

Arbitrate Or Litigate

To Arbitrate Or To Litigate: That Is The Question^{1,1a}

By Kevin Nachtrab*

"The only thing we have to fear is fear itself ..."

Franklin D. Roosevelt²

1. Introduction

It is an issue addressed in virtually all contract negotiations. Anyone involved with transactional work routinely deals with it. When raised, it often becomes the subject of a heated debate. And yet, it is probably one of most important but misunderstood and neglected issues dealt in contractual negotiations.

The "it" is the issue of whether the contract should designate that disputes between parties arising under the agreement should be resolved by either mediation/arbitration or by litigation. In other words: "To Arbitrate or to Litigate."

Often one of the final (if not the final) issues to be dealt with during negotiations and relegated to the end of the contract, it is nonetheless an issue that has an enormous practical impact on the parties dealings under the agreement, facilitating (or not) their parties ability to enforce adherence to its various terms and conditions.

As we shall discuss below, not all disputes easily lend themselves to be resolved by mediation/arbitration. Sometimes the issues to be resolved are more suited for the discovery and investigative procedures that are the hallmark of litigation. In any event, the procedure eventually selected (arbitration or litigation) should always be the result of an informed inquiry on the part of the contract drafter.

However, many (if not most) contract drafters have only a passing knowledge of mediation/arbitration and what it involves. While they may be equally personally unfamiliar with litigation, somehow (owing perhaps to their legal training or perhaps to extensive characterizations of trials in the popular media) litigation seems a much more time-tested and familiar process to them, open to public scrutiny, while arbitration remains a much more distant, remote and unfamiliar process often conducted behind closed doors with a perceived potential for deal-making and abuse.

Thus, when confronted with the choice of arbitration or litigation, the knee-jerk reaction of many negotiators not familiar with arbitration is simply to opt for what they consider as the "safe" option: litigation. While they know that litigation is often a wholly unsatisfactory solution, it is often a case of "better the devil you know than the one you do not." Further, by choosing litigation, some people believe that they have not given up any rights which litigation may afford them while believing that, if they wish, they can always propose to mediation/arbitration later discussing the possibility on an issue-by-issue basis.

The unfortunate downside of this approach is, however, that by then it may be too late in that there is no obligation on the part of the parties to even discuss this issue, let alone to agree to it.

The primary reasons enunciated by most lawyers for disliking arbitration appear to be based on the perceptions that one will get something less than a fair hearing (due, for example, to a lack of discovery and/or cross-examination possibilities)³ and that arbitration lacks many of the court system's fundamental structures that help assure fairness.⁴ An often-heard refrain from such persons is that "my clients would kill me if they found themselves in such a situation." This is especially magnified when the

**Kevin Nachtrab is a Senior IP Patent Attorney with Johnson & Johnson (Europe) in Brussels, Belgium. The author is a member of the Bar of the State of Maryland and the United States 4th Circuit Court of Appeals and a Registered United States Patent Attorney.
E-mail: nachtrab@jppbe.jnj.com*

3. See, for example, "To Arbitrate or Not to Arbitrate: Clients Should Carefully Consider Agreement For Binding Arbitration", at <http://library.findlaw.com/2000/Jun/1/129487.html>.

4. In this regard, one of the primary arguments offered for preferring litigation over arbitration lies in the requirement of courts of first instance, and the appellate courts that review their decisions, to articulate sound legal reasons for their judgments; reasons and judgments which are themselves subject to further review and confirmation. Arbitration, with its absence of appellate review (and, indeed, often its prohibitions against appellate review), lacks such a safeguard.

1. With apologies to Shakespeare.

1a. A contribution from the LESI Life Sciences Committee.

2. First Inaugural Address, March 1933. For a text, see <http://www.historymatters.gmu.edu/d/5057/>.

Arbitrate Or Litigate

arbitration proceeding occurs in a different language in some far away country having legal customs and procedures that seem incomprehensible to the contract drafter.

Not that such concerns are wholly unjustified. One often hears the anecdotal stories of seasoned litigators about this case or that where an arbitrator simply did not understand, or worse ignored, the law and where the procedures used were incomprehensible. These stories are swapped becoming more and more outrageous with each telling until they become the stuff of legends and no longer bear any semblance to the reality.

Nonetheless, the question remains. Why should there be such resistance to resort to a procedure that can be (and the operative words here are "can be") flexible, quick, more often than not less expensive and, particularly when highly technical intellectual property matters are involved, offers the prospect of a more knowledgeable decision.

Why? One Word: Fear

Fear of the unknown arises from an ignorance of the rules and procedures of mediation/arbitration. Fear that they may be confronted with unknowledgeable and unreasonable (or worse, biased) arbiter(s). Fear that they may not get as complete and as fair a hearing than they would get in a court of law. Fear that they may receive a judgment that is either unenforceable or, perhaps worse, too easily enforceable.

Fear

Due to such fears, those who dismiss the arbitration option out-of-hand may be missing a real opportunity. An opportunity to secure a fair hearing, performed under well-established and set rules and procedures, which are conducted by persons who are specifically experienced with the technology and subject matter in dispute and who are capable of issuing judgments that are readily enforceable in many jurisdictions, certainly more jurisdictions than judgments rendered by courts of law.

It is the purpose of this note (and, indeed, of the accompanying articles in this issue) to attempt to remove some of the mystery and fear which shrouds mediation/arbitration by shining some light on the various mediation/arbitration procedures available today and review many of the issues to be considered when making an informed choice. In doing so, the hope is that this note may help the contract drafter better understand the options with which he/she is presented, so that he/she may be able to make a more informed deci-

sion based on fact and not on emotion.

2. Choice of Rules and Procedures

The first issue which one should address in deciding between mediation/arbitration and litigation is whether the choice rules and procedures offered by mediation/arbitration offer one a better route to resolve the disputes which may arise in the context of the contract than is offered by litigation.

The choice of litigation leaves one with little choice as to the dispute resolution procedure. The rules of procedure in many jurisdictions is well-established and leave little, if any, room for deviation. Within certain limits, one can and often does have a choice of the jurisdiction in which the action to resolve the dispute is brought (commonly-referred to as "forum shopping"); but often, little more is available to the parties. Further, it is not unusual for litigants to find themselves litigating the same issues and/or the same dispute in several different jurisdictions due to courts unwillingness to recognize the jurisdiction and/or legal awards of other jurisdictions.

Contrary thereto, when one chooses mediation/arbitration, one will often have a single procedure and one proceeding in which to resolve the dispute. Further, this procedure is flexible and can usually be tailored somewhat so to best suit the parties desires and needs and the circumstances of the dispute.

A. Mediation/Arbitration Organizations

There are a myriad of different systems of mediation/arbitration available that can be tailored somewhat to specific circumstances.⁵

Perhaps the primary international organizations for the mediation/arbitration of intellectual property disputes are those administered by the International Chambers of Commerce, the World Intellectual Property Organization and the London Court of International Arbitration. In addition, many regional and national systems exist administered by such reputable organizations as the American Arbitration Association (AAA), the Japanese Intellectual Property Arbitration Center and the Centre des Etudes Internationales de la Propriété Industrielle (CEIPI). Finally, there are a host of locally-based mediation and arbitration organizations.⁶

5. For an exemplary list of such institutions, see http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration_online.html.

6. Indeed, the provision of arbitration services has been likened to a growth industry with more than one country adapting its laws and procedures governing mediation/arbitration to take advantage of the economic benefits, real or perceived, that they can bring.

Arbitrate Or Litigate

B. The Legal Framework

The basic legal structure governing mediation/arbitration rules and procedures are the laws of nation-states that govern the subject in that particular country. In this regard, most countries have their own legislative and administrative frameworks within which the mediation/arbitration procedure taking place there should stay.⁷ Particularly influential in such matters has been the UNCITRAL Model Law⁸ that is the basis for the arbitration laws of over 50 countries/administrative regions and at least six states of the United States.⁹

The precise rules under which the mediation/arbitration procedure will occur are those of the particular mediation/arbitration service used. Each has its own rules of evidence and procedure and each offers its own advantages and disadvantages to its users. Each also has its own fee structure and list of mediators/arbiters.

Further, the rules often explicitly permit the parties to agree otherwise than is set forth in the rules. However, caution should be taken with deviating too far from the established rules of the organization.¹⁰

Virtually all mediation/arbitration systems have quite extensive rules permitting the parties to produce and gather evidence. However, they are much more informal than those with which attorneys from the common law traditions are familiar, with strict rules of evidence not being applicable. Nonetheless, they are generally recognized to be of such breadth and depth as is normally sufficient for such cases.

7. For example, the Arbitration Act of 1950 in England, the United States Federal Arbitration Act, 9 U.S.C. §1 et seq., the Swiss Federal Private International Law Act of 1985, as amended July 1, 2004 [see Chapter 12 for International Arbitrations], and the Arbitration Law of the People's Republic of China 6 P.R.C. Laws (Effective 1995). For an English language text of the Chinese Arbitration Law, see http://www.cietac.org.cn/english/laws/laws_5.htm.

8. The United Nations Commercial International Trade Law (UNCITRAL) Model Law on International Commercial Arbitration (21 June 1985) United Nations Document A/40/17 Annex 1, (as adopted by the United Nations Commission on International Trade Law on 21 June 1985).

9. For a complete list of where legislation based on the UNCITRAL Model Law on International Commercial Arbitration has been enacted, see http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration_status.html.

10. Attention is drawn to the fact that the ICC can and has refused to administer arbitrations where the parties have made changes to its Rules of Arbitration which it determined as being to fundamental to its procedure. See Takla, Y., *Non-ICC Arbitration Clauses and Clauses Derogating from the ICC Rules*, 7 ICC International Court Arbitration Bulletin 7, 9 (December, 1996).

For example, the WIPO rules of Arbitration¹¹ provide for preparatory conferences (Article 47), the presentation (Article 48(a)) and the ordered production of evidence (Article 48(b)), the performance of experiments (Article 49), site visits to collect evidence (Article 50), hearings (Article 53), witnesses (Article 54), cross-examination (Article 54(c)) and experts (Article 55). Similarly, the International Chamber of Commerce Rules of Arbitration¹² provide for the taking of evidence (Article 20), use of experts (Article 20(4)) and hearings (Article 21).

It should be noted that most mediation/arbitration systems provide for expedited proceedings as well as full-length proceedings. As such, in matters where time is of the essence, arbitration provides for a procedure in which the action may be completed in a timely manner, something which litigation does not provide. When one considers that, in many European jurisdictions it can take many months just to obtain a preliminary injunction, the advantage that such expedited procedures can provide are obvious.

Last but not least, there are many international treaties and conventions that address themselves to arbitration. While, as we shall see at greater length below that these relate primarily to the recognition and enforcement of arbitral agreements and awards, they also set down what are the minimal international standards which such arbitration agreements and processes need to meet in order to enjoy their advantages.

3. Experienced, Neutral Arbiters

When one litigates, one goes to trial with the judge that one gets and not necessarily the judge that one wants.¹³ Choosing the judge who will hear your case is not normally possible and claims of exclusion are often only possible for very limited reasons, such as a conflict of interest. Whether or not that judge has the capability of understanding technical matters, such as are normally at issue in intellectual property cases, does not matter. The only respite from a judge who is "out-of-control" is via an appeal to a higher

11. WIPO Rules of Arbitration, (effective 1 October 2002) (WIPO Publication 446e, ISBN 92-805-1137-7). Unless otherwise specified herein all references to the WIPO Arbitration Rules refer to the 1 October 2002 rules.

12. ICC Rules of Arbitration, in force as from 1 January 1998, ICC Publication No. 808, date of online publication October 2004. See, http://www.iccwbo.org/court/english/arbitration/pdf_documents/rules/rules_arb_english.pdf. Unless otherwise specified herein, all references to the ICC Arbitration Rules refer to the 1 January 1998 rules.

13. To paraphrase Donald Rumsfeld.

Arbitrate Or Litigate

court with all of the attendant time, expense and uncertainty that this implies. Further, in the common law systems in particular, such appellate reviews are often limited to reviews of findings of law and not findings of fact.

Contrary thereto, most arbitration systems provide a bank of experienced litigators/arbitrators who have been prescreened by the organization to insure their competency and neutrality. The parties are informed of the qualifications of the potential arbiters and have the ability to thoroughly vet them before the case. It is the parties themselves who actually agree on the arbitrator(s) to be used. Thus, the parties can assure themselves, prior to initiating the case, that the person(s) hearing it will be knowledgeable and competent. Further, resort to procedures employing multiple arbiters and arbitration appeals courts provide a system where an "out-of-control" arbiter may be able to be more effectively kept under control than a judge.

In addition, many mediation/arbitration systems provide a mechanism for review of arbiters' decisions.¹⁴ In keeping with the spirit of the mediation/arbitration process, such reviews are expedited and limited in scope. Nonetheless, they provide an important check and balance on arbiter(s) exceeding their authority. Finally, such arbiters' decisions and awards are subject to judicial scrutiny, albeit for limited purposes (as will be discussed below), thereby providing yet another important check and balance to the system to insure its fairness.

4. Confidentiality

Many intellectual property disputes involve confidential information concerning patent information, know-how, biologicals and other type of information and materials that are the confidential and proprietary information of one of the parties to the dispute.

Unfortunately, in that litigations are public proceedings, in principle, this means that the information of the record will become public. While documents can be sealed and gagging orders can be imposed, in cases of where multi-state international litigation is involved, it is unlikely that all countries will be able to secure all of the confidential information with the same level of protection—or even with protection at all.

Consequently, the end result is that in multi-state international litigation, much confidential informa-

tion inevitably becomes of record in the case and enters into the public domain.

Contrary thereto, arbitrations are private matters and are not public matters. Perhaps as a consequence, most arbitration rules and organizations place confidentiality obligations on arbiters and arbitral organizations.¹⁵ While these confidentiality provisions do not extend to the parties themselves,¹⁶ an appropriate confidentiality provision in the arbitration agreement itself would address this hole. Thus, mediation/arbitration procedures often present the parties with the ability to resolve their intellectual property disputes, particularly those involving know-how and trade secrets, without destroying the value of the intellectual property.

5. Enforcement

Perhaps the most difficult problem relating to the use of mediation/arbitration proceedings is enforcement of the award. That is to say, they require judicial intervention in order to be enforced on unwilling parties. Nonetheless, on the whole, awards and decisions of arbitration panels tend to be more easily recognized and enforced by courts of law than those awards and decisions that are handed down by regular courts and tribunals.¹⁷

This trend is a result of the existence of both multilateral and bilateral treaties, the most important of which is the Convention on the Recognition and Execution of Foreign Arbitral Awards of 1958.¹⁸ The New York Convention of 1958 is a United Nations sponsored convention that operates under the aegis of the United Nations Commission on International Trade Law (UNCITRAL). With 139 signatory countries,¹⁹ its applicability is widespread.

15. See, for example, Arts. 20.7 and 21.3 of the ICC Rules of Arbitration and WIPO Arbitration Rules 73 to 76.

16. An exception here is England where the courts have imposed an obligation of confidentiality. See, *Hassneh Ins. Co. v. Stuart*, [1993] 2 Lloyd's Rep. 243 (Q.B.); and *Dolling-Baker v. Merrott*, [1990] 1 W.L.R. 1205, [1991] 2 All ER 890 (Court of Appeal (Civil Div.) 21 March 1990).

17. See Newman, Lawrence and David Zaslowsky, *Litigating Commercial Disputes* 185 (1996) ("In many respects, the enforcement of arbitral awards abroad is much simpler than is enforcement of court judgments."). See also more generally Smith, M.A., et al., "Arbitration of Patent Infringement and Validity Issues Worldwide," *Harvard Journal of Law & Technology*, Volume 19, Number 2 Spring 2006.

18. Also known as the "Convention of New York of 1958". The text of the Convention can be accessed at http://www.uncitral.org/pdf/english/texts/arbitration/NY-convention/XXIII_1_e.pdf.

19. For complete list of signatory countries to the New York Convention of 1958, see http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html.

14. See, for example, Rule 27 of the ICC Rules of Arbitration ("Scrutiny by Court").

Arbitrate Or Litigate

According to Article III of the New York Convention of 1958, "Each contracting state shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon, ..." While the New York Convention also includes a list of "outs" or grounds in Article V²⁰ which a court can cite to refuse to enforce arbitral awards and decisions, it is interesting to note that such "outs" are rarely used.

Further adding to the attraction of the New York Convention is the fact that its applicability is well established. Indeed, its provisions have been the subject of over 1,000 national court decisions worldwide and have generally upheld the applicability of the Convention.²¹

Unfortunately, there is no analogous international convention on the recognition and enforcement of

the decisions of national courts. There are, of course, important multilateral regional conventions relating to the enforcement of judicial judgments and awards, for instance in Europe the Brussels Convention²² and the Lugano Convention.²³ However, their scope and universality are much more limited than that of the New York Convention of 1958.

All Is Not A Panacea However

Despite its widespread acceptance, the interpretation and application of the New York Convention has not necessarily been even, a fact that has been described as being problematic.²⁴ Indeed, some leading commentators consider in this respect that "the principal weakness of the New York Convention seems to be its failure to define certain terms" such as for instance "arbitral awards" or "public policy."²⁵

Closely associated with this problem is the fact that there are some issues that, quite simply, fall outside the scope of arbitration. Primary among these are arbitral awards or judgments that would (theoretically at least) require governmental actions or which would be against "public policy." Primary examples of such issues in the intellectual property field are decisions relating to patent validity, which would require an enforcement court to issue an order for the responsible government agency to take an action (expungement from the patent register), or awards requiring the issuance of a patent license (for example, an "exclusive license" whose issuance would be contrary to antitrust principles), which would require a party to take an action which violates national laws. Further, certain "genres" of litigation, such as those involving generics in the pharmaceutical field, do not easily lend themselves to any settlements short of other than holdings of patent validity/invalidity.

While with a little forethought and creativity, experienced contract drafters may be able to hit upon innovative approaches to get around these problems and arrive at the desired result. For example, in cases (other than those involving generics), where patent

20. Article V states:

1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:

(a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or

(b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or

(e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.

2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:

(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or

(b) The recognition or enforcement of the award would be contrary to the public policy of that country.

21. See the Yearbook: Commercial Arbitration Volumes 1-36. The yearbook contains a yearly review of such cases.

22. The Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters of 1968.

23. The Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters of 1988.

24. Gunther, Pierre-Yves, "Enforcing Arbitral Awards, Injunctions and Orders," American Bar Association, Section of International Law and Practice, 1998 Annual Meeting, International Practitioners' Workshop Series, Enforcement of Arbitration Agreements, Awards and Orders Worldwide. Text can be found at: <http://www.psplaw.ch/Publications/AMBAR-1.html>.

25. Ibid.

Arbitrate Or Litigate

validity will be a central issue, the parties can decide that the arbitrator(s) be empowered to issue a ruling requiring a patent holder to give a royalty-free license in the event of an arbitral finding that a patent is invalid. In any event, it is imperative for the parties to be able to identify the types of arbitral awards and any decisions that would not be enforceable and to develop alternatives to them that would satisfy the parties while still being enforceable by the courts.

6. Conclusion

When deciding whether to avail themselves of either mediation/arbitration or litigation, contract drafters should make an informed and deliberate decision based on the facts and circumstances of their case and not make an uninformed decision that is largely driven by ignorance or fear of the unknown.

Arbitration and mediation can often, but not always, present contracting parties with an option to secure for their clients what is perhaps the best opportunity to assure a fair hearing under well-established and set rules and procedures which are conducted by persons who are specifically experienced with the technology and subject matter in dispute and capable of issuing judgments that are readily enforceable in many jurisdictions, certainly more jurisdictions than judgments of courts of law. As such, Mediation/arbitration can often offer the parties with formidable advantages over reliance upon court jurisdiction that should be carefully considered and not overlooked or minimized.

If one avoids mediation/arbitration simply because one fears it due to a lack of understanding one is doing themselves and their clients a disservice. Remember, the only thing you have to fear is fear itself. ■

The viewpoints & opinions expressed herein are those of the author and do not necessarily reflect, or are intended to reflect, the views of any employer of the author (past or present), and/or any association to which the author belongs.