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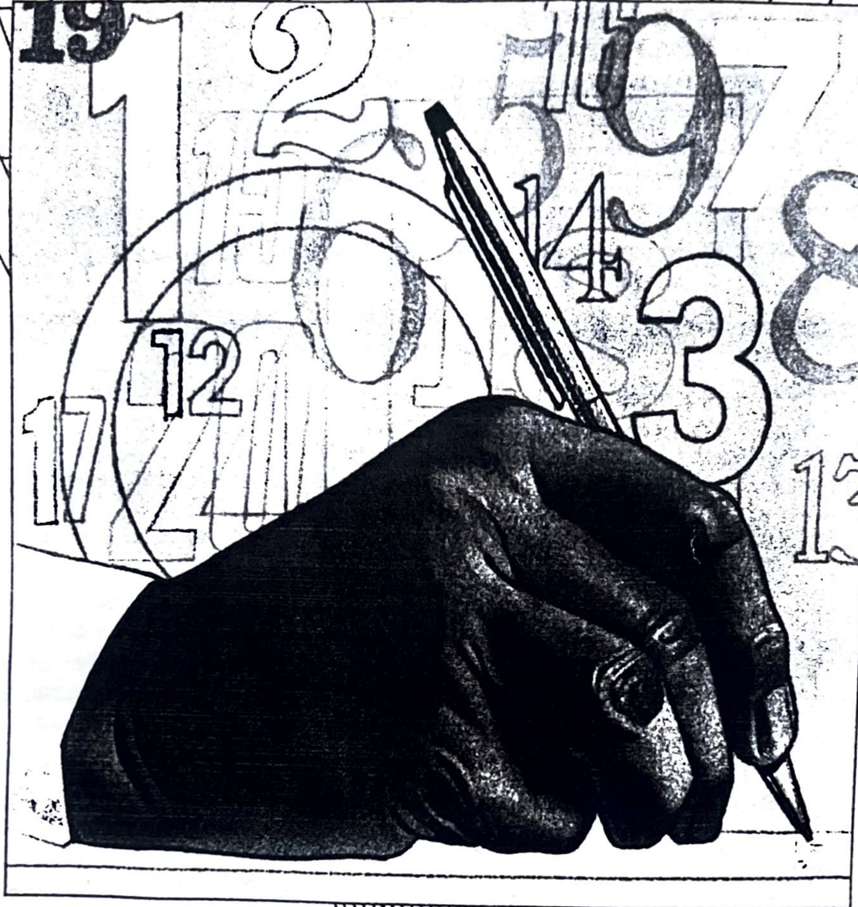

Corporate Laws in the Next Millennium

THE INSTITUTE OF COMPANY SECRETARIES OF INDIA

SETTLEMENT OF COMMERCIAL DISPUTES : INTERNATIONAL ARBITRATION

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INTRODUCTION

Agreement for resolution of commercial dispute by arbitration is very popular and important provision of international commercial agreements which is included in all most every such contract. It is widely recognized that for the settlement of disputes between parties to an international commercial transaction, arbitration has clear advantages over litigation in national courts. A businessman may be unfamiliar with the foreign courts, foreign procedures which may be followed, the laws to be applied, and the mentality of judges. But in an international arbitration, the parties from different countries can provide a procedure and law which is acceptable to both of them.

Some parties due to ignorance, do not understand general and special clauses inserted in arbitration agreement and remain unaware of its financial as well as other impacts on their transaction. The arbitration agreement remains dormant until a dispute or difference arises between the parties. Some time this provision is not invoked for years. But once a dispute arises each and every word of the arbitration agreement is read and interpreted very carefully and implications are noticed. Arbitration is supposed to be simple and cost effective but success of arbitration and costs depends on the provisions and clauses written in the arbitration agreement.

A single provision of law applicable, may change course of the contract and the arbitration. The law applicable should be properly understood and its effects should be analysed at the time of making the agreement. International commercial contracts have involvement of nationals or business entities of two or more countries and subject matter of the agreement also involves connection with two or more countries. Different countries have its own system of law and some times there is conflict of laws. Same contract may be governed by laws of two or more countries and then application in a given situation may be a complicated process. The question whether an arbitration is international or domestic is also significant, as most countries have different legal regimes to govern different type of arbitration.

INTERNATIONAL COMMERCIAL ARBITRATION

International Commercial Arbitration transcends national boundaries. International arbitration usually have a foreign element and most countries treat such arbitration liberally like by providing greater respect for the intentions of the parties and far less judicial intervention in the arbitration process than in the domestic arbitration. Indian Arbitration and Conciliation Act, 1996 has defined International Commercial Arbitration in Section 2(1)(f) as –

> "an arbitration relating to disputes arising out of legal relationships whether contractual or not, considered as commercial under the law in force in India and where at least one of the parties as –

(i) an individual who is a national of, or habitually resident in, any country other than India; or

(ii) a body corporate which is incorporated in any country other than India; or

(iii) a company or an association or a body of individuals whose central management and control is exercised in any country other than India; or

(iv) the government of a foreign country.

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APPLICATION OF LAWS OF DIFFERENT STATES

It is not necessary that entire contract is governed by a single law. It is also not necessary that same law will apply at all times to the contract. The law applicable may change with the stage of the transaction/case. An international commercial agreement has different levels and segments. Indians prefer proper law of the contract to be the Indian law. While concluding an international commercial contract parties have the freedom to choose the governing law, but precise formulations may depend on the facts of each case. There is a standard condition imposed by the Government of India and Reserve Bank of India while approving the technical collaboration and equity participation that the agreement shall be subject to the laws of India. Generally international commercial agreements in India include clause for application of Indian law to the contract. But it is not sufficient to say that contract is subject to Indian laws. This is so because of the autonomy of arbitration clause from the main contract.

PROPER LAW OF CONTRACT

The proper law of the contract is law or relevant legal rules governing substantive issues in disputes. The expression 'proper law of a contract' refers to the legal system by which the parties to the contract itself or its surrounding circumstances, such intention determines the proper law of the contract. Proper law of contract the law which the parties have expressly or impliedly chosen, or which is imputed to them by reason of its closest and most intimate connection with the contract. It must however, be clarified that the expression 'proper law' refers to the substantive principles of the domestic law of the chosen system and not to its conflict of laws rules. The law of contract is not affected by the *doctrine of renvoi*.

Where the intention of the parties is not expressly stated and no inference about it can be drawn, their intention as such has no relevance. In that event the courts endeavour to impute an intention by identifying legal system with which the transaction has its closest and most real connection. Section 28(1) of Indian Arbitration and Conciliation Act, 1996 provides –

(a) in an arbitration other than an international commercial arbitration, the arbitral tribunal shall decide the dispute submitted to arbitration in accordance with the substantive law for the time being in force in India;

(b) in international commercial arbitration, –

(i) the arbitral tribunal shall decide the dispute in accordance with the rules of law designated by the parties as applicable to the substance of the dispute;

(ii) any designation by the parties of the law or legal system of a given country shall be construed, unless otherwise expressed, as directly referring to the substantive law of that country and not to its conflict of laws rules.

(iii) failing any designation of the law under sub-clause (ii) by the parties, the arbitral tribunal shall apply the rules of law it considers to be appropriate given all the circumstances surrounding the dispute.

The expressed intention of the parties is generally decisive in determining the proper law of the contract. Only limitation on this rule is that the intention of the parties must be expressed bona–fide and it should not be opposed to public policy.

Section 9(b) of the Foreign Awards Act, 1961 provided that "Nothing in this Act shall apply to any award made on an Arbitration agreement governed by the law of India". In ***Singer Company case***, (AIR 1993 SC 998), an interim award was made at London by an Arbitral Tribunal constituted by the International Court of Chamber of Commerce in terms of a contract made at New Delhi between National Thermal Power Corporation (for short NTPC) and a foreign contractor namely Singer Company for the supply of equipment, erection and commissioning of certain works in India. NTPC filed a petition in Delhi High Court under Section 14, 30 and 33 of the Arbitration Act, 1940 to set aside the award. The High Court had held that the award fell within the ambit of the Foreign Awards (Recognition and Enforcement) Act, 1961; London being the seat of arbitration, English Courts alone had jurisdiction to set aside the award. In an against the judgements the appeal of Supreme Court has held that the Delhi High Court was wrong in treating the award in question as a foreign award. The Foreign Awards Act has no application to the award by reason of the specific exclusion contained in Section 9 of that Act. The award is governed by the laws in force in India, including the Arbitration Act, 1940.

The provision of the Section 9 which was dormant until decision of the Supreme Court of India in ***Singer Company case*** was widely criticised by experts and persons involved in International Trade. Section 9 of the Foreign Awards Act caused worries for the international business community. Representations were made to the Government of India to reconsider the matter and review the law. Ultimately the provision contained in Section 9 was dropped while re-enacting and consolidating arbitration law in India i.e. the 1996 Act. It has been specifically provided in Section 2(2) of the 1996 Act Part I relating to domestic arbitration shall apply where place of arbitration is in India and further clarified in its Section 2(7) that an arbitral award made under Part I shall be considered as a domestic award. Hence an award made outside India, can not be considered as domestic award under the provisions of the 1996 Act.

In the absence of an express statement about the governing law, the inferred intention of the parties determines that law. The true intention of the parties in the absence of an express selection, has to be discovered by applying "sound ideas of business, convenience and sense to the language of the contract itself." ***Jacobs, Marcus & Co.*** Vs. ***The Credit Lyonnais***, (1884) 12 QBD 589, 601 (C.A.) Selection of courts of a particular country as having jurisdiction in matters arising under the contract is usually, intention of the parties that the system of law followed by those courts is the proper law by which they intend their contract to be governed. However, the mere selection of a particular place for submission to the jurisdiction of the courts or for the conduct of arbitration will not, in the absence of any other relevant connecting factor with that place, be sufficient to draw an inference as to the intention of the parties to be governed by the system of law prevalent in that place. This is specially so in the case of arbitration, for the selection of the place of arbitration may have little significance where it is chosen, as is often the case, without regard to any relevant or significant link with place. This is particularly true when the place of arbitration is not chosen by the parties themselves, but by the arbitrators or by an outside body, and that too for reasons unconnected with the contract. Choice of place for submission to jurisdiction of courts or for arbitration may thus prove to have little relevance for drawing an inference as to the governing law of the contract, unless supported in that respect by the rest of the contract and the surrounding circumstances. Any such clause must necessarily give way to stronger indications in regard to the intention of the parties. (See the Fehmarn, (1958) 1 ALL ER 333.)

The court imputes an intention if proper law is not selected by the parties by applying the objective test to determine what the parties would have as just and reasonable persons intended the applicable law had they applied their minds to the question.

The place where the contract was made, the form and object of the contract, the place of performance, the place of residence or business of the parties, reference to the courts having jurisdiction and such other links are examined by the courts to determine the system of law with which the transaction has its closest and most real connection.

The Privy Council in ***Mount Albert Borough Council*** Vs. ***Australian Temperance and General Mutual Life Assurance Society Ltd.*** (1938) AC 224 at 240 has observed that

> "The proper law of contract means that law which the English or other Court is to apply in determining the obligations under the contract.... It may be that the parties have in terms in their agreement expressed what law they intend to govern, and in that case prima facie their intention will be effectuated by the court. But in most cases they do not do so. The parties may not have thought of the matter at all. Then the court has to impute an intention, or to determine for the parties what is the proper law which, as just and reasonable persons, they ought or would have intended if they had thought about the question when they made the contract....".

It is an internationally recognised principle that awards in the territories of a foreign country are considered as foreign awards. It is very important to know the law before agreeing to it. In some Middle East countries, the claim of interest is illegal and can not be allowed, the arbitrators are required to have religious qualification of being Quazi, and provides restriction on women to act as arbitrator etc.

NEUTRAL LAW AND VENUE OF ARBITRATION

Arbitration in international commercial contracts is preferred over litigation because arbitration is informal, faster, less costly, equitable and conciliatory. Sometimes parties opt arbitration for resolution of a

commercial dispute instead of litigation in open court for the sake of confidentiality and privacy. The parties are usually reluctant to submit their dispute to the national courts of one of the parties due to fear of bias and nationalistic sentiments. Arbitration agreement enables the parties from different nationalities to avoid submitting dispute to the national courts of either of them. It offers choice of judges thereby avoiding fear of biased judgement.

It is repeatedly suggested by the foreign investors with respect to private power projects in India where a foreign investment is attracted that the agreement should be governed by a law neutral to the contracting parties, for example Swiss or English law. It is generally felt that venue for settlement of disputes should also be out side the countries of the contracting parties. Geneva or London are considered as arbitration friendly venues and these have been agreed as the venue for arbitration in number of arbitrations. Government of India has agreed to clauses providing arbitration at London or Geneva. Enrone Power Company's dispute with State of Maharashtra was referred for adjudication at London. Foreign parties usually demand application of rules of arbitration of International Court of Arbitration of International Chamber of Commerce, Paris.

In truth, any international commercial arbitration agreement is a forensic mine field. During its course, as many as five or six different national systems of law, or legal rules, may come into play. It would be too much to expect that there will not be material difference between them. On the contrary the potential for conflict is great.

LAW GOVERNING ARBITRATION AGREEMENT

Most legal systems in the world accord parties considerable freedom in determining arbitration procedure, while reserving the right to ensure the fairness and integrity of the process. International conventions on arbitration are designed to provide an effective international regime for the conduct of arbitration's and obviate the need for states to establish their own domestically influenced regimes. The New York Convention governs only the recognition and enforcement stage of the arbitral process and does not extend to the arbitration stage. Most states have introduced domestic standards in this area to cover the lacunas left by the Convention.

The proper law of the arbitration agreement is normally the same as the proper law of the contract. It is only in exceptional cases that it is not so even where the proper law of contract is expressly chosen by the parties. The law governing arbitration agreement applies to issues such as consent of parties (such as whether or not the agreement was induced by fraud mis–representation or undue influence), validity, effect, interpretation and scope of the arbitration agreement. Such law will decide whether the arbitration clause is wide enough to cover the dispute between the parties. Such law will also ordinarily decide whether the arbitration clause binds the parties even when one of them alleges that the contract is void, or violable or illegal or that such contract has been discharged by breach or frustration.

The proper law of arbitration agreement will also decide whether the arbitration clause would equally apply to a different contract between the same parties or between one of those parties and a third party. Proper law of arbitration agreement should be distinguished from the law applicable to capacity of the parties to arbitrate (subjective arbitrability) and the amenability of subject matter of a dispute to arbitration (objective arbitrability).

LAW GOVERNING ARBITRATION PROCEDURE

The arbitration proceedings are conducted in the absence of any agreement to the contrary, in accordance with the law of the country in which the arbitration is held. On the other hand, if the parties have specifically chosen the law governing the conduct and procedure of arbitration, the arbitration proceedings will be conducted in accordance with that law so long as it is not contrary to the public policy or the mandatory requirements of the law of the country in which the arbitration is held. If no such choice has been made by the parties, expressly or by necessary implication, the procedural aspect of the conduct of arbitration will be determined by law of the place of seat of arbitration.

ENFORCEMENT OF ARBITRAL AWARDS

New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards has been accepted and signed by almost all important countries in the world. Hence an arbitral award is enforceable against a party to the arbitration agreement in any territory of any Contracting State.

An award made at London, may be a purely domestic award in U.K., can be enforced anywhere in India. Similarly an award made at New Delhi, purely domestic award in India, can be enforced against the party at New York or London or anywhere in a country which is a signatory to the Convention. Challenge to a foreign award is subject to law of the territory where it has been made. An arbitrator sitting in New Delhi can write an award/judgement over a subject matter of dispute, may be located in or relating to ten countries, like infringement of patent or trademark, immovable property, or accounts; and such award shall be enforced by the courts in those countries in accordance with the Convention. The recognition and enforcement of a foreign award is easier and simplified under provisions of the New York Convention.

Arbitral awards are like an international currency which can be encased in any country which a party to the New York Convention and where other party has the property.