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Securities Arbitration in the Kuwait Stock Exchange

A Comparative study

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Abstract:

The establishment of a strong securities arbitration policy in Kuwait is still in its infancy. Securities arbitration is an alternative dispute resolution (ADR) process that amounts to an alternative to litigation by way of traditional lawsuits in court. It differs from arbitration proceedings in other ADR cases in that it has a separate set of rules and processes unique to securities exchanges. In Kuwait,⁽¹⁾ a special regulation for securities arbitration was enacted in 2014. However, this system was not practical and therefore is not extensively used.

This article will compare these rules with those of a developed stock exchange such as the New York Stock Exchange (NYSE)⁽²⁾ with a view to making suggestions for improvement and ultimate implementation of securities arbitration in the Kuwait Stock Exchange.

Keywords: Securities Arbitration, Kuwaiti Stock Exchange, Securities Law.

- (1) In Kuwait, article 148 of Law No 7 of 2010 Regarding the Establishment of the Capital Markets Authority and Regulating Securities Activities and its Amendments mentions that 'Disputes arising from the obligations set forth in this Law or any other law if related to transactions of the capital market may be resolved by arbitration, according to such arbitration system as may be adopted by the Authority'.
- (2) The New York Stock Exchange (NYSE) is one of the world's largest marketplaces for stocks and other exchange-traded investments. The NYSE is an example of a trade group. As there was previously no organised stock exchange, in 1792 stockbrokers signed an agreement setting up the Stock Exchange to regulate prices and commissions. Twenty-four stockbrokers gathered under a buttonwood tree outside the building located at 68 Wall Street to sign the agreement known as the Buttonwood Agreement. This agreement remained in force until 1974, when the government broke up the monopoly. Over time, Wall Street has come to represent the US financial markets as a whole. «<http://www.nyx.com/en/who-we-are/history/new-york>».

1. Introduction

The introduction to this paper consists of the following five sections: the aim of the article, the benefits of the article, the methodology of the article, the scope of the article and the organisation of the article.

1.1 The Aim of the Article

Developing a fair, efficient and orderly securities market is one of Kuwait's biggest institutional challenges today. In 2014, a set of rules regulating securities arbitration was issued in order to establish this type of arbitration. However, up to 2019, these rules have not been applied by the Kuwaiti Capital Market.

This article considers alternative dispute resolution mechanisms as used in other stock exchanges, in order to make recommendations for improving the Kuwait Stock Exchange (KSE). This article analyses securities arbitration rules and compares them with the NYSE rules, seeking to improve the standard of the rules and make them more effective.

1.2 The Benefits of the Article

The two main aims of the paper are: firstly, to identify the problems that currently exist for arbitration mechanisms in the securities area in Kuwait. Secondly, to propose solutions that can create a safe legal environment that can be used by the investor when disputes arise on the stock exchange.

1.3 The Methodology of the Article

This article explores how the legal framework for securities arbitration in Kuwait can be improved. The research question addressed by this article is how to make arbitration rules in Kuwait work in practice. In other words, how to enable people who work in the securities markets be in a position to make use of this form of ADR. This research article compares similar legislation in the developed market in the United States (US) to evaluate its potential effectiveness in averting problems. Thus, it contributes to the body of academic and legal knowledge of this subject.

The US legislation ensures that securities arbitration is suitable for its capital markets to solve disputes. This legislation has evolved over many years in an effort to increase the effectiveness of securities arbitration. As a result, the use of a comparative law approach in this article will help to determine which laws and regulations are the most effective. In the NYSE, securities arbitration is the primary means of dispute resolution. This article considers the rules and processes around arbitration and how these can be incorporated into the KSE procedures.

1.4 The Scope of the Article

The article sets out the existing legal framework applicable to securities arbitration in Kuwait and analyses the more controversial role of securities arbitration. It also provides a comparative analysis of securities arbitration systems across the US and Kuwait to gain insight into the Kuwaiti system and to propose recommendations accordingly.

The NYSE was selected for the comparative study due to its long history, its experience in dealing with securities arbitration matters, as well as the specific rules for oversight of arbitrators. The NYSE arbitration law is contained in Article 75 of the New York Civil Practice Law and Rules (CPLR).

1.5 The Organisation of the Article

This article is divided into two sections. The first section describes the meaning of securities arbitration. Section two examines the procedure of the arbitration process.

1.6 Review of Literature

There are a number of studies that deal with arbitration in Kuwait, such as Iqbal Alqilaf book entitled "Arbitration in Kuwait". The book defined arbitration and the conditions in which it can be used, as well as several other general topics relating to arbitration. However, this work did not cover the topic of Securities Arbitration, which is a highly specialized field of arbitration. The topic of Securities Arbitration is relatively new and there is not much literature on the subject. Therefore, this article will discuss the more controversial role of securities arbitration in Kuwait.

2. What is Securities Arbitration?

The following is an introduction to securities. To understand how the law relating to securities arbitration works, one needs to appreciate what is meant by the term ‘securities’.

2.1. What are Securities?

A security represents, firstly, an ownership position in publicly traded company shares. Three rights are given to an investor who buys shares. The first is the right to vote. The second is the right to take delivery of a corporation’s residual cash flows. The third is the right, after all claimants have been paid, to the residual assets in the event of liquidation.⁽³⁾ Secondly, a security refers to the creditor relationship with a government body or a firm’s bonds,⁽⁴⁾ sukuk⁽⁵⁾ and debt securities.⁽⁶⁾ Thirdly, securities are rights to ownership as represented by an option. The purchaser has an option, rather than an obligation, to buy or sell, so the consumer buys the option against a sum of money. The premium paid is the highest loss that the purchaser of an option can suffer.^{(7),(8)} Each of these categories can furthermore consist of different types of security. Each of these has advantages and disadvantages. For example, one of the advantages of issuing shares is that the issuing company does not have to repay the borrowers’ money except in the event of liquidation.

(3) Stephen J Choi and A C Pritchard, *Securities Regulation: The Essentials* (Aspen Publishers 2008) 10.

(4) *ibid.*

(5) An alternative finance investment to bonds are sukuk instruments, which perform an equivalent function to bonds and loans in the western financial system, but which use Shari’ah compliant financial instruments. They are structured to pay a return linked to the assets that the bond has funded, so that they are not paid in a conventional sense. They are a form of asset-based and profit-sharing instrument; Iain G Macneil, *An Introduction to The Law on Financial Investment* (2nd edn, Hart Publishing Ltd 2012) 146.

(6) Debt securities are proof of a monetary debt which must be repaid according to certain terms that define the interest rate and maturity/renewal data. <<http://www.imf.org/external/np/sta/wgsd/pdf/051309.pdf>> accessed 15 July 2019.

(7) Macneil (n 5) 154.

(8) Will Kenton, ‘Investing Essentials: Security’ (Investopedia, 28 May 2019) <<http://www.investopedia.com/terms/s/security.asp>> accessed 16 July 2019.

The list of securities varies from country to country. In the 2010 Law, the Kuwaiti legislature defined securities as:

Any bond of whatever legal form that proves a share in a marketable finance licensed authority including:

- A. Shares issued or proposed to be issued in a company's capital.
- B. Any instrument that originates or proves indebtedness that has been, or shall be, issued by a company.
- C. Loans, bonds and other instruments that could be convertible into shares in a company's capital.
- D. All marketable general debt issued by various government entities or the public authorities and institutions.
- E. The *sukuk* issued under the applicable Shari'ah-compliant contract forms.
- F. Any right, option or derivative relating to any of the securities.
- G. Units in any collective investment scheme.
- H. Commercial paper, such as promissory notes, letters of credit, fund transfers, exclusively inter-bank traded instruments, insurance policies and the rights of beneficiaries in pension schemes shall not be considered as securities.⁽⁹⁾

It can be seen from the above that the definition of securities is quite extensive. Furthermore, by eliminating commercial paper from the definition of securities, the legislature has removed any ambiguity on the subject. In terms of securities law, in some countries such as Kuwait and the US, securities are regulated by separate and special laws called 'Securities Laws', while in other countries, such as the UK, securities law is part of general financial regulation.

(9) Capital Market Law 2010, Article 1.

2.2 Securities Arbitration

Alternative dispute resolution (ADR) is not a new process. Arbitration is one method of ADR, in addition to negotiation, mediation and med-arb. Alternative dispute resolution is well-established in a number of jurisdictions, including Kuwait, and has become an increasingly common way for the resolution of business and international conflicts in the modern context. In fact, many commercial agreements include explicit dispute resolution clauses, in which the contracting parties agree that this method will be used in the event that a dispute occurs during the lifetime of the contract.

Arbitration is a form of ADR in which parties vest a third party, known as an arbitrator, with the authority to decide a dispute. The arbitrator hears the evidence and issues a final and binding arbitration award. Arbitrators are nominated by both parties because of the belief that they are sufficiently capable and knowledgeable to resolve a dispute in accordance with a set of legal rules. Arbitration awards can be either binding or nonbinding depending on the terms of the initial contract.

Securities arbitration is one type of institutional arbitration. It occurs within certain institutions, based on the rules of those institutions, which are recognised by the parties and established before the dispute arises. As a consequence of this, the rules are applied to all disputes that occur within this agreed context at the specific institution. In Kuwait, institutional arbitration includes arbitration on the stock market, which is the subject of this article. Alternative dispute resolution processes refer to ways of dealing with legal disputes in forums other than traditional civil litigation courts. These processes are often cheaper and quicker than traditional trials in court. Disputes in the securities markets are typically handled through arbitration rather than through litigation⁽¹⁰⁾.

A problem can occur when the investor purchases a security of a foreign company or a security listed in a foreign country. This is because there are different legal systems with different rules and laws pertaining to legal action. A

(10) SEC, 'Investor Bulletin: Broker/Dealer Consumer Arbitration' (SEC, 20 December 2016) <https://www.sec.gov/oiea/investor-alerts-bulletins/ib_arbitration.html> accessed 15 May 2019.

simple solution to this is to agree in advance to arbitration being the preferred method of dispute resolution. Furthermore, securities disputes have their own dedicated court that deals only with securities exchange matters. The procedure used in securities courts is different from the traditional civil procedure used in other courts. However, securities courts are beyond the scope of this study.

These kinds of arbitration agreements are controversial due to the fact that they have the potential to block class action litigation or class action arbitration. Therefore, in 2016 the Consumer Financial Protection Bureau (CFPB) issued a rule banning the use of mandatory arbitration clauses where such clauses would result in preventing anyone from instituting class action litigation in court⁽¹¹⁾. Class action refers to matters brought by a group of people who have all been affected by the same injustice. However, class action lawsuits are beyond the scope of this study.

In the US, during the 1980s, companies began to include arbitration clauses in contracts with consumers/customers, investors and employees. These were not always the result of individually negotiated agreements. This trend continued in the 1990s within the consumer financial services industry⁽¹²⁾.

Arbitration is different from a lawsuit in court, in that:

- The parties select a neutral arbitrator or panel of arbitrators.
- Arbitration decisions can only be appealed on limited grounds.
- Arbitrators are not bound by legal precedent but they have to follow a Code of Arbitration Procedure.
- The documents and evidence submitted in arbitration are not publicly available.
- Arbitration may be cheaper (in some countries) and quicker than litigating a dispute in court.

(11) Buckley Sander, 'Special Alert: CFPB Issues Arbitration Rule Banning Future Use of Mandatory Arbitration Clauses' (Buckley Sander, no date) <<https://buckleyfirm.com/sites/default/files/Special-Alert>> accessed 30 May 2019.

(12) <https://files.consumerfinance.gov/f/documents/201707_cfpb_Arbitration-Agreements-Rule.pdf> accessed 30 May 2019.

Securities arbitration is faster and less costly than litigation. Recent studies support the view that average legal costs are less in securities arbitration matters than in litigation brought before courts. From 1988 to 2007, the average litigation costs increased from \$12,000 to \$22,000 and have continued to rise since then⁽¹³⁾. Cases that were brought by way of securities arbitration have been finalised on average 40% faster than cases that were filed in court⁽¹⁴⁾.

In recent times, securities firms have preferred to include a mandatory arbitration clause in contracts with clients. These arbitration clauses are in the style of an adhesive contract (i.e. take-it-or-leave-it style contracts). This, in effect, forces the client (investors) to submit to such a provision should they wish to trade in the market. There are pros and cons to the mandatory pre-dispute arbitration clauses for customers of securities firms. The advantages are that such a clause is useful because arbitration is not only fair to the parties, but also less costly and faster than litigation⁽¹⁵⁾. However, the disadvantages are that investors see the mandatory arbitration clauses as unfair, due to the fact that they prevent them from approaching the courts for assistance. These clauses also prevent investors from having legal representation at the hearing, and the process does not allow for any appeal for the aggrieved party⁽¹⁶⁾.

For dispute resolution, securities arbitration is a preferred option for retail investors⁽¹⁷⁾. It offers protection due to the speedy and uncomplicated

(13) WHITE PAPER ON ARBITRATION IN THE SECURITIES INDUSTRY: The success story of an investor protection focused institution that has delivered timely, cost-effective, and fair results for over 30 years, OCTOBER 2007, <https://www.sifma.org/wp-content/uploads/2017/03/White-Paper-on-Arbitration-in-the-Securities-Industry-October-2007.pdf>, p2.

(14) *ibid*.

(15) Debora Fernandes, 'Investors' protection in the US: the issue of mandatory arbitration clauses in contracts between investors and brokerage/advisory firms' (2017) 13(2) *Revista Direito GV* <http://www.scielo.br/scielo.php?script=sci_arttext&pid=S1808-24322017000200520> accessed 15 May 2019.

(16) *ibid*.

(17) Investors are generally people or companies who want to increase their wealth. They can do so by investing their money in a number of places, such as 1) depositing money in a bank without risk, although the interest rate is generally poor compared to other investments; 2) buying real estate; 3) buying bonds that are issued by companies or by a government, receiving a fixed income on a fixed date in the future; 4) buying vintage cars or antiques or 5) buying shares in a company, which is more flexible, with potentially higher returns than a bank deposit, but presents a higher risk.

nature of the process. Retail investors' protection is different to institutional investors,⁽¹⁸⁾ protection. Securities arbitration allows for a cheaper and faster dispute resolution process that is less complicated and more suited to individuals dealing with matters on their own.

In 1975, the US Congress amended the securities laws to give the Securities Exchange Commission (SEC) oversight of Self-regulatory Organisation (SRO) securities arbitration. Another major change in the securities industry occurred in 2007, when the SEC consolidated SRO oversight of the exchanges to the Financial Industry Regulatory Authority (FINRA). In the US, the FINRA manages the largest securities arbitration forum. In order to improve the KSE, a body with similar powers and authority should be established.

In Kuwait, arbitration in financial markets is permissible⁽¹⁹⁾. An agreement to arbitrate shall be considered valid unless there is no other evidence. An arbitration provision included in a contract is independent from other contract provisions. That means the provision for arbitration is valid in and of itself, even though the original contract may be null, cancelled or terminated. In the KSE, in general, the award of an arbitral tribunal should be issued within six months from the date of the first valid session of which both parties are notified. It can be extended by an additional two months⁽²⁰⁾.

Investors may bring a wide variety of claims against brokers and brokerage firms in arbitration including churning, unsuitability, negligence, misappropriation, failure to diversify, unauthorised trading, material misrepresentation or omission and breach of fiduciary duty.⁽²¹⁾

(18) Institutional investors include pension funds, mutual funds and insurance companies; these have increased significantly over the years.

(19) According to Article 12-1-1 of Settling Disputes with Arbitration and Arbitration Rules 'Disputes arising from the obligations set forth in the Law or any other law may be resolved by arbitration according to arbitration rules referred to in this Module, if in respect of capital market transactions'.

(20) Dr Abdullah Mesfer Al Hayyan, Mohammed Abdullah Rabah Al – Mutairi, Mediator in explaining the law of the Capital Markets Authority: Explanation of Law No. 7 of 2010 and its amendments on the establishment of the Capital Market Authority and the regulation of securities activity and the executive regulations issued in accordance with Resolution No. 72 of 2015 (2019, Dar Alalam for Publishing and Distribution) p 879- 890.

(21) Findlaw, 'Understanding Securities Arbitration' (FindLaw, no date) < accessed 13 May 2019.

In the US, account opening agreements will almost always contain a provision binding the parties to arbitration in the event of a dispute.⁽²²⁾ Contract law gives the parties the freedom to include any kind of provision they wish in their contract. However, in the securities industry, mandatory securities arbitration clauses are included in these contracts. This permits a balance of the needs of the brokerage firm and private investors and maximises the greater societal gain.

2.3. Mandatory Securities Arbitration

The securities arbitration process continues to play a crucial role, possibly even an indispensable role, in national policy to protect investors. While securities arbitration agreements have the advantages of speed, lower costs and greater accessibility for the parties, there are still numerous problems with these types of agreements. Securities arbitration provides strong procedural protection to ensure a fair process for investors and a neutral forum. Some scholars criticise the fairness of compulsory or ‘forced’ arbitration, especially in the consumer context.

In general, an agreement to arbitrate is voluntary and can be cancelled by either party. However, sometimes arbitration can be mandatory. These agreements, although being mandatory, can be fair to both parties. Mandatory arbitration has recently grown to be an area of extreme importance to any legal system. It has become increasingly widespread and is now commonly used in a wide variety of contexts, including in business transactions, employment contracts and consumer claims.

Mandatory arbitration can potentially lead to an abuse of the process, particularly in cases where the parties have unequal bargaining power. Hence, it is not always seen as a preferred option for dispute resolution. Some scholars have criticized the inflexibility of mandatory arbitration clauses in contracts. They believe that these clauses unfairly limit the parties’ options for settling disputes. As a result of this criticism, some countries have introduced systems that include both mandatory arbitration in some instances, while not limiting the parties to only arbitration as a means for dispute resolution. For example,

(22) SEC Investor Bulletin (n 10).

in the UK, the Financial Ombudsman Service (FOS) was established by Parliament to solve problems reported by individuals. The FOS has a statutory function. Its main role is to resolve disputes fairly, reasonably and informally as an alternative to referring these matters to the civil court. With regard to matters related to complaints against authorised firms, the FOS has compulsory jurisdiction to preside over matters between private consumers and businesses that provide financial services. Private investors will always retain the option of approaching the civil courts instead of accepting the FOS jurisdiction. However, the FOS jurisdiction will always be binding on the investment firm.²³

Mandatory pre-dispute agreements have generated the most controversy due to their appearing to be beset with structural bias.

3. The Procedure of the Arbitration Process

Arbitration proceedings generally include matters such as unauthorised trades or matters relating to disputes between broker and customer. In the US, there are actually two arbitration codes, one for customer disputes, and another for industry disputes, although the two codes are substantially similar in content. This paper considers the code for customer disputes.

(23) FCA, 'About the Financial Conduct Authority' (FCA, April 2013) < <http://www.financial-ombudsman.org.uk/about/> > accessed 19 July 2019.

The Capital Market Authority (CMA)²⁴ in Kuwait passed a special rule for arbitration, which reads as follows:

Disputes arising from the obligations set forth in capital market law, or any other law, may be resolved by arbitration according to the arbitration rules referred to in this book, if in respect of capital market transactions⁽²⁵⁾.

(24) The CMA acts according to the 2010 Act. The Act has 13 chapters and 165 articles. The first chapter is about the definitions of words and terms wherever they are used in the Act such as exchange, clearing agency, a security, listed company and others. The second chapter (from article 2 to article 30) is about the Capital Market Authority and its objectives, duties, powers, managing the authority board. For example, Article 3 of chapter 2 mentions the objectives of the Kuwaiti Authority which are:

1- Regulate securities activities in a fair, transparent and efficient manner. 2- Grow the capital markets, and diversify and develop investment instruments thereof in accordance with best international practice. 3- Enhance investors' protection. 4- Reduce systemic risks arising from securities activities. 5- Impose requirements of full disclosure in order to achieve fairness and transparency, and to prevent conflicts of interests and the use of insider information. 6- Enhance compliance with the rules and regulations related to securities activities. 7- Enhance public awareness of securities activities and of the benefits, risks and obligations arising from investments in securities and encourage their development.

The Act has seven aims. The Act mentions the aims but it does not mention the way of achieving them and nor does it explain them. The Act also gives the authority the power to pass rules according to Article 4 stating that 'the Authority's board shall issue necessary byelaws and instruments to execute the Law. It shall also work on issuing recommendations and the necessary studies needed to develop the regulations which assist in achieving its objectives'. Chapter three (articles 31–47) of the Act is about securities exchanges. Chapter four (articles 48–62) covers clearing agency. Chapter five (articles 63–67) relates to regulated securities activities. Chapter six (articles 68–70) provides rules for reviewing the accounts of licensed persons. Chapter seven (articles 71–75) is about acquisitions and protection of minority interests. Chapter eight (articles 76–91 articles) concerns collective investment schemes. Chapter nine (articles 92–99a) is about the prospectus for securities issued by companies. Chapter ten (articles 100–107) is about disclosure of interests. Chapter eleven (articles 108–148) covers penalties and disciplinary actions. Chapter twelve (articles 149–150) sets out general rules. Chapter thirteen (articles 151–165) contains transitional provisions. The Act covers transactions and other dealings with securities.

It was the first major legislation to regulate the offer and sale of securities.

(25) Article 12.1.1 of Settling Disputes with Arbitration and Arbitration Rules.

Therefore, this article allows any dispute related to capital market law to be resolved by these institutional rules. The agreement to arbitrate shall be considered valid unless there is no other evidence⁽²⁶⁾. Further rules are that:

- The ruling of the Arbitral Tribunal shall be issued within six months from the date of the first valid session at which both parties are notified to attend⁽²⁷⁾.
- The parties shall appear before the Tribunal in person, or through an attorney or representative, and all arbitration sessions shall be confidential⁽²⁸⁾.
- The Arbitral Tribunal shall decide on a dispute in accordance with the laws of the State of Kuwait, unless the disputing parties agreed to apply another legal system. However, under no circumstances may decisions violate the rules relating to public order in Kuwait⁽²⁹⁾.
- Arbitration rulings shall be binding and final. They shall be executable only after the writ of execution has been obtained, in accordance with the legal procedures stipulated in chapter twelve of the Civil and Commercial Procedures Law⁽³⁰⁾.

3.1 Pre-Dispute Arbitration Agreements with Customers

Pre-arbitration agreements have a number of advantages such as the fact that they contribute a high degree of predictability to the relationship between the parties. They put the parties on an equal footing when a dispute is declared, in that an arbitration process is agreed upon with an independent arbitrator. This has the effect of deterring selection tactics by either party with a view to securing an advantage in the dispute resolution process. In general, the current system serves the interests of investors. Pre-arbitration agreements allow investors to pursue small claims, provide a friendly forum for claimants, reduce the total costs to investors and securities companies, and secure

(26) *ibid*, Article 12.1.3.

(27) *ibid*, Article 12.1.5.

(28) *ibid*, Article 12.3.14.

(29) *ibid*, Article 12.3.10.

(30) *ibid*, Article 12.4.5.

supervision of expert regulators, all within a framework designed specifically for investor claims.

According to NYSE rule 636, any pre-dispute arbitration clause shall be highlighted and shall be immediately preceded by the following disclosure language (printed in outline form as set forth herein) which shall also be highlighted:

- (1) Arbitration is final and binding on the parties.
- (2) The parties are waiving their right to seek remedies in court, including the right to jury trial.
- (3) Pre-arbitration discovery is generally more limited than and different from court proceedings.
- (4) The arbitrators' award is not required to include factual findings or legal reasoning and any party's right to appeal or to seek modification of rulings by the arbitrators is strictly limited.
- (5) The panel of arbitrators will typically include a minority of arbitrators who were or are affiliated with the securities industry.

No agreement shall include any condition which limits or contradicts the rules of any self-regulatory organisation or limits the ability of a party to file any claim in arbitration or limits the ability of the arbitrators to make any award. Pre-dispute arbitration agreements have a long history, primarily in commercial contracts. In the US, the Securities and Exchange Commission (SEC) has the power to regulate arbitration agreements in contracts between consumers and securities broker-dealers and investment advisers.

3.2 Simplified Arbitration

Unlike the US, Kuwait does not have a simplified arbitration procedure⁽³¹⁾. In the US, simplified arbitration applies to matters involving a claim for \$25,000.00 or less, excluding interest and expenses⁽³²⁾. The two most outstanding features of these proceedings are that a claim is heard by a single

(31) Rules 12800 of Code of Arbitration Procedure For Customer Disputes.

(32) Rule 601 relating Simplified Arbitration of NYSE Arbitration Rules.

arbitrator and it is finalised without the need for a hearing. In these cases, the dispute is submitted to a single public arbitrator who is knowledgeable in the securities industry. Such an arbitrator is selected by the director of arbitration. In general, these matters are heard without the need for a hearing, except where the arbitrator chooses to call such a hearing or the customer demands or consents to such a hearing⁽³³⁾. The arbitrator will consider the pleadings and the materials submitted by the parties and will submit his award after doing so.

It is submitted that the KSE should adopt a similar procedure to that of simplified arbitration in the US, as this will provide a diversified approach to the dispute resolution process for the securities exchange. It would provide protection for investors of small amounts and encourage such individuals to invest in the stock market.

3.3 Start of Arbitration

In the NYSE, the arbitration process starts when one of the parties declares a dispute arising out of a duly executed and enforceable written agreement. In terms of the rules of the exchange, there is a time limit for submitting any dispute, claim or controversy for it be eligible for submission to arbitration. This is within six years of the occurrence of the event giving rise to the act or the dispute, claim or controversy.³⁴ Should no claim be filed within six years of the event, the parties can no longer refer the matter to arbitration⁽³⁵⁾.

In the KSE, the Kuwait Capital Authority shall refer the dispute file to an arbitral tribunal within three business days from the day of its creation. The Authority shall notify the defendant of the arbitration application with provision of its documents and papers as well as the name of the arbitrator chosen by the applicant.

(33) *ibid*, Rule 601(f).

(34) Rule 603 of NYSE Arbitration Rules

(35) The Chief Regulatory Officer shall designate one of the officers or other employees of the Exchange as Director of Arbitration; Rule 635 of NYSE Arbitration Rules

4. Submission Agreement

The following documentation must be submitted to the director of arbitration: a duly executed submission agreement and a statement of claim together with documents in support of the claim. In addition, the required filing fee and hearing deposit fee must be paid before the hearing⁽³⁶⁾.

An agreement to arbitrate shall be considered valid unless there is no other evidence. According to FINRA, about 50% of all investor claims settle without a hearing. Cases that go to a hearing are won by investors approximately 50% of the time.

5. The Statement of Claim

The rules governing arbitration allow a claim to be filed within six years of the occurrence or event giving rise to the cause of action. In the KSE, arbitration applications shall be submitted in writing to the Authority including the following:

1. Arbitration applicant's name, capacity, nationality and address.
2. Defendant's name, capacity, nationality and address.
3. Subject of dispute, its incidents, documents, evidence, supporting documents and demands.
4. A copy of the Agreement to Arbitrate.
5. A copy of receipt of paying the due charges for the arbitration application⁽³⁷⁾.

6. Hearing Location

The advantage of arbitration is that the proceedings are not limited by specific legal processes as in traditional litigation. The time and place for the initial hearing shall be determined by the director of arbitration. The time and place for all subsequent hearings will be determined by the arbitrators⁽³⁸⁾.

(36) Rule 612 of NYSE Arbitration Rules.

(37) Article 12-3-1 (n 25).

(38) Rule 613 of NYSE Arbitration Rules.

In the KSE, the seat of arbitration is normally the premises of the arbitration authority. The authority or the arbitral tribunal may hold the arbitration hearings in any other place it deems appropriate⁽³⁹⁾. The chairman of the arbitral tribunal sets a hearing to consider the dispute and notifies the members of the arbitral tribunal and parties by certified mail or any method agreed upon by the parties to the arbitration.

7. Arbitrator Selection

When establishing a regulatory framework, one of the most serious problems is the shortage of suitably qualified staff such as specialist judges, lawyers and investigators. This is especially true of securities arbitration in that professionals need to be qualified in arbitration procedures as well as the rules and laws surrounding the securities exchange.

Parties are entitled to choose the arbitrator to preside over their matter. The NYSE maintains a database over 2,400 eligible arbitrators that parties can choose from. The number of arbitrators depends of the value of the claim. In selecting a three-arbitrator panel, the director of arbitration will provide the parties with three lists: a list of public arbitrators,⁽⁴⁰⁾ a list of non-public arbitrators and list of public arbitrators eligible to serve as the chairperson of the panel.

In the NYSE, the assigning of number of arbitrators is as follows:

- If the matter in question exceeds \$25,000, an arbitration panel which shall consist of no less than three (3) arbitrators is appointed.
- If the matter in question does not involve or disclose a monetary claim, the Director of Arbitration shall appoint an arbitration panel which shall consist of no less than three (3) arbitrators.

(39) Article 12 3-7 (n 25).

(40) A 'public' arbitrator is a person who is not affiliated with the securities industry.

The arbitrator will be deemed as being from the securities industry if he or she⁴¹ has substantial exposure to the securities industry either as a government securities dealer, or has been part of an organisation that is engaged in the securities business or is a professional, such as an attorney or accountant, who has worked in the securities industry. An arbitrator who is not from the securities industry shall be deemed a public arbitrator.⁴² In the National Association of Securities Dealers (NASD), securities arbitrations usually involve a panel of three decision makers or arbitrators.

In the KSE, each of the arbitration parties, even if many, may choose an arbitrator among those registered in the Arbitrators' Register in the Capital Market Authority, or among others, within seven working days from the date of being notified by the Authority. In the event that an arbitrator is recused, has resigned, been dismissed or their appointment is terminated, a replace-

(41) Rule 607 about Designation of Number of Arbitrators:

- (i) is a person associated with a member, allied member, member organization, broker/dealer, government securities broker, government securities dealer, municipal securities dealer, registered investment adviser, or other organization that is engaged in the securities business, or
- (ii) has been associated with any of the above within the past five (5) years, or
- (iii) is retired from or spent a substantial part of his or her business career in any of the above, or
- (iv) is an attorney, accountant or other professional who devoted twenty (20) percent or more of his or her professional work effort to securities industry clients within the last two (2) years, or
- (v) is an individual who is registered under the Commodity Exchange Act or is a member of a registered futures association or any commodity exchange or is associated with any such person(s)

(42) Rule 607 about Designation of Number of Arbitrators:

- (i) A person will not be classified as a public arbitrator if he or she has an immediate family member who is a person associated with a member, allied member, member organization, broker/dealer, government securities broker, government securities dealer, municipal securities dealer, registered investment adviser, or other organization that is engaged in the securities business.
- (ii) An immediate family member includes a person's spouse, parents, children, siblings, mothers and fathers-in-law, sons and daughters-in-law, and anyone (other than domestic employees) who shares such person's home.
- (iii) A person will not be classified as a public arbitrator who is associated with an entity that, directly or indirectly, controls, is controlled by, or is under common control with, a member, allied member, member organization, broker/dealer, government securities broker, government securities dealer, municipal securities dealer, registered investment adviser, or other organization that is engaged in the securities business.

ment shall be appointed in accordance with the same procedures followed in the original appointment⁽⁴³⁾. The arbitrator's fees are set by the Authority in accordance with the fees schedule approved by the Authority.

Furthermore, the arbitrator cannot resign after accepting the task unless there are serious reasons for doing so, as decided by the Authority based upon an application submitted by the arbitrator. Otherwise, the parties may resort to the courts for compensation. It is not permitted to dismiss the arbitrator without the approval of all the parties. The arbitrator must accept his appointment in writing, and must disclose to the Authority any circumstances or reasons that may raise doubts about his independence or neutrality. It is not permitted to disqualify the arbitrator unless there are serious doubts upon their neutrality or independency⁽⁴⁴⁾. An arbitrator is chosen from those who are more familiar with the security market's regulatory regime.

8. Pre-hearing Discovery

Prior to the hearing of the arbitration, both parties are required to make discovery of all documents in their possession relating to the claim before the arbitrator. The parties are entitled to reach a settlement agreement at any stage prior to the arbitration award being handed down.

In the NYSE, an investor generally receives a decision about their arbitration claim from the arbitration panel within thirty days of the arbitration proceedings.

9. Hearing Procedures

In the NYSE, the parties can waive the hearing of the matter and request that it be resolved solely upon the pleadings and documentary evidence. This needs to be requested in writing⁽⁴⁵⁾. All parties have the right to representation by counsel at any stage of the proceedings⁽⁴⁶⁾.

(43) Article 12-2-5 of Settling Disputes with Arbitration and Arbitration Rules.

(44) Article 12-2-4 of Settling Disputes with Arbitration and Arbitration Rules.

(45) Rule 602 of NYSE Arbitration Rules.

(46) *ibid*, Rule 614.

In the KSE, the arbitral tribunal must respect all the principles of litigation especially the right of defence, confrontation and judicial equality between parties. The language approved for the arbitration is the Arabic language. Parties to the arbitration may accept another language provided that they obtain the approval of all the members of the arbitral tribunal.

10. Rules of Evidence

The arbitrators shall determine the relevance of any evidence submitted and shall not be bound by rules governing the admissibility of evidence⁽⁴⁷⁾. The tribunal must decide on a dispute in accordance with the laws of the State of Kuwait unless the disputing parties agreed to apply another law, but in no circumstances so as to violate the rules relating to public order in Kuwait.

11. The Actual Hearings

In the US, matters are not always dealt with in an actual hearing. Simplified arbitration is a process for dealing with a dispute where the claim amount is less than \$25,000. In these situations, no hearing is necessary, which has the benefit of being a less costly alternative⁽⁴⁸⁾.

In the KSE, parties appear before the tribunal in person or are represented by an attorney or representative. The arbitration sessions are confidential⁽⁴⁹⁾. If the plaintiff or the defendant or both miss the hearings without a valid excuse, the arbitral tribunal may continue procedures up to the point of issuing its ruling. According to KSE rules, both disputing parties may authorise the arbitral tribunal to reconcile them if the tribunal members are appointed by name in the agreement to arbitrate. Moreover, at any stage, they may demand a record be made of what they agreed upon in reconciliation or settlement. The arbitral tribunal will issue its ruling accordingly.

12. The Award

According to rule 605 of the NYSE arbitration rules, the parties are entitled to settle the matter upon any grounds that they choose. All awards

(47) Rule 620 of NYSE Arbitration Rules.

(48) SEC (n 10)

(49) Article 12-3-14 (n 25).

must be in writing and signed by a majority of the arbitrators or in such manner as is required by law⁽⁵⁰⁾. Such awards may be entered as a judgment in any court of competent jurisdiction. All awards rendered pursuant to this code shall be deemed final and not subject to review or appeal.

In the KSE, before issuing a ruling, the arbitral tribunal meet to deliberate upon the ruling. Deliberation is confidential. An arbitration award must be issued in accordance with a majority opinion and is announced by the arbitral tribunal in open court. The announcement of an award shall state the reasons. Arbitration rulings are binding and final, and are executable only after obtaining a writ of execution in accordance with the legal procedures stipulated in chapter twelve of the Civil and Commercial Procedures Law.

13. Mediation

Mediation is the most popular ADR process. In mediation, an independent (neutral) third party is appointed by the parties to facilitate the mediation process and guide the situation towards a mutually acceptable voluntary agreement. The most important characteristics of mediation are as follows. Mediation is more formal than negotiation but less formal than arbitration or litigation. Unlike litigation, mediation is relatively inexpensive, fast and confidential. It does not follow a uniform set of rules. Exchange mediation is a voluntary process that takes place while an arbitration is pending or prior to its initiation⁽⁵¹⁾. Mediation has the benefit of being a confidential process. A mediator acts as a neutral, impartial facilitator of the resolution process and does not render a decision.

14. Conclusion

This article has compared the dispute resolution processes and institutions in the securities industry in the NYSE and KSE in order to improve the KSE dispute resolution process. It is impossible to provide an exhaustive comparison in just one article, but it is hoped that this article will add to the body of knowledge around securities industry protocols.

(50) Rule 627 of NYSE Arbitration Rules

(51) Rule 638 of NYSE Arbitration Rules.

The following recommendations are based on the information presented above:

- In Kuwait, there is no simplified arbitration process. Kuwait does not currently have a process similar to the NYSE of simplified arbitration. This would be a useful addition to the KSE.
- In Kuwait, the introduction of a pre-dispute arbitration clause is recommended, similar to those used in the NYSE. These would be inserted into contracts with securities firms to ensure that disputes are referred directly to arbitration by a body connected to the securities market.
- In the US, the FINRA manages the largest securities arbitration forum. A body with a similar mandate should be established in Kuwait.
- There is currently no mediation rule in Kuwait, hence there is no provision for mediation prior to the arbitration proceedings. The KSE should make provision for such a process to be established, especially where the parties wish to limit the costs of the proceedings similar to the NYSE.
- More research is needed in different areas of securities arbitration. One of the recommendations for future research regarding securities arbitration law in Kuwait is to consider the following question: what is the impact of the class action lawsuit on arbitration in financial markets?

At present, there are problems with the application of the current law relating to securities arbitration. The main reason for this is the Kuwaiti legislature has made provision for specific laws and rules that differentiate between arbitration and securities arbitration but they don't take into account the nature of securities which made it impractical. For this reason, it is recommended that the legislation be amended to provide specific rules relating to Securities Arbitration that provide for the special nature of Securities Arbitration, and in particular, that these rules be based on the corresponding rules in the NYSE that were developed over time.

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التحكيم في سوق الكويت للأوراق المالية

دراسة مقارنة

الدكتور/عبدالله الشبلي

أستاذ مساعد - أكاديمية سعد العبدالله للعلوم الأمنية

دولة الكويت

ملخص :

في عام ٢٠١٤ صدرت لائحة خاصة تتعلق بالتحكيم في سوق الأوراق المالية، إلا أنه حتى وقتنا الحالي لم يتم عرض أي أشكالية للتحكيم. مما يجعلنا نطرح تساؤلات عدة حول أسباب عدم اللجوء لنظام التحكيم حتى الآن.

يتناول هذا البحث واحدة من أهم القضايا المتعلقة بسوق الأوراق المالية في الكويت، وهذه القضية هي نظام التحكيم، وي طرح البحث عدداً من الأسئلة. من أهمها، ما هي الأسباب التي تجعل نظام التحكيم في الكويت غير قابل للتطبيق؟ وما هي الوسائل التي تعمل على تطوير نظام التحكيم في الكويت؟

ومن خلال مناقشة نظام التحكيم في سوق الكويت للأوراق المالية، يقوم هذا البحث عن طريق التحليل القانوني بمقارنة بين نظام التحكيم في بورصة نيويورك ونظام التحكيم الموجد في سوق الكويت للأوراق المالية .

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