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INTERNATIONAL ARBITRATION

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In this issue ...

The importance of meeting a deadline and paying an arbitrator's fees: a cautionary tale

Summary

Any party considering applying for permission to appeal against an arbitration award should take note of Mrs Justice O'Farrell's recent High Court Judgment in the case of *Rollitt v Ballard* [2017] EWHC 1500 (TCC). In particular:

1. Appeals against an award under sections 67, 68 or 69 of the Arbitration Act 1996 must be brought under section 70 "within 28 days of the date of the award".

2. The 28 day period runs from the date of the award and not when it is delivered to the parties. A party who wishes to reserve his right to take the matter to Court by way of appeal must ensure that the award is taken up in time (i.e. by paying an arbitrator's fees) to enable the application to be made.

3. The principles applicable to the Court's discretion to extend time under section 79 of the Arbitration Act 1996.

The relatively short 28 day period reflects the principle of "speedy finality" which underpins the Act. The party seeking an extension must therefore show that the interests of justice require an exceptional departure from the timetable laid down by the Act.

The facts

A dispute arose between Mr Rollitt and Mr Ballard concerning the payment of management fees in relation to a property in Barbados. An arbitrator was appointed by the Chartered Institute of Arbitrators (CIArb) and Mr Ballard made an application to the arbitrator for a ruling on his substantial jurisdiction.

On 12 May 2016 the Arbitrator sent an email to the parties informing them that the Award on the preliminary issues had been completed and that it would be published upon cleared payment of his fees.

Pursuant to section 70(3) of the Arbitration Act 1996 (the **Act**) an unhappy recipient of an arbitration award has 28 days to apply for permission to appeal under section 69 of the Act 1996. In this case the 28 day period expired on 9 June 2016.

However **88 days after the deadline**, on 5 September 2016 the Claimant made an application to the High Court seeking an extension of time and permission to challenge the award pursuant to sections 69 and 79 of the Act.

Principles considered by the Court

In deciding whether to allow the application the Judge considered the following principles set out in recent case law regarding extensions of time to challenge an arbitration award, including:

- The relatively short **28 day period provided for by the Act reflects the principle of "speedy finality" which underpins the Act**. The party seeking an extension must therefore show that the interests of justice require an exceptional departure from the timetable laid down by the Act.

a party who wishes to reserve his right to take the matter to Court by way of appeal... must ensure that the award is taken up in time to enable the application to be made.

- The relevant factors include:

    a. the length of the delay (given the 28 day period provided for a delay of days would be 'significant', a delay in weeks or months 'substantial');

    b. whether the delaying party was acting reasonably;

    c. whether the respondent or the arbitrator caused or contributed to the delay;

    d. whether the respondent would suffer irremediable prejudice;

    e. if the delay impacted on the progress of the arbitration;

    f. the strength of the application;

    g. whether in the broadest sense it would be unfair to the applicant to deny him the chance of having the application determined.

- In deciding whether the delaying party was acting reasonably, the Judge also considered the following points: (a) in seeking relief from the Court the applicant is normally expected to adduce evidence which explains his conduct unless circumstances make it impossible and (b) whether the party acted intentionally in making an informed choice to delay making the application.

- The Court will not normally conduct a substantial investigation into the merits of the challenge application however if, on looking at the material before it, the Court can see that the challenge involves **an intrinsically weak case, it will count against the application for an extension, whilst an apparently strong case will assist the application.**

The Decision

Reasonableness of the Claimant's Delay

The initial period of the Claimant's delay arose as a result of the parties' dispute as to which party should pay the arbitrator's fees or whether they should be shared equally. (The Arbitrator had clearly stated that he required payment of his fees before the Award would be released.) The Judge found that this was not a reasonable excuse for the delay. Case law has clearly stated in the past that "it *is not open to a party to argue…that they were waiting for the other party to take up the award; that they did not know that there was any point they wanted to raise on the award….a party who wishes to reserve his right to take the matter to Court by way of appeal… must ensure that the award is taken up in time to enable the application to be made*."

The fees in question were 'very modest' (£4,052 incl VAT) and the onus was on the Claimant to take the appropriate steps to ensure that he preserved the right to challenge the Award.

The Claimant was also criticised for causing further delay by choosing, when he decided to pay the arbitrator's fees, to pay the funds by cheque (opposed to a quicker method). There was also 'no reasonable explanation' for the final period of delay from 8 August when the funds for the arbitrator's fees cleared on 8 August and the issue of proceedings on 5 September.

Contribution to delay by others

The Claimant sought to argue that the delay was at least in part, the defendant's responsibility by refusing to sign the arbitrator's terms and conditions and by refusing to pay half of the arbitrator's fees and expenses. However the Judge found that while the defendant may not have signed the terms, the Claimant did sign them and therefore must have been aware that it could be required to pay the arbitrator's fees and expenses if the defendant declined to do so and the claimant could not rely on this as contributing for the delay.

Strength of the application

The Claimant sought permission to appeal pursuant to section 69 of the Act which gives a party to arbitral proceedings the right to appeal to the Court on a question of law arising out of an award. Leave to appeal will only be granted where the question of law identified (a) will substantially affect the rights of one or more of the parties; (b) was one which the tribunal was asked to determine; (c) the determination was obviously wrong and (d) it is just and proper for the Court to determine the question.

The Judge found in this case that even if the application for leave to appeal had been made in time, it would be refused on it merits.

Daniella Smith, London

Lessons learned

This case is an important reminder that:

- Arbitrators are entitled to "… refuse to deliver an award to the parties except upon full payment of the fees and expenses of the arbitrators" (section 56 of the Act).
- If your arbitrator withholds an award, they will need to be paid promptly in order to preserve the opportunity to appeal under section 70 of the Act.

English Commercial Court considers the principles relating to setting aside permission to enforce an arbitral award on the grounds of fraud – in *Stati and others v The Republic of Kazakhstan* [2017] EWHC 1348 (Comm)

Summary

The English Court allowed the Republic of Kazakhstan to amend an application to set aside permission to enforce under the New York Convention, as it found that there was a sufficiently strong prima facie case that the original arbitral award had been materially affected by the dishonest representations made by the Claimants in the underlying arbitration. In doing so, the Court clarified the applicable principles relating to public policy and fraudulent behaviour and considered the effect that two decisions in the Swedish and US courts on the same issue, in which the State had been unsuccessful, had on the present application.

The State then commenced proceedings in the English Commercial Court to amend its application to set aside permission to enforce the award, to include the grounds of fraud.

Background to the judgment

The backdrop to this judgment is a Stockholm Chamber of Commerce (**SCC**) arbitration commenced in 2013 pursuant to the Energy Charter Treaty (**ECT**) by two individual investors (the **Claimants**) against the Republic of Kazakhstan. The Claimants claimed compensation in relation to the State's actions concerning their investment in a liquefied petroleum gas plant (the **Plant**). They were ultimately awarded US$500m in damages, and received permission to enforce the award in England and the US under the New York Convention.

The State then brought a series of challenges to the arbitration award, including set aside proceedings in Sweden, and a challenge to enforcement in the US. It concurrently applied for and successfully obtained a third party disclosure order in the US, which revealed documents relevant to the estimated value of the Plant which had formed the basis of the award. The State attempted to rely on these documents to challenge the award on the grounds of fraud in both Sweden and the US, but was unsuccessful in both.

The State then commenced proceedings in the English Commercial Court to amend its application to set aside permission to enforce the award, to include the grounds of fraud.

The dispute

This case turned on the value of the Plant, on which both parties had made submissions during the arbitration, and which the Tribunal took into account when assessing the quantum of damages. The Claimants had argued that the Plant should be valued as a going concern,

based on their alleged spending of US$245m on it. The State's case was that the Plant should be valued as scrap because, they argued, the project behind it had failed. Ultimately, the Tribunal had decided to base its valuation assessment on an acquisition bid made in 2008 by KazMunaiGas (**KMG**) an oil and gas company controlled by the State, of US$199m (the **KMG Bid**).

The State claimed that the new third party disclosure obtained revealed that the US$245m figure was fraudulently inflated and not representative of the Plant's true value. It contended that the new documents showed that a substantive part of the figure had been ascribed to equipment which had been delivered to the Plant but not yet incorporated. It also argued that the figure took into account equipment which had been separately purchased at a far lower cost; and a fee for management services which had never been received. In turn, it claimed, these figures had been considered by KMG in making the KMG Bid. The State concluded that the Tribunal's award had been affected by the Claimants' dishonest submission and permission to enforce should therefore be set aside.

The Court will normally look to see whether "some form of reprehensible or unconscionable conduct has contributed in a substantial way to the obtaining of the award" when considering whether an award has been obtained by fraud or the way in which it was procured is contrary to public policy.

What the Court took into account

Knowles J of the Commercial Court summarised the relevant principles that apply when a party is seeking to set aside the enforcement of an award on the grounds of fraud or public policy. These include the following:

- Under the Arbitration Act (section 103(1) and (3)), enforcement of a New York Convention award can be refused where it would "*be contrary to public policy to recognise or enforce the award*".
- This public policy exception is confined to the public policy of England in maintaining the fair and orderly administration of justice.
- The Court will normally look to see whether "*some form of reprehensible or unconscionable conduct has contributed in a substantial way to the obtaining of the aw*ard" when considering whether an award has been obtained by fraud or the way in which it was procured is contrary to public policy.
- Considerations of public policy should be approached with extreme caution.
- For the English Court to allow a party to pursue a claim that a New York Convention award was obtained by fraud at trial, they should normally fulfil two conditions:
  - Firstly, "that the evidence to establish the fraud was not available to the party alleging the fraud at the time of the hearing before the arbitrators"; and
  - Secondly, that "there is a prima facie case of fraud which is sufficient to overcome the extreme caution of the court when invited to set aside an award on the grounds of public policy".

..there was a sufficiently strong prima facie case that the Claimants' representations as to the value of the Plant had materially influenced the Tribunal and the outcome of the arbitration.

Knowles J held that, if the amount of the KMG Bid was the result of a dishonest representation of the Claimants, then there would be a prima facie case that the Tribunal's ultimate valuation assessment would have been affected by this as well, and that there would have been a fraud on the Tribunal.

In analysing the impact of the State's unsuccessful challenges in other jurisdictions, Knowles J rejected an argument that State was estopped from relying on the fraud. He considered that neither the US or Swedish courts has determined the issue as to whether the alleged fraud had in fact occurred and whether this had impacted the Tribunal's decision. He added, obiter, that even of these courts had determined the issue, the English Court would still need to make a decision on the grounds of English public policy.

The Court also rejected an argument that the State had access to the relevant evidence during the arbitration, and found that the documents in question should have been disclosed by the Claimants.

In view of the above, Knowles J concluded that there was a sufficiently strong prima facie case that the Claimants' representations as to the value of the Plant had materially influenced the Tribunal and the outcome of the arbitration. He granted the State permission to amend its application to set aside permission to enforce. The issue will now proceed to trial.

Comment

In juxtaposing the decisions reached by different Courts in consideration of the same factual matrix, this judgment throws light on the English Court's broad approach to issues of public policy. It is an interesting reminder of the relevant principles that apply when a party is seeking to set aside the enforcement of an award on the grounds of fraud or public policy. It also provides comfort that, when it comes to a suggestion that one of the parties has potentially acted fraudulently, the English Court will not hesitate to thoroughly re-assess the facts and issues at hand even where separate courts have already carried out that exercise.

Canelle Goldstein, Hong Kong

English Court confirms the high hurdle that needs to be jumped if a party wants to enforce an award that has been set aside by the Courts where the arbitration took place – in *Nikolay Viktorovich Maximov* v. *Open Joint Stock Company* [2017] EWHC 1911 (Comm)

Summary

The Claimant applied to the English Commercial Court to enforce a USD 150 million award of the International Commercial Arbitration Court of the Chamber of Commerce and Industry of the Russian Federation (**ICAC**), which had been set aside by an order of the Moscow Commercial Court that had been upheld on appeal. Whilst the Russian Courts' judgments were arguably wrong on a number of points of fact and law, it was held that they were not so wrong as to constitute evidence of bias or lack of good faith on the part of the Russian Courts. The English Court was compelled to recognise the judgment of the Russian Courts and refused to enforce the arbitral award.

Background

The arbitral proceedings concerned a claim by Russian billionaire Nikolay Maximov arising in connection with the calculation of the purchase price of the controlling shareholding in his business, OJSC Maxi-Group, which he had sold to the Defendant, global steel producer NMLK.

In February 2011, four months after the last of three oral hearings of the arbitral claim, NMLK issued a counterclaim alleging fraud and breach of contract. The tribunal refused to hear the counterclaim, giving NMLK's extreme delay as its reason, and noted that NMLK had the right to file a claim on these grounds in separate proceedings instead.

Ultimately, in an award handed down on 31 March 2011, the tribunal, formed of what the English Court described as "*three distinguished Russian arbitrators,*" resolved the dispute in Maximov's favour, valuing the shareholding at c. RUB 9 billion (USD 150 million).

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However, NMLK launched several challenges in a number of fora:

- the first was a claim in the Russian Commercial Court that the Sale and Purchase Agreement that was the subject of the dispute and which contained the relevant arbitration clause was null and void as it had been procured by fraud. After losing at first instance, NMLK appealed the decision;

- the second was an application to the ICAC that the arbitrators should be recused on the grounds of their delay in making the award. This application was refused;

The Claimant applied to the English Court to enforce the ICAC award pursuant to the New York Convention and at common law.

- the third, upon the award being rendered, was an appeal to the President of the Chamber of Commerce and Industry of the Russian Federation (**CCI**). This was refused on the basis that the CCI was functus following the rendition of the award.

- finally, NMLK applied to the Russian Commercial Court to set aside the award on the grounds that two of the arbitrators had failed to disclose links to Maximov's expert witnesses in the arbitration.

The ruling of the Russian Commercial Court to set aside the award

Substantial written submissions were filed by both sides. After a five hour hearing, the Russian judge gave an immediate oral decision, as she was required to do by Russian law, setting aside the arbitral award.

In the written reasons that followed, the judge based her decision on three grounds, only one of which (the non-disclosure ground) was raised by the parties during the hearing. The two additional grounds related to (i) public policy considerations and (ii) the non-arbitrability of the dispute.

The judgment was upheld on appeal by the Federal Appeal Court. The Supreme Appeal Court refused permission to appeal on paper. In the meantime, NMLK's application for the SPA to be set aside was allowed on appeal, with the result that, if Maximov could not enforce the arbitral award in his favour, he had no route by which to recover the purchase price for his shareholding in OJSC.

Application to the English Court to enforce the award

the fact that three courts (the Russian Commercial Court, Appeal Court and Supreme Court) had each determined that the award should be set aside set the bar even higher for the Claimant to establish bias

The Claimant applied to the English Court to enforce the ICAC award pursuant to the New York Convention and at common law.

It was common ground between the parties that in order for the English Court to grant the application to enforce the arbitral award, it would have to refuse to recognise the judgments of the Russian courts setting the award aside.

The test applied by the English Court was whether the Russian decision was "*so wrong as to be evidence of bias, or be such that no court acting in good faith could have arrived at it.*"

In the absence of evidence of actual bias or corruption on the part of the Russian Courts, the Defendant argued that the English Court should infer bias from the perverse/incorrect nature of the Russian Courts' conclusions.

Following *OJSC Bank of Moscow v Chernyakov* [2016] EWHC 2583 (Comm) and *Erste Group Bank AG (London) v JSC (VMZ Red October)* [2013] EWHC 2926 (Comm), it was held that it was insufficient for the foreign court decision simply to be manifestly wrong or perverse, in order for the English Courts to refuse to recognise it.

In reaching his decision that the Russian judgments were not so wrong as to indicate bias or a lack of good faith, Burton J determined as follows:

- the fact that three courts (the Russian Commercial Court, Appeal Court and Supreme Court) had each determined that the award should be set aside set the bar even higher for the Claimant to establish bias.

- there was no evidence of actual bias on the part of the Russian Courts. This was despite (i) the submissions of expert witnesses as to Russian law that the state might have had a vested interest in overturning the high value transaction, on which very little taxation has been paid, and (ii) the fact that a letter had been sent to the Russian Courts by the offices of the Russian President and Prime Minister for NMLK, which, it was suggested, might have influenced the Court by demonstrating that influential people were on NMLK's side.

- unfair / misplaced criticism of the arbitrators was more indicative of the general approach of the Russian Courts to arbitration, rather than evidence of bias.

- it was significant that the Russian judge refused to let in the allegations of fraud made by NMLK, which she could have done if she were determined to find against Maximov.

- although there were elements of the decision at first instance that were plainly wrong as a matter of fact and law, relying on grounds that were described as "*unsupportable*," "*hopeless*" and "*adventurous*" respectively, and the decisions of the appellate courts were undeniably "*flawed*," this was insufficient evidence for inferring bias for the purposes of refusing to acknowledge the judgment.

Commentary

Burton J's decision clearly highlights the difficulties a party will encounter where it seeks to enforce an arbitral award that has been overturned by the courts of the seat of the arbitration. This difficulty will increase exponentially where a claimant is unable to produce evidence of actual bias, or any other clear grounds for denying recognition, beyond infelicities, however stark, in the judgment itself. The decision serves as yet another reminder to parties that they should choose the seat of an arbitration very carefully, having close regard to the judicial processes of that jurisdiction in reaching their decision.

Katie Marquet-Horwood, London

The New Flamenco – a dance around the principles of mitigating damages

Summary

The eagerly anticipated Supreme Court decision in *Globalia Business Travel SAU v Fulton Shipping Inc of Panama (The New Flamenco)* [2017] considered the issue of causation when deciding whether an act resulting in a benefit to the claimants should mitigate the loss claimed against the defendants.

Background

The Claimant, the owner of an aging cruise ship, the "New Flamenco" agreed to the terms of a time charter for a period of 2 years with the Defendants. The agreement was governed by English law and provided for arbitration in London.

The Defendants repudiated the time charter by redelivering the vessel early – which the Claimant accepted as a breach of the agreement. The Claimant found it difficult to source a replacement time charter for the vessel and shortly before redelivery of the ship to the Claimant in October 2007, the Claimant entered into an agreement for the sale of the vessel for almost US$24 million.

By November 2009 (when the ship would have been delivered pursuant to the terms of the time charter) the value of the ship had dropped significantly to US$7 million following the financial crisis and a change in market conditions.

The Claimant commenced arbitration proceedings in September 2011 claiming damages for the loss of profit pursuant to the terms of the time charter as a result of the early redelivery of the vessel by Defendants. The Defendants claimed that the Claimant should have to give credit for the higher sale price it received as a result of being able to sell the ship earlier.

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Proceedings and appeals

The arbitration was heard in March 2013 before a sole arbitrator. The Tribunal found in favour of the Defendant and held that the 'benefit' of the higher sale price should be credited to the Defendant, against the Claimant's claim for damages. This amount was more significant than the amount claimed in damages.

The Claimant sought leave to appeal pursuant to s.69 of the 1996 Act, on a question of law: when assessing the loss of profits, are the defendants entitled to take into account, so as to mitigate that loss, a benefit which flowed to the claimants after the repudiation of a contract?

On appeal to the High Court, Popplewell J found .....in favour of the Claimant and that the Claimant did not have to give credit for the higher sale price.

The Court of Appeal then unanimously reversed this decision.

On appeal to the High Court, Popplewell J found that the difference in value was not caused by the breach but by the fall in the market, which would have occurred regardless of the breach of the agreement. He therefore found in favour of the Claimant and that the Claimant did not have to give credit for the higher sale price. Popplewell J listed 11 principles to clarify when a defendant should be credited for a benefit received by the claimant. One of the most important of these principles (which later became the focus of the Supreme Court's judgment) was that it is insufficient for the breach to be merely the occasion for the benefit, it must be the cause.

The Court of Appeal then unanimously reversed this decision. Longmore LJ held that there was one important principle to be taken from the authorities, being that if a claimant adopts a measure which arises out of the consequence of the breach and results in a benefit, this benefit should be brought to account when assessing the claimant's loss. He therefore applied the arbitrators' findings on the facts.

The Claimant appealed this decision to the Supreme Court.

Supreme Court Decision

In another unanimous decision given by Lord Clarke, the Supreme Court upheld the Claimant's appeal and restored the order made by Popplewell J.

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Lord Clarke made clear in his judgment that the essential question is that of causation and that "*the benefit to be brought into account must either have been caused by the breach… or by a successful act of mitigation*". He found that the benefit was caused by the independent decision of the Claimant to sell the ship, which could have been made at any time, including during the performance of the time charter. It had nothing to do with the charterers. Therefore, while the breach may be the occasion for selling the ship, it was not the cause.

He went on to say that the measure of the loss was that of the income stream from the time charter and should therefore be measured as the difference between the contract rate and, in the absence of an available market, what the Claimant ought reasonably to have earned, rather than the Claimant's capital investment in the ship.

The Court rejected the argument that the benefit had to be of the "same kind as the loss" (referring back to no. 8 of Popplewell J's principles). Lord Clarke found that this could potentially be too vague and arbitrary a test. However, on the facts in this case, the potential income stream from the agreement and the capital realisation upon selling the ship were not sufficiently connected, because there was no causal link between the breach and the decision to sell the ship. This is in spite of the fact that the commercial reason for doing so was that there was no work for the ship.

Comments

The Supreme Court's decision confirms that when assessing mitigation the question of causation is crucial. It should provide some peace of mind to businesses wishing to dispose of an asset in similar circumstances. Although it is worth noting that the facts of this case are unusual, therefore the relevance of this case may be limited.

Therefore, while the breach may be the occasion for selling the ship, it was not the cause.

However there are several unanswered questions on the principles of mitigation beyond those relating to causation. For example, the judgment does not deal with the question of whether a benefit of a different kind would ever be considered mitigation for a loss.

Popplewell J at first instance noted that, "[*t]he search for a single general rule which determines when a wrongdoer obtains credit for a benefit received following his breach of contract or duty is elusive*" and the Supreme Court decision has not been able to provide much further clarity. Nevertheless Lord Clarke did endorse the 11 principles cited by Popplewell J, which may assist when considering mitigation.

The case also highlights the difficulties in distinguishing an act post-breach and an act caused by the breach. The fact that the unanimous judgment reversed an appeal from a unanimous Court of Appeal decision, in turn reversing a decision of a High Court on appeal from an Arbitration Tribunal demonstrates that this distinction is not always clear.

Some commentators have also pointed to the apparent tension between the arbitrator's finding of fact in the arbitration (that the decision to sell resulted from the breach) and the Courts' decision reversing that in law. Some have suggested that this was a question of fact and not a question of law capable of appeal under the 1996 Act. However, Popplewell J considered this issue at first instance and found that the arbitrator's finding that the sale was caused by the breach was nonetheless insufficient to establish a causative link in law. The Supreme Court agreed that this was correct.

Layla Sousou, London

To restrain or not to restrain? Application to continue interim injunction restraining the drawdown on performance securities.

A v *B* (2017 EWHC 2055 (QB))

Summary

In March 2017 Sir Michael Burton sitting as a Judge in the Commercial Court was asked to continue an interim injunction restraining the Defendant from making demands on performance securities provided by the Claimant under the terms of 2 construction contracts (the **Contracts**).

While the Contracts provided for disputes to be resolved by way of arbitration, there was a pre-arbitral dispute board procedure that had to be followed beforehand which meant that at the time of the application there was no arbitral institution able to act effectively and in the absence of an arbitrator being available to grant relief, the Claimant applied to the Commercial Court under section 44 of the Arbitration Act 1996.

Background

In early 2016 the Defendant purported to terminate the Contracts and subsequently in September 2016 made demands on the performance securities. The Claimant denied that the Defendant had lawful grounds for termination or was entitled to make the demands and successfully applied to the Commercial Court for ex parte interim relief to compel the Defendant to withdraw its demands and restrain further calls on the performance securities.

The Claimant also referred the disputes in respect of both the Defendant's termination of the Contract and the Defendant's demands on the performance securities to the Dispute Board. In December 2016 the Dispute Board found that:

- None of the conditions precedents for termination by the Defendant had existed at the time the Defendant had served a Notice of Termination and therefore the Termination Order had no legal effect.

- The Defendant's demands on the performance securities had been based on the Defendant's incorrect belief that it had lawfully terminated the Contract. There was no entitlement to terminate and no entitlement to make a demand on the Guarantee. By making a claim under the performance securities for amounts it was not entitled to under the Contract, the Defendant was acting contrary to the provisions of the clause 4.2.

At the return date hearing Sir Michael Burton Court had to decide whether to continue the interim injunction.

The Court had to consider the following significant terms of the contract:

an arbitration was not yet underway ....therefore the application was made to the Commercial Court under section 44 of the Arbitration Act 1996 for interim relief.

- Clause 2.5 which set out the process the Defendant should follow if it believed it was entitled to a payment in connection with the Contracts.
- Clause 4.2 which required the Claimant to obtain the performance securities for the benefit of the Defendant (performance securities are frequently used in construction contracts as a form of guarantee that imposes a primary obligation on the issuer to pay the beneficiary on its first demand for payment). Clause 4.2 also provides that the Defendant shall not make claims on the performance securities except for amounts which the Defendant is entitled.
- Clause 20.4 which says that if a dispute arises in connection with the contract then it should be referred to the Dispute Board (appointed in accordance with the contract) and that the Decisions of the Dispute Board "*shall be binding on both Parties, who shall promptly give effect to them unless and until (they) should be revised in an .. arbitral award*." It also provides that if a party is dissatisfied with a Dispute Board decision it could give notice of its intention to commence arbitration.

The key issues that the Court had to decide

- Whether it was appropriate for the English Court to grant a remedy under section 44 given the seat of the intended arbitration was in Paris.
- The construction of clause 4.2 and whether it was sufficient that the Defendant believed that it was entitled to sums due under the Contract.
- The effect of the Dispute Board decisions.

Was it appropriate for the English Court to act?

..the most significant factor in establishing the appropriateness of the Court granting interim relief in order to 'hold the fort' until a foreign arbitration was underway was to consider the availability of another forum to do so.

It was common ground between the parties that the most significant factor in establishing the appropriateness of the Court granting interim relief in order to 'hold the fort' until a foreign arbitration was underway was to consider the availability of another forum to do so. The issue was whether such relief was available from the French courts (which would be the appropriate forum if it was given the seat of the Arbitration was to be Paris.) The Claimant's expert contended that the French Courts had no jurisdiction to grant interim relief whereas the Defendant's expert contended that it did. Both parties produced opinions by French law experts. The Judge felt that he couldn't resolve this issue although he said he preferred the Claimant's view. He did however find that there was a connection to England given the bank that issued the performance securities was in London and therefore "*easily amendable to the Court's order*." This is he said was "*relevant to the appropriateness of granting the remedy*."

Should the Court interfere in well-established banking practices?

It was common ground that under English law the Court should only gingerly interfere with the well-established international banking practices exemplified by the performance securities in this case. The only circumstances in which the Court will interfere are:

1 The 'fraud exception' – i.e. when the demands are fraudulent; or

2 The "contractual preclusion" - where the presentation of the demand by a defendant is actually in breach of the conditions under which the security was issued.

The Judge noted that there is a wealth of case law regarding the need, even at the interlocutory stage, for 'established fraud'. The position was most recently described by the Privy Council in *Alternative Power Solution Ltd* v *Central Electricity Board* [2015] 1 WLR 697 as "*it must be clearly established at the interlocutory stage that the only realistic inference is (a) that the beneficiary could not honestly have believed in the validity of its demands under the letter of credit and (b) that the bank was aware of the fraud*."

There are also a string of decisions in relation to the test for a 'contractual preclusion' defence where it was found that there was a need for a "*strong case*" or that it has to be "*positively established*" that the party was not entitled to draw down under the underlying contract.

There was no allegation of fraud in this case in relation to the original presentation of the demand and so the Judge had to decide if a 'contractual preclusion' applied. The Claimant argued that clause 4.2 should be construed as being that sums claimed under the demand **must be due** and **not simply believed to be due** and that there can be no claim under the performance securities unless the procedures in clauses 2.5 and 3.5 had been followed establishing the amounts due to the Defendant. The Defendant however argued that the contractual provisions as to the form of the Security that required the Defendant to state that the Claimant was in breach of its obligations was expressly "*without your needing to prove or show grounds for your demand or the sums specified therein*." The Defendant also relied on the indemnity provision at clause 4.2(5) of the contract which provides for when "*the Employer was not entitled to make a claim*."

The Judge found that 4.2 requires only a "bona fide" belief in entitlement and that there was not a strong, or at least strong, case for the Claimant that there is a contractual preclusion of presentation of a demand under the Performance Security.

The effect of the Dispute Board Decisions

The Defendant argued that the fact that, after it had made the call on the performance securities the Dispute Board had found that the Defendant had no entitlement to terminate the Contracts and no entitlement to make the demands, did not matter as there is English authority which makes it clear that if there is no fraud at the time of the presentation the fact that subsequently even an arbitration decision shows that there were no sums due at the time of presentation does not allow a claimant to challenge the drawdown on the basis of fraud.

The Defendant argued that, on the basis the Judge had decided that no contractual preclusion applied, the original injunction order which had required the Defendant to withdraw its demands should be made null and void and of no effect.

However the Court then took into account clause 20.4 which provides that decisions of the Dispute Board are binding on both parties "*who shall promptly give effect to them unless and until (they) should be revised in an .. arbitral award*." The Judge found that it seemed clear that "*in order to promptly put into effect the decision of the Dispute Board, the Defendant must withdraw, and not pursue the demand."* and that he was therefore "*in no doubt that the Defendant is precluded by contract from continuing with their demands. There is a strong – indeed, very strong – case to that effect."*

The order restraining the presentation of the demands was therefore continued but not on the bass of the position as it was before Walker J (who made the original injunction order) but as a result of the Dispute Board's 2 Referral Decisions in December 2016.

Commentary

Without the Dispute Board decisions the injunction would very likely (if not definitely) have been lifted. The fact the injunction was continued because of the Defendant's obligation to comply with the Dispute Board decisions shows the importance of following the dispute board procedures provided for in a contract and the respect and weight the Court will give to such obligations and procedures.

This application also serves as a good example of the role the Court has to play in supporting the arbitration process - especially when a lengthy pre arbitral process has to be followed before a arbitral tribunal can be appointed. In his judgment Sir Michael Burton noted that there was nothing in either side's evidence or submissions about the balance of convenience which he thought was relevant and that *"it is after all.. only a question of holding the ring pending arbitrations which have already been commenced*." This perhaps indicates how aware he was of the fact his decision would only stand until an arbitral tribunal was formed and an application was made to them.

The decision is also an example of how the Courts are reluctant to prevent the call on performance securities unless narrow circumstances apply.

(Addleshaw Goddard acted for the Claimant in this matter.)

"it must be clearly established at the interlocutory stage that the only realistic inference is (a) that the beneficiary could not honestly have believed in the validity of its demands under the letter of credit and (b) that the bank was aware of the fraud."

it has to be "positively established" that the party was not entitled to draw down under the underlying contract.

Daniella Smith, London

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