

The Pitfalls of Arbitral Dualism: A Comment on *Paharpur Cooling Towers Ltd v Paramount (WA) Ltd* [2008] WASCA 110

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Australian arbitration law is dualist: domestic arbitrations are regulated by the uniform state *Commercial Arbitration Acts* (1984-85) and international disputes fall under the *International Arbitration Act* 1974 (Cth).¹ The IAA adopts the UNCITRAL *Model Law on International Commercial Arbitration* (1985) and ratifies the *New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (1958). Whilst dualism can have practical benefits, in a federated context it can cause undesirable variation in the way state and federal courts read arbitration clauses. Australian state courts sometimes arrive at narrower interpretations than federal courts, where the public policy imperative of promoting International Commercial Arbitration (ICA) is seen as requiring liberal constructions of agreements to arbitrate. The decision in *Paharpur Cooling Towers Ltd v Paramount (WA) Ltd* illustrates this variance: the Court of Appeal of the Supreme Court of Western Australia held that a dispute relating to a subcontractor's liability under a bill of exchange was not arbitrable because the bill named as co-acceptor a third party who had not signed an agreement to arbitrate with the Claimant.

The dispute in *Cooling Towers* arose out of a contract for the design, supply and installation of two cooling towers at an ammonia plant being built by Hong Kong company Paramount for Australian company Burrup Fertilisers Pty Ltd (BFPL). The contract price was \$8,074,770. Indian company Paharpur Cooling Towers undertook to procure and ship from India certain items equipment, and Paramount agreed to pay the contract price (less 5%) within thirty days of the date of shipping as confirmed by the bill of lading. Clause 22 of the contract specified that, in the event of a dispute, the Principal (meaning Paramount) at its sole discretion-

*shall determine whether the parties resolve the dispute by litigation within the jurisdiction of the courts of Western Australia or arbitration under the Commercial Arbitration Act. [Paramount] shall notify [Paharpur], by notice in writing, of its decision to refer the dispute to litigation or arbitration within 28 days of either [Paramount] or [Paharpur] electing that the dispute be determined be either litigation or arbitration.*²

Significantly, the clause further provided that the arbitration was to be conducted by an engineer. About a year later the parties agreed to amend the payment terms of the contract. The new arrangement was that Paramount would pay the balance of the contract price, less \$4,000,000 (plus interest) on first clearance of the equipment from India. The remaining \$4,000,000 was payable to Paharpur 180 days from the date of shipment of the last batch of equipment from India. The parties agreed that this final instalment would be the subject of a bill of exchange accepted by Paramount and its principal, BFPL. Guarantees were put in place by Burrup Holdings Pty Ltd and Mr Pankaj Oswal as trustees for the Burrup Trust.³ Burrup Holdings owns BFPL. The equipment was delivered and Paramount refused to pay. Paharpur commenced action against Paramount, BFPL and the trustee guarantors in the Supreme Court of Western Australia for the monies said to be due and payable under the agreement⁴. After serving Paharpur with a notice referring the dispute to arbitration under Clause 22, Paramount applied to the Supreme Court for a stay.

Paramount's application was brought under IAA section 7, with applications in the alternative under section 53(1) of the *Commercial Arbitration Act* 1985 (WA)⁵ and the inherent jurisdiction of the court. The matter came on before Acting Master Chapman on 5 September 2007. At the hearing, Paharpur conceded that its claim under

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¹ Hereinafter referred to as the 'IAA'.

² *Paharpur Cooling Towers Ltd v Paramount (WA) Ltd* [2008] WASCA 110 at [5], hereinafter referred to as '*Cooling Towers*'.

³ Above note 2 at [8].

⁴ Civ 1549 of 2007.

⁵ Hereinafter referred to as the 'CAA'.

the contract should go to arbitration, but argued that its claim against Paramount and BFPL under the bill of exchange should remain before the court. Acting Master Chapman held that Clause 22 was wide enough to encompass the claim under the bill, commenting in *obiter* that the bill of exchange ‘was born out of the contract and the issues in dispute under the contract have a clear connection with the payment under the bill of exchange’.⁶ Acting Master Chapman also rejected Paharpur’s contention that the disputes clause of the contract excluded the operation of the IAA. Paharpur’s action was stayed in full.

Paharpur appealed on a number of grounds, of which the Court of Appeal only had occasion to consider the first: that the learned Acting Master erred in law by finding that the bill of exchange was subject to the dispute resolution clause in the contract and that Paharpur’s action on it should be stayed in favour of arbitration along with the rest of its claims.⁷ Counsel for Paharpur argued that the bill of exchange was a ‘stand alone contract’ between three parties and was not subject to the arbitration clause.⁸ Counsel also contended that it could never have been the intention of the parties to bind a third party to their arbitration clause, and that because BFPL never was not a party to the arbitration agreement its liability under the bill of exchange could only be resolved by the court. It was also submitted that that it would be inappropriate for an engineer to determine the strictly legal issue of liability under the bill of exchange.⁹ Paramount responded that it was a matter of construction. Counsel for the Respondent submitted that it is well settled that arbitration clauses should be construed broadly and liberally, and the mere fact that a third party had assumed concurrent liability under the bill of exchange did not mean that the rights and liabilities of Paharpur and Paramount under that instrument could not be settled by arbitration.¹⁰ Both parties made submissions on the applicable law, Paharpur arguing that Clause 22 adopted the CAA as *lex arbitri* and Paramount arguing for the application of the IAA.

The matter was heard by President Steytler and Acting Justice of Appeal Newnes. The Court of Appeal quickly identified the question as being whether the claim under the bill of exchange was a ‘Dispute’ for the purposes of Clause 22. Clause 2 of the contract defined ‘Dispute’ in broad terms:

*‘Dispute’ means a dispute or difference between the parties as to the construction of the Contract or as to any matter or thing of whatsoever nature arising, whether antecedent to the Contract and relating to its formation or arising under or in connection with the Contract, including any claim at common law, in tort, under statute or for restitution based on unjust enrichment or for rectification or frustration or a dispute concerning a direction given and/or acts or failing to act by the Engineer or the Engineer’s Representative or interference by the Principal or the Principal’s Representative.*¹¹

Although the Court of Appeal did cite a number of state, federal and House of Lords decisions as authorities for the liberal construction of arbitration agreements, the Court showed itself reluctant to accept the principle of liberal construction as a ‘rigorous notion’.¹² Instead, the Court of Appeal preferred the contractual intentions of ‘rational businessmen’¹³ as the touchstone for interpretation. This is consistent with the doctrine of leading ICA seats: the agreement to arbitrate is a contract and must be interpreted as such. The Court concluded that the arbitration clause in the instant matter was

*intended to apply to a dispute between the parties to the contract only. It was not intended to apply to a dispute involving the parties and a stranger to the contract such as that which arose here, where the dispute involves the liability of to one party to the contract (as the drawer/payee) of two acceptors of a bill of exchange, one of the acceptors being a party to the contract and the other a stranger to it.*¹⁴

⁶ Above note 2 at [21].

⁷ Above note 2 at [25].

⁸ Above note 2 at [26].

⁹ Above note 2 at [27].

¹⁰ Above note 2 at [30].

¹¹ Above note 2 at [6].

¹² This expression comes from the judgment of Austin J in *ACD Tridon Inc v Tridon Australia Pty Ltd* [2002] NSWSC 896, cited at paragraph 34 of the judgment of the Court of Appeal in *Cooling Towers*.

¹³ Above note 2 at [37], citing with approval the judgment of Lord Hoffman in *Fiona Trust & Holding Corporation v Privalov* [2007] UKHL 40 at [13].

¹⁴ Above note 2 at [45].

The Court of Appeal concluded that Paharpur's claim in relation to the bill of exchange did not give rise to a dispute within the meaning of Clause 22 of the contract.¹⁵ The appeal was allowed, and the Acting Master Chapman's decision was set aside in so far as it stayed the civil proceeding on the bill.¹⁶

The Court of Appeal in *Cooling Towers* characterised BFPL as a 'stranger' to the otherwise widely cast agreement to arbitrate. This would appear to be a narrow reading of the clause. The Court of Appeal's apparent reluctance to accept the public policy rule of liberal interpretation – sometimes referred to as the 'Mitsubishi Doctrine' after the landmark United States Supreme Court decision in *Mitsubishi Motors Corp v Soler Chrysler Plymouth Inc*¹⁷ – is to be contrasted with the *dicta* of Justice Allsop of the Federal Court in *Comandate Marine Corp v Pan Australia Shipping Pty Ltd*.¹⁸ In *Comandate Marine* Allsop J approved of the liberal approach to the construction of arbitration clauses and declared the narrow approach taken in *The Kiukiang Career*¹⁹ to be bad law.²⁰ Allsop J also expressly referred to the public policy consideration that favours arbitration as a means of settling international commercial disputes as a source of the rule that arbitration agreements are to be broadly and effectively construed.²¹ In *Cooling Towers* the WA Court of Appeal challenged the primacy of public policy in this context when it approved the statement of Austin J in *ACD Tridon Inc v Tridon Australia Pty Ltd* [2002] NSWSC 896 that 'Australian courts are not constrained by considerations of public policy to adopt a "liberal" construction of arbitration clauses'.²²

The decision in *Cooling Towers* suggests that the Australian version of the *Mitsubishi* Doctrine is more a feature of federal arbitration law than state arbitration law. If the *Cooling Towers* appeal was run in a federal court the writer suspects that it would have been dismissed. This is because Australian federal courts have developed the rule of liberal construction in a UNCITRAL Model Law/New York Convention setting in which international jurisprudential trends are received *directly* from leading ICA seats. Although the common law that informs the state commercial arbitration statutes is in a process of harmonisation with Model Law jurisprudence – and state arbitration law is thereby *indirectly* receiving doctrine from leading ICA seats – *Cooling Towers* illustrates the sporadic resistance of state courts to this process of reception. As a matter of law, the characterisation of the co-acceptor BFPL as a 'stranger' reflects a strict approach to arbitrability and the prohibition against arbitration without privity. Broadly speaking, the doctrine of 'non-arbitrability' is founded upon the public policy rule which holds that the rights of the public must be determined in public. In arbitral contexts there is growing authority for the proposition that privity is a matter of degree: there are *distant* third parties (true 'non-parties' such as consumers in a *Trade Practices Act* price fixing claim) and there are *proximate* third parties (or mere 'non-signatories'). Where complex corporate structures are involved, the rule of 'no arbitration without privity' is challenged by the emerging 'Group of Companies Doctrine'. This doctrine was first applied in 1982 by an International Chamber of Commerce tribunal in the *Dow Chemical* arbitration.²³ In upholding the decision of the ICC tribunal the Paris Court of Appeal held:

The arbitration clause inserted in an international contract has self-standing validity and effectiveness which requires that its application be extended to parties which are directly implicated in the performance of the contract...²⁴

German courts have shown themselves unwilling to accept the Group of Companies Doctrine. After also initially resisting, Swiss courts now accept *Dow Chemical*: in the 2003 case *X S.A.L., Y S.A.L. et A v Z* the Federal Supreme Court held that the fact that a contract containing an arbitration clause was not signed by a

¹⁵ Above note 2 at [46].

¹⁶ Above fn 2 at [50].

¹⁷ 473 US 614 (1985). It is important to note that the United States is not a Model Law jurisdiction. US federal arbitration law has, instead, been brought into line with Model Law standards by Supreme Court Action.

¹⁸ [2006] FCAFC 186.

¹⁹ *Hi-Fert Pty Ltd v Kiukiang Maritime Carriers Inc (No. 5)* (1998) 90 FCR 1.

²⁰ Above fn 18, at [194] per Allsop J.

²¹ *Ibid.*, at [184], [193-4].

²² *ACD Tridon* per Austin J at [120].

²³ *Isover St Gobain v Dow Chemical France et al.*, ICC Case 4131 (1982) Paris Court of Appeal on 21 October 1983 [1984] Rev Arb 98.

²⁴ Decision of the Paris Court of Appeal, 21 October 1983 [1984] Rev Arb 98; (1st Ch D) 1997 Rev Arb 550

third party did not operate as a formal bar to the extension of the clause to that third party.²⁵ The Group of Companies Doctrine has enjoyed a mixed reception in the common law world. United States superior courts liberally apply theories of agency, trust and veil-piercing to bind non-signatories to agreements to arbitrate.²⁶ From the decision of the Commercial Court in *Peterson Farms Inc v C&M Farming Ltd* [2004] EWHC 212 it is clear that English courts treat the identification of the parties to an agreement to arbitrate as a matter of substantive (rather than procedural) law and require clear evidence of agency before they will bind related companies to arbitrate.²⁷ Despite this divergence in municipal judicial opinion, leading ICA practitioners agree that *Dow Chemical* addressed a real procedural need. Writing in 2006 Professor William Park observed:

*the complex structures of many corporate groups means increasingly frequent challenges related to 'non-signatories' whose right or duty to arbitrate is not obvious. In such instances, the arbitrators' jurisdiction must be justified on principles such as agency, piercing the corporate veil, or estoppel.*²⁸

In the instant matter the Group of Companies doctrine was not pleaded. The corporate relationship between BFPL and Paramount was not before the court; the Court of Appeal decided the matter on the definition of 'Dispute' at Clause 2 of the contract. It is submitted, however, that certain facts should have informed the court's reading of Clause 2. BFPL was directly implicated in the performance of the contract. BFPL was principal of the Karratha ammonia plant project. The parent company of BFPL guaranteed Paramount in the transaction, and Paramount appears to have acted as agent for BFPL in the purchase of the equipment from India. In the writer's opinion, the appearance is one of a complex international group of companies.²⁹ The party-crafted definition of 'Dispute' to mean 'any matter or thing of whatsoever...arising in connection with the contract' appears *prima facie* to be wide enough to capture a claim brought under such a crucial contractual instrument as the bill of exchange (which secured payment for almost half of the contract price) even though the instrument was co-accepted by as proximate a 'stranger' as BFPL.

The writer is of the opinion that the learned Acting Master's decision at first instance was consistent with the jurisprudence of leading ICA seats on clause construction and arbitral privity in multi-party disputes. The Court of Appeal's decision in *Cooling Towers* is, on the other hand, at odds with the Federal Court's confirmation of the *Mitsubishi* Doctrine in *Comandate Marine*. *Cooling Towers* isolates Western Australian state law from certain important doctrinal developments in leading ICA seats such as the United States,³⁰ France,³¹ Switzerland³² and England.³³ In this sense, the decision demonstrates Australian dualism in practice: if Australian arbitration law was monist, important doctrines like *Mitsubishi* and *Dow Chemical* would not take so long to filter down to the level of the state court. The increasing international engagement and macro-economic significance of Western Australia dictates that the incorporation of these key new ICA rules should be a priority.

²⁵ *X S.A.L., Y S.A.L. et A v Z, SARL et Tribunal Arbitral CCI*, BGE 129 III 727

²⁶ Hanotiau, Bernard, 'Groups of Companies in International Commercial Arbitration', in Mistelis, L. A., and Lew, J. D. M., *Pervasive Problems in International Arbitration* (Kluwer 2006), p.285. See for example *Thomson-CSF, S.A. v American Arbitration Assoc. and Evans & Sutherland Computer Corp.*, 63 F.3d 773 where the US Court of Appeal for the Second Circuit laid down five principles under which a non-signatory can be bound to arbitrate. See also *JJ. Ryan & Sons vs. Rhone Poulenc Textile, SA*, 863 F.2d 315, 320–21 (4th Cir., 1988)

²⁷ See for example *Peterson Farms Inc v C&M Farming Ltd* [2004] EWHC 212; [2004] 1 Lloyd's Rep 603, 2004 WL 229138 (2004) High Court of Justice, QB Div. Commercial Court), cited in Park, W. W., *Arbitration of International Business Disputes: Studies in Law and Practice* (Oxford 2006) at p.26 (FN 137).

²⁸ Park, above note 28 at 26.

²⁹ This appearance is supported by the fact that a director of Paramount is now a director of BFPL's parent company. According to national broadsheet *The Australian* 'the contractor SNC Lavalin, a Canadian company, had the contract to build the [Karratha ammonia] plant and subcontracted that to Paramount, a Hong Kong company with a registered office in WA which shut up shop last year. Its ownership remains unclear but its directors included Raj Jeyarajah and Vinojit Ambalavaner. Jeyarajah has since been appointed director of Burrup [Holdings] by [Pankaj] Oswal and Ambalavaner has a senior position as director commercial', see 'Legal doubts cloud the rise of the awesome Oswals', *The Australian*, 7 June 2008.

³⁰ *Thomson-CSF, S.A. v American Arbitration Assoc. and Evans & Sutherland Computer Corp.*, 63 F.3d 773

³¹ *Isover St Gobain v Dow Chemical France et al.*, ICC Case 4131 (1982) Paris Court of Appeal on 21 October 1983 [1984] Rev Arb 98.

³² *X S.A.L., Y S.A.L. et A v Z, SARL et Tribunal Arbitral CCI*, BGE 129 III 727

³³ *Peterson Farms Inc v C&M Farming Ltd* [2004] EWHC 212