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Précis Paper

Challenges to International Arbitral Awards

Edward Cox and Ian Benson consider the Australian regime for challenging international arbitral awards at the seat of the arbitration, and two recent Federal Court of Australia decisions dealing with important questions regarding the scope for appeals, procedural fairness and costs.

Discussion Includes

- Appointments of arbitrators under the *UNCITRAL Model Rules*
- Test for determining bias or impartiality on the part of arbitrators
- Procedure for challenging arbitral awards
- Jurisdiction challenges to arbitral awards
- Procedural fairness in arbitrations
- Role of a party's conduct in contributing to denial of procedural fairness under Art 18 of the UNCITRAL Model Rules
- Costs in challenges from arbitral awards: The Australian and international positions

Précis Paper

Challenges to International Arbitral Awards

1. In this edition of BenchTV, Edward Cox (Barrister – Greenway Chambers, Sydney) and Ian Benson (Solicitor – AR Conolly & Company) discuss international arbitration and a recent application to set aside an arbitral award that was heard by the Federal Court of Australia in *Sino Dragon Trading Ltd v Noble Resources International Pte Ltd* [2016] FCA 1131 and *Sino Dragon Trading Ltd v Noble Resources International Pte Ltd (No 2)* [2016] FCA 1169.

Background to the Original Dispute

2. The original dispute in this case arose out of a shipment of iron ore from Australia to China. Contrary to the contract of sale, Sino Dragon (the purchaser) failed to put in place a letter of credit sufficient to cover the shipment value by the time contractually required. An employee of Sino Dragon subsequently indicated by email that the company was not going to be able to perform the contract, and that Noble Resources (the seller) should take steps to deal with the cargo.

3. On receipt of the email, Noble Resources explained that it had accepted Sino Dragon's repudiation of the contract, and gave notice terminating the contract with immediate effect. The cargo was sold to another purchaser in China on a falling market with a substantial loss in value. Noble Resources asserted that because of the alleged breaches of contract, Noble Resources had to find an alternative buyer for the iron ore cargo originally destined for Sino Dragon, and that it had suffered loss and damage caused by those breaches.

The Circumstances of the Arbitration

4. The issues in this case related to the conduct of the arbitration, which took place in Australia, and specifically the appointment of the arbitrators and practical difficulties that arose in the course of the arbitration.

5. The dispute commenced in the usual way, with the party commencing the dispute (Noble Resources) nominating an arbitrator. Pursuant to the *UNCITRAL Arbitration Rules*, Sino Dragon then had 30 days to nominate their arbitrator, however failed to do this within time. As a result, and in accordance with the *UNCITRAL Model Law on International Commercial Arbitration* (as adopted by the United Nations Commission on International Trade Law on 21 June 1985, and as amended by the United Nations Commission on International Trade Law on 7 July 2006), steps were taken for the Permanent Court of Arbitration to designate an appointing authority. A New Zealand barrister was appointed to nominate an arbitrator, in

lieu of the respondent, and a solicitor in Sydney, Mr Bonnell from King & Wood Mallesons, was appointed.

6. It became apparent that King & Wood Mallesons in China was acting for a related Noble entity. Sino Dragon ultimately took an objection based on apprehended bias of the appointed arbitrator, Mr Bonnell. This issue became the genesis of the procedural problems that continued until the ultimate application to set aside the award that was recently heard by Beach J in the Federal Court of Australia.

Impartiality of the Appointed Arbitrator

7. Sino Dragon sought to challenge the appointment of Mr Bonnell as arbitrator on a number of different occasions, including before the arbitrators, the appointing authority, and at an initial application before the Federal Court in 2015 (*Sino Dragon Trading Ltd v Noble Resources International Pte Ltd* [2015] FCA 1028). The basis for the application was that because King & Wood Mallesons China, a related legal practice of King & Wood Mallesons Australia, which used the same name but was not in the same technical partnership, was acting for a related party, Mr Bonnell could not act impartially.

8. Unlike in the domestic Australian context, the test that applies in determining impartiality of international arbitrators is not the "reasonable, fair-minded observer" test set out by the High Court in *Ebner v Official Trustee in Bankruptcy* [2000] HCA 63; 205 CLR 337. Instead, the relevant test can be found in the English authority of *R v Gough* [1993] UKHL 1, which is directly enshrined in Australian law by s 18A, *International Arbitration Act 1974* (Cth) and requires consideration of whether there is a real danger of bias. Section 18A states:

> **Article 12**
> ***Justifiable doubts as to the impartiality or independence of an arbitrator***
> *(1) For the purposes of Article 12(1) of the Model Law, there are justifiable doubts as to the impartiality or independence of a person approached in connection with a possible appointment as arbitrator only if there is a real danger of bias on the part of that person in conducting the arbitration.*
> *(2) For the purposes of Article 12(2) of the Model Law, there are justifiable doubts as to the impartiality or independence of an arbitrator only if there is a real danger of bias on the part of the arbitrator in conducting the arbitration.*

9. This is a significantly higher threshold for determining whether an arbitrator has an interest in the outcome of the arbitration than the Australian common law test. Ultimately, the Court found that the mere fact that a related law practice which did not have a direct financial

relationship was representing a related party could not give rise to apprehended bias under either test.

Procedure for Challenging Arbitral Awards

10. In this case, there was no choice as to location of the arbitration, unless the parties had agreed to vary their original agreement. The original contract contained a clause specifying the seat of any arbitration as Western Australia. If court proceedings had been commenced in any other jurisdiction or arbitration commenced anywhere else, there would have been a mandatory stay in those proceedings.
11. The Federal Court of Australia is designated as the only place in Australia where challenges to the award at the seat can be made.

12. Where, as here, steps have been taken to register an arbitral award in a foreign jurisdiction, questions arise as to whether the award can be set aside and an anti-suit injunction can be granted to restrain enforcement of the award overseas. Ultimately in this case, the Federal Court was able to hear the challenge on an expedited basis so there was no need to determine this question.

13. If a challenge to an arbitral award is brought at the place of enforcement, the court can consider requiring security. This does not arise in the same way where a challenge is brought at the seat under art 34 of the *UNCITRAL Model Law on International Commercial Arbitration*. Where a challenge is brought at the seat, security will not automatically follow, however it will still be a discretionary issue for the court to consider where an injunction is sought.

The *International Arbitration Act 1974* (Cth)

14. The *International Arbitration Act* has brought into Australian law two pieces of international law that regulate international arbitrations:
    - *Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958* ("*New York Arbitration Convention*"), which provides for recognition and enforcement of arbitral awards; and
    - *UNCITRAL Model Law on International Commercial Arbitration* and *UNCITRAL Arbitration Rules.*

15. The *International Arbitration Act* gives the force of law to these pieces of international law with respect to all arbitrations conducted in Australia or arbitrations conducted overseas which are being enforced in Australia.

Jurisdictional Issues

16. The appeal grounds contained in the *International Arbitration Act* are very limited, and do not provide for appeals on the basis of an error of law or factual merits review. The narrow grounds of review provided for are limited to issues such as an absence of notice of the arbitration, denial of procedural fairness, or whether arbitrators have determined issues beyond the referral to arbitration.

17. The rationale for having only narrow grounds of appeal is that because commercial arbitration is agreed to by the parties, and the parties are sophisticated commercial parties who have agreed to a particular procedure, courts should be reticent to interfere in commercial arbitration. Courts have consistently said that they will start from the proposition that awards should be seen as final and binding, and there should only be limited scope of grounds of review.

18. The first challenge as to jurisdiction dealt with by the Federal Court was whether the arbitrators in this case had determined issues beyond their referral. The contract between Sino Dragon and Noble Resources provided that all written communications under the contract were to occur in English. The question before the arbitrators concerned the repudiating email, which had been sent in Chinese. The arbitrators determined that that communication was not a formal contractual notice and therefore it did not matter that it was in Chinese.

19. The question before the Federal Court was whether this same question about contractual interpretation could be advanced on appeal as a jurisdictional question. Sino Dragon argued that because a Chinese language communication was not permitted under the contract, any determination of the question by the arbitrators was beyond jurisdiction.

20. The Federal Court rejected this argument and held that this argument was, in essence, a disguised attack on the merits.

Procedural Fairness Considerations

21. In the challenge to the arbitral award, Beach J considered art 18 of the *UNCITRAL Model Law,* which applies where there is said to be unequal treatment or the absence of a full opportunity to present a party's case. Article 18 has been clarified in Australia by the insertion of s 18C of the *International Arbitration Act*, which provides:

> **Article 18**
> ***Reasonable opportunity to present case***

For the purposes of Article 18 of the Model Law, a party to arbitral proceedings is taken to have been given a full opportunity to present the party's case if the party is given a reasonable opportunity to present the party's case.

22. This section makes clear that what is required is the loss of a reasonable opportunity to present a party's case. In the recent case of *TCL Air Conditioner (Zhongshan) Company Ltd v Castel Electronics Pty Ltd* [2014] FCAFC 83; 232 FCR 361, the Court concluded that to establish a denial of procedural fairness contrary to the public policy of the forum, a party must establish real unfairness or real practical injustice. A minor breach of the rules of procedural fairness is not sufficient to set aside an arbitral award at the seat under Australian law. This forms part of the Court's consistent approach of judicial restraint in interfering with the arbitral process, to ensure that the consistency and finality of international arbitration is maintained.

23. In this case, the factual matrix surrounding the denial of procedural fairness was unusual. Shortly before the arbitration, Sino Dragon indicated that it could not bring key witnesses to Australia and proposed to call evidence by videolink. The witnesses were critical to the issues in the case, including credibility. Although Noble Resources did not consent to the videolink, the arbitrators indicated that evidence could be called by videolink however it was Sino Dragon's responsibility to make the appropriate arrangements.

24. During the hearing, there were multiple technological issues, such that evidence was taken via an image on the screen over the equivalent of Skype, but with the oral evidence being played via a mobile phone. In addition, the interpreter who had been arranged did not have satisfactory level of Chinese to communicate the questions to the witnesses. A paralegal from the firm acting for the respondents ultimately acted as an interpreter. The hearing proceeded in this way until its conclusion.

25. On appeal before the Federal Court, Sino Dragon argued that it had not had proper opportunity to present its case because the videolink facilities were deficient and the witnesses could not be understood. A particular error in translation was also identified, which had been relied upon by the arbitrators in their decision relating to repudiation and waiver.

26. Unlike procedural fairness at common law, the requirement for equal treatment under art 18, *UNICTRAL Model Law* cannot be waived and has been described as non-derogable. The question then arose as to how the Court would deal with a party's role in contributing to a denial of procedural fairness.

27. Justice Beach first considered the question from the perspective of the arbitrators. The arbitrators had said that the evidence had been difficult and unsatisfactory, and they had therefore assessed the witnesses' evidence and credibility in the context of the difficult technical arrangement.

28. In considering whether there had been "real practical injustice", Beach J looked at what role a party's own conduct has in creating an equal and fair hearing or a denial of procedural fairness. Beach J held that there was a range of opportunities when Sino Dragon could have stopped the denial of procedural fairness. Specifically, they could have arranged better quality videolink facilities or sought an adjournment to have witnesses travel to Australia. Moreover, Sino Dragon's legal representatives at the arbitration, who were aware of the difficulties that had arisen, did not make any submissions to the arbitrators in this regard, but essentially made a forensic decision to leave the evidence as it had been presented. Justice Beach determined that art 18 is not intended to protect forensic decisions made by a party or to protect denials of fairness within that party's control.

29. Furthermore, in relation to the translation difficulties, Beach J found that translation is not an exact science, and that minor differences in nuance will not provide a basis for a procedural fairness challenge to the award. The only scenario in which this could form a basis for a finding of denial of procedural fairness is where it can be shown that there was a substantial error that was causative of the particular outcome.

30. For these reasons, Beach J did not uphold the denial of procedural fairness argument.

Costs in Challenges from Arbitral Awards: The Australian and International Positions

31. The question of costs in challenges from arbitral awards remains one of international controversy.

32. The position in Hong Kong and the United Kingdom, following the decisions of *A v R* [2009] HKCFI 342 and *A v B (No 2)* [2007] 1 Lloyd's Rep 358, is that there is a presumption in favour of indemnity costs in challenges to arbitral awards, unless exceptional circumstances exist. This reverses the onus that would ordinarily apply in the Australian context, and reflects the nature of international commercial arbitration as final, where challenges are meant to be rare.

33. This position has not been universally adopted in Australia, and has specifically been disavowed in a number of Australian authorities. The Victorian Court of Appeal, in *IMC Aviation Solutions Pty Ltd v Altain Khuder LLC* [2011] VSCA 248; 38 VR 303, indicated that there would be no reason to depart from the ordinary Australian position as to indemnity

costs. The contrary argument, that was alluded to by Allsop CJ in *Ye v Zeng (No 5)* [2016] FCA 850, is that the structure of international arbitration and the creation of a regime where awards are treated as final provides a sufficient indication of a departure from the ordinary common law position as to costs, however the question has not been determined by the Full Federal Court.

34. In *Sino Dragon Trading Ltd v Noble Resources International Pte Ltd (No 2)* [2016] FCA 1169, Beach J awarded indemnity costs on a different basis, and indicated that he did not think that there ought to be a special rule. Indemnity costs were awarded for two-thirds of the proceedings and party-party costs for one-third.

35. The question of whether Australia will move in line with the Hong Kong and English positions remains an open question.

BIOGRAPHY

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Edward Cox was called to the NSW Bar in 2000. Edward's practice includes general commercial and equity, admiralty and maritime, corporations, insolvency, probate litigation and criminal law. Edward has also appeared in and advised on commercial and sports arbitrations in Australia and Singapore, and has been appointed as an arbitrator in relation to sports disciplinary and maritime matters.

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