LAISSEZ FAIRE OR CONTROL – STRIKING A BALANCE: FOREIGN COURTS IN GRANTING ENFORCEMENT TO AWARDS SET ASIDE AT THE SEAT OF ARBITRATION

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I. INTRODUCTION

International Arbitration is today serving as a crown for the obstacle-free and smooth development of international trade and commerce. The precious and unique gems embedded in the tailor made nature of the international arbitration as a crown have proved immensely useful for the international business fraternity. Providing as a universally accepted alternative to the ancient judicial system showing its ageing symptoms, it offers a speedy and binding resolution of disputes.

In a successful arbitration, there is always a winner and a loser. If the loser voluntarily enforces the award in favour of the winner, the need to get that award enforced through foreign courts does not arise. But when it is not done voluntarily, the winner requests the foreign court to give recognition and enforcement to that international arbitral award. The advantage of the arbitration for the successful party is the production of a binding decision on the dispute, so as to be performed without any delay. The parties of the arbitration should carry out the award impliedly, especially considering that they have agreed into the arbitration procedure.

A landmark Convention which brought a wave of revolution in the concept of International Commercial Arbitration is known as the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958. Also known as the New York Convention 1958 (NYC), it was adopted by a United Nations diplomatic conference on 10 June 1958 and was enforced on 7 June 1959.[1] The Convention has been universally accepted as an instrument to strengthen the foundations of international

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[1] For more details, see<www.uncitral.org/uncitral/en/.../NYConvention.html>

commercial arbitration by establishing the rules on recognition and enforcement of international arbitral awards. Widely considered as the foundational instrument for international arbitration, it is applicable on awards which are not considered as domestic awards in the state where recognition and enforcement is sought. But this universal Convention is not free from loopholes, which calls for the need to discuss one of the uncertainties that the Convention has given rise to.

Before going into the controversy which has arisen from the ambiguous provisions of New York Convention on Recognition and Enforcement of Foreign Arbitral Awards 1958,[2] the concepts of recognition and enforcement should be clarified. Recognition is the source of giving effect to the arbitral award. An award can be recognized and still not be enforced. The recognition is often a defensive procedure. It will usually arrive as a remedy used by the courts when a dispute has already been solved through an arbitral process. The party in whose favor the award has been made will object to any relief sought pertaining to the dispute that has already been determined and then will ask the court to recognize it as valid and binding award between the parties. Whereas, the enforcement is not only to recognize the fact that the award has legal force and effect, but to also ensure that it is carried out, as per its terms. Recognition is needed for the enforcement. Also, the enforcement occurs normally in a country different from the place of arbitration, usually where the assets of the unsuccessful party are established.

II. THE CONTROVERSY

A situation of conflict and uncertainty arises when an international arbitral award has been set aside by the court at the seat of arbitration. Recognizing the fifth ground of Article 5(1) New York Convention 1958, some courts refuse enforcement, whereas, relying on more favourable provision in Article 7(1) New York Convention 1958 and the permissive language of Article 5(1) New York Convention 1958, some courts go ahead with the enforcement of such awards set aside by the courts at the seat of arbitration.

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[2] Further details on the Convention can be found online at <www.**newyorkconvention**.org>

> The New York Convention 1958 provides in its Article 5 (1) (e): If the award has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made, the recognition and enforcement of this award may be refused.

The wording of this provision is controversial, mainly because of its permissive language.[3] Moreover, the wording of Article 7 of the NYC 1958 establishes the so called 'more favorable rule', providing that a party seeking recognition and enforcement may make use of a more favorable provision in the local law or in another international treaty. These contradictory provisions lead to different approaches being adopted by courts in different countries where the recognition and enforcement is sought.

In contrast to NYC 1958, Article IX of the European Convention on International Commercial Arbitration 1961 provides for specific reasons for setting aside the arbitral award and the setting aside shall only constitute a ground for refusal of recognition and enforcement, when made for one of these reasons.[4] The reasons enumerated in the said Convention are as follows:

(a) The parties to the arbitration agreement were under the law applicable to them, under some incapacity or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made, or

(b) The party requesting the setting aside of the award was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

(c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration need not be set aside; or

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[3] The controversy arises out of this provision because the wordings are that the recognition and enforcement "may" be refused, and not "shall" be refused.

[4] For further details, see <http://treaties.un.org/doc/Treaties/1964/01/19640107%2002-01%20AM/Ch_XXII_02p.pdf> Accessed on 15th October 2010.

(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or failing such agreement, with the provisions of Article IV of the European Convention.

These reasons are, in principle, the same as the reasons for the refusal of recognition and enforcement of international arbitral awards under Article 5 (1) (a) to (d) of the NYC 1958. The European Convention 1961, by laying down the grounds for setting aside the award, has contributed in bringing clarity to the grounds on which the enforcement of award can be refused by the foreign courts in case of the award being set aside by the courts at the seat of arbitration.

Because of the lack of the grounds to set aside the award at the seat of arbitration, unlike the European Convention 1961, and the ambiguous use of language in the provisions of NYC 1958, various courts in different countries have been taking divergent views on this issue which has led to a great deal of controversy, uncertainty and forum shopping. This situation of conflict and application of domestic standards to international awards has beautifully been framed in the words of former Secretary-General of the ICC courts as:

> a hitherto rock-solid rampart against the true internationalisation of arbitration because in the award's country of origin all means of recourse and all grounds of nullity applicable to purely domestic awards may be used to oppose recognition abroad...[5]

There are primarily and significantly *three basic reasons* which have given rise to this conflicting situation. *Firstly*, the use of the word 'may' and not 'must' in Article 5(1) NYC 1958 makes the language of the provision absolutely permissive, rather than mandatory, giving a discretionary power in the hands of enforcing courts to grant enforcement or to refuse it, even if the award has been set aside by court at the seat of arbitration. *Secondly*, NYC only lays down the grounds for refusing recognition and enforcement in Article 5, but it does not in any way restrict

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[5] Jan Paulsson, *Enforcing Arbitral Awards Notwithstanding a Local Standard Annulment* (LSA), 9 ICC BULL. 14, 19(No. 1, 1998) (quoting Yves Derains, Foreword, in Homage à FrédéricEisemann (Liber Amicorum) 5, 13 (1978)).

the grounds for setting aside the international arbitral awards by the competent courts[6]. This lack of internationally uniform grounds for setting aside the award compels the state courts to apply their domestic and local laws on international arbitral awards, which, many a times may not be recognized by the other foreign states. *Thirdly and lastly*, the more favourable provision of Article 7(1) NYC 1958 which makes an allowance for overriding the provisions of NYC 1958 and provides for the application of more favourable national laws and conventions towards enforcement present in the state where enforcement is sought enhances the discretionary power of the enforcing courts. Hence, this express and bold allowance for application of local requirements of enforcing state has given a wide discretionary power to the state courts where enforcement is sought.

With this background of reasons, the paper will now analyze the two conflicting views taken by the foreign enforcing courts separately.

One view which has been taken by foreign courts is the refusal of enforcement of an award which has been set aside by the competent court. The arguments advanced by the courts taking this view have been numerous. The first argument taken by the courts in favour of this view is that the courts at the seat of arbitration should have some control over the arbitration proceedings happening on their territory, in order to guard against lack of due process, fraud, corruption or other improper conduct on the part of arbitral tribunal. The philosophy behind this view is that these courts seem to have a primary jurisdiction over these proceedings and awards. Secondly, the argument goes behind the real command of Article 5(1) New York Convention 1958 which intends to expressly lay down the grounds for refusal of enforcement. Thirdly, the most undisputable fact about arbitration is the supremacy of the intention of the parties. When the parties have intentionally and wilfully selected a country as the seat of arbitration, they also have intended to apply the laws of that country on the arbitration proceedings and award, unless specified otherwise. Hence, neglecting the command of the courts at the seat of arbitration would in a way violate the intention of the parties to arbitration. Lastly, this view protects the principle of international comity, wherein each state court respects the decision of the other foreign courts.

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[6] The competent court for setting aside an international arbitral award is only the court at the seat of the arbitration.

Another view which has been frequently taken by the courts, especially in France and is popularly known as *'French Exception'* is *to enforce the international arbitral awards notwithstanding their being set aside by the courts at the seat of arbitration.* The courts have been supporting this view with various arguments. The permissive language of Article 5 (1) and the more favourable provisions of Article 7 (1) of NYC 1958 render arguments in the favour of this view.

The landmark decisions from French courts have expressly decided that an international arbitral award is not integrated in the legal system of that state, and it remains in existence even if it has been set aside or annulled by the court at the seat of arbitration. This argument avoids the localization of the spirit of internationalization of arbitral awards and also protects the spirit of international trade and commerce.

These two contradicting views arising from the ambiguity in the New York Convention 1958 in the matter of recognition and enforcement of international arbitral awards set aside abroad allows for different approaches and wide interpretation by various national courts, which causes problematic and uncertain outcomes.

There are some negative consequences emerging from this state of uncertainty. Few of the unpleasant results which may arise from this situation are as follows:

(1) The state of disorder caused by the lack of harmonization[7]

(2) The possibility of biased decisions of enforcement[8]

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[7] The New York Convention 1958 does not provide the contracting States with a harmonic system of recognition and enforcement of awards. There is a minimum ground for coordination where the referred Convention establishes the exclusive jurisdiction of the courts of the place of arbitration to set aside the awards. However, this minor coordination is put at risk when vacated awards are enforced in other jurisdictions. In addition, an individualistic attitude by the countries is not compatible with the development of the commercial relations between individuals of different countries. It can be interpreted as the return to the application of the principle of absolute territorialism.

[8] Although the occurrence of biased decisions must not be considered a presumption, it is reasonable to point out the risk of corruption or to the use of favoritism by the courts particularly sensitive to their national interests. It is clear that courts do not have the powers of an economic regulatory authority. However, the issue subject to arbitration may be related to the national interest, as these issues are commercial relations that can be significant to a country.

[9] The parties are free to choose the seat of arbitration. Thus, when the court of the seat of arbitration annuls the awards and other jurisdiction decides to enforce the award set aside, it can be construed as a restriction of the parties' free will to choose the seat of arbitration.

(3) Violation of the will of the parties[9]
(4) The problem of forum shopping[10]
(5) The unreliability of the international commercial arbitration[11]

These symptoms may cause obstacles in the operation of the international arbitration, since they bring about instability and unreliability, and may also jeopardize the true spirit of arbitration as an effective means of final and binding dispute resolution mechanism. Even though arbitration is a dispute resolution system used since ancient times, the reputation and reliability of arbitration's modern structure is still being constructed. In this sense, the impact that the arbitral decisions may have on the international relations and economy must not be disregarded. Undermining the system may be harmful to international businesses, which involve not only private parties, but also indirectly involves States in matters of great sensitivity.

The *emergent questions* which arise out of these two conflicting views can be as follows:

- How to harmonise and reconcile these contradictory views?
- Where to strike a balance between control by the competent courts and the laissez-faire approach by the foreign courts where enforcement is sought?
- How far shall we allow this control by the competent courts to go in the wake of safeguard against lack of due process and corruption?
- How far can we allow the laissez-faire approach to be followed by the foreign state courts in the wake of upholding international justice?

III. Proposed Solutions

Even though the New York Convention was considered to be a milestone for the facilitation of the procedure of recognition and enforcement of international arbitral awards, it has been caught by its own shortcomings. Following are the few solutions which can be resorted to for overcoming this stigma of uncertainty:

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[10] The parties to arbitration agreement choose the foreign courts of enforcement which have demonstrated pro-enforcement views, such as France.

[11] The flaws in the attempt of coordination by the New York Convention regarding the enforcement of awards set aside bring about some instability and insecurity to the environment of arbitration.

1. Harmonization through a model law

The idea of harmonization through a model law aims at the synchronization of the laws relating to international commercial arbitration. Each state would apply the model law as the base of its own law, with fewer and harmless modifications. But the idea of harmonization seems unrealistic, considering the cultural, economic, legal and political differences among states.

2. Exclusion of annulment proceedings against international awards.

This proposition was made by Professor Fouchard[12], another exponent of the international community of commercial arbitration. He militates for a more autonomous arbitration by combating archaic and biased annulment decisions which could be accomplished by the exclusion of annulment proceedings in the national arbitration law. This has already been happening in Belgian law, but, as popularly known, choosing Belgium as the seat of arbitration is rarely a real choice for companies or states. But the problem attached with this proposition is the lack of universally accepted definition of what is an international award. Other than the definitional aspect, an award is not a contract. It is a private party act with the effect of *res judicata.*

3. Establishment of a supra-national court of control

Similar to the ICSID system, this solution consists in the creation of a supra-national court that would be able to control the arbitral awards: its compliance, its annulment, its revision. This was proposed by Howard Holtzmann[13]. This court would confer more autonomy for arbitration, without any influence of the national courts. With the unification of the laws, by the establishment of the new multi-lateral Convention, the application and interpretation performed by an exclusive supra-national court will become possible and effective. For that, there will be no contradictory decisions, because only one court would have the jurisdiction to handle annulment and enforcement. Universal acceptance of a single unified world court having jurisdiction over the international arbitral awards is again a major challenge which has to be encountered.

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[12] Hamid G. Gharavi, *The International Effectiveness of the Annulment of an Arbitral Award*, KLUWER LAW INTERNATIONAL 151 (2002).

[13] Howard M. Holtzmann and Donald Francis Danovan, ICCA INTERNATIONAL HANDBOOK OF COMMERCIAL ARBITRATION (United State, 1999) 23.

4. Elaboration of a new multilateral Convention

Following the path of the New York Convention, this new multilateral Convention would be established so as to overcome the problems which have arisen from the New York Convention. The new Convention would be responsible for determining the grounds for annulment of awards, the jurisdiction over the annulment of the award, and the annulment/enforcement control. The major problem of having this new multilateral Convention is the trouble of persuading the majority of states in the world to abide to this new instrument. Different from the way the New York Convention treats the matter, the new Convention would have to establish the exclusivity of the courts of the place of arbitration as the competent courts to analyze the request for annulment of the final and binding decision. It would be important as well to determine a more international approach of the grounds for annulment, aiming to avoid any sort of parochial annulment decisions.

IV. Conclusion

In fact, the most workable and efficient solution to this problem is to follow the approach of the European Convention on International Commercial Arbitration 1961 which restricts the grounds for setting aside the international arbitral awards in Article 9(2). This restricting approach has also been followed by the Hypothetical Draft Convention on International Enforcement of Arbitration Agreements and Awards 2008, as summarised by Prof Van Den Berg, in Article 5(3) (g) which says[14]:

> The award has been set aside by the court in the country where the award was made on the grounds equivalent to grounds (a) to (e) of Article 5(3) of this proposed convention.

Accordingly the refusal of enforcement is limited to cases where the award has been set aside on grounds equivalent to grounds (a) to (e) of Article 5(3) of the Draft Convention. (Corresponding to general grounds of setting aside as in Article 34(2)(a) of the UNCITRAL Model Law). Hence, Article 5(3)(g) offers a sound and efficient solution to the conflict arisen from the mandate of NYC 1958. This Hypothetical Draft Convention further resolves the conflict and ambiguity with Article 5(1) limiting the

[14] For Proposed Draft Convention 2008, see<http://www.arbitration-icca.org/media/0/12133699771230/ny_conv_and_hypo_conv_ajb_rev06.pdf>

grounds for refusal of enforcement to this list only, 5(2) further limiting the refusal of enforcement in manifest cases only, and Article 5(3) making the language further unambiguous by using the word '*shall*' and not '*may*'.

The purpose behind these conventions in force and proposed convention as discussed, is to lay down uniform international standard of grounds for the competent courts to set aside the international arbitral awards, so that the award is freed from the application of local requirements and does not remain integrated and embedded in the domestic legal system of the courts at the seat of arbitration. Both the extreme views emerging out of this controversy cannot be accepted in totality and should ideally be reconciled and harmonized in the manner argued above to avoid the problem of uncertainty and forum shopping. It is important to solve this conflict emerging out from a widely accepted Convention to protect the integrity and spirit of international commerce and trade.