Investment Arbitration's Precarious Perch: A Jurisprudential Lack of Consensus on Pre-Conditions

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Introduction

Investment arbitration, hailed as a cornerstone of international trade and investment, finds itself embroiled in a critical debate regarding the interpretation and application of pre-conditions to arbitration. This article delves into the heart of this debate, analysing the lack of consensus within the jurisprudence and its implications for the legitimacy and effectiveness of the system.

Investment arbitration is a method of resolving disputes between foreign investors and host states. Typically, these disputes arise from breaches of investment agreements, bilateral investment treaties (BITs), or other international agreements. Arbitration clauses within these agreements often contain pre-conditions that must be met before initiating arbitration proceedings. These pre-conditions serve various purposes, including negotiation periods, cooling-off periods, and requirements for amicable settlement attempts.

What are pre-conditions or pre-arbitration procedures?

Many arbitration agreements chart a multi-step journey before reaching formal arbitration. These "pre-arbitration procedures," sometimes called "conditions precedent" or "multi-tier clauses," involve taking specific steps before initiating arbitration. This might involve direct discussions between parties to seek an amicable resolution, seeking a designated individual's decision, or engaging a mediator to facilitate settlement. These procedures aim to encourage quicker, less costly solutions before resorting to formal arbitration, while also preserving confidentiality. However, navigating this multi-tiered path can be complex, potentially introducing delays, uncertainties, and even manipulation risks. Despite these challenges, pre-

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arbitration procedures remain a valuable tool for resolving disputes efficiently and amicably, provided they are approached with understanding and care.[i]

The crux of the issue lies in the absence of a unified approach to interpreting and applying these pre-conditions. Arbitral tribunals, tasked with determining whether pre-conditions have been met, exhibit a wide spectrum of interpretations, leading to inconsistent and sometimes contradictory outcomes.

In India, the Supreme Court has not issued a definitive judgment regarding the legal classification of MTDRC (Multi-Tiered Dispute Resolution Clause). This article explores the differing perspectives adopted by courts concerning MTDRC. The authors also examine the 'claims v. tribunal test' in detail, evaluating its applicability in determining whether a specific MTDRC is obligatory or merely advisory.

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Comparison of Stands for Pre-condition, Mandatory v/s Directory

Mandatory

In the case of United India Insurance[ii], the arbitration clause contained a specific provision dictating that any disputes regarding the quantum of payment under the policy would be settled through arbitration. However, a crucial condition was attached: if the insurance company contested the claim made under the policy, arbitration proceedings could not be initiated. In this context, the Hon'ble Supreme Court, drawing from its earlier decision in Oriental Insurance Company Ltd Case.,[iii] adhered to a stringent interpretation of the arbitration clause. The Court emphasized that the insurance company's refusal to acknowledge the claim as valid was a prerequisite, an indispensable condition for the claim to become arbitrable. Consequently, the Court construed the Multi-Tiered Dispute Resolution Clause (MTDRC) as a precondition, highlighting that the tribunal could not assert jurisdiction unless the prescribed procedural requirements were satisfied. These ruling underscores the significance of adhering to the procedural prerequisites outlined in arbitration clauses, ensuring that disputes are resolved in accordance with the terms agreed upon by the parties involved.

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Directory

In a separate legal matter involving Demerara Distillers Ltd.,[iv] the predetermined conditions were not rigorously enforced as expected. In this particular instance, the involved parties were initially required to engage in mediation and mutual discussions before escalating the claim to arbitration. However, the approach taken by the Honourable Supreme Court diverged from the stringent interpretation of these preconditions. The Court deemed the pre-arbitration process as more of a procedural formality rather than an obligatory step that warranted strict adherence. The essence of the Court's perspective underscored the notion that the Multi-Tiered Dispute Resolution Clause (MTDRC) should not unduly impede the progression of arbitration proceedings.

Similarly, a comparable stance was adopted in the case of M/S Incomm Tele Ltd.,[v] where a provision within the arbitration clause necessitating a 10% deposit of the claim amount before arbitration could commence was challenged. The Court, in its judgment, struck down this requirement, citing concerns about its potential to delay the swift resolution of disputes. The Court's rationale highlighted the overarching objective of arbitration: to facilitate the expeditious resolution of conflicts. Imposing such financial prerequisites, the Court argued, could impede access to justice and prolong the process of seeking relief.

Therefore, the decisions rendered by the Supreme Court in both instances reflect a broader judicial inclination towards prioritizing the efficiency and accessibility of arbitration mechanisms. By mitigating procedural hurdles and streamlining the dispute resolution process, the Court endeavours to uphold the fundamental principle of delivering timely and equitable justice to all parties involved.

Using Tribunal v. Claims test to determine the mandatory or directory nature of MTDRC

The 'Tribunal v. Claims test' is a crucial framework used to discern the nature of Multi-Tiered Dispute Resolution Clauses (MTDRCs). It delineates whether an MTDRC primarily challenges the constitution of the arbitral tribunal or contests the validity of the claim itself. This test is pivotal in distinguishing between issues of jurisdiction and admissibility within arbitration proceedings.

When an MTDRC raises objections to the formation of the tribunal, it essentially questions the jurisdiction of the tribunal to even exist. This means that without adhering to the prescribed pre-arbitration procedures, the tribunal lacks the authority to be formed. In contrast, if the MTDRC challenges the substance of the claim itself, it becomes a matter of admissibility. Under the principle of kompetenz-kompetenz, the tribunal can determine its own jurisdiction and decide whether the claim is suitable for arbitration.

Recent judicial decisions, such as BSNL v. Nortel[vi] the Supreme Court of India and Swisbourgh Diamond Mines (Pty) Ltd. & Ors. v. Kingdom of Lesotho[vii] in the Singapore Court of Appeal, have provided valuable insights into the application of the 'Tribunal v. Claims test'. These cases have underscored the distinction between jurisdiction, which pertains to the tribunal's power to hear a particular case, and admissibility, which concerns the appropriateness of the tribunal adjudicating the case.

In essence, the test serves as a litmus test to determine the mandatory or directory nature of an MTDRC. If a pre-arbitration procedure specified in the arbitration clause is fundamental to the formation of the tribunal, it is deemed mandatory. In such cases, the tribunal cannot come into existence until the prescribed procedures are fulfilled. On the other hand, if the procedure is not pivotal to the tribunal's formation, it is considered directory. In such instances, the tribunal can be constituted first, and it can subsequently assess whether the particular MTDRC needs to be adhered to before proceeding with the merits of the claim.[viii]

This was India’s divergent stand on Pre-conditions, in the next segment let us discuss the stand of other states on the idea of pre-conditions for investment arbitration.

Approach of Foreign States

The United Kingdom

The United Kingdom has adopted a varied approach towards Multi-Tiered Dispute Resolution Clauses (MTDRCs). In the landmark case of Emirates Trading Agency LLC v. Prime Mineral Exports Pte Ltd.,[ix] the England and Wales High Court determined that the failure to comply with an MTDRC constitutes a jurisdictional issue. It decreed that arbitration proceedings

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cannot commence unless the MTDRC conditions are fulfilled, thus deeming the pre-arbitration condition mandatory.

Conversely, in Sierra Leone v SL Mining Limited,[x] a different stance was taken. In a scenario akin to M/s Oasis Projects, where parties were required to undergo LCIA Mediation before resorting to LCIA Arbitration, the court considered the kompetenz-kompetenz principle. It affirmed that arbitrators hold the authority to determine their own jurisdiction. Consequently, the court deemed it within the arbitrator's discretion to assess whether the failure to engage in mediation breached the MTDRC. In this instance, the court treated the specific procedure outlined in the MTDRC as a matter of admissibility rather than jurisdiction.

These cases illustrate the divergent approaches taken by the UK legal system towards MTDRC interpretation. While Emirates Trading emphasizes strict compliance with pre-arbitration conditions as mandatory prerequisites for arbitration, Sierra Leone v SL Mining Limited underscores the judiciary's acknowledgment of arbitrators' authority to evaluate procedural compliance under the kompetenz-kompetenz principle. These decisions highlight the nuanced considerations and judicial discretion involved in navigating MTDRCs and their implications within UK arbitration proceeding.[xi]

The United States

In the United States, there is a prevailing perspective that pre-arbitral procedures outlined in multi-tiered clauses do not necessarily block the formation of the tribunal, thus characterizing the MTDRC as directory rather than mandatory. In the case of BG Group plc v. Republic of Argentina,[xii] the US Supreme Court ruled that conditions precedent were procedural matters and that pre-arbitral steps specified in multi-tiered clauses do not serve as jurisdictional prerequisites unless expressly stated otherwise. However, in instances such as Kemiron Atlantic Inc v. Aguakem International Inc[xiii], US courts have deemed pre-arbitral steps in multi-tiered clauses as jurisdictional prerequisites for arbitration, even in the absence of explicit language indicating such conditions.

To summarize, US courts haven't explicitly stated that MTDRCs are not conditions precedent for initiating arbitration. Instead, they maintain that arbitral bodies are better positioned to determine the consequences of non-compliance, rather than the courts themselves.[xiv]

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Singapore

Until 2019, it seemed that Singapore courts considered non-compliance with pre-arbitral requirements in multi-tiered dispute resolution clauses as having significant jurisdictional consequences. For instance, in cases like International Research Corp PLC v. Lufthansa Systems Asia Pacific Pte Ltd and another, the Singapore Court of Appeal established that meeting these pre-arbitral conditions was obligatory, and failure to do so could result in the arbitral tribunal losing its jurisdiction. However, the perspective changed in 2020 with the case of BTN v. BTP,[xv] where the Singapore Court of Appeal ruled that arbitrators, themselves should determine the enforceability of pre-arbitration conditions. This decision signalled a shift towards viewing multi-tiered dispute resolution clauses as advisory rather than obligatory.[xvi]

Moving forward, the absence of conclusive rulings in foreign jurisdictions mirrors the case-by-case approach adopted by Indian courts concerning the interpretation of pre-arbitration requirements. Given this scenario, embracing the 'Tribunal v. Claims' test to ascertain the nature of Multi-Tiered Dispute Resolution Clauses (MTDRCs) in India could be a positive development. For instance, in the United India Insurance case, the mandatory nature of the requirements fundamentally challenged the establishment of the tribunal. Compliance with pre-arbitration requirements became imperative for tribunal formation. Consequently, applying the claim v. tribunal test could directly address the formation of the arbitral tribunal, thus categorizing the MTDRC as mandatory.[xvii]

Conclusion

In conclusion, the landscape of investment arbitration jurisprudence reveals a profound lack of consensus regarding the interpretation and application of pre-conditions to arbitration included in dispute resolution clauses. This lack of uniformity poses significant challenges for investors, states, and arbitrators alike, leading to inconsistencies in decision-making and potentially undermining the integrity of the arbitration process.

Despite efforts to address these challenges, both domestically and across foreign jurisdictions, no conclusive rulings have emerged. Instead, courts and tribunals continue to adjudicate pre-condition disputes on a case-by-case basis, contributing to a fragmented body of jurisprudence.

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Considering this uncertainty, the proposal to adopt the 'Tribunal v. Claims' test in India represents a welcome step forward. By emphasizing the mandatory nature of pre-arbitration requirements, this approach provides clarity and certainty in determining the enforceability of Multi-Tiered Dispute Resolution Clauses (MTDRCs). The United India Insurance case serves as a pertinent example, highlighting the pivotal role of pre-condition adherence in tribunal formation.

Moving forward, stakeholders must remain committed to fostering dialogue and collaboration to promote greater coherence and consistency in investment arbitration jurisprudence. Efforts to standardize pre-condition language, enhance transparency, and encourage best practices can help address the existing lack of consensus, thereby reinforcing the effectiveness and legitimacy of investment arbitration as a means of resolving disputes between investors and states. Only through continued engagement and innovation can the challenges surrounding pre-conditions to arbitration be effectively navigated, ensuring a fair and equitable resolution for all parties involved in investment disputes.

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Endnotes

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