**[2015] NZLJ 82**

# Arbitration clauses and the summary jurisdiction: the Supreme Court speaks

Jeremy Johnson, Wynn Williams, Christchurch,

on recent case law

## INTRODUCTION

The question of how to handle arbitration clauses in contracts where there is no clear dispute between the parties is one that has long bothered lawyers and clients. If the other party does not respond to demands for payment/remedy of contractual breaches is it appropriate to issue summary judgment proceedings? If the other party does respond but the alleged defence is not reasonably arguable must the parties proceed to arbitration anyway?

In *Zurich Australian Insurance Limited t/a Zurich New Zealand v Cognition Education Limited* [2014] NZSC 188 the Supreme Court has finally given the answer when it considered the meaning of art 8(1) of sch 1 of the Arbitration Act 1996 which deals with the stay of court proceedings.

In its decision — released even though the parties had settled the dispute after the hearing but pre-judgment — the Supreme Court decided that the only way for parties to avoid referral of matters to arbitration when there is an arbitration clause in place is by demonstrating that there is no bona fide dispute. In other words, it may be that there is no reasonably arguable defence, but that is not a matter for the court to determine.

This article examines the rationale behind that decision which placed considerable emphasis, when interpreting the Arbitration Act 1996, on New Zealand's international obligations under the New York Convention 1958 and on consistency with the Model Law on International Commercial Arbitration adopted in June 1985 by the United Nations Commission on International Trade Law (UNCITRAL).

The decision will have significant practical implications for parties. This article will also consider what those practical implications are and how parties can deal with them. The summary jurisdiction is not often used in arbitrations and the reasons for that appear to be both principled and practical.

Nevertheless there are good reasons — both in terms of principle and practicality — why clients might want to have access to a summary jurisdiction and this article will suggest ways in which that can be achieved.

Overall, although arbitrators are reluctant to rule on a summary basis, recognition should be given to the fact that the courts do it regularly in order to resolve disputes quickly and to prevent unarguable cases from running the full distance. There is wisdom in that and as well as clients acting to ensure that there can be a summary jurisdiction, it is worthwhile arbitrators considering afresh whether it is something that should be allowed.

## *ZURICH V COGNITION*

The case involved a contract frustration insurance policy between Zurich (the insurer) and Cognition (the insured). That policy contained an arbitration clause that said:

> … any dispute, controversy or claim arising out of, relating to, in connection with this insurance policy, shall be finally settled by arbitration. The arbitration shall be conducted in accordance with the rules for the conduct of commercial arbitrations of the Institute of Arbitrators and Mediators New Zealand in effect at the time of the arbitration and shall be conducted in English. The seat of the arbitration shall be Auckland, New Zealand or alternative[ly] Sydney, Australia if mutually agreed by all parties.

Cognition made a claim under the policy which Zurich declined to pay. Cognition then applied for summary judgment (presumably because of confidence in its case). In response Zurich filed an appearance objecting to the jurisdiction of the Court and sought a stay of the proceeding under art 8(1) of sch 1 of the Arbitration Act 1996.

Article 8(1) of sch1 is key to this case. That article says:

> 8 Arbitration agreement substantive claim before court
>
> (1) The court before which proceedings are brought in a matter which is the subject of an arbitration agreement shall, if the parties so request not later than when submitting that party's first statement on the substance of the dispute, stay those proceedings and refer the parties to arbitration unless it finds that the agreement is null and void, inoperative, or incapable of being performed, or that there is not in fact any dispute between the parties with regard to the matters agreed to be referred.

The question before the Supreme Court was summarised at [10] of the judgment, where the Court said it needed to assess the final words in art 8(1) which gives the Court the power to not grant a stay where "it finds … that there is not in fact any dispute between the parties with regard to the matters agreed to be referred" (the "added words").

Two interpretations were put forward. The first was for the Court to find there was no "dispute" then it must be satisfied there was no reasonably arguable defence. The second interpretation advanced was that for the Court to find there was no "dispute" meant it had to be satisfied that any dispute raised was not "bona fide".

The Supreme Court described the competing interpretations as the "broad and narrow tests" (at [10]). The Court of Appeal preferred the broad test (*Zurich Australian Insurance Limited v Cognition Education Limited* [2013] NZCA 180). In a well-reasoned decision given by French J the Court viewed the issue as one primarily of statutory interpretation.

In adopting the broader test (and thus allowing courts to grant summary judgment for disputes subject to arbitration agreements) the Court of Appeal placed emphasis on:

a. the legislative history and broader context of the words that were used in including the approach taken by the English Courts when similar words were used in arbitration legislation there (at [32]–[34] and [48]–[54]);
b. existing New Zealand authority (prior to the Arbitration Act 1996) on the meaning of the words (at [40] and [68]);
c. the fact Parliament did not alter the words despite a review of the Arbitration Act 1996 and knowledge of criticisms of the broad test (which had been adopted by the courts) (at [71]); and
d. the presumption that Parliament "does nothing in vain" — the addition of the words "that there is not in fact any dispute between the parties with regard to the matters agreed to be referred" would be rendered meaningless if the narrow approach was taken (at [67]).

What particularly appeared to sway the Court of Appeal was the fact that in the previous iterations of similar English statutes the English courts had adopted similar words to mean that the court could invoke summary jurisdiction and decline an application for a stay and grant summary judgment when there was not a reasonably arguable defence (at [54]). That jurisprudence was well established by the time the New Zealand Parliament came to add these words into the Arbitration Act 1996.

Further the Law Commission, in the report that lead to the Arbitration Act 1996, appeared to say that the words should be added in order to ensure that "the efficiency of the summary judgment procedure as it has developed under the High Court Rules should not be lost by reason of any implication that a dispute where there is no defence must be arbitrated under an arbitration agreement" (Law Commission, *Arbitration* (NZLC R20, 1991) at [309]). This was confirmed by a 2003 review of the Arbitration Act 1996 by the Law Commission (*Improving the Arbitration Act* (NZLC R83, 2003).

In the Court of Appeal's view those factors trumped New Zealand's obligations at international law. The Arbitration Act 1996 was implemented to give effect to New Zealand's obligations as a party to the New York Convention and was largely based on the Model Law adopted by UNCITRAL. While acknowledging that there was some diversion from the Model Law in this regard the Court did not consider that that should mean the words should be interpreted differently from the way it felt Parliament intended them to be interpreted (at [66] and [73]).

The Supreme Court decision overturned that of the Court of Appeal. A significant point of departure was that the Supreme Court felt that the 'natural meaning' of the words in art 8(1) was the narrow meaning (at [36]). In other words, the fact that art 8(1) refers to "no dispute" rather than "no reasonably arguable dispute" suggests that Parliament did not intend to adopt the summary judgment test when deciding not to grant a stay of a court proceeding. In contrast the Court of Appeal thought the words were capable of bearing either the broad or the narrow meaning.

Further, the Supreme Court placed particular emphasis on New Zealand's international obligations in this area. The judgment says, at [40]:

> It will be recalled that art 8 applies not only where the place of arbitration is New Zealand but also where it is outside New Zealand, so that the added words apply to a range of arbitrations. Accordingly, New Zealand's international obligations are engaged, particularly those contained in the New York Convention. The narrow interpretation of the added words is consistent with those obligations. Promoting consistency with international arbitral regimes based on the Model Law is a stated purpose of the 1996 Act, as is giving effect to New Zealand's obligations under the New York Convention. Moreover, it is well established in New Zealand that if statutory provisions can be interpreted in a way that is consistent with New Zealand's international obligations, they should be so interpreted.

The Supreme Court, at [41], then referred to some relevant academic commentary (Albert Van Den Bergh *The New York Arbitration Convention of 1958* (Kluwer Law International, 1991) at 146–148) to establish that "the added words should have the narrow meaning we favour when assessed against the background of the obligations imposed on contracting states by the New York Convention".

The divergent approaches, and the fact that the Supreme Court adopted an interpretation that had not been consistently adopted by the High Court before (there had been a considerable number of cases that discussed the interpretation of art 8(1)), does raise the question of which court can be considered to be right in terms of legal principle. See, for example, *Yawata Ltd v Powell* HC Wellington AP142/00, 4 October 2000; *Mudgway v D M Roberts Ltd* [2012] NZHC 1463; and *Contact Energy Ltd v Contact Gas Corporation of New Zealand Ltd* CA65/00, 18 July 2000 (CA).

In this case it appears to be a question of the placing of differing weight on different factors in statutory interpretation. The Court of Appeal placed primary emphasis on the extra-Parliamentary background, including the Law Commission Report and what it inferred was Parliament's intention in adding the words, given the approach English Courts had taken to similar words in England's then arbitration statute.

In contrast the Supreme Court considered consistency with international obligations to be of primary importance — that was particularly so given that the Arbitration Act 1996 itself says that one of its key purposes is to give effect to New Zealand's obligations under the New York Convention (see, for example, [42]).

In terms of international comity it cannot be doubted that the Supreme Court is right in this case. The criticism of the Supreme Court decision in *Carr v Gallaway Cook Allan* [2014] NZSC 75, [2014] NZLR 792 suggested that the Court paid insufficient attention to New Zealand's international obligations and raised the specter that departure from the Model Law can impact upon the way New Zealand is perceived as a potential seat for international commercial arbitrations. (For example, see D Kalderimis "The New Zealand Supreme Court and Arbitration", paper presented to the AMINZ Conference, 28–30 August, 2014, <www.aminz.org.nz>). That the Supreme Court was able to reach a decision that gave comfort to those worried about the approach the court was taking, while applying orthodox principles of statutory interpretation, is of some relief. (See the pithy summary of the case by Sophie East and Jane

Standage "A win for arbitration: Supreme Court narrows the scope for court involvement in arbitral proceedings" (19 January 2015, Bell Gully, <www.bellgully.com/resources/resource.03894.asp>).

## DOMESTIC IMPLICATIONS

Setting aside the international implications of the decision, the implications for domestic cases are significant. For domestic cases involving arbitration clauses this does solve one of the practical difficulties that lawyers have to consider — namely what precisely clients should do when they have a dispute where there has been a breach of obligations under the contract and the other party, rather than practically disputing matters, has simply failed to engage. The question often confronted is whether it was appropriate to seek summary judgment or whether some sort of arbitration process should have been engaged.

The Supreme Court has provided a clear answer. Unless it is obvious that any dispute raised is not bona fide then you should proceed to court. In cases where there has simply been no reply then parties should probably proceed to court anyway. It is difficult to imagine a court that would say a recently raised dispute after considerable correspondence was in fact "bona fide" and that a court would then refer the matter to arbitration. Even if it did so the risk of an adverse costs award would be low. However, if the case is simply weak, then the dispute resolution process set out in the relevant agreement should be commenced as soon as possible.

What the decision does not provide guidance on, and what parties will still need to grapple with, is how they should deal with circumstances where the plaintiff considers the defendant has no reasonably arguable defence (and also what it means to not have a 'bona fide' defence). The effect of the Supreme Court decision could be that parties to arbitration agreements have no access to the summary jurisdiction (including strike-out applications).

That is because arbitrations generally do not allow for interlocutory applications or summary procedures (especially internationally); as Williams and Kawharu note "[a] recurring criticism of arbitration is that there is no efficient method for the early disposal of meritless claims" (*Williams & Kawharu on Arbitration* (LexisNexis, Wellington, 2011) at 304, and see Walker, C T "International arbitration: return to Eden?" [2008] NZLJ 301 at 302).

Why is that? One reason may be that it is a matter of principle — natural justice does not allow it which raises the risk of any award been set aside. The natural justice requirements for arbitration are set out in arts 12, 18 and 24 of sch 1 and have also been stated in case law.

One of the definitive statements on this was by Fisher J in *Trustees of Rotoaira Forest Trust v Attorney General* [1999] 2 NZLR 452 where his Honour cited the basic requirements, at 459, from the leading English text Mustill and Boyd *Law and Practice of Commercial Arbitration in England* (2nd ed, Butterworths, London 1989) at 301 which were:

1. Each party must have notice that the hearing is to take place.
2. Each party must have a reasonable opportunity to be present at the hearing, together with his or her advisors and witnesses.
3. Each party must have the opportunity to be present throughout the hearing.
4. Each party must have a reasonable opportunity to present evidence and arguments for his or her own case.
5. Each party must have a reasonable opportunity to test his or her opponent's case by cross examining witnesses, presenting rebutting evidence and addressing other argument.
6. The hearing must, unless the contrary is expressly agreed, be the occasion on which the parties present the whole of their evidence and argument.

It is difficult to see precisely what, in those natural justice requirements, would prevent an arbitrator exercising a summary jurisdiction. The essence of a summary jurisdiction is that the parties do have an opportunity to present their case (admittedly in a truncated form). Cross-examination can be made available by way of notice requiring witnesses who provide evidence by way of affidavit to be available for cross-examination. It would appear to meet requirements (1)–(5).

The only concern could appear to be with requirement (6) which is that the hearing must, unless the contrary is expressly agreed, be the occasion on which the parties present the whole of their evidence and argument.

The idea of a potential two-stage process would, on that basis, appear to need to be specifically agreed, although that must be questionable. The requirement appears to be directed more towards communications with the tribunal outside of the hearing itself. However there should be no objection to that — after all "the combined effects of arts 18 and 24 is that no hearing is required unless a party seeks one, that the parties are free to agree on whether to hold a hearing and no hearing will be held if that is what the parties have agreed" (*Williams & Kawharu on Arbitration*, above, at 502). Provided there is agreement between the parties, there should be no risk of any award being set aside in the event a summary procedure is used.

Are there any jurisdictional issues with arbitrators exercising a summary jurisdiction? As a general principle, there would appear not to be: ss 10 and 12 of the Arbitration Act 1996 give broad powers to arbitrators and effectively give them all the powers of a High Court judge. Further, cl 3 of sch 2 sets out that the powers of an arbitral tribunal include "making an interim, interlocutory or partial award". There is no authority and nothing in the wording of the statute that would indicate that that should be limited so that arbitrators can exercise all the jurisdiction of the High Court except for the summary jurisdiction.

The second reason why arbitrators may have been reluctant to exercise a summary jurisdiction is because "add ons" and procedural complexity — such as multiple hearings — undermine one of the advantages of arbitration, namely it can be a "relatively quick, simple, and confidential method of resolving their disputes" (Walker, above, at 303). Further if such applications are unsuccessful then the interim award could "turn out to foreclose different and preferable approaches in a subsequent phase of the proceedings" (*Williams & Kawharu on Arbitration*, above, at 305).

How then should parties approach this issue? First, it must be said that there are benefits to a summary procedure. It does allow parties to quickly resolve a dispute where one party is very confident in their case. There is no reason in principle why that should be available to the Court but not to arbitrations.

There are also practical cost and time savings for the parties and there is no reason why a party that is particularly confident of its case should not have the right to effectively "take the risk" and see whether its case is as strong as it believes or the other side's case is as weak as it believes.

In saying that, there are questions as to whether summary judgment procedure would in fact add much in arbitration. Practically speaking, most arbitrations proceed with evidence on the papers with cross-examination and oral submissions (as do most Court hearings now). If there is, in fact, no reasonably arguable defence then it is difficult to see how a full hearing would be that much longer or more expensive than a partial one.

It would also enable all parties to have appropriate access to documents held by the other side through a discovery process to ensure that the arbitral tribunal is fully informed and that no party is having their rights to justice truncated by the summary procedure.

Further, the primary purpose of the summary jurisdiction is to enable a 'short-cut'. Given that arbitrations are generally swifter than the Court process, without the summary jurisdiction it is difficult to see what is gained.

The only circumstance where it might appear that there would be considerable savings is where a strike-out application would succeed. Of course these are usually brought by a defendant but can, where appropriate, be brought by a plaintiff. Arbitrators having the ability to strike out claims or defences on the basis of established law does offer cost-savings.

The best way for parties to deal with this issue is up front in the arbitration clause. Those drafting arbitration clauses for parties should discuss with them whether or not they want to have summary judgment or strike-out available to them. That could then be inserted into the arbitration clause in a way similar to the following:

The parties agree that any arbitrator appointed under this clause has the jurisdiction to determine an application for summary judgment or for strike-out in the same manner as a judge of the High Court and following the same procedure set out in the High Court Rules. The timeframes for the making of any such application will be set by the arbitrator.

This would appear to resolve the objection to the exercise of a summary jurisdiction by arbitrators on the basis of principle; the parties agreeing to it up front means that no party can be denied natural justice when they are simply being held to the bargain they have already made. As for practicality, such a clause leaves that in the hands of the parties at the time.

## CONCLUSION

The Supreme Court judgment provides much needed clarity in this area and it does so in a way that is consistent with New Zealand's international obligations. There still remain some practical questions that litigants will ultimately need to grapple with. The first question is how to proceed when parties are non-responsive. In that case proceeding to court would appear to be the best way to get the matter brought to a head.

The second practical matter is that of the availability of the summary jurisdiction in arbitrations. In principle there is no objection to it although the practical cost and time savings may not be significant except in circumstances where a strike out might be available. In any event those drafting arbitration clauses should discuss the issue with their clients and if clients do want to have the summary jurisdiction available should provide for it in the arbitration clause so as to clarify the matter 'up front'. ❐