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ReSolution

TRUST IN MEDIATION

Under New Zealand's new trust legislation, parties can be ordered to participate in alternative dispute resolution p 8

It's a lot easier than getting blood out of a stone
Using the Construction Contracts Act to get paid p 19

The treasure of the San José
Arbitration over shipwreck with $20B of treasure p 29

Simplicity over Complexity
UK Supreme Court rules on arbitration agreement p 34

From the Editor

Tēnā koutou katoa

Welcome to the 42nd issue of ReSolution.

Our work at NZIAC and NZDRC in this final quarter of 2024 is as busy as ever. NZDRC launched the Grocery Industry Dispute Resolution Scheme in September and presented a webinar on the scheme jointly with the Commerce Commission via the Food and Grocery Council at the end of October. On 1 October, NZDRC took over responsibility for the Domain Name Commission's .nz domain name dispute resolution scheme. We've already completed one case, and others are underway.

Also in October, NZIAC hosted a delegation from the Institute of Anti-Corruption Studies at Shenzhen University. They were interested in our low rates of corruption and how we achieve this in New Zealand. We remain invested in promoting New Zealand as a high-quality and trustworthy rule-of-law-based, neutral venue for international dispute resolution.

We've participated in two Auckland Chamber of Commerce webinars - one on the 'ABC' of ADR and another on cross-border disputes. This followed the Building Disputes Tribunal webinar 'Getting Blood out of a Stone' regarding using the Construction Contract Act adjudication process to get paid. In November, the BDT was an exhibitor at the Asian Construction Expo in Manukau with strong interest from attendees.

On 28 November, panellist Polly Pope presented a webinar 'Construction Insolvency', with a cameo by me!

ReSolution Issue 42 continues our work bringing together a broad range of topics from around the globe. In our feature article, Kate Holland explores a recent batch of decisions on the newish ADR provisions in the Trusts Act 2019. These tell us that ADR can do a lot to lessen the burden of complicated disputes. Elsewhere in the issue, Sam Dorne looks at an arbitrator's discretion to award costs, Alexander Lyall outlines how we can spot apparent bias in arbitration, and Favour Lawry goes over why adjudication might be the best bet for your construction dispute.

I wish to take this opportunity to thank all those who have contributed to this issue of ReSolution. We are grateful for the support we receive from dispute resolution professionals, law firms, authors and publishers. We are delighted to be able to share world-class articles to bring a more comprehensive understanding of law and evolving trends in domestic and international dispute resolution. Contributions of articles, papers, and commentary for future issues of ReSolution are always welcome.

I do hope you find this issue interesting and useful. Please feel free to distribute ReSolution to your friends and colleagues – they are most welcome to contact us if they wish to receive our publications directly.

Ngā mihi nui, nā
Michael Jamieson
Editor

ReSolution is the quarterly journal of NZDRC and NZIAC, published online each February, May, August, and November. ReSolution contains a wide variety of articles on dispute resolution covering topics relevant to both the domestic and international markets, across a broad spectrum of dispute resolution practices.

Copies of our previous editions can be found on our websites:
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In this issue

Regulars

Articles

“The scheme enables quick, cost-effective resolution of disputes worth up to $5 million between suppliers to and wholesale customers of the regulated grocery retailers"

ReSolution *in Brief*

Grocery Industry Dispute Resolution Scheme Launched

The New Zealand Dispute Resolution Centre (**NZDRC**) is proud to have been selected to provide this scheme for the grocery industry, and to have it available for use from 5 September 2024.

The scheme enables quick, cost-effective resolution of disputes worth up to $5 million between suppliers to and wholesale customers of the regulated grocery retailers: Foodstuffs North Island Limited, Foodstuffs South Island Limited and Woolworths New Zealand Limited and their related parties, including franchisees; and suppliers of groceries under the grocery supply code or wholesale customers for groceries under the wholesale access regime in the Act. All regulated grocery retailers must comply with the scheme's rules.

The available processes are mediation and adjudication, both of which are private and confidential. A tikanga-based option is available on request.

The scheme takes effect under the Grocery Industry Competition Act 2023 (the **Act**) and the Grocery Supply Code 2023, and the rules of the scheme.

Details regarding the scheme can be found on the NZDRC website via: www.grocerydispute.co.nz. Also, the webinar we presented with the Commerce Commission on 31 October 2024 will be available on the Food and Grocery Council website www.fgc.org.nz.

We are delighted to be working with the Minister of Commerce and Consumer Affairs and the inaugural Grocery Commissioner, Pierre van Heerden, to assist the industry participants to resolve their disputes efficiently.

We look forward to working with grocery suppliers, wholesale customers, the regulated grocery retailers and other stakeholders to make the scheme successful.

NZDRC Administers the .nz Dispute Resolution Scheme for the Domain Name Commission

From 1 October 2024, NZDRC

is administering the .nz Dispute Resolution Scheme on behalf of the Domain Name Commission, a subsidiary of InternetNZ. We are delighted to have been selected for this new role, which underscores the NZDRC's commitment to providing reliable and effective dispute resolution services.

This scheme enables parties to quickly and cost-effectively resolve disputes regarding who the holder of a registered domain name should be. The claimant can choose between mediation or expert determination.

More information on the scheme is available on our website at www.domainnamedispute.nz.

"We are honoured to take on this responsibility from the Domain Name Commission and are dedicated to providing an enhanced scheme to the Domain Name Commission for the benefit of all stakeholders," said Michael Jamieson, NZDRC's Commercial Manager.

The transition has involved refreshing the scheme's rules, including a tikanga-based option and accessibility options.

Domain Name Commissioner Barbara Pearse said,

> We are thrilled that the NZDRC will administer the .nz Dispute Resolution Scheme. We want to ensure .nz is world-class, and we have chosen the NZDRC based on their extensive experience and established presence in the market. Their proven track record in implementing a tikanga-based approach within other administered schemes is of particular significance to us as a regulatory body in Aotearoa. We look forward to working with them to serve the needs of our evolving market.

ReSolution writer visits CIETAC in Beijing

In August, ReSolution author and research clerk for NZDRC and NZIAC, Alexander Lyall, visited the China International Economic and Trade Arbitration Commission (**CIETAC**) office in Beijing.

During the tour, Alex and the CIETAC hosts, Ms Yahan Lu and Ms Tao Li, discussed some of the latest developments in global arbitration, including the proposed amendments to the Arbitration Law of the People's Republic of China.

The group also discussed the status of the Southern Link. The Southern Link is a proposed project that would seek to take advantage of New Zealand's physical location, sitting between Asia and South America. The group agreed that CIETAC and NZIAC could work together to develop the idea.

The visit will hopefully be a first of many between the two organisations. In April 2024, CIETAC and NZIAC/NZDRC signed a Memorandum of Understanding (**MoU**) in Auckland for the purpose of mutually developing best-practice dispute resolution.

Indonesia officially applies to become member of CPTPP

In a long-anticipated move, Indonesia has officially applied for membership of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (**CPTPP**).

In September, Airlangga Hartarto, Indonesia's Coordinating Minister for Economic Affairs, announced that the ministry had delivered the application letter to New Zealand. As the CPTPP's depositary member, it is standard practice for New Zealand to receive the application letters of prospective members.

The ministry of economic affairs has acknowledged that the application process will be lengthy. The United Kingdom, the newest member, spent over two years negotiating the terms. The process for Indonesia is likely to be of a similar length. Indonesia will need to consider policies in relation to their top exports – oil, electrical appliances and rubber products.

If successful, Indonesia will join the "CPTPP 12" – Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United Kingdom and Vietnam.

The CPTPP 12 are currently considering the application of a further seven countries (see page 11 of ReSolution Issue 36 to read more about the application from Uruguay). For a State to be accepted into the bloc, each of the 12 must accept the application.

Making history: free trade deal with the United Arab Emirates one of New Zealand's fastest trade negotiations

Four months after formal negotiations began in May 2024, New Zealand struck a Comprehensive Economic Partnership Agreement (**CEPA**) with the United Arab Emirates, one of New Zealand's biggest markets in the Middle East. The CEPA eliminates duties paid on 98.5% of New Zealand exports to the United Arab Emirates, rising to 99% within three years.

The deal is a welcome move for farmers, manufacturers, and investors alike. Key exports to the United Arab Emirates include dairy, industrial products, red meat, horticulture, and travel services. In turn, key imports from the United Arab Emirates are plastics, carpets, travel services, and glass.

Of note is a dedicated cooperation chapter in the CEPA on Māori interests. The chapter reflects opportunities for Māori and protects and promotes Māori and Indigenous resources, traditional knowledge, cultural expressions, names, and uses of plants, including mānuka. In line with other agreements, the CEPA includes New Zealand's Treaty of Waitangi exception to ensure the country meets its treaty obligations. The CEPA also contains a trade and sustainable development chapter, which speaks to labour rights, climate change and women's economic empowerment.

Overall, the deal marks a significant milestone in fostering relations, providing certainty for traders, and creating new opportunities for both nations.

TRUST IN MEDIATION

Written by **KATE HOLLAND**

Under New Zealand's new trust legislation, parties to certain trust disputes can be ordered to participate in alternative dispute resolution (ADR), such as mediation and arbitration. We now have several High Court decisions demonstrating the Court's strong support for the advantages of mediation and providing guidance on the factors the Court will take into account in exercising this discretion. We also have the Court's first decision ordering parties to refer their trust dispute to arbitration.

Use of ADR under the Trusts Act

The Trusts Act 2019 (the **Act**) came into force in 2021. It brought a number of significant changes to trust law and was the first major reform in 70 years. One of the most significant and novel developments in the Act is its express provision[1] for ADR processes, such as mediation and arbitration, to resolve trust disputes.[2]

Trust disputes – 'internal' vs 'external' matters under the Act

The Act divides trust disputes into two broad categories: external trust matters and internal trust matters.[3]

1 Sections 142–148 of the Act.
2 Disputes about the validity of all or part of a trust cannot be referred to ADR.
3 "Matters" include legal proceedings or disputes which may lead to legal proceedings.

- **Internal trust matters** are disputes which arise between trustees, or between a trustee and a beneficiary.
- **External trust matters** are disputes between a trustee and an external third party (a party who is not (or is not acting in their capacity as) a trustee or beneficiary of the trust.

Section 145 compulsory referral to ADR (internal matters only)

Section 145 of the Act gives the Court the power to compel parties to an internal matter[4] to use ADR, even if some are reluctant or refuse to attend.

The Court can make this order on the application of a trustee or beneficiary, or of its own accord. It can also appoint who the mediator or arbitrator will be, and it can order that the costs of using ADR will be paid from the trust fund.

There are two primary questions the Court will address when faced with a section 145 application:

1. Is there jurisdiction to order ADR?

   The Court must first determine whether it has jurisdiction under section 145 to order the parties to mediate (or arbitrate), that is, whether the dispute is an internal matter and whether there is anything in the trust deed preventing referral to ADR.

2. Should the Court order ADR?

   Once jurisdiction to make a section 145 order is established, the Court will consider whether it is appropriate in the circumstances to exercise its discretion and order the unwilling party to attend mediation.

When will the Court order parties to use ADR? The caselaw so far…

It is now almost four years since the ADR provisions in the new Act came into force, and the case law on Court-ordered ADR is beginning to emerge. In each of the cases so far, the ADR had been requested by a party to existing legal proceedings before the Court.

The Court has ordered the parties to mediate in around half of these applications. But even where it has declined to exercise the discretion, the Court has repeatedly expressed its high regard for the suitability and advantages of ADR in resolving trust disputes, and given detailed reasoning explaining why mandatory mediation would not be appropriate in the particular circumstances.

S v N – consideration factors

The first case on section 145 to come before the Court was *S v N*.[5] Wylie J stated that in exercising its discretion to compel parties to mediate, the Court must be mindful of the wishes of the parties and the underlying circumstances and history.

Wylie J set out a non-exhaustive list of relevant factors,[6] which the Court has repeatedly referred to in subsequent section 145 decisions:

- cost
- confidentiality
- speed
- seriousness and complexity of the matter
- suitability of the proposed mediator
- wishes of the parties
- wishes of the settlor (if known)
- finality
- enforceability
- utility.

Having considered some of these factors and identified some unusual circumstances of this case, Wylie J declined to order the unwilling party to mediate.

Wright v Pitfield – if you take a horse to water it usually does drink

In *Wright v Pitfield*,[7] the Court had little difficulty in ordering the reluctant party to mediate.

Venning J confined the outcome of *S v N* to its unusual circumstances,[8] and pointed out that by enacting section 145, Parliament specifically intended to force unwilling parties to mediate. He noted that mandatory mediation is common in other jurisdictions, including New South Wales, and referred to a speech by Lord Phillips on its success rate:[9]

> Those opposed argue that compulsion is the very antithesis of mediation. The whole point of mediation is that it is voluntary. How can you compel parties to indulge in a voluntary activity? You can take a horse to water but you cannot make it drink. To which those in favour of compulsory mediation reply 'yes but if you take a horse to water it usually does drink.' Statistics show that settlement rates in relation to parties who have been compelled to mediate are just about as high as they are in the case of those who resort to mediation of their own volition.

He further pointed out that while an order under section 145 forces a party to *attend* mediation, it does not force that party to *resolve* matters at the mediation.

He identified that in the current case, mediation may resolve more issues than the main proceedings would, avoid costs and preparation costs of the hearing and maintain commercial confidentiality.[10] He concluded that *with appropriate assistance, the issues between* [the parties] *should be capable of sensible resolution*.

In an addendum to the decision, Venning J noted that the mandatory mediation had resulted in successful settlement of all issues between the parties.

Terry v Terry – agreement on the issues to be mediated?

In *Terry v Terry*,[11] Johnson J had high praise for the use of mediation to settle trust disputes:

> When approached in the appropriate manner by all participants, mediation convened by a skilled mediator tends

Mandatory mediation

→ The High Court has now issued several decisions compelling unwilling parties to try mediation to resolve their trust disputes.

4 The Court does not have the power to order ADR for external matters, nor if the trust deed precludes ADR.
5 *S v N* [2021] NZHC 2860. The case concerned resettlement of trust assets of former spouses.
6 *S v N*, above n 5 at [29] referring to Andrew Butler, *Arbitration of Trust Disputes under the Trusts Act 2019* [2021] NZLJ 106, and at [35].
7 *Wright v Pitfield* [2022] NZHC 385. The case concerned the control and sale of trust assets of former spouses (including the sale of a company) and removal of trustee.
8 There was a protection order in place preventing the party requesting mediation from contacting the unwilling party, they had already agreed by consent orders that the issues would be decided by independent trustees, and the Judge considered the requesting party was using the application for mediation as a further delaying tactic.
9 Lord Phillips, Lord Chief Justice of England and Wales *Alternative Dispute Resolution: an English Viewpoint* (India, 29 March 2008).
10 The underlying issues involved the valuation and proposed sale of a company.
11 *Terry v Terry* [2023] NZHC 884. The case concerned mirror trusts owning a farm run by a mother (a settlor) and one of her four children, following the death of their father (a settlor). The mother and son had fallen out over management of the farm. The son sought removal of his mother as trustee.

to resolve a high percentage of cases of all sorts, from the heaviest commercial disputes through to the most trivial matters. And, where successful, mediation is almost always a more efficient process than going to trial. There is every reason then why the Court should encourage use of the process, and the legislation has recognised this in enacting ss 142-148.

However, he saw no realistic prospect of settlement in the circumstances, and declined to order the mediation. This was primarily because the beneficiary bringing the main action (removal of trustee) and requesting mediation had made it clear that his real intention was to have the trust assets distributed to him. This 'disguised' issue of distribution was not the issue in the main action and it was something the trustees had no intention of engaging in at mediation.

Wiggins v Wiggins – will all parties be in the room?

In *Wiggins v Wiggins*,[12] Churchman J refused to order mediation because a third party company involved in the dispute would not be a party to the mediation, and without that company's agreement, a final and enforceable settlement could not be reached. In those circumstances, the Court considered ordering mediation at that stage would be premature and futile, and waste costs.

Gatfield v Hinton – orders for mediation and arbitration

In *Gatfield v Hinton*,[13] the Court not only compelled two reluctant beneficiaries (the plaintiffs in the main action against a trustee) to mediate; it also ordered that if the mediation was unsuccessful then the dispute must be determined by arbitration, and appointed the arbitrator. Both orders were made on the application of the trustee who was the defendant in the main proceedings.

Order for mediation

Lester J noted that just because the trustee now requesting mediation had previously turned down offers of ADR, this was not a barrier to her requesting it now:

> People's views of a dispute change. Sometimes the benefit of independent advice leads a party to reflect on their part in the dispute and on the desirability of resolution.

The Court stated that *one of the key advantages of ADR* …[is] *it is a quicker and cheaper process than commercial litigation* and repeated the benefits of ADR described in *Terry v Terry* above, attaching high importance to the confidential nature of mediation and arbitration in family trust disputes:

> There is a general confidentiality interest in family matters bring dealt with privately… I consider the desirability of family matters being dealt with confidentiality to, on balance, favour ADR.

Lester J explained that unlike in *Terry v Terry*, the parties here agreed on which matters were in dispute and the trustee wanted to mediate the very issue the resisting parties were pursuing in the main proceedings.

He also pointed out that some of the outcomes which the plaintiffs were seeking in their pleadings could in fact only be achieved by mediation,[14] noting that *mediation can explore non-monetary outcomes* …and *is aimed at addressing the parties' interests and not necessarily their strict legal rights*.

> One of the advantages of ADR is that, at least as regards mediation, the parties are not necessarily tied to pleadings when exploring issues and outcomes … at ADR a wide range of issues can be addressed, not necessarily only those in a pleading.

Unlike in *Wiggins v Wiggins*, in the present case all other persons (the other beneficiaries) whose agreement was required to make a mediated settlement final and enforceable were willing to attend.

Lester J further noted that:

> even if an overall settlement is not reached, the reality is that a mediation serves the secondary purpose of being an issues conference… If mediation is not wholly successful, then there will be some cost saving in terms of the issues being narrowed.
>
> A skilled mediator will get the parties to critically examine the assumptions that underpin their [view] of the merits of their positions. It is also not uncommon for mediation to result in a solution that neither party has contemplated.

The judge noted his view that the reluctant parties were *unrealistically pessimistic at what can be achieved at a well-run mediation*, and in response to their objection that confronting the trustee would be "psychologically unsafe" for them, he reassured them that *a skilled mediator can deal with the emotion in this case*.

Order for arbitration

On the application for referral to arbitration (if mediation were unsuccessful), Lester J agreed that an arbitrator would be able to exercise the same jurisdiction as a High Court judge, including any inherent jurisdiction. He added that:

> All the interlocutory applications available in this Court are available in arbitration but can be dealt with more quickly in arbitration. That also creates cost savings. Interlocutory issues are dealt with by the final decision maker, creating a practical incentive for the parties to demonstrate that they are adopting a reasonable approach to the litigation as their whole conduct of the litigation will be under the scrutiny of the final decision maker.

Lester J noted several advantages of arbitration over litigation, including that that *the parties would be lucky to get a* [Court] *hearing in 2026* and by rejecting ADR, the unwilling parties *are saying they prefer approximately two years of complicated and expensive litigation*. Whereas, if they used arbitration, they would avoid Court filing *fees of approximately $33,600*, *have a choice of venue and hearing date* and *likely see the matter determined before the end of the year*.

The Court acknowledged that the losing party may be exposed to potentially higher costs in arbitration than in the Court, in the event that the arbitrator orders them to pay the arbitrator's fee. However, Lester J noted that this is a shared risk for each party and in his view should not carry significant weight because it is a risk inherent in the section 145 ability to order arbitration.

Lester J ordered the parties to attend mediation, and if the mediation was unsuccessful, appointed an arbitrator to conduct an arbitration.

Leave to appeal and stay of mediation and arbitration orders

The unwilling parties applied for leave to appeal the decision and requested a stay of the orders for mediation and arbitration pending the appeal.

Lester J granted the stay of the order for arbitration pending the application for leave to appeal, but denied a stay of the mediation, and ordered that it proceed as scheduled.[15]

Lester J found there was no prejudice to the unwilling parties in attending the mediation:

> If settlement is reached, all well and good. If settlement is not reached, then at least the parties will have had an opportunity to explore the issues in this proceeding with the benefit of input from the mediator, a senior King's Counsel, who will help them test the assumptions that underlie their positions.

The parties attended the mediation. However, it was unsuccessful.

In September 2024,[16] Lester J held it was appropriate to grant the application for leave to appeal to the Court of the Appeal given the lack of existing authorities on the new section 145 power to order arbitration.

Addleman v Lambie Trustee Limited – disclosure before mediation?

In *Addleman v Lambie Trustee*

12 *Wiggins v Wiggins* [2024] NZHC 863. This was a dispute between a brother and sister who were the trustees of their family trust which received income from shares in a family business.

13 *Gatfield v Hinton* [2024] NZHC 1712. The dispute concerned two will trusts and the ownership of a family bach. The plaintiff beneficiaries claimed the defendant trustee had agreed to sell a share in the bach to them but instead sold it to other beneficiaries.

14 The plaintiffs wanted the share in the bach to be transferred to them (from beneficiaries who were not parties to the proceedings), as well as an apology from the trustee.

15 *Gatfield v Pearson* [2024] NZHC 2074.

16 *Gatfield v Hinton* [2024] NZHC 2603.

Limited,[17] Andrew J observed that *Parliament has clearly recognised the significant benefits that ADR might offer in contrast to the expense and damage that adversarial litigation can give rise to*.

In this case the reluctant party was resisting mediation on the basis that the defendant trustee had not complied with court-ordered disclosure of trust information, leaving her unable to be fully informed and advised of her settlement options ahead of the mediation.

Andrew J acknowledged that the parties' position was *polarised and far apart* and that the reluctant party was *handicapped* by the lack of disclosure. However, he reassured her that *there is a clear mechanism within a mediation referral for resolution of outstanding disclosure issues*:

> Disclosure issues will, of course, not be unfamiliar to any experienced mediator… The parties, with the assistance of good counsel and an experienced mediator, are more than capable of designing a process to address outstanding disclosure issues. This might involve a pre-mediation meeting with the mediator. …

Andrew J ordered the mediation and directed that the mediator resolve any disputes regarding disclosure necessary for the parties to attend mediation. He further required that the reluctant party, who is based overseas, should attend in person in New Zealand, not by videoconference:

> In my view, there is a clear need for some honest reckoning in this case which would involve the parties sitting down in the same room and candidly and sensibly addressing their concerns… there is a clear need to try the alternative route of ADR with a view to avoiding the real risk in this case of extreme cost and delay leading to further and irreparable breakdown in the relationship between the parties. ADR potentially presents a wider range of settlement options for the parties and despite what appears to be an intractable dispute, disputes of this kind are not unfamiliar to experienced mediators … Resolution of even some of the issues at mediation may materially reduce the extent of discovery eventually required as well as the length of any trial.

17 *Addleman v Lambie Trustee Limited* [2024] NZHC 1790. The proceedings are part of a long-running dispute brought by a beneficiary (the reluctant party) against her sister, the trustee-beneficiary of a very lucrative family trust. In 2021 the Supreme Court ordered disclosure of all trust accounts and legal advice paid for from the trust fund up to the date of commencement of proceedings.

Innes v Darlow – likelihood of settlement in unmeritorious claims

In *Innes v Darlow*,[18] Paulsen J stated that the Court should be slow to order mediation where the case is *plainly unmeritorious*.

The Court found it could not order mediation in the present case because the dispute was an external matter.[19] As this was not an internal matter, it did not come within section 145.

However, Paulsen J went on to note that in the unusual circumstances of this case, even if it had been an internal matter, he would not order the requesting party's eight reluctant siblings to attend mediation with her.

Paulsen J's reasons included the high costs involved in mediating with such a large number of parties, that the main action claim had no merit and that there was little chance of settlement as the requesting party's conduct and damaging actions against her siblings in previous public litigation meant that she could not now expect them to mediate with her.

Conclusion

Trust disputes are particularly suited to ADR. The arbitration or mediation of trust disputes can help parties to avoid publicly litigating their private matters in the courts.

Litigation in the courts is not only an expensive, stressful and time-consuming option but it also often involves the public disclosure of matters which are inherently personal to the parties. This can include personal information as well as financial and business matters which would otherwise remain confidential.

The emerging case law on mandatory trust ADR clearly shows the Court's recognition of these and other benefits. While most of the cases so far have focused on mediation, we look forward to guidance from the Court of Appeal on the recent orders for mandatory trust arbitration in *Gatfield v Hinton*.

Voluntary agreement to try ADR – internal and external matters

It is well worth remembering that internal trust matters (where all parties to the dispute are acting in their capacity as a trustee or beneficiary) can be referred to ADR without Court involvement,[20] if all of the parties (and all beneficiaries) are willing to attend.

Under the Act, trustees can also refer external matters (disputes with a third party) to ADR if the other party agrees to it. Trustees do not require beneficiaries' consent to use ADR to resolve external matters.

NZDRC provides expert arbitration and mediation services for Trust disputes. We place great importance on effective and efficient dispute resolution processes. Our services cater to various needs, whether you prefer arbitration to avoid court proceedings or mediation to preserve relationships. Our robust and efficient service ensures the best outcomes for parties dealing with Trust disputes. With a high success rate and a reputation for cultivating positive outcomes, NZDRC is a trusted choice for dispute resolution. You can find out more about our trust ADR services on our website.

18 *Innes v Darlow* [2024] NZHC 2614. The case concerned a family trust with nine sibling beneficiaries. The plaintiff claimed a larger share of the trust fund from her siblings because of services she had provided to their parents (the deceased settlors) in caring for them.

19 The dispute was a claim brought by a sibling in her capacity as an alleged creditor of the trust (and therefore, a third party), not in her capacity as one of the beneficiaries.

20 However, if the trust deed includes beneficiaries who are unascertained, minors, or otherwise lack capacity, then the High Court will need to appoint an independent person to represent the interests of those beneficiaries during the ADR process. The Court must also approve any settlement agreement reached.

About the author

Kate Holland works as a Knowledge Manager in The ADR Centre's Knowledge Management Team, working with NZDRC and NZIAC. She previously practised as a solicitor in the UK with an international commercial firm and has particular experience in trust law and succession planning in New Zealand.

ARTICLE

Negotiation stalemate

→ Why a party with a poor case won't accept a rational settlement offer.

They have a hopeless case, so why won't they settle?

Written by **MICHAEL JAMIESON**

Have you ever wondered why the other party won't give up on a case they are almost certain to lose? This article seeks to explain why.

The late Nobel prize-winner Daniel Kahneman and his late research partner Amos Tversky provide the answer. This is set out in part 4 of Kahneman's excellent book *Thinking, Fast and Slow*,[1] which I attempt to summarise in this article. (I hope to do it justice and apologise for the over-simplification!)

Losses loom larger than gains of the same amount

On average, losses feel twice as bad as the positive feelings of a gain of the same magnitude (they range between 1.5 and 2.5 times greater).[2] Imagine your positive feeling if you find a $100 note on the footpath. However, if you lose the $100 note, your negative reaction to the loss will be about twice as strong as the positive feeling of the gain. In other words, you would need to find around $200 (for most people, between $150 and $250) to compensate for losing $100.

This relates to the concept of 'loss aversion' – *we are driven more strongly to avoid losses than to achieve gains*[3] (probably for evolutionary reasons). The reference point can be the status quo (such as current wealth) or a future goal[4] or target (say, a desired settlement amount). Exceeding the target is experienced as a gain, while not achieving the target is experienced as a loss.

This suggests that the more realistic the settlement target is and the less any concession is viewed as a loss, the greater the chances and the higher the utility of settlement.

Decision weights, possibility effect and certainty effect

We over-weight unlikely events and under-weight likely events. Kahneman refers to *decision weights*. For example, people give the probability of a 5% gain a decision weight of 13.2, overweighting it by more than 2.5 times. This is known as the 'possibility effect' – the possibility of a rare event is over-emphasised in our minds.

At the other end of the scale, a 95% probability of a gain is given a decision weight of 79.3: a 5% reduction from a certain outcome feels like a 20% reduction. This is called the 'certainty effect', where highly probable outcomes are under-weighted.[5]

	GAINS	LOSSES
HIGH PROBABILITY (Certain Effect)	95% chance to win $100,000 Fear of disappointment RISK AVERSE Accept unfavourable settlement	95% chance to lose $100,000 Hope to avoid loss RISK SEEKING Reject favourable settlement
LOW PROBABILITY (Possibility Effect)	5% chance to win $100,000 Hope of large gain RISK SEEKING Reject unfavourable settlement	5% Chance to lose $100,000 Fear of large loss RISK AVERSE Accept unfavourable settlement

Diminishing sensitivity to gains and losses

Kahneman invites us to consider two problems.[6] Which option would we prefer in each?

1. Get $900 for sure OR a 90% chance to get $1,000?
2. Lose $900 for sure OR a 90% chance to lose $1,000?

In problem 1, most people are risk averse and prefer the sure thing: subjectively, we value the gain of $900 at more than 90% of the value of a $1,000 gain (even though the expected value is the same for both options, at $900).

In problem 2, most people are risk-seeking and take the gamble: subjectively, the negative value of a $900 loss is more than 90% of the negative value of a $1,000 loss (even though the expected value is the same for both options, at -$900).

Fourfold pattern

The above factors combine to produce Kahneman and Tversky's 'four-fold pattern':[7]

In each quadrant:

- The top row is a possible gamble or outcome.
- The second row is the operative emotion.
- The third row shows how most people act when faced with a choice between the gamble and a sure thing of the same expected value, for example, between a 95% chance of winning $100,000 and $95,000 with certainty.
- The fourth row shows the expected attitudes of parties to a dispute.

The possibility effect influences the bottom row. In the bottom left-hand quadrant, the overweighting of the chance of a large gain explains why we buy lottery tickets and overpay for a very small chance of winning. The bottom right-hand quadrant is where insurance is bought. People overweight the possibility of a large

1 Daniel Kahneman *Thinking, Fast and Slow* (Penguin Books Ltd, 2012) at 269–321.
2 Above n 1, at 284.

3 Above n 1, at 302.
4 Above n 1, at 303.
5 Above n 1, at 315.
6 Above n 1, at 279.
7 Above n 1, at 316–319.

loss and pay more than its expected value to avoid it.

The certainty effect influences the top row. In the top left-hand quadrant, people are risk-averse and will pay a premium to lock in a certain gain.

On the other hand, in the top right-hand quadrant, people are risk-seeking and will gamble to avoid a certain loss now, even at a high risk of a larger loss later.

This is due to (a) diminished sensitivity: a $100,000 loss does not feel much worse than a $95,000 loss; and (b) decision weight: for a 95% chance, the decision weight of 79.3 feels much less than the probability.

This is where bad options and desperate gambles are taken. The small hope of a favourable outcome is magnified, and the high chance of disaster is minimised. As we feel losses more than gains, we are hard-wired to avoid the pain of a certain loss now, and the remote possibility of relief is powerfully attractive.

Consequences for litigation

Kahneman cites work done by legal scholar Chris Guthrie[8] and concludes that a party with a strong case is likely to be risk averse and be attracted to the certainty of a settlement and the avoidance of the (low but magnified) risk of disappointment. Conversely, a party with a weak case will be loss-averse and risk-seeking, prepared to gamble (overweighting the chance of success) rather than accept a certain loss.

As Kahneman says: *In the face-off between a risk-averse plaintiff and a risk-seeking defendant, the defendant holds the upper hand.*[9] This is reflected in negotiated agreements where the plaintiff settles for less than the trial's expected value (expected outcome x probability). It explains why vexatious litigants may win a more favourable settlement than the merit of their case justifies.

It also explains why the other party, with a weak case, won't accept your perfectly reasonable settlement offer!

Unfortunately, you may need to pay 'over the odds' to settle. As a one-off proposition, this may be acceptable, but Kahneman sounds a note of warning.[10] In each quadrant of the four-fold pattern, systematic deviation from the expected return (for example, paying a premium to avoid a small risk of losing) for many similar decisions is expensive in the long run. It leads to sub-optimal outcomes for that party.

8 Above n 1, at 319.
9 Above n 1, at 320.
10 Above n 1, at 320–321.

About the author

Michael is the Commercial Manager of the New Zealand Dispute Resolution Centre.

Michael brings 30 years of legal practise, including 20 years gained in-house, most recently as General Counsel and Company Secretary for a State-owned enterprise.

CCA Payment Claims

Valid payment claims can help get your clients paid in a timely fashion.

It's a lot easier than getting blood out of a stone

Using payment claims and adjudication under the Construction Contracts Act to get paid

Written by **FAVOUR LAWRY**

A booming construction industry is an indicator of a healthy and growing economy. However, for a sector that is heavily cash-flow dependent, the lack of timely payment can stifle growth and be fatal to a business.

The Construction Contracts Act 2002 (Act) is a "pay now, argue later" regime that aims to keep cash flowing through the statutory payment regime and adjudication process. Find out how this works.

What is the payment regime under the Act?

The Act defines construction work very broadly. It includes, for example, building work, maintenance, demolition, design and engineering across projects as diverse as residential homes through to aqueducts so it is accessible to a wide range of contractors, subcontractors and "tradies".

Section 20 of the Act allows a party who has performed construction work under a construction contract to formally demand payment for that work by issuing a valid "payment claim".

If the recipient does not respond to a valid payment claim with a valid "payment schedule" within the timeframe specified in their construction contract (or, if the contract does not stipulate a timeframe, within the statutory default timeframe of 20 working days), then they are liable for the amount specified in the payment claim. This creates what is known as a "default liability", and the payer must pay the amount claimed on the specified due date for payment.

The provisions relating to payment claims and payment schedules are known as the "payment regime".

What constitutes a "valid payment claim" under the Act?

A payment claim must comply with the requirements stated in section 20 of the Act to be valid. The payment claim must:

- be in writing;
- contain sufficient details to identify the construction contract to which the payment relates;
- identify the construction work and the relevant period to which the payment relates;
- state a claimed amount and the due date for payment;
- indicate the manner in which the claimed amount has been calculated;
- state that the claim is being made under the Construction Contracts Act; and
- be accompanied by a written notice outlining the process for responding to the claim and explaining the consequences of not responding if payment of the claimed amount in full is not made by the due date for payment.

Failure to meet these requirements can render the payment claim invalid.

What constitutes a "valid payment schedule"?

If the recipient does not agree with the amount claimed in the payment claim, they must respond with a valid payment schedule. The payment schedule must be in writing and state the amount the other party views as being payable instead. This may be all of the amount claimed, or only part of it (the "scheduled amount").

Section 21 of the Act states that a valid payment schedule must:

- be in writing;
- identify the payment claim to which it relates; and
- state a scheduled amount.

If the scheduled amount is different from the claimed amount then the payment schedule must also indicate:

- the manner in which the payer has calculated the scheduled amount;
- the reasons for any difference between the scheduled amount and the claimed amount; and
- where the difference is because the payer is withholding payment on any basis, the payer's reasons for withholding payment.

If the recipient does not respond or does not pay the scheduled amount they agreed to by the due date for payment, the person claiming the money (claimant) is not at a stalemate because the Act provides a mechanism for speedy dispute resolution and enforcement.

What if the recipient does not provide a valid payment schedule or pay up?

Where a recipient has failed to respond to a payment claim with a valid payment schedule, or pay up, within the required timeframe, the claimant is entitled under the Act to initiate an adjudication claim for payment in full on the basis of default liability.

If the claimant proves that they issued a valid payment claim and that the recipient did not respond with a valid payment schedule, or did not make payment of scheduled amount by the due date for payment, then the adjudicator will make a decision whether 'default liability' exists. That is, whether the recipient of the payment claim is liable to pay the amount claimed based on compliance with the technicalities of the Act. The 'merits' of any underlying dispute between the parties are not relevant. The adjudication process typically takes six to eight weeks.

The recipient must pay the amount ordered by the adjudicator within two working days after the determination is issued. If they don't pay, the determination can be enforced as if it was an order of the District Court. The recipient cannot use arguments regarding the merits of any disputes to delay their payment.

What if the recipient provides a valid payment schedule?

If the recipient of the payment claim responds with a valid payment schedule within the required timeframe, then the amount that they agree is owed (if any) becomes a debt due and owing as above, leaving only the disputed amount at issue.

The claimant can then address the disputed amount through an adjudication 'on the merits' of their claim.

It is not uncommon to see an adjudication claim that argues both default liability claims and claims on the merits.

Conclusion

The power of the Act's payment regime should not be lost on any party to a construction contract or their advisers. Compliance with the statutory requirements for payment claims sets the claimant up for valid enforcement, while non-response exposes the other party to a default liability adjudication determination and a requirement to pay within two working days after that determination is issued.

Even if a valid payment schedule is issued, the adjudication process can quickly and relatively cheaply determine the merits of the dispute. This enables prompt payment of the amounts ordered and gives the parties certainty.

Although a dissatisfied party can appeal to the District Court, in our experience, this happens less than 1% of the time.

When used as intended, the payment regime in the Act provides a pathway to prompt payment and resolution of construction contract disputes.

Template payment claims and payment schedules can be found here.

The Building Disputes Tribunal also provides a fixed fee adjudication service for low value claims of low complexity (claims under $100,000 that involve no more than 3 issues in dispute). You can view our fixed fees here.

To learn more or start the adjudication process see our website.

At the Building Disputes Tribunal, we are always willing to answer any questions you or your clients may have. Feel free to call +64 9 486 7143 or email registrar@buildingdisputestribunal.co.nz and we will be happy to assist you.

About the author

Favour Lawry is a Registrar in The ADR Centre's Commercial team working with the Building Disputes Tribunal, New Zealand Dispute Resolution Centre and the New Zealand International Arbitration Centre. She holds an LLB from the University of Auckland as well as a BA in German and Sociology. She recently joined the ADR Centre after several years in General Practice and has particular experience in the areas of residential property and estates.

ARTICLE

Shifting the focus: New Zealand High Court adjusts the lens in digital media business dispute

Written by ALICE ELCOAT

Background

On 7 July 2020, David Akal (**Akal**) and Nahuel Lukomski (**Lukomski**) partnered with Lucas Marin (**Marin**) to form Mediaflow Limited (**Company**), a digital media business for tourism operators in Queenstown. The Company was structured so that each partner held 33% of the shares and was a director.

One year later, Akal and Lukomski's relationship with Marin began to sour when Marin restricted Akal's access to the Company's software and source code so that he could not assist clients. Marin claimed Akal's *lack of programming experience had previously caused problems* and that he did not need access to the source code to perform his role.[1] In September 2022, the pair withdrew $12,000 from the Company's account without Marin's permission and resigned as directors.

Having become a one-man band, Marin formalised an employment agreement on 12 December 2022 between himself and Mediaflow (**Employment Agreement**). The terms of the contract stipulated that Marin would (a) be paid a gross annual salary of $500,000, (b) receive 12 months' salary in the event of redundancy, and (c) that restraint of trade did not apply upon the termination of his employment.

On 6 June 2023, Akal and Lukomski reappointed themselves as directors of the Company. Not long after their appointment, the pair discovered that the Company had paid Marin $183,076 without their knowledge or approval. Over the next few months, the Company reduced Marin's annual salary to $130,000. By August 2023, Marin had received $269,418.97 under the Employment Agreement. One month later, the Company avoided

1 *Mediaworks Limited v Marin* [2024] NZHC 2369 at [17].

the Employment Agreement under section 141 of the Companies Act 1993 (the **Act**). Marin's new salary was negotiated at $908 per week.

Procedural history

In September 2023, the Company applied, under Akal and Lukomski's direction, for an interim injunction to restrain Marin from withdrawing funds from the Company to prevent it from becoming insolvent. Justice Dunningham dismissed the Company's application on the basis that she was not prepared to consider the matter without notice.

Present application

Over the next few months, tension between the parties continued. On 20 July 2024, Marin resigned as an employee of the Company. He claimed the Company constructively dismissed him. Following Marin's resignation, the Company withdrew its first injunction application and applied for a summary judgment to get Marin to repay the Company some of the salary he had paid himself without shareholder approval and an interim injunction to grant Akal and Lukomski access to the Company's software and source code.

Issues

The issue for the Court regarding the summary judgment application was whether Marin had an arguable defence under section 161 of the Act regarding the repayment of $205,418.97.

In terms of the interim injunction application, the issues were:

a. whether there is a genuine question to be tried regarding the ownership of the software and source code paid for and used by the Company; and

b. whether the balance of convenience and overall justice favour the making of orders requiring Marin to deliver to the Company the software and source code it paid for and used.

Summary judgment

Legal principles

Rule 12.2(1) of the High Court Rules 2016 allows the Court to give judgment against a defendant where the plaintiff demonstrates that *there is no real question to be tried on the basis that the defendant has no defence to the claim*.[2] The Court *must be left without any real doubt or uncertainty that there is no defence* to the claim.[3] In terms of the credibility of deponents, *the Court need not accept evidence uncritically*.[4]

The Company's submissions

The Company has the burden of establishing that Marin has no arguable defence to its claim for summary judgment. It argued that the payments were *plainly unfair* to the Company and should be repaid for several reasons.[5] First, there was no evidence that Marin was doing more work to justify the additional pay. Second, the salary payments exceeded the Company's gross profit and were therefore disproportionate. Third, the payments substantially reduced the Company's net assets from $103,118.80 in December 2022 to $15,514.53 in August 2023. Fourth, there was no evidence regarding the number of hours Marin worked. Fifth, Akal and Lukomski did not approve the payments. Sixth, the payments were major transactions under section 129 of the Act.

A tenable basis?

Under section 161(5) of the Act, Marin sought to show a *tenable basis* on which his salary was fair to the Company when it was made. In *Madsen-Ries v Petera*,[6] the Court of Appeal held that for the purposes of section 161 of the Act, fairness is based on the facts of the case having regard to factors such as *whether the company derived full value from the work*.[7]

At this interlocutory stage, Justice McHerron found it was reasonably arguable that the Company had gained full value from Marin's work.

2 High Court Rules 2016, r 12.2; *Mediaworks Limited v Marin*, above n 1, at [27].

3 *Mediaworks Limited v Marin*, above n 1, at [27] citing *Partners Finance v Richmond* [2019] NZHC 34, [2019] NZAR 168 at [62].

4 *Mediaworks Limited v Marin*, above n 1, at [27] citing *Krukziener v Hanover Finance Ltd* [2008] NZCA 187, [2010] NZAR 307 at [26].

5 *Mediaworks Limited v Marin*, above n 1, at [40].

6 *Madsen-Ries v Petera* [2016] NZCA 103 [2018] 2 NZLR 500.

7 *Mediaworks Limited v Marin*, above n 1, at [47].

While the Company's finances could not be fully evaluated, it had obtained a profit while Marin was the sole director. His Honour found no evidence that the payments to Marin impacted the Company's creditors nor that it could not pay its taxes. In terms of the amount being a major transaction, Justice McHerron said that since the Act does not state what happens when a company enters a major transaction without shareholder approval, this argument cannot be used to show the payments were unfair. On balance, the Court found no *real doubt or uncertainty* that Marin has no defence. The Company's summary judgment application was dismissed.

Interim Injunction

While the summary judgment application did not succeed, the Court granted the Company's application for an interim injunction.

Legal principles

The test for obtaining an interim injunction requires an assessment of[8]

a. whether there is a serious question to be tried;

b. whether the balance of convenience favours relief; and

c. where the overall justice of the case lies.

Serious question to be tried

The first limb of the test requires the Company to produce sufficient evidence that it has a *real prospect of succeeding in the claim for a permanent injunction at trial*.

The Company argued that it is the legal and equitable owner of the source code and software used by and for its business. Applying the principles in *Vitof Ltd v Altoft*,[9] Justice McHerron found there is a serious question to be tried regarding whether Marin's work and the software he developed were for the benefit of the Company and, therefore, held on trust for it. His Honour did not consider damages an adequate remedy as it was challenging to ascertain the harm suffered.

Balance of convenience

Turning to the balance of convenience, the Company claimed it could not operate satisfactorily while Marin retained control over the software and source code. By counterargument, Marin argued that there is a risk that Akal and Lukomski are not qualified to interact with the software and source code and would infringe Marin's copyright.

After weighing the competing arguments, Justice McHerron found that the balance of convenience favours the Company on two grounds. First, Marin allowed another contractor to interact with the source code after Akal and Lukomski resigned. Second, there was no evidence that Marin owned the source code for the Company's business.

Overall justice

On the last limb, his Honour found that the Company's interests and the successful operation of its business had to prevail at the interim stage.

Commentary

Before concluding his judgment, Justice McHerron invited the parties to reflect on the likelihood that *a solution may best lie in a commercial negotiation rather than in a decision of the Court*.[10] Indeed, had the parties implemented a strategy for what might happen should their business relationship turn sour, the dispute could have been mitigated from the outset.

About the author

Alice Elcoat is a Research Clerk in the ADR Centre's Knowledge Management Team, working with NZDRC and NZIAC. Alice holds a Bachelor of Laws (Honours) degree from the University of Auckland. Her dissertation, "The (in)visible Child: *Empowering Paediatric Patients to Participate in Shared Medical Decision-Making Processes in Aotearoa New Zealand,*" explores the emotional and complex task of creating a mechanism that gives children a right to participate in decisions affecting their bodies.

8 *Klissers Farmhouse Bakeries Ltd v Harvest Bakeries Ltd* [1985] NZLR 129 (CA).

9 *Vitof Ltd v Altoft* [2006] EWHC 1678 (Ch).

10 *Mediaworks Limited v Marin*, above n 1, at [150].

NORTON ROSE FULBRIGHT

Tesseract International Pty Ltd v Pascale Construction Pty Ltd - Proportionate liability in arbitration

Written by **PHIL MINCHER AND JEFFREY GOLDBERGER**

August 2024

In *Tesseract International Pty Ltd v Pascale Construction Pty Ltd* [2024] HCA 24, the High Court of Australia decided by a majority (Edelman and Steward JJ dissenting) that the South Australian proportionate liability regime applied to arbitral proceedings. In so deciding, the High Court reversed the decision of the South Australian Court of Appeal, and overturned the approach of both the Supreme Court of Tasmania in *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3 and the Supreme Court of Western Australia in *Curtin University of Technology v Woods Bagot Pty Ltd* [2012] WASC 449.

Background

The appeal that came before the High Court arose out of a construction dispute. The appellant, Tesseract, and the respondent, Pascale, entered into a contract for Tesseract to provide engineering consultancy work in relation to design and construction by Pascale of a Bunnings warehouse in South Australia.

A dispute ensued as to whether Tesseract's work was performed to the standard required under the contract. The parties failed to resolve the matter by way of conciliation process under the contract and the matter was subsequently referred to arbitration.

Tesseract denied liability and, in the alternative, argued that its liability should (on account of the alleged negligence of a third party) be reduced in accordance with the proportionate liability regime established by Part 3 of the *Law Reform Act (Contributory Negligence and Apportionment of Liability) Act 2001* (SA) or Part VIA of the *Competition and Consumer Act 2010* (Cth) (together referred to as the relevant provisions of the Law Reform Act and Consumer Act).

The arbitrator then referred the following question of law to the South Australian Court of Appeal:

Do the relevant provisions of the Law Reform Act and Consumer Act apply to this commercial arbitration proceeding conducted pursuant to the legislation and the Commercial Arbitration Act 2011 (SA) (CAA)?

The South Australian Court of Appeal answered "no".

High Court decision

As a starting point, the High Court emphasised that party autonomy underpins commercial arbitration. The High Court noted that the UNCITRAL Model Law on International Commercial Arbitration (Model Law), which governs international commercial arbitration conducted under the *International Arbitration Act 1974* (Cth), is mirrored in domestic commercial arbitration legislation, including the CAA. Gordon and Gleeson JJ in their joint reasons said (at 87):

"*Foundational to the Model Law – and, in turn, to the Arbitration Act – is the principle of party autonomy. One of the clearest expressions of that principle is that the parties to an arbitration agreement are generally free to choose for themselves the law or legal rules applicable to that agreement.*"

In this context, Gageler CJ identified the different choices given to parties as follows:

- the substantive law that will govern the arbitration (s28 of the CAA);
- the procedural law that will govern the arbitration (s19 of the CAA); and
- the seat or place of arbitration (s20 of the CAA).

Subject to questions of arbitrability and public policy of the law of the seat of the arbitration (in this case South Australia), the majority held that the South Australian proportionate liability regime formed part of the substantive law of that State and applied to the arbitration. Conversely, the question of joinder of parties to an arbitration was a question of procedural law which did not affect the application of the regime. Gageler CJ said (at 63):

"*The operation of the central provisions does not depend on all concurrent wrongdoers being parties to one proceeding for a determination to be made as to the proportionate liability of any one concurrent wrongdoer. Nor does their operation as between the parties to a dispute depend on any effect that the resolution of the dispute between those parties might have on third parties.*"

Gordon and Gleeson JJ in their joint reasons similarly referred to the dichotomy between substantive law and procedural law noting as follows (at 128):

"*The proportionate liability laws do not require a plaintiff to sue all wrongdoers in a single proceeding or assume that a plaintiff will wish to or be able to sue all wrongdoers in a single proceeding.*"

Accordingly, the High Court rejected Pascale's submission that the proportionate liability regime did not apply to an arbitration because of the arbitrator's inability to order joinder of a concurrent wrongdoer.

Takeaways

First, the parties are free to choose separately the substantive law, the procedural law governing the arbitration and the seat of the arbitration.

Secondly, in those state or territory regimes which are silent on excludability (Victoria, South Australia, the Australian Capital Territory and Northern Territory), it appears that the parties are free to exclude proportionate liability from the arbitral process. Gordon and Gleeson JJ said (at 131):

"*To the extent that a plaintiff would be disadvantaged by s 11, South Australian law does not prevent a party from contracting out the proportionate liability laws in any arbitration clause.*"

However, the Queensland regime expressly prohibits exclusion. Where Queensland is the seat of the arbitration attempting to exclude the regime would be problematic.

Thirdly, *Tesseract* raises some important questions for parties to consider when negotiating dispute resolution clauses, especially where the nature of the transaction is likely to result in multi-party disputes. These include:

- whether arbitration or litigation should be selected as the dispute resolution mechanism in the contract (noting that an applicant in an arbitration which does not exclude the proportionate liability regime may need to commence litigation against other alleged wrongdoers following the outcome of the arbitration);
- whether to exclude the proportionate liability regime from arbitration under the contract (in jurisdictions where this is possible). If proportionate liability is not excluded, and the concurrent wrongdoer is not joined to the arbitration. there is a real risk of an arbitral award (that finds a respondent proportionally liable) being inconsistent with a subsequent determination (in a proceeding by the applicant against the other alleged wrongdoers). If that was to eventuate, the opportunity for the innocent party to fully recover from all wrongdoers could be lost; and
- whether all relevant contracts for the project can be drafted to provide for all potential parties to a dispute to be joined in the same arbitration.

Norton Rose Fulbright has one of the most dynamic dispute resolution practices in Australia and globally. We have strong expertise in construction project delivery issues and disputes, including litigation and alternative dispute resolution (ADR). Please contact us if you require advice on dispute resolution mechanisms or assistance with drafting on future projects.

With thanks to Norton Rose Fulbright *for the original article published on their website* here.

About the authors

Phil Mincher is a projects and construction lawyer based in Brisbane. He has notable experience acting on high profile and large-scale matters within the construction and infrastructure industry across Australia, the UK and the Middle East.

Phil provides front end advisory, claims advice during project delivery and acts in all forms of dispute resolution, with a particular focus on arbitration.

Jeffrey Goldberger is a construction and infrastructure lawyer based in Sydney. He is a contract law specialist and a recognised authority on Australian contract law, with over 25 years' experience in private and public sectors.

Owing to his extensive experience and expertise in the negotiation and resolution of complex contractual issues, Jeffrey has also previously served on the then Federal Attorney General's Expert Panel on the effectiveness of Australian contract law. His ability to articulate the application of contract law in a practical and commercial way is widely known and highly regarded nationally.

Jeffrey is well known to, and highly regarded by, major government, finance, resources and corporate clients. He has also formerly lectured in contract law, commercial law and private international law at the University of Sydney Law School.

As a thought leader, Jeffrey has presented papers on Australian and English contract law at numerous conference and seminars throughout Australia and the United Kingdom.

THE TREASURE OF THE SAN JOSÉ

Written by **KATE HOLLAND**

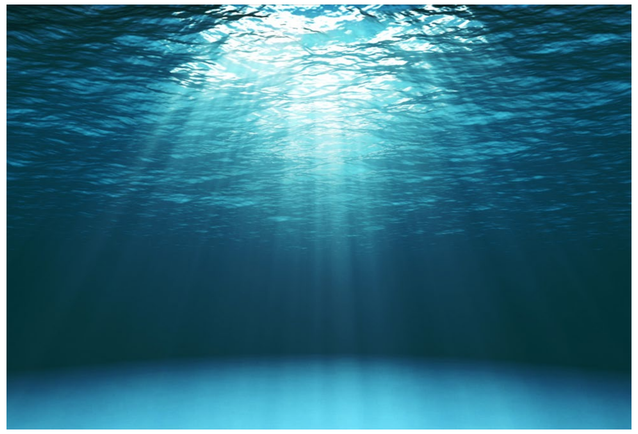
An investor-State arbitration is currently underway between the Republic of Colombia and a US company over a 300-year-old shipwreck containing treasure estimated at $20 billion – the most valuable sunken treasure in history. The company claims Colombia has unlawfully expropriated its rights to the treasure, in breach of a US-Colombia investment treaty, and seeks nearly $10 billion in damages.

The treasure ship San José and the battle that sank her

On 8 June 1708, a fleet of Spanish treasure ships was sailing along the coast of Colombia. Its flagship was a 64-gun galleon called the Galeón San José (the **San José**). The San José was loaded with a cargo of immense value – 200 tons of gold, silver and rough emeralds from the New World – to be taken back to Europe to fund Spain and France's military efforts in the War of the Spanish Succession.

But close by, British navy warships were lying in wait to ambush the Spanish fleet, disable and commandeer the San José and seize the treasure. Just before sundown, the British intercepted the galleon and launched their attack.

Unfortunately, the battle did not go to plan when one of the British ships accidentally fired a cannonball right into the San José's gunpowder magazine. The galleon exploded and within minutes the ship and all



Do you know the way to San José?

A US company is claiming $10 billion in an arbitration against Columbia over the discovery of a 300-year-old sunken treasure ship. Columbia denies that the company reported the correct location of the shipwreck, and is keeping its true location a secret.

of its treasure sank to the bottom of the Caribbean Sea. They have remained there ever since.

Discovery and recovery

In the 1980s, an American salvage company (the **salvage company**) claimed to have found the shipwreck in Colombian waters. In 2015, Colombia confirmed that the San José had been discovered, but claims it was found in a different location to that reported in 1982. The location of the wreck is a tightly guarded Colombian State secret.

Over 300 years after the battle that sank her, and 40 years after being first allegedly discovered, the San José remains on the sea floor. Attempts at recovery have been beset by new battles – legal battles over who owns her USD 20 billion treasure.

Who owns the San José?

A US company called Sea Search-Armada LLC (**SSA**) claims it is entitled to 50% of the value of the San José's treasure under an agreement in place between Colombia and the salvage company that allegedly made the discovery in 1982[1]

Colombia denies the salvage company discovered the wreck of the San José. It claims that the San José and its contents belong to Colombia and are assets of national cultural interest, which do not qualify as 'treasure'. In February 2024, Colombia announced plans to investigate and explore the wreck.

According to Spain, neither Colombia nor SSA owns the San José, and the galleon and its treasure remain Spanish public property and are Spain's underwater cultural heritage.

Indigenous peoples of Peru and Bolivia have also voiced objections on the basis that the San José's cargo of gold, silver and emeralds were mined by their ancestors or on their land during colonial times and plundered by Spain. Earlier this year a group of indigenous South American communities sent a petition to Spain and UNESCO that they should share in any proceeds from the San José as their common and shared heritage.

Other groups, including some archaeologists and historians, insist the wreck should be respected as a gravesite and left untouched.

Against this wider international background of disagreement, the focus of this article is the narrower issue of SSA's claims against Colombia and their ongoing arbitral proceedings.

The salvage company's dispute with Colombia

The exploration permit and the 1982 discovery

In 1980, the Colombian authorities granted an underwater exploration permit to the salvage company (the **permit**).

After two years of searching, in 1982 the salvage company sent a report to Colombia that a wreck had been located and provided the wreck's coordinates (the **reported coordinates**).

1 In 2008, the salvage company's assets and rights were transferred to SSA in an asset purchase agreement. SSA is the claimant in the current arbitration.

Colombia issued a resolution recognising the salvage company as a reporter of treasure in the reported coordinates (the **1982 recognition letter**). SSA claims that under Colombian law at that time, the salvage company had rights as the discoverer and reporter of the wreck, to 50% of the value of the treasure.

Following the discovery, relations between Colombia and the salvage company broke down and attempts to agree contract terms to recover the wreck were unsuccessful. SSA claims that Colombia instead began approaching other operators to investigate and recover the wreck using the salvage company's reported coordinates.

The 2015 discovery

Colombia claims that following further investigations in 1994, it turned out that what the salvage company had found at the reported coordinates was not the wreck of the San José.

In 2015, Colombia announced that the San José had been found. Colombia claims the San José wreck had been discovered that year by a Swiss operator, in a different location to the salvage company's reported coordinates.

On that basis, Colombia claims that SSA has no rights to the San José, because the salvage company did not discover it. However, Colombia refuses to disclose the actual coordinates of the San José, and its location is a secret.

The Colombian Supreme Court decision (2007)

The salvage company and its successors have been engaged in litigation against Colombia since 1989, both in Colombia and in the US.[2]

In 2007, the Colombian Supreme Court issued a decision on the salvage company's rights. However, SSA and Colombia disagree over what the Supreme Court determined.

SSA claims the Supreme Court's decision was that the salvage company had rights to 50% of the value of any items qualifying as "treasure" at the reported coordinates and surrounding area. Colombia disagrees with SSA's interpretation of the Court's decision.

In 2008, the salvage company transferred its rights and assets to SSA.

The United States-Colombia Trade Promotion Agreement (2012)

In 2006, the United States and Colombia signed a free trade and investment treaty. The US-Colombia Trade Promotion Agreement (**TPA**) entered into force in 2012. Article 10 of the TPA protects US companies investing in Colombia against discriminatory or unlawful treatment.

Under Article 10 of the TPA, US companies with a dispute against Colombia that qualifies as an 'investment dispute' can refer their dispute to arbitration.

Colombia passes a new classification law (2020)

In 2020, Colombia passed a new law classifying the San José and its contents as 'assets of national cultural interest'. This means that under current Colombian law, the San José and its contents do not qualify as 'treasure'.

SSA claims that Colombia passed the classification law with the specific purpose of circumventing the result of the Supreme Court's decision and depriving SSA of its right to 50% of the value of the San José's contents.

Arbitration between SSA and Colombia (2022 – 2025)

In December 2022, SSA commenced arbitration against Colombia under the UNCITRAL Arbitration Rules.

SSA claims that Colombia's classification law is arbitrary and unreasonable conduct which expropriates and interferes with SSA's rights to 50% of value of the San José treasure.

Specifically, SSA claims that the classification law breaches Colombia's investment obligations under the TPA regarding:

- expropriation of investments and compensation (Article 10.7);
- minimum standard of treatment for investments, including fair and equitable treatment and full protection and security (Article 10.5); and
- national treatment and most-favoured-nation treatment for investors and investments (Article 10.3).

SSA seeks restitution of its rights, or compensation for damages in the amount of approximately USD 10 billion.

2 The US proceedings were withdrawn.

In July 2023, Colombia advanced a number of preliminary objections to the arbitral tribunal's jurisdiction under the TPA to hear the dispute, all of which have recently been dismissed.

Spain and the US apply to intervene in the arbitration (December 2023)

Ahead of the jurisdictional hearing, the US (which is a party to the TPA but not a party to the dispute) made submissions as a 'non-disputing party' on the interpretation of the terms of the TPA.

Spain unsuccessfully sought leave to intervene in the arbitration as an *amicus curiae*. Spain argued in its application that the San José is in fact Spain's public property and that there is a legal dispute between Spain and Colombia over its ownership (although it gave no details of any proceedings). Spain explained it was intervening in the arbitration in order to defend its interests in the San José.

In December 2023, the tribunal dismissed Spain's application. It held that the issue SSA has referred to arbitration is not whether Spain owns the San José, but whether Colombia has breached its obligations under the US-Colombia TPA investment provisions.

The tribunal acknowledged that Spain may have a significant interest in the arbitration but found that it was unlikely to provide assistance to the tribunal on the interpretation of the TPA and whether SSA has a qualifying 'investment dispute' for the purpose of determining whether the tribunal has jurisdiction to hear the dispute.

However, the tribunal left the door open for Spain to make a further application for leave to intervene at a later, substantive stage of the arbitration.

Colombia's unsuccessful jurisdictional challenge (February 2024)

In February 2024, the tribunal dismissed all of Colombia's preliminary objections to jurisdiction. The tribunal held it was satisfied, on a prima facie basis, that under the TPA:

- SSA is a protected investor with a qualifying 'investment' (Article 10.28). The 1980 permit and the 1982 recognition letter created and recognised rights capable of comprising an 'investment' and those rights were validly acquired by SSA under its asset purchase agreement with the salvage company.
- The actions of Colombia which SSA claims breach the TPA took place after the TPA entered into force (Article 10.1.3). The action SSA complains of in the arbitration is the classification law of 2020, which happened well after the TPA's entry into force in 2012.
- SSA's claims are not time barred (Article 10.18.1). The classification law was announced in January 2020. SSA could not have become aware of Colombia's action, or the resulting alleged expropriation of that action, before the 2020 announcement. SSA commenced arbitration alleging the breach in December 2022, which was within the TPA's three-year time limit to bring a claim.

Evidence Preservation Protocol (June 2024)

On 28 June 2024, the tribunal granted (against Colombia's objections[3]) an application made by SSA for interim measures, ordering Colombia to commit to an Evidence Preservation Protocol.

Colombia must catalogue, preserve and protect evidence (including records, recordings, objects and artifacts) identified, recovered or salvaged from the San José, create and maintain a catalogue of this evidence and report to the tribunal on a bi-monthly basis until the dispute is determined.

However, Colombia is not required to disclose the coordinates of the wreck's location under the Protocol.

Substantive hearing on the merits (to be held in November 2025)

Following Colombia's unsuccessful jurisdictional challenge, SSA filed amended submissions on its substantive claim. In September 2024, the tribunal granted Colombia an extension of time to file its response, which must be received by December 2024.

The substantive hearing is currently timetabled for the end of November 2025, and we look forward to reporting on the tribunal's decision on the merits of SSA's claim in due course.

3 Colombia denies that it plans to commence any recovery operations at the current time.

ARTICLE

Simplicity over Complexity - UK Supreme Court rules on governing law of arbitration agreement

Written by **IAIN SHARP AND REEMA SHOURR**

UniCredit Bank GmbH -v- RusChem Alliance LLC [2024] UKSC 30

Originally published by Hill Dickinson on 19 September 2024

Keep it simple! That was the unanimous message from the UK Supreme Court when it considered a jurisdiction issue appeal on what was the governing law of the arbitration agreement in performance bonds that were governed by English law but provided for ICC arbitration in Paris.

The beneficiary under the bonds had sought to argue that the governing law of the arbitration agreement should be French law as the parties had chosen Paris (in France) as the seat of arbitration. It submitted that a French Court would apply French law principles to any international arbitration agreement that provided for a French seat.

The Supreme Court rejected this approach, which it believed could lead to complications and a lack of clarity. It preferred the general rule of English common law that the law chosen by the parties to govern their contract will usually also apply to the arbitration agreement in the contract if the arbitration agreement does not expressly provide for a different governing law. Choosing a different country as the seat of arbitration will not, of itself, be sufficient to displace the general rule.

The Supreme Court, therefore, upheld the Court of Appeal's decision that the arbitration agreements in the bonds were governed by English law. As a result, the English Court had jurisdiction over the issuing bank's claim for an anti-suit injunction to restrain Russian Court proceedings brought in breach of the arbitration agreements. The Supreme Court upheld the final anti-suit injunction issued by the Court of Appeal.

The background facts

In 2021, a Russian company, RusChemAlliance LLC (RusChem) contracted with two German companies for the construction of LNG and gas processing plants in Russia. Pursuant to the contracts, RusChem made advance payments to the German contractors. A German bank, UniCredit Bank GmbH (UniCredit), issued seven on demand bonds to guarantee the contractors' performance under the construction contracts.

All seven bonds expressly stated that they were governed by English law and provided for disputes to resolved in ICC arbitration seated in Paris but conducted in English.

Following the invasion of Ukraine in February 2022 and the imposition of EU sanctions on Russia and designated Russian entities and individuals (but not RusChem), the contractors decided that they could no longer continue to perform the construction contracts. RusChem terminated the contracts and sought reimbursement of the advance payments it had made. The contractors declared that they could not repay the advance payments because of the EU sanctions.

RusChem made demands for payment under the bonds, which UniCredit rejected because it believed that the sanctions prevented it from making any payment to RusChem.

In 2023 RusChem commenced proceedings against UniCredit in the St. Petersburg Arbitrazh Court in Russia, claiming payment under the bonds. Among other things, RusChem relied on provisions of the Russian Arbitrazh Procedural Code (APC) (promulgated in 2020) which confers exclusive jurisdiction on the Arbitrazh Courts over disputes between Russian and foreign parties arising out of foreign sanctions and treats foreign arbitration agreements as inoperable. The APC allows Russian persons affected by foreign sanctions to apply to the Arbitrazh Court for an anti-suit injunction in relation to foreign court or arbitration proceedings.

UniCredit sought to have the Russian proceedings dismissed on the basis of the parties' agreement to arbitrate in Paris under the ICC Rules. The Arbitrazh Court concluded that it had jurisdiction and dismissed UniCredit's application. However, the Arbitrazh Court did adjourn its own proceedings pending the outcome of the English Court proceedings.

The English lower court proceedings

After RusChem commenced the Russian proceedings, UniCredit commenced proceedings in the English Commercial Court seeking an injunction and declaratory relief in relation to RusChem's breach of the arbitration agreement in the bonds. UniCredit obtained an interim anti-suit injunction (ASI) to restrain the Russian proceedings on a without notice basis.

RusChem subsequently disputed the English Court's jurisdiction to hear the claim for an ASI, arguing primarily that the claim did not satisfy the contractual gateway under the English civil procedure rules (i.e. contract governed by English law) and that in any event the proper place to bring the claim was the French Courts.

The Commercial Court found it did not have jurisdiction but continued the ASI pending the outcome of an appeal from its order. The appeal was heard in January 2024.

The Court of Appeal allowed the appeal and granted a final ASI. It concluded that it had jurisdiction over the claim because: (i) the arbitration agreements were governed by English law; and (ii) England and Wales was the proper place to bring the claim.

In February 2024, RusChem was given permission to appeal to the Supreme Court on the jurisdiction issue – whether the English Court has jurisdiction over UniCredit's claim.

The caselaw

In *Enka Insaat ve Sanayi AS -v- OOO Insurance Company Chubb* [2020] UKSC 38, the Supreme Court held that where the parties have not chosen (whether expressly or impliedly) a governing law for the arbitration agreement, the governing law of the underlying contract will also apply to the arbitration agreement. This is so even where the seat of the arbitration is in a country with a different system of law. The majority also held that if there was no choice of law to govern the arbitration agreement but there was a choice of seat, the law of the seat of arbitration should apply.

In *Kabab-Ji SAL -v- Kout Food*

Group [2021] UKSC 48, the Supreme Court applied the principles identified in *Enka*. In *Kabab-Ji*, the contract provided for English governing law and for disputes to be resolved in ICC arbitration in Paris. The Court stated that it was clear English law governed the arbitration agreement.

This approach has been adopted by the Supreme Court because it is considered to provide certainty and consistency.

The Supreme Court decision

The Supreme Court unanimously dismissed the appeal and upheld the Court of Appeal's findings.

The governing law issue

Once again, the Supreme Court applied the principles set out in *Enka*. The governing law clause in the bonds was widely framed and there was no reason to find that the arbitration agreement was excluded from its scope. The choice of a different country for the seat of the arbitration did not justify such an exclusion. The arbitration agreement was, therefore, governed by English law.

The Supreme Court heard expert evidence on French law, including to support RusChem's contention that a French court would find that French law applied to the arbitration agreement because the seat was in France. RusChem also argued that the majority decision in Enka (where there was no choice of governing law but there was a choice of seat) should apply so that the parties could be taken to have intended French law to govern the arbitration agreement.

The Supreme Court rejected these arguments. There was a choice of governing law in this case because the governing law clause in the bonds, properly construed, applied to all the contractual provisions including the arbitration agreement. The fact that the courts of the arbitral seat might take a different view and regard their own law as governing the arbitration agreement was not a good reason to reach a different conclusion.

Proper place

The Supreme Court clarified that where, as here, the parties have contractually agreed on a forum for resolving their disputes, the issue of whether there is a more appropriate forum ('forum non conveniens') does not arise. Rather, the English Court will give effect to the chosen forum unless there are strong reasons not to do so. This is equally applicable whether the chosen forum is a court or arbitration.

The fact that the Russian Arbitrazh Court treated a foreign arbitration agreement as inoperable was not sufficiently strong reason for the English Court not to seek to enforce the parties' arbitration agreement. Under English law, the arbitration agreements in the bonds were valid and RusChem was in breach of them.

Where the seat of the arbitration was in England, the English Court would not hesitate to grant an ASI against foreign court proceedings to restrain breach of the arbitration agreement. Where the seat was not in England, the English Court would still seek to enforce the parties' contractual bargain because this would not be inconsistent with comity as regards the foreign court.

The role of the French Court in this case was to supervise the way in which the arbitration proceedings were conducted, not to prevent a breach of the contractual obligation to arbitrate. Furthermore, on the evidence, the French Court could not grant an ASI and therefore the claim for an ASI could not be brought in the French Court.

While an arbitrator could in principle make such an order, it would not have the coercive effect required because the arbitrator does not have the same powers to enforce performance of an ASI in the way that an English Court could.

The Supreme Court concluded that there was no other appropriate forum and England was the proper place to bring the claim for the ASI. The final mandatory ASI was upheld.

Comment

An Arbitration Bill is currently before the UK Parliament which incorporates an amendment to the Arbitration Act 1996 to provide that the arbitration agreement is governed by the law of the seat unless the parties expressly provide otherwise.

This amendment was made on the recommendation of the Law Commission, following its review of the Arbitration Act 1996 and in view of feedback it had received during the consultation period which suggested that the law as stated in Enka was "complex and unpredictable."

The Supreme Court in this case declined to reconsider the applicable principles while draft legislation is before Parliament.

In the meantime, those who are concerned about the risks and costs of a dispute concerning the governing law of their arbitration agreement should clearly define the governing law of the arbitration agreement.

More generally, the Supreme Court's decision reflects the English Courts' continued support of international arbitration and traditional stance of enforcing arbitration agreements and granting ASIs (where appropriate) to restrain breaches of such agreements.

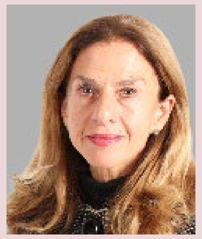
For further details on our international arbitration law services, please contact us or a member of our dispute resolution team.

About the authors

Iain Sharp

Iain has over 20 years' experience of international trade and commodities, and international commercial dispute resolution, including alternative dispute resolution. Prior to joining Hill Dickinson, Iain was Asia-Pacific Head of Legal at leading international trading house, Gunvor Singapore, where his work covered the full spectrum of commercial, advisory and disputes for oil and gas (including crude and middle distillates), metals/ores and energy products (including LNG and LPG and biofuels).

Iain regularly advises clients on a broad range of contracts and legal issues (non-contentious and contentious) surrounding the sale and purchase of hard and soft commodities, letters of indemnity, trade and economic sanctions, operational and legal risk management, and trade finance. His dispute resolution experience spans a wide range of sectors (including energy and natural resources, pharmaceuticals, technology and defence products) and includes arbitrations under institutional (ICC, LCIA, SIAC, HKIAC, LMAA), ad hoc, and trade association rules (including LME, GAFTA, FOSFA and PORAM). Iain is a Member of the Chartered Institute of Arbitrators (MCIArb) and the LCIA Asia Pacific Users' Council.



Reema Shour

Reema Shour is a qualified barrister (non-practising) and an experienced senior knowledge lawyer in Hill Dickinson's global shipping team. She spent her first 15 years post-qualification as a fee earner in international commercial litigation, with particular experience in the shipping, international trade and commodities sectors and has worked as a professional support lawyer since 2009, joining Hill Dickinson in 2023. Reema keeps the firm's shipping and trade groups fully informed on all legal and regulatory developments within the industry and authors a number of internal updates. Reema holds two master's degrees, one in law and one in translation. In addition to English, she speak Arabic, French, German and Italian.

Case in Brief:

Written by **ALEXANDER LYALL**

Third party rights in arbitration: can an arbitral award impact a non-party to the agreement?

In KZ v KY,[1] the Hong Kong Court of First Instance (the **Court**) considered whether an arbitral award impacting third parties can be enforced by a court. More fundamentally, the Court also asked whether any third parties had been impacted at all.

Background

KZ and KY were brothers embroiled in a dispute following the restructure of various family companies.

As part of the company restructure, KZ agreed to give KY shares (the **restructure agreement**). Under the restructure agreement, the shares would be returned to KZ once the restructure had been completed. However, KY did not return them.

1 *KZ v KY* [2024] HKCFI 1880.

Third party interests

The Court of First Instance did not think third party rights had been impacted by the award.

The proceedings

The parties went to arbitration to settle whether the shares should be returned. The tribunal declared that these shares belonged to KZ and that KY should transfer them back.

KZ went to the Court to enforce the Award. In response, KY sought to have the Court set the Award aside.

KY argued that the Award had to be set aside on the grounds that:

- the arbitration impacted third parties;
- People's Republic of China (**PRC**) law governed the agreement but the tribunal had assessed the matter using Hong Kong law; and
- the matter itself was not capable of being arbitrated.

The decision

The impact of arbitration on third parties

Central to KY's argument was that an associate, Mr Mak, held shares by way of the agreement subject to the arbitration. Therefore, the arbitration would impact a third party. KY argued that there was authority to suggest this would invalidate the award.

The Court agreed to an extent. When an arbitral award impacts rights of third parties, a court can set aside the award. However, that does mean a court must. Rather, *it is open to the court faced with an application for leave to enforce an award to decide whether third party interests provide a reason not to allow enforcement*.[2]

KY then argued that an analogy should be made with equity. Equitable remedies such as specific performance will not be ordered by a court when the remedy would negatively impact a third party.

However, in this case Justice Mimmie Chan did not see how the rights of third parties would be

2 Citing *Sodzawiczny v McNally* [2021] EWHC 3384 (Comm).

impacted. In order to demonstrate this, Justice Mimmie Chan broke down the particulars of the agreement to prove a lack of third party rights:

1. Despite the third party's arguments to the contrary, the share transfer at the heart of the dispute did not concern their sole share.
2. The Award did not bind the third party.
3. The third party was claiming that their rights had accrued by way of an oral agreement between them and the respondent. Justice Mimmie Chan reminded them that they were welcome to start their own independent proceedings.

The impacts of PRC law

One of KY's arguments was that the matter was a succession issue and would therefore be governed by PRC Succession Law. However, Justice Mimmie Chan did not agree that this meant it could not be decided by arbitration. Any arbitrator would simply only have to consider the dispute on those terms.

Furthermore, as the companies were incorporated under Hong Kong law, Justice Mimmie Chan was doubtful that PRC law would apply in any case.

Non-arbitrable

Justice Mimmie Chan adopted the view of the Singapore Court of Appeal that the presumption of arbitration is that arbitral awards will be enforced.[3] One of the key exceptions to the rule is whether the enforcement of an award would contravene public policy in Hong Kong. With KY having failed on the other arguments, Justice Mimmie Chan could not see how this would occur.

Conclusion: arbitration is sensitive to third party interests

The difficulty in having a court set aside an award no doubt shaped KY's argument around Mak being impacted by the award. The idea that Mak was an impacted third party was a stretch, but clearly there is something to the idea that arbitral awards are unenforceable when third parties are impacted.

3 *Larsen Oil and Gas Pte Ltd v Petroprod Ltd* [2011] 3 SLR 414.

Court confirms it takes two to tango but there was only one party at this dance!

Written by MARIA COLE

Manufactured dispute

Alarm bells set ringing where parties manufacture a dispute about a claim never made against them.

A Hong Kong Court of Appeal

For an arbitrator to have jurisdiction under an arbitration clause in a contract, there must be a dispute between the parties to the contract for the arbitrator to resolve, and that dispute must fall within the scope of the arbitration clause. The Hong Kong Court of Appeal recently upheld a challenge to parts of an arbitral award finding there was no dispute between the parties, which meant the arbitrator did not have jurisdiction to grant the declarations of non-liability that he had made.[1]

1 *CMBICDHAW Investments Limited v CDH Fund V Limited Partnership & Ors* [2024] HKCA 516.

Background

In 2014, the bewilderingly-named plaintiff, CMBICDHAW Investments Limited (**CMB**) entered into a co-investment agreement (the **Agreement**) with the first defendant, CDH Fund V Limited Partnership (**Fund**) and the second defendant, CDH Grand Cattle Holdings Limited (**Cattle**), in which CMB agreed to invest USD 10,000,000 for a stake in a meat production and processing company which sold its products into China (the **Cattle Company**). The Agreement was governed by Hong Kong law and disputes were to be settled by ICC arbitration in Hong Kong.

What was the beef between the parties?

By 2019, trouble was brewing and in June 2020, allegations of fraudulent misrepresentation, conspiracy to defraud and breach of trustee duties were made. CMB commenced legal proceedings in the Hong Kong High Court against the two representatives of Fund and Cattle who had negotiated the Agreement, and against a director and an employee of the Cattle Company (the **Defendants**). The claim centred around representations that the Cattle Company would be listed on the Hong Kong stock exchange and that CMB's investment in it would have a substantial yield.

Of note, Fund and Cattle were not defendants in the High Court proceedings and no claims where made against them by CMB.

In July 2020, three of the Defendants plus Fund and Cattle (the **Claimants**) commenced an ICC arbitration against CMB for interim and permanent anti-suit injunctions[2] The focus was to stop CMB pursuing the High Court proceedings and to obtain injunctions restraining it from commencing or pursuing any other proceedings relating to disputes arising out of the Agreement other than by ICC arbitration.

There were a couple of fundamental flaws in all of this. First, the Agreement was between CMB, Fund and Cattle. The Defendants were not parties to it and so there was no contract or agreement to arbitrate between CMB and the Defendants. Second, there was no actual dispute between CMB and Fund and Cattle. The claims made in the arbitration were on behalf of and for the benefit of the Defendants, who were non-parties to the Agreement, and the Agreement contained a clause which stated the Agreement was only for the benefit of the parties.

Further skirmishing occurred in relation to the High Court proceedings, including an application for stay of the proceedings in favour of the arbitration by three of the Defendants, and an amended statement of claim by CMB. Again, no claim was made by CMB against Fund or Cattle.

In December 2020, the Claimants served their statement of claim in the arbitration. Of relevance, the Claimants asked the arbitrator to declare that Fund and Cattle had no liability to CMB with respect to its allegations of fraud, conspiracy and breach of trustee duties and that all such allegations were false.

The arbitrator did as asked and made a declaration of non-liability.[3] CMB responded by applying to the High Court to have the declaration set aside, on the basis Fund and Cattle had been granted a *declaration of non-liability in respect of something for which CMB had never asserted they were liable, arising out of allegations CMB had never made against them.*

The Judge at first instance granted the application to set aside the declaration of non-liability, agreeing that CMB had never made claims against either Fund or Cattle and noting that damages had only been sought against the Defendants. The Judge also stated that it did not matter if Fund and Cattle had an interest in the declaration of non-liability if there was no dispute to begin with between Fund, Cattle and CMB, and held:

> Even if a claim is not essential for a dispute, there must nevertheless be something in the nature of an assertion by one party, and a situation in which the parties neither agree nor disagree about the true position is not one in which there is a dispute. No matter how wide an arbitration clause, it can only cover disputed claims between the parties to the Agreement, namely claims and disputes between CMB and Cattle and Fund.

2 An anti-suit injunction is an order of an arbitrator or a court which prevents a party from commencing or continuing a proceeding.

3 Although it is worth noting that the declaration granted by the Arbitrator was in different terms from that sought and the Court found at [70], that the very changes made pointed to his absence of jurisdiction.

Leave was granted to appeal and the matter went before the Court of Appeal.

The Court of Appeal confirms it takes two to tango

With a memorable opening line, the Court succinctly introduced the issue it had to decide:

> It is well-settled that it takes two to tango. The question which arises in this appeal is whether it also takes two to create a 'dispute', capable of giving jurisdiction to an arbitrator to resolve that dispute.

The Court set out the principles it had to apply as follows:[4]

> … On the one hand, arbitration agreements are construed widely, as it is the policy of the Court to uphold a contract made by consenting parties to submit their disputes to their forum of choice. On the other hand, a party is only bound to that choice against its proper contracting counterpart, and it would be artificial for an arbitration to be commenced in order to compel a party to admit the lack of merit in a claim never made by him.

We can also point out the following settled principles:

(1) In the arbitration context, the term "dispute" should be construed inclusively and not overly legalistically.

(2) For a "dispute" to exist, it is unnecessary for there to be a "claim" in the sense of a legal claim or legal cause of action

4 Above n 1, at [52] and [53].

asserted by one party against the other.

(3) Various phrases have been adopted in previous authorities to identify the sufficiency of existence of a "dispute", such as "assertion or adoption of a position by one party which is expressly or by implication rejected or at least not accepted by the other" and "a difference of opinion about the central issues".

(4) Therefore, there must be something in the nature of an assertion by one party, and a situation in which the parties neither agree nor disagree about the true position is not one in which there is a dispute.

(5) Further, some cases identified that silence in the face of a claim or assertion does not raise a dispute, as what is required is a rebuttal or denial of the claim or assertion.

(6) The phrase "arising out of or relating to" is to be given a broad construction, and "relating to" has a wide meaning intended to convey some connection between two subject matters.

(7) The time for determining whether a "dispute" has arisen is as at the time of the commencement of the arbitration, when the arbitrator's jurisdiction is invoked, because it is the existence of the dispute which engages that jurisdiction.

(8) In other words, it must be possible to formulate the "dispute" which is said to engage the jurisdiction.

(9) A "dispute" may arise and continue to exist, unless there is a clear and unequivocal admission of both liability and quantum.

The Court had little trouble in finding that the Arbitrator was wrong to have proceeded on the basis he had jurisdiction. It said it was *difficult to see* [that] *any dispute between CMB on the one hand and Fund and Cattle on the other, falling within the terms of the Arbitration Agreement, had come into existence.*

After testing the jurisdiction question, which led it to find the lack of any actual "dispute" was *rendered stark*, the Court concluded by stating:

> [78] Lastly, we think the very fact that Fund and Cattle were seeking a negative declaration – a declaration of non-liability – tends (at least on the facts of this case) to point to the artificiality of the suggestion that there was a dispute. In the factual context, we think that this form of relief sought should have set alarm bells ringing as to whether there was an attempt to engineer the existence of a dispute, so as to bring into the arbitral process for determination those matters which already arose for determination in the [High Court proceedings] involving persons not themselves parties to, or able to take the benefit of, the Arbitration Agreement.
>
> [79] We do not rule out the possibility that there can be a 'dispute' between parties to a contract, when non-contractual claims and assertions are made against a third party who was a stranger to the arbitration agreement, on the basis that there is an assertion "arising out of or related to" the contract. But each case must turn on its own facts, and the particular facts and peculiar circumstances of this case do not fall within that.

Conclusion

Al Pacino's character famously said there's "No mistakes in the tango... Not like life. It's simple, that's what makes the tango so great. If you make a mistake, get all tangled up, just tango on."

It's clearly only good advice if you're tangoing in the first place!

About the author

Maria Cole works as a Knowledge Manager in The ADR Centre's Knowledge Management Team, including working with NZDRC and NZIAC. She was previously a civil litigation barrister for over a decade. During that time, she worked on several multi-million-dollar development disputes and was involved in arbitrations and mediations.

COULD SUPREME COURT SEWAGE DECISION OPEN THE FLOODGATES?

A judgment of the Supreme Court, handed down earlier this week, could lead to an increase in claims against sewage companies initiated by private companies and individuals.

Written by **NEAL GIBSON AND TOM SANDEMAN**

4 July 2024

CMS law·tax·future

Summary and background

In *The Manchester Ship Canal Company Ltd (Appellant) v United Utilities Water Ltd (Respondent) (No 2)* [2024] UKSC 22, the Supreme Court was asked to decide whether the existing statutory framework governing the supply of water and provision of sewerage prevented the owner of a waterway from taking action against a utility company responsible for discharging sewage into the water.

The judgment marks the conclusion of long-running litigation between The Manchester Ship Canal Company Ltd ("**MSCC**"), the owner of the Manchester Ship Canal (the "**Canal**"), and United Utilities Water Ltd ("**United Utilities**"), as the statutory sewage undertaker for the North West of England. The judgment itself was 16 months in the making, the case having been heard by the Supreme Court in March 2023.

The case has been closely followed by industry stakeholders as it has moved through the High Court and Court of Appeal to the Supreme Court. The final ruling clarifies that the legislative framework under the Water Industry Act 1991 (the "**Act**") will not provide sewage undertakers with immunity from nuisance claims brought by those who own or enjoy rights over polluted watercourses. The decision continues the long line of cases dealing with the question of the extent to which a utilities provider, operating under powers prescribed to it by statute, can rely on that authorisation to protect it from claims arising from the undertaking of its function.

Importantly, the claim that was the subject of the Court's judgment was not a claim by MSCC in nuisance and, as such, the Court was not required to consider or make any decision as to whether a claim in private nuisance could be supported. Rather, in response to a threat by MSCC to pursue a claim of that nature, United Utilities sought a declaration from the Court that any such action would be barred by the statutory scheme established by the Act.

Whilst the High Court agreed to make that declaration (as per *The Manchester Ship Canal Company Ltd (Appellant) v United Utilities Water Ltd (Respondent) (No 2)* [2021] EWHC 1571 (CH)), upheld by the Court of Appeal, the Supreme Court has allowed MSCC's appeal. In a detailed judgment which carefully considers a long line of private nuisance case law, the Supreme Court unanimously held that the Act does not prevent MSCC from bringing a common law claim in private nuisance against United Utilities. That is even in circumstances where there has been no negligence or deliberate misconduct on the part the sewage company.

Detail of the decision

The common law position as to the availability of private nuisance in the context of pollution to waterways is – as recognised in the judgment – well-established. The owner of a watercourse, such as MSCC, has a right to use or enjoy it, including a right to preserve the quality of the water. If that right is interfered with because of pollution, it may give rise to an actionable nuisance. The question for the Supreme Court to determine was the extent of the application and effect of the Act on existing common law rights.

A detailed consideration of the relevant statutory scheme is outside of the scope of this case report but, in summary, United Utilities argued that the statutory framework, in particular the duties and functions imposed by it, would prevent MSCC from pursuing a claim in private nuisance. MSCC argued that, on a proper interpretation, the Act did not ouster its common law claim.

The Court sided with MSCC and gave the following reasons:

1. Nothing in the relevant provisions of the Act authorise a sewage undertaker such as United Utilities to discharge foul water into a watercourse. A sewage undertaker is expressly required to carry out its functions so as *not* to create a nuisance.

2. Any argument that the polluting discharges could be regarded as having been impliedly authorised by Parliament, because they are an inevitable consequence of United Utilities' performance of its statutory powers and duties under the Act, could not be supported. United Utilities could have avoided contamination of the Canal if it had invested in improved infrastructure and treatment processes.

3. A number of provisions of the Act indicate that Parliament's intention, in enacting the legislation, was *not* to exclude the common law rights of those with property rights in watercourses:

    a. Depriving a victim of nuisance of their common law rights of action would be a substantial change to the law as it stood before the Act came into being. In the judgment, the Court considered in detail relevant case law dating back as far as the 1850s to show the existence of the common law right. The Act is a consolidation act, designed to reorganise and restate the existing law so that it is clearer and easier to understand, rather than to effect substantive changes.

    a. The Act is detailed and elaborate legislation. It would be surprising if Parliament had left an important change to the law to be implied rather than expressly stated. The Court also considered the principle of legality, which provides that fundamental common law rights, such as rights of action to protect private property, are not taken to be abrogated by statute unless there is express language or necessary implication to that effect.

    a. The Act makes express provision for statutory compensation where damage is caused by acts of sewerage undertakers that are authorised by the Act (for example, the laying of pipes across private land). However, there is no similar compensation available for damage caused by acts which are not authorised (such as discharge of pollutants). The Court held that this strongly supports the view that victims of unauthorised damage retain their common law rights of action – if the position were otherwise, those victims would be left without any remedy for damage suffered and (perversely) treated less favourably than victims of authorised damage.

<u>Injunctive relief</u>

Whilst confirming the availability of common law damages for owners of polluted waterways, the Court did cast doubt on the availability of an injunction as a remedy in some circumstances. United Utilities raised the potential for injunctive relief to disrupt the enforcement regime envisaged by the Act. Improvements to the sewerage system are prioritised through discussions between the relevant sewerage undertaker, the Environment Agency and Ofwat and agreement of five-year programmes of service provision (to include details as to the amount of capital expenditure on improvements and the level of that expenditure that a sewerage undertaker may seek to recoup from customers).

The Court accepted that injunctions requiring sewerage undertakers to spend significant sums on new infrastructure aimed to prevent nuisance might unhelpfully cut across that specific statutory regime (not to mention interfere with the operation of a system working to process sewage). That may militate against the granting of injunctions that required the upgrading of a sewerage system. However, the Court was careful to make clear that this does not in any way exclude a remedy in the form of damages and the Court referred its power in equity to award damages for future or repeated invasions of rights (for example, pending the upgrading of sewerage infrastructure in line with Ofwat's approval).

Implications

The Supreme Court did not of course, for the reasons mentioned above, give any consideration as to whether or not a private nuisance could be made out on the facts. MSCC can be expected to face a number of challenges if it does decide to pursue a nuisance claim. For example, the question of causation is highly fact-specific in the context of private nuisance and demonstrating that issues with water quality in large and fast-moving watercourses are caused by the discharge of sewage from outlets that only operate periodically when conditions require it is likely to prove challenging.

There is also the question of quantum. Private nuisance is an area noticeably lacking in reported decisions on the amounts received by successful claimants and the judgment refers to previous case law on the topic where public interest has been cited as a relevant factor in relation to appropriate remedy. When quantifying damages, the Court may give consideration to factors such as the capital investment requirements on sewage companies and the potential for an increase in private claims to impact the Ofwat price-setting process that determines what consumers must pay. That could impact a claimant's decision as to whether nuisance claims are worth pursuing.

What is more certain is that a wide range of parties will be considering the judgment with interest, including environmental groups and claimant law firms. The issue could hardly be more topical at a time when water and sewage companies are under significant pressure, both financially and in terms of scrutiny over the discharge of waste material. There is already talk of the floodgates having been opened and undertakers in the industry should expect and plan for receiving test nuisance claims on the back of the Supreme Court's decision.

We are experienced at CMS in defending private nuisance claims including group actions brought by large numbers of individuals. Please get in touch with the authors of this article if you are affected by the issues in this case, or similar cases, and would like advice as to how to deal with claims received or potential future claims.

A copy of the judgment is available here.

About the authors

Neal Gibson
Neal is a partner in the Dispute Resolution Group at CMS, London. He has a wide-ranging commercial litigation and arbitration practice, representing clients in complex, high-value, domestic and multi-jurisdictional disputes.

Neal's practice covers a variety of industry sectors including waste management and environmental services. Neal also has extensive experience of handling, both at first instance and on appeal, high profile follow-on actions under group litigation orders.

Tom Sandeman
Tom is a Senior Associate in the Dispute Resolution Group at CMS, London. He specialises in commercial dispute resolution and has experience dealing with English High Court litigation and international arbitration, as well as pre-litigation advice and litigation strategy. Tom advises clients in a wide range of industry sectors with a particular focus on environmental disputes, including defending corporate clients against group claims brought by large numbers of private individuals.

High Court legal battle over bullish legal costs

Proportionality in costs

→ The arbitrator's balanced approach fit the circumstances.

In *StockCo Ltd v The Big Basin Ltd* [2024] NZHC 2438, a legal costs dispute arose after a final arbitral award was made in a long-running dispute involving a livestock agreement regarding the purchase and rearing of a herd of bulls. The cost dispute made its way to the High Court, where the issue over proportionality and the arbitrator's discretion to award costs were examined.

Written by **SAM DORNE**

Background

StockCo Ltd (**StockCo**), a livestock financier, provided funding for the purchase of 787 bulls, which were subsequently farmed by The Big Basin Ltd (**Big Basin**). The dispute arose after Big Basin defaulted on its obligations under the master livestock agreement, leading StockCo to terminate the agreement in August 2019.

The core dispute was over Big Basin's liability for the bulls, specifically whether it had received all of them. The arbitral tribunal ruled in favour of StockCo, determining that Big Basin was liable for over $1.2 million.

Arbitrator's ruling on costs

StockCo claimed over $843,000 in costs (tribunal fees, legal fees, and disbursements).

The arbitrator looked at proportionality and reasonableness. The arbitrator expressed concern over the proportionality of the costs claimed by StockCo, especially the pre-hearing costs, which he deemed excessive given the nature of the dispute. He also noted that both parties contributed to the complexity of the case but primarily attributed more failings to Big Basin, which had pursued a flawed defence. Nevertheless, at the same time the arbitrator found that StockCo did not fully acknowledge its own contributions to the complexities of the case, particularly regarding its processes and record-keeping.

The arbitrator awarded costs of $375,000 and $75,000 in disbursements. StockCo argued that this represented only 51% of its total costs and deemed the award unreasonable, prompting it to apply for a variation under the Arbitration Act 1986. Big Basin argued that the costs awarded were reasonable and that the arbitrator had exercised his discretion correctly.

The cost issue went to the High Court.

High Court decision

The High Court examined the arbitrator's reasoning over costs and found it was well-supported and reasonable. The High Court noted that the arbitrator was in a good position to make a ruling on costs as he examined each of the points raised *with the depth of understanding that can only come from someone who has presided over the proceeding for several years and who has seen primary witnesses in person.*

The High Court noted that StockCo's claim of being "wholly successful" in the primary dispute was countered by Big Basin's assertion that it had succeeded on certain lesser issues. The High Court recognised that while StockCo had achieved a favourable outcome, it had also contributed to the intricacies of the case.

In looking at proportionality the High Court held:

> There was no unfairness in my view in the arbitrator not taking discounts on recorded time into account and there can in my view be no issue with his conclusion that the pre-hearing costs, in particular, were out of proportion with the dispute. It is recognised, as Mr Morrison said, that StockCo needed to spend considerable time dealing with Big Basin's allegations in response, even if they were regarded as being untenable. But proportionality was required nonetheless.

Standing back, the High Court held, it could be said that StockCo's legal costs were *of a magnitude which an objective observer would not have expected for this litigation, however egregious Big Basin's conduct may have been*. The High Court was careful not to make this observation as a criticism. It stated that StockCo was entitled to incur whatever level of costs it considered appropriate. But when looking at everything in the round the arbitrator's conclusions about the proportionality of StockCo's legal fees, and the adjustments that the arbitrator made, were reasonable.

The High Court upheld the arbitrator's award and declined StockCo's application to vary the costs, affirming the arbitrator's discretion in determining the allocation of costs.

Conclusion

The case underscores the importance of proportionality in costs awards in arbitration, the responsibilities of both parties to manage costs effectively, and the discretion afforded to arbitrators in determining reasonable costs in the context of the specific circumstances of the dispute. The arbitrator's balanced approach and thorough analysis were recognised as appropriate in the face of a contentious arbitration process.

About the author

Sam Dorne works as a Knowledge Manager in The ADR Centre's Knowledge Management Team, working with NZDRC and NZIAC. He recently returned to NZ after nearly 19 years of living in the UK where he spent the last several years working as a civil litigation solicitor mainly dealing with the recoverability of legal costs and consumer claim cases. He has experience in advocacy, case management and legal drafting and had several cases go to the Court of Appeal in England.

Apparent bias: the Hong Kong Court of First Instance did not find any, but the Court of Appeal will have more to say soon

Written by **ALEXANDER LYALL**

The Hong Kong Court of First Instance (the Court) has granted a party leave to have their allegations related to bias heard in the Court of Appeal.[1] The decision may come as a surprise to many. In its initial decision, the Court had thoroughly rejected claims of apparent bias.[2]

We discuss the original case in detail below:

TGL v. SDC [2024] HKCFI 1796

An array of associations

The claimant, TGL, had been successful against SDC in arbitration in China. TGL then sought to have the Court enforce the resulting award. The respondent, SDC, argued that the nature of the arbitrator's relationship with TGL demonstrated bias.

SDC alleged that the relationship was indirect. Over the course of many years, the arbitrator had associated themselves with the "corporate grandparents"[3] of TGL. SDC complained that this association involved:

- the arbitrator giving a lecture at a conference on the invitation of a "corporate grandparent";
- the arbitrator's firm acting for a "corporate sister" of TGL; and
- the arbitrator's firm being awarded a tender by the "corporate grandparents" of TGL.

How to establish apparent bias

The Court emphasised that the test of apparent bias did not concern whether the unsuccessful party

1 *TGL v. SDC* [2024] HKCFI 2393.
2 *TGL v. SDC* [2024] HKCFI 1796.
3 For a more comprehensive explanation of the web of companies involved, see above 2 at [9].

Duties on arbitrators

→ The Court of Appeal will reassess the duty to disclose.

thought there was bias. Rather, the authority lay with the *viewpoint of the hypothetical objective fair-minded and informed observer*.

The Court ran through further descriptions of how a court may establish apparent bias, including whether:

- *an objective fair-minded and informed observer, having considered the relevant facts, would conclude that there was a "real possibility" that the tribunal was biased;*[4]
- there is *only a real possibility of unconscious bias*[5] and
- bias would be picked up by a certain type of individual – one who is not a lawyer but is also not completely *uninformed and uninstructed* on the issues to be decided, or the governing law.[6]

The Court concluded that while the perception of impartiality was important, courts were also not to take a *hypothetical or unrealistic* view of the significance of the arbitrator's associations. Where a court does identify links, it must look for a rational basis to say that these are capable of influencing the impartial mind of the decision maker.

What would the objective and informed observer think?

The Court was comfortable in finding that there was no apparent bias. The arbitrator had links only with what the Court called TGL's "loosely associated companies". Such associations would not cause the observer to feel *unduly suspicious* of the arbitrator's impartiality. There was no reason to suspect that the arbitrator had knowledge of the links, and that the non-disclosure was deliberate.

No problems enforcing the award

Having found no bias or lack of impartiality, the Court held that enforcing the award would not go against fundamental concepts of morality and justice. Nor would enforcement be *so shocking to the court's conscience as to render enforcement repugnant*.[7]

How about a duty to disclose the connections to the parties?

The association between the arbitrator and TGL had not been declared at any point during the arbitration. TGL stated that the arbitrator had not known of these links. SDC stated that the arbitrator should have known.

Not disclosing the links, SDC argued, denied SDC the opportunity to select another arbitrator. Furthermore:

- the use of a biased arbitrator would mean that the parties' agreement to arbitration could not be valid; and
- to enforce the award would be to go against Hong Kong public policy.

The Court used the reasoning of the lack of bias to dismiss the related, but separate, claims here. The Court put it simply – *if* [the arbitrator] *had no knowledge of the tender and any association with TFH, he was not in breach of his duty to make disclosure.*

TGL v. SDC [2024] HKCFI 1796 – SDC lives to fight another day

Undeterred, SDC sought leave in September to have the matter heard in the Court of Appeal.[8]

For the most part, the Court did not see anything material in SDC's submissions. SDC had still not claimed anything that proved, or would even suggest, that the arbitrator had known about their links to TGL.

Without this, the matter was not worth going further. It would be unlikely that the Court of Appeal would deviate from the Court's view. Principally, that there was not a rational link between the arbitrator and the companies associated with TGL.

The duty to disclose

The Court found that the parties had not discussed the duties regarding disclosure to a sufficient degree. Related to this, the parties had not substantively raised points about whether the arbitrator ought to have known of the connections.

In Hong Kong, this duty is to be considered by way of section 25(1) of the Arbitration Ordinance.[9] Having not properly raised the points, the Court was limited in its ability to consider matters which may have been of importance to the arbitration community.

Consequently, the Court granted SDC the right to appeal.

About the author

Alexander Lyall is a Research Clerk in The ADR Centre's Knowledge Management team, working with NZDRC and NZIAC. He gained his LLB from the University of Canterbury, and he also holds a BA in political science, media studies, and Te Reo Māori. His writing has previously been published by Radio New Zealand, The Spinoff, the Kluwer Arbitration Blog and The Press. Alexander has just completed a Mandarin course at Peking University.

4 *Director General of Fair Trading v Proprietary Association of Great Britain* [2011] 1 WLR 700.
5 *Lawal v Northern Spirit Limited* [2003] UKHL 35.
6 *Johnson v Johnson* (2000) 201 CLR 488.
7 *Hebei Import & Export Corp v Polytek Engineering Co Ltd* (1999) 2 HKCFAR 111.
8 *TGL v SDC*, above n 1.
9 Largely adopting Article 12(1) of the UNCITRAL Model Law on International Commercial Arbitration. Article 12(1) instructs that an arbitrator must disclose to the parties any circumstance present likely to give rise to *justifiable doubts* as to their impartiality.

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