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Setting aside or non-enforcement of arbitral awards in international arbitration on the public policy ground and for breach of natural justice

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As a general proposition it may be said that the Courts will not interfere with the merits of an arbitral award in international commercial arbitration ("ICA") and at least in ‘Model Law’ countries there is no right of appeal. An award will only be liable to be set aside, or refused recognition or enforcement, if the arbitral process is subject to some serious procedural irregularity (and in a limited range of other circumstances).

The grounds which may justify interference are contained in Articles 34 and 36 of the Model Law (UNCITRAL Model Law on International Commercial Arbitration). These grounds are similar and are derived from Art. V(1)(a)-(e) and V(2)(a) and (b) of the New York Convention (NYC).
The grounds upon which an award in ICA may be set aside or denied enforcement or recognition in ‘Model Law’ countries are as follows:

- A party to the arbitration agreement was under some incapacity (Art V(1)(a) and Arts 34(2)(a)(i) and 36(1)(a)(i) of the Model Law).
- The arbitration agreement is not valid under the law applicable to the parties (Art V(1)(a), and Arts 34(2)(a)(i) and 36(1)(a)(i)).
- The objecting party was not given proper notice of the arbitration or was otherwise unable to present its case (Art V(1)(b) and Arts 18, 34(2)(a)(ii) and 36(1)(a)(ii)).
- The award deals with a difference not contemplated by… the submission to arbitration or contains a decision on a matter beyond the scope of the submission to arbitration (Art V(1)(c), and Arts 34(2)(a)(iii) and 36(1)(a)(iii)).
- The composition of the arbitral authority or the arbitral procedure was not in accordance with arbitration agreement or applicable law (Art V(1)(d), s 8(5)(e), and Arts 34(2)(a)(iv) and 36(1)(a)(iv)).
- The award has not yet become binding”, “set aside” or “suspended” (Art V(1)(e), Art 36(1)(a)(v)).
Introduction – setting aside or non-enforcement/recognition of an ICA award

- A court may ALSO set aside, or refuse recognition or enforcement, of an ICA award, if it finds that:
  (a) the subject-matter of the dispute is not capable of settlement by arbitration under the law of that State; or
  (b) the award is in conflict with the public policy of that State.

  Art 34(2)(b)(ii), Art 36(1)(b) of the Model Law; Art V(2)(a) and (b) NYC

- See, s. 37(1)(b)(ii) Arbitration Act 2005 (Malaysia); International Arbitration Act (Cap. 143A) (Singapore); s. 8(7) IAA; cf. ss. 40 – 45 Arbitration Act B.E. 2545 2002 (Thailand); Art 66 of the Arbitration Law 1999 (Indonesia)

- An important feature of public policy is procedural fairness, see Art 18 of the Model Law.

- It has been suggested that the public policy exception is really superfluous given the fundamental procedural fairness ground under Art V(1)(b) and Arts 18, 34(2)(a)(ii) and 36(1)(a)(ii) of the Model Law (Berrman, p70)
Awards may be contrary to public policy at least in Malaysia, Singapore and Australia where there is illegality, or where there has been a breach of natural justice, or fraud or corruption on the part of the arbitral tribunal.

Section 37(2) of the Arbitration Act 2005 provides two circumstances where an award will be in conflict with the public policy of Malaysia:

“Without limiting the generality of subparagraph (1)(b)(ii), an award is in conflict with the public policy of Malaysia where –

(a) the making of the award was induced or affected by fraud or corruption; or

(b) a breach of the rules of natural justice occurred:

i. during the arbitral proceedings; or

ii. in connection with the making of the award.”

See also: ss. 8(7A), 19 IAA; s. 24 International Arbitration Act 1994 (Singapore); s. 103(3) Arbitration Act 1996 (UK); ss. 81(2)(b)(ii), 86(2)(b), 89(3)(b), 95(3)(b), 98D(3)(b) Arbitration Ordinance (HK) cf. s. 40(2)(b) cf. Arbitration Act B.E. 2545 2002 (Thailand); Arbitration Law 1999, Indonesia (“public order” no definition); see also Law on Commercial Arbitration 2010 (Vietnam), Art 68; Philippine Arbitration Law
The "contrary to public policy" ground

- The "contrary to public policy" ground then is derived from the NYC, Art V(2)(b)

- In civil law jurisdictions an award will only be set aside on this ground if it is contrary to “truly transnational” public policy. For example, in France traditionally ICA awards could only be rejected on the grounds of public policy or ordre public if there was shown to be a contravention of international public policy: NCCP Article 15002 Societe Impex v Societe PAZ, Judgment of May 18, 1971, Cour de Cassation, [1972] DS Jur 37.

- International public policy is defined as a violation of really fundamental conceptions of legal order in the country concerned; or norms that embody and reflect fundamental notions of morality and justice (Bermann, p. 71)

- The concept is described by Bokhary PJ and Sir Anthony Mason NPJ in Hebei Import & Export Corp v Polytek Engineering Co Ltd [1999] 2 HKC 205; 215-216; 232-233 in similar terms.
The "contrary to public policy" ground

While the public policy ground is narrowly construed, there have been rare examples of the ground being successfully invoked, for example:

- An English court refused to enforce an award which gave effect to a contract between a father and a son that involved exporting carpets from Iran in breach of Iranian revenue laws and export controls and an illegal contract: *Soleimany v S* [1999] QB 785; [1999] 3 All ER 847

- A court in Argentina refused to enforce an award that imposed on the party costs that greatly exceeded the value of the award itself: *Odgen Entertainment Services Inc*, cited in Berrmann at p. 73.

- A Canadian court refused to enforce a foreign award as the award gave the party a double recovery: *Subway Franchise Systems v Laitch*, 2011 SKQB 249 cited in Berrmann, ibid.
TCL v Castel – Australian position

- The law in relation to setting aside or non-enforcement of an arbitral award on the public policy ground and for breach of the principles of natural justice has recently been clarified in so far as Australia is concerned by the decision of the Full Federal Court in:

- *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 311 ALR 387; [2014] FCAFC 83
  (respectively “TCL” and “Castel”).
TCL v Castel Electronics – Australian position

- **Background facts:**
  - Castel was an Australian electrical goods distribution company.
  - TCL was a Chinese manufacturer of air conditioning units which had granted Castel exclusive right to sell TCL air conditioners in Australia.
  - Castel claimed that TCL had breached their agreement by, inter alia, manufacturing and supplying air conditioners to other Australian distributors which were not branded “TCL”, to be sold in competition to those distributed by Castel.
The dispute between the parties was referred to arbitration in Melbourne pursuant to an arbitration clause in the distribution agreement referring disputes to arbitration in Australia.

Following the hearing, the tribunal made an award in favour of Castel requiring TCL to pay it $2,874,870, and subsequently a costs award of $732,500.

TCL failed to pay the awards (referred to hereafter as “the award”).
TCL v Castel Electronics – Australian position

- Castel made application in the Federal Court under the *International Arbitration Act 1974* (Cth) (“IAA”) (Australia’s Arbitration Law or *lex arbitri*) to enforce the award which TCL opposed on the grounds that:
  - the application was defective and the Court had no jurisdiction to enforce the award; or
  - if there was jurisdiction, the award should be set aside or not enforced as being contrary to public policy because of a breach of the rules of natural justice in the arbitral hearing.
At first instance the Federal Court in *Castel Electronics Pty Ltd v TCL Air Conditioner (Zhongshan) Co Ltd* [2012] FCA 21; 287 ALR 297 dealing with the issue whether the court had jurisdiction to enforce the award, concluded that it did.

TCL then applied to the High Court to prohibit the Federal Court from hearing the matter on the grounds of lack of jurisdiction and constitutional invalidity of the conferral of jurisdiction on the Court under Art 35 of the Model Law. The High Court dismissed the application in *TCL Air Conditioner (Zhongshan) Co Ltd v The Judges of the Federal Court of Australia* [2013] HCA 5; 295 ALR 596.

Subsequently in *Castel Electronics Pty Ltd v TCL Air Conditioner (Zhongshan) Co Ltd (No 2)* [2012] FCA 1214 the Federal Court made orders enforcing the award and dismissing TCL’s application to set it aside in the face of lengthy complaints by TCL about the arbitral tribunal’s findings of fact. TCL again appealed.
The Full Federal Court dismissed the appeal and held that the trial judge was correct in ordering the enforcement of the award against TCL largely endorsing his approach. In so doing the court illuminated the power to set aside, or not to enforce, an award as contrary to the public policy of Australia, and specifically for breach of natural justice under Arts 34 and 36 of the Model Law.

It was held that an award made in ICA will not be set aside, or denied recognition, or enforcement, by reference to the principles of natural justice, under Arts 34 and 36 of the Model Law and s. 8 (7A) IAA unless there exists real unfairness or real practical injustice in the conduct of the arbitration, or making of the award (at [111]).
The presence of “real prejudice” is likely to be part of the evaluation which should be able to be established without a detailed re-examination of the facts.

In the context of ICA, a challenge to an arbitral award on the “no probative evidence” ground will only be successful if real unfairness or practical injustice is suffered.

In reaching its conclusion the court was informed by the statutory context, the interpretation of the critical international instruments both internationally and in Australia, the concept of “public policy”, the principles of natural justice, and relevant international, and particularly regional, jurisprudence.
The court emphasised that in interpreting the IAA it was important to establish and maintain, in so far as its language permits, a degree of harmony and concordance of approach to ICA, by reference to the jurisprudence of common law countries in the region which is part of the growing harmonized law of international commerce.

After examining these sources the court concluded that the meaning of “public policy” in Art V of the NYC and Arts 34 and 36 of the Model Law and in turn ss. 8(7A) and 19 IAA was limited to the fundamental principles of justice and morality of the State acknowledging the international context.
While at common law it is an error of law to make a finding of fact where there is no probative evidence, in ICA, a wrong finding of fact resulting from an absence of probative evidence may, but does not necessarily without more, amount to a breach of natural justice.

In the context of ICA the *no probative evidence* ground will only form the basis of a successful review or refusal to enforce an award *if real unfairness or real practical justice* was suffered.

The party representatives would need to ensure that this be “expressed shortly” and “demonstrated tolerably shortly”.
TCL v Castel Electronics – Australian position

Conclusion

- The court’s approach in this case was to examine the relevant provisions of the IAA, the concept of “public policy” and the relevant principles of natural justice, in the context of the history and interpretation of the critical international instruments both internationally and in Australia.

- The examination is to take place in light of international and regional case law. This approach emphasises the international nature of ICA, as well as the development of an “internationally recognised harmonised procedural jurisprudence”.

- There are significant parallels to the approach taken in Australia to that adopted in other countries in Asia.
Contrary to public policy ground – comparative analysis - Malaysia

Malaysia

- In Malaysia in order to set aside an award it would need to be established that there was a “conflict with the public policy of Malaysia in the narrow sense of something offending basic notions of morality and justice or something clearly injurious to the public good in Malaysia”: Majlis Amanah Rakyat v Kausar Corporation Sdn Bhd [2009] 1 LNS 1766

- The High Court favoured an approach for Malaysian Courts based on “comparative jurisprudence in the interests of maintaining comity of nations and a uniform approach to the model law, so far as that is possible, to the concept of “public policy” in relation to foreign awards”

- See also, Open Type Joint Stock Company Efirnoye v Alfa Trading Ltd [2012] 1CLJ 323, HC
In Singapore courts the public policy exception will be construed narrowly: *AJU v AJT* [2011] SGCA 41. An award will only be refused enforcement if it would ‘shock the conscience’ or ‘violate the forums most basic notions of morality: *PT Asuransi Jasa Indonesia (Persero) v Dexia Bank SA* [2007] 1 SLR (R) 597. See also, *AJU v AJT* [2011] SGCA 41; *AQU v AQV*[2015] SGHC 26; *AKN v ALC* [2015] SGCA 18.

When faced with such an objection the court must assess the real nature of the complaint: *AKN v ALC* [2015] SGCA 18. [38]. To successfully set aside an arbitral award for breach of natural justice, it must be established: (a) which rule of natural justice was breached; (b) how it was breached; (c) in what way the breach was connected to the making of the award; and (d) how the breach prejudiced its right: *John Holland P/L v Tokyo Engineering Corp (Japan)* [2001] 1 SLR (R) 443 at [18] affd in *Soh Beng Tee & Co Pte Ltd v Fairmount Development Pte Ltd* [2007] 3 SLR (R) 86 at [29].

The breach must have necessarily made a difference to the outcome: *LW Infrastructure Pte Ltd v Lim Chin San Contractors Pte Ltd* [2013] 1 SLR 125 and culminated in actual prejudice to a party (*Soh Beng Tee* at [98]).
Contrary to public policy ground – Hong Kong

Hong Kong:

In *Hebei Import & Export Corp v Polytek Engineering Company Ltd* (1999) 2 HKCFAR 111, [1999] 1 HKLRD 665; *Hebei Import & Export Corp v Polytek Engineering Co Ltd* [1999] 2 HKC 205; it was held that "contrary to the public policy of that country" means "contrary to the fundamental conceptions of morality and justice" of the forum (see Sir Anthony Mason at 232- 233).

Another application of this ground in Hong Kong is the well known case of *Gao Haiyan and anor v Keeneye Holdings Ltd and anor* [2011] HKCA 459; [2012] 1 HKLRD 627; [2012] 1 HKC 335; CACV 79/2011. The unsuccessful party in an arbitration in the PRC appealed against the award on the basis that there had been favouritism and malpractice by the tribunal. In particular the tribunal was criticised for holding a private mediation session over dinner at a 5 star hotel.
Contrary to public policy ground – Japan

Japan:

- The public policy exception in Art 45(2) refers to a conflict between the arbitral award and the public policy and good morals of Japan.
- Japanese courts have narrowly interpreted ‘public policy’ in light of the purposes of the Arbitration Law, and according to one source have always rejected it, but there appear to be isolated examples.
Contrary to public policy ground – India

India:

- Narrowing the public policy exception in *Shri Lal Mahal Ltd. -v- Progeto Grano Spa Civil Appeal* (2014) 2 SCC 433, [48] the Supreme Court held that the broad interpretation of "public policy" used for setting aside a domestic arbitration award will not be applied to enforcement of an ICA award in India. Enforcement of an ICA award could only be opposed on grounds of "public policy" when the award is contrary to: the fundamental policy of Indian law; the interests of India; or justice and morality.
Contrary to public policy ground – China

China

- While the “public policy” exception is not expressly included as one of the grounds in Art 260 of the Civil Procedure Law of the PRC, if the people’s court determines that the enforcement of the award goes against the social and public interest of the country it will not allow enforcement.

- There is evidently an increasing reluctance on the part of the courts in the PRC to invoke “public policy” type grounds to interfere with the enforcement of awards.
The Korean Supreme Court has likewise adopted a narrow interpretation of “public policy”. The Supreme Court has stated that the public policy exception was intended to protect only the most fundamental moral beliefs and social order in the enforcing country.

In applying NYC Art V(2)(b), the Supreme Court has ruled that “recognition or enforcement may be refused on public policy grounds only if the consequences would be against the good moral and social order of the country.”

The existence of fraud in the arbitration would be valid grounds to refuse enforcement under Article V(2)(b)

Korean Supreme Court, 2006Da20290, Decided on 2009. 5. 28.
Conclusion

- It is suggested that when a national court is seeking to construe the concept of “public policy” in a particular case, an approach of examining:
  - the relevant provisions of its own ‘lex arbitri’; and
  - the concept of “public policy”, and the relevant principles of natural justice in the context of:
    - the history and interpretation of the critical international instruments - both internationally and locally - in light of international and especially regional case law -
    - is in accord with international, and in particular, Asian practice.
- It is suggested that ICA awards will not be set aside or refused recognition or enforcement on the public policy ground, at least where a breach of natural justice is asserted unless there is real prejudice to the party or parties and the breach has made a real difference to the result\(^1\).
To reiterate and paraphrase the Malaysian High Court, an approach by courts which emphasises *comparative jurisprudence* will assist in maintaining:

- a uniform approach to:
  - the interpretation of the Model Law; and
  - the concept of “public policy” in ICA; and
- the comity of nations
Thank you

Notes:

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