Hong Kong Arbitration Week Recap: Private Equity, Financial Services and Insurance Disputes – Don’t Hesitate to Arbitrate!

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Introduction

Kicking off Hong Kong Arbitration Week (“HKAW”) 2019 on Sunday was a joint seminar hosted by KCAB INTERNATIONAL and Freshfields Bruckhaus Deringer (“Freshfields”) titled: “Private Equity, Financial Services and Insurance Disputes: Don’t hesitate to arbitrate!” The seminar was an Oxford-style debate of the motion: “this house believes that private equity, financial services and insurance disputes are uniquely unsuited for arbitration.”

The speakers were divided by sector, with Sue Hyun Lim (KCAB INTERNATIONAL), Nick Lingard (Freshfields) and SeungMin Lee (Shin & Kim) in support of the motion and Dana MacGrath (Bentham IMF), Simon Powell (Powell Arbitration) and Yong Wei Chan (Freshfields) opposed. John Choong (Freshfields) acted as moderator.

Before beginning the debate, a poll of the audience revealed only 22% were in favour of the motion that arbitration is unsuitable for private equity, financial services and insurance disputes.

Financial services

With a “heavy heart”, Ms Lim began the debate with four key arguments for why financial services disputes are not suited to arbitration.

First, “if it ain’t broke, don’t fix it.” Financial services litigation has a long history that yielded a wealth of expertise and binding precedents. This provided stability and consistency for the parties which are essential conditions for investment. Court litigation minimizes the real risk of anarchic, conflicting decisions.

Second, “why settle for second-best?” Ms Lim wondered why parties would choose arbitration when the courts provide more comprehensive interim relief and comparative ease to join parties and consolidate claims.

Third, “what are you getting yourself into?” Ms Lim pointed to the lack of accountability when it comes to arbitrators. Judgments are publicly available, providing insight into judges’ reasoning. Arbitrators lack the same level of transparency and accountability. It can lead to counsel running “everything but the kitchen sink” arguments at the expense of efficiency of time and cost.

Fourth, “show me the money!” Ms Lim reminded the audience that arbitration is often neither faster nor cheaper than litigation. Financial services stand to lose due to the lack of early dismissal procedures in arbitration. Despite their “broad discretion” arbitrators typically suffer from “due process paranoia” that leads to lengthier proceedings in arbitration, adding to the expense.

In response, an “at ease” Ms MacGrath begged to differ. She conceded that the courts are good, but pointed to the fact that the parties’ choice to arbitrate is not about courts not working, but the parties making a specific choice to arbitrate due to its advantages. In the US, the courts can be much slower and more expensive than arbitration. The lack of finality in court litigation is a distinct disadvantage.

Ms MacGrath stated that the lack of precedents is an unlikely risk and may even be healthy. A better result may be derived from arbitrators deciding on each case according to its merits. Further, confidentiality remains a hallmark of arbitration. In today’s world of “trial by Twitter”, the ability for financial services providers to keep their disputes private is invaluable.

Ms MacGrath pointed to the various institutional rule changes to facilitate joinder and consolidation as evidence of arbitration doing the "best it can". She stated it is a rare case where there are non-parties that cannot be joined to an arbitration. She also pointed to the increasing accountability of arbitrators amidst the increasing publication of awards. As for delay, Ms MacGrath made the point that all arbitration participants share responsibility, but institutions are increasingly vigilant in enforcing efficiency.

Private Equity

Mr Lingard began by sharing insights into the private equity mindset. It is a fast moving business with fundraising, deployment and realization typically taking place in short time frames. Clients expect a high degree of responsiveness and Mr Lingard suggested that an arbitral tribunal is never sufficiently responsive. He referred to an arbitration in which the proceedings closed in June 2018, but the award is still pending.

Mr Lingard acknowledged the expedited procedures offered by many arbitral institutions, but made the point that the relevant monetary thresholds are too low to be of much use in private equity transactions. While arbitration may be all about obtaining monetary relief, the possibility of court-ordered freezing or relief injunctions with teeth is arguably more useful to private equity clients. The stylistic aspects of arbitration and its effect on enforceability will typically generate a "you're kidding me" from clients.

Mr Lingard also referred to private equity claimants preferring an advantageous exit from investment terms in disputes, such as the ability to force an IPO as opposed to damages. Finally, Mr Lingard questioned the appropriateness of arbitration particularly for non-arbitrable claims in relation to minority shareholder oppression or insolvency.

In response, Mr Powell promised to be the audience's "guardian angel" following the previous "hogwash". Private equity moves fast, but arbitration is speedy, efficient and institutional rules provide adequate interim measures to the parties. It is responsive to the needs of the parties. As a result, it is continually improving. While a delay of over a year is unacceptable, he pointed to various rule revisions enshrining tight time frames for awards. Mr Powell also referred to the support

from commercial courts for arbitration, excepting the limited non-arbitrable matters. He stated that judges can lack the expertise to decide matters in private equity, especially when compared to party-appointed arbitrators with private equity backgrounds.

Insurance

Ms Lee began by discussing the origins of insurance as a means of spreading risk from the individual to the wider community, ensuring a speedier recovery after an unpredictable event. This is a relationship that should be treated different from other contractual relationships. She stated that arbitrators in insurance disputes may have a predisposition towards insurers, who will be more likely to appoint arbitrators in the future. Arbitration's flexibility has a downside in insurance disputes, where the insurers tend to be able to manipulate the arbitration agreement in their favour, causing delays and limits to remedies.

Ms Lee pointed out that through arbitration, insurers can avoid class actions. Given the multitude of policy holders with similar contracts, the lack of judicial interpretation is a disadvantage to expediency and consistency in decision making and avoids public scrutiny. Ms Lee concluded by stating that arbitration risks the foundations of insurance, where fairness, mutual trust and the promise of compensation after an insurable event should be preserved.

In response, Mr Chan defended the suitability of arbitration by pointing out that partisan arbitrators who favour insurers risk their reputations and future appointments, particularly in the face of increasingly tight institutional rules. By contrast, the tenure of judges limits accountability, because judges generally have their positions till retirement. Further, the resources of an insurer can have a similar impact in litigation, where delay and other strategies can limit a policyholder's relief. But unsatisfied customers can always switch insurers.

As for limited legal development, this is not a problem for liability insurance, where bypassing the courts has little negative effect on the public interest. Mr Chan referred to the use of the "Bermuda Form" in response to asbestos litigation, applying New York law to the contract and English law to the arbitration agreement. This avoided the problem of jury-awarded damages that was pricing insurers out of the market, leading to under-insurance. Here, arbitration came to

the rescue. However an audience member made the point that a lot of Bermuda Form arbitration is spent on contractual interpretation, all of which remains confidential and cannot assist future parties. This led to a wider audience-led discussion on the importance of increasing the anonymizing and publication of arbitral awards where possible.

Comments

After an entertaining and engaging debate, the audience had the opportunity to vote once more. It is perhaps unsurprising that the results of the second vote revealed that the number of audience members who agreed with the motion nearly doubled to 42%.

Those who spoke in support of the motion made frequent reference to broader public policy questions, the lack of precedent, biased arbitrators, Warren Buffet and even the protection of the rule of law. Such arguments can easily tug at the heartstrings and their broad, nebulous nature makes them harder to rebut.

Yet the result arguably suggests that arbitration is no less suited to such financial services, private equity or insurance disputes than other mechanisms of dispute resolution, but there are expectations that arbitration must continue to take advantage of opportunities to improve, particularly in respect to efficiency, cost and transparency. As is so often the case, it is not so much whether arbitration is or is not suited to such disputes, but rather “it depends” and should be assessed on a case by case basis.

More coverage from Hong Kong Arbitration Week is available here.