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The Importance of Arbitration to the Resources Sector

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1) The Importance of Arbitration to the Resources Sector -
Transcription of Video Presentation by Professor Doug Jones AO

Good afternoon.

Firstly, my apologies for my virtual presence today but I am presently committed to chairing an arbitration in London, so unfortunately I can't be with you in person this afternoon. I would like to say, however, that it's a wonderful thing to have a conference such as this based in the centre of the resources industry in Australia in Perth, and I'd personally like to thank Professor Gabriel Moens for all the effort he's put into making this conference a success, and the Australian Institute of Management for their assistance.

I've been asked to speak about the importance of arbitration to the resources sector, and to a degree that topic looks at potential failures of contracts in the resources context. I wouldn't wish, by having this as the topic, to have you believe that dispute resolution is at the very centre of the resources industry. Most of the projects and contracts entered into in and around the resources sector proceed to conclusion without any dispute, however it is important to provide a relief valve in the event that commercial disagreements emerge between parties to the resources process, and it's in that context that I am talking about the contribution of arbitration to the resolution of differences of commercial opinion in relation to the resources sector.

To put a context around the sort of differences of opinion that can potentially emerge between the commercial parties, I'd firstly like to talk about the nature of resource contracts. Then, I'd like to look at the arbitration framework in Australia as setting a context for Australian contribution to the resolution of disputes. Next I will look to the benefits that arbitration provides to the resolution of differences of opinion in the resources sector. Finally, I'd like to express some conclusions about the future of dispute resolution in the resources industry.

Let me come to the first of those topics, namely the nature of the sort of agreements which parties enter into in the context of resource projects. These are really very diverse, ranging from development agreements before any ground is broken or well drilled, to feasibility studies which will predict the economic viability or otherwise of projects, through to initial and then detailed design of the resource projects themselves.

Other agreements relate to the protection and exploitation of intellectual property and process design and other important issues of intellectual property, and, very importantly of course, on and offshore construction once the commitment has been made to do the resource development. Then, of course, the exploitation of the resource itself, which is at the commercial heart of the resources industry, and commodity sales agreements, many of which are very long-term and in respect of a variety of potential resource products.

There are also commercial agreements regarding the transportation of resource commodities both on land and, as Australia is an island, on sea. The inter-relationship between the transportation of resource products and the shipping and other transportation issues involved in the sale of resource products is a whole area of commercial endeavour in itself.

Another issue centres on the insurance that relates to all the different stages of a resource project, from design through construction, through to the sale of the product and the performance of the product.

Finally, long-term gas and oil pricing agreements which can be intended to last for many, many years are commercial arrangements which often need relief valves when the commercial assumptions underlying the initial agreements turn out to be different to what was originally envisaged, and, of course, many parties in the resource sector are involved in changes in shareholding, which we would broadly describe as merger and acquisition activity.

These various agreements represent a vast array of contract structures which have the potential, differently within each structure, for commercial differences of opinion to emerge. The contracts which are entered into are, in many instances, high value, high risk and long term, and consequently the structuring of relief valves to deal with commercial differences of opinion in these contracts is absolutely critical.

There are a number of reasons why the resolution of these commercial differences can and should be effectively solved by the application of arbitration. One such reason is the very technical character of a lot of the contracts and commercial differences of opinion, and the fact that many, if not all, are transnational - that is, parties from different countries are contracting with each other and the performance of contracts often occurs in differing jurisdictions as the product moves or the design is fulfilled or the construction occurs.

There are overlapping commercial interests and the players involved in the various forms of contract are often fulfilling a variety of roles, such as service provision, provision of capital, provision of debt, and the like. These sophisticated contracts with overlapping commercial interests are contracts where there is often a need to draw on the characteristics of arbitration, to which I will come shortly. Before I do, however, let me say that I am by no means advocating that the only means of resolution of commercial differences and disputes is arbitration. It is very important to remember that there are a variety of tools in the dispute resolution tool kit. Of course, in the context of binding dispute resolution, of which arbitration is one such option, courts in the various States where work is performed or goods are delivered also provide very effective commercial dispute resolution services. As an example, the Western Australian Supreme Court has the capacity to provide very effective commercial dispute resolution services to those who wish to bring their disputes to it.

In addition to court dispute resolution processes, there are binding determinations by experts, dispute boards, and other means of issue resolution which are available to be considered as options in the process of the resolution of commercial differences of opinion in the resources sector. It is a matter of appropriately choosing a combination of these tools in the dispute resolution tool kit that is the challenge for those engaged in this wide variety of commercial activities.

Having set the scene, therefore, of the variety of needs which the resources sector has for issue resolution, let me come now to the context of arbitration in Australia, because that is an important characteristic to keep in mind when considering arbitration as an option for dispute resolution for the resources industry.

It is appropriate in this context for there to be consideration of two different types of arbitration, and although their legal characteristic is identical, their capacity to contribute to dispute resolution can be quite different. The two different types of arbitration to which I refer are domestic arbitration on the one hand, and international arbitration on the other. In both of these contexts, the legal scene in Australia has changed very dramatically in recent years.

First, let me say a little about the differences between domestic and international arbitration. By use of the term 'domestic arbitration', I refer to disputes between parties who are purely Australian - that is, two Australian companies who have a difference of opinion and who have the capacity to choose what form of binding dispute resolution will be adopted by them in the event of differences of commercial opinion.

For there to be arbitration between two such domestic entities, there needs to be an agreement to arbitrate. The usual way in which an agreement to arbitrate is established is via a clause in the main contract dealing with the particular commercial activity in question which says that in the event of differences of opinion arising between the parties to that agreement, the parties agree that they will refer those differences of opinion to arbitration. It is, of course, possible after a dispute has arisen, in the absence of such a clause in a contract, for parties to agree to refer a ripe dispute that then exists to arbitration. However, agreement is relatively thin on the ground when disputes arise, and so agreements to refer existing disputes to arbitration in the absence of a prior agreement to arbitrate are relatively rare compared to the pre-written arbitration clauses contained in contracts.

When two domestic parties decide to arbitrate, they have decided, for better or for worse, to turn their back on the court option. However, courts do represent, in Australia and in Western Australia in

particular, a very real option for the resolution of commercial disputes. As I said a moment ago, the Western Australian Supreme Court has now established a very effective commercial dispute resolution process which provides expeditious, flexible and expert determination of commercial disputes.

The parties who choose the court option, who are domestic Australian parties, also choose the publicity which comes with court proceedings. It is very rare indeed for court proceedings to be other than public, whereas arbitration is almost always private, and domestic arbitration in Australia is not only private but confidential. So, leaving aside some other characteristics of domestic arbitration the privacy and confidentiality attributed to arbitration can be a major influence in parties' choice of process.

In the domestic context, we have had arbitration for many years. Indeed, arbitration as a method of dispute resolution goes back thousands of years where parties in civilised societies have almost always had an alternative to established court structures which business people in particular have used, and so it is in Australia that domestic arbitration has a long legal history. In recent times, however, there has been adopted for domestic arbitration in Australia a wholly new legal framework, which is now uniform between the States. I say 'uniform' because the constitutional responsibility for legislation in relation to domestic arbitration lies with the States, and the States have recently agreed to enact uniform legislation completely different to that which previously existed. It is in all respects, except for some areas of detail, identical now to the legislative structure for international arbitration in Australia, which has hithertofore been a completely different legal structure for the reasons which I will come to in a moment.

So there is a new dawn, if you wish to describe it as that, for domestic arbitration in Australia, arising from the capacity in this new reformed legislative structure to make arbitration a truly different and alternative method of dispute resolution to the courts. That is, not just in providing confidentiality and privacy, but also in providing procedures tailored to the particular dispute and designed to get the dispute done and dusted quickly.

We have yet to fully realise the potential of that in Australia, with domestic arbitration having in the recent past failed to provide a true effective commercial alternative to dispute resolution to the courts. I am hopeful, however, that this legislative change will represent a real opportunity for commercial parties in the domestic context, and to emphasise the point, I will say again that there is a very real choice between domestic court proceedings and domestic arbitration which doesn't necessarily exist in the international context. I will come to the reasons for this non-existence shortly.

The second type of arbitration about which I would like to speak is international arbitration. For the Australian context, an arbitration is international if, obviously, it involves parties to the dispute and thus the agreement from which the dispute arose, coming from different countries. However, that is not the only characteristic of international arbitration. An arbitration will also be international if it involves two Australian parties performing a contract outside Australia, or two Australian parties choosing to have their commercial relationship governed by a law other than the law of one of the Australian States. From these definitions, it is seen that there is a broader concept in Australia of international arbitration than just parties from different countries.

We have had, for many years now, very different and modern arbitration laws for international arbitration based on the United Nations Commission of International Trade Law (UNCITRAL) Model Law on international arbitration. In recent years, these have been significantly updated to incorporate amendments by UNCITRAL to its original Model Law and to make some tweaks to the legislation which adds value in the Australian context.

However, it is not just legislation which makes arbitration relevant as a dispute resolution technique. There has to be appropriate infrastructure available, both in terms of professional services and other things, to make arbitration work in any place. In Australia, we've had in recent years a significant growth in the expertise of Australian lawyers and those who service the dispute resolution industry in international arbitration, and we can now say with confidence that in Perth and in other parts of Australia there are practitioners able to provide commercial parties with highly sophisticated international arbitration services. Indeed, Australian lawyers are in demand the world over and many of them leave our shores to practise in North America and in Europe and then come back with the expertise that they have developed in those places. There are also many of them practising in Australia and, indeed, in Perth.

International parties contemplating the use of international arbitration in Australia can be confident that we have both a legal framework which is state-of-the-art and practitioners who can service the needs of commercial parties looking to use international arbitration at a standard second to none.

Let me come now to the third topic that I would like to address, and that is the benefits that arbitration offers the disputes that might result in any of that variety of resource industry contracts that I identified earlier. In this context, let me concentrate on international arbitration if I may. I said a moment ago that there are some characteristics of international arbitration that make the choice which is available for domestic parties to choose either arbitration or the courts not so relevant in the international context. The reason I said that is that there is a fundamental difference between domestic and international arbitration when it comes to enforceability. Once an arbitration is concluded and a decision made by the arbitrators, they produce what is called an award, and that award is available for enforcement within Australia as if it is a court judgment, and where assets are contained within companies existing in Australia, there is no problem of enforcement of the outcome.

However, many of the transactions involved in the resources sector, in the wide variety of agreements that I identified earlier, are with parties who are offshore, who have no assets in Australia, and therefore decisions made by arbitrators in the awards delivered need to be enforced against assets outside the jurisdiction. It is very difficult indeed, not impossible, but very difficult, to take a judgment from the Western Australian Supreme Court and have it enforced in China against assets in China, for example. However, an international arbitral award, as a consequence of a very successful international convention, is enforceable in China even if delivered in Australia. It will be treated as if it is a judgment of the Chinese courts.

The convention that allows for this is called the New York Convention on the Enforcement of Arbitral Awards, and over one hundred and fifty countries are parties to it. This means that international arbitral awards can be taken around the world and enforced in ways in which domestic court decisions cannot, and therefore in that context, when one considers enforceability of the outcome, international arbitration has a virtual monopoly on international commercial dispute resolution. It would only be for very particular reasons that well informed and advised parties would choose in an international transnational contract to adopt court proceedings in a local court.

However, there are other advantages of international arbitration - neutrality being one. Choosing a court usually involves choosing a home town advantage for one of the parties. Arbitration has, as its very essence, the ability to allow for the determination of a dispute in a neutral geographic environment, by neutral parties, and that is a big advantage for those who trade transnationally, but neither party gets a perceived or real home town advantage.

There is, as I earlier mentioned, confidentiality and privacy. There is also flexibility - an arbitral process can and should be designed to suit the particular dispute and be just as short and efficient as it needs to be to satisfy the parties' necessary requirement for a fair process. International arbitrations can and should be a lot cheaper and a lot quicker than many court proceedings - not all, but generally speaking, that is what international arbitration can deliver.

In many of the sectors in which resource contracts are entered into, such as development agreements, construction contracts, pricing arrangements, and shipping and insurance, there is a long tradition of arbitration as a means of resolving those disputes, and the resources sector will pick up in relation to those contracts the more traditional approach to dispute resolution which arbitration represents. However, I think it is worth taking a more holistic view of dispute resolution in the context of the resources sector by saying that arbitration in its many forms is a means for effective dispute resolution. That is already recognised the world over.

In the context of Australia, the message that I would like to leave you with is that we now have the legal and actual expertise structures which enable international arbitrations to be successfully conducted, providing in Australia an effective means of resolving the disputes that emerge in the resources sector. That is, to a degree, saying Australia is a place where, in appropriate circumstances, arbitration should be considered as the preferred method of dispute resolution, particularly in the international context.

To conclude, I think arbitration is already widely used in the resources sector, and the whole panoply of commercial transactions is likely to continue to use arbitration, but it will, I think, continue to grow in Australia as a preferred method of international dispute resolution. It has and is able to deliver the flexibility required in the long-term agreements which many resources contracts involve. Arbitration is and should remain more streamlined and more flexible than domestic court processes, and dialogues such as this conference and regular communication between the service providers and the purchasers of services in the resources sector, in relation to the effectiveness of international arbitration and how it can provide dispute resolution services, is of enormous value.

I wish you well with the conference and hope that from this conference there will emerge some real thought provoking value about dispute resolution and arbitration in the resources sector.

Thank you.

2) The Importance of Arbitration to the Resources Sector - Accompanying Paper

1. Introduction

As a process that might appear to be in constant competition with litigation, which is often perceived as the more traditional method of dispute resolution, arbitration has proven itself to be an effective and reliable means of solving commercial disagreements. This has been t

he case even more so in the context of disputes within a few particular and technical subject matter areas, namely the technology, construction, and resources sectors, where arbitration has retained its position alongside litigation as a permanent feature of dispute resolution.

In the context of resources disputes, litigation presided over by a judge unfamiliar with the subject matter is likely to be costly and quite slow. Critics of arbitration have sometimes contended that it may, in a worst case scenario, imitate court processes and exhibit similar symptoms of inefficiency. It is also their position that in these circumstances, arbitration may even cost more than its litigation counterpart, adding the costs of the hearing (such as venue hire and the arbitrators' fees) to the final bill.

However, there are various features of the arbitration process, both in the domestic and international contexts, that give it an advantage over its litigation counterpart in being able to efficiently resolve disputes in the resources sector.

Beginning with a discussion on the nature of the disputes that arise in the resources sector, this paper will address the Australian position with respect to both domestic and international arbitration to assess the importance of arbitration generally to Australia's resources sector.

2. The Nature of Resource Disputes

One of the difficulties with addressing the issue of disputes within the resources sector is the wide ambit of disputes that arise in the industry—from relatively simple disputes between two parties, to complex, multi-party disputes involving extremely valuable projects that can potentially take years to finally determine. Often, these disputes involve complex questions of law and fact, including issues around national boundaries, environmental claims, insurance and reinsurance, sanctions, bribery and anti-corruption.

As a result of the variety and complexity of resources disputes, a wide range of dispute resolution measures have been implemented over the years, with varying measures of success. Other than arbitration and litigation, such measures have often included various forms of mediation and conciliation. However, with its ability to be customised for any particular dispute and still produce binding results, arbitration has outshone many of these other processes.

There are a number of characteristics of resources disputes that contribute to the important position that arbitration holds in the resources industry. Such characteristics include:

(a) *Technicality of resources disputes*

The technical nature of the disputes that arise in the resources sector often requires a degree of expertise and technical skill that is not guaranteed when a judge is appointed through court processes. Further, as resources disputes often involve complex factual situations requiring voluminous document discovery, the flexibility available to arbitral tribunals in tailoring the arbitral process can streamline the dispute resolution process. To provide some examples, the process might be tailored to include limited time procedures and limited document discovery to provide for a more expeditious procedure.

(b) *International nature of resources disputes*

The international nature of the operations of multinational oil and gas companies and cross-border oil and gas fields result in a number of issues that make arbitration an appealing alternative to litigation. For example, enforcing arbitral awards in different jurisdictions is generally much easier than attempting to enforce a court judgement in another jurisdiction.

(c) *Overlapping commercial interests in resources disputes*

Overlapping commercial interests and long term contractual relationships between oil and gas companies militate against litigation which is often expensive, time consuming, adversarial and destructive of good working relationships.

(d) *Sophisticated resources contracts which anticipate disputes and their resolution*

The proliferation of sophisticated contracts in the resources sector means that disputes are anticipated, and that well planned dispute resolution procedures are able to be put into place much ahead of time. By foreseeing the potential for disputes, and implementing appropriate processes and procedures for their resolution ahead of time, uncertainty and risk can be minimised, even once a dispute has arisen. This is of vital importance to parties in the resources sector given the inherently high levels of uncertainty and risk already associated with their ventures.

3. The Australian Arbitration Framework

Over the last few years, Australia's domestic arbitration regime has undergone significant reform in order to bring it into line with international standards. Similarly, Australia's international arbitration regime has been brought into line with international best practice. Both of these developments have significant implications for the resources sector, as discussed below.

3.1 Domestic Arbitration

Prior to 2010, Australia's arbitration system distinguished between a federally regulated international regime based on the United Nations Commission on International Trade Law (UNCITRAL) Model Law, and a state/territory governed domestic regime that had been implemented in the mid-1980s. In 2010, however, the Standing Committee of Attorneys-General (SCAG) agreed that a new, uniform *Commercial Arbitration Bill* was to be implemented in each state and territory. Under this new Bill, which has now been introduced in all but one Australian jurisdiction,[1] the distinction between international and domestic arbitration has, for the most part, been abolished, and the UNCITRAL Model Law is to be applied to both domestic and international arbitrations in Australia.

The process of moving Australia's domestic arbitration over to the new commercial arbitration acts based on the UNCITRAL Model Law is almost complete. As at the time of writing, New South Wales, Victoria, South Australia, Tasmania, Queensland and the Northern Territory are the Australian jurisdictions in which the new *Commercial Arbitration Act* is in force, while the remaining jurisdictions of Western Australia and the Australian Capital Territory are expected to follow suit in due course. It is likely that the Western Australian *Commercial Arbitration Act* will come into effect this year, as it has already received assent and merely awaits proclamation. It is anticipated that the new Act will stimulate activity and opportunities in the Western Australian resources sector upon its coming into effect.

3.2 International Arbitration

The UNCITRAL Model Law, which was initially drafted in 1985, has formed part of Australia's federal *International Arbitration Act 1974* (IAA) since 1989, in an effort to support the practice of international

[1] The Australian Capital Territory (ACT) is yet to introduce the *Commercial Arbitration Bill*.

arbitration in Australia. This commitment to international arbitration has been maintained over successive governments, with a number of steps taken over the years to continually improve Australia's international arbitration infrastructure.

In July 2010, the IAA underwent significant reform with the enactment of the federal *International Arbitration Amendment Act 2010*. The most important modifications made by this amending act were the incorporation of the 2006 UNCITRAL amendments to the Model Law and the repeal of provisions that allowed parties to opt out of the Model Law.

These amendments, among others, ensured that the IAA remained in line with international best practice, and assisted in further advancing Australia as a centre for international arbitration, encouraging parties to seriously consider it as a potential arbitration venue. These legislative changes also sought to increase the quality of international arbitration in Australia by creating consistency and certainty in the application of Australian international arbitration law.

As a result of the government's commitment to international arbitration, alongside the involvement of various professionals and industry bodies such as the Australian Centre for International Commercial Arbitration (ACICA), the Australian Commercial Dispute Centre (ACDC), the Institute of Arbitrators and Mediators Australia (IAMA), the Chartered Institute of Arbitrators (Australia) (CIArb Australia) and the National Alternative Dispute Resolution Advisory Council (NADRAC), Australia has a very well developed international arbitration industry.

Given the large amount of foreign investment in the resources sector, it is essential that foreign parties feel confident in Australia's dispute resolution framework. Further, the availability of a robust international arbitration framework ensures that the disputes that arise in the international arm of Australia's resources sector can be determined in a confidential, flexible, neutral and enforceable manner.

3.3 Benefits of Arbitration in Resources Disputes

As has been mentioned, arbitration has retained its position of prominence in the resources sector even amongst the various methods of dispute resolution which have been implemented in the industry over the years. There are a variety of reasons why this is the case. In addition to the aforementioned characteristics of resources sector disputes that likely render them more easily resolved by arbitration, there are a number of features of the arbitration process itself that make it well suited to resources disputes. These features include:

(a) *Confidentiality*

The opportunity to keep confidential any disputes arising from resources projects can be of critical importance to reputation and market value.

(b) *Flexibility*

The flexibility that arbitration can provide - that is, a dispute that has arisen can be resolved by an arbitration which can be tailored and conducted in a streamlined manner so as to allow the project or joint venture to continue smoothly.

(c) *Neutrality*

The ability to select an arbitrator who is of neutral nationality, or who is an expert in the particular energy and resources field, is also likely to be beneficial, especially from both cost and time perspectives. Further, this can give the parties confidence that the arbitrator has properly considered both the technical and legal issues that may be relevant to the dispute.

(d) *Enforceability*

With such a large sums of money at stake and projects often being carried out in developing countries where confidence in national court systems may not be high, the ability to enforce any judgment against a foreign national or state entity may be uncertain. Thus, enforceability is of vital concern.

To this end, over 145 countries have adopted The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention 1958). In doing so, they have agreed to enforce international commercial arbitration awards made in foreign countries, provided that the conditions of the New York Convention 1958 are met. In contrast, international conventions on the recognition and enforcement of foreign judgments have had very limited success. Whether a foreign judgment will be recognized in another country will depend on the laws in that country and, in extreme cases, it may be necessary to start the proceedings from scratch.

4. The future of resource disputes

As the resources sector continues to develop, and as the nature of its associated disputes become ever more technically complicated, it is likely that the use of arbitration within the industry will grow. Given the flexibility of arbitral processes, arbitration has the potential to meet the particular requirements of disputes and the changing needs of its users. For example, the increasing popularity of streamlined arbitral procedures has come about in response to the need to have commercial disputes determined more expeditiously in particular circumstances. The sustained commitment by arbitrators, practitioners and parties to ensuring that arbitral processes do not mimic court procedures has assisted in providing for such increased efficiency.

All indicators suggest that arbitration is going to retain its position of importance within the resources sector. Thus, it is to the benefit of both the resources sector and the dispute resolution industry for there to be continuing dialogues, such as the conference to which this paper relates, in order to ensure that arbitration continues to meet the needs of the resources sector.