of arbitral institutions, on the other hand, are fixed. The tribunal fee under LCIA India is Rs20,000 an hour. Administrative

and arbitrators' fees at the SIAC are set into slabs and vary according to the amounts in dispute.

"If a party asks me today how much arbitration will cost him, I have to throw up my hands and say, 'I don't know'," bemoans Advani. "The economics of ad-hoc arbitration have all gone awry." In certain cases, the cost of arbitration has veered close to, or even exceeded, the amounts in dispute. Domestic arbitration, therefore, is no longer cost-effective or quick.

The prevalent system is clearly in degeneration. One reason is the absence of strong, credible Indian arbitral institutions. The Delhi International Arbitration Centre, set up by the Delhi High Court in 2009, has made some headway.

It receives around 200 cases a year. Who is to blame for the situation? It cannot be apportioned to greedy arbitrators alone. Law firms, counsels, and parties, all protecting their narrow interests, are also playing insidious roles. Over 95% of arbitration is ad-hoc in India today because many want it to be this way. It goes without saying that ad-hoc arbitration, without any institutional oversight, is amenable to manipulation. It lends an opportunity to 'manage the process.'

Many infrastructure companies, outwardly, lament the mess but they are the ones who lay the grounds for ad-hoc methods in contracts, for they know, in all probability, they will be the respondents in a case and wouldn't want processes to be expedited. Delays work in their favour.

Cash-bleeding, ad-hoc arbitration can also be used as strategy by companies. In an arbitration process between a company with deep pockets and one with limited means, the latter will eventually wilt and give up. The weaker party, in a way, is financially bludgeoned to come to a settlement.

Judicial intervention has only added to the mess. Courts are expected to refrain from interfering in arbitration processes but often draw on the Arbitration and Conciliation Act, 1996, when parties seek redress.

It manifests in three stages. In the 'pre-arbitration' stage, a party can seek a judicially-ordered appointment of an arbitrator, or a party can challenge the constitution of a tribunal on grounds of impartiality or conflict of interest.

Sometimes, the mere appointment of an arbitrator through the court system can take

years. Court interference 'during' a process is rare but it does happen. It is the 'post' period that is an area of concern. A party can challenge an arbitral award in a court. Most public sector undertakings do it as routine.

"In London or Singapore you won't be entertained for a minute by a court after an award is given," says Advani. "Applications to set aside awards are often thrown out." Advani is also president of the newly-created Indian Arbitration Forum, a lobby group seeking reforms in Indian arbitration.

Interestingly, the SC, through a series of pro-arbitration judgements, has begun to retrieve the situation. For instance, in the NBCC versus JG Engineering case, it clarified that the mandate of the arbitrator expires if an award is not delivered within the time limit stipulated by parties. Last year, in RIL's KG-D6 dispute with the government, the court set aside the nomination of the chairman of the arbitration tribunal on the grounds of independence and impartiality.

The turning point, however, came slightly earlier when the SC, in 2012, in the Balco and subsequent Lal Mahal decisions, secured the sanctity of a foreign award where the seat of arbitration is a foreign country, and removed barriers to its enforcement in India.

Meanwhile, the Law Commission, under the chairmanship of Justice AP Shah, in its 246th report last year, has suggested an overhaul of the existing Act to make arbitration more robust and also sought to banish anxieties about the role of courts by quoting the late Lord Mustill of the commercial bar in UK: "It is no good complaining that judges should keep right out of arbitration, for arbitration cannot flourish unless they are ready and waiting at the door, if only rarely allowed into the room." The recommendations by Justice Shah include a model schedule of fees, dedicated benches for arbitration-related cases, and challenges to arbitral awards to be disposed within a year. He has also sought to increase the threshold of judicial intervention at various stages of the arbitral process.

When a party challenges an award in court, an automatic stay on the award comes into operation and a court is not even permitted to impose terms on the applicant. The Law Commission wants to alter this situation; which means the court can direct an applicant to deposit the award amount or a portion of it prior to any stay on the award. The incentive to litigate diminishes a great deal.

Even as amendments to the Arbitration & Conciliation Act are awaited, a cultural shift

is also happening amongst corporates. The GC in a large infrastructure group recalls the time he had joined an infrastructure company in the airports sector. He was one of the few legal experts but when he finally left, he was heading a legal team of 45.

Legal experts were earlier banished to the corporate dungeons but are now finding their place under the sun as GCs. They are now seen on par with CFOs, he says, and a not a day passes, for him, without a meeting with the CEO. It is expected that with this trend, India will move towards institutional arbitration. The sector itself is throwing up innovations difficult to ignore.

Take the emergence of 'emergency arbitration' in which an arbitrator is appointed to deal with requests for urgent interim relief like an interim injunction before the actual arbitration tribunal is constituted. Thomas says even the LCIA India has an answer to this in 'expedited formation of a tribunal;' all within 48 hours. "It will be in place next month," he says.