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Banking and finance disputes: to arbitrate or not to arbitrate, that is the question

Nicolas Ollivier | Caroline dos Santos*

"It has been said that "[b]ankers have traditionally preferred judges to arbitrators". Indeed, where banks or financial institutions are involved in a dispute, state courts have usually been preferred, while arbitration has, so far, often been overlooked. However, in the last decade, the financial landscape has endured colossal changes worldwide. The 2008 crisis led to a paradigm shift. Banks – and notably Swiss banks – have suffered the hostility of certain jurisdictions' national justice systems, while also enduring increasing regulatory burdens. Fintech startups are also remodeling the traditional ways banks have made business and creating some competition while bringing new legal challenges. The COVID-19 pandemic is still currently affecting every region of the globe, disrupting economic growth and foreshadowing a severe global recession. Banks already experience an increase of disputes. In the context of this new décor, it is the opportunity to forget preconceived ideas and to reconsider arbitration as a dispute resolution method. This contribution sheds light on the common – but often unjustified – criticisms that have traditionally been made against arbitration in this field, as well as the reasons for the recent growing interest it has generated. The benefits of arbitration as a dispute resolution method for specific activities of the industry will be discussed, without any preconceived ideas. As will be seen, while arbitration will not be a "one fits all" solution for all types of banking and finance disputes, it may provide unexpected benefits for banks and financial institutions, such as derivatives, advisory work, M&A, and smart contracts.

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I. Introduction

"The world of arbitration and the world of banking are apart. Arbitration practitioners consider bankers as being most ungrateful for not showing more gratitude to the many advantages that arbitration offers. […] *Conversely, bankers reproach arbitrators for not understanding the basics of a banker's business".*[1]

In the last few decades, arbitration has become the worldwide method for dispute settlement. Surveys show that, in case of disputes, for some industries, the use of arbitration has become more mainstream than recourse to court litigation.[2] There is, however, a stark contrast when one looks at the banking and finance sector where only 23% of its stake-

holders rank arbitration as their "most preferred" method of dispute resolution.[3]

Indeed, "[b]*ankers have traditionally preferred judges to arbitrators"*.[4] Choice of forum in financial hubs such as New York or London is usually contractually provided,[5] while international arbitration is rarely considered.

However, in the last decade, the financial landscape has endured colossal changes worldwide. The 2008 crisis and its disastrous aftermath struck the financial services sector and its stakeholders with full force. Its impact is felt to this day.[6] The cataclysm within the sector led to a shift in focus towards emergent markets disrupting the market equilibrium, a trend which prevailed until recently.[7] Banks – and notably Swiss banks – have suffered the hostility of certain jurisdictions' national justice systems, while also enduring increasing regulatory burdens. Fintech start-ups are also remodelling the traditional ways banks have made business and creating some competition while bringing new legal challenges. Last but not least, at the time of writing, the COVID-19 pandemic is affecting every region of the globe, disrupting economic growth and foreshadowing a severe global recession. Banks and financial institutions, who have witnessed an almost unprecedented surge in market volatility, already expect an increase of disputes following this new crisis.

It is unlikely that all these disputes will be handled by national courts. Rather it can be expected that alternative dispute resolution methods, and in particular arbitration, will play a significant role. In the context of this new *décor,* it is worthwhile reconsidering arbitration as a dispute resolution method.

This contribution briefly explores the reasons – legitimate or otherwise – that led to the scepticism – or ignorance – of certain banks and financial institutions with regards to arbitration, as well as the circumstances contributing to its recent redemption, before turning to current practice and potential increasing use of arbitration for a number of specific areas in the finance industry.

II. Arbitration in the banking and financial sector: an asset or a liability?

1. Common (but not necessarily justified) criticisms

1.1 Lack of consistent body of case law and of precedent

It is argued that the absence of a **doctrine of precedent in international arbitration** contributes to its unpopularity amongst banks and financial institutions.

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1 *G. Affaki,* A Banker's Approach to Arbitration, *in* G. Kaufmann-Kohler/V. Frossard (eds) Arbitration in Banking and Financial Matters, ASA Special Series No. 20, Basel 2003, p. 63.

2 Respectively 68% and 56% of respondents from the construction and energy sectors consider international arbitration as their "*most preferred*" method to resolve cross border disputes. See Queen Mary University of London and PricewaterhouseCoopers LLP, Corporate Choices in International Arbitration: Industry Perspectives, Queen Mary University of London and PricewaterhouseCoopers LLP, 2013, p. 6, available at: *<https://www.pwc.com/gx/en/arbitration-dispute-resolution/assets/pwc-international-arbitration-study.pdf>.*

3 *Ibid*.

4 *M. C. Boeglin,* The Use of Arbitration Clauses in the Field of Banking and Finance: Current Status and Preliminary Conclusion, (1998) Journal of International Arbitration, Vol. 15 Issue 3, p. 29.

5 *J. Freeman,* The Use of Arbitration in the Financial Services Industry, (2015) Business Law International, p. 77 *et seq*.

6 Queen Mary University of London and PricewaterhouseCoopers LLP (n. 2), p. 2.

7 *E.g., G. Affaki/A. Koenig,* Nouvelles tendances de l'arbitrage international en Afrique: le cas des litiges financiers, (2014) Comité Français de l'Arbitrage, Vol. 2014 Issue 3, p. 545 *et seq*.

Under this doctrine – which originates in the common law – national judges are required, when faced with similar cases, to follow the prior rulings of higher courts.[8]

The effect is that precedent yields consistency of outcomes and therefore attracts banks and financial institutions which seek predictability. The said consistency is also strengthened by the reputation of certain hubs often designated as forums for banking and finance disputes, such as London and New York, which, in turn, also reinforces homogeneity, since the more parties elect a specific forum, the more its judiciary gains expertise in the field.

Arbitrators, on the other hand, are not *stricto sensu* subject to this doctrine. In addition to the fact that awards are usually confidential, the diversity in cultural origins and legal backgrounds among arbitral tribunals or arbitrators – whilst also often perceived as an advantage – play to arbitration's disadvantage for banks and financial institutions.

That said, the absence of precedent could sometimes be to banks' advantage, especially where they strive to avoid the development of a precedent having a global negative impact on the banking industry,

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triggering the filing of new claims seeking damages on this basis.[9]

1.2 The apparent difficulty to obtain interim relief

Banks and financial institutions have for a long time feared a lack of responsiveness from arbitration should interim relief be sought.

While national courts are indeed particularly well-equipped to respond when immediate relief is needed, the reputation of arbitration is that no such response could be rapidly provided *before* an arbitral tribunal is constituted, *i.e.,* often times at the earliest stage of a dispute. The popular belief was – and remains – that in such cases, the applicant would in any event have to turn to national courts *("juge d'appui")* in order to obtain **interim relief** before an arbitral tribunal is constituted.

However, this fear is now outdated, as most arbitral institutions today offer the possibility to appoint a so-called "*emergency arbitrator"* to provide immediate relief even before the arbitral tribunal is constituted.[10]

1.3 The lack of power to compel joinder and order consolidation

The reality of business involves sophisticated contracts binding several parties and thus multi-party disputes.[11] Even in post-mergers and acquisitions **("M&A")** disputes, where the use of arbitration is not uncommon (see below Section III.3), litigation is often preferred due to national judges' power easily to **consolidate proceedings** or **join additional parties to ongoing proceedings**.

While several arbitral institutions have tackled this issue in their set of procedural rules – now providing for joinder and consolidation – parties' prior consent usually remains necessary.[12] Unlike state judges, arbitrators "*cannot order consolidation of related arbitral proceedings nor compel joinder";*[13] arbitration being

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8 Civil law jurisdictions are not familiar with such a strict doctrine but usually follow past decisions rendered thus also yielding consistency in the result.

9 *E.g.,* see Swiss Supreme Court Decision 4C.125/2002. The Swiss Supreme Court has ruled that finders' fees, or any kind of retrocessions transferred to banks following investment of a bank's client's assets in an investment fund, for instance, belong to the said client and not to the bank, entailing that the latter must thus transfer these amounts to the former. While this case law is now established in the case of broad asset management mandates, banks are reluctant to see it extended to narrower mandates concluded with clients, such as the so-called "execution only" mandate, or advisory mandates.

10 *E.g.,* Art. 29 ICC Rules; Art. 43 Swiss Rules; Art. 23 HKIAC. It is, however, true that an arbitral tribunal only has power over the parties to a dispute and not on third parties, which cannot be forced to take or refrain from taking a certain action. In such a case, the *juge d'appui*'s action will still be required.

11 *E.g.,* in lending and secured finance, where agreements provide typically for guarantee instruments.

12 *E.g.,* Art. 7 ICC Rules; Art. 4 (1 and 2) SRIA; Art. 27 and 28 HKIAC. For a comparison of joinder and consolidation clauses under major arbitral rules, see *G. Smith,* Comparative Analysis of Joinder and Consolidation Provisions Under Leading Arbitral Rules, (2018) Journal of International Arbitration, Vol. 35 Issue 2, p. 173 *et seq*.

13 *G. Kaufmann-Kohler/A. Rigozzi,* International Arbitration: Law and Practice in Switzerland, Oxford 2015, p. 15 (para. 1.49).

14 *I. Han,* Rethinking the Use of Arbitration Clauses by Financial Institutions, (2017) Journal of International Arbitration, p. 218.

a consensual dispute resolution method.[14] According to surveys, potential users of arbitration thus perceive the lack of a third-party mechanism as one of the *"worst characteristics"* of international arbitration.[15]

Consolidation and joinder are indeed useful procedural tools which reinforce consistency, hence attracting banks and financial institutions to opt for litigation rather than arbitration. That said, this issue could well be remedied by providing for well-drafted and coordinated dispute resolution clauses and/or by agreeing on consolidation and joinder options.[16]

1.4 Speed and cost

Arbitration is sometimes criticized for its cost and the length of the proceedings.

However, this criticism is only partially justified. On the one hand, arbitration is still, in most cases, quicker than litigation in court. There is only one arbitral tribunal and, in most jurisdictions, its awards can be challenged only in very limited circumstances. By contrast, court litigation will almost invariably involve several instances and appeals. Even in summa-

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ry court proceedings, respondents will have at their disposal an array of measures to obstruct the proceedings by raising certain objections, causing a complicated trial to ensue.

The costs of an arbitration compared with those of a full-blown court litigation (and potential appeals) will most often be lower. More importantly, the focus on cost and speed distracts from the crucial question of what you get for your money. An arbitral award can be enforced in almost all countries more easily than a foreign court judgment; this is an essential advantage, especially in cross border disputes involving assets in several jurisdictions (see below II.2.1).

On the other hand, most arbitral rules now offer *fast-track* procedures for disputes with relatively low amounts at stake.[17]

Arbitration is thus a valid alternative for both complex and minor disputes.

1.5 Limited arbitrability of a dispute

While arbitrators generally have full authority to rule on disputes involving all sorts of parties and sectors (including banking matters), depending on the seat of the arbitration, the **arbitrability**[18] of certain aspects of disputes may be subject to exceptions that may be deemed to be the prerogative of national courts.

In the context of banking and finance disputes, this might be perceived as particularly problematic in cases involving consumers, which, depending on the seat of the arbitration, could be non-arbitrable disputes.[19] While related disputes are arbitrable under the Swiss Federal Statute on Private International Law **("PILA")**[20] this might well not be the case in other jurisdictions, such as for instance Germany.[21] In cases where non-arbitrability is an issue, enforcement could later be denied at the place of enforcement (Article V(2)(a) of the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards, "**New York Convention"**).[22]

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15 Queen Mary University of London and White & Case, 2015 International Arbitration Survey: Improvements and Innovations in International Arbitration, p. 7, available at: <*http://www.arbitration.qmul.ac.uk/media/arbitration/docs/2015_International_Arbitration_Survey.pdf*>.

16 See for instance Art. 4 of the Swiss Rules, which is a far-reaching joinder/consolidation provision. See also *Han* (n. 14), p. 218.

17 *E.g.,* Art. 5 SIAC Rules; Ch. IV CIETAC Rules; Art. 41 HKIAC Rules; Art. 42 Swiss Rules.

18 Arbitrability concerns whether a type of a dispute can or cannot be settled by arbitration.

19 ICC, Arbitration and ADR Commission report, Financial Institutions and International Arbitration, 2016, p. 16.

20 *Kaufmann-Kohler/Rigozzi* (n. 13), p. 102 (para. 3.4).

21 *B. Badertscher,* Arbitrating banking and finance disputes – What are the benefits, available at: <*https://www.lexology.com/library/detail.aspx?g=09cb1405-c618-422c-8a61-d25754ba69b0*>.

22 *Ibid,* p. 529 (para. 8.271).

2. Why many commercial disputes are being arbitrated – and more banking and finance disputes will be arbitrated in the future

2.1 Universal enforceability of awards

Cross-border enforceability of arbitral awards under **the New York Convention**[23] is, without a doubt, the strongest suit of international arbitration. Under this key convention, national courts of contracting states shall recognize and enforce arbitration awards made in other contracting states (*i.e*. the 161 state parties) in a quasi-automatic manner.

By contrast, to this day, the recognition and enforcement of national courts' judgments has not had similar success as they still rely on heterogeneous cross-border regimes of enforcement. In the best-case scenario, enforceability of judgments is based on bilateral treaties or multilateral conventions efficiently applied. In the worst case scenario, a party seeking recognition and enforcement will face the meanders of the domestic law of the place of enforcement, which, depending on the jurisdiction, might be a long and hard battle.[24] The New York Convention is thus the Swiss army knife of arbitration and all the more so when one single award can be enforced in multiple jurisdictions, unlike a court judgement which must be recognized and enforced under several regimes to reach the same result.

In this respect, arbitration therefore offers a significant advantage, in particular when banks deal with jurisdictions without strong enforcement regimes. This might increasingly be the case given their focus on emerging markets where, far from enjoying

a culture of voluntary compliance with judgments, they might be very difficult to enforce.

2.2 "One-stop shop"

While decisions rendered by national judges are often subject up to a two-tiered appeal mechanism, arbitral awards are (save for a contrary agreement by the parties) not appealable. Arbitral awards are therefore **final and binding,** offering no room for the losing party to initiate a long climb to the final instance of appeal. Few and limited grounds will unlock the gates to an admissible challenge of an arbitral award before a national court.[25] In this sense, enforcing a final arbitral award might be quicker than resorting to court litigation which can take several years to obtain the same result.[26]

2.3 Privacy and confidentiality of arbitration

Unlike litigation where public interest necessitates public hearings, commercial arbitration proceedings are **private** and therefore far from prying eyes (both of the press and of state authorities).[27]

As to **confidentiality,** although the Swiss PILA is silent on the topic, parties are free to provide for it or to choose arbitral rules which provide for confidentiality.[28]

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23 The New York Convention was a resounding success and counts today no less than 161 signatories, facilitating and automatizing the process of recognition and enforcement of final awards worldwide. See <https://treaties.un.org/Pages/ViewDetails.aspx?src=TREATY&mtdsg_no=XXII-1&chater=22&clang=_en>.

24 Although the newly adopted (2 July 2019) Hague Convention on the Recognition and Enforcement of Foreign Judgments in Civil or Commercial Matters is promising in order to facilitate recognition and enforcement of a judgment in other jurisdictions, it remains to be seen which states will sign and ratify the Hague Judgments Convention, and in what timeframe.

25 *Kaufmann-Kohler/Rigozzi* (n. 13), p. 420 *et seq*.

26 *E.g.,* Swiss Supreme Court Decisions 4A_379/2016 of 15 June 2017 and 4A_119/2018 of 7 January 2019 concerning a case of unauthorized transfers that occurred between 2008 and 2010. The client filed a claim on 15 November 2012. The bank appealed the judgments of the State Court twice to the Swiss Supreme Court which, in turn, remanded the case to the lower court twice, the last time on 7 January 2019. A new ruling will be issued by the lower court, which will be subject to a final appeal to the Swiss Supreme Court. If a new appeal is lodged to the Swiss Supreme Court, its final decision on the merits may be expected by summer/fall 2020, i.e. approximately *8 years* after the filing of the initial claim.

27 *B. Berger/F. Kellerhals,* International and domestic arbitration in Switzerland, 3rd ed., Berne 2015, p. 429 et seq. (paras.1230 et seq.).

28 *Ibid*. See for instance Art. 44 Swiss Rules.

These features certainly are considerable advantages for financial institutions, notably regarding the preservation of their reputation which may otherwise be in tatters when a high profile and/or politically-exposed person makes vindictive public statements in the media. Banks should, however, draft the confidentiality clause carefully, so as to permit the required communications to its auditors and Swiss and foreign authorities. Notably, Article 29 of the Swiss Financial Market Supervisory Authority Act provides that banks and their audit companies must immediately report to the Swiss Financial Market Supervisory Authority **("FINMA")** any event that is of substantial importance. For instance, a client's claim concerning a colossal amount in dispute should be reported to FINMA if it may jeopardize a condition that must be met to maintain a bank's licence, such as its capital adequacy and/or liquidity[29] or the proper business conduct requirement.[30]

2.4 Appointment of arbitrators with key characteristics and P.R.I.M.E. Finance

Arbitrators whose profiles fit **key characteristics** such as legal background or in-depth expertise in certain fields can be appointed by the parties. The same goes to cases where relevant documents are expected to be in a foreign language; arbitrators proficient in that language can be selected, thus minimizing translation costs.

The ability to appoint established practitioners with a high level of expertise or language proficiency can be a welcome feature in financial disputes of a complex and technical nature, or in the context of fintech disputes which require understanding of both finance and technologies.[31] The arbitrators' prior area of practice or expertise or their ability rapidly to apprehend the challenges of a certain field can thus result in cost efficiencies, as well as lower chances of an unsatisfactory decision.[32]

In this regard, in 2012 the Hague the Panel of Recognised International Market Experts in Finance **("P.R.I.M.E. Finance")** was established, namely an arbitral institution specialized in the settlement of financial disputes which not only provides for dispute resolution services, but also judicial training and a

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database of important decisions rendered worldwide in cases involving complex financial transactions.[33]

This initiative responds to a challenge faced by practitioners open to the idea of arbitrating their dispute but not finding decision-makers who fit the job. P.R.I.M.E. Finance provides a vast panel of decision-makers, not only significantly experienced in the field but also with arbitration practice.[34]

P.R.I.M.E. Finance also offers a modern set of rules which ensure the efficient settlement of the parties' dispute. The P.R.I.M.E. Finance Arbitration and Mediation Rules indeed provide for, *inter alia,* expedited proceedings, interim measures and emergency arbitral proceedings, default proceedings and joinder of third parties.[35]

2.5 Flexibility of international arbitration

International arbitration allows parties to resolve their dispute outside a strict framework. Parties are indeed free to choose the seat of their arbitration, the language of their proceedings, the procedural rules applicable to their dispute (or choose a set of arbitration rules) as well as, more generally, to mould the way they intend to conduct their proceedings.[36]

This has proven essential in the context of global crises such as the eruption of the Icelandic volcano Eyjafjallajökull, which caused the closure of European airspace for over a week, or, on a greater scale, the

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29 See Art. 4 of the Banking Act.

30 See Art. 3(2)(c) of the Banking Act.

31 *E.g.,* the WIPO Arbitration and Mediation Center provides procedural advice and case administration to help parties resolve disputes arising in the area of financial technology (FinTech) without the need for court litigation.

32 *N. Blackaby/C. Partasides et al.,* Redfern and Hunter on International Arbitration, Oxford 2015, p. 30 (para. 1.104).

33 See <*https://primefinancedisputes.org/*>.

34 Arbitrators will be appointed amongst "[…] *carefully vetted international group includes sitting and retired judges, central bankers, regulators, academics, representatives from private legal practice and derivatives market participants* […]". See <*https://primefinancedisputes.org/page/list-of-experts*>.

35 Respectively Art. 2*a*, 26 and 26*a*, 31, 17 (5).

36 *E.g.,* Parties can decide, for instance, not to provide translations of documents; to only file their submissions electronically etc.

current COVID-19 pandemic. [37] While the national courts of most jurisdictions around the globe have been forced to suspend or postpone non-urgent proceedings, the arbitration community has adjusted quickly, providing a real advantage over traditional litigation in these challenging times.

Arbitrators and arbitral institutions, who are already used to dealing with parties based in different jurisdictions, are already digitalized and used to holding online meetings or hearings, notably to attempt to reduce the need for travel and in-person meetings. However, this trend has quickly and significantly been accentuated during the COVID-19 pandemic, since parties to ongoing arbitrations have been able to pursue their proceedings by holding online merit hearings.

Such was the experience of two Brazilian parties to an International Chamber of Commerce (ICC) arbitration at the outbreak of the current pandemic. The parties, who did not want to suspend their proceedings, were able to maintain their scheduled hearing – despite most of its participants being in quarantine – and hold it via Zoom in March 2020. While the arbitrators were located in the regions of Galicia, São Paulo and Rio de Janeiro, participants were located in Singapore, London and New York. Participants reported that the virtual hearing (which gathered up to 70 people) was a success.[38] This is however not the only successful example of such "e-hearings". The Global Arbitration Review reported that parties to an arbitration administered by the Singapore International Arbitration Centre **("SIAC")** agreed to conduct a virtual hearing, which was considered a "very positive [experience]".[39]

"Outside the box" initiatives have also sought to support online administration of proceedings in these challenging times. The Stockholm Chamber of Commerce **("SCC"),** in partnership with Thomson Reuters, also provided a version of the SCC Platform – a secure digital platform for communications and file sharing – to *ad hoc* arbitration (i.e., an arbitration not

administered by a particular institution), free of charge during the COVID-19 outbreak.[40]

The flexibility of arbitration in a period of crisis extends further. Most arbitral institutions have facilitated online, rather than hard copy filings, including for requests for arbitration or applications for emergency arbitrators. More importantly, unlike national courts which are usually bound by strict notifications rules for their decisions, parties to an arbitration are free to agree on a valid notification of the award by e-mail. Such efficient notification is particularly practical in a context where the courts' activity is slowing down and postal services are overwhelmed. It also contributes to a quicker and more efficient enforcement of awards.

2.6 Safe harbour from punitive damages

Last but not least, arbitration can also be perceived as a safe harbour where parties – who would otherwise see their dispute litigated in a jurisdiction permitting it – are safe from being ordered to pay punitive damages.[41] Although parties are always free to exclude such a remedy expressly, in the absence of an express exclusion arbitrators are likely to treat punitive damages with caution and not to order them for three main reasons. First, the substantive law applicable to the dispute (usually provided by the parties in their contract) is likely to prevent arbitrators from granting punitive damages. Second, punitive damages are also likely to be deemed inadmissible under the *lex arbitri* (i.e., the "law of the place where arbitration is to take place"[42]). Finally, it could well be that an award granting the said damages would be unenforceable.[43] In the

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37 Anecdotally, in 2010, when the Eyjafjallajökull caused the closure of European airspace for over a week, the organisation following an ICC hearing had to be changed to allow "three arbitrators, an ICC secretary, two teams of opposing counsel and numerous rock, geology and quantum experts" to be able to return home to their professional obligations, notably to attend another ICC hearing starting the following Monday. They all squeezed on to a 50-seater bus and took the way home, travelling, together, through Sweden, Denmark, Germany, Belgium and France by bus. See <*https://globalarbitrationreview.com/article/1029369/arbitration-and-volcanic-ash#.XqV_6vcgrGY.mailto*>.

38 See <*https://exame.abril.com.br/negocios/a-pandemia-na-maior-arbitragem-societaria-do-pais-a-disputa-pela-eldorado/*>.

39 See <*https://globalarbitrationreview.com/article/1225832/covid-19-participants-in-siac-case-share-success-of-virtual-hearing*>.

40 See <*https://sccinstitute.com/scc-platform/ad-hoc-platform/?link_id=vtCJAUQDbEdyU*>.

41 These damages aim at compensating the wronged party but rather to punish and deter the wrongdoer. See *N. Blackaby/C. Partasides et al.,* Redfern and Hunter on International Arbitration, Oxford 2015, p. 516 (paras. 9.44 *et seq*.).

42 *I.e.,* in Switzerland, Chapter 12 of the Swiss Federal Statute on Private International Law.

43 *Blackaby/Partasides et al*. (n. 41), p. 516 (paras. 9.44 *et seq.*). In Switzerland, the Swiss Supreme Court has not yet ruled on the issue, but it seems it would be inclined not to consider an order to pay punitive damages as contrary to public policy. See Swiss Supreme Court Decision 4P.7/1998.

context of banking and finance disputes where losses can already be colossal even without the risk of being ordered to pay punitive damages, arbitration could be seen as a safer option than litigation.

III. The use of arbitration with respect to specific activities of the banking and financial sector

1. Wealth management (asset management/advisory services)

Wealth management services relate to investment advice as well as discretionary asset management. A bank generally establishes, after discussion with its clients, an investment strategy that takes into account the client's risk profile, investment objectives and other stipulations and restrictions. The bank's main goal is to generate profit by investing its clients' assets deposited with the bank, by researching and analysing statistical analyses of companies and market trends, while respecting the client's investment profile.

Asset management differs from banks' other activities in the sense that it does not necessarily involve the traditional "b-2-b"[44] parties, but often confronts a private banker to a less experienced party, ranging from a family estate or a non-profit organisation to common individuals with possibly no financial background whatsoever. Although Swiss courts have in some cases ordered banks to pay colossal damages in disputes with bank customers – even sophisticated ones[45] – Swiss banks are, rightly or wrongly, generally reluctant to have their wealth management disputes resolved through arbitration, mostly for the above-mentioned reasons (see above Section II). Court litigation is the usual way to solve such disputes.

In Switzerland, recourse to state courts in the event of a dispute is the result of a long-standing market practice according to which banks impose on their clients non-negotiable general business terms and conditions containing a choice of court. Oftentimes, these will be the ones of the place of business

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of the bank, *i.e.,* where the account is maintained or where the bank's headquarters are located.

As a result, throughout the years, the Swiss national courts' case law has developed substantively. Banks' duties have been specified, and their general terms and conditions have been adapted thus yielding consistency in the outcome of their disputes (see above, Section II.1.1).

In addition, Swiss case law sets a high threshold on claims filed by customers against banks. For instance, a commercial customer is deemed to know the usual risks associated with financial transactions (*e.g.,* fluctuation of interest rates and foreign exchange risk) and is required to take pro-active behaviour to mitigate his/her damage.[46] In this context, mere passive behaviour from customers after realising that the bank did not follow their investment instruction or strategy is not accepted and would lead to the court reducing or even excluding damages.[47]

In the same vein, the strict assessment of losses – which is a prerequisite to any damages claim under Swiss law[48] – is another reason why Swiss banks appreciate the Swiss courts' jurisdiction. For instance, in the context of an advisory agreement where the bank carried out transactions without instructions from the client, the claim was dismissed by the Swiss Supreme Court because the client failed to demonstrate the losses related to each and every unauthorized transaction (*i.e.,* concrete damage calculation). It also failed to prove that it incurred a loss by comparing the disputed portfolio with a benchmark.[49] This very strict notion of the assessment of damages might, therefore, entice Swiss banks to resort to litigation and rely on the above case law making it difficult for clients (especially individuals without much experience in the field) to prove their loss, leading to their claim to being dismissed.

That said, arbitrators are applying the law strictly too. Given the recent developments in Swiss case law with respect to the assessment of damages in asset management disputes in particular, the appointment of arbitrators with a proven **financial industry knowledge** could become an interesting prospect for banks.

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44 *I.e.,* business to business.

45 See *e.g.,* Decision of the Swiss Supreme Court 4A_302/2018 of 17 January 2019, holding a Swiss bank liable for EUR 106 million, subject to deduction of certain amounts to be determined by the cantonal appellate court to which the case has been referred.

46 Swiss Supreme Court Decision 119 II 333, c. 5b, of 23 March 1993; Decision of the Swiss Supreme Court 4A_449/2018, c. 5.2.3, of 25 March 2019.

47 *E.g.,* Swiss Supreme Court Decision 4P.192/2004 of 26 January 2005.

48 Art. 42 of the Swiss Code of Obligations.

49 Swiss Supreme Court Decision 4A_586/2017 of 16 April 2018.

The Swiss Supreme Court has indeed recently softened its position by ruling that a client no longer has to show what its gains would have been had its assets been invested according with its instructions/the elaborated strategy. Clients can now merely claim damages for the losses suffered *i.e.,* the difference between the amount invested and the remaining assets on its portfolio.[50] In other words, although the bank does not bear the burden of proof, it may have to justify its objections to the damages calculation provided by the client since it is the party with the technical investment knowledge. As a consequence, a bank may have an interest to prove through experts that negative performance would have inevitably resulted regardless; that is to say, even if the portfolio had been managed by implementing a strategy considering the criticisms formulated by the clients. Appointed arbitrators with practical financial experience could in this context be a strong advantage as it is often difficult for judges to instruct a court-appointed expert by defining precisely to what their report should pertain.

An optional right to recourse to arbitration could therefore be implemented for these kinds of disputes. Banks could insert in their terms and conditions the right for clients to opt for arbitration in addition to the right to go to state courts.

2. Derivatives

Derivatives are financial instruments whose value is derived from underlying assets, benchmark rates or indices.[51] The derivative market has widely expanded in the last decade. Likewise, so have related disputes – ranging from mis-selling and wrongful advice, to disputes related to convoluted calculation methods or to the quantity or quality of commodities.[52]

Again, here parties have traditionally turned to litigation to resolve those disputes, in particular to New York or London courts. However, a recent trend shows that, although not frequently used, "[the par-

ties'] *familiarity with arbitration and willingness to utilise it have been on the rise"*. This is linked to several factors.

First, considering trading derivatives increasingly involve parties originating from emerging markets, a convention such as the New York Convention which guarantees almost universal enforcement of awards is appealing.[53]

Second, any banker (or counsel) having acted in disputes involving derivatives can confirm the complexity of the matter. The ability to appoint decision-makers with financial experience would be an important advantage.

Third, the use of arbitration for these disputes has been democratized and advocated by the International Swaps and Derivatives Association **("ISDA")** through its "ISDA Arbitration Guide" and the commonly referred-to "ISDA Master Agreement", *i.e.,* a standardized contract proposed by the ISDA to enter into derivative transactions. Originally set up in 1992 and 2002, the ISDA Master Agreement only provided for court litigation in London or New York in case of a dispute. However, since 2013, when the ISDA Arbitration Guide provided model clauses for arbitration along with guidance notes[54] – also proposed in the ISDA Master Agreement – this method of dispute resolution has gained in popularity for these disputes.[55] By popular demand, following the users' feedback on these adjunctions, further arbitration model clauses have now been added in its 2018 update.[56]

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50 Swiss Supreme Court Decision 4A_449/2018 of 25 March 2019.

51 Swiss Bankers Association's Guidelines on Special Risks in Securities Trading, 2008, para. 3.

52 ICC, Arbitration and ADR Commission report, Financial Institutions and International Arbitration, 2016, p. 11 (para.67).

53 *Ibid,* p. 11 (para. 69).

54 Including P.R.I.M.E Finance as described above.

55 *Han* (n. 14), p. 233 *et seq;* see also News, April 2019, *in* Asian Dispute Review, Hong Kong International Arbitration Centre (HKIAC) 2019, Vol. 21 Issue 2 p. 91.

56 See <*https://www.isda.org/book/2018-isda-arbitration-guide/*>.

3. Advisory work – M&A

Arbitration has been a long-standing feature in M&A transactions, particularly for cross-border transactions.[57] Given the typically complex issues involved, the frequent need for safeguarding confidential commercial information, and the potential difficulty of enforcing court judgments in foreign jurisdictions, arbitration has long since been a match. This tendency has also been reinforced by the right to select a neutral forum and decision-makers experienced in the specific kind of transaction.[58] Arbitrators having adequate case management and expertise in the field have also been proven to tackle the sheer number of documents, the technical regulatory framework applicable, or the multi-jurisdictional aspects involved in any M&A transactions efficiently, and possibly more adequately than state judges who may have less flexibility and time to devote to such cases.

By contrast, what has been perceived as a drawback for such disputes is the lack of power of arbitrators to order consolidation or compel joinder of parties (see above, Section II.1.3). M&A disputes might indeed involve several sellers, buyers, targets, insurers and other third parties, which, failing coordination, can lead to parallel proceedings and conflicting decisions. This pitfall can, however, be avoided by ensuring arbitration clauses are carefully drafted and avoiding "*midnight clauses".* In this context, the choice of the applicable arbitral rules is crucial since requirements to join a third party or consolidate cases can vary vastly from one set of rules to the other (certain rules do not even provide for consolidation).[59]

4. Blockchain and smart contracts

Switzerland has emerged as a global hub for distributed ledger and blockchain technology as well as smart contracts.

A distributed ledger is a consensus of replicated, shared and synchronized digital data geographically spread across multiple sites, countries, or institutions. There is no central administrator or centralized data storage. Underlying distributed ledger technology is the blockchain. [60] A smart contract is a self-executing contract with the terms of the agreement be-

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tween parties being directly written into lines of code. The code and the agreements contained therein exist across a distributed, decentralized blockchain network. The code controls the execution, and transactions are trackable and irreversible.[61]

The evolution of these technologies has the potential for innovation and growth in the future. They could reduce transaction costs, expedite settlements and offer nearly an infinite amount of new decentralized applications.[62] The market has developed strongly in recent years, particularly in the field of finance, where blockchain could, in particular, improve the situation in wealth management, capital markets and international trade finance.[63]

In this context, parties will use smart contracts, based on blockchain technology, to execute transactions when certain pre-defined conditions are fulfilled. While smart contracts could help to reduce litigation, in particular, in disputes relating to non-performance of payment obligations, [64] it will evidently not prevent all disputes; technical issues relating to non-performance are still likely to occur, such as those caused by

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57 *Joe Liu,* Arbitration of Cross-Border M&A Disputes, Kluwer Arbitration Blog, 21 April 2015, <*http://arbitrationblog.kluwerarbitration.com/2015/04/21/arbitration-of-cross-border-ma-disputes/*>.

58 *H. Frey/D. Müller,* Arbitrating M&A disputes, *in* Manuel Arroyo (ed), Arbitration in Switzerland: The Practitioner's Guide, 2nd ed., Haywards Heath 2018, p. 116 (paras. 6 et seq).

59 For a comparison of joinder and consolidation clauses under major arbitral rules, see *G. Smith,* Comparative Analysis of Joinder and Consolidation Provisions Under Leading Arbitral Rules, (2018) Journal of International Arbitration, Vol. 35 Issue 2, p. 173–202.

60 <*https://en.wikipedia.org/wiki/Distributed_ledger*>. See also <*https://www.investopedia.com/terms/d/distributed-ledgers.asp*>.

61 <*https://www.investopedia.com/terms/s/smart-contracts.asp*>.

62 See Swiss Legal Tech Association, Data, Blockchain and Smart Contracts – Proposal for a robust and forward-looking Swiss ecosystem, White paper, 27 April 2018, p. 39–40.

63 *J. Anthamatten/P. Lago,* Après la frénésie de la blockchain – Une opportunité pour la place financière suisse, 4 June 2019.

64 Swiss Legal Tech Association, White paper (n. 62), p. 12.

defective coding or bugs. Smart contracts will, therefore, not be free from the usual legal issues such as illegality, error, misrepresentations, duress and force majeure, or international sanctions against a party. Parties will thus still bring certain matters before decision-makers.[65] But who, between judges and arbitrators is likely to be in charge?

The main challenge state courts will certainly face in the particular field of smart contracts is the lack of efficient means to enforce their judgments given that smart contracts are self-executing, embedding the automation of the performance of the parties' obligations.[66] A judgment rendered by a national court ordering a reversal of an executed transaction would not be enforceable due to the irreversibility of the performed transaction. Even if the disputed transaction is not yet performed, neither a national judge nor the parties have means to amend the code of a defective smart contract. As a result, a judgment could only compensate the effect of a transaction that occurred in the blockchain (e.g. if 100 bitcoins are transferred, the recipient party could be ordered to pay the corresponding CHF amount to the other party's bank account). This *off-chain* compensation would work for monetary claims. However, for claims relating to the ownership of (tokenized) assets transferred by the smart contract, an *off-chain* compensation would not be able to retransfer the ownership to the legitimate owner.

Another difficulty lying with national judges will be to determine, in the absence of a choice of forum in the smart contract, which judge has jurisdiction. Under Swiss law, the determination of the forum would depend on the place of domicile/place of business[67] of the parties and the place where the essential performance must be rendered.[68] However, these concepts are rather difficult to apply in the context of a smart contract embedded in a blockchain, where the performance is carried out in multiple places, each of them storing and recording the blockchain.

Arbitration may be more suitable than national courts for resolving these issues, not only because the seat of arbitration can be chosen, but more importantly since a coded dispute mechanism could be developed allowing a party to "pause" the disputed transaction of the smart contract and trigger an arbitration. Arbitration would also offer a system of enforcement of the award directly into the smart contract. The obvious advantage is that the award would be integrated into the blockchain and automatically executed.[69]

IV. Conclusion

Banks are usually reluctant to opt for arbitration. However, arbitration has proven to be an efficient dispute resolution mechanism in many other sectors and could also highly benefit banks and financial institutions. The lack of precedent doctrine in arbitration may create a fear of uncertainty but the higher exper-

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tise of arbitrators in the financial industry should dissipate this concern. Certain areas in the financial sector may be a better suit for arbitration than others, but its adoption depends on a cultural shift (and thus, more information on the topic). To provoke and ease this, banks should conduct an overall assessment of what advantages arbitrations could bring instead of

litigation in relation to their operative business, taking into account the types of services, products and types of clients (such as sovereign funds, states, professional investors, high net worth individuals and consumers), in connection with which disputes may arise.

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65 *Ibid,* p. 54–55.

66 *Ibid,* p. 53.

67 Art. 10 and 31 of the Swiss Procedure Civil Code, Art. 112 PILA.

68 Art. 31 of the Swiss Procedure Civil Code and Art. 113 PILA.

69 Swiss Legal Tech Association, White paper (n. 62), p. 13.