International Arbitration

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# INTERNATIONAL ARBITRATION QUARTERLY

## Which arbitrator to choose?

Arbitration is a creature of contract and party choice; one of the significant advantages of this is that it offers parties the ability to choose a tribunal to determine their dispute. This article will consider some of the issues a party should take into account when choosing an arbitrator and the extent to which institutional rules and law restrict that choice.

As a first step, consideration should be given to whether the parties themselves should voluntarily fetter their choice by specifying requirements for qualification as an arbitrator in the arbitration agreement. For example, if the arbitration agreement relates to a construction contract, should the matter be decided by engineers experienced in the construction industry? It is common in trade arbitrations for the agreement to restrict the parties' choice of arbitrator by requiring that they be experienced in the relevant trade. However this is not so common in international commercial arbitration, where parties frequently have an unfettered, free choice.

The practice of having party appointed arbitrators is reflected in most institutional arbitration rules, although most require that arbitrators are "nominated" by the parties, and then formally appointed by the institution itself. For example, Article 5.5 of the LCIA rules states that *"The LCIA Court is alone empowered to appoint arbitrators"*. The reason for this is to ensure compliance with a general obligation of law, enshrined in Article 11 of the UNICTRAL Model law, that arbitrators be impartial. Impartiality is a key requirement for an arbitrator which is not only contained in institutional rules but also in most national arbitration legislation (for example the obligation for a dispute to be decided by an impartial tribunal is found at Section 2 of the English Arbitration Act 1996 (the Act)).

In order to ensure that this requirement is met, most arbitral institutions provide that arbitrators must submit a statement of independence and impartiality on nomination and before appointment. This statement contains a section for the nominated arbitrator to declare any

issue which might impact on his or her independence and impartiality. The general current practice is for arbitrators to adopt a cautious approach when completing these statements and if in doubt, to make a declaration.

What does "independent and impartial' mean? This is not always straightforward, since the legal system of each seat of arbitration will interpret it in a different way. In England, Section 24 of the Act states that a party can apply to remove an arbitrator on the ground that *"circumstances exist that give rise to justifiable doubts as to his impartiality"*. English case law has established that it is sufficient for the removal of an arbitrator under this section to show that *"...the fair minded and informed observer, having considered the facts, would conclude that there was a real possibility that the tribunal [would be] biased"* (*Porter v Magill [2002] AC 357*). This is an objective test, and it is sufficient to show that there is a real possibility that an arbitrator would be unconsciously biased in order to mount a successful challenge to their appointment.

In an attempt to provide some clarity and uniformity across different jurisdictions, the IBA published the *"IBA Guidelines on Conflicts of Interest in International Arbitration"* in 2004. Whilst this document is not binding, it attempts to bring case law together in one place and to provide practical examples of what is a conflict, what might be a conflict, and what is not a conflict using a "traffic light" list. The red list is split into two categories: non waivable (for example where an arbitrator has a significant financial interest in one of the parties) and waivable (for example where at the time of the appointment, the arbitrator represents one of the parties in a legal capacity). There is then an orange list (setting out issues which the arbitrator should disclose) and a green list (setting out issues where no conflict of interest arises from an objective standpoint).

A further purpose for publishing the list was to reduce the number of unmeritorious challenges to the nomination of an arbitrator by providing clear guidance to the international arbitration community. Despite this intention, there is a regrettable increasing tendency for nominated arbitrators to be challenged by the non-appointing party to an arbitration, either for the reasons disclosed in the statement of independence and impartiality by the appointee, or because of some reason known to the party contesting the appointment. These challenges can be for a legitimate reason; however they can also be tactical. Challenging an arbitrator's appointment might be a way for a reluctant respondent to delay the progress of the arbitration, or to put pressure on the opponent's arbitrator even where a debatable challenge is unsuccessful.

In order to minimise the opportunity for an opponent to mount a challenge, it is important when choosing an arbitrator to ensure insofar as is possible that he or she is independent and impartial.

Apart from the legal requirements and guidelines, there are other factors to consider for a Claimant and a Respondent when choosing an arbitrator. For the Claimant, a key issue is to consider who will be appropriate to handle the nature of the particular dispute. Are there specific issues which will require the arbitrator to have specialist knowledge or experience? Is the case one which is strong on the legal merits, or commercially? From a practical perspective, does the proposed appointee have sufficient time available to ensure the arbitration is conducted within a reasonable time frame? A more difficult question for the Claimant is to consider the dynamics of the Tribunal and whether the appointed arbitrator will have sufficient gravitas to ensure their views carry weight when the Tribunal comes to make its decision on the merits of the dispute. This will require consideration of the candidate likely to be appointed by the Respondent. It has also been known for both parties to consider who their appointed arbitrator might choose as the third arbitrator and chairman of the tribunal, since most arbitrators will have preferences.

For the Respondent, there may be different factors in play. If their defence is weak, they may decide to make a tactical appointment, for example of a busy arbitrator whose lack of availability is likely to impede the progress of the arbitration, or even an arbitrator whose appointment might be challenged in order to slow the progress of the main dispute. Whilst not within the spirit of the arbitration clause, this does regrettably happen. When making their nomination, the Respondent has the advantage of knowing which arbitrator has been nominated by the Claimant. This enables them to consider who might work well (or not) with the Claimant's candidate.

Finally, for both parties there will be practical issues to take into account. For example, it will be important for their appointees to have experience of the proper law of the agreement under which the matter will be decided. In addition, they must be sure that their candidate will be willing to travel to the location where the hearings will take place (which may be the same location as the seat of the arbitration, but can be different) and they should take into account how onerous their travel requirements may be.

These are complicated issues which are important to get right: the choice of arbitrator may have a significant influence on the eventual outcome of an arbitral dispute.

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## Arbitration in the EU - exclusion from the Brussels Regulation

Plans are afoot to modify (but retain) the exclusion of arbitration from the Brussels Regulation. The Brussels Regulation addresses the jurisdiction of the national courts of EU Member States in civil and commercial matters. Currently, Article 1(2)(d) provides that arbitration is not subject to these jurisdictional rules, leading to inconsistent decisions in parallel proceedings across Member States, a situation which the proposed amendments are intended to address. A high profile example of the difficulties created under the current Regulation has been the long running dispute in the *"Front Comor"*.

In October 2008, West Tankers Inc, the owners of the vessel the *"Front Comor"*, were found by a London arbitration tribunal not to be liable for damage caused to a pier in Sicily belonging to Erg Petroli SpA (Erg). Despite the charterparty between West Tankers and Erg containing a provision that disputes were to be referred to arbitration in London, and the fact that Erg had already commenced arbitration proceedings against West Tankers in London, Erg's insurers, Allianz SpA, commenced proceedings in the Court of Syracuse to recover policy payments made to Erg.

West Tankers obtained two anti-suit injunctions, one in the English Commercial Court and one in the London arbitration proceedings, restraining Erg's insurers from continuing the Italian proceedings. Pending the decisions of the English House of Lords (as it was) and the European Court of Justice (ECJ) relating to the validity of these injunctions, certain matters were held over to be decided by a second London arbitration tribunal.

The Opinion of Advocate-General Kokott and the subsequent decision by the ECJ in 2009 determined that the anti-suit injunctions were interfering with a party's fundamental right of access to a national court under EU law. The ECJ decided that, notwithstanding that arbitration proceedings are expressly excluded from the Brussels Regulation, an anti-suit injunction "runs counter to the trust which Member States accord to one another's legal systems and judicial institutions". In addition, Article 5(3) of the Brussels Regulation allows for a party who causes another party harm to be sued in the court of the Member State where the harmful event occurred; in this case, Italy. In light of this decision, the English House of Lords had no choice but to discharge the anti-suit injunctions.

In an award dated 14 April 2011, the second London tribunal found that Erg's insurers were not liable in damages for West Tankers' legal fees, costs and expenses incurred in connection with the Italian proceedings. This was a blow for West Tankers who, after all, had successfully defended an arbitration claim brought against them pursuant to a valid arbitration agreement but who now had to bear unexpected and significant further costs in the Italian court. West Tankers appealed to the English Commercial Court.

Advocates for arbitration welcomed as a positive development the decision of the English Commercial Court on 4 April 2012. Mr Justice

Flaux upheld West Tankers' appeal, entitling them to equitable damages for Erg's insurers' breach of their obligation to arbitrate. He found that the second tribunal had failed properly to apply the decisions made by the Advocate-General and the ECJ in 2009: an award of equitable damages was not at odds with the European legal principle of effective judicial protection, that gives parties the right to commence claims in other European courts. Whilst Erg (or their insurers) must be able to bring proceedings against West Tankers in the place where the harmful event occurred, it did not follow that the arbitration tribunal was restricted in making decisions on the scope and effectiveness of the arbitration agreement itself. The tribunal would have been within its rights to award damages or an indemnity to West Tankers for Erg's insurers' breach of their obligation to arbitrate the disputes.

An arbitral tribunal could not be treated in the same way as the court of a Member State for the purposes of the Regulation. Whilst the court in another Member State could not review the decision of the court first seised, an arbitral tribunal is not subject to the Regulation because of Article 1(2)(d). Similarly, the principle of mutual trust in respective national legal systems between the courts of Member States could not be applied to the tribunal.

Additionally, the English Court noted that the Advocate-General had recognised that the decision of an arbitration tribunal could be different to the decision of a national court on either the merits of the case and/or on the scope of the arbitration agreement itself.

Unsurprisingly, Erg's insurers have launched an appeal against the Commercial Court's judgment. A hearing is scheduled for early 2013. In the meantime, the threat of being liable for compensatory damages may discourage parties from pursuing so-called 'torpedo' court actions alongside existing arbitration proceedings. Parties faced with a torpedo action should consider amending their claim submissions to include a claim for damages and/or a declaration for an indemnity. Parties should also consider including an express indemnity in relation to breach of the arbitration agreement at the time of negotiating contractual terms, in order to avoid such future issues arising.

The twists and turns of the *Front Comor* dispute illustrate the need for review of the current, unsatisfactory position under the Brussels Regulation. The position of both the European Parliament's Legal Affairs Committee and the European Council is that arbitration should remain excluded from the Brussels Regulation because it is dealt with by the New York Convention and the Geneva Convention, to which all Member States are party. However, each has proposed amendments to the Regulation's current wording which, whilst slightly different, seem intended to undo the effect of the 2009 decision of the ECJ in the *Front Comor.*

Last week, the European Parliament voted in the substantial majority to amend the Brussels Regulation with the insertion of four new recitals relating specifically to arbitration in order to try and mitigate the effects of the *Front Comor* decision. This will mean that a Member State that is seised in respect of a matter where the parties have entered into an arbitration agreement may refer the parties to arbitration or stay the court proceedings in favour of arbitration proceedings. Additionally, the courts of the Member State where arbitration proceedings have commenced shall be excluded from the Brussels Regulation where they are called by the parties to decide matters relating to arbitration rules and procedures, such as the appointment of arbitrators. The proposals will now be considered by the European Council in December. It is to be hoped that this may lead to an effective solution.

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## Chasing assets - the importance of the enforcing state

The enforceability of an arbitral award is critical to the effectiveness of arbitration. It is the law of the enforcing state (often different to the law of the seat of arbitration) which will determine whether an award can be successfully enforced against target assets. This important point is sometimes overlooked when negotiating the terms of an arbitration agreement.

The long-standing dispute between Yukos Capital SARL ("Yukos") and OJSC Rosneft Oil Company ("Rosneft") has shone the spotlight on enforcement of arbitral awards. It demonstrates how an award obtained in one jurisdiction can be successfully enforced in another, despite having been annulled by the courts of the seat. The latest judgment in the dispute, from the English Court of the Appeal (27 June 2012), also considered the "Act of State" doctrine in detail and assessed what constitutes foreign issue estoppel. More generally, the decision highlights the importance of the laws of the enforcing state and increasing recognition for the independence of arbitration.

### Background

Yukos obtained ICC arbitration awards against Rosneft, a Russian government-controlled entity, in relation to sums due under loan agreements. It began enforcement proceedings under the New York Convention in Amsterdam, where Rosneft's assets were located. Shortly thereafter, Rosneft obtained an order from the Russian Arbitrazh court for the awards to be annulled.

The Dutch Courts initially refused to enforce the awards on the ground that they had been annulled in Russia. Eventually however, the Amsterdam Court of Appeal refused to recognise the annulment and gave Yukos leave to enforce. This was because the appellate court found that the Russian annulment decisions resulted from a partial and dependent judicial process (that is, not impartial and not independent).

Yukos then obtained payment of the award in full, except that Rosneft did not pay interest. Subsequently, Yukos brought proceedings against Rosneft in the English Commercial Court, seeking permission to enforce the awards under the English Arbitration Act 1996 and bringing a claim for the amount awarded as debt and/or damages, with post award interest (totalling US$160 million), pursuant to article 395 of the Russian Civil Code and/or section 35A of the Senior Courts Act 1981.

Two preliminary issues were to be decided by the Commercial Court:

1. Following the Amsterdam Court of Appeal's judgment, did issue estoppel prevent Rosneft from denying that the Russian annulments resulted from a partial and dependent judicial process?

2. If not, did the Act of State doctrine or the non-justiciability principle prevent Yukos from establishing that the Russian annulments decisions resulted from a partial and dependent judicial process? (The Act of State doctrine provides that an English Court will not adjudicate on the validity or lawfulness of acts by a foreign sovereign state within the limits of its own territory. )

The Commercial Court held that there was an issue estoppel on the question of Russian judicial bias, and also that the Act of State doctrine did not apply. Rosneft appealed. In a unanimous judgment dated 27 June 2012, the English Court of Appeal allowed Rosneft's appeal in part.

### Foreign issue estoppel

Yukos argued that the decision of the Amsterdam Court of Appeal created an issue estoppel in relation to the annulment decisions by the Russian Court. Rosneft disagreed, arguing that the issue should also be decided by the English Court according to English laws of enforcement and in particular, public policy principles.

The Court of Appeal agreed with Rosneft because public policy was typically different in each country. The principles used to determine whether the Russian courts were partial and dependant may vary considerably from country to country.

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English public policy requires specific examples of partiality before a decision not to recognise the judgment of a foreign state can be made. Therefore, Rosneft was not estopped from claiming in the English Courts that the Russian Court decisions were impartial. The bias allegation against the Russian Courts will now be heard in the English enforcement proceedings.

### Act of State doctrine and its limitations

After a detailed analysis of the law, the Court of Appeal concluded that an English Court is not prevented by operation of the Act of State doctrine from considering whether there has been a substantial injustice in a foreign court. Judicial acts are generally not regarded as acts of the state for the purposes of the Act of State doctrine. The principle of comity cautions that judicial acts of a foreign state should not be challenged without cogent evidence.

### Arbitration theory

The English Court of Appeal's decision demonstrates that an enforcing state will generally approach the question of enforcement by reference to its own laws, without much deference to other national legal systems. It also contributes to the ongoing debate amongst arbitration theorists as to the relationship between the enforcing state and the seat state.

There are two competing theories about this relationship. The delocalised or 'separate legal order' theory, popular amongst French scholars, recognises arbitration as a dispute resolution system in its own right, independent from national legal systems except at certain points in the arbitral process. The parties' consent to arbitration is fundamental, and the role of seat state is less significant. The derogation theory argues that arbitration is only given life by virtue of a national legal system. The parties only participate in the arbitration process in clearly prescribed procedural circumstances. Greater significance is therefore placed on the laws of the seat and the supervisory role of the seat state.

In its finding that an arbitration award should not be subject to clear partiality of the courts of the seat, the Dutch Court's decision in *Yukos* effectively supports the separate legal order theory and the independence of the arbitration process. This may appear controversial given both that the parties chose the courts of the seat to govern the procedure of the arbitration and that one of the grounds for refusing enforcement under the New York Convention is that an award has been set aside by a competent authority of the country where the award was made (Article V.1(e)). However, in circumstances where there is cogent evidence of corruption or partiality by the courts of the seat, an enforcing state will be reluctant to dismiss an enforcement application, preferring to uphold the decision of independent arbitrators.

In this ongoing dispute, the English Court must now reach its own decision, applying English law on enforcement by reference to its own public policy principles after hearing full argument and all evidence. Should it arrive at the same conclusion as the Dutch Court, this would confirm an increasing willingness by enforcing states to uphold the independence of the arbitration process.

### Enforcement as a matter for national law – the New York Convention

The *Yukos* dispute clearly highlights the significance of the laws of the enforcing state. What is the significance of the New York Convention?

There are 147 state parties to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, commonly known as the New York Convention. It is widely regarded as successful and effective. States incorporate it into national law by express reference or by relying heavily on its provisions in drafting relevant legislation. Under the Convention, enforcement *may* be refused (Article V.1) in certain instances, requiring proof:

1. Incapacity/invalidity of arbitration agreement.
2. No proper notice of arbitration.
3. Matters decided outside scope of arbitration agreement.
4. Arbitral tribunal/process not properly constituted/followed.
5. The award is not yet binding or set aside/suspended.

There are also two discretionary grounds upon which an enforcing state may refuse enforcement under Article V.2:

1. The subject matter of the difference/dispute is not capable of arbitration under the law of the enforcing state (ie. arbitrability).

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2. If contrary to public policy.

Some states, including France, have additional specific requirements.

The widespread adoption of the New York Convention does not guarantee uniformity of interpretation by the courts of enforcing states, particularly in respect of the discretionary grounds in Article V.2. For example, in *Yukos*, the English Court may come to a different view from the Dutch Court because it will approach the public policy issue by reference to its own laws and traditions.

### Conclusion

The English Court of Appeal's judgment in *Yukos* confirms that the Act of State doctrine does not apply to judicial acts, as well as providing guidance on foreign issue estoppel (which does not apply in this case). The bias allegation against the Russian courts will now be tried in the English enforcement proceedings. If, like the Dutch courts, the English courts give leave to enforce awards that have been set aside by the courts of the seat of arbitration, this would be significant.

Whilst the conflicting decisions in *Yukos* add to the interesting theoretical debates on arbitration, they will inevitably create unwelcome uncertainty in relation to enforcement. However, there may be some consistent threads to pull together: first, arbitration seems to be continuing to receive increased recognition in its own right; and second, the importance of the enforcing state should not be underestimated.

In respect of international commercial contracts containing an arbitration agreement, it is of course important and prudent to consider where a counterparty's assets are located and whether it will be possible successfully to enforce an arbitration award in the jurisdiction of those assets. The earlier this assessment is made, the better.

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## Conferences & Events

HFW is planning a series of arbitration seminars in Australia in March 2013. These will be held in Melbourne, Sydney and Perth. If you would like further details, please contact events@hfw.com.