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The Troubled Waters of Asymmetric Arbitration Clauses

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by Dr Andreas Respondek and Frederike Marina Löwenthal

Even though asymmetric arbitration clauses seem to be used frequently in dispute resolution clauses for various industries, there is very little statutory guidance with regard to the validity of such clauses. Ultimately, the validity and use of asymmetric arbitration clauses depends on the circumstances in a specific jurisdiction. This article will examine in a snapshot how the validity of asymmetric arbitration clauses is dealt with in eight different jurisdictions.

An "asymmetric arbitration clause" or "unilateral option arbitration clause" (**AAC**) is a clause under which the parties bound by it limit themselves to bringing an action in a particular jurisdiction, while at the same time allowing one or more parties to choose whether to refer a dispute to arbitration. [1] Asymmetric arbitration clauses are often used in specific industries such as finance and construction.

Despite the regular use of asymmetric arbitration clauses in various dispute resolution clauses, there is no statutory guidance explaining the use or enforcement of asymmetric arbitration clauses. As a result, there is some uncertainty as to the use of such clauses, especially since the validity and enforceability of such clauses seem to vary widely from jurisdiction to jurisdiction.

Introduction: What is an "Asymmetric Arbitration Clause" or "Unilateral Option Clause"?

Dispute resolution clauses in contracts are usually either arbitration clauses or jurisdiction clauses. While the arbitration clauses refer the parties to arbitration, the jurisdiction clause confers jurisdiction to a particular competent court. [2] If the parties have the right to choose between arbitration and litigation, then one can speak of a hybrid dispute resolution clause. [3]

An arbitration clause usually provides for the seat/venue and applicable law of the dispute, amongst other things. [4] More precisely, one party is restricted to bringing proceedings in a particular jurisdiction

while the other party has the option of electing to have their dispute referred to arbitration. [5] The "unilateral" or "asymmetric" part of a clause refers to the beneficiary party's exclusive right to choose the type of dispute resolution. [6]

Are There Other Types of Clauses for a Dispute Resolution Agreement?

The other option is the "symmetrical agreement" or "bilateral option" clause, where each side has the same right to invoke arbitration. [7]

What are the Pros and Cons of an Asymmetric Arbitration Clause?

As the AAC only gives one party the advantage of choosing whether the dispute should be resolved by means of arbitration or litigation, [8] it follows that the party entitled to decide has a certain advantage. For the beneficiary party, an AAC can represent an effective risk management mechanism as he will have the security and flexibility to initiate the proceedings in the most attractive jurisdiction at the time of the dispute. [9] This however only applies when the AAC is deemed valid. As this article will discuss below, not every jurisdiction is comfortable with AACs and a prospective litigant would be well advised to conduct due diligence regarding the use of an AAC in advance, adjusting the underlying contract and dispute resolution clause accordingly.

Should a Party Agree to an Asymmetric Arbitration Clause?

The party with the greater bargaining power usually has a better chance of "persuading" the other party to reserve the right to choose between the various options for settling disputes. [10] However, for the economically weaker party, it does not necessarily always have to be disadvantageous to agree to an AAC.

Depending on the legal system, it could be a case where the AAC is invalid or unenforceable, which in turn could give the economically weaker party an advantage. On the other hand, the weaker party does not give up its legal position completely even if it accepts a valid AAC. The case will be heard in one way or another before an independent judicial institution, be it a Court or an arbitral tribunal.

Which Countries Consider AAC's to be Valid and Enforceable?

We will first look at the ways on how AACs can be agreed upon in a valid and enforceable manner. This depends largely on the agreed jurisdiction. For better comprehensibility and clarity, we will examine selected venues and their jurisdictions in detail.

Singapore

In *Wilson Taylor Asia Pacific Pte Ltd v Dyna-Jet Pte Ltd* [2017] SGCA 32 [11] the Singapore Court of Appeal had to decide whether the agreed asymmetrical arbitration clause was valid. The clause in dispute read as follows:

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> *“Any claim or dispute or breach of the terms of the Contract shall be settled amicably between the parties by mutual consultation. If no amicable settlement is reached through discussions, at the election of Dyna-Jet, the dispute may be referred to and personally settled by means of arbitration proceedings, which will be conducted under English Law; and held in Singapore.”* [12]

This was the first decision of the Court of Appeal regarding the validity of asymmetric arbitration clauses. In its decision, the Court stated that despite its asymmetrical nature, the clause between the parties was a valid arbitration agreement. More specifically, the fact that only one party gets to choose how the dispute should be resolved is not inconsistent with the meaning or nature of an arbitration agreement and fell within the meaning of section 2A of the International Arbitration Act. [13]

We can conclude from this that the Court of Appeal in Singapore sees no problem in granting the parties considerable private autonomy when it comes to resolving how they want to settle their disputes. The protection of the individual party, having the same means of dispute resolution at its disposal, therefore appears to be of lesser importance. Singapore thus seems to be a safe choice for parties wanting to use an AAC. This is further proof that Singapore’s Courts respect party autonomy. It can be assumed that the Singapore Courts will review the scope and content of the underlying dispute as well as the corresponding clause before deciding as to whether or not this will ultimately result in the dispute being referred to arbitration. [14]

Germany

German Law does not forbid the use of AACs. The German Courts have also yet to invalidate the use of AACs. This applies at least in cases where the clause had been freely negotiated. The same cannot be said if the clause had been introduced into the agreement through the use of general terms and conditions. [15]

Section 307 of the German Civil Code states that:

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> *“Provisions in the General Terms and Conditions shall be ineffective if they unreasonably disadvantage the contractual partner of the User contrary to the requirements of good faith. […]”*

In its decision of 24 September 1998,[16] *the Bundesgerichtshof*[17] *determined a case in which such unreasonable disadvantage was deemed to have existed. This would be the case if, at the time the appeal was lodged, the contracting party of the AAC's beneficiary did not know whether the benefitting party would be exercising their right of option.* The party therefore runs the risk of having its action (that it had brought before the competent state court) become inadmissible due to objections towards arbitration. This risk, associated with loss of costs and time, is, according to the German Court, not a reasonable one for the contractual partner. Such unreasonable disadvantage can be eliminated by a supplementary agreement which obliges the user of the AAC (where such party is the would-be Defendant), to exercise its right to decide whether it wants to resolve the dispute through arbitration or litigation at the request of the other party before the trial. The additional agreement also needs to address the consequences of a refused or delayed decision. In the present case however, such an agreement had been completely absent.

The *Bundesgerichtshof* did not decide directly in its decision that the use of an AAC in general would be null and void. Therefore, it can be assumed that an AAC is valid to the extent that it contains a clause protecting the disadvantaged party from the inadmissibility of an action brought before a Court because the beneficiary party decided to exercise its right to the option afterwards. Of course, something else could apply under German Law if the AAC is not a general contract term, but a freely negotiated clause.

China

In the Chinese commercial sector (as opposed to its labour sector) AACs that lead to arbitration are invalid.

Article 7 of the interpretation of the Supreme People's Court on the application of the People's Republic of China Arbitration Law states that:

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> *"Where the parties concerned agree that they may either apply to the arbitration institution for arbitration or bring a lawsuit with the people's court for settlement of dispute, the agreement for arbitration shall be ineffective, unless after one party applies to the arbitration institution for arbitration, the other party fails to propose any objection within the period prescribed in Paragraph 2 of Article 20 of the Arbitration Law."*[18]

It can therefore be said that in principle, AACs are not valid under Chinese Law. On 26 December 2017, the Supreme People's Court of China released a new judicial interpretation – the Provisions of the Supreme People's Court on Several Issues concerning Deciding Cases of Arbitration-Related Judicial Review.[19] *According to Article 14 of the new interpretation, an AAC could be valid to the extent that it is included in a foreign-related contract.*

Article 14 of the Judicial Interpretation states that:

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> *“A people’s court shall, when deciding the law applicable to the recognition of the effect of a foreign-related arbitration agreement under Article 18 of the Law of the People’s Republic of China on Choice of Law for Foreign-Related Civil Relationships, invoke the law recognizing the effect of the arbitration agreement, where neither party chooses an applicable law, and the application of the law in the place of the arbitral institution will lead to a recognition conclusion regarding the effect of the arbitration agreement different from that of the law in the place of arbitration.”*

The Judicial Interpretation came into force on 1 January 2018 and it can be expected that because of it, the People’s Court may now be more inclined to accept the validity of an AAC in a foreign-related contract – if there is no choice of the governing law, the Court is required to apply the law under which the clause is effective. [20]

India

Decisions taken by Indian courts regarding the validity of AACs seem to be inconsistent. The sticking point under Indian Law is that there must be reciprocity in an arbitration agreement. [21] *The Indian Courts have also had to decide whether they ought to uphold the validity of AACs in the interest of party autonomy or to intervene on public policy grounds.* [22]

In the decision Union of India vs Bharat Engineering, [23] *the Delhi High Court held that the mutuality under the agreement should exist from the moment the beneficiary party exercised its right to choose. However, in its decision Emmsons International Ltd. vs Metal Distributors,* [24] *the same Court denied the validity of the AAC due to its asymmetry.*

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> *“[…] being in the nature of a unilateral covenant depriving the plaintiff to enforce its right under the contract either through the ordinary tribunals set up by the State or through alternate dispute resolution mechanism is void and cannot be enforced in India.”*

The contradictory judgments of the High Courts, especially in the absence of a clear decision of the Indian Supreme Court, provide no legal clarity and certainty for parties seeking to secure their rights from AACs. [25]

United Kingdom

Under English Law, AAC s are valid and enforceable. The English Courts will confirm the parties' agreement on the dispute settlement procedure applicable to their contract [26] irrespective of whether the parties' dispute resolution clause is asymmetric. [27]

France

Even though the French Courts' line of decisions over the last 40 years [28] is not entirely clear, one of the latest decisions containing an AAC [29] seems to lead in the direction that AACs are generally valid under French Law, provided that the choice offered to the beneficiary party is narrowly defined, limited and predictable. [30]

Russian Federation

If parties want to use asymmetric arbitration clauses in the Russian Federation, they have to make sure that this type of clause is enforceable in their country of choice. This is due to the fact that in some jurisdictions, the asymmetric arbitration clause is seen as incompatible with the cornerstone principle of agreement between the parties. [31] The beneficiary party may invoke the AAC directly in accordance with the agreement between the parties. [32] If the AAC is valid in the relevant jurisdiction, the arbitration proceedings can then continue as usual.

Are AACs in Violation of European Union Law?

It is arguable that an AAC inherently involves a certain imbalance between the parties. This leads to the question of whether an AAC is compatible with the European Convention on Human Rights (**ECHR**). [33] More specifically: does an AAC negatively affect the right to a fair trial as insured by Article 6 of the ECHR?

> *"In the determination of his civil rights […], everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law. Judgment shall be pronounced publicly […]." Article 6 Section 1 ECHR*

Some authors believe that the institution of a "fair trial" regarding Article 6 of the ECHR only insures procedural rights, which means that the parties are granted equal rights before a specific forum and not the choice of the forum. [34]

Others see the use of an AAC and some other general arbitration practises as contrary to Article 6 of the ECHR (for example hearings in (commercial) arbitrations are generally not open to the general public) but focus on the waiver of rights provided under Article 6 ECHR. [35] Since the principle of arbitration itself does not violate Article 6 of the ECHR there is a possibility to wave the rights granted by Article 6 of the ECHR but for the waiver to be valid, a number of things must be taken into account. First of all, the waiver must be freely agreed upon. In addition to that, the waiver must be made in writing and be "unequivocal". [36]

What Should Parties Consider When Drafting or Using AACs?

When drafting arbitration clauses, parties need to ensure that these are tailored to the specific circumstances of their individual contract and jurisdiction. Of course, if parties want to use AACs, they should first check whether the use of AACs is approved in the relevant jurisdiction. Since the validity of an AAC – as summarised above – is not always easy and clear to determine, the following points should be given even more attention. It is important that such clauses are drafted as narrowly, clearly and precisely as possible. Besides that, one should:

- Draft the litigation and arbitration clause as separate clauses so that the validity of one clause doesn't affect the other one;
- Make sure that the standard clause is reasonable, adequate and acceptable; and
- Determine the point in time when the beneficiary party must exercise its right to exercise its option and also what happens in the event of refusal.

Conclusion

Even though the use of AACs seems rather common, the validity of an AAC is dependent on the jurisdiction of the country that the parties choose.

Some countries, such as Singapore, do not seem to have a problem with giving one party in the agreement more power and choice than the other party. Other countries, such as China, have a different view and do not agree with the concept of unilateral option clauses.

It can be argued that an AAC can lead to the exploitation and deepening of the economically dominant party's position of power as it gives one party more opportunities than the other. On the other hand, one of the core principles of private autonomy is to not only tailor the proceedings according to the parties' wishes, but also the right to waive certain rights. Although the beneficiary party will naturally always choose the procedure that it considers best for itself, it should not be forgotten that an AAC implies the choice between different dispute resolution procedures. In other words, no matter what the beneficiary party decides, the end result will be that a judicial institution will always be appointed that will follow due process considerations, be it in the context of Court or arbitration proceedings.

Parties seeking legal certainty however should refrain from using an AAC or limit themselves to “safe” locations such as Singapore or the United Kingdom, which fully recognise the validity of AACs.

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Dr Andreas Respondek

Rechtsanwalt (D), Attorney at Law (USA), Chartered Arbitrator (FCIArb)
Respondek & Fan Pte Ltd
E-mail: respondek@rflegal.com

Frederike Marina Löwenthal

Assessor
Respondek & Fan Pte Ltd