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Leveling the playing field

Partner Douglas Mancill of *Deacons* (*Price Sanond Prabhas & Wynne Limited*) explains why the Thai government's poor track record in arbitrated disputes, and its recent efforts to even the score, may go against international trends and potentially dampen commercial activity and investment.

Thailand has traditionally been an arbitration friendly state, embracing and promoting arbitration as a method of resolving commercial disputes. In fact, Thailand was among the first countries to adhere to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention), which it adopted in December of 1959. Thailand's recognition of arbitration as a fair, transparent and efficient means of settling commercial disputes has also traditionally extended to disputes between the private sector and government agencies, with Section 15 of its current arbitration law – the *Arbitration Act*, B.E. 2545 (Arbitration Act) – specifically providing that disputes between private parties and the government can be settled by arbitration, as follows:

> *"In any contract made between a government agency and a private enterprise, regardless of whether it is an administrative contract or not, the parties may agree to settle any dispute by arbitration. Such arbitration agreement shall bind the parties."*

Thailand is also a party to over thirty-five bilateral investment treaties (BITs) that include some form of arbitration requirement.

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In recent years, however, the Thai government has begun to back away from the use of arbitration to settle disputes between private parties and government agencies. Following an unfavorable arbitration decision against Thailand in a dispute over construction of an expressway, the Thai Cabinet concluded in early 2004 that concession contracts are a kind of administrative contract and should therefore be submitted to the Thai administrative courts or the courts of justice. The Cabinet also concluded that contracts with the Thai government should be only be executed in the Thai language and governed exclusively by Thai law. If a Thai agency wanted to enter into a concession contract that departed from these principles, the contract would need to be submitted to the Thai Cabinet which would decide if a departure was warranted on a case-by-case basis.

On 28 July 2009 this matter was again considered by the Thai Cabinet, which observed that in many contracts between state and private agencies, particularly mega-projects or state concessions, arbitration was the agreed form of dispute settlement. Distress was expressed over this practice because, according to a report about the Cabinet meeting

issued by the Secretariat of the Cabinet, "most state agencies lost the cases or were required to pay the compensation, resulting in huge national budget burdens" when arbitration was employed. The Cabinet therefore decided to require all governmental agencies to first obtain Cabinet approval before executing any contract that contained an arbitration provision. No regulations or guidance were provided as to when such approval would be provided; rather, decisions would be made on a case-by-case basis.

Taking matters a step further, a bill has been introduced to amend the *Arbitration Act* to replace the language in Section 15 – which expressly provides that arbitration clauses in contracts with government agencies are enforceable – with the following:

> *"This Act shall not apply to the contracts between government agencies and private entities, regardless of whether such contracts are administrative contracts or not."*

The rationale behind this proposed amendment was the government's poor track record in arbitrated disputes.

These developments are puzzling and troubling for everyone, Thai or foreign, doing business in Thailand. The proposed amendment to the *Arbitration Act*, for example, creates tremendous uncertainty. Even if this legislation is amended to essentially reverse the language of Section 15, Thailand is still obliged under the New York Convention to recognise existing arbitration clauses and enforce existing arbitration awards. Meanwhile, Thailand has similar obligations under its BITs with other countries. Changing the language of the *Arbitration Act* and adopting these Cabinet resolutions should not change the country's treaty obligations to submit disputes to arbitration and enforce foreign arbitration awards, but they will raise unsettling questions about the government's willingness to arbitrate disputes.

These measures also go against international trends, potentially dampen commercial activity, and deter investment, particularly in the infrastructure sector where investment is much-needed. Looking forward to future contracts between private parties and Thai government agencies, these developments will undermine investor confidence and increase the cost of government projects. When arbitration is not available disputes must be litigated (or abandoned), which often leads to dueling court proceedings in multiple jurisdictions. This is not only expensive and inefficient, but also generates considerable and often damaging uncertainty.

There are also serious and real limitations on the enforcement of foreign judgments in many jurisdictions, including Thailand. Under the New York Convention, however, countries are treaty-bound to recognise and enforce arbitration clauses and awards. Moreover, an arbitration award can only be challenged on very narrow, limited grounds, therefore limiting the prospect of lengthy, costly and multi-tiered appeals that are available in litigation.

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Arbitration is widely recognised as a neutral means of dispute resolution because it is designed, and has been agreed to, by the parties in advance of any dispute. It is seen as efficient, fair and transparent. Many major lenders therefore require project contracts to have an arbitration clause. Consequently, if arbitration is not available, tendering parties will need to increase the price of their bids to cover their higher risks and funding costs. Of course, they may refuse to bid altogether. These ramifications limit the pool of qualified bidders, increase project costs and retard the development of quality infrastructure.

There is very real concern in the foreign and local business community about this move away from arbitration in Thailand. The success of domestic and international trade and investment depends on several core issues, one of which is having a method by which parties can resolve commercial disputes quickly and effectively. Because many businesses believe arbitration has serious advantages when compared to litigation, they are more willing to trade with and invest in states where arbitration is supported as an effective procedure for resolving commercial disputes. Restrictions on the availability of arbitration to resolve commercial disputes will,

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therefore, have a negative effect on investment in Thailand, the Thai business environment, and the ability of Thailand to effectively pursue complex development projects in the public interest.

Precluding the use of arbitration when a government agency is a party to a contract with a private party will increase rather than decrease the costs of infrastructure development in Thailand. There are also related reputational issues at stake. Claiming that a prohibition on arbitration is justified because Thai government agencies tend to lose arbitrated disputes could be mistakenly read to suggest that securing a fair and transparent outcome to infrastructure disputes is of secondary importance to ensuring that government agencies procure a favorable outcome in such disputes.

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Many of those familiar with Thai practices suggest that better and more proactive contract management practices would substantially (and fairly) strengthen the hands of government agencies when disputes arise – as they almost inevitably do – in large projects. Retention of experienced counsel from the private sphere would also go a long way in leveling the playing field, and this does appear to be the government's real objective. Whilst taking such steps may run contrary to the current practices of many Thai government agencies and will come up at an initial cost, in the long run Thailand will benefit more from such measures than from adopting Cabinet resolutions and laws that run contrary to the international trend of arbitrating disputes and which, in spirit at least, are inconsistent with Thailand's treaty obligations.

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In next month's issue...

A rocky global economic climate in the past eighteen months has led to an unprecedented upturn in cross-regional acquisitions by Asia and Middle Eastern players, with cash-rich individuals and corporations domiciled in these regions eager to participate in a spate of outbound foreign investment. Many have been attracted to investment opportunities in the United States especially. Don't miss next month's edition of *Asian-Counsel* in which we cover the major challenges, benefits and risks to Asian investors looking to do business in the Americas, from forming an effective M&A strategy (and avoiding the pitfalls) and buying out of bankruptcy, to the obstacles to investment and the dangers of entering a sophisticated market such as the US.

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