Don't Forget These Points When Negotiating the Arbitration Clause of Your International Construction Contract

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Don't Forget These Points When Negotiating the Arbitration Clause of Your International Construction Contract

By David W. Salton*

With several economic forecasts predicting a rise in oil prices for the rest of 2017 and 2018, domestic and foreign companies might find themselves more frequently negotiating construction contracts. A key consideration when drafting agreements is whether to resolve any disputes in the courts or through an alternative dispute resolution procedure, like arbitration. In a global economy, companies embroiled in cross-border disputes are trending towards using arbitration to offer quicker resolution and flexibility.[1] Aside from more-obvious decisions like choice of law, there are many sub-issues to consider when crafting the dispute resolution clause, such as: (i) which institution will administer the arbitration; (ii) where venue will lie; (iii) the type of discovery permitted; and (iv) dealing with old (and possibly untimely) claims.

A. What institution will administrate the dispute?

Before drafting other portions of an arbitration clause, decide which institution will administer the arbitration. Three well-known international institutions that are not industry-specific[2] are: (i) the International Centre for Dispute Resolution ("ICDR"), which is the international branch of the American Arbitration Association ("AAA"); (ii) the International Court of Arbitration, which administers arbitrations under the International Chamber of Commerce ("ICC"); and (iii) the London Court of International Arbitration ("LCIA"). Each body has its own features.

As just one example of many, arbitration costs under the ICC generally are determined at the beginning of the arbitration on a fixed-fee basis (subject to adjustment), depending on the amount in dispute. Conversely, arbitration costs under the ICDR generally are incurred based on the time and resources the tribunal dedicates to the matter. While inflated claims may unnecessarily result in a higher fixed-fee in ICC arbitration—thereby favoring ICDR arbitration at a surface level—the fixed-fee structure arguably promotes efficiency, which ultimately helps minimize costs to the parties. In fact, within the last few months the AAA sent out a survey addressing this exact point; namely, whether to offer alternative fee structures in the future. Meanwhile, the LCIA presents a middle-of-the-road approach, whereby the default is to utilize hourly rates with a not-to-exceed amount, while also offering the flexibility to fix fees in exceptional cases.

Choosing whether to arbitrate under the ICDR, ICC, LCIA, or any other institution is purely a manner of preference and, similar to setting the scope of discovery (discussed below at Section C), is certainly worth devoting meaningful thought to when negotiating a dispute resolution clause.

B. Where will venue lie?

Many times, parties will seek to have a dispute decided in their home state or country. However, the laws of many states make void—as being against public policy—any provision in a construction contract that requires litigation or arbitration to be conducted in a state *other than* where the construction work is performed.

For example, New York makes "void and unenforceable" any provision in a construction contract making the contract subject to the laws of another state or requiring litigation or arbitration to be conducted in another state.[3] New York law has an exception for contracts with someone who supplies materials.[4] Arizona's laws go further by expressly *requiring* that "any mediation, arbitration or other dispute resolution proceeding arising from a construction contract for worked performed in this state shall be conducted in this state."[5]

Conversely, Texas is less restrictive in that it makes such contracts "voidable" (rather than unenforceable) "by the party obligated by the contract to perform the construction or repair."[6] And while Colorado law provides that any construction agreement affecting real property in Colorado will be subject to Colorado law, it does not expressly require that Colorado be the venue for any dispute.[7]

Not every state has statutes addressing this matter. Consequently, it is essential to review the specific laws of the state where the construction will be performed in conjunction with negotiating the dispute resolution, choice of law, and venue clauses.

C. What type of discovery will be permitted?

Particularly in the United States, which generally allows broad discovery under federal and state court rules, arbitration is viewed as a desirable alternative for its comparatively-limited exchange of information. With near uniformity, institutional rules require tribunals to establish the facts of the case as quickly as possible[8] and conduct the proceedings with a view towards expediting the resolution of the dispute.[9] The tribunal in international arbitration generally retains final authority to manage the exchange of information, so long as it does so in an efficient and economic manner.[10] The International Bar Association Rules on the Taking of Evidence ("IBA Rules") are often incorporated into dispute resolution clauses or agreed-to during the course of the arbitration proceeding. Those rules provide for document requests[11] but not other types of discovery frequently used in United States litigation, *e.g.,* interrogatories, requests for admissions, or depositions. Indeed, it is not unusual for litigators unaccustomed to the nuances of discovery in international arbitration to carry a belief of entitlement to discover certain types of information—only to find out their belief is shared by neither their adversary nor the tribunal.[12]

Yet, there also are certain disputes where discovery beyond document requests may be warranted, such as a complex construction dispute involving numerous fact witnesses. "The construction and design industry imposes unique problems on an attorney seeking information in connection with an arbitrated or litigated dispute. Unlike other disputes, construction and design disputes do not involve limited numbers of participants or repeat fact patterns."[13] Construction and design disputes "require evaluation of extensive documentation and other information."[14] Put differently, "discovery in construction litigation is generally an extensive undertaking involving an overwhelming amount of information and requiring a large number of professional hours. The enormity of the undertaking underscores the need for planning before implementation."[15] "Often attorneys embark on discovery without conscious planning. In such a case the discovery program may proceed without direction and without success. Thus, time involved in planning will be well spent and may achieve significant results for clients."[16]

Therefore, in such cases and under the right circumstances, other forms of discovery may be appropriate or necessary to help streamline the process and cut to the heart of the dispute.[17] One alternative is to contractually allow the taking of depositions after showing a compelling need, which—at the time the party seeking such discovery makes its application—must be coupled with a description of the specific topics to be covered. Or, perhaps after due consideration, the parties opt to follow the traditional view in international arbitration of limited discovery, irrespective of the subject matter in dispute, and preclude depositions.[18] Either way, because discovery is time-consuming, expensive, and susceptible to abuse, it may be worth dealing with the matter on the front-end.

D. Do statutes of limitations apply in Arbitration?

Perhaps surprisingly, there are a number of authorities indicating that by agreeing to arbitrate, a party gives up its right to assert a "statute of limitations" affirmative defense[19] that would otherwise be available in state or federal court. Underlying this view is a distinction that some courts draw between an "action" and a "suit." For instance, in *Har-Mar, Inc. v. Thorsen & Thorshov, Inc.,* the Minnesota Supreme Court concluded that the term "action" was "restricted [] to the prosecution in a court of justice of some demand or assertion of right by one person against another" and was "intended to be confined to judicial proceedings."[20]

The objective of this article is not to opine on which view is correct, but to instead point out that there are authorities on each side of the issue[21] and recommend an easy solution. To avoid an unanticipated defense, consider starting the dispute resolution clause with the following: "Within any applicable limitations or repose period, either party may demand arbitration by filing a Notice of Arbitration with the [ICC/ICDR/LCIA/etc.]…." Such language should provide sufficient protection against stale claims—and also help avoid a potentially-expensive battle about whether the parties intended that statutes of limitations apply to their dispute.

E. Conclusion

Arbitration is a creature of contract. A party can be compelled to arbitrate only if it agrees to do so and only in the manner in which it agrees. There are many nuances to arbitration that are often afterthoughts, or not thought about at all. Addressing these issues up front, and before construction is underway, can eliminate time-consuming disagreements after arbitration commences. If carefully planned, it may even provide an advantage during the course of the proceeding.

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[1] Jane Croft, *Arbitration on the rise for cross-border disputes*, Financial Times (April 9, 2017), https://www.ft.com/content/bf0bc638-1baf-11e7-a266-12672483791a.

[2] *E.g.*, the Financial Industry Regulatory Authority, known as "FINRA," and the Internet Corporation for Assigned Names and Numbers, known as "ICANN," are specialized fora.

[3] N.Y. Gen. Bus. Law §757.

[4] *Id.*

[5] A.R.S. §32-1129.05.

[6] Tex. Bus. & Comm. Code §272.001.

[7] Colo. Rev. Stat. §13-21-111.5(6)(g).

[8] ICC Rules of Arbitration, Article 25.

[9] International Dispute Resolution Procedures ("ICDR Rules"), Article 20 (Effective June 1, 2014).

[10] ICDR Rules, Article 21; *see also* LCIA Rules, Article 22 (providing tribunal with power to order production of relevant documents).

[11] *See* IBA Rules, Article 3.

[12] *See* Redfern and Hunter on International Arbitration, 6.94 (6th ed., 2015). For more on the differences between discovery in litigation and international arbitration, *see* Giacomo Rojas Elgueta, *Understanding Discovery in International Commercial Arbitration Through Behavioral Law and Economics: A Journey Inside the Minds of Parties and Arbitrators*, 16 Harv. Negot. L. Rev. 165 (Spring 2011).

[13] Callahan, Bramble, and Rapoport, Discovery in Construction Litigation, p. 1 (1987) (2nd Ed.).

[14] *Id.* at 18.

[15] *Id.* at 17.

[16] *Id*.

[17] *See, e.g.,* William G. Horton, *"Discovery" in International Arbitration*, Canadian Arbitration and Mediation Journal, 26 (Spring 2011) (noting the unfortunate and unhelpful situation where anyone advocating for anything beyond document production "is accused of attempting to 'Americanize' international arbitration.").

[18] Without such agreement, the majority view of narrow discovery will likely be the default, such that arbitrators will be encouraged to use their discretion narrowly when considering discovery requests. Giacomo Rojas Elgueta, *Understanding Discovery in International Commercial Arbitration Through Behavioral Law and Economics: A Journey Inside the Minds of Parties and Arbitrators*, 16 Harv. Negot. L. Rev. 165, 171 (Spring 2011) (citing Robert von Mehren, Rules of Arbitral Bodies Considered from a Practical Point of View, 9 J. Int'l Arb. 105, 111 (1992)); *see also* 24 Am. Rev. of Int'l Arb. No. 4 at 553-54, Obtaining and Submitting Evidence in International Arbitration in The United States, Claudia T. Salomon and Sandra

Freidrich (2013) ("Indeed, the limited availability of disclosure in international arbitration is a key difference between judicial and arbitral proceedings.").

[19] *See, e.g., NCR Corp. v. CBS Liquor Control, Inc.,* 874 F. Supp. 168, 172-73 (S.D. Ohio 1993) ("the Arbitrator was correct in holding that the statute of limitations is not directly applicable in arbitration….").

[20] 218 N.W.2d 751, 754 (Minn. 1974).

[21] *Nielsen v. Barnett,* 485 N.W.2d 666, 667 (Mich. 1992) (concluding that policies underlying statutes of limitations "are equally relevant both to actions filed in court and to claims pursued in binding arbitration.").

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