International Arbitration

April 2017

ENGLISH COURT REVIEWS THE "FRAUD UNRAVELS ALL" PRINCIPLE IN ENFORCEMENT OF CIETAC ARBITRATION AWARD

In *Sinocore International Co. Ltd. v RBRG Trading (UK) Limited*[1], HFW, acting for Sinocore International Co. Ltd (the Seller), successfully argued that a foreign arbitral award should be enforceable in England notwithstanding the allegations made by RBRG Trading (UK) Limited (the Buyer) that the relevant transaction had been 'tainted' by fraud and was therefore unenforceable on the grounds of public policy.

The case reinforces the important principle that the public interest in the finality of arbitration awards, particularly an international award as in the present case determined as a matter of a foreign law *"clearly and distinctly outweighs any broad objection on the grounds that the transaction was 'tainted' by fraud"*.

Background

The Seller agreed to sell 1450m/t of cold rolled steel coils to the Buyer (the Sale Contract) at a price of US$870 m/t. Pursuant to the Sale Contract, the Buyer was to open an irrevocable letter of credit (on UCP600 basis) for the purchase price.

A letter of credit was issued by Rabobank Nederland (Rabobank) on 22 April 2010, which stipulated the latest date of shipment as 31 July 2010 (the Letter of Credit). However, on 12 June 2010 and, crucially, without the agreement of the Buyer, the Seller then instructed Rabobank to issue an amendment to the Letter of Credit, amending the shipment period to read "20 to 30 July 2010".

The coils were loaded on 5 and 6 July 2010 and bills of lading were issued showing the same dates. On 7 July 2010 the vessel departed the load port and the Seller sent an advice to the Buyer, recording that the bills of lading were dated 6 July 2010.

On 22 July 2010, the Seller sought payment from Rabobank under the revised Letter of Credit, by presenting bills of lading bearing the dates 20 and 21 July 2010. As shipment had taken place on 5 and 6 July 2010, it is plain, and Sinocore accepts, that those bills were incorrectly dated so that documents could be presented to Rabobank which, on their face, evidenced shipment within the period required by the purported amendment to the Letter of Credit referred to above.

1 [2017] EWHC 251 (Comm). Full judgment can be found here: http://www.bailii.org/ew/cases/EWHC/Comm/2017/251.html

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BRIAN PERROTT, PARTNER

On 26 July 2010, the Buyer successfully petitioned the Court of Amsterdam to grant an injunction restraining Rabobank from making payment to the Seller. The Seller then terminated the Sale Contract and sold the coils to another buyer at a price below that agreed with the Buyer.

The Chinese arbitration proceedings

In accordance with the Sale Contract's law and jurisdiction clause, the Buyer commenced CIETAC arbitration proceedings against the Seller in Beijing and under Chinese law, for damages caused by the Seller's alleged breach of an inspection clause. In this regard the Buyers argued that the Seller shipped the coils early so that the Buyer could not inspect the coils and then proceeded to forge bills of lading to cover this up.

The Seller, also alleging breach of contract, issued a counterclaim for the difference in the sale price eventually obtained and the original price agreed with the Buyer.

In its award, the Tribunal determined that:

- The Buyer had not requested that the Seller allow it to inspect the coils before or during shipment and the Seller was not therefore in breach of the Sale Contract.
- As the Seller had not agreed to amend the shipment date on the Letter of Credit, the Buyer was in breach of the Sale Contract and it was this breach which caused the termination of the Sale Contract and the losses that flowed (in fact, the Tribunal found that the Buyer's purported amendment of the Letter of Credit *"was like a trap set by the buyer for the seller"*).
- The Seller's incorrect dating of bills of lading under the Letter of Credit constituted a deception of Rabobank but it did not deceive the Buyer, because the Buyer had actual knowledge (from the Seller) of the true shipment dates.

The Award required the Buyer to pay the Seller damages of US$4,857,500, costs of RMB535,492 as well as a proportion of the arbitration fees (the Award).

Enforcement application[2]

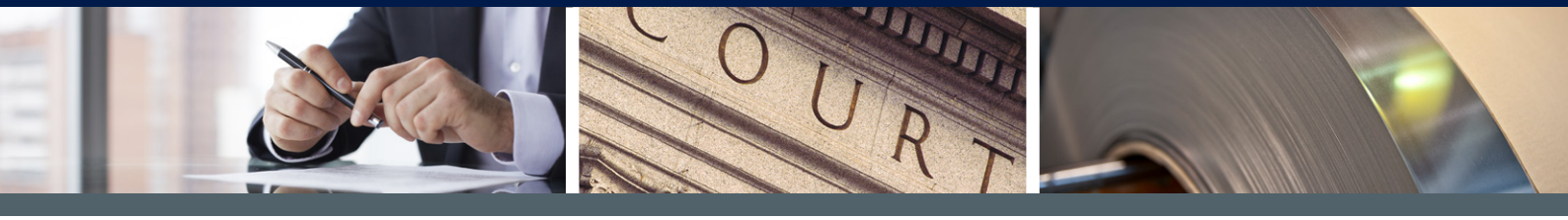
As the award was made in China, a party to the New York Convention 1958, the Seller issued an enforcement application seeking an order on the basis of s.101(2) of the Arbitration Act 1996 (the Act) which states: *"A New York Convention award may, by leave of the court, be enforced in the same manner as a judgment or order of the court to the same effect"*.

On 2 March 2016 an order was made giving the Seller permission to enforce the Award (the Order). The Buyer challenged the Order on the basis of s.103(3) of the Act, which provides that recognition or enforcement may be refused if such recognition or enforcement would be contrary to public policy.

The Buyer sought to argue that enforcement of the Award would contradict the English courts' policy of not allowing its courts to be used to give effect to fraud. The Buyer argued that:

- The Seller's claim was based on its own fraudulent action and the court would be giving effect to this fraud by enforcing the Award; and/or
- The English courts should not assist a seller who has presented forged documents under a letter of credit since letters of credit are *"the life-*

2 In *IPCO (Nigeria) Limited v Nigerian National Petroleum Corporation* [2017] UKSC 16 the English Supreme Court has recently ruled that security is not a requirement to challenging enforcement of arbitration awards



blood of international commerce" and that banks are excepted from paying out against documents where they contain fraudulent statements on the basis that *"fraud unravels all"*.

The court's approach

The usual approach to an objection on the basis of public policy is that there will be a strong presumption that an award issued in a country that is a party to the New York Convention will be enforceable, and that public policy defences will be *"treated with extreme caution"*[3].

Whilst the court will consider refusing to enforce awards which give effect to fraudulent or illegal enterprises or claims on the basis of the approach set out above, it will not refuse to enforce a lawful claim under a lawful transaction, even if voidable, on the basis that the transaction is *"tainted"*.

Going "behind" the Award

The Buyer argued that the presentation of the incorrectly dated bills and not its own breach was in fact the operative cause of the loss, since the Seller could have received payment if it had simply presented the genuine bills of lading for payment, as the purported amendment of the Letter of Credit was not binding on the Seller by virtue of the UCP.

The court recognised that the Tribunal had expressly considered (and rejected) these arguments. The judge applied the principle identified in *Soleimany v Soleimany*[4] and *Westacre Investments Inc v Jugoimport-SPDR Holding Co. Ltd*[5], that it was not open to him to go behind the Award and apply English law to the issue which had been determined by the Tribunal. As such it was not necessary or appropriate for the judge to reconsider the merits of the underlying claim under English law – even if English court may not have reached the same conclusion as the Tribunal, as a matter of English law or even as a matter of logic.

Fraud unravels all

The Buyer's wider argument that the court should not assist a seller who presented incorrectly dated documents was also dismissed by the court, who held that the maxim 'fraud unravels all' should not facilitate a situation whereby a seller who presents incorrectly dated documents cannot recover damages even if his claim relates to a prior breach of contract by his counterpart. By preventing relief on the basis that that transaction has been 'tainted' would *"introduce uncertainty and to undermine party autonomy"*, as stated at paragraph 46 of the judgment quoting Mr Justice Burton in National Iranian Oil[6]. Mr Justice Phillips also recorded the need to balance such arguments against the public interest in the finality of international arbitration awards. On this balancing act, Mr Justice Phillips held that the enforcement of the Award would not be contrary to public policy and the Buyer's application to prevent enforcement was dismissed, concluding at paragraph 47:

"Further, even if it was appropriate to consider such a wider issue, I would nevertheless conclude that public interest in the finality of arbitration awards, particularly an international award such as in the present case determined as a matter of a foreign law, clearly and distinctly outweighs any broad objection on the grounds that the transaction was "tainted" by fraud."

Leave to appeal was refused by the High Court, although it is still possible that the Buyer will seek to challenge this decision.

HFW comment

The English courts remain very reluctant to restrict enforcement of an arbitration award on the basis that the underlying transaction was 'tainted' and therefore contrary to public policy.

In reaching its decision, the court was clear that a balance must be struck between the importance of enforceability of an arbitral award and the need to prevent a party prospering from improper activity. In this regard Mr Justice Phillips was undoubtedly of the mindset that the public interest in recognising the finality of an arbitration award would not be overridden lightly.

From a legal perspective this is encouraging. The New York Convention is key to providing commercial parties with confidence on how international law will support their contracts via a uniformly recognised system and approach to enforcement . To undermine its applicability on the basis that a transaction was later 'tainted' by fraud would undoubtedly erode its effectiveness.

This decision is also of major significance from a commercial perspective. Business is inherently international and when contracting with counterparties in multiple jurisdictions it is crucial to have comfort that, should the unfortunate occur and a dispute arise, proper and effective recourse can be sought in the necessary jurisdictions.

In this case Brian Perrott, Rachel Turner and Marie-Anne Boothroyd acted for the claimant/seller Sinocore International Co Ltd.

3 *IPCO (Nigeria) v Nigerian National Petroleum* [2005] 2 Lloyd's Rep 326

4 [1999] QB 785

5 [2000] 1 QB 288

6 *National Iranian Oil v Crescent Petroleum* [2016] *2 Lloyd's Rep 146*



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