# TRADE DISPUTES SOLVING MECHANISMS

by

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## 1.0 INTRODUCTION

The flow of goods and services in a modern economy and international trade is based on contracts agreed by the parties. Such contracts are in turn based on trust that the other party will carry out the contracts as agreed. Should a dispute arise, it is possible to take legal action against a offending party. Commercial disputes may range from small to large ones.

Although there are no statistics, it is generally accepted that a large number of disputes never get anywhere near lawyers. It is inevitable that parties will try to turn away from allowing disputes to fester until they mature into a state in which third party interventions become the only available option. It is now common in international trade for commercial entities to evaluate risks and develop mechanisms for early dispute evaluation and prevention.

The procedures available for the resolution of trade disputes extend over a wide spectrum. Either, the parties resolve the disputes promptly by reaching an agreement on an “interest basis” rather than a “rights basis” or they are nipped in the bud before they can burst into flower.

In such circumstances, the parties assess whether it would be advantageous to implement a solution reflecting elements such as fairness, maintenance of long-term relationships and which of them will feel less pain in taking a hit.

It is suggested that an interest-based approach is not confined to a resolution that is based on rights claimed by the parties and remedies offered by the legal system, the mediator and the parties can probe more deeply to meet the disputants real interest and needs.

There are as many ways to structure a settlement as there are parties with individual needs and desires.' (see Aibel, HJ, *Meditation Works: Opting for interest-based solutions to a range of business needs*. Dispute Resolution Journal (1996) Vol 5 at p 26.) These elements have little to do with contractual rights and obligations.

## 2.0 DISPUTE RESOLUTION MECHANISMS

There is an increasing recognition that no single means of resolving dispute is appropriate in all cases. There is no magic wand for the settlement of disputes.

However, when disputes do remain, parties are faced with three quite different types of dispute resolution mechanisms:

1 Litigation in courts;

2 Arbitration, designed to achieve a *final and enforceable* outcome; and

3 Other Alternative Dispute Resolution (ADR) mechanisms such as mediation, conciliation, mini trials, rent-a-judge, med-arb, dispute resolution board, adjudication and other 'touchy-feely' ways of engaging the intervention of a third party to achieve an agreed settlement between the parties.

All the above three dispute resolution mechanisms are based on resolving mature disputes through the intervention of a third party that has substantial formal or informal authority over the parties. The role of the third party varies in each of the three different mechanisms.

The nature and progression of the three processes are different. The parties know and are aware that the outcome from each of the first two mechanisms referred to above will necessarily be based on a third party's assessment of their legal rights and obligations.

Depending on the nature of the dispute, and the circumstances of the parties, several alternatives may be open for its resolution ranging from litigation to some form of Alternative

## 3.0 NON-BINDING ADR METHODS

The problems of litigation and arbitration in terms of costs, delays and disruption have led many to consider other non-binding ADR techniques like mediation, conciliation, adjudication and expert determination.

If an issue between the parties is one where an expert opinion is required, then expert determination would be the appropriate method. Alternatively, if the parties wish to resolve the matter amicably, then mediation or conciliation would be the appropriate method. It is now quite common for parties to agree to submit their disputes to a non-binding ADR mechanism, either with or without arbitration, as a fallback in the event that ADR fails.

Mediation is available in the insurance and banking industries through the Insurance Mediation Bureau and the Banking Mediation Bureau set up in 1991 and 1997 respectively under the *Companies Act 1965 (Act 125) s 24*.

As a condition precedent for a petition for divorce, except for dissolution on grounds of conversion of religion or for dissolution by consent, Malaysian divorce law also provides for the reference of a matrimonial difficulty to a Marriage

Tribunal, which will attempt to conciliate the said difficulty between spouses. The Malaysian Bar Council established the Malaysian Mediation Council in 1999 to promote mediation and to provide a range of mediation-based services for commercial disputes.

## 4.0 ARBITRATION AS AN ALTERNATIVE

Arbitration represents an alternative to the judicial process and is one of the available methods appropriate for resolving complex disputes between the parties, particularly where points of law are involved.

Disputes have to be settled rapidly. The business world has long recognised the need for removing delays and other impediments to settlement of commercial disputes.

It has resorted to an organised form of arbitration by creating arbitration facilities within many business organisations, chambers of commerce, exchanges and trade associations. For example, arbitration facilities are provided by the PORAM, Pertubuhan Akitek Malayisa and Institution of Engineers and the Malaysian Rubber Exchange acts as an arbitration centre to settle trade disputes arising out of standard form contracts issued by the bodies.

Arbitration should be distinguished from the non-binding ADR techniques. The function of an arbitrator is not to decide how the dispute can most readily be resolved but rather to apportion responsibility for that dispute.

## 5.0 ARBITRATION DEFINED

Mustill and Boyd in their book, *Commercial Arbitration*, 2nd Edition, 1989, pages 41 to 42, have listed some of the attributes which must be present for an agreement to be considered as an arbitration agreement as follows:

1. The jurisdiction of the tribunal to decide the rights of the parties must derive either from the consent of the parties or from an order of the court or from a statute, the terms of which make it clear that the process is to be an arbitration;

2. The agreement must contemplate that the substantive rights of the parties will be determined by the agreed tribunal;

3. The tribunal will determine the rights of the parties in an impartial and judicial manner with the tribunal owing an equal obligation of fairness towards both sides;

4. The agreement of the parties to refer their disputes to the decision of the tribunal must be intended to be enforceable in law; and

5. The agreement must contemplate that the tribunal will make a decision upon a dispute which is already formulated at the time when a reference is made to the tribunal.

## 6.0 WHY ARBITRATE

Why should anyone arbitrate?

After all, the parties must pay the fees of the arbitral tribunal whereas the use of the court comes almost free. As a start, there are several reasons why parties agree to arbitrate instead of litigating. Arbitration promises a fair trial by an impartial tribunal. The parties to arbitration can keep the details of their dispute private and out of the glare of public scrutiny. The parties have various options in line with the concept of party autonomy with respect to the conduct of arbitration.

They have flexibility in choosing the procedure, applicable rules, hearing times and venue. For example, the arbitrator and the parties have the option of choosing the place of meetings other than the place of arbitration in certain situations. Parties can establish their own ground rules. Arbitration provides a simplified commencement of proceedings and service of process, neutrality and facilitated taking of evidence and *prima facie*, promises the possibility of comparatively expedited proceedings.

Arbitration may be helpful where the dispute involves extremely technical matters, for example patent or software copyright or geotechnical litigation, where scientific and mechanical principles are involved. By their very nature, such disputes are difficult for a non-expert to understand. The arbitral process can be tailored to fit the dispute, which in turn allows some scope for time and costs savings.

The general preference for arbitration in certain industries and international trade has nothing to do with the advantages of speed and cost-saving, which are often emphasised in arbitration textbooks and conferences. The main reason why

there is more arbitration clauses inserted in commercial contracts is simply the unwillingness of the parties to litigate in court. The courts do have important supportive and supervisory roles in relation to arbitrations and parties revert to them when absolutely essential.

Other reasons include the expeditious issuance of an award, confidentiality and simplified enforcement. The last point is a strong positive feature of arbitration in that arbitration awards can be enforced both domestically and in foreign jurisdictions (by way of the *Arbitration Act 2005*. By contrast, it may be difficult to enforce a favourable court judgment in another country, as there are no multilateral treaties covering the reciprocal enforcement of court judgments.

Lord Mustilll in his Foreword to D Mark Cato, *Arbitration Practice and Procedure*, 2nd Edition, 1997, LLP made the point for arbitration when he said:

> *"The great advantage of arbitration is that it combines strength with flexibility. Strength because it yields enforceable decisions, and is backed by a judicial framework which, in the last resort, can call upon the coercive powers of the state. Flexible because it allows the contestants to choose procedures which fit the nature of the dispute and the business context in which it occurs. A system of law which comes anywhere close to achieving these aims is likely to be intellectually difficult and hard to pin down in practical terms."*

The role of the arbitrator is judgmental and arbitration will thus always be needed where for one reason or another, a final and enforceable outcome is necessary. There are situations where one party needs an award – a final and binding solution imposed by a third party – rather than an agreed compromise settlement or even a consent award.

Often not just money is at stake. Sometimes one party may be bankrupted if it does not achieve a complete victory. Matters of principle or the positioning of a party in a long-term relationship may be in issue. Sometimes, the management of a party cannot afford to take the responsibility of being a party to a compromise settlement. In such cases, the party may need an 'official' piece of paper, such as an arbitrator's award, before agreeing to contribute to a settlement.

## 7.0 THE CONTRAST WITH LITIGATION

Litigation, unlike arbitration, does not require consensus of the parties. It is the right of any citizen to bring an action in the courts for breach of contract or a tortious wrong.

1997 was a watershed year in Malaysia. The Asian financial crisis coupled with the greater willingness of parties to commence legal action to enforce and protect their legal rights resulted in a tremendous deluge of civil suits in the courts. Although there are no statistics, it is generally accepted there has also been a substantive increase in references to arbitrations.

While the crowded court lists and the resultant hearing delays have further boosted the use of arbitration, there are also contributory reasons why arbitration is popular in Malaysia as compared to litigation (see Cecil Abraham, *Arbitration in Asia: Division X: Malaysia*. November, 2001 Butterworths p X1–X2).

The first reason is the increasing requirement by the courts that the national language (Bahasa Malaysia) be used for its proceedings and cause papers. This has inevitably led foreign parties to prefer arbitration with its flexibility on language use so that they themselves can follow the proceedings. For a foreign

litigant, arbitration as compared to court litigation in Malaysia is more helpful in avoiding the vagaries and uncertainties of foreign litigation.

Such uncertainties may include whether a foreign court will assume jurisdiction to hear the case, the necessity for advice and representation by lawyers of that jurisdiction, the necessity for translation of documents and interpretation of evidence, exposure to technical and formal rules of procedure and evidence and the risk of having the dispute resolved by inexperienced and incompetent judges.

Secondly, the parties are neither bound to be represented by lawyers nor are they prohibited from being represented by them. Any persons of their choice may represent the parties in arbitration and they are not required to be represented by Malaysian lawyers. Particularly, they can engage persons possessing technical knowledge, skill, training and experience, in cases involving technical and scientific issues. The court in *Zublin Muhibbah Joint Venture Sdn Bhd v Government of* Malaysia [1990] 3 MLJ 125 decided that an arbitral forum is a private tribunal that does not fall within the ambit of the *Legal Profession Act 1976.*

Thirdly, the Malaysian *Evidence Act 1950* does not apply to arbitration, thus giving a greater degree of flexibility from the rigid rules of evidence, as opposed to court proceedings. Especially, it gives ample opportunity to the arbitrator to adopt suitable procedures to assess evidence and with respect to other issues, particularly where the parties of different nationalities are involved.

Lastly, it is quite common for Malaysian standard form contracts, for example the various *PORAM* contracts provide for arbitration as the means for resolving disputes. Such forms capitalise on the fact that the parties can choose who

should hear their dispute and what powers the arbitrator should have to conduct the proceedings.

Parties are free to choose an arbitrator whose technical expertise and experience may resolve the dispute in its commercial setting. This has the advantage that the arbitrator is already familiar with the subject matter of the dispute. With greater scope of reducing acrimony, disputing parties may be able to preserve their continuing business relationship and confine the dispute between them.

Judges in the Session Courts and High Courts hear a wide variety of cases and will not generally have the technical knowledge of a technical arbitrator. On the other hand, the legal knowledge of such arbitrators can never equal that of a judge but there are several ways of compensating for this. Parties have a choice of selecting an arbitrator from the legal profession or, the parties can allow the arbitrator to take legal advice.

While it is recognised that technical expertise and experience is available in litigation through the appointment of experts, there is a real danger that an arbitrator without the requisite technical expertise and experience may be influenced more by the eloquence and powers of explanation and persuasion of the expert than by the technical merits of his evidence.

The available arbitrators in Malaysia include retired judges, lawyers, architects, engineers, traders and other professionals. If the parties cannot agree on the arbitrator, they can invariably agree on some institution to make the appointment as contained in the various arbitration clauses of the standard supply, building and engagement contracts. Hearings could be quicker because the technical knowledge of the arbitrator necessitates far less background explanation.

Other factors include the technicality and time-consuming court rules, the adversarial court process which foster hostility and increase costs, lack of senior executive involvement at a sufficiently early stage of the dispute resolution, an ingrained attitude that attempts at early settlement is a sign of weakness and inability of judges to resolve issues in a case containing highly technical factual matters (P Dwight, *Commercial Dispute Resolution in Austrialia: Some trends and misconceptions* (1989) 1 *Bond Law Review* 1 at pages 1 to 2).

## 8.0 THE DURABILITY OF ARBITRATION

All said and done, in its essentials, arbitration has not changed. Its desirability cannot be denied. It is still the preferred method of dealing with commercial and technical disputes effectively. It must be emphasized that the *Arbitration Act 2005* provides only the framework. It is possible to achieve a fair and just dispute resolution at a minimal cost where the arbitration clause or the arbitration rules incorporated by reference (or specifically agreed upon) are so designed to do so.

Mustill LJ concludes,

> *"Arbitration has come to occupy an influential position in the conduct of international trade. It has a great deal more to contribute, and it can and should grasp the opportunities which stand before it. But there is no room for complacency."* (see Mustill LJ, Arbitration: History and background (1989) *6 Journal of International Arbitration* 43 at 56).

## 9.0 TYPES OF ARBITRATIONS

In international trade, 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. 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 arbitrators. 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.

## 9.1 AD HOC ARBITRATIONS

Ad hoc arbitration refers to arbitration where the parties and the arbitrator will conduct the arbitration according to procedures which will either be agreed by the parties or, in default of agreement, laid down by the arbitrator at a preliminary meeting once the arbitration has begun. However, this is not the only way of proceeding. There are many sets of arbitration rules available to parties who contemplate arbitration including where appropriate the rules of their own trade associations.

The expression ‘ad hoc’, used in ‘ad hoc arbitration’ or ‘ad hoc submission’ is used in two different senses; an agreement to refer an existing dispute, and/or an

agreement to refer either future or existing disputes to arbitration with an arbitral institution specified to administer the proceedings or without any procedural rules specified. Therefore, ad hoc arbitration may be stipulated either in the 'submission agreement' or in the arbitration clause provided it broadly establishes the arbitral tribunal, venue of arbitration, the governing law and procedural or arbitration rules.

Thus, if, an arbitration agreement stipulates that the arbitration shall be administered by an arbitral institution, it is an institutional arbitration. In the absence of such stipulation, the arbitration is 'ad hoc'. 'Ad hoc arbitration' is, therefore, arbitration agreed to and arranged by the parties themselves without assistance from or recourse to an arbitral institution. Such arbitration may take place in accordance with the rules of the institution. It is, however, open to the parties to agree to adopt the rules framed by a particular arbitral institution without submitting its disputes to such institution. 'Ad hoc arbitration' may encompass domestic or international commercial arbitration (see PO Malhotra, *The Law and Practice of Arbitration and Conciliation*: The Arbitration and Conciliation Act 1996,2nd Edition, 2006, pages 115 to 116, LexisNexis Butterworths.

The advantage of ad hoc arbitration is that it 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, in an ad hoc arbitration, are in a position to devise a procedure fair and suitable to both sides by adopting or adapting to suitable arbitration rules.

The disadvantage of an ad hoc arbitration is that it depends for its full effectiveness upon the spirit of co-operation between the parties and their lawyers backed up an adequate legal system in the place of arbitration. This may

not necessarily exist. 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 impartiality of the arbitral tribunal. In such a situation, the provisions of the arbitration law become crucial in terms of offering necessary support Redfern, A and Hunter, M, *Law and Practice of International Commercial Arbitration*, 4th Edition, 2004, Thomson/Sweet & Maxwell, p 76).

## 9.2 INSTITUTIONAL ARBITRATION

Institutional arbitration is an arbitration administered by an arbitral institution. The parties may stipulate, in the arbitration agreement, to refer a dispute between them for resolution to a particular institution, for example, PORAM, the *Regional Centre for Arbitration Kuala Lumpur (KLRCA)* or *Singapore International Arbitration Centre (SIAC)* or *Hong Kong International Arbitration Centre (HKIAC)*. Other leading international institutions are the *International Chamber of Commerce (ICC), London Court of International Arbitration (LCIA), International Center for Settlement of Investment Disputes (ICSID)*, *China International Economic and Trade Arbitration Commission (CIETAC)*, *American Arbitration Association (AAA)*, *World Intellectual Property Organisation (WIPO)*.

Such institutions operating in various fields of arbitration undertake to supervise or conduct arbitration in accordance with their rules. Though institutional arbitration may be more expensive, they provide procedural framework, specialised expertise and services. 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.

The parties under an institutional arbitration have available to them a well-tried and tested set of arbitral rules. The arbitration rules provide for the various

factual situations which may arise in arbitration. The institutions have panels of experienced arbitrators specialising in various areas like construction, maritime, contract, trade, commodity, etc available to them.[4] This is clearly an advantage. There is a mechanism in the rules to challenge and, if necessary, remove arbitrators.

They generally arise under the institutional arbitration clause in the agreement between the parties. The clause recommended by the *KLRCA*, 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'.*

Redfern and Hunter state that such a 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 (see OP Malhotra, *The Law and Practice of Arbitration and Conciliation*: The Arbitration and Conciliation Act 1996, 2nd edn 2006, p 117–118. LexisNexis Butterworths).

Institutional arbitration rules are normally set out in a booklet. Parties who agree to submit their dispute to arbitration in accordance with those rules effectively incorporate those rules into the arbitration agreement. The main disadvantage is costs as the institution will charge an administrative fee on top of the fees payable to the arbitral tribunal. Another disadvantage is the possible delay that arises from having a layer of institutional administration of the arbitration.

## 9.3 LOOK SNIFF ARBITRATION

There are many disputes, particularly in the commodity field, that are purely disputes of quality. The relevant question arising from the dispute is whether the commodity delivered complies with the quality specification or agreed sample. Some institutions specialize in these types of disputes with special rules to meet the specific requirements for the conduct of arbitration in their specialized areas, for example, the *Malaysian Rubber Exchange* acts as an arbitration centre to settle trade disputes affecting rubber. Another institution is the *Grain and Feed Trade Association (GAFTA)*.

Such questions of pure quality are best resolved by experts in the field by way of an arbitral procedure. 'Look-sniff arbitration' or 'quality arbitration' is a combination of the arbitral process and expert opinion. The parties select the arbitrator on the basis of his specialized knowledge, expertise and experience in a particular area of business or trade. In such arbitration, the parties will disclose to the arbitrator the relevant documents setting out the required specification and may show him the agreed sample.

If necessary, the arbitrator arranges to take inspection of the goods or commodities, which are the subject matter of the dispute. For taking such inspection, he need not make any further reference to the parties. Such inspection may be even in the absence of the parties. There are no formal hearings for the taking of evidence or hearing oral submissions. The arbitrator is looking or sniffing, using his own experience and knowledge, and coming to an award based on the evidence placed before him and gathered by him.

This type of arbitration is an exception to the rule that an arbitrator should not normally take into account his own opinions unless he has explained these

opinions to the parties and given them an opportunity to deal with them in evidence or submission. The arbitrator has wide discretion to find the necessary relevant evidence and information.

## 9.4 DOCUMENTS ONLY ARBITRATION

Some arbitration proceeds on the basis of exchange of written documents only. Redfern and Hunter state that 'such arbitrations are commonplace in certain categories of domestic arbitrations, notably in relation to small claims cases involving, for example, complaints by holiday-makers against tour operators and claims under insurance policies.

In the international context, the main examples of 'documents-only' arbitrations are those conducted under the rules of the London Maritime Arbitrators Association in connection with disputes arising out of charterparties and related documents (see Redfern and Hunter, *Law and Practice of International Commercial Arbitration*, 4th Edition, 2004, Sweet & Maxwell at pages 286 and 315-316).

It is useful where limitation of costs is an overriding consideration, for example, in consumer disputes. The documents-only arbitration is not oral. It is based only on the claim statement and statement of defence and written reply by the claimant, if any. It also includes the documents submitted by the parties with their statements along with a list of references to the documents or other evidence submitted by them. The parties deliver written submissions and supporting documents in turn to the arbitrator. The written submissions may simply take the form of a letter to the arbitrator from the parties or his representatives, or may be a more formal document produced by lawyers.

Once these written submissions are complete, the arbitrator proceeds immediately to write his award on the basis of the submissions and documents in his possession. If the arbitrator needs clarification on any point, he may write to the parties to seek this clarification. Generally, the arbitrator will make his decision without further reference to the parties. A documents-only arbitration may not work in disputes where there are conflicts of facts as the arbitrator does not have the benefit of observing a witness cross-examined.

## 9.5 DOMESTIC AND INTERNATIONAL ARBITRATIONS

The terms ‘domestic’ and ‘international’ arbitrations as defined in the Malaysian *Arbitration Act 2005* are used in referring to certain types of arbitrations which occur in Malaysia.

A domestic arbitration would mean an arbitration in which the arbitral proceedings are held in Malaysia and in accordance with Malaysian substantive and procedural law and the cause of action for the dispute has wholly arisen in Malaysia or where the parties are subject to Malaysian jurisdiction.

An arbitration is international if:

(a) The parties to an arbitration agreement have, at the time of the conclusion of that agreement, their places of business in different States; or

(b) One of the following places is situated outside the State in which the parties have their places of business:

(i) the place of arbitration if determined in, or pursuant to, the arbitration agreement;

(ii) any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject matter of the dispute is most closely connected; or

(c) The parties have expressly agreed that the subject matter of the arbitration agreement relates to more than one country. International arbitration is commercial if it relates to disputes arising out of a legal relationship, whether contractual or not, considered as commercial under Malaysian law.

Under the Malaysian *Arbitration Act 2005*, there is minimal court intervention in International arbitration.

## 10.0 CONCLUSION

There is today a surfeit of dispute resolution methods in resolving trade disputes. It is clear that such many procedures do contribute to the efficacy of international trade. Some of these mechanisms are of recent origin and others are long standing. Some will, and should, pass the test of time.

In international trade, only arbitration provides for party autonomy, privacy and confidentiality, finality and ready enforceability of the decision. Parties, of their own volition or with the guidance of a competent arbitral tribunal can have tailor made procedures to suit their particular circumstances, their needs, the nature of the dispute, the degree of urgency and other matters of importance to them.

Arbitration is the process which has stood the test of time and will continue to hold its importance in resolving trade disputes.