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Do We Need Another Arbitral Institute? Maybe.

Lisa Bench Nieuwveld (Conway & Partners) · Tuesday, December 7th, 2010

Another arbitral center may be opening its doors soon, but this one intends to be global and to focus exclusively on complex financial disputes, including the over-the-counter derivatives market.

The World Legal Forum, a non-profit organization located in The Netherlands worked with varying other groups to create this idea. On October 25, 2010, at the International Expert Roundtable the topic of opening this facility was discussed and met with positive review. The roundtable involved private legal practitioners, financial institutions and regulators from 14 different countries. The results from this meeting were to recommend both the benefit of creating the institute and the plan to open it in the spring of 2011.

Who will be the parties involved? Large, international banks, investment and pension funds and investors fighting over complex financial arrangements make up the parties. Traditionally, banks have steered clear of international arbitration. In fact, with New York and London dominating the financial world, these banks have always enjoyed the power to insist on their own local courts as the dispute forum resolution. Now, it may be possible for international arbitration to rise as the forum of choice for these complex deals.

Is it truly needed? The President of De Nederlandsche Bank, Nout Wellink certainly gave a convincing speech in the affirmative. Pres. Wellink relayed the concerns that arose during the crisis when large, innovative deals were created at a rapid rate and even those who created the products often did not fully comprehend all the associated risks. Pres. Wellink stated, “Risk management systems of financial institutions could hardly keep up with the product innovation.”

Prior to the crisis, and certainly even more so now after the crisis, the standardization of the over-the counter derivatives market has occurred as an attempt to create greater transparency and minimize the negative affects and aftershocks of the risks involved. In other words, the financial markets are trying to avoid another economic crisis. Pres. Wellink asserted two important principles to help reach this goal: transparency and legal certainty. He argued that both of these principles would be more attainable through greater standardization. This stems from standardizations which have already occurred such as global ISDA Master Agreements which has helped stabilize the terms and conditions of the markets; however, he argued that creating a global institute concentrating entirely on handling disputes arising under this deal is the next step. He stated, “It can lead to a further improvement of legal certainty and thereby – at least in an indirect way – support financial stability.”

Pointing to the discrepancies which arise when varying courts globally interpret the same contracts,

Pres. Wellink supported his argument that it is imperative to have a focused global tribunal to govern these disputes. Of course, the nature of arbitration is voluntary and arbitrators themselves will vary; therefore, even this dream can only be achieved to a certain extent. However, it certainly seems worth the effort when you consider having a pool of experts on these financial products available to act as the arbitrators.

If successful, this new facility will be located in The Hague, The Netherlands, which is an ideal location for a facility seeking a reputable neutral forum. As already a sort of international capital, The Hague also boasts the presence of the Permanent Court of Arbitration (“PCA”). In fact, the new facility intends to use the PCA as an appointing authority similar to that outlined in the UNCITRAL rules. The unique and attractive attribute of this possibility is in fact the prospective list of arbitrators – experienced practitioners who actually understand and know how to respond to complex financial deals – the same deals which went sour and contributed to the financial crisis. Many arbitrators know arbitration but few have worked on complex and innovative financial transactions, with ISDA Master Agreements and associated terms/products, much less even know what these are.

Therefore, for those banks traditionally steering clear of arbitral institutes on a more global level, this may just be the answer they need to get involved.

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