

Not arbitrary in the least

Arbitral awards and the TCL judgment

A recent High Court decision provides a timely reminder to practitioners in international commercial arbitration of some of the elements that underscore practice in this area of law. **By Deborah Tomkinson and Tomoyuki Hachigo**

On 13 March 2013 the High Court of Australia rendered its decision in *TCL Air Conditioner (Zhongshan) Co Ltd v The Judges of the Federal Court of Australia (TCL)*.¹ In this landmark judgment, the High Court unanimously rejected a constitutional challenge to the *International Arbitration Act 1974* (Cth) (*IAA*), which gives force of law and effect to the United Nations Commission on International Trade Law (UNCITRAL) Model Law on International Commercial Arbitration (Model Law) and to Australia's obligations under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention).

The High Court decision not only assures commercial parties that arbitral awards will continue to be recognised and enforced by Australian courts, it also provides a timely reminder to those involved in international commercial arbitration of some of the

fundamental elements that underscore practice in this area of law.

Background

The proceedings concerned a dispute arising out of a distribution agreement between a Chinese company, TCL Air Conditioner Co Ltd (TCL), and an Australian company, Castel Electronics Pty Ltd (Castel). The parties' agreement provided for the submission of disputes to arbitration in Australia. In July 2008 Castel commenced arbitration proceedings claiming damages for breach of contract. TCL counterclaimed. The arbitral tribunal made two awards, in damages and for costs, which were principally in favour of Castel.

Castel applied to the Federal Court of Australia to enforce the awards under Part III of the *IAA* which, in s16(1), confirms that "the Model Law has the force of law in Australia". Article 35 of the Model Law (the text of which is set out in Schedule 2 to the *IAA*) governs the enforcement of arbitral awards made in

Australia ("non-foreign awards").² Article 35 provides:

"An arbitral award, irrespective of the country in which it was made, shall be recognised as binding and, upon application in writing to the competent court, shall be enforced subject to the provisions of this article and of article 36".

TCL opposed enforcement of the awards on the ground that the Federal Court lacked the necessary jurisdiction to enforce. TCL also applied to have the awards set aside or refused enforcement under Articles 34 and 36 of the Model Law, claiming breaches of the rules of natural justice.

At first instance, in a judgment issued on 23 January 2012, Murphy J held that the Federal Court had jurisdiction to enforce the awards.³ The balance of the parties' applications (to enforce the awards and seeking to set them aside) was heard separately in April 2012 and judgment was reserved.

In July 2012, TCL applied in the original jurisdiction of the High Court for the issue of





The High Court focused on the fact that tribunals derive their power from the agreement of the parties as the key factor distinguishing arbitration from the exercise of judicial power.

a constitutional writ of prohibition directed to the judges of the Federal Court seeking to restrain them from enforcing the awards, and *certiorari* to quash any orders made by Murphy J that might be issued prior to the High Court determining TCL's application.

Four days before the High Court hearing, Murphy J rendered judgment on the balance of the parties' applications, rejecting TCL's application to set aside and making orders in terms of the awards, allowing their enforcement.⁴

As a matter of critical importance to international arbitration in Australia, each of the attorneys-general of the Commonwealth and the states of Queensland, South Australia, Victoria, Western Australia and New South Wales intervened in the High Court proceedings in support of the constitutionality of the *IAA*. The Australian Centre for International Commercial Arbitration also intervened, with the Institute of Arbitrators and Mediators Australia and the Chartered Institute of Arbitrators (Australia), as *amici curiae*.

Two limbs of TCL's argument in the High Court

Chapter III of the Australian Constitution prevents the conferral of commonwealth judicial power to a body other than Chapter III courts and requires the function of a Chapter III court to be compatible with the essential character of a court. TCL submitted that s16(1) of the *IAA*, in giving force to the Model Law, is incompatible with Chapter III of the Constitution. Two separate arguments were advanced by TCL.

1. Impairment of the institutional integrity of the courts

TCL asserted that the *IAA* substantially impairs the institutional integrity of the Federal Court by effectively co-opting the Federal Court into providing assistance during the course of arbitral proceedings and requiring the enforcement of awards regardless of any legal error evident on their face. TCL contended that the *IAA*, by denying the court any scope for review of awards

for errors of law, requires the Federal Court to knowingly perpetrate legal error.

To supplement this argument, TCL claimed that Article 28 of the Model Law, which provides that the arbitral tribunal "shall decide the dispute in accordance with such rules of law as are chosen by the parties", confines the authority of a tribunal to decisions made correctly at law and that an erroneous award is not binding. In the alternative, TCL submitted that a term of similar effect is to be implied into every arbitration agreement.

2. Impermissible vesting of judicial power

TCL's second argument was that the *IAA* impermissibly confers tribunals with commonwealth judicial power. It submitted that the Federal Court is required to enforce awards without the opportunity for any independent exercise of judicial power, which effectively vests tribunals with judicial power, as it is the tribunal that finally determines the parties' rights and obligations.

The High Court decision

The High Court unanimously rejected both of TCL's objections in two separate judgments, one of French CJ and Gageler J, and the other of Hayne, Crennan, Kiefel and Bell JJ. The basis for the High Court's reasoning was as follows:

1. No compromise of institutional integrity: courts exercise judicial power when enforcing awards

The High Court distinguished between a cause of action heard and determined by a tribunal, and an enforcement action that is subsequently brought before the courts. The High Court confirmed that the rendering of an award by a tribunal extinguishes the original cause of action and replaces it with new rights and obligations set out in the award. In the majority of cases, enforcement will not be required, as the parties will abide by the award rendered.⁵ When proceedings are required to enforce an award, the court's role is to consider whether to enforce the obligations set out in the award in accordance with relevant provisions of the *IAA* and the Model

Law. This reflects the court's proper role in holding parties to their contractual promise to have their disputes finally determined by arbitration. The High Court found that the power to set aside or refuse to enforce an award in specified circumstances under the Model Law is protective of the court's institutional integrity.⁶

TCL's argument based on Article 28 of the Model Law was also rejected, with the High Court finding that this provision is primarily directed to questions of choice of law and not the correctness of their application.⁷ Moreover, the High Court determined that no term could be implied into an arbitration agreement limiting the tribunal's authority to the correct application of law.⁸

2. No delegation of judicial power: power comes from the agreement

In rejecting the second argument advanced by TCL, the High Court focused on the fact that tribunals derive their power from the agreement of the parties as the key factor distinguishing arbitration from the exercise of judicial power. Arbitral awards are final and conclusive because parties have agreed to submit a dispute of the relevant kind to binding arbitration and legal policy requires contractual bargains to be upheld.⁹

When enforcing a resulting arbitral award, contrary to TCL's contention that the courts do not independently exercise any powers, the High Court confirmed that courts are being asked to determine the enforceability of the award by reference to the grounds of challenge set out in Article 36 of the Model Law.¹⁰ As such, the High Court held that the conferral of jurisdiction on the Federal Court to determine the enforceability of arbitral awards by reference to criteria which do not include a specific power to review an award for error is not incompatible with Chapter III of the Australian Constitution.

Implications of the decision

The judgment has been welcomed by the international arbitration community both in Australia and overseas as one which embraces the policy and intent of

international arbitration practice. It provides comfort to the business community regarding the finality of arbitral awards and advances Australia's efforts to establish itself as a hub for international arbitration in the Asia-Pacific region.

Given this, and with the use of international arbitration in Australia growing, the High Court judgment comes as a timely reminder of some of the fundamental features of international arbitration practice that must be kept in mind when practising in this area of law. For practitioners and the business community alike, the decision provides a number of practical tips for consideration.

The wider context

The High Court judgment places the Model Law in context, explaining its international origins and development. First adopted in 1985, the Model Law is considered to reflect an international consensus on arbitral practice, and is intended to "assist States in reforming and modernizing their laws on arbitral procedure so as to take into account the particular features and needs of international commercial arbitration".¹¹ It is the product of extensive preparatory work by

highly regarded practitioners from around the world.

As outlined in the decision of French CJ and Gageler J in *TCL*, the Model Law also finds its origins in the text of the New York Convention (NYC). Both were developed with the aim of achieving uniformity at an international level in relation to the recognition and enforcement of awards. The Model Law was developed to complement the NYC and must be construed in light of its objectives, including the specific and limited bases upon which enforcement may be challenged and refused. By giving force of law to the Model Law and the NYC, the *IAA* supports this pro-enforcement bias.

The High Court made it clear that, given this international context, it is "imperative that the Model Law be construed without any assumptions that it embodies common law concepts or that it will apply only to arbitral awards or arbitration agreements that are governed by common law principles".¹² The High Court also referred to s17 of the *IAA*, which provides that reference may be made to the documents of UNCITRAL and the UNCITRAL working group in the interpretation of the Model Law. A review of these documents shows that both common and

civil law processes were drawn on to develop the concepts of arbitration practice set out in the Model Law.

It is therefore crucial that practitioners and parties understand the wider historical context in which international arbitration operates. This will ensure an understanding of the objectives that are sought to be achieved by the international framework for enforcement, and inform the practice of international arbitration in Australia. International arbitration has developed "as an alternative method distinct from litigation",¹³ reflecting a combination of common and civil law traditions. As such, practice in this area requires knowledge of specific processes that will go beyond many practitioners' usual domestic or litigation experience.

The global context of international arbitration also serves as a reminder that the focus of arbitration must not just be on the jurisdiction in which the arbitration will occur. There are a variety of significant factors that may impact on advice given in relation to the enforceability of an arbitration award. For example, a particular dispute may be capable of being resolved by way of arbitration under the law of the place (seat) of the arbitration but may not be considered arbitrable in

Your trust
isn't discretionary
(That's why we focus on currency & compliance).

Cleardocs online legal document creation process is easy.
Company registration, trusts, estate planning, SMSF and more.
Master documents, interfaces and legal information are signed-off by top 20 lawyers, Maddocks.

Cleardocs
clarity | simplicity | ease of use

www.cleardocs.com/legal
Helpline 1300 307 343



the jurisdiction where enforcement is likely to be sought. In order to ensure that parties' objectives are achieved and that any ultimate award is enforceable, it is critical that specialist advice from experienced international arbitration practitioners is obtained both at the stage of drafting an arbitration agreement and when a dispute under that agreement arises.¹⁴

For practitioners, there is extensive reference material available to assist with the interpretation of the Model Law and the NYC, as was pointed out by the High Court. Other documents detailing the practice of international commercial arbitration, including expert texts and guidelines, practice notes and protocols developed by UNCITRAL and other highly regarded bodies such as the International Bar Association and the Chartered Institute of Arbitrators, are also worthwhile tools for an international arbitration practitioner to keep at hand.

It's all in the arbitration agreement

The High Court's decision in *TCL* centres on the importance of the arbitration agreement as the mechanism giving rise to the right to refer disputes to private arbitration. The consensual nature of arbitration sets it apart from court proceedings, in which judicial power is exercised coercively.¹⁵

It is the parties' agreement, including any reference to applicable procedural rules and the law of the seat (the *lex arbitri*), from which a tribunal derives its authority. The tribunal cannot exceed that authority and doing so may form the basis of an application to set aside or refuse enforcement of the award under the Model Law.¹⁶

Given the significance of the arbitration agreement, it might be assumed that a good deal of time and care would go into its drafting to ensure that the agreed process best suits the parties' requirements and the relevant transaction. However, this is not always the case. Poorly drafted arbitration

agreements are all too common and can cause difficulties for parties at all stages of arbitration proceedings. Most significantly, serious defects in an arbitration agreement can lead to the validity of the agreement being challenged or to a dispute between the parties as to the intended effect of the agreement. This defeats the purpose of an arbitration agreement and leads to a significant increase in the time spent and the cost of proceedings.

There are a number of important elements that should be fully considered when drafting an arbitration clause, including the constitution of the tribunal, the choice of seat, language and procedural rules, provision for confidentiality and consolidation of arbitrations or joinder of parties. Certain elements, in particular the choice of seat, will have significant consequences for any dispute that arises.

The beauty of the arbitration agreement is that it represents the parties' accord with regard to the method of dispute resolution and parties should take full advantage of the opportunity to tailor their chosen process. To avoid any pitfalls and best take advantage of the flexibility that arbitration has to offer, parties should obtain specialist advice.

Errors of law: the last word

The crux of *TCL*'s argument, as further elucidated in oral submissions, was that the inability of the courts to refuse to enforce an arbitral award based on error of law contravened the Australian Constitution. As noted above, the High Court found this to be incorrect.¹⁷

What this means is that, under the *IAA*, a party does not have the right to "appeal" an arbitral award (that is, to challenge its enforcement or seek to have it set aside) on the basis that the award contains an error of law. Australian courts are required to enforce awards unless one of the grounds of challenge specified in the Model Law is conclusively proven. This operates to prevent

parties from seeking time-consuming, costly merits review and is reflective of legitimate legislative policy aimed at encouraging efficiency, impartiality and finality in international arbitration.¹⁸ Practitioners need to have a clear understanding of the recourse available against an international arbitral award and advise accordingly.

It is also critical, given that the grounds of challenge are limited, that much care be taken when appointing a tribunal. Choice of arbitrator(s) may be the single most important decision parties make in an international arbitration and there is a wide range of factors that parties should consider when making appointments. These may include an arbitrator's relevant qualifications, technical expertise, legal background (common or civil law), experience acting in international arbitrations, likely availability to hear the matter, impartiality and independence from the parties, language skills and knowledge of relevant practices or customs (business or otherwise). It should not be assumed that "one size fits all"; a tribunal appointed in one case may not necessarily be appropriate in another. When a dispute arises, it is open to the parties to reach an agreement on the constitution of the tribunal. Alternatively, parties may wish to consider providing for appointments to be made through a well-recognised arbitral institution, which should take into account relevant factors in order to ensure that an impartial and independent tribunal is appointed.

Conclusion

The High Court decision in *TCL* acknowledges the importance of international commercial arbitration and the historical, international context in which it operates. It recognises that international arbitration, through the framework of the NYC and the Model Law, provides recognition and enforcement of commercial awards on a global scale far exceeding the enforceability

LIV Privileges
exclusive offers for members



*Conditions apply.

AUSTRALIAN UNITY

Enjoy peace of mind and a generous discount with quality health cover from Australian Unity. Join or switch to Australian Unity and you'll receive a 7.5% discount* off your health cover when you pay by direct debit.

Visit www.australianunity.com.au/liv/ or call 13 29 39
8.30am to 8.30pm EST Monday to Saturday

Terms and Conditions The LIV receives revenue on member generated activity through this member benefits program. The revenue is applied to maintain the quality and diversity of LIV services, further benefiting you professionally, personally and in your career and business. All costs incurred in marketing specific LIV programs are borne by the member benefit partner.



of foreign court judgments. By providing a binding mechanism to resolve disputes between parties located in different jurisdictions, international arbitration facilitates cross-border trade and commerce.

Apart from providing finality of process, arbitration affords parties a high level of procedural flexibility, allowing a cost-effective and efficient process, appropriate to the relevant transaction, to be structured. Parties should make use of the flexibility available to them and ensure that they design a process that delivers an appropriate and valuable commercial dispute resolution outcome. In order to do so, and to avoid any possible pitfalls, it is recommended that parties routinely seek advice from specialist arbitration practitioners when negotiating an arbitration agreement or commencing and pursuing arbitration proceedings. ●

DEBORAH TOMKINSON is the deputy secretary-general (Sydney) of the Australian Centre for International Commercial Arbitration (ACICA) and the dispute resolution manager of the Australian International Disputes Centre (AIDC). **TOMOYUKI HACHIGO** was an intern at ACICA and AIDC in 2013 through the University of New South Wales AIDC intern program.

Practitioners need to have a clear understanding of the recourse available against an international arbitral award and advise accordingly.

1. *TCL Air Conditioner (Zhongshan) Co Ltd v The Judges of the Federal Court of Australia* [2013] HCA 5.

2. Under the IAA, the enforcement provisions of the Model Law also apply to awards made in countries that are not signatories to the New York Convention. By comparison, Part II of the IAA is concerned with foreign awards made in New York Convention countries other than Australia.

3. *Castel Electronics Pty Ltd v TCL Air Conditioner (Zhongshan) Co Ltd* [2012] FCA 21.

4. Note 3 above, at 1214.

5. See Queen Mary University of London and PricewaterhouseCoopers report *International Arbitration: Corporate Attitudes and Practices*, 2008.

6. Note 1 above, at [103].

7. Note 1 above, at [15] (French CJ and Gageler JJ) and [71] (Hayne, Crennan, Kiefel and Bell JJ).

8. Note 1 above, at [74].

9. Note 1 above, at [108].

10. Note 1 above, at [32].

11. The Model Law was revised in 2006. It is the 2006 version that is given force of law under the IAA (as amended in 2010). See UNCITRAL, *UNCITRAL Model Law on International Commercial Arbitration (1985), with Amendments as Adopted in 2006*: www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html.

12. Note 1 above, at [8].

13. Note 1 above, at [45].

14. It is worth noting that the majority of respondents to the Queen Mary University of London and PricewaterhouseCoopers report *Corporate Choices in International Arbitration: Industry Perspectives 2013* regarded expertise in the arbitral process as more important in the choice of outside counsel in an international arbitration than industry specialism.

15. Note 1 above, at [9]–[10].

16. Note 1 above, at [17].

17. Note 1 above, at [33].

18. Note 1 above, at [105].

Unisearch Expert Opinion Services

Never Stand Still



UNSW Global
AUSTRALIA

PROFESSIONAL • EXPERIENCED • RELIABLE

- Managing over 900 matters per year
- Finding you the best expert for your case within two working days
- 5000 experts spanning 2000 fields of expertise

www.unisearch.com.au

Melbourne (03) 9909 7443 • Sydney (02) 9385 5555

Unisearch is a business group of UNSW Global Pty Limited