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International Commercial Arbitration vs. U.S. Commercial Litigation – Key Differences

Client Advisories

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Introduction

Companies doing business internationally often insert arbitration clauses in their contracts. They do so for good reasons. One is to ensure that future disputes will be resolved in a neutral forum, not in the home court of the counterparty. Another is to maximize the chances that the decision will be enforceable where the counterparty's assets are located. Indeed, foreign courts are generally under no obligation to recognize and enforce U.S. court judgments. By contrast, under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the "New York Convention"—a treaty in force in over 160 countries—decisions rendered by arbitrators (known as "arbitral awards") benefit from a favorable enforcement regime.

While the benefits of arbitration to resolve disputes arising from cross-border transactions are generally well understood, the same is not true of the differences between international commercial arbitration and U.S. commercial litigation. On the surface, U.S. litigation and international arbitration may appear similar. But there are crucial differences between them that the parties should consider.

Consent

Arbitration is a dispute resolution mechanism in which a third-party neutral is empowered by agreement of the parties to issue a binding legal decision. In this way, arbitration may appear similar to a court proceeding, with adverse parties pleading their case before a neutral decisionmaker. However, the arbitral process is fundamentally based on the parties' consent, and everything about the process derives from that mutual consent. By contrast, so long as a U.S. court has jurisdiction over a claim between the parties, all it takes is one party to sue in court and force the other to defend itself, regardless of whether or not the defendant consents to that process.

Before any arbitral process begins, the parties to that process must have first agreed to resolve their dispute through arbitration. The parties' consent to arbitration may be memorialized in one of two ways:

- In most cases, the parties' consent to arbitrate is given in advance by inserting a provision (an "arbitration clause") into a relevant contract, requiring any dispute arising from that contract to be resolved by arbitration.
- Parties may also refer an existing dispute to arbitration by concluding a submission agreement; however, such submission agreements are much less common than pre-dispute arbitration clauses embedded in relevant contracts.

Following such an agreement to arbitrate, an arbitral tribunal will have the power to hear and adjudicate the parties' dispute. This of course will not stop an unwilling party from arguing that an arbitral tribunal lacks jurisdiction, meaning that they do not have authority to arbitrate the specific dispute between the parties. In practice, jurisdictional objections are not uncommon in international commercial arbitrations.

Third parties that are not bound by the underlying arbitration agreement may not be named a respondent in an arbitration. This occasionally creates difficulties in multi-party, multi-contract transactions, especially in the presence of layers of corporate entities. For example, an arbitration agreement may extend to include a non-signatory that shares ownership with, or is a subsidiary to, a signatory, depending on the body of law, the rules of the forum, and the specific contours of the arbitration agreement.

As a result, parties contemplating arbitration need to carefully consider who the proper parties to the arbitration agreement should be, and whether additional measures are needed prior to beginning arbitration.

Procedural flexibility: a process with few hard rules but many soft ones

Whereas court proceedings are governed by detailed and often rigid rules of procedure, arbitration is more flexible. Because it is based on the parties' consent, the arbitral process varies widely case by case and the parties have much freedom to adapt the procedure to their circumstances.

Take for example the costly process of document production, known in U.S. litigation as part of "discovery." Parties to U.S. court proceedings often have broad rights and responsibilities with respect to the search and exchange of records that are relevant and material to the dispute. Depending on the complexity of the dispute, this process can be extremely time-consuming and expensive.

In a commercial arbitral proceeding, document production is generally much more limited, and in some circumstances the parties may be able to agree to skip the process entirely. Doing so, or otherwise restricting the scope of document production, can greatly reduce costs for the parties. However, the tradeoff is that the parties will have to pursue their claims with less information and documentary support than they otherwise would in a U.S. court proceeding. In effect, a claimant in arbitration may have to prove its case out of its own files.

Arbitral practice involves countless unwritten rules and best practices which often vary from forum to forum and are not readily apparent to outsiders. This creates an informational asymmetry between frequent and occasional participants in arbitration; retaining experienced counsel may thus drastically increase the chances of winning a case.

A chance to pick the decision-maker

Before substantive proceedings begin, parties in a commercial arbitration have the opportunity to select the arbitrator (or arbitrators), who will adjudicate their dispute. The process for the selection and composition of the arbitral tribunal varies based on the parties' arbitration agreement, including the rules of any agreed upon arbitration institution.

In arbitration, selecting the arbitrator (or arbitrators) is often considered the most important phase of the case. Inexperienced practitioners, who have not had a chance to work for, alongside, or against potential arbitrators are less likely to accurately gauge how a potential arbitrator may approach the issues underlying the dispute. In addition, the procedural maneuvering around the appointment of arbitrators, including challenges to an arbitrator's appointment,

requires not only strategic consideration, but familiarity with the forum, rules, norms and real-life circumstances, which may lead to potential disqualification. This, again, advantages experienced arbitration practitioners, who are familiar with both – the rules and the people in arbitration.

Generally, commercial arbitration has a distinct advantage over litigation when a dispute involves highly specialized knowledge. This is because the parties often can select arbitrators that have past experience relevant to the dispute at hand. Doing so can save time and legal fees by reducing the need to educate the arbitrators in a particular area. By contrast, in U.S. court proceedings the parties are limited in their ability to select a venue for the adjudication of their dispute, let alone a particular judge to hear their dispute. (There are certain exceptions within U.S. courts, including patent litigation, which is highly concentrated before only a handful of district court judges.)

Advocacy style

Advocacy (both written and oral) looks very different in international commercial arbitration than in U.S. commercial litigation.

At the risk of overgeneralization, good written advocacy matters more in international arbitration than litigation. In many cases, parties' written pleadings will take the form of so-called "memorials." A memorial not only sets out a party's claims and defenses in full, but it also attaches all supporting evidence from documents, witness statements, expert reports, and legal authorities. Arbitrators will then rely heavily on those submissions in making their award.

This consolidation of information in international commercial arbitration is distinct from U.S. commercial litigation, which is typically marked by piecemeal submissions: Following the completion of the discovery phase (which frequently involves multiple and extensive requests), parties may be given a chance to file dispositive motions, with attendant briefs in support. Finally, they will compose pre-hearing submissions, which may refer to, but not replicate, arguments made in their prior submissions. That multi-step process, where argument is spread over many documents, contrasts starkly with international arbitration practice.

Oral advocacy also tends to be less belligerent in international commercial arbitration than U.S. court litigation. Most arbitrators will be unimpressed by overly aggressive cross-examinations, overheated rhetoric, bombast and factual overstatements. Adapting one's advocacy to the tribunal is also a skill that takes more importance in international arbitration, where the decision-makers routinely come from different jurisdictions.

Hearings in international commercial arbitration often look quite different from U.S. court trials as well. Often, hearing rooms more closely resemble large conference rooms than formal courtrooms. Advocates typically present their case sitting down rather than standing at a lectern. The flexibility in presentation often depends on the preferences of the arbitrators, requiring practitioners to be flexible and understand how to best adapt the case to those preferences.

Confidentiality

In the process of adjudicating the dispute, the parties may wish to keep the proceedings, and the information exchanged in connection with the proceedings, out of the public eye. While some degree of privacy is part and parcel of international commercial arbitration, keeping information confidential is much more difficult in U.S. commercial litigation. In U.S. court proceedings, the parties often enter into a protective order that could require certain agreed-upon information to be marked as confidential. As a general matter, however, court proceedings, document filings, and resulting decisions are open to public access. While avenues exist for parties to challenge the use of material designated as confidential, there is a limit to what the parties can keep private.

By contrast, while confidentiality is not automatic under most arbitration rules, arbitration gives the parties much more flexibility to ensure confidentiality of both the proceedings and the underlying substantive information. Depending on the rules of the forum, parties can often agree to keep all proceedings and any decision issued by the arbitrators confidential. Many arbitral awards are never officially published, in contrast to U.S. court decisions.

Similarly, documents or information exchanged by the parties in an arbitration are rarely disclosed to third parties other than the arbitrators. Given the overarching absence of public scrutiny, international commercial arbitration is much more protective of sensitive information than U.S. litigation.

Cost shifting

Another important differentiator between international commercial arbitration and U.S. court proceedings is the prospect of cost shifting. "Cost shifting" occurs when an arbitrator awards the prevailing party some or all their legal costs, including their attorneys' fees. Most arbitral forums permit cost shifting and some, like the rules of the London Court of International Arbitration, make it the default rule. [The London Court of International Arbitration (LCIA)]

This contrasts greatly with U.S. court litigation. Any recovery of court fees is exceedingly rare, and with respect to attorneys' fees, the "American Rule" prevails, meaning that each side must pay their own attorneys' fees regardless of who wins the case. While there are narrow exceptions to the American Rule set by law, cost shifting is nearly non-existent in U.S. court litigation.

Parties should consider several aspects of cost shifting prior to choosing arbitration over litigation. The prospect of cost shifting influences settlement strategies, the parties' conduct in the proceedings, and even the arguments they make before the arbitrators. Cost shifting can also influence the very parties brought to the dispute, especially when there is a disparity of resources.

Time and Finality

As a general matter, commercial arbitral proceedings, from initiation to the issuance of a final award, tend to take less time than U.S. court litigation [Hughes Hubbard & Reed | Comparing Timelines: What Do Statistics...]. The average duration of arbitral proceedings can vary widely from forum to forum, partly due to differences in the complexity of the disputes as well as the intricacy of the rules of the arbitral forum.

While appeals have the potential to significantly prolong U.S. court litigation, U.S. law and various international treaties, including the New York Convention, have limited parties' ability to challenge the enforcement of a final arbitral award. In general, parties in arbitral proceedings can forecast with a greater degree of certainty when their dispute will truly be over.

Conclusion

While both types of proceedings can be used to resolve commercial disputes, international arbitration and U.S. litigation are two very different animals. Potential parties to a commercial dispute should stop and consider the differences between these two dispute resolution mechanisms and, choose counsel accordingly. As famously put by Albert Einstein: The only source of knowledge is experience.

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