Litigation, Arbitration & Dispute Resolution

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GLOBAL

Arbitration Clauses in Commercial Agreements

BY HOWARD ROSEN | FTI CONSULTING

As business grows increasingly global and companies from more developed countries conduct business in less developed countries, arbitration clauses are routinely entered into as a means of defining a dispute resolution process that is not subject to local rule of law and local courts.

It is imperative that businesses understand the implications of the arbitration clauses that they have entered into, both from a legal and damages perspective. As well, once a dispute arises there is a choice between initiating arbitration and attempting to settle outside of the arbitration clause. Business leaders would be well advised to examine the potential size and identifiable risks associated with their claim, before initiating proceedings.

While a legal analysis is outside of my expertise, from this perspective there are at least two issues to be aware of in drafting arbitration clauses. The first deals with the *governing law* clause in the contract. This will determine the laws of which country will be applied in the arbitration. The second issue deals with the *seat of arbitration,* which will be specified in the arbitration clause in the contract.

The governing law clause in a contract will define the laws of which country that will apply to disputes governed by the contract. A detailed knowledge of the laws of particular countries is therefore essential before agreeing to be bound by the laws of a country other than your own.

The seat of arbitration chosen in the arbitration clause can also have a dramatic impact on the outcome of the arbitration. A desirable location chosen for logistics, shopping, restaurants, etc., may have an adverse impact on the outcome of arbitration proceedings. Before, during, or after an arbitration the seat of arbitration provides the arena for potential intervention. Local Courts can be used to attack the proceedings by seeking injunctions prior to the hearings commencing (or in some circumstances, while the proceedings have commenced). As well, an award can be attacked in the local courts through an annulment proceeding after it has been rendered.

In general, a "pro" arbitration seat should be sought out to provide a properly neutral venue for the arbitration. In searching out a pro arbitration seat, a careful review of any interventions made by local Courts in past arbitration cases should be sought out to ensure that there has not been any untoward interference. In one recent case in 2009, the hearing was interrupted by the Respondent who had obtained an *ex parte* injunction to halt the arbitration proceedings. This was an example of the seat of arbitration being in a country where the local Courts were willing to intervene.

From a damages analysis point of view, arbitration clauses should spell out, as best they can, the type and measurement of damages that are envisaged for a breach or non-performance of the agreement at the outset.

Depending on the nature of the business relationship, this may be quite straightforward, and be calculated as

a loss of profits. In these types of cases typically damages are calculated based on the profits that would have been earned by the business enterprise but for the breach.

Profits, however, have many different definitions and interpretations. Economic and accounting concepts such as: marginal cost, direct cost, incremental cost, etc., may impact greatly on the calculation of damages. Differences in the customary way in which lost profits is calculated can differ in different geographies around the world as well as in different industries. The recent introduction of international accounting standards (IFRS) may result in more comparable financial statements worldwide, but gaps can and will still continue to exist in the methods and precision of the calculation of damages. It is best to define what is intended to compensate an aggrieved party in these circumstances as far as you can.

In the case of a catastrophic loss or expropriation, which leads to the loss of a business or the entire opportunity, the measurement of *fair market value* may be the appropriate measurement of loss. Again, it is best to define what is intended in these circumstances, and how fair market value should be determined (valuation date, discount rate). The various components that go into a determination of fair market value are not always determinable by formula, so some broader guidelines may need to be employed.

In essence, what you should be trying to achieve is some enhanced degree of certainty in entering into contracts in countries other than your own. In a recent construction dispute, there was a termination clause that called for "fair compensation of an amount no less than the value of the project at the time of termination in addition to a sum representing not less than half of the anticipated net profits for the period remaining in the contract period". Without discussing the merit of the contract or circumstances of the case, this is an example of contract language that does not achieve the goal of removing uncertainty in the calculation of damages.

This leads to the last area of discussion: how to evaluate and decide if settlement is a better option to initiating or conducting the arbitration. As with most business decisions, there is uncertainty and risk associated with this process.

It is important to understand not only the financial merits of the case you are presenting or defending, but also to ensure you have a good understanding of the arbitration risks. The decision to settle or arbitrate should be based on a thorough understanding and quantification of the amounts at dispute, the risks in the legal arguments being presented, likely size of any award of damages, and an appreciation of the time and cost associated with the arbitration proceedings.

For the purposes of this discussion, let us assume that the decision to settle or arbitrate is purely a financial one. For some disputes this is not the case; there is some intangible value to carrying through with the arbitration. That can be an important consideration, for example, when a company is engaged in arbitration disputes in a number of venues around the globe and needs to demonstrate the seriousness of its resolve to take disputes to a conclusion. If a company is not known to be willing to take a dispute all the way through an arbitration, companies involved in other disputes with them may not negotiate as readily.

Once legal counsel has reached a level of comfort about the merits of the legal argument, you should be able to quantify this risk with some approximate probability. Your financial expert should be able to quantify the amount of damages, taking into account all of the relevant business risks. A combination of these two analyses, together with the knowledge of what arbitration panels have considered as appropriate damages on similar cases, should provide a good benchmark as to a probable outcome.

On top of this, there will be a requirement to devote corporate resources to bringing or answering a claim in an

arbitration. The resources required will depend on the complexity of the claim. A further consideration, depending on the forum of the arbitration, is the magnitude of the costs associated with the proceedings.

Business leaders and decision makers must take into consideration all of these points (and any others that are relevant to their specific case) in order to make rational business decisions about entering into arbitration proceedings before exhausting settlement opportunities.

Howard Rosen is a Senior Managing Director at FTI Consulting.


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e-Disclosure 2020

BY TOM LEWIS, JON HAYTON AND DAVID MOLONEY | PRICEWATERHOUSECOOPERS

A new era of rapid technological advancement is upon us, bringing new methods of communication and electronic information that have no precedent and no counterpart in any traditional model. With it, the way in which the office environment works – how it transfers, uses and stores data – is changing.

Today's disclosure issues of proportionality and reasonableness are expressed in terms of volumes of data and cost burden, but tomorrow's likely challenges bring issues of a different kind. We must start now if we are to be successful addressing those challenges.

What will e-disclosure look like in 2020? The question is worth posing because companies and the professionals advising them need to understand the impact of changing technology. New technologies are bringing innovative ways for people to work and communicate and it is these activities and communications that are relevant to the underlying matters. "Who did what when?" and "Who knew what when?" are two of the questions driving disclosure. Because new technologies will hold information that answers these questions – the evidence – it follows that parties will want that information disclosed. We anticipate that requirements for companies to retrieve targeted data will increase. This will become more difficult as the types of data become more diverse. It will require improvements in the processes and controls associated with the creation, management, monitoring and retrieval of data.

The Journey So Far

As corporate information moved from paper to computer, disclosures became electronic, increasingly focused on e-mail and electronic files. In turn, e-disclosure brought a multitude of new issues that courts, lawyers and IT professionals had to deal with – forensic data capture, metadata, deleted documents and slack space being just a few.

Disclosure rules have evolved to include these attributes of electronic data, yet in hindsight the evolution from paper disclosure to e-disclosure was merely incremental. e-Disclosure was simply a modernisation of traditional disclosure; even now the majority of disclosure consists fundamentally of documents—albeit stored electronically rather than in filing cabinets. The memorandum has been replaced by e-mail, yet the

two are essentially the same.

It follows that changes to disclosure rules have also been incremental rather than radical. Disclosure requires an understanding of the corporate information universe: the type, location and relevance of information. Disclosure rules direct parties to search electronic systems, servers and databases for relevant data. While the majority of debate has focussed on the costs and efficiency of e-disclosure, technological advances mean that many of those grappling with e-disclosure today are already behind where they need to be, even before they consider the implications and consequentially, the regulations, necessary to address the business data practices of the near future.

What will e-Disclosure Look like in 2020?

The answer, of course, will largely be driven by how the business technology environment will evolve. Consider the following:

- *Social networking:* Along with instant messaging, wikis and tweets, social networking is already becoming part of corporate communication. What are the implications on relevance, privacy, confidentiality and ownership of this information?
- *Cloud computing:* Servers and storage will move into the network "cloud". The cloud can automatically move data from a full server to one with available space and move a processing job from a busy server to an idle one, anywhere on the globe. Which jurisdiction(s) apply to data that moves itself between countries? How might that affect data capture?
- *Tablet computing:* With the increasing use of tablet PCs as traditional notebooks, will organisations need to produce the electronic jottings of users in a similar fashion to the handwritten notebook?
- *Voice data:* Due to regulatory requirements, companies are increasingly forced to record telephone conversations. We must not forget that this information is still regarded as data and is subject to e-disclosure. The convergence of voice and data has been promised for a while, aided by technologies such as voice over IP. There are many services that now convert voice messages into text and vice versa. Are there implications to disclosing a message as text when it originated as a voice message?
- *Servers in space:* Could jurisdictions create data centres that are neutral in location and difficult to reach? Is the way in which data is stored and transferred likely to involve more regulators and legislation? Taking the idea one step further, what are the implications of data servers orbiting in space?
- *Eye gaze tracking:* Cameras in the computer screen can track a user's gaze-point thus allowing an operator to interact with their environment using only their eyes. Might future disclosures include this tracking data, perhaps to prove that someone had actually read a document? Could biometric passwords be used to confirm an individual was actually using a computer at the time?
- *Three-dimensional holographic projections:* 3D holographic projections are a staple of science fiction and will probably be here eventually. Until then we have a massively growing body of unstructured data including recordings of telephone calls, conference calls, video conferences, web casts, boardroom TV and CCTV footage. Will we be able to search video for people whispering in corridors the way we can search audio recordings phonetically?

How might these developments in technology impact e-disclosure?

- As the information we search extends from documents to include complex models, financial and enterprise data, social networking forums, and video recordings, identifying, searching and disclosing relevant data will become harder. e-Disclosure technology will need to evolve and adapt to the evolution of business technology.
- Today, e-mails are considered less formal than letters, or, say, board meeting minutes. Might e-disclosure rules need to adapt to deal with even less formal media such as instant messaging and social networking? If the sites are public rather than internal corporate social networks, will the data be challenged as unreliable opinion rather than corporate fact?
- Relevance of all this electronic data will still be tied directly to social and corporate behaviour. The need to understand, discuss, argue and agree proportionality will become more complex and be more important than ever.
- Relevance will also be tied to business context. Tweets from the executive suite will likely be more relevant than tweets from the call centre's break room. Can we record that context when the data is recorded?
- We are seeing increasing use of user-written applications. Will we see a growth of bespoke systems from which it is difficult and costly to recover data?
- Increasingly complex IT infrastructures make it harder to locate relevant data and identify key custodians. It is getting increasingly difficult to track all the data across the enterprise that a given person might have touched or seen.
- We have already seen disputes over ownership where individuals have used personal computers to store corporate data belonging to their employer. Will working at home increasingly blur the point at which the corporate line stops and the individual's privacy starts?
- With advancements in storage capacity, will regulators or opposing parties expect organisations to retain all their data? Might they look unfavourably on those who fail to do so?
- Likewise, new technologies bring better ways to store and retrieve data, with tools being developed to assess and categorise data in real time, as opposed to the traditional method of capturing and then searching historical data sets. Will it become expected that organisations can easily control and secure their data?
- As the volume and type of disclosed data changes, current e-disclosure techniques, such as keyword searching, will become inadequate. Concept-searching, context-searching and automatic document grouping are already assisting companies trawl through massive amounts of data and these new technologies will continue to be developed and refined. How quickly will search technology keep up with new types of data such as CCTV and video conferencing?

The specific future of business technology and its implications on e-disclosure are difficult to predict. Regardless, consultation on today's technology framework and the challenges of the future must start now.

Posing such questions and considering the possible implications allows us to move the debate on e-disclosure from the traditional discussions – about volume of data and cost – to a real understanding of how enlightened businesses will address these future and potentially larger challenges.

Legal practitioners and those who set the rules will need to understand the agenda of those shaping the corporate network – software, applications and behaviours of the future – and how companies are adapting and using business information systems as these will shape e-disclosure in 2020 and beyond.

Tom Lewis is a Partner and Jon Hayton and David Moloney are Directors at PricewaterhouseCoopers.

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Detecting Improper Activity in a Client's Bank Account: "Churning"

BY PENELOPE LEPEUDRY AND ABIGAIL CHEADLE | KORDAMENTHA

Since the financial crisis, most financial products have lost value and a number of banking customers have seen their portfolio nearly wiped out. For those who had margin-trading accounts, the wake-up-call was even worse as some customers have faced margin calls that took them by surprise.

But were such investments wiped out "only" as a result of the financial crisis and client's own investment decisions or has the bank account been excessively traded and mismanaged by the broker or the bank?

A growing number of private banking customers have come knocking on the door of their lawyers or advisors for an answer to that question. Lawyers and financial industry experts have assisted their clients in establishing whether their bank account had been mismanaged – usually referred as "account churning".

What is Churning?

Churning refers to the excessive buying and selling of financial products in the customer's account by a broker or banker, for the purpose of generating commissions, fees and/or bonuses and without regard to the client's investment objectives.

To prove churning occurred in an account, three elements must be shown:

- First, the broker or banker had control over the account. Under a discretionary mandate (for an account managed under a Discretionary Mandate, all investment decisions are made by the Bank based on the investment objectives and risk appetite of the client as defined at the outset of the banking relationship), the bank has control over the account because when the account is under a discretionary account, the client has authorised the bank to trade without first consulting him or her and the Bank makes the investment decisions. The client receives a portfolio statement on a regular basis – usually monthly. De facto control can be established in managed accounts (also referred to as execution-only accounts or advisory accounts), mainly when it can be shown that a client routinely followed the banker or broker's advice on most transactions.
- Second, there is "scienter" from the banker or broker. The broker or the banker *intentionally* engaged in excessive trading in order to generate increased commissions and/or bonuses for his own benefit,

disregarding the client's best interest. If a client is sold financial products with high fees towards year end (such as life insurance products), this can be an indication of the banker trying to meet year-end revenue targets and therefore secure a higher bonus from his company.

- Third, excessive trading occurred, i.e., transactions in the account are excessive in cost, size or frequency in view of the client's risk profile and investment objectives-as defined at the inception of the banking relationship. Excessive trading is usually determined by looking at the following three factors: (i) annualised turnover ratio; (ii) annualised cost to equity ratio; and (iii) trading activity in the account. A client's investment objectives and risk appetite will also be considered when determining whether excessive trading occurred or not.

The first two elements in establishing churning – control and scienter – are best answered by a lawyer but the third element – determining whether excessive trading occurred – will usually require the involvement of a financial industry expert.

- The turnover ratio measures the number of times the bank account is traded in a year. The turnover rate is calculated by dividing the total cost of purchases in the account by the average monthly equity. In existing case law from the U.S., it has been generally recognised that an annual turnover ratio of 2 times infers churning for a conservative investor, a turnover ratio of 4 presumes churning, while 6 times is conclusive of churning. This is also referred to as the 2-4-6 Rule. In determining whether the turnover ratio is excessive, it will also be relevant for the financial industry expert to compare the turnover ratio with the ones of mutual funds with similar investment objectives.
- The cost-to-equity ratio looks at the annual cost associated with operating the account, commissions, fees charged, margin interests, etc. The cost-to-equity ratio is a measure of the amount an account must appreciate on an annual basis to cover costs. For example if the cost to equity ratio is 10%, then the account needs to return 10% annually simply to cover the costs associated with the account. In general, costs in excess of 5% should be seriously questioned. In looking at the reasonableness of the cost-to-equity ratio, the securities industry expert may also look at industry benchmarks such as costs charged by mutual funds with similar investment objectives.
- Lastly, the securities industry expert will look at the number of trades in the account, the level of in-and-out trading and whether the holding periods are very short.

At the end of the day, churning constitutes fraud. In the U.S., churning is a violation of state and federal securities laws.

One must remember that all it takes for an individual to commit fraud is: (i) an opportunity (in this case, this means having control over a client's account); (ii) pressure (lower compensation for the broker or financial adviser due to the financial crisis – or pressure to meet sales targets that are tougher to achieve in times of financial crisis); and (iii) rationalisation (the broker or financial advisor will rationalise his act by thinking that "I am increasing the trades not to generate commissions for myself but mainly because I think my client will earn more in the long term").

While the economy was thriving, a number of customers were not scrutinising the activity in their bank account as overall their portfolio was growing. When portfolios were hit by the financial crisis, and clients noticed that the

bottom line of their bank account statement showed a loss, clients all started scrutinising their accounts, but filing a claim for churning is not an easy battle.

Once churning has been established it is then time to quantify damages. Damages are usually quantified by looking at a "benchmark portfolio", i.e., what would the client's equity would have been had the account been appropriately managed. Typically a benchmark portfolio would be a mutual fund in which the client could have invested in, and should be in line with the client's investment objectives.

Accountants and securities industry professionals are often called as expert witnesses to assist lawyers, their client and arbitrators in determining whether a bank/trading account has been excessively traded and, if so, quantify the damages suffered by the client.

Penelope Lepeudry is a Director and Abigail Cheadle is a Partner at KordaMentha.

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Settlement in International Arbitration: the CEDR Rules

BY PEDRO SOUSA UVA | ABREU ADVOGADOS

The complexity of many international arbitration disputes led to decisions that may take several years to achieve. This reflects the idea that settlement in international arbitration is not always in the mind of the parties or of the arbitrators. The recent CEDR Rules represent a step away from this trend and encourage a more proactive environment towards facilitating settlement.

On November, 26 2009, the Centre for Effective Dispute Resolution (CEDR), a widely-known London based organisation that provides alternative dispute resolution services, launched a body of rules highly expected by those leading with international arbitration. These rules have been designated "Rules for the Facilitation of Settlement in International Arbitration" (the "CEDR Rules") and pursue a clear goal: to enhance the possibilities of reaching settlement in international arbitration proceedings by means of a more proactive approach by tribunals and parties.

The CEDR Rules were not created instantaneously. They are, in fact, the product of a two-year project developed by a CEDR special Commission, formed in 2007, engaged in reviewing the current practice of settlement facilitation by international tribunals. The purpose of such Commission was to come up with recommendations that would provide arbitral players the necessary tools to increase the possibilities of settlement without necessarily implying the need to reach the conclusion of arbitral proceedings.

Relying on research which shows that settlement in arbitration is not as frequent as in many national courts, and based on the premise that parties want their disputes to be solved cost effectively and efficiently, such recommendations have been created and included in a Final Report that was published on the very same day as the CEDR Rules. The purpose of such recommendations is to guide and provide background information to the CEDR Rules.

Apparently, the CEDR Rules are straightforward, concise and unambiguous. They may be chosen by the parties either in an arbitration clause, by way of a procedural agreement made by the parties or even by inclusion by

arbitral institutions in their rules of arbitration.

Composed of seven articles, the CEDR rules are supposed not to replace any of the legal provisions or institutional *ad hoc* rules governing the arbitration, but merely to supplement them. Be that as it may, in case of conflict with the General Rules ("the Institutional or ad hoc rules according to which the Parties are conducting their arbitration", as per article 1.4), the CEDR Rules prevail. This means that the CEDR Rules are only subject, in case of conflict, to the mandatory provisions of law applicable to the case (article 2).

Looking at the most relevant provisions one may find, firstly, a set of general principles that serve the purpose of guiding the tribunal, or the parties, when approaching the desired proactive approach reflected in these rules.

One of these general principles establishes, for instance, that when "assisting the Parties with settlement, the Tribunal shall not knowingly act in such a way as would make its award susceptible to a successful challenge" (article 3.3). An example of a behaviour that could potentially lead to a challenge of the arbitrator would be the case where the arbitrator meets one of the parties in a private session (caucus).

In order to avoid risks of challenge, certain safeguards for arbitrators have been previewed in Appendix 2 of the recommendations ("Safeguards for arbitrators who use private meetings with each party as a means of facilitating settlement"), notably requiring the parties' consent in writing as to the way the arbitrator will deal with the disclosed information, either before and/or after the mediation / conciliation phase.

Accordingly, CEDR Rules establish that parties agree that proactive steps taken by the tribunal while assisting them in achieving a negotiated settlement may not be asserted by any party as grounds for disqualifying the tribunal or for challenging any award.

Moreover, according to the CEDR Rules, nothing that has been said or done by a party or its counsel, while trying to settle, shall be used against a party in the event that the arbitration resumes (except for allocation of costs). Similarly, the tribunal may not take into account any substantive matters that have been discussed in settlement meetings or communications, unless such matter has been introduced in the arbitration. Thus, any given witness shall not have his or her credibility tested due to having been a representative of a party during settlement discussions, or due to anything said or attributed to such witness, while in settlement discussions.

In compliance with general principles, the CEDR Rules also establish the obligation of the tribunal to request the presence of the parties themselves to participate in the First Procedural Conference. The goal is for the parties (represented by a member of their management or in-house legal function, but not by means of their counsels) to speak directly with the arbitral tribunal regarding settlement matters. This reflects the understanding that a first personal contact between parties and the tribunal may be more helpful towards settlement than if the party is represented by the counsel. It may be doubtful whether such approach will always imply better results. Notwithstanding, a counsel may apparently rely on the fact that whatever said by such party while settling can not be used against it, as referred above.

Other examples of proactive steps by the tribunal are foreseen in the CEDR Rules.

Firstly, the duty to make clear to the parties the options that they have at their disposal, notably that they may settle fully or partially at any time. Secondly, that other dispute resolution processes exist that may facilitate settlement at any time during the arbitration, such as, for instance, by opening a so called "mediation window", a "period of time during an arbitration that is set aside so that mediation can take place and during which there is no procedural activity", according to article 1.5 of the CEDR Rules. Thirdly, the duty of the tribunal to agree with the parties on steps to be followed towards facilitating settlement. Finally, the duty to agree with the parties

on the possibility of the tribunal to take into account, for purposes of allocation of costs, any offer to settle that was not accepted. This means that if the party that refused an offer has not done better in the arbitration award when compared to the terms of proposed settlement, it may be sacrificed at the end of the arbitration in what the costs of the arbitration are concerned (article six, *ex vi* article 4, 2.5).

The above mentioned general principles and issues regarding the First procedural conference are unquestionably significant. Nonetheless, the CEDR Rules go further and refer to the precise steps the tribunal may and may not take towards facilitating settlement, as follows.

If not agreed otherwise by the parties, the tribunal may provide all parties with a preliminary view on the matters discussed and which the tribunal considers relevant in terms of evidence for a claim to prevail or not. The tribunal may also give the parties preliminary non-binding findings on law or fact regarding the most relevant issues in discussion. These provisions, in practice, may well give the parties a relevant input to the perception of success of their case as it may allow them to balance the option between moving forward with their claim or envisaging a potential negotiation for settlement.

Moreover, if requested by the parties in writing, the tribunal may also suggest terms of settlement as a basis for further negotiation, as well as chair one or more settlement meetings attended by representatives of the Parties where possible terms of settlement may be negotiated.

Additionally, an important feature of the CEDR Rules is the possibility of the arbitral tribunal to insert a "Mediation Window" if requested by all parties. This enables settlement discussions to take place, either by means of mediation or other process, while arbitral proceedings are set aside.

Finally, when requested by one party, the tribunal may also adjourn the proceedings for a certain specified period in order to enable mediation, when the contract in dispute has a mandatory mediation clause and mediation has not been followed before the issue is raised in arbitration (provided the failure was not due to the party who requested the adjournment).

There are, however, certain negative obligations incumbent on the tribunal. The latter is forbidden to meet with any party without all parties being present (or at least without the agreement of all parties, as mentioned above). In addition, it is restricted from obtaining information from any party that is not shared with the other parties.

As a final remark, one may say that the CEDR rules represent a step toward efficient dispute resolution. Such rules provide the parties with tools that lead to a more proactive approach by the tribunal while attempting to reach settlement. These rules are open to any party in international arbitration proceedings. They have no limit of application except the will of the parties and mandatory provisions of the applicable law of the case.

If the resort to CEDR Rules implies a swifter resolution of international arbitration disputes, turning tribunals into active participants in facilitating settlement and not mere decision-makers, then parties will only have to gain with them. If, at the end of the day, such rules imply additional costs for the parties with mediation fees or a potential increase of challenges to arbitrators or awards, only practice and time will tell. Meanwhile, it seems that the CEDR Rules have the potential to lead to more efficient dispute resolution in international arbitration.

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AMERICAS

UNITED STATES

Piercing the Corporate Veil and Best Practices to Avoid it

BY GREGORY A. MARKEL AND MARTIN L. SEIDEL | CADWALADER WICKERSHAM & TAFT LLP

A corporation is a legally separate entity and generally neither its shareholders nor its officers and employees are liable for its debts or obligations. This is equally true of parent corporations with respect to the obligation of their subsidiaries, even wholly-owned subsidiaries. Litigants, however, frequently seek to embroil parent corporations in the legal disputes of their subsidiaries – either for tactical reasons, or to obtain access to a deeper pocketed defendant – using the doctrine of "piercing the corporate veil". As discussed below, this doctrine provides a limited right to "look past" the separate corporate existence of the parent and subsidiary and hold the parent liable for the obligations of the subsidiary where it would be inequitable not to do so. This article summarises the veil piercing doctrine and identifies practices that will help a corporation prevent the application of the doctrine to its relations with its subsidiaries.

A Parent Company is generally not liable for the acts of a subsidiary, even where the Parent is the sole shareholder of the subsidiary. *See Bennett v. GAF Corp*., 1994 WL 279752 at *2 (D. N.H. June 4, 1994) (Parent is not liable for the acts of its subsidiary merely because it owns all of the subsidiary's stock); *In re Silicone Gel Breast Implants Prod. Liab. Litig*., 887 F. Supp. 1447, 1452 (N.D. Ala. 1995); *see also* Delaware General Corporate Law, Section 102(b)(6) ("... the stockholders or members of a corporation shall not be personally liable for the payment of the corporation's debt except as they may be liable by reason of their own conduct or acts"). Courts are reluctant to pierce the corporate veil and hold a Parent liable for judgments against its subsidiary, absent "exceptional circumstances". *Mobil Oil Corp. v. Linear Films, Inc.,* 718 F. Supp. 260, 270 (D. Del. 1989); *see also Manville Sales Corp. v. Paramount Sys. Inc.,* 917 F.2d 544, 552 (Fed. Cir. 1990); *Wausau Business Insurance Co. v. Turner Construction Co.,* 141 F. Supp. 2d 412, 418 (S.D.N.Y. 2001).

In order to determine whether to pierce a corporation's veil a Court will apply a two-pronged analysis. First, a court will examine whether the Parent has exercised such dominion and control over the subsidiary that the subsidiary may be deemed a mere instrumentality or alter ego of the parent. *See, e.g., Smoothline Ltd. v. N. Am. Foreign Trading Corp.,* 2002 U.S. Dist. LEXIS 24619 (S.D.N.Y. Dec. 27, 2002). Among other things courts consider whether the Parent and subsidiary have separate bank accounts, offices and other facilities, separate phone numbers, as well as whether the subsidiary observes corporate formalities such as keeping minute books, operating through its own officers and board, and the like. *See, e.g., Fletcher v. Atex, Inc.,* 68 F.3d 1451, 1458 (2d Cir. 1995); *Nelson v. Int'l Paint Co.,* 734 F.2d 1084 (5th Cir. 1984); *Gabriel Capital, L.P. v. NatWest Fin., Inc.,* 122 F. Supp. 2d 407, 432 (S.D.N.Y. 2000); No single factor is dispositive. Rather, courts look at the totality of circumstances, *United Steelworkers v. Connors Steel Co.,* 855 F.2d 1499, 1506 (11th Cir. 1988).

Second, the court must also find either that it would be unfair or unjust to allow the Parent to avoid liability for actions of the subsidiary or that harm or loss resulted from the misuse of the corporate entity. *Outokumpu Eng'g Enters, Inc. v. Kraerner EnviroPower, Inc.,* 685 A.D.2d 724, 729 (Del Super. Ct. 1996) ("[m]ere dominion and control of the Parent over the subsidiary will not support alter ego liability"). Plaintiff must also demonstrate that not piercing the veil will result in unfairness from defendants' misuse of the corporate form. *See, e.g., In re Birmingham Asbestos Litig*., 997, F.2d 827, 829-30 (11th Cir 1993) (requiring, in addition to dominion and control by parent, that "there must be the added element of harm or loss resulting from the misuse [of the separate corporate entity]."); *Fletcher v. Atex, Inc.,* 68 F.3d 1451, 1461 (2d Cir. 1995) (requiring an "'overall element of injustice or unfairness' that would result from respecting the two companies' corporate separateness.").

By adopting sound corporate practices, however, a company can minimise the risk that it will be forced to satisfy the obligations of a subsidiary.

- Observance of basic corporation formalities is generally considered the *most* important factor by courts when determining whether a Parent exercises improper dominion and control. *See Carte Blanche (Singapore) PTE, Ltd. v. Diners Club Intl., Inc.,* 2 F.3d 24, 28 (2d Cir. 1993). Accordingly, each subsidiary should each hold regular board meetings, and maintain minute books. Each subsidiary should regularly elect directors and officers. While those directors and officers may be employees of the Parent, the directors should be elected by valid documented shareholder votes or unanimous consents. Additionally, actions by a subsidiary should be done in accordance with the subsidiary's charter and by-laws and the parent should only act through shareholder votes or consents on issues requiring such approval.
- The Parent and each of its subsidiaries should establish separate bank accounts to avoid the appearance and reality that their funds were co-mingled. Alternatively, the Parent and its subsidiaries may employ a unified cash management system provided each company's funds are segregated. *See Japan Petroleum Co. (Nigeria) Ltd. v. Ashland Oil, Inc.,* 456 F. Supp. 831, 843 (1978).
- The Parent should not micromanage the day-to-day affairs of its subsidiaries or permit officers or directors of the parent to act on the subsidiaries' behalf; however, involvement in a subsidiary's *significant* business decisions typically is not evidence of undue control. *See Mobil Oil Corp. v. Linear Films, Inc.,* 718 F. Supp. 260, 270 (D. Del. 1989); *Pritchard Services (NY) Inc. v. First Winthrop Properties, Inc.,* 568 N.Y.S.2d 775, 776 (N.Y.A.D. 1st Dept. 1991).
- Whenever the Parent or one of its subsidiaries provides services to another entity within the corporate family, a written servicing agreement should be used to govern the transaction. The Parent and subsidiaries should also execute licensing agreements governing the use of intellectual property. *See, e.g., Wausau Business Inc. Co. v. Turner Construction Co.,* 141 F.Supp.2d 412, 419 (S.D.N.Y. 2001).
- The Parent and its subsidiary should, where possible, maintain their own office facilities. *See, e.g., Pledger v. United States,* 236 F.3d 315, 323 (6th Cir. 2000); *see also Smoothline Ltd. v. N. Am. Foreign Trading Corp.,* 2002 U.S. Dist. LEXIS 24619 (S.D.N.Y. Dec. 27, 2002). If office space is shared, both the Parent and its subsidiary should scrupulously abide by other corporate formalities to counteract the appearance of domination and control. *See In re Foxmeyer Corp.*, 290 B.R. 229, 245 (Bkrtcy. D. Del., 2003).

- Each subsidiary should maintain its own letterhead and corporate logos. Its personnel should have stationery and business cards clearly identifying them as employees of the subsidiary. If the Parent's name or logo appear on the subsidiary's written material, the corporate relationship between them should be made explicit. *See OTR Assoc. v. IBS Services, Inc.,* 353 N.J. Super. 48, 54 (2002) (veil was properly pierced where, *inter alia,* wholly-owned subsidiary's letters to plaintiff were on Parent's letterhead). A subsidiary should not be referred to in internal documents or any written material as a "Department," "Division," or the like. *See Stedman Energy, Inc. v. Lenape Resources Corp.,* 175 A.D.2d 646 (1991).
- A Parent and its subsidiary may share resources, including accountants and attorneys, to achieve cost-savings if the corporations follow proper procedures. *See, e.g., Hukill v. Auto Care, Inc.,* 192 F.3d 437, 443 (4th Cir. 1999) (shared administrative departments and services not sufficient to permit piercing corporate veil); *Quarles v. Fugua Indus.*; 504 F.2d 1358, 1363 (10th Cir. 1974) (same); *Japan Petroleum Co. (Nigeria) Ltd v. Ashland Oil, Inc.,* 456 F.Supp. 831, 846 (D. Del. 1978).
- A Parent Company's failure to adequately capitalise its subsidiary is often the most significant factor in determining whether piercing the corporate veil is necessary to avoid an inequitable outcome or whether the Parent has used the separate corporate form to defraud others. *See Nelson v. International Paint Co.,* 734 F.2d 1084 (5th Cir. 1984); *In re Foxmeyer Corp. v. General Electric Capital Corp.,* 290 B.R. 229, 244 (Bkrtcy. D. Del., 2003); *In re Hillsborough Holdings,* 166 B.R. at 474. Courts generally require the undercapitalisation to be severe. *See, e.g., Carte Blanche (Singapore) PTE, Ltd v. Diner's Club Int'l, Inc.,* 2F.3d 24 (2d Cir 1993). Undercapitalisation and/or insolvency are particularly problematic if they have existed from the time the subsidiary was created. *Foxmeyer* 290 B.R. at 244. In creating new subsidiaries, the Parent Company should provide sufficient capital "in relation to the nature of the business of the corporation and the risks the business necessarily entails". *J-R Grain Co. v. FAC, Inc.,* 627 F.2d 129, 135 (8th Cir. 1980).

Courts also consider whether the Parent Company has stripped assets from the subsidiary, leaving it unable to meet its obligations. *In re Foxmeyer Corp. v. General Electric Capital Corp.,* 290 B.R. 229, 244 (Bkrtcy. D. Del., 2003). Such "asset-stripping" will be inferred where the subsidiary declares and pays excessive dividends to the Parent corporation or pays less than fair market value for goods, services or assets of the subsidiary. *See id.* Accordingly, it is essential to ensure that the subsidiary will remain adequately capitalised after any dividend or asset transfer.

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Jurisdiction in the Digital Age

BY GREGORY A. MARKEL AND MARTIN L. SEIDEL | CADWALADER WICKERSHAM & TAFT LLP

A state or federal court in the United States can only exercise power over a defendant if that defendant has had sufficient contact with the jurisdiction that it would not offend fundamental notions of fair play to require it to appear and defend itself. Courts often look at whether the defendant does "substantial business" in a state to determine whether it has personal jurisdiction over that defendant. In the age of virtual or telepresence, electronic communications and e-commerce, however, the concept of "doing business" in a particular jurisdiction has evolved beyond simple physical presence.

The U.S. Constitution requires that a defendant have sufficient "minimum contacts" with the forum state such that "maintenance of the suit does not offend traditional notions of fair play and substantial justice." *Int'l Shoe Co. v. Wash.,* 326 U.S. 310, 316 (1945) (quotation and citation omitted). Personal jurisdiction can be either general or specific. General jurisdiction exists if a defendant has "continuous and systematic general business contacts" with the forum state, *Helicopteros Nacionales de Colombia v. Hall,* 466 U.S. 408, 416 (1984). General jurisdiction requires a high level of contact by the defendant with the forum state, and it is irrelevant whether the claim arose from the defendant's activities in the forum state. Courts consider, among other things, the extent of defendant's contacts, including whether the defendant regularly makes sales, solicits or engages in business, holds a licence or is incorporated in the forum state.

Specific jurisdiction exists where the defendant purposefully directs activities toward the forum state, and the cause of action arises out of those activities. *Burger King Corp. v. Rudzewicz,* 471 U.S. 462, 472-73 (1985). The purpose of this test is to protect a defendant from having to defend itself in courts where they should not anticipate being sued. *See World-Wide Volkswagen Corp. v. Woodson,* 444 U.S. 286, 297 (1980).

The United States Supreme Court has developed a three part test to determine whether a court has personal jurisdiction over a defendant: (i) the extent to which the defendant purposefully availed itself of conducting activities in the state; (ii) whether the plaintiff's claims arise out of those activities directed at the state; and (iii) whether the exercise of personal jurisdiction would be constitutionally reasonable. *See Burger King,* 471 U.S. at 475-76.

In analysing the threshold purposeful availment factor, a court may consider: (i) whether the defendant maintains offices or agents in the forum state; (ii) whether the defendant reached into the forum state to solicit or initiate business; (iii) whether the defendant deliberately engaged in significant or long-term business activities in the forum state; and (iv) whether the parties contractually agreed that the law of the forum state would govern disputes. *See Burger King,* 471 U.S. at 475-76, 481-82; *McGee v. Int'l Life Ins. Co.,* 355 U.S. 220, 221 (1957). To satisfy the second prong, defendant's contacts with the forum state must form the basis of the suit. *See Burger King,* 471 U.S. at 472; *Helicopteros Nacionales,* 466 U.S. at 414. After the first two prongs of the minimum contacts test are satisfied, the third prong permits a court to consider additional factors to assess the reasonableness of exercising jurisdiction, including the burden on the defendant in litigating in the forum and the interests of the parties and the state. *See Burger King,* 471 U.S. at 477 (citing *World-Wide Volkswagen,* 444 U.S. at 292).

These traditional notions of jurisdiction have been expanded in recent years to apply to those corporations who conduct business through the Internet. The analysis applied depends upon whether the court seeks to

exercise general or specific jurisdiction over the defendant corporation. If the court seeks to exercise specific jurisdiction, the court generally examines the defendant's activities under *Zippo Manuf. Co. v. Zippo Dot Com, Inc.,* 952 F.Supp. 1119 (W.D. Pa. 1997). *Zippo* establishes three categories of internet presence for the purpose of determining whether specific personal jurisdiction can be exercised over the corporation maintaining that internet presence. Generally, if the defendant clearly "does business" over the internet, for example entering into contracts or engaging in repeated transmission of files over internet, courts have held that personal jurisdiction is appropriate. *See Compuserve, Inc. v. Patterson,* 89 F.2d 1257 (6th Cir. 1996). If a defendant's web presence is "passive", only making information available for those who wish to seek it out, courts have generally found that personal jurisdiction does not exist. *See Bensusan Restaurant Corp., v. King,* 937 F.Supp. 296 (S.D.N.Y. 1996); *Haggerty Enters., Inc. v. Lipan Industrial Co.,* 2001 U.S. Dist. LEXIS 13012, at *15-16 (N.D. Ill. Aug. 22, 2001).

Courts have been divided, however, with respect to those corporations whose web presence falls somewhere in the middle. If a defendant has an "interactive" web presence, permitting visitors to exchange information with a host computer, some courts have found that personal jurisdiction may be appropriate. Courts then examine the level of interactivity and commercial nature of the exchange of information that occurs over the website to determine whether the defendant "purposefully availed" itself of the forum. Courts consider whether the website allows visitors to purchase goods; whether defendant ships its goods into the forum; whether defendant solicits business in the forum; whether the website allows defendant to communicate with customers in a forum; the overall volume of sales in the forum; and whether defendant's website permits defendant to "transact business" within the forum.

No clear-cut standard has emerged to determine whether an electronic presence subjects a company to general jurisdiction. Some courts use the *Zippo* test; other courts have held that a higher standard must be applied to subject a corporation to general jurisdiction for electronic activity. For example, in *Coastal Video Communication Corp. v. Staywell Corp.,* 59 F.Supp. 2d 562 (E.D. Va. 1999), plaintiff, a Virginia corporation, filed a copyright infringement action against a corporation with its place of business in California arguing that defendant's website allowed customers in Virginia to make purchases online and that it was therefore doing business in Virginia. The court analogised defendant's "interactive" website to the presence of a physical store in the forum state, and noted that the presence of such a store would not support general jurisdiction unless that store generated sufficient sales to satisfy the "systematic and continuous" contacts standard. Accordingly, the interactive website alone was insufficient to subject defendant to general personal jurisdiction. Because the *Zippo* test does not consider the type or quality of the internet contacts in the forum state, which in turn would help determine whether contacts are systematic and continuous, the *Coastal Video* court found *Zippo* inapplicable. Instead, the court advocated a deeper analysis of other factors in internet cases, including the amount of sales in the forum state generated by or through an interactive website and the number of hits on that website coming from the forum state over a certain relevant time period. *Coastal Video,* 59 F.Supp. 2d at 572. The court concluded that "it is not enough to find that an interactive website has the potential to reach a significant percentage of the forum state's population" when considering whether the exercise of general jurisdiction is appropriate. *Coastal Video,* 59 F.Supp.2d at 571. *See also Lakin v. Prudential Securities Inc.,* 348 F.3d 704, 712 (8th Cir. 2003). *Revell v. Lidov,* 317 F.3d 467, 471 (5th Cir. 2002); *Bell v. Imperial Palace Hotel/Casino, Inc.,* 200 F.Supp.2d 1082, 1091 (E.D. Mo. 2001).

Other courts have found general jurisdiction if defendants' contacts were aimed at or *felt* in the forum state. This can lead to finding jurisdiction even where a passive website would not support jurisdiction under *Zippo*. For

example, in *Panavision International, LLP v. Toeppen,* 141 F.3d 1316 (9th Cir. 1998), the court of appeals, citing *Zippo,* found general jurisdiction even though defendant's websites were not interactive, holding that because defendant intended to cause harm to a California resident, it was or should have been aware that the effects of its website would be felt in California.

Conversely, in *Voltraix v. NanoVoltraix,* 2009 U.S. Dist. LEXIS 91380, at *10 (D.N.J. 2009) the court denied the exercise of jurisdiction because defendant had not expressly aimed his tortious conduct at the forum state, concluding that because defendant's website was available nationwide and because plaintiff could not prove that defendant targeted its website specifically at New Jersey residents or aimed to exclude residents in other states, the forum was not the focal point of the tortious activity.

While courts differ in their approaches, corporations seeking to avoid being hauled into a particular forum on the basis of their internet activity should consider the level of their contacts with that form and limit it as necessary. Companies using the internet to enter into contracts, generate sales, directly target and solicit residents of the forum are more likely to be subject to U.S. jurisdiction than those who merely provide information about its products or services.

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Mediation of Complex Multiparty Commercial Litigation

BY GREGORY A. MARKEL AND MARTIN SEIDEL | CADWALADER WICKERSHAM & TAFT LLP

Complex, multiparty commercial litigation is often difficult to settle. The parties tend to have divergent interests and partial settlements may not make sense to one side or the other for a variety of reasons. An example would be securities class actions where there is a committee of lead plaintiffs' counsel and defendants that include an insured issuer, individual defendants, investment banks, an accounting firm and other defendants. Adding in the fact that large dollar amounts are frequently claimed and are difficult to estimate, class issues are involved, opt-outs are a potential threat, the plaintiff's counsel don't always speak with one voice and insurers sometimes have viewpoints that differ from their insured's on at least some issues and the complexity of negotiations is obvious. In short, there are many moving parts, no one party may be able to organise the others and achieving global settlement can seem like herding cats. This article will address the value of mediation and a good mediator in dealing with settlement in this kind of context.

Early Case Assessment

To evaluate whether and when a settlement overture is prudent, early case assessment by counsel is essential. What are the underlying facts, applicable law and other considerations bearing on the settlement value of the litigation? Often this analysis must be done with incomplete information because discovery is not complete and

may not have even have started if an early settlement is what is contemplated. Nonetheless, the better the early case assessment, the better the early strategic decisions for the case. If and when a decision is made that exploring resolution with the opposition might have value, it is necessary to decide how to approach the opposition. For reasons described below, in complex litigation it is often useful to enlist the help of a mediator.

Mediation

There are several arguments often made against proposing mediation, particularly early in a case, such as:

- Suggesting mediation is a sign of weakness.
- The mediation process will reveal information to the opponents.
- Some hard-nosed litigation and further discovery will soften up the other side.

We would agree that there can be validity in some situations to each of these points. However, the weight of each depends on the particular circumstances of each case. Large litigation tends to be *sui genesis*. No rule fits every case and the reasons not to mediate or not to mediate early will not always apply.

There are cases where a suggestion of early mediation is not a sign of significant weakness. Although judgment must always be exercised, often experienced lawyers on both the plaintiffs and defence side know each other and a low key suggestion of mediation at an appropriate time in a careful way would generally not be viewed as a significant sign of weakness.

As to other factors to consider, the relative strength of a party's case may or may not be apparent. Knowledgeable inside and outside counsel may have some insight early in a case on whether improvement or deterioration of the prospects of success is likely if and when discovery moves forward. On the other hand, one often does not know what the other side has in the way of evidence nor what might lurk in voluminous, so far not fully reviewed, email. Therefore, one cannot generally be certain early in a lawsuit if the case will get better or worse.

Although disclosing one's main themes in an early mediation may have some downside, it is not often a very great downside and needs to be weighed against the value of possible resolution of the matter. The costs of full blown discovery in securities class actions, can be assumed to be very high.

Thus, one comes back to the conclusion that an overall evaluation must be done based on all the facts and circumstances of each case to determine whether proposing mediation at any given time makes sense.

What Mediation Adds

Education of the Parties on the Merits

Often settlement talks go nowhere for a variety of reasons.

- The parties don't realistically know their own case.
- Parties don't understand their opponent's case very well.
- The parties assess both their case and their opponent's with the prejudice and even emotion of advocates or participants, not the eyes of neutral sophisticated observers.
- It is hard to get multiple parties to talk seriously at the same time.
- As a result, the parties frequently have mismatched evaluations of a case that gets filed.

One value of a mediation can be to aid in the education of the parties on the strengths and weaknesses of their relative positions. The natural tendency of each party to a dispute will be to try to convince the others and the mediator that they know everything they need to know about a dispute, and that their "position" is the right one. The reality generally is somewhere in between. A mediator can assist the parties in improving their understanding of the value of the case by encouraging the exchange – under mediation privilege – of briefing that lays out the key factors in the case. Setting down in writing the strengths and weaknesses of one's own case is often a useful educational exercise in itself. In conjunction with a review of the opponent's briefing, preparation for mediation can lead to new awareness and help narrow the differences in the evaluations of a given case.

A good mediator will encourage parties to share information early in an effort to help each of the parties to understand the case better. It is true that there is often concern that some tactical advantage or surprise might be lost by sharing information with an opponent – but the reality in modern litigation is that providing carefully selected information early can be worth more than saving it for possible surprise use later. The calculation is simple: Few key pieces of information escape notice until trial (and most cases are never tried anyway) but if given to an opponent it may have a meaningful impact on the opponent's evaluation of the value of its case in the settlement process. The information received from the other side can clearly be valuable for similar reasons.

The mediation process can help force participants to look more closely at their own position, the other party's positions and get some input from a respected neutral observer. If the process helps bring the respective parties' evaluation of their position more closely in line with each other, it can materially improve the chances of settlement. The mediation process may also be the only chance a client gets to hear the unvarnished merits and demerits of its case. This can obviously be extremely valuable particularly early in a case when strategic decisions are being made.

Negotiating Process

One thing aided by mediation is speeding up the settlement process. Often one can evaluate the likelihood of an early resolution in one mediation day. By contrast, settlement discussions without a mediator often, though not always, devolve into a long and desultory settlement dance with little learned about the merits or the other party's real settlement position. If evaluating settlement prospects quickly, without appearing anxious, is of importance, mediation is a great help.

The Mediation Process

Once parties arrive for the day of mediation, the mediator's job is to foster constructive consideration of the issues. The first event is often an opening presentation. Mediators often encourage counsel to avoid being overly strident and to think carefully about mediation tone, making concessions, focusing on the key issues and keeping credibility. The opening session of a mediation is often the only time during litigation and before a trial when the parties have the opportunity to talk directly to the decision makers on the other side of the table. Mediators can help the parties to have an opening session that involves constructive and frank dialogue about what the case is about and helps the parties to focus on the key issues.

One valuable tool a mediator has for use in trying to bring a matter to resolution is access to information about what the parties are thinking. During the course of the day the mediator spends time with each side alone in private caucus. Discussions with parties in private caucus are generally much more constructive than with their adversary sitting across the table. The parties generally feel more comfortable giving information, pushing

and being pushed and having limits tested in private caucus. If a mediator can earn the trust of the parties he or she can use the insights gained in each room to help move the discussions forward and try to lead the parties to realistic expectations. A skilled mediator can thereby greatly improve the chances of settlement.

Often the bargaining process in settlement gets bogged down on ego and minor tactical considerations. The relative size of changes in offers and counteroffers or the midpoint between the parties' positions can take on an exaggerated importance that obscures and detracts from the real goal of ultimate resolution of the dispute. A skilled mediator usually tries to avoid back and forth bids in small steps and is much more than a messenger. He or she subtly guides the parties to a range of possible resolutions while trying to suppress the importance of ego and gamesmanship. The way mediators achieve this is difficult to describe in detail because it is as much art as science and because every case and the personalities involved are different. However, the mediator's skill and the use of creative ways of developing settlement ranges can be vitally important in getting to a successful result.

Of particular relevance here, a mediator who is experienced and skilful at dealing with the particular problems of securities class action settlements is extremely valuable. A good understanding of the defences, damage issues, class issues and dynamics of plaintiffs counsel and insurers is invaluable in helping get to settlement.

In complex litigation expense can be very material in absolute terms and relative to the amount in dispute and to the cost of settlement. In the right circumstances mediation and the right mediator can help bring about earlier settlements and result in saving all parties on litigation expense and that saving itself can help bridge gaps to settle some cases.

Conclusion

Mediators can bring real value to the resolution of disputes by speeding up the settlement process, causing the parties to educate themselves on the real merits of their position, tempering expectations, facilitating negotiations, finding common ground, reducing ego and posturing and saving litigation expenses.

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A Practitioner's Guide to Domestic Enforcement of Foreign Arbitral Awards

BY GREGORY A. MARKEL AND MARTIN L. SEIDEL | CADWALADER WICKERSHAM & TAFT LLP

In the United States, as in many countries, courts favour the use of arbitration as an alternative to judicial resolution of disputes. *See Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.,* 473 U.S. 614, 615 (1985) (federal policy in favour of arbitration "applies with special force in the field of international commerce."). The enforcement of arbitral awards is governed by international treaty, U.S. Federal law and the law of each of the fifty states. Practitioners seeking to enforce arbitral awards in the United States need an understanding of how these

regimes interact, which law applies in what circumstance, and how to navigate the state law/federal law divide.

In the United States, enforcement of foreign arbitral awards is governed by the Federal Arbitration Act (the "FAA") (9 U.S.C. §§ 1-14), and applies to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention") (9 U.S.C. §§ 201-208), and the Inter-American Convention on International Commercial Arbitration (the "Panama Convention") (9 U.S.C. §§ 301-307). Collectively forming the federal law of arbitration, the FAA is binding in all federal courts and may be applied in state courts as well. *See, e.g., Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.,* 460 U.S. 1, 2 (1983) (in enacting the FAA, Congress created a "substantive rule applicable in state as well as federal courts.").

The New York Convention provides that all signatories must enforce arbitral awards rendered in other party states, and federal courts will enforce this requirement through Section 2 of the FAA. *See* 9 U.S.C. § 205; *see also Thomas v. Carnival Corp.,* 573 F.3d 1113, 1116 (11th Cir. 2008). Likewise, the Panama Convention provides for full enforcement by signatory states of arbitral awards rendered within any signatory's borders (there are 19 signatory States to the Panama Convention).

The FAA provides for enforcement under both the Panama Convention and the New York Convention depending on the state of origin of the majority of the parties to the arbitration agreement and which convention they have ratified. 9 U.S.C. §§ 305(1) and (2). Pursuant to the FAA, enforcement under the Panama Convention is subject to the same procedural rules as those of the New York Convention. 9 U.S.C. § 302 (making 9 U.S.C. §§ 202-205 and 207, regarding the New York Convention, applicable to the Panama Convention). Parties seeking to enforce an award rendered under either the New York or Panama Convention may do so in either federal or state court. 9 U.S.C. §§ 205 and 302.

Enforcement in Federal Court

As in all federal cases, a federal district court must, prior to entertaining an action to enforce a foreign arbitral award, satisfy itself that it has jurisdiction over the subject matter of the action and the party against whom enforcement is sought. In general, the party against whom enforcement is sought must have sufficient minimum contacts with the forum state in which the district court is located. *Int'l Shoe Co. v. Washington,* 326 U.S. 310, 316 (1945). While not dispositive, "the fact that the proceeding [is] one for the enforcement of an arbitral award, rather than an adjudication on the merits," positively influences the personal jurisdiction analysis. *Telcordia Tech Inc. v. Telkom SA Ltd.,* 458 F.3d 172, 179 (3d Cir. 2006). Indeed, "although the New York Convention does not diminish the due process constraints in asserting jurisdiction over a non-resident alien, the desire to have portability of arbitral awards prevalent in the Convention influences the answer as to whether" personal jurisdiction exists. *Id.* Thus, although minimum contacts must be shown for a federal court to assert jurisdiction and enforce a foreign arbitral award, the federal policy favouring arbitration and the desire for uniformity in enforcement of international arbitral awards make it more likely that a party to an international arbitration agreement could reasonably foresee being brought into a court in another nation in connection with the arbitration. *See id.*

Additionally, any action for enforcement must arise under either federal question or federal diversity jurisdiction. *Durant et al. v. DuPont,* 565 F.3d 56, 63 (2d Cir. 2009). The FAA does not, by itself, confer independent federal question jurisdiction upon the district courts. *Id. See also Moses H. Cone Mem'l Hosp.,* 460 U.S. at 25. An action to enforce a foreign arbitral award falling under either the New York or Panama Convention, however, is justiciable as a federal question because such an action is deemed to arise under the laws or treaties of the United States.

See 9 U.S.C. § 203 (conferring original jurisdiction upon the federal district courts in actions to enforce arbitral awards under the New York Convention); *see also Jacada Ltd. v. Int'l Mktg. Strategies,* 403 F.3d 701, 709 (6th Cir. 2005); *Int'l Ins. v. Caja Nac. De Ahorro Y Seguro,* 293 F.3d 392, 395 (7th Cir. 2002). Nevertheless, to enforce an award issued under the New York Convention, one of the parties must be foreign or, if both parties are United States citizens, the dispute must have a "reasonable relation with one or more foreign states." *See* 9 U.S.C. § 203. Similarly, the Panama Convention provides for enforcement only where the award was rendered in one of its member States. *See id.* at § 304.

Under the FAA, a petitioner seeking to enforce a foreign arbitral award must commence the enforcement action within three years from issuance of the award. *Id.* at § 207. The petitioner must provide the district court with: (i) an original or certified copy of the award; and (ii) an original or certified copy of the parties' written agreement to arbitrate. *Id.* at § 13. If the petitioner fails to produce the written arbitration agreement, the court may dismiss the action for lack of jurisdiction. *See Czarina, L.L.C. v. W.F. Poe Syndicate,* 358 F.3d 1286, 1291 (11th Cir. 2004). When evaluating a party's request for enforcement, the district court's task is one of limited discretion: "[t]he court shall confirm the award unless it finds one of the grounds for refusal or deferral of recognition or enforcement of the award specified in the [New York] Convention." *Id.* While a court may not refuse to enforce an award merely because the arbitrator may have misapplied the law, it may refuse enforcement where the New York Convention's requirements for enforcement have not been satisfied. *Karaha Bodas Co. v. Perusahaan Pertambangan Minyak,* 364 F.3d 274, 288 (5th Cir. 2004). *See also Mitsubishi Motors Corp.,* 473 U.S. at 629 (emphasising need for uniformity in enforcement of arbitral awards, "even assuming that a contrary result would be forthcoming in a domestic context.").

Accordingly, a district court may decline enforcement of a foreign arbitral award where any of the following defects enumerated in Article V of the New York Convention exist: (i) the parties to the original agreement were without legal capacity to enter into the agreement, or the agreement was legally invalid under the law of the rendering jurisdiction; (ii) the arbitration proceeding was lacking in fairness or fundamental due process requirements; (iii) the award is based upon matters outside the scope of the arbitration agreement; (iv) the arbitration procedure or the arbitrators selected were either outside the bounds of the agreement or unlawful under the rendering jurisdiction's laws; or (v) the award has yet to become binding on the parties. *See* 9 U.S.C. § 207. Enforcement may also be denied where the subject matter of the arbitration would have been unfit for arbitration under United States law or policy. Article V of the Panama Convention provides the same grounds for non-enforcement of a foreign arbitral award.

Enforcement in State Court

Each state in the United States is permitted to enact its own rules regarding enforcement of arbitral awards. The majority of states—like the federal government—favour arbitration and many have modelled their enforcement rules after those of the Uniform Arbitration Act (the "UAA"). *See, e.g., Lane v. Urgitus,* 145 P.3d 672, 678 (Colo. 2006); *Tim Delmarva Power v. NCP of Virginia, L.L.C.,* 557 S.E.2d 199, 202 (Va. 2002). Under Section 22 of the UAA, where a party to an arbitration agreement has applied for confirmation of an arbitral award, the court must confirm the award unless grounds for non-enforcement similar to those enumerated in the FAA are present. *See* UNIF. ARBITRATION ACT § 23 (2000). The UAA provides that the individual state's statute of limitations shall apply to all actions to confirm or enforce an award. UNIF. ARBITRATION ACT § 22, COMMENT 2 (2000).

PRACTITIONERS bringing enforcement actions in state court must, therefore, apprise themselves of the relevant jurisdiction's procedural requirements for enforcement of arbitral awards.

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A Rumour vs. Insider Trading – A Line You Don't Want to Cross

BY STEVEN D. FELDMAN | HERRICK, FEINSTEIN LLP

The F.B.I. and Securities and Exchange Commission are focusing on insider trading among financial industry professionals – hedge fund traders, analysts, stock brokers and company insiders. The cases focus on industry professionals who use a network of industry contacts to gather information on a company. Potentially, a trader may come across a piece of problematic information when building a big picture mosaic about the company. In these situations, ignorance of the basic rules can expose you or your company to monetary and criminal liability. You build your overall assessment of an investment with many pieces of information. What if one out of a hundred constitutes insider information? Below, we look at certain "grey areas" of the law to help you avoid crossing the line.

When a Rumour is Already Public, You may Still be at Risk

Picture the following scenario: a major publication releases news that a potential takeover of Company A may be in the works and could even be imminent. Obviously, you can trade on this information since it is available to the general public. The night of the publication's release, you get a phone call from a friend who works at Company A telling you that the takeover is likely to occur. You might think to yourself that this isn't inside information since the rumour is already public knowledge and the phone call simply confirms this.

But you would have been better off if your friend had never called you, because now you may be breaking the law if you make that trade. While the law provides an "escape clause" for traders where the information has already been "publicly disclosed by the press or otherwise," public disclosure won't relieve a trader from liability if he or she in fact trades on material, non-public information (i.e., the confirmation phone call). In *United States v. Mylett*, a *Wall Street Journal* report speculated about a possible takeover of NCR Corp. by AT&T. After the article was published, an insider told an investor that the news story was accurate but the deal was still "contingent and speculative". This investor traded on the information. The court found the investor guilty of insider trading, concluding that the information provided by the source was non-public since it was "substantially more specific than in the newspaper" and would make a reasonable investor less likely to believe that "nothing" would happen. So the courts consider any such non-public information which is likely to make someone more confident in the truth of a rumour to be inside information – and trading on this information can be a crime.

Materiality: Can a Drop of Insider Information Change the Colour of the Entire Picture?

You've crossed the line between rumour and insider trading only if the information you received is "material". What does this mean? Courts use what's called the "total mix" test – there must be a substantial likelihood that a reasonable investor would view the "inside tip" as having altered the "total mix" of information available. In other words, without that "inside tip" the investor's opinion of the stock would be different and he would most likely not trade it. For example, in the course of her research an analyst may stumble upon a small bit of non-public information that she takes into account in making her recommendation. While she may believe this information is harmless given the amount of information she has collected, the courts may disagree. The courts believe that if a "reasonable investor" would find this bit of information important enough to alter the total picture in some way, then the information is material. And if you trade on it, you've broken the law.

The source of information is also important in determining whether a bit of information is "material". For example, one court noted that "[t]he fact that the information comes from an executive, who worked twenty-three years at Burlington and who was privy to the company's confidential information, heightens the credence a reasonable shareholder would attach to such information." *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410 (3d Cir. 1997).

Finally, the specificity of the statement is crucial. While there is no definitive test, the following lists provide examples of pieces of information and how courts view them:

Material & Non-Public Inside Information	Immaterial
Information regarding a meeting between a potential target company and bidder.	Information from an insider about a company's mere intention to pursue a merger at some time in the future, prior to any contact with potential suitors and absent any evidence of an interested suitor.
A company vice president's "speculative" prediction of an acquisition by his company.	An assistant comptroller's estimate of year end earnings that was 2% lower than the company's announcement ten days earlier.
The dissemination of bookings data for a company.	A corporate spokesperson's disclosure to an outsider that preliminary earnings statements for the company will be coming out in a week.
When asked if earnings for the 2nd quarter will be down, a corporate spokesperson tells the questioner that there is a good possibility and to keep the information confidential.	A forecast that future sales and revenue would not be as good as in the past.

What this Means to You

For financial institutions: Hedge funds, investment advisors or any other financial services firms must ensure that their insider trading compliance programs are robust and active so that they are insulated from employees' illegal actions. Does your company provide an annual insider trading training class to your employees? Does your company enforce its insider trading policy? If you become aware of a suspicious trade by an employee, do you investigate it thoroughly and self-report to the authorities? Do you record employees' business phone calls to

compel compliance with your company's anti-insider trading policy?

For financial industry professionals: You must understand the "grey line" between permissible industry rumour and illegal inside information. When confronted with questionable information, always err on the side of caution and involve your compliance department and outside counsel if necessary. If the information seems suspect, it most likely is.

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Prepare Now for the Knock on the Door: As Tax Enforcement Accelerates, Legal Counsel Must be Prepared for Many Layers of Client Need

BY DAVID GANNAWAY | MARKS PANETH & SHRON

Is your client a target of federal tax authorities?

The odds that you answered "yes" are higher today than they have been at any time in recent memory. The federal government is on a drive to increase tax revenue, and part of their effort involves a much higher level of tax enforcement – up to and including the dreaded "knock on the door" – a full-scale visit to the taxpayer's home, often after hours, by multiple law-enforcement agencies, not just the IRS but also the FBI, as well as local and state law enforcement agencies.

Taxpayers are typically unprepared for sudden, intensive scrutiny – which might even involve arrest and attendant publicity. In a state of distress, they will typically turn to legal counsel. Counsel, in turn, must be prepared to meet the demands of the investigation or of multiple overlapping investigations by different agencies.

Budget Shortfalls and a Fraud Epidemic Have Lead to an Aggressive Enforcement Campaign

There are multiple reasons for the heightened level of enforcement. The first and most obvious is that authorities are under pressure to generate revenue. As a result of the massive economic downturn, tax revenue has declined as a direct result of the drop in individual and corporate incomes. This has happened just as increased government spending on recovery programs increased the pressure on the shrinking revenue pool. Any additional revenue that can be found can help close the gap. They are targeting any and all revenue that will help close the "tax gap" – the gap between what taxpayers actually pay, and what the U.S. Internal Revenue Service believes they should pay. This is a recipe for heightened enforcement – enforcement that in particular targets individual taxpayers, who have the greatest discretion over how much tax to pay.

At the same time, fraud is on the increase, as it always is in difficult economic times. Individuals want to make up their portfolio losses, and fall prey to "too good to be true" schemes (the Madoff case is only the most famous of many examples). This is especially true of high-net-worth individuals, who have more losses to make up. Businesses desperate to maintain cash flow begin to cut corners as well.

The result is a "perfect storm" of enforcement – intensive demand for revenue just as instances of taxpayer fraud hit peak levels.

High-Net-Worth Individuals are the Primary Enforcement Targets

As noted, individual taxpayers are the primary enforcement targets.

Among individual taxpayers, the IRS is in particular targeting high-net-worth individuals. Of those, highest on the list are those who have high income and/or net worth, and who in addition are responsible for reporting their own income and expenses. Included as well are officers of businesses – family-owned, S-corporations or partnerships – that are not subject to reporting requirements. Finally, there are a limited number of wage-earners, very senior and highly compensated, whose complex investments open them to attention.

The reason these individuals are targeted is due first of all to the fact that their discretionary control over income reporting and declaration of expenses is much greater than that of large corporations, which are tightly regulated and are effectively subject to constant audit. Wealthy individuals are attractive to the IRS most obviously because of simple return on investment. A successful enforcement action against a wealthy taxpayer means more tax revenue for each enforcement dollar spent. Under new tax rates – the top bracket in the Obama Administration's tax plan is now 39.6 percent. This means a $1 million judgment produces nearly $400,000 in tax revenue.

Then there is the deterrent effect. An enforcement against a prominent person will have a chilling effect on many others. A senior surgeon or a CFO is a far more valuable target than a factory worker who claimed a questionable expense.

An additional risk affecting certain high-net-worth individuals is the holding of undisclosed overseas accounts. The federal government recently closed its window for voluntary foreign account disclosure. There are likely to be stringent enforcement efforts and strict penalties for those taxpayers who did not take advantage of the disclosure period and who continue to hold these accounts.

Enforcements Are Complex, Aggressive, and Spill Over into Business and Personal Finances

What does a tax enforcement action entail?

The answer is as complex and individual as the taxpayers involved. The IRS can and often does limit itself to civil enforcement actions. But it also has the power to bring criminal charges, and often does this too, both on the merits and for the sake of deterrent effect. In a civil action, consequences involve the recovery of unpaid taxes and the imposition of penalties. A criminal action adds the possibility of conviction and sentencing, perhaps to a prison term.

In addition, when a criminal action includes the participation of multiple agencies, such as federal, state and local law enforcement, multiple charges in multiple jurisdictions are a likely outcome. The U.S. attorney might bring an action alongside the IRS, and state or local charges might follow depending on the nature of the activity. A multi-jurisdiction criminal enforcement action can quickly spiral to levels of extreme complexity.

A criminal action typically includes all the usual techniques in the enforcer's toolkit, techniques designed to persuade him or her to disclose more information, and disclose it sooner, than necessary. The knock on the door during dinner is typical, and the knock on the door at 6 a.m. is not unheard of. The accused finds his home suddenly occupied by tax officials, FBI agents and/or police. Officers fan out to seize documents and computers. The accused often begins to talk, rather than remaining silent and requesting counsel, as he or she has a right to do.

The records seized often cover years of financial activity, and the investigation often looks back years as well.

Fraud is not a sudden crime. It takes years to develop. Investigators know this, and will generally want to review tax, investment and business documents stretching back three years or longer.

Accounting Expertise is Needed, but Using the Individual's Current Accountant Means Waiving Attorney-Client Privilege

Therefore, the client who arrives in your office is often in a state of extreme distress, is facing scrutiny for an extended period of financial activity, and has sometimes shared information that need not have been shared. As counsel, you are immediately in challenging circumstances having to deal with a frightened client and very possibly with multiple investigations by multiple agencies in multiple jurisdictions.

The essential step for counsel is to put the right support team in place. Attorneys will know how to deploy their own firm's resources to support the defence. But when it comes to adding additional skill sets, in particular accounting, there are pitfalls to be avoided.

One of the most common mistakes is to engage the client's current accountant. Sometimes counsel does this. More often, it is the client who seeks out the familiar tax professional who has worked on the account for years. This can be catastrophic. The problem is that if the accountant has been involved in the client's affairs on an ongoing basis, attorney-client privilege does not apply. The accountant can and will be questioned, not just about the matter at hand, but about the full range of the client's business and financial activity. The effects of the greatly expanded scope of the investigation can be devastating. Do not engage the current accountant as part of a fraud defence. Instead, it is essential that counsel hire a new accountant or, preferably, an accounting team that comes fresh to the case and will be protected by privilege.

A Full-Service Accounting Firm Brings Multiple Capabilities to Bear – Capabilities that Match All the Complexities of the Client's Situation

As to the merits of an accounting team, the ideal support for counsel in a tax enforcement action is a full-service accountancy that can offer multiple disciplines and skill sets. The reason is simple. The investigation will typically range across all of the client's business, investment and personal financial activity. The accountants at the table need to be deeply familiar with all of that activity as well. That way, they can play their most valuable role – serving as investigators of fact, while the legal team develops its defence, negotiation and/or trial strategy.

Among the accounting skill sets that ought to be represented are:

- *Tax litigation/IRS experience:* Many accounting firms hire IRS veterans to play key roles in their tax litigation practices. These former IRS officials know what motivates the IRS, and how the agency will develop its investigative strategy. They can develop and run the parallel investigation that is essential to the defence team. They also understand what kind of outcome will be acceptable to IRS investigators, and can thus guide negotiations should the case develop in that direction.
- *High-net-worth experience:* A firm with a specialised practice advising high-net-worth individuals will be better able to understand, review and track the complex tax filings and investment instruments that are at the heart of the federal enforcement action.
- *Small and family-owned business experience:* As noted, small and family-owned businesses are a particular target for tax enforcement, overlapping with the high-net-worth category. Again, experienced accounting

professionals can better understand the client's business actions and how they generated tax consequences. In addition, accountants versed in small business issues can add value by helping guide the client through the current effects of the investigation, which typically put severe demands on the business and may require its reorganisation.

- *Bankruptcy experience:* Bankruptcy may be an outcome of litigation for both businesses and individuals, and may be an advisable strategy in advance of any outcome. The accounting team can add value by being able to manage the tax aspects of the bankruptcy filing.
- *Matrimonial experience:* Just as the financial impact of tax litigation can affect business structures, it can also affect personal and household finances and tax strategies. Experienced accountants can manage a range of outcomes, including the restructuring of household accounts, and the financial effects of separation and divorce.

Overall, accountants with some combination of these skills will be the best partners for legal counsel, best able to plan and manage the needed parallel investigation and add value by helping counsel advise the client. Note that many of the events at issue such as bankruptcy and other business consequences might happen even if no investigation occurs.

It would be sensational but not inaccurate to say that it is now "open season" on those who have committed tax fraud, and on those who are suspected of having done it. The stress on at-risk individuals will be high, and that stress will spill over to their counsel. At the same time, tax litigation defence is bound to be a growing area for law firms for the foreseeable future. Counsel will have an easier time, and will be more effective, if it can assemble a multidisciplinary team to meet the government's effort. An accounting firm with diverse, specialised skills should be a part of it. This extended team is best qualified to defend, and create value for, the client.

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The Case for the "Gold Standard": Why the US Must Adopt International Financial Reporting Standards

BY ANNA ZUBETS | MARKS PANETH & SHRON

Can you envision a world in which the U.S. is no longer the world's premier marketplace for capital? We can. In fact, unless U.S. companies and exchanges act, we believe that the world may be well on its way to a new financial order, one in which the U.S. no longer leads.

At issue is the adoption of International Financial Reporting Standards ("IFRS"), a set of reporting requirements promulgated by the International Accounting Standards Board ("IASB") that establishes "principles based" standards for financial reporting. By contrast, the U.S. system, rooted in GAAP (Generally Accepted Accounting Principles), is (in spite of the use of "principles" in the name) more rules-based and thus more restrictive.

IFRS is Gaining Momentum

The push for IFRS is gathering momentum around the globe. According to the American Institute of Certified Public Accountants ("AICPA"), more than 12,000 companies in approximately 113 nations have adopted IFRS. The numbers include listed companies in the European Union. AICPA reports that other countries, including Canada and India, are expected to transition to IFRS by 2011. Mexico plans to adopt IFRS for all listed companies starting in 2012. By some estimates, the number of countries requiring or accepting IFRS could grow to 150 in the next few years. Japan has introduced a roadmap for adoption that it will decide on in 2012 (with adoption planned for 2016). Still other countries have plans to converge their national standards with IFRS – with IFRS likely to dominate.

But Many in the U.S. Resist IFRS – This is a Serious Mistake

But the pattern of adoption is not uniform. While in the U.S. there are signs of movement toward IFRS adoption (the Obama administration and the SEC have both indicated support for uniform global standards), many U.S. companies and the major exchanges have indicated resistance toward IFRS. There has even been talk of an IFRS "resistance movement."

Rejection of IFRS would be a serious mistake. And convergence, suggested as a less burdensome alternative, would be an unsatisfactory half-measure. The reason is that full-scale adoption of IFRS represents more than just a shift toward an alternative accounting system. It represents a clear commitment to the highest standard of financial reporting – a commitment that confers competitive advantage.

Conversion to IFRS Will Challenge Businesses – Large and Small, Public and Private

Conversion to IFRS presents a series of challenges to business organisations of all sizes, challenges that go far beyond financial reporting requirements. For example:

- Companies must establish internal controls that comply with IFRS and not U.S. GAAP. During the transition, companies will need to develop controls that bridge the old and the new environments.
- Audit committees' expertise will need to be refreshed. This will require specific, detailed training for each committee's designated financial expert.
- Sarbanes-Oxley 404 compliance procedures and systems will need to be revised to allow for operation under IFRS.
- Extensive staff training will be required, as will significant revisions to information systems.
- Contractual arrangements (e.g., debt covenants and bonus plans) will require changes to conform to IFRS standards.
- Tax reporting will require reconciliation of IFRS to GAAP income.
- Transaction structures will have to be built with IFRS in mind.
- Investor and stakeholder communications programs will be required to educate all parties about the company's financial health and its go-forward strategies in IFRS terms.
- Financial reporting must be in place long before the conversion to IFRS is complete. Companies will need an opening balance sheet that meets IFRS standards two years prior to adoption, as well as at least one year of financial statements in both IFRS and U.S. GAAP.

These challenges fall not only on public companies, but on private companies that anticipate going public, or that need access to bank financing – banks are likely to demand IFRS financials as a condition for lending.

The question therefore comes to mind: Is IFRS conversion worth the effort? We believe the answer is a resounding "yes."

IFRS is an Information "Gold Standard" that Investors will Favour

Across the globe, IFRS is increasingly regarded as the "gold standard" – the highest quality of information available to investors, regulators and other stakeholders. Markets always favour the best information, and they will favour the companies and exchanges that provide it. Companies and exchanges that do not provide that information will suffer. Companies will find it harder to attract capital, and exchanges will find it harder to attract listings.

In addition, there is a global trend toward uniformity. Uniform standards mean predictability, and divergence from uniform standards represents risk. Investors will reward uniform standards and punish divergence.

Capital will Seek Out Exchanges and Companies that Adopt IFRS

At a time of global consolidation of financial exchanges, such shifts in investor preference can mean life or death for the exchanges, the companies that list on them, and the financial services industry that, in each nation, supports the capital formation process.

Actelion, a Swiss pharmaceutical firm, serves to illustrate what's at stake. Actelion initially wanted to list in the U.S., but did not because of the unfavourable accounting treatment under U.S. GAAP relative to IFRS that would have affected its reporting. Had Actelion applied U.S. GAAP, the result would have been the deferral of significant revenue, causing the company to report a large deficit in shareholders' equity. This prospect led management and its advisors to decide against a U.S. listing. NASDAQ lost the listing opportunity, and U.S. financial services firms lost the chance to support the listing.

Project this experience out on a macro scale – involving thousands of companies and all seven global exchanges – and the risks of rejecting IFRS become clear. In a truly globalised financial environment, where capital flows freely, there is no requirement that all seven exchanges survive, and no guarantee that they will. Capital will flow to the exchanges – and their listed companies – that seem to offer the highest level of predictability and the best quality of information.

Resistance to IFRS Will Damage Companies, Exchanges and the U.S. Economy

In other words, U.S. resistance to IFRS will damage U.S. companies, U.S. exchanges, the U.S. financial services industry and U.S. economic competitiveness in the long run. The effects will be far-reaching. For example, it is not just exchanges, companies and investment banks that will suffer. The U.S. trial bar – and its clients – will pay a penalty as well. If companies avoid U.S. listings, the bar's ability to prosecute cases will be greatly limited since U.S. law no longer predominates.

The case for IFRS is clear. It represents a higher standard and will emerge as the global standard. U.S. regulators and exchanges need to hasten its adoption. U.S. companies need to hasten to support it. And the U.S. financial services industry, as well as other professional constituencies that serve public companies, need to speak forcefully in favour of IFRS. The shift to IFRS will be challenging, but the alternative is to fall behind, and never recover. And that is not an alternative that any responsible participant in the U.S. financial system can reasonably contemplate.

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CANADA

Enforcement of Letters of Credit in Ontario

BY MICHAEL D. SCHAFLER | FRASER MILNER CASGRAIN LLP

In *Nareerux Import Co. Ltd. v. Canadian Imperial Bank of Commerce* [2009] O.J. No. 4553, 2009 ONCA 764, the Ontario Court of Appeal considered whether an issuer of a letter of credit could refuse payment based on the beneficiary's non-compliance with the letter's terms and conditions. The Court ruled in favour of the beneficiary and held that where the issuer has knowingly contributed to, or acquiesced in, the circumstances that undermined the prospect of strict compliance, then that issuer is prevented from relying upon the defence of non-compliance. The issuer's conduct was a direct breach of the principle of autonomy underpinning letter of credit transactions and a breach of the issuer's implied duty of good faith.

Facts

Thai Fisheries Co. Ltd. ("Thai Fisheries") accepted letters of credit from Canadian Imperial Bank of Commerce (the "Bank") in order to ensure payment for shipments of large quantities of Thai shrimp to Douglas R. Robertson International Inc. ("Robertson") in the United States. The shrimp was to be ultimately sold by Robertson to Sam's Club.

Thai Fisheries and the Bank agreed to include the following provision in the letters of credit: "Payment of drafts or drafts drawn hereunder will be effected when accompanied by required documents and after receipt from the applicant of a signed purchase order(s) issued by Sam's Club and related delivery receipt(s) showing container number(s), number of cartons and evidencing that goods have been received by Sam's Club Distribution Centre(s)."

This provision provided the Bank with added protection as the payment to Thai Fisheries pursuant to the letters of credit would be delayed until a purchase order had been delivered by Sam's Club along with related delivery receipts.

Robertson failed to deliver the receipts from Sam's Club to the Bank and as a result Thai Fisheries did not receive payment for substantial amounts of shrimp supplied. The proceeds of sale, however, were used by Robertson to pay down his line of credit at the Bank. The Bank was informed that Robertson may have been withholding the required documents and that there would be no further shipments to Sam's Club. Thai Fisheries was not advised of this information for more than a year thereafter.

Thai Fisheries claimed that the Bank and Robertson acted in collusion by arranging for shrimp to be sold without documentation from Sam's Club and using the proceeds from sale to reduce Robertson's overdraft, and therefore the Bank's exposure.

The Bank claimed that the provisions of the letters of credit were not honoured because the requisite documentation was not presented, and that Thai Fisheries knowingly ran the risk of such an eventuality when it accepted the letters of credit in the first place.

Trial Judge's Decision

The trial judge ruled in favour of Thai Fisheries and awarded approximately US$10.4 million, the unpaid balance under the letters of credit.

The trial judge held that by accepting the monies in payment of the loan owed by Robertson, the Bank acted as a lender seeking satisfaction of what it was owed. However, in doing so, it breached the separate and independent contract it had entered into with Thai Fisheries and an implied duty of good faith which was part of the contractual relationship between the Bank and Thai Fisheries.

The Bank appealed the trial judge's decision.

Court of Appeal Decision

The central issue on the appeal was whether the Bank could rely on the defence of non-compliance, that is, the failure to receive receipts from Sam's Club that would have triggered payment to Thai Fisheries.

The Court held that the Bank was disentitled from relying upon this defence as its own conduct partially generated the documentary non-compliance. The Court based its decision on the trial judge's finding that the Bank was aware that no receipts were produced for US$6.9 million of shrimp delivered by Robertson to Sam's Club and that shrimp was being sold to purchasers, other than Sam's Club, that should have been subject to the requirement of producing receipts. The Bank failed to bring this information to Thai Fisheries' attention and continued to accept the proceeds of sale to reduce Robertson's line of credit.

The Court upheld the trial judge's decision and held that the Bank's conduct was correctly characterised as a direct breach of the principle of autonomy underpinning letter of credit transactions and as a breach of the Bank's implied duty of good faith.

Breach of Principle of Autonomy

The fundamental principle of autonomy requires that the contract between (i) the buyer and the seller, (ii) the buyer and the bank, and (iii) the bank and the beneficiary seller be recognised and treated as three separate and distinct agreements. The Court agreed with the trial judge's finding that the Bank permitted its conflicting concern respecting its financial over-exposure in the creditor/debtor relationship with Robertson to interfere with its payment obligation to Thai Fisheries under the letters of credit. As a result, the Bank had put itself in a position where its obligation under the letters of credit to act independently of the underlying relationships between it and its customer, or between its customer and the beneficiary, had been compromised. In finding a breach of the guiding principle of autonomy by the Bank, the Court held: "Letters of Credit by the issuer and its customer as a tap for payment, depending upon when the Bank and its client wanted to effect such payment – in order to better their own positions vis-à-vis each other as debtor and creditor – nullifies the entire autonomy principle and the independent role required of the Bank under the Letters of Credit."

Breach of Implied Duty of Good Faith

Canadian law recognises an implied contractual duty of good faith to not act in a way that defeats the very purpose

and object of an agreement. The Court agreed with the trial judge's finding that the letters of credit were infused with this implied duty of good faith, which the Bank breached by acting out of self interest and undermining the purpose of letters of credit, that is to provide a degree of financial security.

Failure to Provide Timely Notice

The Court identified an additional basis to reject the Bank's appeal by finding that the contractual language of the letters of credit sufficiently engaged the Uniform Customs and Practice for Documentary Credits (UCP) 500. The letters of credit included the following provision: "This cable is the operative instrument and *subject to* the U.C.P. 1993 revision ICC Publication No. 500 and engages us in accordance with the terms thereof."

Pursuant to UCP 500, the Bank failed in its obligation to provide timely notice of dishonour to Thai Fisheries when it held back on notifying the seller for more than a year that no receipts would be forthcoming and that the letters of credit would be cancelled. The lack of timely notice prevented Thai Fisheries from taking steps to protect itself by seeking return of the shrimp until it was too late and the shrimp had been sold.

Bank's Arguments on Assumption of Risk and Passing of Title

The Court agreed with the Bank that Thai Fisheries assumed the risk of delayed payment and even the risk that Robertson would act dishonestly and fail to provide the required receipts. However, Thai Fisheries' assumption of risk could not be stretched to include the possibility of the Bank and Robertson colluding together to frustrate compliance with the terms of the letters of credit and breaching principles of autonomy and the implied duty of good faith. The Court held that to interpret otherwise would "render the letters of credit commercially meaningless".

The Court also rejected the Bank's claim that upon Robertson acquiring title of the shrimp, the Bank acquired an interest in the shrimp as a secured lender, in priority to Thai Fisheries' interest as an unsecured creditor of Robertson. The Court held that ownership of the shrimp was irrelevant for disposing of this action as Thai Fisheries was not seeking to assert its rights as an unsecured creditor of Robertson. Rather, it was seeking to enforce its contractual rights against the Bank under the letters of credit.

Comments

This case highlights the commitment of Ontario courts to ensure that letters of credit are interpreted in a manner that promotes commercial efficacy and the relative certainty that must surround the use of this financial instrument. This decision also emphasises the importance of incorporating principles of contract law, including those invoking notions of fairness and equity, when enforcing letters of credit.

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The New Summary Judgment Regime in Ontario – From Paper Trial to Mini Trial

BY MICHAEL D. SCHAFLER | FRASER MILNER CASGRAIN LLP

Effective January 1, 2010 the *Rules of Civil Procedure* (Ontario Regulation 194 of R.R.O. 1990, as amended by O. Reg. 438/08), the procedural rules governing litigation in Ontario, were radically overhauled. While there were sweeping changes regarding mediation, discovery, motions and applications procedure, experts and case management, perhaps the most significant change occurred with respect to the summary disposition of claims and defences – the so-called "Summary Judgment Rule 20".

The prior Rule 20 was adopted in 1985. Many had then felt and hoped that it would permit the court to expeditiously dismiss claims or defences that had no real prospect of success. The result was to be a more efficient and cost effective dispute resolution system. The concept was quite simple: once a defendant had determined to bring a motion to dismiss the claim against it, or the plaintiff had concluded that the defendant could not possibly prevail at trial, each party filed with the court affidavits on the merits of the case. There would then typically be cross-examinations, conducted out of court, with the transcripts then also being filed for the judge to read. The parties would then file written arguments setting out why their position should carry the day. The judge would read all the material in advance of oral argument. And, if the court was thereafter satisfied that there was "no genuine issue for trial with respect to a claim or defence", the court became obliged to grant summary judgment. The entire case (or at least part of it) could thus be determined on the basis of a "paper trial".

That, at least, was the contemplated theory. The reality, shaped by a series of judicial pronouncements from the highest court in Ontario, the Court of Appeal, was somewhat different. The Court of Appeal held that in ruling on a motion for summary judgment the court "will never assess credibility, weigh the evidence, or find the facts. Instead, the court's role is narrowly limited to assessing the threshold issue of whether a genuine issue exists as to the material facts requiring a trial. Evaluating credibility, weighing evidence, and drawing factual inferences are all functions reserved for the [trial judge]" (*Aguonie v. Galion Solid Waste Material Inc.* 1998 Carswell Ont 417 (C.A.)).

The consequences of this approach were palpable. Many lawyers and judges were of the view that the Court of Appeal's interpretation of the scope of the motion judge's authority was too narrow. By 2006, summary proceedings were commenced in only 642 or 1% of the 63,251 Superior Court proceedings then pending. It was generally agreed that Rule 20 was not working as originally intended ("Civil Justice Reform Project", The Honourable Coulter A. Osborne, Q.C., November 2007 at p. 33).

In 2006, the Attorney General of Ontario asked the Honourable Coulter Osborne, former Associate Chief Justice of Ontario, to lead the "Civil Justice Reform Project". Justice Osborne's mandate was to propose options to reform Ontario's civil justice system with a view to enhancing accessibility and affordability. Justice Osborne delivered his report in late 2007. As to the restrictions imposed by earlier case law, Justice Osborne had this to say: "If the objective is to provide an effective mechanism for the court to dispose of cases early where in the opinion of the court a trial is unnecessary after reviewing the best available evidence from the parties, then it seems to me to be preferable to provide the court with the express authority to do what some decisions of the Court of Appeal have said a motion judge or master cannot do. That is, permit the court on a summary judgment motion to weigh

the evidence, draw inferences and evaluate credibility in appropriate cases. Therefore, any new rule 20 should provide a basis for the motion judge to determine whether such an assessment can safely be made on the motion, or whether the interests of justice require that the issue be determined by the trier of fact at trial" (*Ibid,* at p. 35).

Indeed, the new Rule 20, on its face, has been drafted to expressly override the earlier jurisprudence. One of the two principal features of the new summary judgment system is new subrule 20.04(2.1) – "Powers": "In determining…whether there is a genuine issue requiring a trial, the court shall consider the evidence submitted by the parties and…the judge may exercise any of the following powers for the purpose, unless it is in the interest of justice for such powers to be exercised only at a trial: 1. Weighing the evidence. 2. Evaluating the credibility of a deponent. 3. Drawing any reasonable inference from the evidence."

It follows that even in the case of a pure "paper trial", the court can exercise the same functions that a trial judge usually carries out with the benefit of *viva voce* evidence.

However, there is a second key element to the new Rule that represents a true departure from the *status quo*. This is the so-called "mini trial". In his report, Justice Osborne stated: "As rule 20 matters now stand, the result of a rule 20 motion is binary: the motion is granted and the action ends, or it is dismissed and the parties are on the way to full trial. In my view, there should be more flexibility in the system. Where the court is unable to determine the motion without hearing *viva voce* evidence on discrete issues, the rules should provide for a mini-trial where witnesses can testify on these issues in a summary fashion, without having to wait for a full trial. This can be done in British Columbia through rule 18A. It could be done in Ontario through a similar rule, i.e., by amending rule 20.

"As noted, at the conclusion of a summary judgment motion, subrule 20.05(1) already confers on the court the power to order matters to proceed to trial "forthwith" on a list of cases requiring speedy trial. In my view, amendments to rule 20 ought to be made to permit the court, as an alternative to dismissing a summary judgment motion, to direct a "mini-trial" on one or more discrete issues forthwith where the interests of justice require viva voce testimony to allow the court to dispose of the summary judgment motion. The same judge hearing the motion would preside over the mini-trial."

The result of Justice Osborne's recommendation is subrule 20.04(2.2) "Oral Evidence (Mini-Trial)" which provides that: "A judge may, for the purposes of exercising any of the powers set out in subrule 2.1, order that oral evidence by presented by one or more parties, with or without time limits on its presentation."

To complement the rule changes, effective January 1, 2010, the Ontario Superior Court promulgated a new Practice Direction (practice directions are notices, guides or other publications that govern the practice for proceedings subject to the appropriate rules of procedure) for cases pending in the Toronto region, where many complex commercial disputes are litigated. With respect to the new Rule 20 regime generally and mini trials in particular, the Practice Direction states as follows: "Amended Rule 20 contemplates that some summary judgment motions will proceed by way of a hybrid hearing (written record, plus some oral evidence) or by way of a hearing on the written record followed closely by a tailored trial of issues. Scheduling the expeditious hearing of these new Rule 20 motions will require greater management by the judiciary. Accordingly, all motions for summary judgment will undergo a scheduling and monitoring process commencing with an attendance at Motions Scheduling Court.

"In addition, in the normal course, the court will contact the parties a few weeks before the hearing of the summary judgment motion to inquire into its status, its readiness for hearing, and whether oral evidence may be required at the hearing of the motion. If the parties advise or the court determines that the motion is not ready

for hearing, the parties may receive further directions from the court regarding the scheduling of the hearing of the motion" (Practice Direction for Civil Applications, Motions and other Matters in the Toronto Region Effective January 1, 2010, para. 12-13).

The consequences of these changes should be felt fairly soon. It is expected that in relatively simple cases counsel will now advise their clients to bring motions for summary judgment when, in the past, they would have been reluctant to do so. However, the same may also hold true for complex cases. At worst the moving party will have compelled a trial of an issue. This alone could result in greater efficiencies, both in terms of time spent litigating and possibly also in terms of motivating parties to an early out of court settlement. One potential disadvantage could be the over proliferation of Rule 20 motions, resulting in unintended stresses on the judicial system and longer than expected times for motions to be heard and decided. Whatever the outcome, though, it is submitted that the new regime is an improvement to the old one.

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The "Gatekeeper" Requirement and Secondary Market Liability Class Actions in Canada

BY MARK EVANS AND MATTHEW FLEMING | FRASER MILNER CASGRAIN LLP

In Canada, proposed class actions by shareholders who acquired their shares in the secondary market have traditionally met with little success. While a statutory cause of action has long existed in connection with the primary market, where investors purchased securities pursuant to a prospectus or an offering memorandum, shareholders who acquired securities in the secondary market were essentially forced to rely on the common law claim of negligent misrepresentation. With rare exceptions, Canadian courts refused to certify such claims on the basis that whether or not a shareholder relied on an alleged misrepresentation was an individual issue and thus unsuitable for resolution in the context of a class proceeding. In doing so, Canadian courts have largely rejected the "fraud on the market" doctrine adopted in the United States, which presumes that most, if not all, of a company's public information is reflected in the market price of its securities with the result that an investor's reliance on any public material misrepresentation may be presumed.

Against this historical backdrop, each of the jurisdictions in Canada has recently adopted statutory provisions which expose reporting issuers, together with their directors, officers and professional advisors, to the threat of statute-based secondary market class action liability. In essence, the new secondary market liability provisions allow security holders of a public company to bring an action for damages where a company releases a public document or makes a public statement which contains a misrepresentation, or fails to make timely disclosure of a material change, irrespective of whether or not such security holders actually relied on the alleged misrepresentation.

Significantly, the new statutory provisions include a "gatekeeper" mechanism which provides that no such action may be commenced without leave of the court. Recently, this gatekeeper provision was the subject of

judicial interpretation, for the first time in Canada, in *Silver v. IMAX Corporation,* Court File No.: CV-06-3257-00, December 14, 2009 (Ont. S.C.J.) wherein the Ontario Superior Court granted leave to plaintiffs to proceed with a secondary market liability claim.

The Statutory Regime and the Test for Leave

Section 138.3 of the Ontario *Securities Act* (the "Act") creates a statutory cause of action where a reporting issuer or any other issuer with a real and substantial connection to Ontario releases a document or makes a public oral statement that contains a misrepresentation. Persons who acquire or dispose of the issuer's security during the period between the date the document was released or the statement was made and the date the "misrepresentation" was publicly corrected, irrespective of whether or not they relied on the misrepresentation, now have a statutory right of action against, among others, the issuer, each director at the time the misrepresentation was made, each officer who authorised, permitted or acquiesced in the making of the misrepresentation and, in certain circumstances, "experts" such as auditors, accountants, engineers or lawyers.

Importantly, the legislation was influenced by the prior experience in the United States with "strike suits". Noting that the burden of such unmeritorious suits would ultimately be borne by the long-term security holders of reporting issuers, the drafters adopted several provisions aimed at reducing their likelihood (such as due diligence defences, limits on liability and "loser pays" costs rules) and at minimising the impact on long-term shareholders.

In addition, the drafters recommended the adoption of a preliminary screening mechanism which would require a proposed plaintiff to obtain leave from the court before proceeding with a secondary market liability claim. In this regard, s. 138.8 of the Act provides that the court shall grant leave to proceed with a proposed claim only where it is satisfied that: (i) the action is being brought in good faith; and (ii) there is a reasonable possibility that the action will be resolved at trial in favour of the plaintiff. As discussed below, the court considered each of these elements of the test for leave in *IMAX*.

Background to the IMAX Decision

The central defendant in the *IMAX* case, IMAX Corporation ("IMAX" or the "Company"), is a publicly-traded company engaged in the sale and leasing of 3D theatre systems. In February 2006, IMAX issued a press release announcing, among other things, that it had completed a record 14 theatre installations in the fourth quarter of 2005 and that it expected to meet or exceed its full year earnings guidance for 2005. In March 2006, IMAX filed, among other things, its 2005 annual financial statements.

In August 2006, IMAX issued a press release indicating that it was in the process of responding to an informal inquiry from the SEC regarding the timing of its revenue recognition, including the recognition of revenue in connection with theatres that had not yet been installed. The next day, IMAX's share price dropped 40%. In 2007, the Company restated its 2005 financial statements and acknowledged that it had: (i) erred in recognising revenue for theatre systems that had yet to be completed; and (ii) failed to comply with generally accepted accounting principles.

Based upon the foregoing, the plaintiffs sought leave to proceed with a secondary market liability claim against IMAX and as against several of its directors and officers. In opposing the motion for leave, the defendants made the strategic decision (at the leave stage) to assert and rely upon the due diligence defences of "reasonable

investigation" and "expert reliance" as are made available under s. 138.4 of the Act.

In Brief – The Court's Analysis of Section 138.8

With respect to the first element of the test – that the plaintiffs must be acting in good faith - the court rejected the defendants' assertion that the plaintiffs faced a "substantial" onus in demonstrating good faith. The court concluded that the plaintiffs met the test in that: (i) the plaintiffs had pleaded a misrepresentation which was supported by the evidence of IMAX's restatement of its financial statements; (ii) the plaintiffs had established that they were bringing their claim in the honest belief that they had an arguable case and not for a collateral or ulterior purpose; and (iii) the claim was consistent with the purpose of the statutory cause of action.

Turning to the second element of the test – whether there was a "reasonable possibility that the action would be resolved at trial in favour of the plaintiffs" – the court held that this element required a consideration as to whether or not there was evidence which, if believed, would support the plaintiffs' action. The court went on to note that, although the threshold was "relatively low", the addition of the word "reasonable" in the second element of the test suggested that there must be more than a *de minimis* possibility of success at trial and that the determination of whether such a possibility exists must be based on a "reasoned consideration of the evidence".

Ultimately, the court had little difficulty in determining, based primarily on the restatement of IMAX's financial statements, that a misrepresentation had been made and that leave should be granted as against the Company and most, but not all, of the proposed individual defendants. In doing so, the court stated: "The statutory leave provision is designed to prevent an abuse of the court's process through the commencement of actions that have no real foundation, actions that are based on speculation or suspicion rather than evidence."

As we noted above, the defendants opted to try and defeat the leave motion by relying upon the assessed strength of their "due diligence" defences. For the most part, and on the facts of this case, the court provided little comfort that such a strategy would be successful. Indeed, and with respect to the "reasonable investigation" and "expert reliance" defences relied upon by the proposed defendants, the court noted that it must be satisfied that the evidence in support of such defences would foreclose any reasonable possibility that the plaintiffs would succeed at trial: "In this regard it is not sufficient (as the [defendants] contend) to put forward defences which the plaintiffs must "overcome"...the court must consider all of the evidence put forward in the leave motion, including evidence supportive of any statutory defence. Because the onus of proof of a statutory defence is on the respondents, the court must be satisfied that the evidence in support of such a defence at the preliminary merits stage will foreclose the plaintiffs' reasonable possibility of success at trial."

In making this determination, the court has set a very high bar to the ability of a defendant, at the leave stage, to successfully invoke the due diligence defences prescribed by the Act in order to defeat a plaintiff's motion for leave to proceed with a secondary market liability claim.

Outside Directors

With respect to the proposed defendants who were "outside" directors of IMAX, the Court drew an interesting distinction between the outside directors who were members of the audit committee and those who were not. The evidence suggested, among other things, that the audit committee members were aware that several of the theatre systems in respect of which the Company recognised revenue were in fact incomplete, with the result that the plaintiffs had a reasonable possibility of success at trial as against these directors. However, the Court found

that the remaining outside directors had a limited role in respect of IMAX's financial reporting and did not receive the information provided to the audit committee. The Court therefore dismissed the plaintiffs' motion for leave to proceed with their secondary market claims against the remaining outside directors – vindicating the decision, at least of these defendants, to proactively assert the available statutory defences at the leave stage.

Conclusion

The court's decision in *IMAX* establishes a relatively low hurdle for plaintiffs to clear in seeking leave to proceed with a secondary market liability claim in Ontario. Conversely, defendants appear to face a significant barrier in successfully invoking the statutory due diligence defences at the leave stage.

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Recent Developments Affecting Arbitrations and Arbitration Awards in Canada

BY CHRISTOPHER J. MATTHEWS | FRASER MILNER CASGRAIN LLP

In the past months, Canadian courts have continued to travel down the long road to full recognition and acceptance of the arbitration process. There continue, however, to be a few obstacles along the way. In some courts, there appears still to be a reluctance to relinquish jurisdiction and control, which is manifested through the use of public policy arguments or an overly narrow view of the arbitration process. Nonetheless, protection of the court's turf is increasingly rare, and the Supreme Court is expected to give further guidance on these issues in the coming year.

A few examples of these developments are outlined in the four cases summarised below.

Are International Arbitration Awards the Same as Foreign Judgments?

The Supreme Court of Canada recently heard argument in a case from Alberta, *Yugraneft Corporation v. Rexx Management Corporation,* 2008 ABCA 274. The narrow issue in *Yugraneft* is what the limitation period is in Alberta to claim on an international arbitration award. The case presents an opportunity, however, for the Supreme Court of Canada to provide guidance generally on the recognition of such awards in Canada.

Yugraneft was argued on the basis that the limitation period for seeking recognition of an international commercial award was either two years or ten years, depending on which provision of the Alberta *Limitations Act* applied. If the period was two years, the plaintiff, Yugraneft, would be out of time and unable to enforce the award.

The Alberta Court of Appeal treated the foreign arbitral award as being akin to a foreign judgment. As Canadian courts have held "for more than a century" that an action to enforce a foreign judgment is treated as an action upon a contract debt, it found that the limitation period is also the same as for a contract debt, that is, two years.

Yugraneft argued that the ten year limitation period under the Act to enforce a "judgment" should apply and that both foreign judgments and arbitral awards should be included in the definition of "judgment". The Court of Appeal

found that a foreign judgment is not a "judgment" and that, in any case, "an arbitral award can be in no better position than a judgment."

The parties appear to have accepted the presumption that an arbitral award can be given no greater recognition than a foreign judgment. One might have thought, however, that this would be the first ground of appeal.

It could be said that the Court of Appeal was answering the wrong question. After all, why does a foreign arbitral award have to be treated the same way as a foreign judgment? There is ample authority in Canada that properly distinguishes between arbitral awards and judgments. As the Supreme Court of Canada stated in *Dell Corp. v. Union de Consommateurs,* 2007 SCC 34, arbitrators are not representatives of the state. They are privately appointed and derive their jurisdiction from the mutual agreement of the parties. The question of comity and recognition of foreign judgments has little or no relevance. In Alberta, and in other Canadian provinces, the recognition of awards is given statutory force by the New York Convention and the Model Law, one or both of which are incorporated into provincial legislation.

In looking at limitation periods for enforcing arbitral awards, one must also ask why they should be treated the same as foreign judgments. In its factum before the Supreme Court of Canada, Yugraneft correctly noted that Alberta's *International Commercial Arbitration Act* (which appends both the Convention and the Model Law) do not impose any limitation period at all. Yet, Yugraneft did not argue that there is no limitation period for international arbitral awards. Its factum rather asked the question: "What limitation period under the *Limitations Act* should apply to an international arbitration award?"

In so doing, it committed itself to forcing an arbitral award into one of the provisions of the *Limitations Act*. This was not an easy exercise for the parties or the court.

Rexx Corporation argued convincingly that an international arbitral award is not a foreign judgment and should not be considered to be akin to one. Not surprisingly, however, Rexx did not take the next step and argue that the *Limitations Act* did not apply to international arbitration awards. It argued that the failure to obey the award was an "injury" for which there was a two year limitation period.

An argument that could have been emphasised by Yugraneft is that any limitation or expiration date on an arbitration award should emanate form the arbitration process itself, and not from the procedural rules of the jurisdiction in which the award is to be enforced. This would be consistent with prior decisions of the Supreme Court of Canada to the effect that limitation periods are substantive rather than procedural (*Tolofson v. Jensen,* [1994] 3 S.C.R. 1022).

We will soon see whether the Supreme Court of Canada clarifies and confirms the unique attributes of international arbitral awards. Perhaps it will find that they are not subject to provincial limitations statutes unless they are specifically referred to in such statutes. It may agree that what Ontario has done in its *Limitations Act, 2002,* (in which it is specifically stated that there is no limitation period for enforcement of an "order of a court" or, mirroring the language of the Ontario *International Commmercial Arbitrations Act*, "any other order that may be enforced in the same way as an order of a court") properly recognises the distinction between awards and judgments and usefully does away with the expiration date on either.

How Broadly should Jurisdiction (or Arbitration) Clauses be Interpreted?

In *Matrix Integrated Solutions Limited v. Radiant Hospitality Systems Limited* 2009 ONCA 593, the Ontario Court of Appeal considered the breadth of a forum selection clause. The case did not involve an arbitration clause but similar principles apply when the court decides whether or not to decline jurisdiction.

A difficult set of facts may have caused the court to interpret narrowly a jurisdiction clause that would have required the parties' dispute to be heard in the Texas court. The Court of Appeal found that claims for breach of fiduciary duty and conspiracy were not claims that "may arise out of or [are] in connection" with the agreement that governed the parties' relationship.

The factual context did not bode well for the strict enforcement of the jurisdiction clause in a reseller agreement. Matrix sued Radiant Hospitality Systems as well as two former employees of Matrix. The employees had left Matrix and started up their own business, allegedly in collusion with Radiant, which then terminated Matrix's reseller agreement. The two employees were residents of Ontario, which is also where the new business operated.

The case was decided on the basis that the fiduciary and conspiracy claims were not in "pith and substance" claims in connection with the reseller agreement. This is somewhat difficult to understand given the broad scope of the jurisdiction clause and because in that context there could be no fiduciary duty in existence without the contractual relationship between Matrix and Radiant. Nonetheless, the undercurrent of unfairness to the plaintiff if the matter was sent to Texas was plain to see. Although it was not addressed by the court, it is unlikely that the exclusive jurisdiction clause was negotiated or that it truly reflected the parties' intentions. Further, should the court have examined forum non conveniens principles, Texas may well not have been found to be the proper forum.

The case demonstrates the importance of drafting forum selection (or arbitration) clauses to address all possible claims arising out of the relationship. It may not be enough merely to state that all claims "in connection with" the contract itself are covered. The court may still find a way to limit the effect of an arbitration or exclusive jurisdiction clause (and thereby hold onto jurisdiction) if it perceives unfairness will result.

Can an Arbitrator Order Security for Costs? Even if he or she can't, can a Court do Anything about it?

The power of the arbitrator to control the arbitration process received a shot in the arm recently from the Ontario Court of Appeal in *Inforica Inc. v. CGI Information Systems* (2009), 97 O.R (3d) 161. At issue was whether an arbitrator had jurisdiction to order a party to post security for costs of the arbitration. Inforica, the party ordered to post the security, moved to quash the arbitrator's order on the basis that he had no jurisdiction to make such an order and because the parties had not agreed on the particular set of arbitration rules that contemplated security for costs orders.

The motions judge quashed the order, relying on a line of cases beginning with Unione Stearinerie Lanza, [1917] 2 K.B. 558 (C.A.) and including a 1979 Ontario Divisional Court decision, *Ramot Gill Development Corp. Ltd. and Precision Homes Corp. Inc.* (1979), 27 O.R. (2d) 199, which supported the argument that an arbitrator had no inherent power to order security for costs.

The Court of Appeal refused to follow this line of cases and found that the motions judge had no jurisdiction to set aside the arbitrator's order. The old line of cases had no application "under today's very different statutory regime limiting recourse to the courts and respecting the autonomy of the arbitral process." The judge's power to review is limited by section 17 of the Ontario *Arbitration Act, 1991*. A review can be only of an order ruling on the arbitrator's "own jurisdiction to conduct the arbitration". As the question of security for costs is not such a ruling, there is no power to review.

The court did not specifically find that an arbitrator has the jurisdiction to order security for costs under section 20 of the Arbitration Act, 1991, which permits an arbitrator to determine the procedure in the arbitration. In fact, Justice Sharpe refused to deal with it, only commenting that the arbitrator had ample evidence to find that the parties had agreed to adopt the arbitration rules at issue.

Whether or not there is jurisdiction to order security for costs, however, may not make any difference, particularly if there is nothing the party can do to overturn the order. The effect of Inforica is that the arbitrator will have the power to control the course of the arbitration free from judicial interference, unless the order goes to the jurisdiction to hear the arbitration itself or is a review of the award disposing of the dispute.

Can the Solicitor Client Relationship be Arbitrated?

In Ontario, the client's right to contest a lawyer's account through the court system has long been well protected. The client may ask the court to examine or assess accounts even if the client earlier agreed to the fee structure and, in some circumstances, even if the account has already been paid. Further, it is only relatively recently that lawyers in Ontario have been permitted to enter into contingency fee arrangements, and then only if the arrangement adheres to a comprehensive code under Ontario's Solicitors Act.

In this context, the Ontario Court of Appeal recently decided in *Jean Estate v. Wires Jolley LLP* (2009), 96 O.R. (2d) 171 whether a dispute over a contingency fee arrangement could be arbitrated under Ontario's *International Commercial Arbitration Act*. The court found that it could be, but, for public policy reasons, also required that the arbitrator take into account the substantive statutory protections available to the client under the Solicitors Act.

The solicitor/client retainer involved estate litigation in Ontario, British Columbia, Hong Kong, China and Japan. The lawyer and the client agreed upon a contingency fee arrangement whereby the lawyer would be paid a "success fee" of 10% of the value of the assets obtained by the client. Disputes relating to the fee arrangement were agreed to be arbitrated. When a dispute arose as to the valuation date of the assets, however, the client brought a motion to strike out the notice of arbitration. The motions judge agreed with the client that the arbitration agreement could not be enforced because it was an improper contracting out of the protections under the *Solicitors Act*.

The Court of Appeal reversed this decision. It agreed that the arbitration agreement could be enforced, citing the "strong policy of deference afforded to arbitration agreements". Justice Weiler, writing for the majority, also relied on the Supreme Court of Canada's reasoning in *Desputeaux v. Editions Chouette (1987) Inc.,* [2003] 1 S.C.R. 401, stating that merely because the *Solicitors Act* "refers to a Superior Court judge as having the jurisdiction to protect clients' rights ... does not mean that disputes arising between a solicitor and a client may not be submitted to arbitration."

The majority of the court did not simply refer the matter to arbitration. On the basis of public policy and a long history of cases that do not allow contracting out of the *Solicitors Act,* it ordered that the arbitrator "must" make the decision in accordance with the protected statutory rights. Justice Jurianz, who wrote a concurring opinion, did not agree with this interventionist approach. His view was that any need for judicial control to meet public policy concerns could be met through a review of the arbitration award.

Conclusion

The pendulum of Canadian jurisprudence continues to swing towards greater recognition and understanding of the arbitration process. As the above cases show, however, the pendulum does not necessarily follow as true a course as some might wish.

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MEXICO

Litigation, Arbitration and Alternative Dispute Resolution

BY JOSE MARIA ABASCAL | ABASCAL & ASOCIADOS

This article deals with commercial or mercantile dispute resolution under Mexican law. Since there are almost no differences in the practice and legal regime of domestic and international disputes, unless otherwise indicated the comments in this article apply equally to both.

Court Litigation

The default dispute resolution method, under Mexican law, is court litigation regulated in the Commercial Code ("CC") (Book Five, Title First (commencing in article 1049) to Title Third Bis, (ending in article 1414 bis 20)). Title First (articles 1049 to 1376 Bis) provides the General Provisions; Title Second (articles 1377 to 1390) regulates ordinary proceedings; Title Third (articles 1391 to 1414) executory proceedings; and Title Third Bis (articles 1414 bis to 1414 bis 20) proceedings for dispossession and enforcement of credits arising out of pledges without transfer of possession and guarantee trusts *(fideicomisos de garantía)*.

There are special procedures, or provisions, on certain branches or categories. Among them, insurance claims, financial leases, law of the sea, corporation law, consumers protection and protection of users of banking services.

The CC gives preference to agreed court proceedings (articles 1049 to 1052). These agreed court proceedings are different from arbitration because they are substantiated before a court. Notwithstanding, the advantages these proceedings offer to the parties are factually ignored in current practice. This practice does not mean that, should the parties agree to tailor rules or proceedings before a court, these would be invalid in Mexico.

Court proceedings under Mexican law and practice follow the written civil law tradition, and are substantially different from oral, common law, proceedings. Two of the more relevant differences with the common law tradition and practice are: (i) parties, following their initial submissions, must present their full case with little, if any, possibility of departing from their initial positions; and (ii) there is no discovery. The practical significance of these differences means the absence of a pretrial stage. Common law lawyers are regularly surprised by these features, find them difficult to swallow, and often develop inappropriate litigation strategies based on their practices.

Court proceedings are, in general, inappropriate for dealing with international disputes, especially large or complex ones. This is partly due to the saturation of courts and recent legal amendments that favour speed over a reasonable opportunity to comply with reasonable due process of law.

Perhaps the only exceptions to this are: (i) collections; (ii) small disputes; and (iii) disputes over rights *in rem*. This caveat is relevant when considering situations like the enforcement of first lien securities over goods or real

state. Foreign judgments over rights *in rem,* are not recognised nor enforceable in Mexico.

Summing up, when considering a forum selection clause in Mexico, it is important to take prior advice from Mexican counsel. Also, advice should be sought to anticipate the circumstances under which a final judgment is expected to be recognised and enforced in Mexico.

Alternative Dispute Resolution

Alternative Dispute Resolution ("ADR") is widely understood to be outside of court litigation and arbitration, but for the purposes of this article, ADR will include arbitration. This terminology is not devoid of practical implications, because it stresses the unavoidable need to opt in for arbitration and its contractual nature, underlining the legal reasons behind its flexibility as opposed to the above-mentioned formalities and rigidity of court proceedings. This is especially true when dealing with obstinate litigators that invoke general rules of civil procedure to delay, obstruct or reverse awards negative to their clients. Fortunately, courts in Mexico have sustained the arbitral awards and these attempts have proved unsuccessful, except for some delays.

Negotiation and Mediation

Freedom of will is the seminal rule in business transactions (Federal Civil Code ("FCC") articles 7 and 1796 and Article 78 of the Commerce Code). Thus, unless expressly prohibited by a law, parties may agree the terms and conditions that settle their disputes.

Negotiation is the preferred mode of dispute resolution in Mexico. However, the parties also resort to mediation through the intervention of a neutral third party who makes efforts to help them settle. Under Mexican law, the terms conciliation and mediation are synonymous.

The freedom of will permits the parties to agree to conciliate, to choose the applicable rules of the conciliation and to appoint the mediator or mediators of their choice. In Mexico, there are two main domestic institutions that perform commercial mediation, under their respective rules: the CANACO Mediation and Arbitration Commission and the Mexican Institute of Mediation. Also, international institutions such as the Commercial Arbitration and Mediation Center for the Americas ("CAMCA"), the International Chamber of Commerce Court of Arbitration ("ICC") and the International Centre for Dispute Resolution ("ICDR"), offer ADR services, and are frequently considered by the parties in their agreements.

Settlement agreements are regulated in the FCC as a nominated contract (*"Transacción"*; its translation to English "transaction" may lead to confusions and it is better to refer to them as "settlement agreements"). Settlement agreements, irrespective of being the result of a negotiation or conciliation, are *res judicata* and may be enforced by Mexican courts, if appropriately executed, through executory proceedings.

Arbitration

Finally, the parties may agree to arbitrate. Year after year, the number of arbitration agreements and arbitration proceedings grown substantially in Mexico – both in terms of national and international transactions. Mexico is party to the United Nations Convention for the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention or "NYC") (since 1975) and the Inter American Convention on International Commercial Arbitration (since 1976), and other less relevant international treaties. Regarding Investor-State disputes, Mexico is part of the NAFTA and other similar treaties and numerous bilateral investment treaties.

In July 1993, Mexico incorporated in the CC, practically verbatim, the UNCITRAL Model Law on International Commercial Arbitration (UMLA) (Book Five, Title Four (articles 1415 to 1463). A very important characteristic of the Mexican implementation of the UMLA is that it applies to both, international and domestic arbitration.

The CC provides for an expedited court proceeding to decide petitions for setting aside arbitral awards and for their recognition and enforcement (CC articles 1460 and 1463 and Federal Code of Civil Procedure, article 360).

The Mexican judiciary, in general, has observed a supporting attitude in the application of the arbitration law in general, and abstaining to interfere with arbitration proceedings. Special mention merits the positive attitude in the recognition and enforcement of both arbitral agreements and arbitral awards. There have not been reported cases of nullification of agreements to arbitrate or, with a few justified exceptions, setting aside or refusing enforcement of arbitral awards. In general, the view prevailing in the courts is that, when the dispute deals with private party interests, the courts do not revise the substance of the arbitral tribunal decision.

The leading arbitral institutions in Mexico are the Arbitration and Mediation Commission of the Mexico City CANACO ("CANACO"); and the Centro de Arbitraje de Mexico ("CAM"). CANACO has two sets of rules, for arbitration and conciliation, both modelled after the UNCITRAL Conciliation Rules and UNCITRAL Arbitration Rules. CAM has arbitration rules modelled after the ICC Arbitration Rules. CANACO is the Mexican Section of the Inter American Commission of International Commercial Arbitration, and the Mexican part of CAMCA. CANACO also provides services as appointing authority and administrative support to arbitrations agreed under the UNCITRAL Rules and other ad hoc arbitrations.

The ICC Arbitration Rules and the ICDR Rules are widely used; not only in international disputes, but in domestic ones also. To a lesser extent, CAMCA and IACAC Rules are also used.

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Arbitration Law in Mexico

BY ROMUALDO SEGOVIA | HAYNES AND BOONE, S.C.

This article intends to provide a basic overview of the law applicable to commercial arbitration in Mexico.

On July 22, 1993, Mexico adopted the Model Law on International Commercial Arbitration ("Model Law") of the United Nations Commission on International Trade Law ("UNCITRAL"), with a few modifications, by adding Title IV of Mexico's Commerce Code ("Commerce Code"). Mexico is also a party to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitration Awards (the "New York Convention") and the 1975 Inter-American Convention on International Commercial Arbitration (the "Panama Convention"), in both instances without any reserves.

The adoption of the Model Law by Mexico is the result of the recognition of its long use for international agreements and investments. Since then, arbitration as an alternative dispute resolution method has been fostered by clear and consistent judicial precedents and case law that recognise and enforce arbitration proceedings and

awards. As noted by the Mexican Congress in its initiative to reform Mexico's arbitration law, experience has shown that the enforcement of national and international arbitration awards has proven to be more effective than the enforcement of foreign judgments. In addition, the numerous judicial precedents and case law pertaining to arbitration proceedings serve as measure of the extent to which parties to national and international commercial agreements have adopted arbitration as an appropriate, effective and agile dispute resolution method.

As a civil law country, statutes are interpreted broadly by courts in Mexico, which are authorised and customarily recur to doctrine and treatises for interpretation and integration of the law. The explanatory note by the UNICTRAL Secretariat on the Model Law, therefore, serves as a basis for the interpretation by courts in Mexico of the arbitration law adopted in the Commerce Code. In addition, the UNCITRAL Secretariat established a system for collecting and disseminating information on arbitral awards relating to the Model Law, among other works of UNICTRAL, that promotes international awareness of the legal texts and facilitates uniform interpretation and application of those texts. This will no doubt diminish non-Mexican nationals' uncertainty about the applicability of arbitration law in Mexico, furthering even more the decision of parties to international agreements involving Mexican parties to arbitrate their commercial disputes. Also, the number of experienced lawyers participating in arbitration make Mexico a serious candidate as a place for arbitration.

In order for an arbitration agreement to be enforceable in Mexico, the Commerce Code and the New York Convention require the agreement to be in writing. Pursuant to the agreement, the parties submit all or certain disputes which have arisen or may arise between them in respect of a specified legal relationship, whether contractual or not. The agreement to arbitrate a dispute may form part of the contract, or be undertaken in a separate and independent document (note should be taken that certain disputes are not susceptible of being resolved through arbitration). Mexican courts have and will enforce an agreement to arbitrate, and further refer the parties to arbitration unless the court finds that the arbitration agreement is null and void, inoperative or incapable of being performed.

The arbitral tribunal may consist of one sole arbitrator or more as the parties agree. In the absence of such agreement, the arbitration tribunal is to consist of one sole arbitrator. When the arbitration tribunal is composed of more than one arbitrator, decisions are to be adopted by simple majority, provided that the president of the arbitral tribunal may decide by itself procedural matters if so authorised by the parties or the other members of the arbitral tribunal. Unless the parties have expressly authorised the arbitral tribunal to make its decision and award based on amicable composition or *ex aequo et bono,* the arbitral tribunal is required to render its award based on the body of substantive law elected by the parties or otherwise applicable as determined by it in the absence of such agreement.

Following the Model Law, Mexican arbitration law limits the involvement of competent courts in arbitration proceedings. Court involvement may be required in connection with: (i) the appointment, challenge, and termination or substitution of arbitrators, in cases where the parties have not agreed to specific rules to be applied to the arbitration agreement, or have failed to agree on such rules in non-administered or ad hoc arbitrations; (ii) decisions pertaining the jurisdiction or competence of the arbitral tribunal, provided that the arbitral tribunal is authorised to decide with respect to its own jurisdiction or competence *(kompetenze-komptenze)*; (iii) the assistance of competent courts in connection with any interim measures of protection that a party may seek, including the taking of evidence; and (iv) the setting aside or recognition and enforcement of the arbitral award. Aside from these matters, no court intervention is permitted by Mexican arbitration law. It is important

to note that the arbitration law of Mexico allows a court or the arbitral tribunal to grant any interim measures of protection it deems necessary in connection with the subject matter of the dispute. The court or the arbitral tribunal may require a bond to be placed as a condition for the granting of any such interim measures. Interim measures of protection may be requested from a court of competent jurisdiction at any time before or during the arbitration proceeding, including injunctive relief. Any cause of action brought directly before a court of competent jurisdiction challenging the arbitration clause, will not suspend, preclude or otherwise interfere with the arbitration proceeding.

The basic principle of underlying arbitration law in Mexico is the authority and freedom of the parties to select or tailor the procedure rules, and in the absence of such agreement, the authority of arbitral tribunal to conduct the arbitration proceeding as it deems appropriate. The arbitration is to be conducted pursuant to the agreement of the parties, which are allowed to incorporate by reference the rules elected or by designating the arbitration administration institution. Notwithstanding this authority, the parties are to be treated with equality and be given a full opportunity to present their case. This flexibility allows the parties to select or tailor the proceeding rules in accordance with their wishes or needs and the specific case, without regard to the rules that are otherwise applicable to judicial proceedings locally. It is worth noting that in addition to internationally recognised institutions that administer arbitration proceedings such as the International Centre for Dispute Resolution (ICDR), a division of the American Arbitration Association, and the International Chamber of Commerce (ICC), there are two organisations in charge of administering arbitrations in Mexico. The Mediation and Arbitration Commission of the National Chamber of Commerce of Mexico City *(Comisión de Mediación y Arbitraje de México)* and the Arbitration Centre of Mexico *(Centro de Arbitraje de México)*. The first institution has adopted rules modelled after the UNICTRAL arbitration rules, while the later, based on the ICC rules. In our view, an administered arbitration will provide certain advantages, particularly with respect to the establishment of the arbitral tribunal. Nothing in Mexican arbitration law prevents the parties from designating an international institution to administer the corresponding arbitration proceeding. The Commerce Code does not limit the ability of the parties to elect arbitrators irrespective of their nationality.

The parties are free to determine the place of the arbitration proceeding, and the arbitral tribunal is authorised to meet, hear the parties and other witnesses or to examine documents and other evidence, wherever the arbitral tribunal decides, whether in Mexico or abroad. The place of arbitration is important also as it will determine the competence or jurisdiction of courts when their intervention is required. Also, the parties have no restriction to agree on the language pursuant to which the arbitration proceeding will be conducted. When a language other than Spanish is elected, for the purposes of the enforcement of the award in Mexico, the award is required to be translated into the Spanish language by a court approved translator and approved by the court after the defendant has been given an opportunity to be heard with respect to the accuracy of the translation, and the enforcement proceeding would thereafter be based on the approved translation.

The arbitral award is required to be in writing and signed by arbitral tribunal. When the arbitral tribunal has more than one member, the signature of the majority will suffice, provided that the reasons for the lack of one or more signatures is stated in the award. Unless otherwise agreed by the parties, the arbitral tribunal is required to state the reasons for its award. In addition, the award must include the date and place where rendered. The award is final, conclusive and binding unless the parties have previously agreed to resort to an arbitral tribunal of second instance. A party seeking the award to be declared null and void is required to file its claim before a court

sitting where the arbitration took place, within a period of three months following the date of the notification of the award. The only and exclusive grounds pursuant to which an award may be annulled by a court of competent jurisdiction mirror those contained in the New York Convention.

Also and following the Model Law, the arbitration award may only be set aside or otherwise attacked by limited and exclusive grounds that essentially copy those contained in Article V of the New York Convention, and that deal with: (i) the lack of capacity of the parties or validity of the arbitration agreement pursuant to the laws elected by the parties; (ii) lack of notice of the appointment of arbitrators or the arbitration proceedings, or the inability of a party to present its case; (iii) the award deals with matters that are not part of the arbitration agreement or exceeds the terms thereof; (iv) the establishment of the arbitral tribunal or the arbitration proceeding were not made or conducted in accordance with the agreement of the parties, or in the absence of such agreement, pursuant to the laws of the place of the arbitration; or (v) if the award is not yet final and conclusive or has been set aside or annulled or suspended by a court sitting where the arbitration took place, or pursuant to the laws of which the arbitral award was rendered.

In addition, the award may be set aside to the extent that the subject matter of the dispute is not susceptible to resolution through arbitration pursuant to the applicable laws of Mexico, or the recognition and enforcement of the award would be contrary to public policy.

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Recommendations for Selecting an Arbitrator

BY CECILIA FLORES RUEDA | SANTAMARINA Y STETA

Since arbitration is a proceeding based on the will of the parties and since the rules to follow are flexible and may be adapted, the role of the arbitrator is essential to maintain the integrity, efficiency and effectiveness of the proceeding. This way, an essential element in the arbitration is the arbitrator, who will solve the dispute between the parties. It is even said that “arbitration is only as good as the arbitrators are”.

Unlike judicial proceedings, in arbitration the parties have the possibility to select who will decide the dispute. The parties are the ones who know better than anyone what the dispute is about, thus, depending on its characteristics, they may determine the intellectual and professional qualities and skills that the arbitrator must meet. Likewise, it should be kept in mind that to the extent that the parties are convinced of the arbitral tribunal and of the proceeding, they will be in a better disposition to accept the result of the arbitration and therefore, they will voluntarily comply with the award to be issued. That is why it is convenient that the parties make use of their right to participate in the composition of the arbitral tribunal.

The disputes solved in arbitration are very different in nature, as are the circumstances surrounding them, so there is no rule of thumb to determine the most appropriate qualities that an arbitrator must meet. However, besides the impartiality and independence that any arbitrator must show, the following aspects may be taken into

consideration:

- The arbitrator must have the knowledge and the experience necessary to solve the dispute raised to him by the parties, be familiar with the subject matter of the arbitration and have experience on the law and practice of the arbitration. For this reason, parties frequently select someone that they know professionally and in whose capacity they trust. This is subject to them being, and remaining, impartial to and independent from the parties.
- There is no demand on the legal capacity of the arbitrator, even though in practice, attorneys are preferred as arbitrators. That is due to the fact that sometimes the merits of the lawsuit requires solving legal matters such as the applicable law, the place of the arbitration, the interpretation of applicable clauses, and the rights and obligations of the parties.
- In domestic arbitrations it is convenient to designate an arbitrator of the same nationality as the parties, making them closely related to the parties in terms of culture, ways of analysing litigious matters and understanding the idiosyncrasy of the parties. In the case of international arbitrations, if the tribunal is to be composed of one arbitrator, it is common that the arbitrator has a nationality other than that of the parties. If the tribunal is to be integrated by three arbitrators, the most convenient is that each party appoints an arbitrator of its same nationality and that the third one be of a different nationality. The reason for this is that the parties would be safer if at the arbitral tribunal there is a person keeping a certain affinity with their legal tradition. Likewise, the reason for a third party to have a different nationality is in the interest in keeping a balance between the parties. Article 1427 of the Mexican Code of Commerce provides that, except for agreement otherwise of the parties, the nationality of a person will not be an obstacle for him acting as arbitrator. Article 6.4 of the UNCITRAL Arbitration Rules and article 8.3 of the CANACO Arbitration Rules do not require that the sole arbitrator or the president of the arbitral tribunal be of a nationality other than the one of the parties, however, it provides for that upon making the appointment, the appointing authority will take into account the convenience of appointing an arbitration of a nationality other than the ones of the parties. Likewise, article 9.5 of the ICC Arbitration Rules provides that the sole arbitrator or the president of the arbitral tribunal may have a nationality other than that of the parties, notwithstanding, in adequate circumstances and provided that none of the parties oppose it, such arbitrator may belong to the country of which one of the parties is national. Article 6.4 of the International Arbitration Rules of the ICDR provides that at the request of any party or on its own initiative, the administrator may appoint nationals of a country other than that of any of the parties.
- The arbitrator may have a sufficient command of the language of the arbitration, since that guaranties understanding between the arbitrator and the parties. Otherwise, it will be necessary to resort to an interpreter, which will necessarily complicate, increase the price of and delay the proceeding.
- The arbitrator accepting the position must be willing to give priority to said task to conclude it in accordance with the reasonable expectations of the parties. Likewise, the arbitrator must know how to listen to the parties and have the time to conduct the arbitration directly and not through assistants.
- Besides the aforementioned qualities, the arbitrators must: (i) be secure, stand firm to exercise control of the proceeding and be flexible and polite at the same time; (ii) have the creativity necessary to adopt the most convenient resolutions depending on the circumstances of the claim; (iii) think logically and have the capacity to reason; (iv) have a good physical and mental condition; and (v) have high standards of probity, honesty and moral integrity.

Due to the important role performed by the president arbitrator in conducting the proceeding, it is required that he has additional qualities such as: (i) leadership; (ii) strength and determination; and (iii) organisation and skills to divide the work and assign responsibilities.

The above mentioned aspects are kind of universal; however, there may be other aspects that should be taken into consideration depending on the circumstances surrounding the parties and the dispute.

To select the arbitrator, it may be useful: (i) to review his resume to know the studies that he has made, his professional career and experience; (ii) to request references from other colleagues; (iii) to review his publications to know his expression capacity and his knowledge on the matter; and (iv) perhaps briefly interview the candidate to know him in person, not discussing the merits of the controversy and without such candidate expressing any opinion on the matter; the interview must be limited to learn about his qualities to act as arbitrator, possible conflicts of interest and his availability.

It is difficult to anticipate the controversies that may arise between the parties. For this reason, among others, it is not advisable that the parties agree from the arbitration clause the person who may act as arbitrators when any controversy surfaces. Likewise, it is not advisable to impose requirements to be complied with by the persons who will act as arbitrators, since in practice this may turn out to be a problem.

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Increase in Disputes due to Economic Conditions

BY MARCO TULIO VENEGAS | VON WOBESER & SIERRA, SC

In 2008 and 2009 the world experienced an unprecedented economic crisis which started in the United States of America and expanded to the rest of the world including Mexico, which was the Latin American country that saw the greatest negative impact on its economy.

The recession, which crossed borders and is still being felt in some economies, brought several consequences, among which was an immediate increase in the breach of commercial, civil and labour agreements.

The recession also caused an increase in the value of the dollar against the Mexican peso, preventing many merchants from fulfilling their payment obligations, especially in matters regarding the payment of credit cards, mortgages, promissory notes, leases and bonds, among others (*Excelsior* Newspaper, "[Commercial disputes doubled in Distrito Federal] *Se duplicaron juicios mercantiles en D.F.*", published on December 14, 2009).

Mexico is a federal state and therefore its court system is divided into federal and local courts. The local courts, under the Superior Court of Justice of each state, act as courts of first instance, and are the first ones to hear a dispute and the first ones to issue a decision on the matter.

In this article we will take Mexico City as a sample of the increase in the number of disputes in the local courts of Mexico which has resulted from the current economic conditions.

Each year the Superior Court of Mexico City releases a statistical report concerning several aspects of the

justice system, including the increase in the number of courts, the number of lawsuits filed in the year, the budget expended and the budget required to continue working over the next year, among other information.

For 2008 the report showed an increase of 3.9% of the total admitted cases per 100,000 inhabitants of the city. Such increase reflects an increase of 48,917 lawsuits with respect to 2007 (Superior Court of Justice of Mexico City, [Statistic Summary] *Compendio Estadístico 2004-2008,* March 2009, page 35).

The economic conditions of such year brought with it an unprecedented increase of 20.8% in the number of court proceedings (*Idem*, page 56).

This increase affected many areas of the Justice System of Mexico City including the criminal area, the area responsible for resolving family disputes, the leasing disputes area, and the commercial and civil areas. However, it was in these last two areas where the bigger increase of proceedings was recorded.

By the end of 2008, each of the Civil Courts had 1,400 lawsuits to solve. At the beginning of 2009 the Superior Court of Justice was still receiving more new proceedings than it could resolve. In January the number of lawsuits in courts of first instance was 1,664, which was 30% higher than the number recorded in January 2008 (Superior Court of Justice of Mexico City, [Statistic Summary] *Estadistica Judicial,* September 2009, page 7), and the expected figure for the end of 2009 was 2,000 proceedings per court. Mr. Edgar Elías Azar, president of the Superior Court of Justice of Mexico City stated that these figures were alarming, since the amount of cases considered appropriate per court is 1,000.

In Mexico – having a civil law system – all civil and commercial proceedings are carried out in written form, each phase and action of the court requiring a ruling by the judge. Therefore, the increase in the number of cases also resulted in an inability of the courts to resolve cases in a timely manner, causing a serious delay in the delivery of justice.

The Labor Courts of Mexico City were also affected by the economic conditions of 2008. By the end of such year the number of ongoing cases was 21,864, when in December 2007 the report of the Labor Court showed a total of 12,406, meaning that labour proceedings increased by more than 50% during 2008. By September of 2009 the number was 22,379, suggesting that labour suits resulting from the economic conditions are not decreasing yet.

The lawsuits filed in the Labor Courts of Mexico City for dismissals have increased by 73% since the beginning of the economical crisis (El Universal Newspaper, "[Crisis boosted suits for layoffs before the labour courts] *Crisis disparó juicios por despido ante JLCA*", published on October 23, 2009).

It is important to consider that the problem caused by the increase of legal proceedings is amplified by the lack of government budget to face it. The president of the Superior Court of Justice of Mexico City has expressed his concern regarding this matter, stating that if the percentage of the budget dedicated to the administration of justice does not increase proportionally to the number of cases it could generate a crisis in the judicial system of the city.

However, there has been one resource which has helped with the situation faced by the Superior Court for the past two years. Such resource is the Alternative Center for Justice *(Centro de Justicia Alternativa)*, created a few years ago by the Superior Court of Justice of Mexico City, the purpose of which was to resolve family issues through mediation, which is an alternative mean of dispute resolution that involves a third party who only facilitates the dialogue, the communication and the understanding between the parties.

In these last few years the Center has also helped resolve commercial and civil disputes, and thus this Center has brought a little relief to the courts' overload of work.

The Superior Court has started to give more publicity to the Center since the beginning of the economic crisis. This Center could represent a way to decrease the number of new lawsuits and the increase in ongoing cases.

In addition to the Alternative Center for Justice, during 2008 the Civil Procedure Code of Mexico City was amended to allow civil and commercial disputes for less than $212,000 pesos to be resolved in an oral trial, reducing the processing time and the load of work in the Courts. This amendment will apply, in cases such as lawsuits for credit card collection between banks and cardholders, and for leases, mortgages and car loan disputes, among others (El Universal Newspaper, "[Oral civil trials start] *Arranca oralidad en juicios Civiles*", published on September 10, 2009).

Hopefully, the Alternative Center for Justice and the amendments will help the Superior Court of Justice of Distrito Federal cope with the tremendous work increase registered in the last year and a half. While judicial reforms are being promoted by Mexico's Presidency to make the justice administration system a more agile and efficient one, the lack of budget complexity over the whole country, will still constitute a heavy burden for the local courts.

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Fact-Gathering and Background Information

BY DIEGO SIERRA | VON WOBESER & SIERRA, SC

The gathering of information in Mexico represents a very crucial part of the preparation for a legal action. At the time the lawsuit is filed, it must contain all the proof and evidence that the plaintiff would like to be taken into consideration by the Judge, including the names and addresses of any witnesses and the defendant must do the same when answering the lawsuit.

Gathering Information

When gathering information there are several scenarios which need to be analysed, such as how to obtain governmental information or documents that are in the possession of the counterparty; which evidence is allowed in court and which is prohibited; and which evidence is more valuable, among others. All these subjects will be analysed in this article, highlighting the more important aspects of each one.

When a lawsuit is being prepared it is very important to analyse the legal requirements for the type of proceeding to be pursued. For example, when the legal action is based on a document ready for execution (such as a promissory note or an acknowledgement of debt granted before a notary public), the Commerce Code requires that the claimant present its claim accompanied by the document to be executed (Commerce Code, article 1061). In this case when gathering the evidence, this should be the first document to obtain.

In certain special cases there are some measures that might be taken in preparation for a lawsuit and that

can help obtain an executive action against the debtor:

- To prepare an executive action, the debtor can be requested to testify under oath before a judge. If duly served, the debtor fails to testify, the judge will declare that the alleged debt is valid and will order the seizure of property.
- If a private document contains an immediately due and payable debt, the exhibition of such document to the judge will allow the creditor to initiate preparatory measures.

The requesting party must prove to the judge that the document contains a certain, liquidated, and payable debt as well as the origin of the debt.

Thereafter, the judge will order the document to be presented to the debtor requesting him to, under oath, recognise the signature on the document, the origin of the debt and its amount. The serving must be conducted with the legal representative of the debtor if it were a corporation and not an individual. If the debtor is asked twice to recognise under oath the signature and it omits any pronunciation in that respect, the document's signature will be considered as recognised.

When served, the debtor may recognise the signature but not the amount of the debt or its origin. If that is the case, the debtor will be granted a five day term to exhibit evidence which proves his declarations. When no such evidence is filed, the judge will declare the debt to be conclusive and the document will become constitutive of an executive action.

Furthermore, if the debtor does not recognise the signature as its own, the creditor will have the option to file a criminal accusation against it for declaring falsely under oath.

Governmental Information

In Mexico there is a special law regarding access to public information which allows any person to request any public information, including salaries of public officials, companies which have entered into agreements with the government and the amounts of such agreements, etc. Also, there are civil and commercial public registries which provide information on companies and information regarding real estate properties.

If the government was unable to provide such information by the time the lawsuit has to be filed, the plaintiff can show as evidence the request for information and request the judge to order the presentation of said information during the trial once it is available.

Privileged Information

As a general rule, in Mexico all documents are privileged, that is, there is no obligation to show them to the other party. This includes documents written by an in-house lawyer.

Moreover, the Mexican Federal Criminal Code regulates professional privilege, in which people who render professional or technical services or public employees are obliged to keep professional secrets or communications. If they reveal such information without the consent of the private party who is its proprietary or if harm is caused to its employees or clients they could be eligible for a sanction of a prison term of between one and five years and professional disqualification for as long as a year (Federal Criminal Code, article 211). An exception to this obligation to keep professional secrets would be a just cause – such as a judicial order.

The Financial Institutions Law establishes the confidential status of all the deposits, operations or services of the Financial Institutions' clients and users in order to protect their privacy right. As an exception the law requires these Institutions to provide such information when requested by a judicial authority for a court procedure where the owner, trust beneficiary, trustor, fiduciary, principal or agent is a party or is the accused (Financial Institutions Law, article 117).

Documents in Possession of Another Party

Even though Mexican legislation, specifically the Commerce Code, does not establish an obligation to disclose documents in the possession of any of the parties in the sense of having a discovery figure, the disclosure of documents may be obtained if precise documents which the counterparty is obliged to keep, are requested from it.

The Commerce Code states that merchants have the obligation to keep an accounting system with certain minimal requirements that: (i) will allow it to identify its individual operations; (ii) will permit to trace its individual operations to its accumulations; (iii) that will allow to prepare financial statements; (iv) that allow to do a connection between the ciphers of those statements and the accumulations and the individual operations; (v) and that will include control systems to verify the certainty and accuracy of the previous requirements (Commerce Code, article 33). Apart from the accounting system, the merchant – such as any commercial corporation – will be obliged to keep a file with all the original documents that support its operations in such a way that they may be related to their accounting registries. The obligation to keep such documentation will remain for a ten year period.

Regarding the production of evidence, the opposing party or the judge can request the production of minutes and documents which are the property of merchants when the owner has a special interest or responsibility in the matter which is being discussed (such as in cases in which the liability of an administrator of a corporation is in question) (Commerce Code, article 44). The identification of such documents will be carried out in the place where the documents are kept and under the supervision of the merchant, and will cover only the matters that are specifically under discussion.

Moreover, in June of 2008 Mexico's highest courts issued a binding precedent – jurisprudencia – that allows a judge to issue an order of production of documents with a prevention of having the offering party's affirmations in connection with those documents as conclusive (the identification data of such precedent in Spanish is the following: *"Registro No. 169509; Localización: Novena Época; Instancia: Tribunales Colegiados de Circuito; Fuente: Semanario Judicial de la Federación y su Gaceta; XXVII, Junio de 2008; Página: 1098; Tesis: I.4o.C. J/28; Jurisprudencia; Materia(s): Civil."*). Thus, if the party obliged through the judicial order to present certain documents of its property which it is obliged to keep, omits to present such documents with the judge, its counterparty's declarations of the content or evidence reflected on such documents will be accepted by the court as certain and true.

The referred precedent will certainly have a great impact on the development of future commercial disputes in Mexico because even though a traditional common law discovery is not allowed, the effects of this precedent may allow parties involved in litigation to achieve the production of documents from their counterparties by pressing them with the risk of having the requesting party's declarations regarding such documents, as true and conclusive if the proprietary of the documents should omit producing them in court.

Foreign Documents

When documents stored overseas, electronically or otherwise, need to be brought into jurisdiction for the purpose of litigation, the Mexican Judge can ask the foreign Judge through an exhortation to send such documents to be produced in litigation. Such request must be made by the plaintiff in its lawsuit.

The judge has the prerogative to ask for any element or document, even if they are stored electronically to find the truth regarding doubtful and controversial facts, including documents held by a third party, subsidiary or parent companies or any other person or company.

Probative Value

Not all evidence has the same value before a Mexican court. The law as well as court precedents and practice determine their value.

For example, the value of an agreement executed before a notary public or a fact which a notary attests to have seen are considered conclusive evidence. However, testimonial evidence could be very useful to persuade a judge or could not be taken into consideration at all.

In conclusion, fact gathering in Mexico requires ability and creativity from the leading counsel. If full knowledge of the procedural rules, and the judicial precedents that have interpreted them, are taken into account by the litigation attorney, he will most likely be enabled to get access to sufficient information to give support to its claim or defence in court.

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Product Liability Claims

BY CLAUS VON WOBESER | VON WOBESER & SIERRA, SC

In this article two alternative procedures for resolving product liability claims in Mexico will be addressed, from the perspective of jurisdiction and competence of the Mexican courts in this matter. Also, the rules establishing when a person can submit to such jurisdiction will be analysed and the Federal Labor Law's relevance in this matter will be explained.

Product liability claims can be related to any kind of products, from food to toys to cleaning products or even to work machinery. In Mexico there is a special Agency called the Consumer Protection Agency whose function is to monitor the effectiveness and functionality of different products available to consumers and to resolve consumer complaints regarding these matters.

In fact, this Agency is the only one recognised by the Federal Law for Consumer Protection as competent to exercise class actions in representation of consumers before the courts (Federal Law for Consumer Protection, article 26).

However, when a consumer suffers a tort, damage or loss because of the use or consumption of a product, it

is empowered to: (i) pursue arbitration in accordance with the Federal Law for Consumer Protection; or (ii) go before a Mexican Court with jurisdiction over the matter to pursue a monetary indemnification through a civil liability lawsuit.

In the first option when a consumer has been harmed by the use of a product it may resolve the dispute through arbitration in two ways:

- The parties can choose to have the Federal Consumer Protection Agency *(Procuraduría Federal del Consumidor)* act as arbitrator (Federal Law for Consumer Protection, article 117). In this case the award will be considered as an act of an authority and therefore it may be appealed through an amparo proceeding. This first option has the advantage of reducing the cost by paying a lower fee than with an independent arbitrator; however, the procedure will be more similar to an administrative proceeding than to an arbitral one, because it would be led by an administrative organism;
- The parties can choose an independent arbitrator to resolve the dispute (Federal Law for Consumer Protection, article 118). A procedure for the recognition and enforcement of the arbitral award will be necessary in order to enforce it. This process may be more expensive depending on the fees of the arbitrator.

In both cases the parties can choose whether to resolve the arbitration according to strict rules of law, by establishing the procedural rules, or to resolve it as an *amiable compositeur,* by leaving the decision to the arbitrator's conscience and to good faith, always observing the essential formalities of the proceeding.

Another option to be considered is to go before a Mexican Court with jurisdiction over the matter to pursue a monetary indemnification through a civil liability lawsuit.

Jurisdiction is the State's sovereign power to decide legal disputes by means of final binding and enforceable judgments rendered by duly appointed courts. Such jurisdiction is divided among different courts. Such division limits the jurisdiction of each court and therefore establishes its competence considering the following four different factors:

- Territory: The competence of the court to exercise its jurisdiction is limited to a specific geographic area determined by law, e.g., Mexico City.
- Substantive applicable law: The court can only exercise its jurisdiction in a specific area of substantive law, such as Civil law, Commercial law, Labor law and Criminal law, among others.
- Amount: There are Mexican courts whose jurisdiction is limited according to the amount in dispute.
- Instance: The court can exercise its jurisdiction in first instance, as court of origin, or in second instance, as court of appeals to review the decisions made by a lower court.

The territorial competence of Mexican courts in relation to product liability claims through a civil lawsuit is not so easy to determine in some cases. The affected consumer, the producer of the product and the place where the damage was caused are not always in the same place. Sometimes they are even in different countries.

According to Mexico's Constitution and Federal and Local Statutes the territorial competence of the Mexican courts can be established by way of express or tacit submission.

The aforementioned means that the affected consumer can choose one of the competent courts by territory to conduct the legal action and such choice can be made expressly or tacitly.

The Federal Civil Procedure Code (applicable in procedural matters to the Federal Law of Consumer Protection) establishes that tacit submission will take place when the plaintiff files a lawsuit before the court and the defendant files a response or counterclaim in such court without filing a motion for lack of competence (Federal Civil Procedure Code, article 23).

It is important to mention that a Court located in a State which has a point of contact with the dispute will not be able to dismiss a lawsuit. This means that if the defendant is not domiciled in the specific geographic area of the Court, the proceeding will have to wait until the defendant submits tacitly to the Court's jurisdiction or challenges it.

In a product liability claim there could be many points of contact that would establish the competence of a certain Court, such as the plaintiff's domicile, the defendant's domicile, the area where the product was sold or made, among others, and by filing the complaint before any of the Courts located in those areas, the plaintiff will tacitly submit to its jurisdiction.

It is also possible to extend the territorial competence of a Court by way of express submission. The ability to establish the territorial competence of a court by express submission is not only set out by statute (Federal Civil Procedure Code, article 23), but has also been the rule and practice followed by Mexican courts. Its highest courts have determined in several binding precedents that the competence by territory of a Court is extendable by express submission.

The parties are entitled to expressly agree in the lawsuit to submit their legal dispute to the Mexican courts; in fact, these submissions are very common and often serve as the basis for the Mexican Courts to assume jurisdiction over cases.

It is important to bear in mind that the statute of limitations to claim the damages or losses derived from product liability is two years from the date on which the tort occurred.

The importance of the Federal Labor Law in product liability claims is based on the reference made to such law in the Federal Civil Code. Such Code establishes that any person who has suffered a permanent or temporary disability, whether total or partial, may request an indemnification from the person responsible in accordance with the provisions of the Federal Labor Law (Federal Civil Code, article 1915).

Thus, it is important to bear in mind that the Federal Labor Law is relevant to product liability claims because it establishes limitations to the amounts which can be sued by a consumer to the alleged responsible when the product caused such person's death, total or partial permanent disability or total or partial temporary disability.

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BRAZIL

Recognition of Foreign Arbitral Awards in Brazil

BY FABIANA VIDEIRA LOPES | SIQUEIRA CASTRO ADVOGADOS

To be enforced in Brazil, foreign arbitral awards must first be recognised by the Superior Tribunal of Justice (the highest court for non-constitutional matters), according to Article 105, II, "i", of the Federal Constitution and Article 35 of Law 9307/96. Before the enactment of Constitutional Amendment 45 in December 2004, the Federal Supreme Court had original jurisdiction on recognition of foreign judicial and arbitral decisions.

Law 9307 (the Arbitration Law), enacted in 1996, had its constitutionality challenged but was finally found constitutional in a Supreme Court decision in 2004. This greatly encourage the inclusion of arbitration clauses in contracts.

Although Brazil signed the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention, internationally in force as of June 7, 1959), it was only included in Brazilian law upon the publication of the Decree 4311 on July 23, 2002. The convention is in line with the Brazilian Constitution and the Civil Procedure Code, which require previous recognition of the foreign judgments.

In deciding on whether or not to recognise a foreign arbitral award, the Superior Tribunal of Justice (STJ) does not analyse its merit. It only examines the formal requirements specified in the Arbitration Law (Article 38 and 39), the New York Convention (Articles IV and V) and STJ Resolution 9 of May 4, 2005. This resolution provides the internal rules on the recognition procedure.

Since jurisdiction over recognition of foreign judgments was transferred to the STJ, that court has confirmed on a number of occasions that it is impossible to reopen discussion of the merits of the dispute. The summary below is emblematic in this respect:

"RECOGNITION OF FOREIGN ARBITRAL AWARD. SECURITY PLEDGE. UNNECESSARY. LAW 9307/96. IMMEDIATE APPLICATION. UTILIZATION OF ARBITRATION TO RESOLVE DISPUTES. NO VIOLATION OF PUBLIC POLICY. IMPOSSIBILITY OF EXAMINING THE MERIT OF THE MATERIAL LEGAL RELATIONSHIP. NO OFFENSE TO THE RIGHT OF REBUTTAL AND AMPLE DEFENSE. RULE OF *EXCEPTIO NON ADIMPLETI CONTRACTUS*. *SETTING OF ATTORNEY'S FEES*. *ART. 20,* § 4, OF THE CIVIL PROCEDURE CODE. REQUEST FOR RECOGNITION GRANTED. I – It is not required to post a security pledge to request recognition of a foreign award. Precedents from the Federal Supreme Court. II – The arbitral award and its recognition are governed in Brazil by Law 9307/96, and that law has immediate and constitutional application, as already decided by the Federal Supreme Court. III – According to the position of this Tribunal, the use of arbitration to resolve disputes does not violate public policy. IV – The judicial control of recognizing foreign arbitral awards is limited to the aspects set forth in Articles 38 and 39 of Law 9307/96, and there may be no analysis of the merit of the material

right involved in the award in question. Precedents. V – There is no offense to the right of rebuttal and ample defense if the respondents freely entered into the contracts that contained an express arbitration clause and were fully aware of the arbitral proceeding, with presentation of preliminary considerations and defense. VI – The Special Court of this Tribunal has already ruled that the question of the rule on *exceptio non adimpleti contractus is not a matter of public policy and is not connected to the concept of national sovereignty*. Moreover, this matter specifically refers to the merit of the foreign award, something that may not be analyzed by the present route. VII – The decision to recognize a foreign award must be based only on analysis of its formal requirements. This means the subject matter at issue in an action for recognition of a foreign award is divorced from that in the proceeding that produced the foreign decision and has no economic content. It is the enforcement proceeding, to be commenced after obtaining the certified copy of judgment, that an economic issue may be involved. VIII – In the great majority of proceedings for recognition of foreign decisions – more specifically those involving arbitral awards – the value attributed to the cause corresponds to the economic content of the arbitral award, generally a large sum. Therefore, when the recognition is contested, the possible setting of attorney's fees at a percentage of this value can be exaggerated. IX – In cases of contested foreign decisions, since there is no judgment on the merit, the setting of attorney's fees must occur pursuant to Art. 20, § 4, of the Civil Procedure Code, also observing the lettered items of § 3 of that article. However, according to the position of this Court, the judge is not restricted to the percentage range [from 10% to 20% of the value of the award] set in the referred § 3. X- Request for recognition granted." (Contested Foreign Decision 560/EX – Reporting Judge Gilson Dipp – Special Court of the Superior Tribunal of Justice – judged on October 18, 2006; cases in higher courts in Brazil are heard by panels or chambers of judges, and the case is first assigned to one of them acting as the relator, or reporting judge. This judge's job is to analyse the case in detail, summarise it for the other judges and write a leading opinion, which may or may not prevail).

According to the New York Convention (Article IV), for a foreign arbitral award to be recognised and enforced, the requesting party must present the duly authenticated original award or a duly certified copy thereof and the original agreement of the parties to submit the dispute to arbitration. These provisions are reproduced in Law 9307/96 (Article 37, I and II). Any documents in a foreign language must be accompanied by a sworn translation into Portuguese.

In turn, Article V of the New York Convention establishes that recognition and enforcement of an arbitral award may be refused if it is proved that: (i) the agreement containing the arbitration clause is not valid; or (ii) the party against whom the award is invoked 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 (ii) the award deals with a difference not contemplated or not falling within the terms of submission to arbitration or it contains decisions on matters beyond the scope of the submission; or (iv) the composition of the arbitral authority or the procedure is not in accordance with the agreement of the parties or the law of the country where the arbitration took place; or (v) the award has not yet become binding on the parties or has been set aside or suspended by a competent authority of the country under whose law the award was made; or (vi) according to the law of the country where recognition is sought, the subject matter of the dispute is not subject to solution by arbitration; or (vii) the recognition or enforcement of the award would be contrary to public policy of that country. These situations are also set forth, in Articles 38 and 39 of Law 9307/96.

In summary, as long as the above requirements are satisfied and there is no offense to national sovereignty, good

customs and public policy, the winner of a foreign arbitration can rest assured that the award will be recognised in Brazil, allowing its enforcement. The party seeking recognition must only follow the procedural rules set by the STJ in its Resolution 9, among them service of notice on the losing party to the arbitration, allowing a chance to contest the case. If recognition is contested, the only arguments that can be pressed regard whether the above requirements have been met. The case will be sent to the Special Court of the Superior Tribunal of Justice, which will request a legal opinion from the Federal Prosecutor's Office and then decide on whether the formalities have been satisfied.

It must be acknowledged, however, that contestation will slow the case down. The STJ has been doing its best to decide quickly in recognition cases. Analysis of its website shows that when recognition is contested, it takes an average of sixteen months to reach a decision, while for uncontested cases the average is six months. By the standards of the Brazilian court system, these intervals are very fast. Combined with the fact that the arbitration proceeding itself is almost always much faster than a court case, and that obtaining a court award still requires an enforcement phase where various motions and dilatory manoeuvres are possible, arbitration has substantial advantages on speed alone. This is without mentioning the greater privacy and better expertise on the questions in dispute in an arbitral proceeding.

Another relevant point is the attorney's fees set in contested recognition proceedings. There should be an adverse cost award of some type, because the contestation slows the case down and requires added effort by counsel for the prevailing party. However, since the amounts involved in arbitral awards are generally high, the Superior Tribunal of Justice has been acting prudently in setting legal fees, taking as a basis the parameters of Article 20, § 4, of the Civil Procedure Code rather than its § 3 (which calls for 10 to 20% of the amount of the award). These parameters allow the court wide discretion in setting adverse costs at what is deemed a fair amount, considering the nature and importance of the case and the effort involved.

Since it assumed authority to recognise foreign awards, STJ shows in its website twenty-two decisions on contested requests for recognition of foreign arbitral awards. Of these, seven were denied, three for absence of a signature on the arbitration clause or submission agreement, two because the petitioner had not participated in the arbitral proceeding, causing loss of legitimacy, and two for absence of summoning of the opposing party in the recognition proceeding (which as stated is an essential requirement). In this last case, the petitioner can file for recognition again in order to properly serve notice (article 40 of Law 9307/96).

Finally, there is the question of actual enforcement of the award once it is recognised. A recognised award has the status of an enforceable judicial instrument (the same as a domestic judicial award). This makes the proceeding fairly straightforward and assured. According to Article 109, X, of the Brazilian Constitution, the competent federal court has jurisdiction to enforce a recognised foreign arbitral award. In this phase, the parties must follow the rules established by the Brazilian Civil Procedure Code. If the claimant seeks to receive an amount of money, the debtor will have fifteen days to pay the amount due or a 10% fine will be applicable. On the other hand, if the award involves a positive or negative covenant, then the judge can establish a term for compliance with the obligation. In both cases, if the defendant does not present a defence (the very few defence possibilities are established in Article 475-L of the Civil Procedure Code), then this phase can take less then four months. If the defendant does present a defence, the case can theoretically drag on for one year.

Therefore, it can be concluded that as long as the rules of the New York Convention (internalised by Decree 4,311/2002), the Brazilian Arbitration Law and STJ Resolution 9 are satisfied, the winning party can be sure that the

foreign arbitral award will be recognised in Brazil, and that the enforcement proceeding will be straightforward. In comparison to resorting purely to the judiciary to resolve disputes, arbitration is much quicker, even considering the need to recognise and enforce the award, not to mention the advantages of greater privacy and expertise. This fact is reflected by the growing trend of choosing arbitration to resolve disputes in international agreements involving Brazilian parties.

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The 45th Amendment in the Federal Brazilian Constitution and its Effects on the Brazilian Judiciary System

BY ANTONIO URBINO PENNA JR. AND GLEDSON MARQUES DE CAMPOS | TRENCH, ROSSI E WATANABE

Conflicts are inevitable where people interact with one another. There was a time when rich, powerful and influential parties involved would lord it over the weak ones to resolve any number of conflicts.

Such method to resolve conflicts lasted until the State established certain conditions (legitimation) to promulgate laws regulating human conduct and behaviour as well as to grant their enforcement whenever such laws were infringed, regardless of the intention of the parties.

As of the moment, the great majority of the States have established a "monopoly" of resolving conflicts and named the relevant function "jurisdiction". Therefore, "jurisdiction", i.e., the function of laying down the law, is fundamentally the State's activity whereby, replacing the involved parties, the State presents a solution to a conflict in order to ensure that people live and work in relative peace and in an organised society.

In Brazil, a Civil Law country and where legal tradition dates back to the time of old Portuguese *Ordenações* (Ordinances) *Afonsinas, Manoelinas e Filipinas* enacted by Kings Afonso, Manoel and Felipe during the 15th and 16th centuries, its judiciary system has undergone transformation since Brazil gained its independence in 1822. Unfortunately, however, such transformation has not produced the desired results mainly in relation to the Judiciary's capability to quickly resolve conflicts and to decide cases submitted to it, thus resulting in a crisis. In 2004, our Federal Constitution was changed by virtue of the 45th Amendment (also called the *Judiciary Reform*) to modify relevant articles related to the Judiciary.

This article will analyse the relevant amendment and its major effects, mainly in relation to an attempt to simplify judicial proceedings hoping to grant parties involved what is legally due them and to turn the wheels of justice at speed.

The 45th Amendment and its Effects

The 45th Amendment was promulgated on December 8, 2004. Its purpose was to modify the Judiciary in order to ensure that legal cases and lawsuits will be resolved swiftly and justly.

Apart from that, as a result of the pressure of public opinion, the Amendment has created a superior council

to monitor the administrative conduct of the Courts officers. The relevant modification was introduced with the amendment of the Brazilian Federal Constitution as the jurists were unanimous in defending the argument that a simple modification in the federal laws would not produce the required results.

Among the modifications introduced in the structure of the judiciary in order to guarantee the celerity involving "consumers of the judiciary services", the 45th Amendment has had immense impact on procedural civil law, such as: (i) reasonable time limit for proceedings; (ii) extension of the jurisdiction of labour courts; (iii) jurisdiction for the homologation of a foreign sentence and/or international award; (iv) appeals to the Supreme Court on constitutional matters; and (v) binding precedents (certiorari).

As a consequence of such changes in the years that followed the enactment of the 45th Amendment, several laws *(statutes)* were approved by the Brazilian Congress which necessitated relevant modifications to the Brazilian procedural law.

Principle of Reasonable Time Limit for Proceedings

The most important modification of the 45th Amendment is the insertion in Article 5 of the Brazilian Federal Constitution which governs the individual and collective rights and duties. Paragraph LXXVIII provides that "to all parties, in both judicial and administrative proceedings, a reasonable term of duration of proceedings and the means to guarantee the celerity of proceedings are assured."

Even before the 45th Amendment was introduced, there was a general understanding/principle that legal proceedings might be able to provide parties involved with the best solution in the quickest time possible or at least within a reasonable time. It is unacceptable to "impose" on the parties the need to wait for 10 or 15 years for a final decision. Likewise, simply granting the parties the right to submit claims to the Judiciary is not enough. It is also important to assure the parties that they will have the best solution in the quickest time possible.

The debate that we are facing nowadays is the meaning of the expression "reasonable time for a decision". Although there are some boundaries, it is not easy to define "reasonable time". The European Court of Human Rights, for example, states three criteria in order to establish a reasonable time for a decision, to wit: (i) the complexity of the matter involved in the claim; (ii) the behaviour of the parties and their attorneys; and (iii) the performance of the Judiciary. Therefore, in order to verify whether or not the extension period of any proceeding would be "reasonable", the compliance with all these criteria must be analysed. If all these criteria were observed, the duration would be deemed "reasonable".

Despite the difficulty in determining what the expression "reasonable duration" means, it is expected that the Judiciary, without prejudice to the observance of the due process of law: (i) is prepared to render a decision as soon as possible; and (ii) does not tolerate any judge keeping court records for months in order to render a decision or a sentence.

Extension of the Jurisdiction of the Labour Courts

The 45th Amendment has extended the jurisdiction of labour courts. Generally, under the relevant Amendment, the jurisdiction of labour courts was limited to analyse and decide conflicts involving employees and employers. Since the Amendment took effect, the labour courts' jurisdiction has no longer been conditioned upon the existence of a relationship involving employees and employers. Currently, the existence of a single labour link is enough to deprive, for example, the civil and commercial courts of adjudicating the conflict described by the claimant.

Jurisdiction for the Homologation of a Foreign Sentence and/or International Award

Since Brazil has become an independent country, the Supreme Court on Constitutional Matters has exercised jurisdiction to homologate foreign sentences and, depending on certain strict requirements, international awards (i.e., those rendered by arbitration panels located outside Brazilian territory).

However, the 45th Amendment has modified such jurisdiction, removing it from the Supreme Court on Constitutional Matters and establishing that the Superior Court will have jurisdiction to verify if foreign sentences and international awards comply with the requirements set forth under the Law in order to allow their enforcement in Brazil.

Except for the modification in the jurisdiction, the Amendment did not change (i.e., add or remove) any of the requirements of the homologation of foreign sentences and international awards in Brazil. It can be concluded, therefore, that the relevant modification introduced by the 45th Amendment was based on the understanding that homologation proceedings before the Supreme Court on non-constitutional matters would be more time-consuming than matters brought before the Superior Court.

Appeal to the Supreme Court on Constitutional Matters

The 45th Amendment also modified the requirements to be complied with by the parties in regard to the merit of appeals to be analysed by the Supreme Court on Constitutional Matters. Among the other requirements already provided for in the Brazilian Federal Constitution, the Amendment included another one needed for the merits of appeals to be analysed by the Supreme Court on Constitutional Matters, to wit: the general repercussion of the proceeding. In other words: to have its merits analysed by the Supreme Court, the content of an appeal must be an issue that supersedes the interest of the involved parties. That means that the subject matter of the appeal must be important not only to the involved parties but also (and mainly) to society in general for the Supreme Court to accept analysing the appeal and examining its merits.

According to the relevant modification introduced by the 45th Amendment, at the beginning of an appeal, the appellant must evidence that the subject matter under discussion is important to society in general and not only to the parties involved in the claim. Actually, such modification has revived a requirement existing in the Brazil's former Constitution.

There is no doubt that the relevant modification aims to decrease the volume of appeals by reinforcing the primordial duty of the Supreme Court as the guardian as well as the official and ultimate interpreter of the Federal Constitution.

Binding Precedents (certiorari)

The most controversial modification introduced by the 45th Amendment was the creation of binding court precedents. Notwithstanding the existence of court precedents in Brazil, such precedents did not used to have a binding effect.

Based on Brazilian tradition, precedents were not binding because the lower courts could, for instance, interpret an issue completely different from the interpretation of the same issue by a higher court. Until the 45th Amendment, precedents were only a usual interpretation of the Court of Appeals about certain specific issues and did not have a binding effect, as the lower courts or judges were not obliged to accept or honour the interpretation described in the precedent.

This situation completely changed when the 45th Amendment was introduced. When the Amendment took effect in 2004, the Supreme Court on Constitutional Matters has since been allowed to render binding precedents, which must be complied with by the lower courts even if the latter do not agree with the Supreme Court's legal rationale.

According to Brazilian doctrine, the major disadvantage of binding precedents is the limitation on the evolution of the precedents and on the interpretation of law. As the lower courts, from now on, have been obliged to adopt the legal rationale of biding precedents issued by the Supreme Court on Constitutional Matters, the doctrine has created public apprehension about the evolution of these court precedents, which could be prejudiced as a result of their binding effect.

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Arbitration and the Brazilian Judiciary in the 21st Century

BY RODRIGO GARCIA DA FONSECA | WALD E ASSOCIADOS ADVOGADOS

Arbitration was asleep in Brazil for decades. It was something virtually unknown to the local legal community. The number of cases that actually went to arbitration in Brazil, or involving Brazilian parties, was almost insignificant.

For many years, Brazilian law regarded an arbitration clause *("cláusula compromissória")* as a mere promise to arbitrate, which, if broken, might give rise to a claim for damages, but would not prevent the merits of the dispute from being adjudicated by a judge. Only a submission agreement *("compromisso arbitral"),* entered into by the parties after an actual dispute had already arisen, could force the initiation of an arbitration proceeding. On the other hand, even if the parties did go to arbitration, the final arbitral award was not really final. It would only be enforceable after a recognition or homologation procedure *("homologação de laudo arbitral"),* before a court of law, one that would allow the losing party to rediscuss the merits of the whole case. If the award was rendered abroad, then it was even worse, because it had to go through double judicial homologation – the Brazilian Supreme Court would not homologate a foreign arbitral award before it had first been homologated at the Judiciary of the seat of the arbitration. No wonder arbitration was seldom used.

This scenario began to change in the 1990s, and Brazilian Courts played and important role in this respect. After a somewhat slow start, the Brazilian Judiciary has since firmly adapted to the new times, and particularly in the first decade of the 2000s, put aside old habits and case-law, and embraced a very modern and pro-arbitration stance that has effectively transformed Brazil into a friendly jurisdiction for commercial arbitration, be it domestic or international. Now, in 2010, well into the 21st Century, the situation seems to be quite stable in this respect, and promises to remain so for a long time.

The 1990s marked an important increase in globalisation, which affected Brazil and the whole of Latin

America. It was a time most of the region had new democratic governments, after many years of military rule, and experienced a significant economic recovery after the high inflation, debt crisis and recession of the 1980s. In the wake of these changes, most Latin American jurisdictions started to look at arbitration differently. Many countries in the region enacted new legislation on arbitration during this period, and Brazil was no exception.

In Brazil, a new Federal Constitution went into force in 1988, and general elections for President of the Republic were held in 1990, for the first time in almost 30 years. A movement of revision of the national legislation quickly ensued. From then on, not only did Brazil adhere to and promulgate a number of international conventions about commercial arbitration, but most important of all, in 1996 a new Arbitration Statute – Law n. 9.307 – was finally approved.

Law 9.307/96 – the Brazilian Arbitration Act ("BAA") – created a favourable legal framework for arbitration in Brazil, and removed those obstacles for its effectiveness. The BAA gave full force to arbitration agreements, enabling their specific performance in case of defiance by one of the parties (BAA, articles 5, 6 and 7). It set the arbitral award at equal footing with judgments from judicial courts of law (BAA, articles 18 and 31) and did away with the double homologation requirement for foreign arbitral awards (BAA, article 35).

Nevertheless, old concepts are hard to be overcome, and in the beginning some judges still saw arbitration as an unfriendly competitor to the Judiciary system, as something that would unduly take their prestige and power away. For some years, many courts around the country held that the BAA was unconstitutional, because by giving specific performance to arbitration agreements, it would deny parties access to courts of law once a dispute arose (Article 5, XXXV, of the Federal Constitution, states that no law shall prevent the Judiciary from being accessible to decide on an alleged violation or threat of violation to someone's right). Only in 2001, five years after the enactment of the BAA, its full constitutionality was affirmed by the Brazilian Supreme Court. The Court recognised that the BAA does not deny anybody access to the Judiciary. It only guarantees the enforcement of arbitral clauses voluntarily entered into by contracting parties. The Supreme Court also made it clear that the BAA has preserved the Judiciary's power to void arbitral awards in case of serious procedural defects, and therefore, access to the courts is not forbidden, it is only postponed in time (this decision was rendered by the Plenary Session of the Supreme Court, by a majority vote, in the case of Homologation of Foreign Award n. 5.206, originated from Spain, decided on 12/12/2001). As a consequence, although it some took years, the alleged problem of the constitutionality of the BAA is now over in Brazil.

After this landmark decision of the Supreme Court in 2001, legal security was guaranteed in Brazil for those involved in arbitration. The number of contracts with arbitration clauses grew rapidly. Arbitration institutions were created in many places throughout the country, and became more and more experienced in the administration of proceedings, given the rising number of cases filed with them. Local and international statistics are a testament to the success of the BAA and the development of a true Brazilian arbitral culture, perfectly inserted in the international arbitral context (by way of example, the statistics of the International Chamber of Commerce, in Paris, show that Brazil is now the leading country in Latin America – and one of the leaders in the world – in the number of parties involved in ICC arbitrations. The numbers of Brazilian arbitrators, of Brazilian counsel, and of cases seated in Brazil have also grown dramatically over the last decade).

Beginning with the Supreme Court decision referred to above, the local Judiciary played a major role in

making sure this new reality saw the light of day. Although a novice in the field of arbitration, the Brazilian Judiciary came to respect and understand it, and embraced its principles in a clever and modern way. At least in the more developed areas of the country, judges no longer distrust or are prejudiced against arbitration. People and companies using arbitration know that if something goes wrong, one way or the other, most of the time the courts will get it right at the end of the day. 100% legal certainty does not exist anywhere in the world, but today there is a reasoned expectation that a certain trend will be maintained, and that the backbone principles that support arbitration, as a rule, will be respected whenever discussed before a Brazilian judicial court.

For example, there is no longer any reasonable doubt that an arbitration award is a final decision on the merits, not appealable, with equivalent enforceability to that of a court judgment (the Superior Court of Justice has repeatedly confirmed this principle).

As far as foreign arbitral awards go, the Superior Court of Justice has made it repeatedly clear that it will only review if the relevant formalities were observed, but it will not engage in any discussion as to the correctness of the decision rendered by the Arbitral Tribunal on the merits. The Superior Court recognises that it is an imperative of good faith, and of the way that international transactions are carried out in today's world, that arbitral awards are respected and honoured by the parties and by their respective jurisdictions (this issue has been dealt with by the Superior Court of Justice many times).

As to the issue of arbitrability, always a delicate matter, the Brazilian Judiciary has also taken very positive steps towards ensuring the proper functioning of arbitration. The BAA, in article 1, allows for capable parties *("pessoas capazes")* to arbitrate disputes involving disposable patrimonial rights *("direitos patrimoniais disponíveis")*. Although the subjective standard for arbitrability – legal capability to enter into agreements – is fairly simple, the objective standard is a somewhat complicated one, as the statute does not define what those disposable patrimonial rights are. However, Brazilian Courts have since looked into this matter and rendered a number of very interesting decisions. The country can now be said to be at the international forefront insofar as arbitrability goes. For example, different from many jurisdictions, Brazil has now settled that state entities can take part in arbitration, and if they signed an arbitration agreement, it is a duty of good faith and of preservation of the legitimate expectations of the other party that they do so. It has also been decided that the supervening insolvency or bankruptcy of a company does not void an arbitration agreement that had been validly contracted before. Both issues of arbitrability – arbitration involving state entities and insolvent companies – still give headaches to practitioners in many sophisticated jurisdictions, but are now quite consolidated in Brazil (it is true there are still some delicate issues in terms of arbitrability in Brazil, particularly in the areas of consumer and labor laws, where various conflicting decisions from different courts can still be found. But these are very specific matters that do not really impact the effectiveness of commercial arbitration).

Moreover, anti-arbitration injunctions are getting rare these days. The principle of *Kompetenz-Kompetenz* of Arbitral Tribunals, their jurisdiction to decide on their own jurisdiction, is now understood and correctly applied, following decisions of various courts, including the Superior Court of Justice (*Kompetenz-Kompetenz* is a principle embodied in articles 8 and 20 of the BAA).

In international transactions connected to Brazil, arbitration has become commonplace. It is important to notice that Brazilian Courts will enforce arbitration agreements regardless of the chosen seat, even if it is

located abroad. The same cannot be said of forum selection clauses, because the choice of a competent court in a foreign jurisdiction may not prevent a case from being heard in Brazil. This situation makes arbitration clauses especially appealing in international agreements.

Brazil is a huge country, so from time to time bad court decisions may come up in one place or another. Most of the times they will end up reversed on appeals, but not everything is perfect. However, as mentioned before, problems exist everywhere around the world, and unexpected or disappointing court decisions can happen in any place. The important point to stress is that, today, the Brazilian Judiciary is doing a very good job in terms of preserving legal security for arbitration in Brazil. The system is working properly. This allows arbitration to have a bright present and an even brighter future in this jurisdiction.

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EUROPE

EUROPE

Electronic Skeletons: Databases and Your Document Retention Policies

BY JIM VINT | FTI CONSULTING

Recent investigations by the European Commission, FSA and U.S. SEC /DOJ have required pharmaceutical, oil and gas and financial services firms to produce data going back almost 10 years. Due to an organisation's inability to produce this information during an investigation or in an electronic disclosure exercise, sanctions and fines have been incurred. In many cases, over production of information occurs due to the inability to carve out relevant material from information systems, consequently raising costs. Specific to financial, transactional and operational data, general disarray arises while attempting to produce information. These situations are familiar to many firms as a result of years of ineffective document retention policies specific to the information that most firms consider its lifeblood – application (or structured) data. This is clearly evident in the recent *Earles v Barclays Bank plc* decision from which the QC highlighted that it is reasonable to expect major corporations to have sufficient means of identifying, preserving, restoring and producing its ESI during disclosure or investigations. In this instance, part of the exercise entailed production of structured data in the form of "transfer sheets". Transfer sheets are a means though which banking customers can ensure settlement of real time monetary transfers between banks or financial institutions.

Structured data is the information that lives within database environments, not email or MS Office type files. This includes software specific to Enterprise Resource Planning ("ERP"), Customer Relationship Management ("CRM"), supply chain tracking, operations and manufacturing, trading systems, tracking sheets and the like. These usually fall outside "document" retention policies but changes in the UK (and the U.S.) to the Civil Procedural Rules a few years back now stipulate that these information sources are to be included in disclosure and consequently need to be included in retention policies.

Throughout 2009, pressure regarding electronic document production continued: specifically the requirements have been to do more for less and to do it quicker, all the while remembering to adhere to proportionality without failing to produce the obvious. Add the fact that more organisations are seeing exponential growth in their data volumes and one can easily begin to go cross-eyed. If we dig a bit deeper on this last fact, it becomes obvious that it is not a dramatic increase in messaging, file shares or backup tapes upon which traditional e-disclosure exercises have focused, rather significantly more information is being captured and stored in ERP, CRM and financial application databases (Corporate eDiscovery Technology Trends 2009 IDC, 2009 N=115).

Application information becomes more complex to produce as time elapses for a variety of reasons. First, software applications evolve over time to accommodate fixes and bugs (a great example is the Windows 7 release to "fix" Vista). As a result, software contemporaneous to 5 years ago cannot be restored to a current platform and the licence for

the earlier version is almost never renewed for restoration purposes. Second, certain information is consolidated or rolled-up at year end or quarterly close. The detail is retained for audit purposes in an extracted format and saved "somewhere on the network". This information may be unreliable since it is likely stored in a series of Excel files or an Access database, and is at best, a snapshot of the data at a point in time. Finally, similar to the upgrade issue above, firms migrate from one software package to another over time to accommodate growth and flexibility. While the firm may currently be using Oracle or SAP, there may have been multiple applications running historically. So how do companies mitigate these risks moving forward?

Expanding data governance and retention policies to include application data is the first step. As enterprise data management and e-disclosure efforts converge, the cost of not addressing these issues far outweighs the costs of ignoring them. While every organisation will differ, the following provides a brief outline for structured data retention policies.

Information Management Protocols: Data Management and Information Retention

As data flows through an organisation, it is manipulated and migrated from raw data format through consolidation into financial reporting packages. During this course, relational components are included to help define the raw data and make it information. For example, an order for item number 123abc for customer zyx987 means nothing on its surface. It is only after the item number and customer number are "related" to the item and customer tables, that we are able to understand this transaction to be the purchase of a Blackberry for a John Smith Consulting. Since customer and product catalogues can change on a daily basis, it is imperative to concentrate on data quality and data consistency when retaining structured information. Special attention needs to be devoted to ensuring that all relational data points are retained and not simply the transaction log. It may also be prudent to back up data in a universally accepted format (such as an SQL server) in efforts to avoid software compatibility and licensing issues.

In order to facilitate data management, institutional knowledge of what data the organisation has and where it is located throughout the IT estate should be documented. This may become even more important moving forward as larger organisations move to the concept of "cloud computing" from a storage, software or infrastructure standpoint. Defining cloud computing is a topic sufficient for an entire article in and of itself, however in broad terms, cloud computing is utilising a network of servers managed by a third party in various locations to run software as opposed to running an application locally on a laptop or desktop. The recent introduction of the Chief Data Officer ("CDO") as a new executive position is allowing companies to gain an understanding in this area from both an unstructured (emails and documents) and structured aspect. As firms migrate away from local document storage and application installations, more e-disclosure will be required from "cloud" locations. The CDO's primary responsibility is for data integrity, availability and storage location of data in an organisation and coordinating litigation holds and eDiscovery request responses.

Legal Hold Policies and Procedures

While a duty to preserve structured data may not explicitly exist, there is certainly an implied duty not to destroy. Structured data sources and applications are extremely dynamic in nature and change constantly as new data is uploaded or entered and temporary data is overwritten or modified. As a result of the constant movement within these databases and the sheer volume of data, it is relatively impractical to keep track of changes or capture any removal or deletion of data during the normal course of business. However, once a legal hold is enacted, it is important to establish procedures for suspending this routine deletion and addressing preservation obligations. A simple solution

to this may be to enact the audit log, which is typically turned off (due to performance concerns). Another solution might be extracting specific data from a third party provider in order to preserve information. (As an aside, while negotiating with any cloud computing provider, be sure to include eDiscovery response mechanisms in the contract.) Either of the solutions posed above, along with others, may require firms to dedicate additional hardware and network space, but will ensure compliance with necessary requests when / if needed.

Additionally, thought needs to be given to application upgrades, decommissioning and data consolidation projects. Specifically, what happens to the software when it becomes "obsolete" to the organisation? Unlike emails, which have limited formats depending upon the platform used, applications are highly customisable allowing firms to manipulate "off the shelf" products like SAP and Oracle to a high degree in order to meet their business functions. The result: an inability to restore this data to any other environment if simply backed up to tape. The actual process of preservation and retention should address future capabilities of restoration and the proper medium and format should be implemented when decommissioning and upgrading.

Have an eDiscovery Response Plan (Request to Produce ESI)

As noted above, the CDO has the responsibility for coordinating responses to eDiscovery requests, which ultimately will entail directing the eDiscovery response team. This cross functional group of internal and external professionals typically includes deep functional and technical expertise in critical application databases and email / archiving systems, legal representatives for privileged review and data privacy concerns and IT personnel to accommodate any hardware or software issues or concerns. If an organisation is experienced in these types of requests, they likely have a healthy understanding of their pertinent data inventory and have created defensible approaches to preserving and producing their data. However, this plan has probably not traditionally included the production of application data. Many of the same risks and challenges encountered with emails and documents are present with application data as well, and defensibility and repeatability remain paramount in any process under disclosure rules. We believe that if you build the following practices into your response plan, at the very least you will have an elevated level of certainty should the need to produce application information arise:

- Maintain market knowledge regarding the tools and services available to facilitate enterprise data management with a view toward preservation;
- Prepare a plan of action for producing enterprise wide data from ERPs or CRMs (in accordance with data privacy laws), with minimal disruption to the business; and
- Retain code, system schema and data flow diagrams for archived and current applications and define retention periods in line with emails and documents for raw data backups.

Additional steps can be added to ensure a comprehensive response plan is in place, however, these will vary by application, usage and organisational structure and are best addressed by the entity in conjunction with discovery experts.

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UNITED KINGDOM

Arbitration or Litigation in Complex Commercial Contracts: Private Beauty vs. Public Beast

BY NIC FLETCHER AND ED HOOD | BERWIN LEIGHTON PAISNER LLP

Commercial clients are understandably keen to ensure that their disputes are resolved promptly and with minimum disruption to business.

So far as arbitration is concerned, the length of time that it takes to obtain a final award depends on a number of factors. The first is the nature of the dispute. Disputes which are relatively straightforward and do not involve complex factual enquiries will require less in the way of disclosure and witness statements and are unlikely to require expert evidence. Such cases can be disposed of reasonably quickly. If the case is factually complex and/or it is likely to involve expert evidence, then more time will have to be allowed for this evidence to be gathered. The rules of most arbitral institutions also permit disclosure (although this is usually more limited than in court proceedings). Time has to be allowed for the disclosure process to run its course. Sometimes, a dispute can be resolved quickly by identifying a preliminary issue which may avoid the need for complex factual enquiries.

If both parties are willing, even complex cases can be dealt with on an expedited basis. This does, however, require the cooperation of the parties. Sadly, once a dispute has arisen, it is often quite difficult to reach agreement on an expedited hearing. One party or the other usually decides it is against their interest. One way of avoiding this is to incorporate a specific provision in the contract requiring the arbitration award to be delivered within a limited period.

The number of arbitrators is an important factor. An arbitration hearing can only take place if each of the arbitrators is available. It is a lot easier to juggle one arbitrator's diary than to try to find a convenient date for three arbitrators. This may militate in favour of an arbitration clause providing for the appointment of a sole arbitrator.

Once the arbitration hearing is over, the Tribunal has then to write its award. Again, in a complex case this may take some time. When appointing a tribunal, you should check that the chairman has the time to dedicate to the task.

What all this means is that, in a case of average complexity, you can expect to receive an arbitration award within a period of 18-24 months.

Turning to litigation, whilst historically arbitration was viewed, probably correctly, as by far the faster option to resolve disputes with some court cases taking many, many years to resolve, following the various reforms to the court processes, led primarily by Lord Woolf, and greater judicial management over the litigants and their lawyers plus the gradual reduction in the number of cases actually going to trial court cases now tend to get resolved much more quickly. Facing an imminent and likely public trial tends to focus the litigants' minds perhaps more than a less

formal arbitration. The courts now impose strict timetables and will simply not countenance the old "game playing" that could go on in the past and favour the more wealthy litigant. Perhaps one crucial difference between arbitration and litigation can be found in the resolver of the dispute. Arbitration provides a certain flexibility in, say, picking an expert in a particular field who understands the underlying business issues. In litigation, this is simply not an option and one gets given a judge who may, or may not, be familiar with the complexities of a certain business arena.

In terms of cost, arbitration was traditionally cheaper than litigation. The commodity trade associations, for example, have streamlined rules and panels of commercial arbitrators who are active in the particular trade. They deal with cases efficiently and cheaply. A complex international arbitration, however, is likely to involve the same level of fees as court proceedings. In some cases, the cost may be higher. If the arbitration is administered by one of the institutions, there will be an administration fee. This can vary significantly between institutions. The arbitrators will also charge for their time. Self-evidently, a tribunal of three arbitrators will be more expensive than a tribunal comprising a sole arbitrator.

Litigation itself is certainly not inexpensive. However, the Pre-action protocols (in simple terms these require parties to put most of their cards on the table at the outset so the opponent can make an informed decision as to their position and settlement issues) and case management tools available to both the courts and litigants has, to a noticeable degree, brought costs under some control. The ability for either a Claimant or Defendant to make what is known as a "Part 36" offer to pressurise an opponent into being reasonable in terms of expectation and not adopting a slash and burn policy has had a marked effect. Misjudge your litigious behaviour and you pay the price. More reforms of this nature are anticipated following Lord Justice Jackson's recent review on litigation funding and costs to allow further innovative ways of gaining access to justice at a more reasonable price and with more risk sharing options between litigants and indeed third parties.

Whether pursuing arbitration or litigation, the successful party can usually recover its costs. Under English law, an arbitral has the power to make an award allocating the costs of the arbitration between the parties. Unless the parties have reached a contrary agreement, the Tribunal is required to award costs on the principle that costs should "follow the event" – in other words, the loser pays. Arbitrators do, of course, have a broad discretion not to award costs if they feel that it is not appropriate in relation to the whole or part of the costs and can reach different decisions on costs in relation to different issues in the case.

Companies should, however, bear in mind that they cannot agree with their contract counterparty that one of them has to pay the whole or part of the costs of the arbitration in any event unless that agreement is made after the dispute has arisen.

For its part, litigation offers more precedent and rule-led flexibility than arbitration. If a litigant has been successful but has previously refused an offer the Court regards as having been reasonable it can cost dearly despite the winning result. This is another area in which experienced advice is critical as costs tactics are an essential part of any dispute. Quite obviously, an adverse costs order can destroy the advantage of a supposed win.

Confidentiality is often a concern for disputing parties. This is one of the great strengths of arbitration. It is a confidential process. This makes arbitration ideal for commercial relationships where disputes might involve confidential processes or trade secrets. It is also useful for parties who do not want their private commercial dealings exposed to the full glare of public scrutiny. That said, there are some arbitral processes which are not confidential. Investment treaty arbitration administered by the International Centre for the Settlement of Investment Disputes (ICSID) is a relatively open process.

Most litigation, on the other hand, is open to the public including Court records. One can apply for the Court file to be effectively sealed and for hearings to be heard in private but there is no guarantee. From experience, one can end up with a mixed bag – private hearings but public judgments on the basis that the latter is in the public interest. Judges tend to be sensitive in judgment if the hearings were in private. Nevertheless, the short point is that privacy favours arbitration and if one is likely to wish for an ongoing commercial relationship with a potential opponent then arbitration is the better bet.

When negotiating dispute resolution clauses, it is critical to bear in mind the potential need to enforce any decision in your company's favour. Generally speaking, the enforcement of arbitration awards is governed by the New York Convention of 1958. Subject to certain very limited exceptions, countries which have ratified the New York Convention agree to enforce arbitration awards issued by arbitral tribunals which have their "seat" in another convention country. At the present time, some countries have ratified or acceded to the New York Convention. Although the precise mechanism of enforcement may vary from one country to another, the principle is well established. Indeed, there are a number of countries (e.g., Russia) where English court judgments are not recognised, but arbitration awards are.

The position is more difficult in countries which are not party to the New York Convention. Where and how the courts in such countries will enforce an arbitration award is something that has to be approached on a case by case basis.

Again, generally speaking, judgments from the English Courts are relatively easy to enforce in most jurisdictions. We have a respected judiciary and developed legal system. There are obviously exceptions which makes it essential to check where one might have to enforce against relevant assets because the cost of enforcement, or attempted enforcement, can far outweigh the benefits. One also needs to take into account local idiosyncrasies to gauge the likelihood of practical success. The practical point is to have a keen eye to the risks associated with a dispute. It is all well and good to have an apparently English friendly jurisdiction only to find you are wrapped up in expensive litigation for years with, for example, curious insolvency rules.

Speaking generally, arbitration, like litigation, has both strengths and weaknesses. Perhaps the greatest convenience of arbitration is its flexibility. There is considerable scope for the parties to agree a procedure for the arbitration which suits the particular case. Even if there is no agreement between the parties, a skilful lawyer will be able to design and shape an arbitration procedure that enables them to present the client's case in the most effective manner.

The sad truth is, however, that parties frequently dispute any point they can for a perceived advantage. The skilful lawyer can narrow the margins of dispute and get down to sensible parameters. Perhaps a key difference between arbitration and litigation can be put like this. Arbitration is less formal, brutal and stressful in the main and puts clients in less fear of the dispute resolution process. However, this can tend to let things drift. The fear of Court really does focus the mind for lawyers and clients alike.

At the end of the day, both arbitration and litigation have their merits and de-merits. What is right for one deal is wrong for another. Absolute care needs to be taken on a deal by deal basis as to what is right for your business. Beware the standard form.

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Directors Beware – A New Right for Shareholders

BY SIMON PAINTER AND SINÉAD LESTER | BIRCHAM DYSON BELL

There have long been ways in which dissatisfied shareholders can challenge decisions made on behalf of a company by its directors. On 1 October 2007 a new procedure came into being designed to provide "more modern, flexible and accessible criteria for determining whether a shareholder can pursue such an action". The Companies Act 2006 enables shareholders of a company to bring a "derivative claim" challenging the actions of those running it if they allege that they are in breach of their duties as directors.

There have been a few of these new actions pursued in the two years since the right came into being and it is not hard to think of certain groups of shareholders who must be feeling deeply aggrieved, not to mention out of pocket, following last year's record bank bail outs.

In order to bring a derivative action a shareholder must first obtain the permission of the court to do so. At the first stage, a shareholder must demonstrate a prima facie case, considered by the court on paper without hearing evidence either from the defendants against whom relief is sought (for example, the directors) or the company. If a prima facie case is established, the permission process moves to the second stage whereby the court will ordinarily direct the company itself to give evidence at a hearing. At the substantive hearing of the permission application, the court must refuse permission if it finds that a person acting in accordance with the general duty to promote the success of the company would not seek to continue the claim or where the act or omission giving rise to the cause of action has been authorised, ratified or approved by the company. In deciding whether a person seeking to promote the success of the company would continue the claim, the court looks at various factors which include:

- whether the member (i.e., shareholder) is acting in good faith in seeking to continue the claim (the intention being to assist in preventing vexatious claims at an early stage);
- the importance that a person acting in accordance with the duty to promote the success of the company would attach to continuing the claim;
- whether the act or omission giving rise to the cause of action could be (and in the circumstances would be likely to be) authorised or ratified by the company;
- whether the company has decided not to pursue the claim;
- whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in his own right rather than on behalf of the company; and
- any evidence before the court as to the views of members of the company who have no personal interest (direct or indirect) in the matter.

As the court is required to take account of the views of uninterested shareholders, this should make it harder for a shareholder to bring a claim against the general wishes of the shareholder body, thereby seeking to maintain the common law principle of "majority rule" from the established case of *Foss v Harbottle (1843) 2 Hare 461*.

Why is this two-stage procedure necessary? Its purpose is to dispose of unmeritorious or frivolous claims at an early stage. So far, there are no reported English claims that have made it past the permission stage. One of the first reported decisions was *Franbar Holdings Ltd v Patel and ors [2008] EWHC 1534 (Ch)* where permission to continue a derivative claim was refused. Following a series of disputes between F Ltd (the holder of 25% of the

shares in M Ltd) and C Ltd (the holder of 75% of the shares in M Ltd), F Ltd issued three sets of proceedings:

- A claim against C Ltd for breach of the parties' shareholders' agreement;
- An "unfair prejudice" petition against C Ltd.
- A claim against the directors nominated by C Ltd and M Ltd, which F Ltd sought permission to continue as a derivative claim as it sought a remedy on behalf of M Ltd.

The court refused permission to continue the derivative claim principally due to its conclusion that a person acting in accordance with the duty to promote the company's success would be unlikely to attach much importance to its continuance; a hypothetical director acting in accordance with the prescribed duties would take into account a wide range of considerations when assessing this, including such matters as the prospects of success of the claim, the ability of the company to make a recovery on any award of damages, the disruption which would be caused to the development of the company's business by having to concentrate on the proceedings, the cost, and any damage to the company's reputation and business if the proceedings were to fail. The judge considered that the hypothetical director would be more inclined to regard pursuit of the derivative claim as less important because several of the complaints were better formulated as breaches of the shareholders' agreement and acts of unfair prejudice which were already the subject of proceedings.

Following on from the *Franbar* case was that of *Stimpson and others v Southern Private Landlords Association and other [2009] EWHC 2072 (Ch))* where Bircham Dyson Bell achieved a notable success for the National Landlords Association (NLA) in defeating a permission application. The claim arose following the merger of the NLA and Southern Private Landlords Association (or the NFRL (National Federation of Residential Landlords) as it is commonly known) in July 2008 to form the largest private residential landlords' association in the UK. The companies involved were limited by guarantee rather than by shares. The merger was welcomed across the industry as an important step towards a unified voice for landlords at the national level. Shortly after the merger was announced, 11 members (out of a total membership of approximately 5,200) of the NFRL sought permission to bring a derivative claim against the NLA and the majority NFRL directors who were in favour of the merger, as well as injunctive relief against the NLA. The claim arose from a boardroom dispute involving one of the claimants who was determined to challenge the merger at whatever cost.

In May 2009, the High Court dismissed the legal challenges to the merger. The court found that a hypothetical director, acting in accordance with his duty to promote the success of the NFRL, would not continue the claim. The court came to this decision for various reasons including the speculative nature and modest value of the claim, the vast expense of the proposed litigation and the fact that the interests of the members could be provided for by the NLA. It also ordered those who brought the action to pay the NLA's costs.

The application was one of the first cases to come to court concerning whether or not permission should be granted to bring a derivative claim under the new Act since it came into force in October 2007. The NLA's involvement was as a third party which made the case even more novel as derivative claims against third parties are exceptional.

The claimants also sought sequestration of the NLA's assets for an alleged contempt of court in purported breach of various undertakings following an injunction application but the claimants dropped this claim shortly before the hearing. Costs were awarded to the NLA on an indemnity basis.

How can directors avoid derivative claims being brought against them? The short answer is to make sure that

they are aware of and comply fully with their duties as directors. The 2006 Act codified these, largely (but not completely) replacing the former legally recognised list of duties. These include duties to exercise independent judgment and reasonable care, skill and diligence.

Directors should acquaint themselves thoroughly with the detail and extent of their duties and comply with them fully; by doing so they will minimise the possibility of a derivative action coming their way.

Watch this space – in the current economic climate a raft of new claims could well be on the way from shareholders who are deeply aggrieved at the drop in the value of their investment shares.

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The Illegality Defence – Recent Developments in English Law

BY JONATHAN THORPE AND ROB MORRIS | CMS CAMERON MCKENNA

It is a well-established principle of English law that, as a matter of public policy, a claimant cannot rely on his own wrongful act to make a claim. The principle is commonly known as the illegality defence and the English courts have held that it applies in circumstances where the claimant is involved in criminal or other sufficiently serious wrongful activity. For example, a claimant committing an illegal act, such as a burglary, may be prevented from claiming compensation for personal injury that he sustains as a result.

The extent of the application of the illegality defence has been the subject of much judicial debate and in a consultative report published in 2009 the English Law Commission criticised the resulting body of case law as "technical, uncertain and sometimes arbitrary". The Law Commission has indicated it will publish a final report following public consultation. In the meantime, however, issues relating to the application of the defence came before the courts on a number of occasions in 2009.

Recoverability of Losses the Claimant would have Sustained Anyway

In *Gray v Thames Trains and Others,* the claimant, who was a victim of the Ladbrook Grove rail crash in 1999, developed post-traumatic stress disorder. He went on to commit manslaughter and it was accepted that he would not have committed the offence but for the psychological injuries caused by the accident. The claimant brought a claim against the train company (who admitted that their negligence had caused the crash) which included a claim for loss of earnings both for the period from the crash to the killing and for the period following his incarceration in a secure hospital under the Mental Health Act following his conviction for manslaughter.

The House of Lords held that the claimant could not claim for the consequences of a criminal sentence being imposed based on both the illegality defence and on a causation defence. The House of Lords concluded that to allow him to be compensated in tort for such losses would be inconsistent with the criminal law holding him personally responsible for his criminal act. He also could not recover compensation for loss of earnings that he would have suffered in any event as a result of the train crash (whether or not he had been convicted of manslaughter) because,

for public policy reasons, the court would view the subsequent conviction as a supervening cause of loss.

Application of the Illegality Defence to Claims Brought by Corporate Entities

The House of Lords again considered the illegality defence in *Moore Stephens v Stone & Rolls*. The case concerned the application of the defence to companies in the context of fraud. Mr S was the directing mind and will of a company which he used to defraud banks. The banks successfully claimed against the company and Mr S. Neither the company nor Mr S had sufficient assets to pay the damages awarded to the banks and the company went into liquidation. The liquidator brought a claim against the company's auditors who, it was alleged, had failed to spot that the company was being used as a vehicle of fraud and had therefore failed in their duty of care.

The House of Lords (by a majority of 3:2) held that the claim against the auditors (which was in fact the company's claim although brought by the liquidator) would fail because in bringing it the company would be relying on its own wrongful conduct.

The application of the illegality defence to companies rather than individuals has always proved difficult and was the subject of lengthy discussion and fierce disagreement between their lordships.

In reaching the decision the House of Lords considered the following issues.

- Whether the fraudulent behaviour of the company's director (Mr. S) could be attributed to the company, i.e., whether the company was in fact the victim of the fraud or the villain?
- If the fraud could be attributed to the company, did this prevent the company from claiming against the auditors?
- Did it make a difference that one of the very things that the auditors were engaged to do was to detect fraud?

Although the precise reasoning varied, the following conclusions can be drawn from the majority judgments:

- Mr S was the sole controlling mind and will of the company and, accordingly, the company was attributed with knowledge of the fraud and was primarily i.e., personally (rather than vicariously) liable. It appears that it was an important factor that there was no one else involved in the management or ownership of the company other than the fraudulent director, Mr S.
- To bring a claim against the auditors the company would need to rely on its own illegal act – which it was not entitled to do.
- It was irrelevant that one of the very things the auditors were engaged to do was to detect fraud.

Against the background of the current recession and expected increase in claims against professional advisors, the decision will have provided some comfort to auditors. This was, however, a case where the company was controlled by a single individual who was responsible for the fraud and it remains unclear what the position would be if a similar claim were brought by a company not so fully immersed in the fraud as in this case.

Whether the Untainted Part of a Claim will Fail if Part is Tainted for Illegality

K/S Lincoln and Others v CB Richard Ellis Hotels Limited concerned the over-valuation of hotels which caused the claimants to pay too high a price for them. Of the total price that the claimants paid for the hotels, 92% was paid direct to the seller and 8% was paid to a property location agent. The defendant alleged that the additional 8% paid to the property location agent had been added to the purchase price for illegal tax evasion purposes. The defendant contended that accordingly the whole claim should fail on the basis of the illegality defence.

The claimants applied to have the allegation struck out on the grounds that even if the motivation for paying the additional 8% was illegal tax evasion, the illegality defence should not apply to defeat their claim.

Although the judge declined to strike out the illegality defence, he noted that it was likely to fail in relation to the claim as a whole because the claim against the defendant relied on the contract to value the hotels whereas the alleged illegality was contained in the contracts for the sale of the hotels. There may have been some illegality in the arrangements as a whole, but the alleged fraud was too remote from the alleged breach of contract/negligence of the defendant.

The judge indicated, however, that although the whole claim was unlikely to fail for illegality, the claim for the additional 8% might and that it is possible for the illegality defence to apply to defeat a particular head of loss or portion of the quantum claimed but for the remainder of the claim to succeed.

Whether an Attempted Illegal Act will be Sufficient to Defeat a Claim

The recent case of *Nayyar and Others v Denton Wilde Sapte and Another* concerned a payment made by travel agents as part of negotiations for a global sales agency appointment by Air India. The claimants were not awarded the GSA appointment and brought a claim in damages against the solicitor who had introduced the business opportunity to them to recover the amount they had paid.

The judge held that in civil law terms the payment was intended to be a bribe and that this was sufficient to engage the principle of the illegality defence. In this case the bribe had been unsuccessful but the judge found that it was not necessary to establish that the intended illegal purpose had been effectively carried out. Nor was it necessary to decide that there had been a breach of the criminal law. There was a clear and close connection between the wrongful conduct and the claim made. The making of the payment for a wrongful purpose was an effective cause of the claimants' loss and the illegality defence would operate to defeat the claim.

Conclusion

The application and scope of the illegality defence remains a complicated and uncertain area of law but a number of principles can be drawn from the recent cases:

- In general the illegality defence will operate to prevent a claimant from recovering the benefit of his own wrongdoing. The defence may operate to defeat a claim by a corporate entity in circumstances where the wrongdoer(s) can be shown to be the controlling mind and will of the company.
- Even if a claimant would in any event have suffered loss as a result of another party's negligence, his own supervening wrongful act may operate to preclude him from claiming for such loss.
- It is not always necessary to establish that a criminal offence has occurred in order for the defence to succeed.
- If the illegal conduct is sufficiently remote from the contract the claimant is seeking to enforce, the illegality defence may not apply.
- It is possible for the illegality defence to be applied to part only of a claim where the head of loss tainted by illegality can clearly be carved out from the reminder of the claim.

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Should Forensic Accountants have to be Accredited in Order to Give Expert Evidence?

BY ANDREW J. MAINZ | FTI CONSULTING

The Institute of Chartered Accountants in England and Wales thinks they should. It has set up a "specialist online register that is an independent and reliable source of specialist forensic accountants" able to give expert evidence. These accountants will have "recent and relevant experience" of giving expert evidence on accounting matters and/or of carrying out forensic accounting investigations. The register will "allow accredited individuals to be recognised as the highest quality specialists in their field". It will "instil confidence in clients and instructing lawyers that they have access to the very best advisers". The ICAEW say that their register will "set the standard for excellence and commitment."

This initiative raises two questions. Is accreditation necessary? If it is, does the ICAEW register provide the right way to go about accrediting expert witnesses?

The role of any expert witness is to assist whoever is deciding a legal dispute, whenever the dispute depends on an assessment of technical issues. Most commonly, this applies to judges hearing cases in court. The judges need expert help to understand any technical issues arising before they can reach a judgment. For example, a legal dispute may raise questions about whether a set of financial statements has been prepared in accordance with Generally Accepted Accounting Principles. The judge won't know the answer to these questions and will need expert witness help from an accountant to understand the questions and how they may be answered.

Any expert witness must fulfil two basic criteria if his or her expert evidence is to assist the judge. First, the expert must have the relevant knowledge (i.e., expertise). Second, the expert must provide comprehensive and unbiased evidence designed only to help the judge. The expert's evidence must not be designed to advance the case of whichever party has instructed the expert.

Although these basic criteria are well established, they have not always been followed. There has been, and still is, a tendency for expert witnesses to get too involved in helping "their" side with the result that their expert evidence is partisan and has to be rejected by the judge. This is of course a very unsatisfactory outcome for all concerned and can result in large costs being wasted as well as hardship for all concerned. Perhaps the most notorious recent instance of an expert witness going beyond his expertise, and influencing the outcome of cases badly, is that of Professor Sir Roy Meadow. He was a well known expert in cases of infants dying unexpectedly in their cots. Eventually, it was discovered that his evidence (that multiple cot deaths in a family were always suspicious) was wrong and could not be supported. As a direct consequence, many cases had to be reviewed in which mothers had been found guilty of killing their children based largely on his evidence.

However, it must be borne in mind that there are far more good expert witnesses than bad ones. The few bad ones should not be allowed to damage the reputations of all the good ones. Nor should the few bad expert witnesses be allowed to damage the legal system by calling into doubt the whole concept of expert evidence to help the judge. It should also be borne in mind that no-one can be compelled to give expert evidence. If this work becomes too onerous or risky, experts needed by the courts will simply not be available and the courts will be unable to function properly.

The English judicial system already requires expert witnesses to certify their competence, their independence

and the completeness of their evidence. Experts who fail to meet these criteria can be, and are, criticised by judges and can be reported to their professional bodies and face sanctions from those bodies.

The first question posed above is whether accreditation is necessary. This is a debatable point as regards accountants, since they are all likely to be members of a well run professional body and are already subject to professional disciplinary measures if they fail to act in a proper way. However, there is much more sense to accreditation if an expert is needed in a less well regulated area of expertise. There is also the point, made by the ICAEW, that accreditation provides some level of confidence about a potential expert witness for clients and instructing lawyers. Accreditation can also be used to enforce higher standards of performance from expert witnesses. Those who fail to meet the expected standards can be struck off and this information could itself be included in a register.

Assuming that some form of accreditation for expert witnesses is needed, the second question raised in this article is whether the ICAEW model is the right way forward. This would appear not to be the case. There are many problems with the register which the ICAEW has set up, including the following matters. It is expensive to apply to join the register and the application process makes too many demands on those who want to be accredited. The ICAEW also requires five years of past experience in order to be admitted to the register, making the whole exercise self-defeating. Any expert with five years track record does not need to go on a register to be able to demonstrate his or her competence.

The ICAEW says its register will provide access "to the very best advisers". It is not clear how the Institute will be able to support this statement as its register is open to all who apply and pass the tests. If it is only to include the "very best advisers", it will presumably be a small register. If it is a large register, it will inevitably include advisers of different talents and skills. And it will of course not include anyone who has not chosen to be included, even though they may be the "very best".

So, a register of the kind which the ICAEW is using could be a dangerous move, making it more difficult for the courts to have access to independent and competent expert witnesses. It may well be that the ICAEW scheme will be run immaculately but if it is not, it could become a restraint on trade, allowing only those experts of whom the ICAEW approves to give evidence. If this type of register becomes the norm, we will go the way of Continental Europe where expert witnesses are chosen by the courts from an approved list. Membership of the list is valuable both professionally and as a source of income. It is perhaps not surprising that those included on the list of approved experts rely heavily on the guidance provided by the courts in reaching their professional conclusions. This may make for quick and easy justice but it may not be real justice.

As indicated above, the ICAEW register is purely voluntary. It will still be possible for anyone to give expert evidence about accounting and financial matters whether or not he or she is on the ICAEW's register. This is true and should be. In an adversarial, common law legal system, people should be allowed to present their cases to the courts as they wish. This includes the right of lay clients and their lawyers to select the expert witnesses whom they wish to use. However, as the whole point of the ICAEW register is to create approved experts, if this register becomes established, it is very likely that lawyers will put pressure on their clients to use only registered experts. Non-registered experts could find their absence from the register is used to challenge their credibility in court.

If the ICAEW approach to accreditation is not the best way forward, what is? It may be that the answer is to be found in a different approach to accreditation, one favoured by at least some of the expert witness professional groupings. This approach sets much lower hurdles for admission to a register than the ICAEW propose. The

intention of other registers is that people who have never given expert evidence before, but who have relevant expertise and are interested in doing expert witness work, should be helped to place that expertise at the service of the courts. They need help to do so, not hindrance. This help should take the form of ready access to extensive training and reference materials. By signing up to a register, the experts should make a commitment to be trained and to take their responsibilities seriously. There should be different categories of membership of the register, to allow those starting on this type of work to gain some recognition and begin to work their way up the ladder in an affordable and supportive way.

More experienced experts who have been on a register for some time should have to go through a revalidation process from time to time. The whole process should be transparent and accountable.

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Efficiency from eDisclosure

BY CRAIG EARNSHAW AND NICK ATHANASI | FTI CONSULTING

2010 is going to be an exceptionally busy year for litigators with a number of large, public-interest cases heading to court. Issues of cost are also likely to dominate. For some companies seeking justice, cost is often perceived as a deterrent in the current economic climate. For others, the financial downturn has made them even more litigious. Meanwhile, Lord Justice Jackson's year-long review of the costs of civil litigation could see new methodologies and approaches emerge in 2010.

Adding to the cost of litigation is the disclosure of data in electronic format which has, according to LJ Jackson, become "prodigiously expensive". The reality is that any company, of any size, can be asked to turn over data on emails, intranets, accounting systems, databases, USB drives, memory sticks and the like – all are admissible in court. As a consequence, the hunt for documents that could prove or disprove a case, be it litigation or arbitration, has got much tougher.

Now, litigation cases involving electronic data have a 2008 judgment ringing in their ears (Digicel (St. Lucia) Ltd & Ors v Cable & Wireless Plc & Ors 2008 EWHC 2522 (Ch) 23 October 2008). Here, in a case brought by Caribbean mobile phone company Digicel, a judge ordered searches of electronic documents to be restarted from scratch, using wider criteria and a larger number of sources. For the defendant, communications giant Cable & Wireless, the upshot was massive additional costs. The ruling set the tone for future litigation by encouraging greater collaboration between parties on the scope, process and methodology for disclosure.

The case also raised the profile of technology in electronic data searches. eDisclosure (electronic disclosure) technologies can whittle down enormous volumes of electronic data into the morsels that really matter. Instead of lawyers poring over mountains of documents, technology handles the mundane, costly, data-intensive side of the search, making the process much quicker and cheaper. Lawyers can then get on with the value-adding, analytical side of scrutinising honed data for relevance and materiality.

Identifying and Collecting Data

So how efficient is eDisclosure?

It depends on how well you manage the process. For instance, bringing together lawyers and forensic technology consultants early on makes for a more collaborative and efficient process.

Technology experts, with their individual competencies and knowledge, can contribute from the outset, working with the company's IT department and legal team to meet the data disclosure needs. They can quickly pinpoint sources of information required by the legal team within corporate systems and preserve them. Their input keeps the investigation on track and avoids unnecessary costs. Good communications between the parties help to focus the process and to reduce the risk of duplication or erroneous pursuit of information.

Consultation in this initial phase can help to identify IT systems, hardware and individuals for investigation. It also means that informed decisions can be made about whether to preserve only data in certain locations or all of it. The first approach means sitting down with the people whose data is being reviewed to understand where it is saved. It can be time consuming but targeted; it preserves a smaller volume of data but demands upfront understanding about the nature of data that is likely to be integral to the case. A wholesale preservation approach is quicker but may preserve more data than is needed. In a collaborative environment, these decisions are based on how much knowledge there is about the data to be collected. It is a vital first step in reducing data volumes and, by implication, costs.

Technology, of course, speeds up the process of identifying and extracting data from corporate systems. Technology can be used to recover data deleted from PCs or to resurrect historic data from back-up tapes. It can filter out files by type, eliminating, for instance, those that are not user-generated but which make the computer and its applications run; it can identify graphics or sound files and exclude them if they are unlikely to be relevant; it can root out files that exist in multiple locations and keep just one copy for review.

Now, with advancements in technology, the contents of more complex databases – such as accounting, bank trading and settlement systems – can be routinely preserved, reviewed and disclosed cost-effectively, without manual and labour-intensive intervention.

However, this is not just about responding when a situation arises but also about being prepared. Companies can catalogue their in-house systems and develop procedures and protocols to locate and preserve relevant documents. They can develop an IT estate map to identify what information is stored where within the organisation and who is responsible for it. They can ensure that growth, mergers and acquisitions do not compromise procedures for backing-up and controlling data. They can establish document management, retention and destruction policies. In short, they can proactively control their data and can lay their hands on what they need, when they need it.

Reviewing Data

Typically, it is the lawyers' time, not technology that is the most costly part of a document review exercise. eDisclosure helps to reduce overall costs and time by using technology to whittle down millions of documents to a fraction of their original number. Now, when lawyers get involved, they can make effective use of their time and skills by reviewing the most pertinent documents.

Even at this manual review stage, technology has an important role to play. Filtering can further pinpoint documents for inclusion by:

- De-duplication: identifying multiple instances of identical emails and documents so that only a single copy is retained.
- Near de-duplication: identifying and removing all but the last message in a thread of emails.
- Keyword and date-range searches: identifying documents with certain keywords or strings of keywords. These can be further refined by date range and named contact.
- Criteria scoring: documents are scored according to the number of criteria they meet to hone in on "hot" documents more quickly.
- Language identification: assigning foreign-language emails to appropriate foreign-language speaking lawyers as part of a review workflow.

Technologies that cluster similar documents by concept can significantly increase the efficiency of the document review. Clustering works by bringing together similar documents so that there is a theme and sequence to the content being read. This helps the brain to make quicker decisions – to keep or eliminate – because the train of thought is maintained throughout. A lawyer who takes a linear approach, reading one email after another regardless of topic, can make around 300 document decisions a day. However, when documents are clustered by concept, lawyers are typically three to five times more productive and can even make decisions on up to 2,000 documents in a day.

Seeding is a technique which plants a relevant document, such as a whistleblower's letter, into a document set. Acting like a magnet, it attracts other similar documents when clustering techniques are applied.

The review process can be made more efficient by using technology to model the existing working practices of the legal team. Mapping workflow processes to how lawyers usually work, rather than requiring them to adapt to the technology, means there are no major learning curves or shifts in routine. Automated quality control can be built into the process to check on the output of the review team. It improves efficiency by requiring that every element of the review is completed before the next batch of documents is opened.

Furthermore, as electronic document review is increasingly internet-based, reviewers no longer need to be geographically close to their clients. The initial document review can be outsourced, either domestically to locations where lawyers' salaries are lower and office rental cheaper or, subject to satisfaction of data privacy requirements, to other jurisdictions – such as India, South Africa or Canada – which, subject to data protection restrictions and appropriate management of the process, can deliver significant efficiency gains and cost savings.

The Future for Electronically Stored Information

In litigation, the Digicel case gives clear guidance about practical approaches to eDisclosure. It criticises unilateral decision-making and directs parties to set adversity aside in the interests of efficiency. It encourages them to engage in early case management conferences to determine the scope and methodology for the eDisclosure process and to contain costs.

Already parties are beginning to confer and agree on the format for producing and disclosing data. Using the same format makes the process more cost and time-efficient for both sides when data is exchanged and converged.

Shared document databases are also likely to make a debut. They will give access to common areas where data is posted for review by both parties while maintaining secure segregation. Although a significant cost saver,

sharing a document review platform in this way will require a considerable leap of faith by both parties. A more palatable starting point might be for parties to use a shared system only at the point at which documents are disclosed.

LJ Jackson, in his Civil Justice Costs Review, acknowledges the need for consensus and greater collaboration between parties. As he weighs the dilemma of cutting the cost of litigation while delivering better disclosure, he might want to take note: A traditional linear electronic document review, going through document by document, will see around 15 percent of costs spent on technology and 85 percent on lawyers' time. Moving to an eDisclosure platform that uses concept-clustering techniques means technology rises to 20 percent of overall costs yet lawyers' time drops to just 20 percent of the overall cost; effectively cutting the cost of the review process by 60 percent.

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Tackling Bribery and Corruption: The Serious Fraud Office, Self-Reporting and the Bribery Bill

BY JEREMY COLE AND MICHAEL ROBERTS | LOVELLS LLP

This article looks at recent enforcement trends and, in particular, the Serous Fraud Office (SFO)'s attempts to emulate the culture in the US where corporates routinely "self-report" instances of bribery and corruption in exchange for more lenient treatment. We also examine the compliance requirements increasingly expected, by both regulators and prosecutors, in this field.

After years of relative inactivity, the UK authorities are talking tough on overseas corruption. The Attorney-General, Baroness Scotland, recently commented that the UK authorities would soon be giving their aggressive US counterparts a "real run for their money". She indicated that the coming year will see a "step change" in the UK's record on financial crime. Recent press leaks indicating that the Serious Fraud Office may be seeking an eye-watering £500 million to £1 billion from BAE Systems suggest that the authorities are determined to make good on this promise.

Whatever the outcome with BAE Systems, 2009 will already be remembered as a watershed in the UK's enforcement record. The year began with action by the Financial Services Authority against AON Limited in relation to its engagement of overseas brokers and, amongst other things, subsequently saw the first successful prosecution of a UK corporate for overseas corruption. With tough new legislation currently before Parliament in the shape of the Bribery Bill, anti-corruption is set to be an increasingly important aspect of any corporate or financial institution's compliance programme.

UK Bribery Bill

At the heart of the Government's initiative to tackle bribery and corruption is the Bribery Bill. Existing UK anti-corruption legislation is contained in a patchwork of Acts dating back to the late nineteenth century which are widely

acknowledged as being out of date and in need of reform. As a result of the deficiencies in the current law, bribery and corruption issues are often prosecuted as accounting or money laundering offences. After more than a decade of failed attempts at reform, the Bribery Bill was formally introduced into Parliament in November 2009, and the Government seems set on trying to get it through Parliament before the General Election.

One of the most significant aspects of the Bill is a new offence for businesses where bribes are paid on their behalf, whether in the UK or overseas. Following the recommendation of the Parliamentary Committee responsible for scrutinising the draft Bill, this offence will not require the prosecution to prove negligence on the part of the business organisation itself. If it makes it onto the statute books, the offence is instead likely to be one of strict liability. As a result, the organisation would itself be guilty of a criminal offence, where a bribe is paid on its behalf by an employee, agent or subsidiary, subject only to a defence of "adequate procedures designed to prevent bribery". In other words, the onus would be on the organisation to show that the failings were not systemic.

The Government has, however, offered business something in exchange. In place of the negligence requirement, the prosecution must now prove not merely that a bribe was paid in connection with the company's business, but that it was paid with the intention to obtain or retain business for the company itself. This new requirement may go some way to assuaging concerns about the breadth of the offence in terms of the company's liability for the actions of its agents and subsidiaries. This is particularly important in scenarios, such as JVs and minority shareholdings, where the organisation will not necessarily have any practical control over the relevant entity.

Different Regulators

In one sense, the new proposed corporate offence reflects the position which already applies in the financial sector under the Financial Services Authority's (FSA) Principles of Business. Principle 3 provides that a regulated firm "must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems".

In January 2009, the FSA found AON Limited to be in breach of this Principle by failing to take reasonable care in establishing and maintaining effective systems and controls for countering the risk of bribery and corruption in the context of its use of third party brokers operating in high risk overseas jurisdictions. AON Limited was subject to a penalty of £5.25 million. Significantly, this was without the authorities having to prove the commission of any actual offence of bribery.

The AON decision was the first time the FSA has used its regulatory powers in respect of bribery and corruption, which have traditionally been seen as the domain of the Serious Fraud Office. Ironically, whilst the FSA has been stressing its determination to "make full use of [its] criminal prosecution tool in the interests of gaining maximum deterrent effect", the SFO has attracted criticism in some quarters for increasingly focusing on civil settlements and penalties.

SFO Guidance

In late July 2009, the SFO issued guidance outlining how it intends to deal with overseas corruption, and particularly how it intends to respond to companies which "self-report" instances of bribery and corruption. The chief incentive for companies to come forward is the indication that "wherever possible" the SFO will seek a civil settlement rather than a criminal prosecution. For many businesses this will be key as it avoids the mandatory disbarment from public procurement which results from a conviction under EU law. In addition, companies who self-report will be given the

"opportunity to manage...the issues and any publicity".

As well as offering a carrot for self-reporting, the SFO has stressed its intention to wield the stick against those who do not come forward voluntarily. The decision not to self-report will be treated as a "negative factor", and the SFO has emphasised the "considerable publicity and disruption to the business of the corporate" which will result from them then deploying "all tools" at their disposal. They have stated that the chances of a criminal prosecution will then be "high", and have also hinted that they would then be more likely to look at the position of individual directors.

To Plea or Not to Plea?

The SFO is at pains to emphasise that, in contrast to past years, it poses a genuine threat to those who commit offences of bribery and corruption. In particular, it has stressed the "serious prospect" that, in the absence of a voluntary disclosure, it will still learn about the issues from another source, such as a "whistle-blowing" employee or competitor, or a Suspicious Activity Report under money laundering legislation.

At this stage, the SFO guidance is still relatively fresh, and it remains to be seen quite how it will be operated in practice. Inevitably, despite the guidance, there is still uncertainty about how the authorities would respond in any given scenario. The SFO freely acknowledges that it cannot give an "unconditional guarantee" that, depending on the precise circumstances and the degree of wrongdoing on the part of the company and its senior management, it would not still pursue a criminal prosecution.

Mabey & Johnson

This is illustrated by the recent case of Mabey & Johnson, the British manufacturer of steel bridges. On 7 August 2009, the company pleaded guilty to two charges of overseas corruption relating to payments made to influence officials in Ghana and Jamaica when bidding for public contracts. Significantly, this was the first ever prosecution of a UK corporate for overseas corruption. Equally of note, however, is the fact that, despite the company making a voluntary disclosure following an internal investigation, the SFO decided that a civil settlement would not be appropriate.

Nevertheless, the SFO has still sought to use this case as an illustration of the benefits of a voluntary disclosure. In particular, Richard Alderman, Director of the Serious Fraud Office, has stated that Mabey & Johnson's cooperation "enabled this case to be dealt with in just over a year and is a model for other companies who want to self report corruption and have it dealt with quickly and fairly by the SFO".

AMEC plc

More recently, the SFO did choose to pursue a civil settlement in the case of AMEC plc. Following an internal investigation into the receipt of irregular payments, AMEC also made a voluntary disclosure to the SFO. The SFO concluded that the manner in which the payments had been entered in AMEC's books and records amounted to a violation of the accounts provisions of the Companies Act 1985. As part of a civil settlement, AMEC agreed to pay approximately £5 million plus costs. According to the SFO, the penalty might have been far greater if AMEC had not "acted promptly and responsibly in referring the case".

Plea Negotiations

In addition to the other incentives for "self-reporting", the SFO's guidance indicates that, if it does conclude that a

civil settlement is inappropriate, it "would be prepared to enter into plea negotiation discussions within the context of the Attorney-General's Framework for Plea Negotiations".

Plea negotiations are not intended, at least officially, to permit US-style "plea bargaining" where the sentence is negotiated and set up-front in exchange for the defendant's guilty plea. The sentence will always remain at the discretion of the judge. Nevertheless, "plea negotiations" may still allow the company to have some impact on the framing of the charges and to agree, at least with the prosecution, broad parameters for the appropriate sentence.

In a bribery and corruption case, this is likely to include not only financial reparation, but remedial steps to overhaul the company's compliance and monitoring procedures. As has been common for some time in the US, that is increasingly likely to include the appointment of an external monitor (at the company's expense).

Plea negotiations, in the context of a cooperative dialogue with the SFO, may also allow a company to retain greater control over the PR aspects, and particularly to avoid the reputational damage associated with a lengthy trial in the Crown Court.

Notification Requirements

In the case of financial institutions, the question of self-reporting also has to be viewed in the context of the notification obligations under FSA Principle 11 and SUP 15. Those provisions will in many cases impose a positive obligation to self-report, rather than merely provide an incentive for doing so. Financial institutions may well then find themselves having to deal with two different authorities, with different powers and ways of working. This is of course in addition to any overseas regulators who may then be notified by the SFO.

"Adequate Procedures"

The climate in the UK has clearly shifted, and the renewed vigour on the part of the authorities to combat overseas corruption looks set to continue. If the draft Bribery Bill makes it onto the statute books in anything like its current form, the prospect of further enforcement activity is only set to increase.

In such an environment, businesses are well advised to review their systems and procedures to ensure that they have the best prospect of meeting the "adequate procedures designed to prevent bribery" defence to the new corporate offence. Regulated entities in any event need to ensure that they meet the standard expected by the FSA under Principle 3. In both cases, the precise requirements will depend on the nature of the entity's business. Nevertheless, subject to an appropriate risk assessment, both the FSA and the SFO are likely to expect similar procedures for, amongst other things, internal training and certification, the vetting and monitoring of third party agents, and regular checks and auditing to ensure that policies and procedures are actually complied with in practice.

When issues do come to light, companies in this jurisdiction will increasingly be faced with the critical decision whether or not to make a voluntary disclosure to the authorities. Whilst that will always be an uncomfortable decision, the SFO is increasingly making a case for the merits of "self-reporting".

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Plea-bargaining: The New Regime

BY SHANE GLEGHORN AND JULIE SIMPSON DAY | TAYLOR WESSING LLP

The FSA has been lobbying for some time for statutory powers to use the promise of lesser sentences or, in appropriate cases, immunity from prosecution for co-operating witnesses, in order to obtain successful outcomes in market abuse cases. Certain prosecutors, including the Serious Fraud Office, the Department for Public Prosecutions and tax officials, have already been afforded such powers on a statutory basis in their capacity as "specified prosecutors" under the Serious Organised Crime and Police Act 2005 (SOCPA). In the US, the SEC has similar powers to encourage "whistleblowers". Although the FSA has made it clear that it is unlikely to make frequent use of this kind of statutory power, it believes that (as has been the case with the SEC) it will assist greatly in some cases.

This has now been achieved through the Coroners and Justice Act 2009 (the "Act"), which received Royal Assent on 12 November 2009. Although not yet in force and the implementation date has yet to be decided, Section 113 of the Act amends SOCPA by adding the FSA (and the Secretary of State for Business, Innovation and Skills ("BIS")) to those prosecutors permitted to use the powers under sections 71 to 74 of SOCPA. Those powers include:

- Powers to grant immunity from prosecution and provide undertakings regarding use of evidence (sections 71 & 72);
- Power to prosecutors to enter into an agreement for the defendant to provide assistance to the prosecutor in relation to an offence and power to the court to take that into account when determining what sentence to pass on the defendant (section 73); and
- Power to refer any case back to court for re-sentencing where the defendant reneges on any such agreement (section 74).

The possibility of the FSA reaching immunity agreements with informers is clearly a welcome addition to the enforcement tools of the FSA. Indeed, Mr Hector Sants, Chief Executive, FSA (who recently tendered his resignation), reportedly commented in evidence to the Treasury Select Committee on the FSA Annual Report in November, 2009: "I think, broadly speaking, we do now have all the powers we need and we are very determined to make sure that they are fully utilised – plea bargaining being a key one. As we have observed here before, when you look around the world, plea bargaining is a vital ingredient of success in insider dealing cases and that power will make a visible difference to our ability to deliver credible deterrents." (Uncorrected transcript of oral evidence of Mr Hector Sants, Chief Executive, Financial Services Authority to the Treasury Select Committee regarding the Financial Services Authority Annual Report on 25th November, 2009.)

It is worth noting, however, that a significant curb on the extensive use of the power afforded to the FSA (and the Secretary of State for BIS) to grant such immunity, is that immunity may only be given with the consent of the Attorney General. It is also clear that although these additional powers add to the FSA's armoury, such powers do not always match those that the FSA's US counterpart, the Securities and Exchange Commission (SEC), can command. The SEC (in conjunction with the FBI) has the ability to employ aggressive surveillance techniques against those indulging in insider trading; most notably through the use of wiretaps. In the recent case of billionaire

Raj Rajaratnam of Galleon Group, arrested for alleged insider trading in October 2009, for example, it is clear that substantial evidence was collected from telephone calls between suspects who were unaware that their calls were being recorded.

In the UK, the Regulation of Investigatory Powers Act 2000 ("RIPA") provides the FSA with enhanced powers of surveillance and it is able to "monitor, observe or listen" to suspected insider traders (section 42(2)(a), RIPA). An express prohibition on the interception of communications sent via post or the telecommunication system, however, prevents the use of wiretaps (section 1(1), RIPA). The FSA may face substantial difficulties in obtaining hard evidence in the form of recorded conversations, therefore, unless such calls take place on employees' recorded lines.

Although the FSA requires, with the aim of minimising market abuse, that FSA-regulated firms record all telephone conversations and electronic communications with an exemption for mobile devices (paragraph 2.33, FSA Policy Statement 08/1: Telephone recording: recording of voice conversations and electronic communications), and retain them for six months, it has not called for wiretapping powers akin to those of the SEC.. Although the FSA is currently reviewing the mobile device exemption, this is still unlikely to be as effective an enforcement weapon as wiretapping, given that insiders are unlikely to use mobile phones that they know are being recorded.

As to how the new powers that the FSA has been granted should be exercised, under Section 75B of SOCPA, the Attorney General may issue guidance to specified prosecutors such as the FSA. In 2008, The Financial Services and Market Legislation City Liaison Group Enforcement Committee (the "Committee") made a number of proposals for the amendment of the FSA's Enforcement Guide regarding the operation of a leniency factor in Section 12.8(12A), whereby the FSA would take an individual's co-operation into account in deciding whether to prosecute the individual for market misconduct or bring market abuse proceedings against them. These suggestions were eminently sensible and would seem to be equally relevant to the exercise of statutory powers that will be available to the FSA when the amendments to SOCPA described above come into force. The Committee believed that guidance was required as to how a decision to offer leniency would be taken, including the timing of the decision to offer leniency. In particular, it called for guidance addressing, for example, the following:

First, the general principles to be applied including: (i) advising the offender of their right to seek independent legal advice; (ii) requiring the offender who reaches an immunity agreement with the FSA to admit fully their own criminality and provide investigators with all relevant information available to them; (iii) requiring any agreement to be in writing; and (iv) assessing the strength of the prosecution case with and without the information from the offender, taking into account the following factors:

- the seriousness of any offence(s) to which the information to be provided relates and the seriousness of any offence(s) which the potential witness might have committed;
- the importance and value of the evidence/ information to be provided;
- whether it is possible to obtain such information from another witness, or in another manner;
- the strength of the prosecution case without the evidence the witness is expected to give; and, if some other charge could be made against the defendant without that evidence, the extent to which that other charge would reflect the defendant's criminality;
- the impact of the witness's expected evidence on the prospects of conviction in the case taken as a whole;
- the criminal history of the witness and details of contacts with the police in order to assess credibility;
- whether there are other indicators tending to confirm that the evidence of information that the witness

might give is true;

- the number and circumstances of any such agreements with the witness in the past; the expectation of a discount in sentence should not be seen as a licence to continue to commit offences; and
- whether the interests of justice would be better served by obtaining the proposed evidence or by the conviction of the person with whom it is proposed to make an agreement.

Second, that a report should be prepared setting out the quantity and quality of the assistance given and any results arising from it.

Third, that where leniency has been given as a result of the assistance given or offered this fact will normally be stated in the final notice.

Finally, that all leniency agreements will contain a statement of truth by the witness and that the agreement can be rescinded if it can be demonstrated that the information is false, with the potential prosecution of any false statements.

As the Committee found, such guidance would incorporate important protections for both the accomplice and the accused, and that such guidance, if followed, would reduce the risk of FSA failing to obtain a conviction on the basis of accomplice evidence.

Overall of course, while such statutory powers regarding the granting of immunity by the FSA are welcome, they are only likely to be effective if informers feel there is a real danger of conviction if they do not co-operate. In his evidence to the Treasury Select Committee, Hector Sants addressed this point, stating: "We currently have enough capacity to handle roughly five, or six, or so complex criminal cases in 12 months, but that capacity is being put in place to deal with expected demand from the supervisors...We do not have cases sitting there that we would like to prosecute that we are not prosecuting because we do not have enough capacity in our integrated enforcement area. ... Insider dealing prosecutions is a very specialised area. We have built up a strong team now and we expect to see a steady stream of cases coming through the court of ever greater complexity. We acknowledge that true deterrence is going to require successful prosecutions of complex cases, with the judges, hopefully, delivering a strong message through the sentencing process, and we would expect that to happen." (Uncorrected transcript of oral evidence of Mr Hector Sants, Chief Executive, Financial Services Authority to the Treasury Select Committee regarding the Financial Services Authority Annual Report on 25th November, 2009.)

Whether his projections are borne out, remains to be seen. It would now appear that the FSA has most, if not all, of the tools it requires to prosecute insider trading cases, but it would be interesting to see if there are any moves to acquire the wire-tapping powers which the SEC have at their disposal.

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Corporate Investigations

BY REBECCA PALSER | THE RISK ADVISORY GROUP

In today's economic climate, there is an ever increasing need to engage corporate investigators. A brief review of today's headlines illustrates just that.

The breadth of services that corporate investigators offer is impressive. They can help corporate lawyers, litigators or dispute resolution lawyers at almost every point in the process – and therefore their clients. In-house lawyers have very different needs but they can assist them too in conducting internal investigations. And yet, there are some lawyers who have never met a corporate investigator, let alone engaged one.

This article provide some insight into the services a good corporate investigator can provide and dispel a few of the myths that plague the industry.

What Can They Do?

The UK press is reporting that reported fraud topped £2 billion in the past year, with some claiming that this is likely to soar to more than £5 billion in the next couple of years. There are still stories appearing about the collapse of the Ponzi schemes made famous by Madoff and Stanford. And the Icelandic banks are in the midst of lengthy investigations into possible Enron-style scams. That's not to mention the financial difficulties in the Middle East that most recently have shaken Dubai World and the bitter dispute that has toppled the business empire of one of the region's richest men. Or indeed, the numerous lengthy investigations launched by the DOJ and the SEC into alleged breaches of the FCPA or enquiries launched by their counterparts in other countries into allegations of bribery.

Corporate investigators can – or already are – helping in all of these cases and many more that haven't hit the headlines. But the cases needn't be so grand and, in fact, you needn't be in the throes of a dispute at all.

Put simply, if you have a question, corporate investigators should be able to help you to answer it, whether that question is one that has a bearing on whether or not to litigate, such as: Is it worth suing this company? Do they have any assets? How will the other side react to discussions about a settlement? Or whether it goes to the essence of whether or not you can prove your case, such as: Is there any evidence of fraud? Is the whistleblower right, has my employee been paying kickbacks? Is the witness lying? Or just a plain and simple: What on earth happened here?

How Do They Do It?

It depends who you talk to. Some like to maintain an air of mystery about their methods. Others will try to explain it to you in straightforward terms to make you feel more at ease. More often than not, the answer is a rather evasive "it depends on the problem".

A good investigator has plenty of tools at his or her disposal. They are too numerous to discuss in detail here but the public record is – for the most part – the first port of call. To the uninitiated this can include corporate records, litigation filings, credit information, bankruptcy records, property ownership information, the telephone directory – you name it, they'll search it and nobody will know.

Anyone can access this information but what the corporate investigator brings is an unnerving familiarity

with all of these sources and, most importantly, a nose for what is normal and what is not. Combined, these two things mean that it is often quicker and more effective to instruct an investigator to plough through the reams of information and read their report, rather than to do it yourself.

What do you do, though, where the public record isn't reliable, is non existent, or doesn't get you close enough to the problem? It's in cases like this when corporate investigators really come into their own. They have access to people, sources and contacts and best of all, they know how to get information from them. We all know that the rumour mill or water cooler chat is very often on the money. Corporate investigators can help you tap into that. They can provide you with indirect access to their established network or help you develop a particular source to gather the evidence you need. While this information might not be admissible in court, it may lead you to something that can be, or alternatively just influence your strategy.

Their arsenal of tools extends even further, though, and, if you don't mind people knowing that you are investigating, companies' books and records are a mine of information, as are its employees, both of which investigators can help you to access. That is to say nothing about the information that can be retrieved from servers, computers, mobile telephones, blackberries or just about any other electronic device or the many other tricks of the trade.

What will be suitable will depend on the circumstances and a good corporate investigator will take the time to understand the background and discuss the options with you. The more information you can give them, the more beneficial this process will be.

Conclusion

So next time you need help, give them a call. Ask them questions. You never know, instructing them and working in partnership with them could be the difference between identifying the wrong-doer; settling the case on the best possible terms; winning that case in court – or not.

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FRANCE

Recent Developments in French Arbitration Case Law

BY BERTRAND DERAINS | DERAINS & GHARAVI

French arbitration law is based on the premise that arbitration is a normal, if not a privileged way, of settling international commercial disputes. Accordingly, French courts, in particular the Paris Court of appeal and the *Cour de cassation,* have built up over time a coherent set of case law aiming to ensure the "effectiveness of arbitration" (C. cassation, 1ère Ch. civ., 7th June 2006, *Jules Vernes,* Rev. arbitrage 2006, 945). They have done so through the creation of substantive rules applicable to international arbitration, such as "the principle of validity of the convention to arbitrate" (C. cassation, 1ère Ch. civ., 5th January 1999, *Zanzi,* Rev. arbitrage 1999, 260). These rules tend both to strengthen and extend the enforceability of the arbitral clause and to facilitate the enforcement of the arbitration award.

The Enforceability of the Convention to Arbitrate

In line with their judicial policy favouring arbitration, French Courts long ago inferred from the principle of autonomy of the arbitral convention that it was not governed by the law applicable to the contract, in which it is included, but rather by a substantive rule providing for the validity of the arbitral clause. This principle, referred to for the first time by the *Cour de cassation* in 1972 (C. cassation, 1ère Ch., 4th July 1972, *Hescht,* JDI 1972, 843), in order to ensure the efficiency of international arbitration clauses at a time when French law was reticent to arbitration in domestic matters, has been recently restated in *Jules Verne,* by the *Cour de cassation,* which stated that "the principle of validity of the international convention to arbitrate and the principle that the arbitrator may rule on his jurisdiction are substantive rules of French international arbitration law which establish on the one hand the lawfulness of the convention to arbitrate independently from any reference to a national law and, on the other hand, the efficiency of arbitration by allowing the arbitrator, when his jurisdiction is disputed, to rule first…"

Recourse to the creation of substantive rules applicable in international arbitration, in favour of the efficiency of arbitration, has recently known a new development with the *Cour de cassation*'s decision in the *Soerni v Air Sea Broker* case. The *Cour* held that the validity of a company undertaking to arbitrate is not assessed by reference to a national law but rather by application of a substantive rule inferred from the principle of validity of the arbitral convention based on the common will of the parties, the requirement of good faith, and the legitimate belief in the power of the convention's signatory to enter in a binding ordinary management agreement on behalf of the company (C. cassation, 1ère Ch. civ., 8th July 2009, Rev. arbitrage 2009, 529).

Recent decisions have also addressed and illustrated the principle of *Compétence-Compétence*. Under the

French conception of arbitration, the principle has two aspects: the first one, usually referred to as the *effet positif,* allows arbitrators to rule on their jurisdiction when it is disputed, either because the convention is allegedly void, voidable or would not encompass the issues at stake; the second aspect, referred to as *effet négatif,* precludes national courts from examining the validity or applicability of the convention prior to the arbitrators, except when the convention is obviously void or inapplicable. National courts have final control of the arbitrators' jurisdiction, but only at the annulment or enforcement stage.

In *DMN Machinefabriek BV,* the Cour de cassation recently disproved the decision by a Court of appeal assessing jurisdiction on a dispute between a distributor and its past supplier based on alleged breaches by the latter in negotiations for the renewal of their expired contract. The observation by the *Cour* that the claim had a tort nature and was based on a breach of negotiations without direct links with the contract was not enough to demonstrate the obvious nullity or inapplicability of the convention to arbitrate (1ère civ., 25th April 2006, Rev. arbitrage 2008, 299). In another case (C. cassation, 1ère Ch. civ, *UOP c/ BP France,* 20th February 2007, Rev. arbitrage 2007, 775), the *Cour*, referring to both the principle of *Compétence-Compétence* and Article 1493 of the French Civil Procedure Code which provides for the jurisdiction of the Paris *Tribunal de grande instance* to assist in case of difficulties in the constitution of the arbitral tribunal, found that the existence in the same agreement of two arbitral conventions referring to two different arbitration institutions did not sufficiently demonstrate the obvious inapplicability of the parties convention to arbitrate since the absence of intention to arbitrate was not established and the parties had not referred to the *juge d'appui* which has sole jurisdiction for solving difficulties in the constitution of the arbitral tribunal. A few months earlier, the Cour had decided that the juge d'appui could not, without breaching the principle that arbitrators have calendar priority in the assessment of their jurisdiction, deny a request to appoint an arbitrator on behalf of a party, on the ground that the contradiction resulting from the presence in the same document of clauses providing for the jurisdiction of both arbitration and national courts was a serious difficulty preventing the intervention of the judge in a summary proceeding (C. cassation, 1ère civ., 14th November 2007, *SIAL c/ Vinexpo,* Rev. arbitrage 2008, 453).

French courts can no longer assess jurisdiction on the ground that the dispute does not clearly enter in the scope of the arbitration convention. The French *Cour de cassation* held that a convention providing for arbitration of disputes relating to the interpretation or enforcement of the contract was not obviously inapplicable to a claim that the contract was void (1ère Ch. civ., 12th December 2007, *Prodim c/ Lafarge,* Rev. arbitrage 2008, 677) or a convention limited to warrantees was not obviously inapplicable to calls of share (1ère Ch. civ., 9th july 2008, *Sté Océa c/ Bouet,* Rev. arbitrage 2008, 677) and thus that the issue of jurisdiction should have been referred to an arbitral tribunal.

For similar reasons, the *Cour de cassation* ruled that the sole fact that a convention to arbitrate was binding on only part of the parties implicated in a litigation, hence that enforcing the convention would prevent examining all parties to the contractual relationship in one procedure was irrelevant, since those circumstances did not characterise an obvious nullity or inapplicability of the convention to arbitrate (1ère Ch. civ, 23rd January 2007, *Levantina c/ Scala,* Rev. arbitrage, 2007, 279).

The above case law confirms the previous trend of decisions requiring a restrictive application of the notion of "obvious nullity or inapplicability" of the convention to arbitrate. As observed by a commentator, "the simple fact that a national judge examines the elements of the case … shows that he exceeded the limits of a control of the obvious nullity or inapplicability" of the convention to arbitrate (F.-X. Train: observations on Cour de cassation,

1ère Ch. civ., 11th February 2009, Laviosa, Rev. Arbitrage 2009, p. 155)

The International Efficiency of International Arbitral Awards

French law's inclination in favour of arbitration is also illustrated by French courts' tendency to facilitate the recognition and enforceability of international awards in France. An obvious example of this trend may be found in the courts' denial to consider the annulment of awards in the country where they were rendered. That jurisprudence, strongly established in the Hilmarton case (C. cassation, 1ère Ch. civ., 23rd March 1994, *Hilmarton c/ OTV*, Rev. arbitrage 1994, 328) was recently confirmed in the *Putrabali* decisions where the *Cour de cassation* stated that "the international award, which is not linked to any state legal judicial system, is an international decision of justice whose regularity is assessed with respect to the rules applicable in the country where recognition and enforcement are requested" (C. cassation, 1ère Ch. civ., 29th June 2007, Rev. arbitrage 2007, 507).

Two other examples of this trend may be found in the introduction to French law of the common law concept of estoppel and in the limitations brought to the control of awards through verification of their compliance to international public order.

In the *Golshani* case, the *Cour de cassation* ruled for the first time – although it was already a well established principle that a party cannot challenge an award if it did not do so as soon as possible – that the "rule of estoppel" precluded a party who had filed a claim with an arbitral tribunal and participated to the arbitral proceedings without having alleged that the arbitral tribunal had no jurisdiction for issuing an award (C. cassation, 1ère Ch. civ., 6th July 2005, Rev. arbitrage 2005, 993). There from, the concept of estoppel has been used in many occasions: a party that waited one year after expressing doubts about the independence of an arbitrator is estopped from requesting the annulment of the award on that ground (C. Appel Paris, 7th February 2008, Rev. arbitrage 2008, 501); a party is estopped from submitting in the annulment proceeding that it was not invited to comment the methodology of calculation of damages proposed by the other party if it had not complained during arbitration (C. appel, Paris, 28th February 2008, Rev. arbitrage 2008, 712); when the parties have requested the arbitrators to take their agreement on authorising appeal against the award in consideration in the terms of reference, a party cannot, "without contradiction", claim that the convention to arbitrate is void because appeal against international awards is not available under French law (C. cassation, 1ère Ch. civ, 28th May 2008, Rev. arbitrage 2008, 691).

A last example of French courts' favour to arbitration in recent years may be found in the famous *Thalès* decision where the Paris Court of appeal ruled that a breach of international public order justifying the annulment of the award must be "obvious, actual and tangible" (C. appel Paris, 18th November 2004, *Thalès Air Défense c/ GIE Euromissile,* Rev. arbitrage, 2005, 751). This restrictive position, aimed at avoiding the risk of control of the award on the merits, was approved by the *Cour de cassation* in SNF c/ Cytec (C. cassation, 4 juin 2008, Rev. arbitrage 2008, 473).

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The Transmission of the Arbitration Clause under French Law

BY BERTRAND DERAINS | DERAINS & GHARAVI

Traditionally, French courts have favoured assignment of the arbitral convention to parties implicated in the performance of a contract even if they are not party to it. However, while it was easily agreed that the arbitral clause was assigned in the case of change of parties in an agreement, French Courts' doctrine regarding the scope of *ratione personae* of an arbitration clause included in one contract of a chain of contracts is still evolving.

Transmission of a Contract or of Rights Arising out of a Contract

In 1999, the *Cour de cassation,* referring to the principle of validity of the international arbitration clause, ruled that the assignee of a claim *("cession Dailly")* related to a contract with an arbitration clause was bound by the latter even if it had not expressly agreed to the clause (C. cassation, 1ère Ch. civ. 5th January 1999 and 19th October 1999, *Banque Worms* and *Banque Générale du Commerce*, Rev. arbitrage 2000, 85). The Paris Court of appeal, further approved by the *Cour de cassation,* also ruled that "the assignment of a claim or a contract necessarily implies the transmission to the assignee of the benefit of the arbitration clause, which is inseparable of the economy of the initial contract. In international matters, the arbitral clause which is linked to the right to sue rather to material rights, is separable from the contract in which it is included, is governed by specific rules without necessary reference to conflict of laws rules or to a law designated by such rules, and thus, is assigned as an accessory to the contract in which is included or to the right related to the contract"; the *Cour* held that "the validity of the assignment is not affected by defects regarding the assignment of the material right, ..." (C. appel Paris, 25th November 1999, *CIMAT c/ SCA,* Rev. arbitrage 2001, 165, approved by C. cassation, 1ère Ch. civ., 28 may 2002, Rev. arbitrage 2003, 397). The *Cour de cassation* latter held in general terms that an "international arbitration clause is binding on all parties substituted in rights" arising from the contract that includes the arbitral clause (C. cassation, 8 February 2000, *Taurus Film*, Rev. arbitrage 2000, 280).

In accordance with French Courts' policy to favour arbitration and in conformity with a methodology currently adopted in arbitration matters, the assignment of the arbitration clause is therefore governed under French arbitration law by a substantive rule providing for the assignment of the clause with the assignment of the contract or the right to sue arising from the contract. French courts have stated *in dictum* that some very limited circumstances could preclude assignment of the arbitration clause, rarely if ever encountered: the original party establishes that the arbitration clause had been agreed *intuitu personae,* in consideration of the personality of the other party to the contract (C. cassation, 1ère Ch. civ., 28 may 2002 *CIMAT,* Rev. arbitrage 2003, 397); or the assignee establishes that "it reasonably ignored the existence of the clause" (Cour d'appel Paris, 1ère Ch. civ., *Peavey,* 6th February 2001, Rev. arbitrage 2001, 765). Accordingly, the arbitration clause is assigned, irrespective of the law applicable to the contract and its provisions regarding assignment, without any requirement to examine conflict of laws rules, except it can be established that the parties refused the transfer of the clause. Otherwise, since arbitration is seen as the usual way of settling international commercial disputes, acceptance of transfer is presumed. While in 1997, in *Société Carter c/ société Alsthom et AGF* (Cour

d'appel de Paris, 6th February 1997, Rev. arbitrage 1997, 556) the *Cour* had decided that the arbitral clause was binding and could be raised by an insurance company after having partially indemnified its client on the ground of the mechanism of subrogation under French law, the *Cour de cassation* has recently held that, in the context of maritime context, an insurance company could not claim that it was not bound by the arbitration clause because it had not expressly agreed to it on the sole ground that "it is usual to agree to an international arbitration clause in a maritime international transport contract" (C. cassation, 1ère Ch. civ., 22th November 2005, Axa Corporate Solutions c/ Nemesis Shipping Corporate, Bull. civ., n° 420).

Chain of Contracts

By contrast, in a 1990 decision, the *Cour de cassation* ruled that an arbitration clause included in a sale contract was not binding on further buyers of the good sold when they sue the initial sellers on a contractual ground, which is possible under French law, in the case of a succession of contracts providing for a transfer of property (C. cassation, 1ère Ch. civ., 6th November 1990, *Fraser,* Rev. arbitrage 1991, 73), even though in such situation, other clauses of the initial contract are normally binding on successive buyers.

On 6th February 2001, however, the *Cour de cassation* reversed its previous holding in the *Peavey* decision holding that "in a chain of homogenous sales contracts, the international arbitration clause is transmitted with the contractual action, unless there is reasonable evidence that the existence of the clause was ignored" (C. cassation, 1ère Ch. civ., Peavey, 6th February 2001, Rev. arbitrage 2001. 765).

The French position on the transmission of arbitration clauses has further developed in recent years, expanding even more the application of the principle set out in the above decision. In particular, for the arbitral convention to be transmitted, French Courts no longer require that the contracts be homogenous.

In société Alcatel Business Systems (ABS) SA et autre c/ société Amkor Technology et autres, the *Cour de cassation* held that an arbitration agreement is binding on the parties that are directly involved in the performance of the contract (C. cassation, 1ère Ch. civ. 27th March 2007, Rev. arbitrage 2007, 785).

ABS entered into a contract with Alcatel micro electronics (AME), both being part of the same group, for the production of an electronic chip. AME then entered into a contract with Amkor technology Inc. (Amkor) for the provision of electronic components. Their contract provided for arbitration before the American Arbitration Association (AAA) of Philadelphia. Amkor was contractually bound with Anam semiconductor Inc. (Anam), a component maker, by a contract which provided for arbitration before the AAA in Santa Clara California.

The electronic chips made by Anam were sent directly to AME, whom after "encapsulating" the chips, delivered them to ABS. Afterwards, production problems arose and ABC sued both Amkor (and its French subsidiaries) and Anam before the *Tribunal de commerce* seeking payment for damages and interest. The defendants challenged the jurisdiction of the Court by invoking the existence of the arbitration agreement that provided for arbitration before the AAA in Philadelphia.

The *Cour de cassation* approved the decision by the first judge that it had no jurisdiction because of the existence of a *prima facie* valid arbitral clause. The *Cour* held that in a chain of transfer of property contracts, the arbitration agreement is transferred automatically as accessory to the right to sue, which is in itself an accessory to the substantial right transferred.

Accordingly, since *Alcatel,* whether the contracts forming the chain are identical or not is not relevant for the transfer of the arbitration agreement. It is moreover noteworthy that the exception managed in *Peavey* for

the situation where "there is reasonable evidence that the existence of the clause was ignored" is not restated which seems coherent with the principle of an automatic transfer of the clause as accessory to the right to sue.

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Fraud and Corruption Investigations in France – is Change Afoot?

BY ANTHONY CHARLTON AND CHARLOTTE ADAM | FTI CONSULTING

The Association of Certified Fraud Examiners notes in one of its training manuals that "one difficult aspect of white-collar crime and fraud is that it is hidden – we only know the cases that surface". The first step in the process of fighting fraud necessarily implies the uncovering of hidden facts and patterns. In France, a number of legal, economic and social factors set some fairly significant limits on what a professional investigator or organisation can do in the context of an investigation.

This article provides a general overview of some of the key aspects of the current landscape in France relating to fraud and corruption investigations, and highlights a number of major developments likely to have a significant impact.

Reporting Fraud Anonymously is Not Fully Accepted

To use a military analogy, it is extremely difficult to fight an unseen enemy. Whilst other major countries such as the US and the UK have conducted numerous assessments of both the scale and impact of fraud and corruption on their national economies, virtually no such studies have been made to date in France. How then can we uncover what is presently hidden? Focusing on the corporate world, in some countries, companies' internal control systems provide an avenue for employees to report (or "blow the whistle", usually on an anonymous basis) their suspicions of fraud, thus allowing management to conduct an internal investigation.

Whistle blowing can be an extremely powerful tool for uncovering fraud, corruption and wrongdoing. An ACFE study of occupational fraud in the United States concluded that 46% of cases were detected by tips from employees, customers, vendors and other sources (31% of which were made via formal reporting mechanisms such as hotlines). The same report showed that tips were also the most common means of detection in 2002, 2004 and 2006 (Report to the Nation on Occupational Fraud & Abuse 2008, Association of Certified Fraud Examiners). Within the US government, the figures are even more telling. In 2007, the US Government recovered $2 billion related to fraud in USG agencies, of which $1.45 billion – or 72.5% - was associated with suits initiated by whistleblowers under the False Claims Act qui tam provisions ("Justice Department Recovers $2 billion for Fraud against the Government in FY2007; more than $20 billion since 1986", US Department of Justice, November 1, 2007).

On the other hand, whistle-blowing systems can only serve as effective detection instruments if socially accepted as such. In France, evidence points to the contrary. As of now, some 1,346 French companies have Sarbanes-inspired whistle-blowing systems in place ("Le Système d'Alerte Professionnelle de Dassault considéré comme Illégal", Le Point, 8 décembre 2009). Their experience shows, however, that only a tiny number of their employees feel comfortable using

the mechanism *("La Dénonciation Légale peine à s'imposer en France", Le Monde, 9 Novembre 2009, « Le Système d'Alerte professionnelle de Dassault considéré comme illégal », Le Point, 8 décembre 2009)*. Dassault-Systèmes, a leading French corporation with 7,875 employees and 2008 revenues of approximately €1.3 billion, has only registered one complaint since its program began (Dassault Systèmes, 2009 Earnings). The CNIL, the national agency mandated with regulating such systems, noted in its 2007 annual report that French employees are uncomfortable with formal reporting mechanisms and prefer to report wrongdoing through their line managers (Commission Nationale de l'Informatique et des Libertés, 28e Rapport d'Activité, 2007).

This preference can be observed in other European countries, such as the UK, and there certainly are several potential explanations for the reluctance to use such systems in the French context. For instance, reporting wrongdoing or abuse is still reminiscent of the wave of denunciations under the World War II Vichy regime. Commonly referred to as "snitching", there appears to be considerable disdain for the system. Perhaps sensitive to these issues, the CNIL has imposed a number of restrictions on the applicability of these reporting mechanisms in France. In France, the CNIL actively discourages anonymity of reporting.

Specificities of the French Legal Framework for Investigations: Some Obstacles Remain

The legal framework seems to mirror societal anxieties on how to properly expose white-collar crime. The ability to conduct investigations successfully is hindered by several restrictions in areas of civil and criminal law, including in respect of data protection laws, labour and civil law, and laws on privacy. A full discussion of how these laws blunt the tools an investigator has at his disposal is beyond the scope of this article but an example will serve as a useful illustration of the general principle.

In many countries forensic technology has become a virtual industry. Data held on the computers of company employees, suspected of malpractice, can easily be accessed, copied and analysed by teams of investigators, often without the employee being aware; this is especially the case in the U.S. In France, if not handled correctly, such practices are illegal and are deemed to breach the employee's right to privacy – rights which exist even in the workplace. A well-known 2001 court case (Cass.soc., October 2, 2001, Nikon, appeal n°99-42.942) emphasised these rights, with specific reference to documents labelled as "personal", and held on the employee's computer.

Blocking Legislation

Beyond the sphere of employee-related privacy issues, other legal procedures can potentially slow down or in some cases ultimately halt investigations. One such recourse is the *secret défense*. Regimented by the penal code (Article 413-9 du Code Penal, modifié par la Loi no 2009-928 du 29 juillet 2009 – art.12), the *secret défense* authorises the Executive branch (President, Prime Minister, various Secretaries) to classify – and declassify – sensitive documents deemed to relate to national security. Concerns have been voiced around the potentially far-reaching application of the term "national security". In 2008, for instance, Judge Renaud von Ruymbeke abandoned a large-scale corruption investigation involving a large French military contractor, Thales, following several unsuccessful attempts to lift the *secret défense ("Affaires des frégates de Taiwan: non-lieu général", Radio France International,* 1 Octobre 2008). Without a declassification and access to key documents, the investigation reached a dead-end.

Another such piece of legislation is France's "Blocking Statute", Article 1bis of which prohibits individuals and companies from providing foreign authorities with any economic, commercial, industrial, financial or technical information which could lead to the establishment of proof in a foreign-led action or investigation *(Loi No 80-538 du 16 juillet 1980 relative*

à la communication de documents et renseignements d'ordre économique, commercial ou technique à des personnes physiques ou morales étrangères).

The recent US Department of Justice inquiry into Siemens' alleged corrupt practices was the largest such investigation in history, resulting in over €1.1 billion in fines paid to U.S. and German authorities. Despite having a significant presence in France, and being subject to specific allegations (Siemens AG Corporate Communications and Government Affairs, July 30, 2009), the investigation did not extend to Siemens France. Counsel for the company's audit committee determined that the Blocking Statute prevented the investigative team from working in the country. Until very recently, no prosecution had been made in relation to breaches of the Blocking Statute. In December 2007 however, the *Cour de Cassation,* France's Supreme Court, prosecuted and fined a French lawyer €10,000 for attempting to obtain information from a French defendant company in the context of litigation in the federal court of Los Angeles *(Cour de Cassation, Cass. Crim., 12 décembre* 2007, No. 07-83.228). This decision, the first conviction under the Blocking Statute, sent a strong signal to interested observers that France was serious about using a previously dormant piece of legislation to protect privacy around vital pieces of information.

Is Change Afoot?

Many lawyers, non-governmental organisations and other stakeholders cite cultural issues as being core to what Anglo-Saxon audiences often view as inefficiencies. France, however, may be on the brink of significant change. Several reform efforts have been proposed recently which could radically modify the investigative landscape. Obviously, until the exact scope and nature of the reforms is known, we can only speculate as to how the future French landscape will change.

Proposed Introduction of an Expanded Plea Bargaining Procedure

In several countries, self-reporting and/or plea bargaining by individuals and corporations now represent an essential part of the fight against fraud and corruption.

In France, only a limited application of plea bargaining currently exists, extending only to torts liable to less than 5 years of imprisonment. In practice, plea bargaining concerns mainly driving offenses, and does not extend to white collar crime such as fraud and corruption. Under present reform proposals, plea bargaining would extend to criminal offences tried in France's *cours d'assises,* or criminal courts. As elsewhere, as a result of a confession to a crime, a reduced sentence may be pronounced by the judge. The procedure, if implemented into law, would thus extend to serious crimes of corruption and fraud liable to more than 5 years of imprisonment. In France for instance, acts of corruption are liable to 10 years of imprisonment and a €150,000 fine, thus falling under the purview of the *Cour d'Assises* (Article 435-1 of the Penal Code). In contrast to the U.S. where a plea bargain may not lead to trial, in France a trial would still take place. The focus of the debate, however, would shift away from establishing responsibility towards other elements such as the circumstances of the crime and the personality of the defendant.

In many countries, the ability of corporations to volunteer information concerning misdemeanours in return for reduced sanctions and/or fines has opened up access to key information as well as increased the pace at which investigations can be resolved. In the landmark Siemens case for instance, the German company, along with three of its subsidiaries, pleaded guilty in federal court in the United States to various charges under the U.S. Foreign Corrupt Practices Act ("Siemens AG and Three Subsidiaries Plead Guilty to Foreign Corrupt Practices Act Violations and Agree to Pay $450 Million in Combined Criminal Fines", US Department of Justice, December 15, 2008). The plea bargain resulted in the negotiation of a $450 million fine with the Department of Justice (DOJ). The amount of this fine is dwarfed by the

$2.7 billion which could have been levied by the DOJ under the United States' Federal Sentencing Guidelines ("Siemens Agrees to Pay the Largest FCPA Penalty Ever Imposed", December 16, 2008, Ropes & Gray). In this light, plea bargaining represents a significant economic benefit to the company, and provides an incentive to the company to conduct its own investigation with a view to cooperating with regulatory authorities. The DOJ acknowledged that the level of cooperation displayed by Siemens was crucial in resolving the criminal proceedings.

Depending on the form and extent of reforms to plea bargaining procedures, a sea-change may potentially occur in France. One of the pending questions, however, is what stance will be taken on debarment procedures; this is a key issue since the FCPA provides that if a company is found guilty of an offence involving the bribing of an overseas official then the company is automatically blacklisted by certain international financial institutions such as the World Bank. Indeed the willingness of a company to plead guilty to certain charges related to fraud and corruption may depend on the risk that a company may be debarred from future public procurements. It will be interesting to see whether the reforms in France take this risk into account.

Proposed Suppression of the Investigative Judge

A further proposed reform is the suppression of the system of independent investigative judges, instituted by Napoleon Bonaparte himself. Investigating judges have traditionally been in charge of France's more complex and sensitive criminal investigations, including large fraud and corruption investigations. Several reasons have been invoked to justify his disappearance; among these is the argument that his role is "schizophrenic", given he is both an investigator and a judge. The investigative judge acts in an inquisitorial capacity and is mandated to investigate facts to support both the claims of the prosecution and those of defence, adding to the complexity of the role.

In practice, the investigative judge only covers about 5% of all investigations ("La possible disparition du juge d'instruction fait des vagues", Le Figaro, 6 janvier 2009); however, these tend to be the most serious and politically sensitive ones, including major fraud and corruption cases. Arguably it is the judge's very independence that has allowed him to conduct highly sensitive investigations; many commentators doubt, for example, that Government-mandated prosecutors today would initiate a similar investigation to the infamous Elf Aquitaine case of 1991 in which the fearless Eva Joly took on the elite of the French business world and made her name. Whilst we await the precise scope and nature of the reforms, many in the investigation community fear that the end of the *juge d'instruction* will mark a retrograde step in the global fight against fraud and corruption.

On the other hand, one of the arguments in favour of the proposed reform is that it will give more weight to the presumption of innocence on the part of the defendant. Supporters of the proposed reforms argue, for example, that the investigating judge was never truly independent and was often more inclined to find evidence to establish a defendant's guilt. Should the rights of the defence be strengthened under this new scenario, this could very well encourage, or even actively empower, the defence to seek out pre-trial independent private expertise, in contrast with the current landscape where such expertise is rarely used in the context of a trial.

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ITALY

The Class Action in Italy

BY ANTONIO AURICCHIO AND PAOLO PETROSILLO | GIANNI, ORIGONI, GRIPPO & PARTNERS

Law no. 244 on 24 December 2007, introduced, for the first time in the Italian law system, a type of class action for awards of compensatory damages or payments of amounts to multiple individual consumers or users.

This represents an important change for the Italian legal system, where previously consumers and users could seek protection of their rights only through individual actions.

In particular, the class action is regulated by the new article 140 *bis* of the Italian Consumer Code (Legislative Decree n. 206, dated 6 September 2005) and is in force from 1 January 2010.

Entities Entitled to Propose a Class Action

The capacity to start a class action belongs to:

- single consumers and users;
- national consumers associations empowered by them or committees of which they are members.

The action can be brought against any commercial, financial, banking and insurance company, as well as any public or private body, in the interest of the consumers who have been damaged by the same act.

Scope of the Class Action

According to the Italian Consumers Code, the above mentioned entities may ask the Court for damage compensation and refund of the sums due to consumers concerning:

- contractual rights of a plurality of consumers and users who are in an identical situation vis-à-vis the same company, including the rights related to contracts entered into through standard forms and general conditions under articles 1341 and 1342 of the Italian Civil Code (e.g., those stipulated with banks, insurance companies or financial institutions);
- rights of end consumers and users deriving from defective products, regardless of contractual relationship (i.e., product liability);
- rights deriving from unfair trade practices and anti-competitive behaviour.

First Stage of the Proceeding

The claim is started by the service of a writ of summons. The writ is served also upon the Public Prosecutor at the Court in charge, who may intervene only with regard to the judgment on the admissibility of the action.

With a few exceptions, jurisdiction is given to the Court in the capital city of the Region where the defendant has its registered office.

Upon first hearing, the Court shall decide by a certification order on the admissibility of the claim; however, the Court may suspend judgment when there is an ongoing preliminary investigation before an independent Authority on the facts which are relevant to the decision, or a trial is pending before the administrative judge.

The action shall be declared inadmissible if:

- the same is clearly groundless;
- there is a conflict of interest;
- the Court does not find that the individual rights to be protected are identical;
- the proposing party seems not to be in a position to adequately protect the class's interests.

The certification order that decides on the admissibility may be challenged by an interlocutory appeal filed before the Court of Appeal within a mandatory term of 30 days after having been served with the certification order. The appeal against this order, however, does not stay the underlying proceeding before the Court.

If the action is considered inadmissible, the Court decides over the legal costs and may condemn the plaintiff to compensation for gross negligence, as well as order to give publicity of the rejection of the action (pursuant to article 96 of the Italian Code of Civil Procedure).

On the contrary, if the action is considered admissible, the Court orders the most appropriate forms of publicity for the proceeding (i.e., newspapers, websites) in order to allow class members to join it. Public notice is a condition for the prosecution of the claim.

By the same order the Court shall:

- determine the individual rights involved in the proceeding, specifying the criteria according to which individuals seeking to join are included in the class or must be regarded as excluded from the class action;
- establish a mandatory term (not exceeding 120 days from the expiration of the term granted to the plaintiff to give publicity of the existence of the action) by which a consumer or user, who wishes to join the class action, may file a notice with the Court's clerk office, even by the plaintiff. A copy of the order is sent by the Court's clerk office to the Ministry of Economic Development which provides to further publicise the action, including on its website.

Joining the Class Action

Consumers and users who intend to benefit from the collective action may join it, without the need of the assistance of a counsel, within the terms fixed by the Court (as we said, the time period for joining the action may not exceed 120 days from the expiration of the term set for publicity).

Starting or joining a class action implies waiver of any individual restitutory or remedial action based on the same reason. The rights of each consumer and user in the class action are autonomous (therefore waivers or settlements taking place between the parties shall not affect the rights of those who have not expressly consented to them).

The notice to join the action shall indicate all the constitutive elements of the asserted right with the relevant probative documentation. This deed shall be then filed with the Court's clerk office, even by the plaintiff, by the date fixed by the Court.

According to articles 2943 and 2945 of the Italian Civil Code, the lapse shall take effect on the date of service of the writ of summons and, for those who joined later, after filing of said notice.

Proceeding and Final Judgment

By the same order in force of which the Court admits the action, the Court states also the course of the procedure. In accordance with the general principle of *"audiatur et altera pars",* the fair, effective and prompt course of the trial is thereby ensured. By the same or subsequent order, which can be modified or revoked at any time, the Court:

- prescribes measures aimed at preventing undue repetitions or complications in the presentation of evidence or arguments;
- burdens the parties with the publicity considered as necessary to protect rights of the subjects who joined the action;
- regulates the discovery stage and disciplines any other procedural issue, except for any formality which is not essential to the debate.

If the Court admits the claim, by its decision the Court sets out: (i) the final amount to be awarded to each damaged party, pursuant to article 1226 of the Italian Civil Code; or (ii) the criteria to be used in calculating the amount to be awarded or returned.

The decision is enforceable 180 days after its publication.

Appeal and New Class Actions

The decision of the Court of first instance may be challenged before the Court of Appeal within the ordinary term of 6 months from its publication and/or within 30 days of its service.

Should the Court of appeal be requested to suspend the enforceability of the decision, the Court shall also take into account: (i) the total amount of the sum owed by the debtor; (ii) the number of creditors; and (iii) the difficulties in returning undue payments if the appeal is admitted. In any case the Court may order the respondent to deposit the aggregate amount due until the decision becomes final.

The final decision is binding upon the subjects who have joined the class action. On the contrary, subjects who have not joined the class action retain the right to start an individual action.

No other class action may be brought against the same company or entity based on the same facts after the expiration of the terms for joining the action as set by the Court. Actions started within said deadline are automatically joined if pending before the same Court; otherwise, the Court next in charge orders the removal of the trial from the general roll, and grants the parties with a mandatory term (not exceeding 60 days) to reinstate the trial before the first judge.

Comparison with US system

Italian class action differs from US class action mainly from two important profiles.

Firstly, an Italian consumer who joins a class action – charged by an association or a committee – will have to exercise its "opt-in" right. Once the deadline for the opt-in is fixed, it will be impossible to accept the proposition of further actions for the same fact and against the same company or entity.

On the contrary, under the US legislation interested consumers may ask not to take advantage of someone else's action (thus filing their own) by exercising their "opt-out" right, or simply by staying inert, thus taking advantage of others' proceedings.

Secondly, under the US legislation, the adjudgement may be extended to the so called punitive damages, with the aim of punishing and deterring; *vice versa* in the Italian legislation, civil liability has the only task of restoring the damaged or refunding party's assets.

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Recognition and Enforcement of Foreign Awards in Italy

BY ANTONIO AURICCHIO AND PAOLO PETROSILLO | GIANNI, ORIGONI, GRIPPO & PARTNERS

Arbitration proceedings in Italy are governed by the Italian Code of Civil Procedure ("ICCP").

In order to update the procedure and incorporate the terms of several international conventions ratified by Italy, the ICCP was amended by several laws and, finally, by the Legislative Decree No. 40 of February 2, 2006.

The ICCP applies to all arbitration proceedings taking place in Italy (so called "domestic arbitration"), unless otherwise agreed by the parties. The enforcement of domestic awards is subject to an application to the competent national Court where the arbitration has its seat. Upon assessment of the formal requirements of the award, the Court shall issue an execution order (so called *"exequatur"*).

The ICCP also contains provisions regarding the recognition and enforcement of foreign awards, but the main regulation of the international arbitrations is the Convention of New York on the Recognition and Enforcement of Foreign Arbitral Awards, dated June 10, 1958 (the "Convention").

Requirement for the Recognition and Enforcement in Italy of Foreign Awards

As general rule, it is possible to obtain the recognition and enforcement in Italy of a foreign award.

The requirements to obtain the recognition are provided for by the Convention, ratified in Italy by Law No. 62/1968 (no reservations to the Convention have been entered by Italy).

The Convention applies to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought, and arising out of differences between persons, whether physical or legal.

The Convention applies also when:

- parties belong to the same State but the award is issued in a foreign country;
- parties belong to States which have not acceded to the Convention;
- the award is issued in a State which has not ratified the Convention.

The term "award" includes not only the awards made by arbitrators appointed for each case but also those made by permanent arbitral bodies to which the parties have submitted.

Each contracting State must recognise an agreement in writing under which the parties undertake to submit to arbitration all or any disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration in the contracting State where the recognition and enforcement are requested.

According to article 5 of the Convention, recognition and enforcement of the award may be refused, upon request of the party against whom it is invoked, only if that party furnishes to the competent Court where the recognition and enforcement is sought, proof that:

- the parties to the arbitration agreement were under some incapacity, or the agreement was not valid under the law chosen by the parties or, failing any indication thereon, under the law of the State in which the award was issued; or
- the party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or
- the award deals with a dispute not provided for by or 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 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 may be recognised and enforced; or
- the composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was not in accordance with the law of the country where the arbitration took place; or
- the award has not yet become binding on the parties, or 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.

Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds *ex officio* that:

- the subject matter of the dispute may not be settled by arbitration under the law of that country; or
- the recognition or enforcement of the award would be contrary to the public policy of that country.

All the above listed requirements coinciding with those provided for by article 840 of the ICCP.

Procedure before the Italian Competent Court

A party wishing to enforce a foreign award in Italy has to file a petition with the President of the Court of Appeal of the district in which the other party is resident; if that party has no residence in Italy, the Court of Appeal of Rome has jurisdiction.

The petitioner has to supply the original award (or a certified copy), together with the original arbitration agreement or equivalent document (or a certified copy) and a certified translation if these documents are not written in Italian (article 839 of the ICCP).

The President of the Court of Appeal, after ascertaining that:

- the award complies with formal requirements,

- the dispute may be decided through arbitration under Italian law, and
- the award does not contain provisions contrary to public policy, has to declare the award enforceable in Italy.

With regard to the definition of "public policy", it has to be pointed out that usually the party against whom the award is issued invokes the contrast with the public policy in order to avoid the recognition and the enforcement of the award. The arguments brought to this purpose are, for example, the no impartiality of the arbitrators, the inexistence of the grounds for the award, breach of law or breach of the general principle of *"audiatur et altera pars"*. Therefore, Italian scholars and courts make a very prudent use of this concept – sometimes by a strict construction of the same concept – in order to not jeopardise the recognition and enforcement in Italy of foreign awards.

The order issued by the President of the Court of Appeal becomes final if no objections are raised within the term of 30 days.

Challenge of the Award

It is possible to file a challenge against the order granting or denying the recognition or the enforcement of the award, by filing a writ of summons with the Court of Appeal within 30 days from, respectively, the service or the notice of the decree.

The party challenging the order has to prove the existence of one of the circumstances set out in article 840 of the ICCP and coinciding with those provided for by article 5 of the Convention (see paragraph 2 above). If this party proves the existence of one of said circumstances, the Court of Appeal must deny the recognition or the enforcement of the award.

Recognition and enforcement of an arbitral award may also be refused if the Court finds *ex officio* that:

- the dispute may not be settled by arbitration under Italian law; or
- the recognition or enforcement of the award would be contrary to the public policy.

The Court of Appeal may not review the award on the merits but only to ascertain if there are or not the conditions for the recognition and the enforcement of the award.

The final decision of the Court of Appeal may be challenged before the Italian Supreme Court on limited ground.

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Mediation in Civil and Commercial Matters in Italy: The Strong Legislative Push

BY GIUSEPPE DE PALO AND SARA CARMELI | JAMS INTERNATIONAL

In June 2009, the Italian Senate approved an important civil procedure reform (Law 18/2009, No. 69), which also contains rules regulating and promoting recourse to mediation in civil and commercial disputes. These rules have been the subject of a scrupulous debate within the Italian Parliament. Through them, the Italian Parliament seeks to abide by the rules of the European Directive on Mediation of 21 May 2008 (see Directive 2008/52/EC; the "EU Directive"). According to the rules approved by the Italian Senate, the Italian government had to adopt one or more decrees with specific principles and rules within 6 months (i.e., by December 2009). The first of these decrees, approved by the Italian government on October 28, 2009, was the decree to introduce mediation into the Italian legal system. In Italy, mediation will finally play an important role in the settlement of future disputes arising in all civil and commercial matters.

The decree applies to all disputes arising out of civil and commercial issues (Art. 2).

Mediation and conciliation have two different meanings under the new law (Art. 1). Mediation is the *activity* carried out by an *impartial third party* to assist two or more parties to join in an amicable settlement of their dispute or to present a proposal that can settle the controversy. Impartiality and neutrality are the main duties imposed on mediators by law (Art. 14). Conciliation describes the positive outcome of the whole procedure, that's to say the settlement of the disputes after mediation.

The law addresses various aspects of mediation, including procedural rules (Articles 3 to 15); accreditation of mediation organisations (Articles 16 to 19); tax benefits and duty of information (Articles 20 to 21).

Concerning procedural rules, mediation is considered to be an *informal way* (articles 3 and 8) to settle disputes that will be regulated by the internal Mediation Rules adopted by each private or public-sponsored mediation body, registered in the National Register. Professionalism and efficiency are the two main requirements for mediation organisations wanting to appear in the National Register. Separate sections of the Register will be established for specialised mediation bodies that possess, for instance, specific skills in international matters (Art. 16).

All Mediation Rules adopted by mediation organisations will guarantee the confidentiality of the mediation procedure and the impartiality and capability of mediators appointed by the body to carry out a fast procedure (Art. 3).

The procedure must last no more than 4 months (Art. 6) and it is a compulsory step before starting any legal action in the main areas of conflicts: banking, health, insurances, finance, family agreements, co-ownership, leases, and libel. This means that these kinds of disputes have to go through the mediation process before passing through the door of a Court (Art.5).

Lawyers have the duty to inform their clients about the option to use mediation to solve his or her dispute while specifying all tax benefits of the mediation procedure. The information must be provided in writing and signed by the client so it can be joined to the writ of summons. If the document is not joined, the judge will inform the party about mediation. (Art.7)

The judge may suggest to the parties at any point during the proceedings to solve their dispute through mediation.

An important aspect of mediation procedure is now regulated by law. *Mediation confidentiality* is standardised, either during the process (Art. 9) or out of the mediation procedure (Art. 10). All people working for the mediation body have the duty to keep all information received or offered during the mediation process confidential. The same principles apply to information exchanged during private sessions (caucus), where the mediator cannot offer the information to the other party without the disclosing party's permission.

But the more important aspect is the *substantive* protection finally recognised for mediation confidentiality. According to article 200 of the Code of Criminal Procedure, mediators cannot be obliged to testify about information obtained during their work. To testify about information obtained during mediation will result in the mediator committing a crime. Information and declarations exchanged during the mediation procedure cannot be used as evidence during Court proceedings started to solve the same dispute.

Another crucial aspect of mediation has also been regulated by the new law. What previously was defined as the "weakest" aspect of mediation – the *enforcement of mediation agreements,* now is monitored under the new law. Till now, the agreements reached during voluntary out-of-court mediation were considered private agreements that could not be enforced directly. If they were enforced, it was only through an action for breach of contract. One exception was the mediated agreements in corporate and financial matters, usually reached through the assistance of registered organisations, which were judicially enforceable. Now, according to article 12 of the Decree, this principle applies to all agreements in civil and commercial matters resolved through the mediation process handled by mediation bodies registered with the National Register.

After validation of the mediation agreement by the president of the court where the mediation organisation has its main office, the agreement contains an enforcement action empowering the parties to levy execution.

If the parties do not reach an agreement, the mediator has to present a proposal to them, which they are free to accept or not, in order to settle the dispute. This proposal has to be sent to the parties in writing and if they do not respond, their silence is considered as non-acceptance of the proposal (Art. 11), with negative consequences for the allocation of process fees (Art.13). The winning party of a trial – who has not accepted the mediator's proposal– can be condemned by the judge to pay fees to the counterpart.

Contrary to legal proceedings, all mediation acts, documents and agreements enjoy tax benefits (Art. 17).

Aware of lack of information and with the aim to promote the use of mediation, the Italian Government will undertake advertising campaigns, especially via internet, of the mediation process and the registered mediation bodies that are permitted to handle the mediation procedure under Italian Law.

This new reform has incited significant debate within the Italian legal community, especially in relation to the two new components of the law. First, the concept of tax breaks, as provided under the new law, has created discussions concerning the implications for the budget in Italy. The new law offers tax breaks under Article 20. Under this article, the parties receive up to 500 euro in tax breaks for agreeing to participate in mediation and sending the dispute to a mediation center. The current debate concerns where the money to provide these tax breaks will come from – will there be additional taxes levied in other areas or will programs be cut to provide for these tax breaks?

The second debate, and perhaps the larger discussion of the two, concerns the provision stating that, should the parties fail to arrive at a settlement, the mediator shall provide a proposal for their consideration. Currently, this is a mandatory feature of the new law. However, over the next 60 days, this option may be changed to reflect the current debate raging in the Italian legal community. The discussion among the members of the legal community

is focused on whether including a mandatory option like this removes the voluntary nature of mediation and would prevent parties from actively trying to settle their cases. Options to change or replace this current provision include: (i) allowing the mediator to propose a settlement but not making it mandatory; (ii) having a mandatory proposal by the mediator only if both parties ask for it or if only one party asks for it; and (iii) providing for a mandatory proposal by the mediator that the mediator has the option of denying in certain cases. In addition, the debate also includes the idea that a mandatory proposal will be permitted only if there is a mandatory mediation. This debate will most likely continue regardless of whether or not the provision is changed because this strikes at the heart of what mediation is – is it a purely voluntary process or should there be mandatory components to ensure that the parties reach settlement?

All in all, the overall consensus regarding the new law is that this is a positive change for Italian law. The use of mediation in civil and commercial disputes is expected to increase while the new protections offered by the law will assist the mediators in remaining truly neutral. Like all new reforms, there is debate concerning certain aspects of the law but in the end, the law will most likely provide new venues for dispute resolution in Italy.

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BELGIUM

Insider Dealing: a Belgian Law Update

BY NORA WOUTERS AND HENDRIK BOSSAERT | ARENDT & MEDERNACH

Insider dealing is regulated in Belgium by the Law of August 2, 2002 on the Supervision of the Financial Sector and the Financial Services, as amended (the "2002 Law"), which implements among others the European Directive 2003/6/EC of January 28, 2003 on insider dealing and market manipulation (Market Abuse Directive).

Article 2,14 of the 2002 Law defines inside information as "information which is precise and has not been disclosed yet and (in)directly concerns one or more issuers of financial instruments or one of more financial instruments and could, if would be disclosed, seriously influence the circulation of these financial instruments or the financial instruments derived from them". In relation to derivatives on commodities, inside information "shall mean information which is precise and which has not been made public, relating, directly or indirectly to one or more derivatives and which users of markets on which such derivatives are traded would expect to receive in accordance with accepted market practices on those markets". Users of markets on which such derivatives are traded may expect to receive information which is: (i) customarily provided to all the users of these markets; and (ii) must, by law, be published in accordance with administrative and market rules, agreements or customs of the market concerned for the underlying commodity or for derivatives of such commodities.

The 2002 Law applies to financial instruments which are traded on a Belgian regulated or other market or alternative trading platform irrespective of whether the insider dealing took place on the Belgian or foreign territory. It also applies to financial instruments traded on a regulated or other market or alternative trading platform in another Member State of the European Economic Area (EEA) when the insider dealing took place on the Belgian territory. The prohibition also applies to financial instruments derived from such financial instruments but not traded on the above-mentioned markets.

Compliance and Sanctions: A Two-Track Policy

The Belgian legislator has opted for a double enforcement action on insider dealings and provides for criminal sanctions in addition to administrative penalties. Whereas in general, the scope of application of the criminal and administrative proceedings are quite similar, there are some minor but significant differences.

The Difference ratione personae

The administrative proceeding is regulated by Article 25 et seq of the 2002 Law, whereby the prohibition applies to "everybody" (Article 25§1 of the 2002 Law). As a result, there is no distinction between primary and secondary inside traders. If the prohibition is addressed to a legal entity, it also concerns the individuals who are involved

in the decision to carry out a transaction or to place an order for the account of the company concerned (Article 25§2 of 2002 Law).

On the other hand, criminal proceedings are limited to the people who obtained inside information: (i) by virtue of their membership of the administrative, management or supervisory bodies of the issuer or a company closely associated with the issuer; (ii) by virtue of their holding in capital of the issuer; or (iii) by virtue of their having access to the information through the exercise of their employment, profession or duties and who should knew or reasonable ought to have known that the information concerned was insider information. If a company itself is seen as a primary insider, then there is a carry-over towards each individual who is involved in the execution of the transaction or the placing of the order for that company (Article 40§1 of the 2002 Law). A second group of insiders are those who did not obtain the information directly, but consciously obtained it whereby they knew or ought to have known that this is inside information (in)directly received by a primary insider (Article 40§3 of the 2002 Law). As a result, the person who is not a primary insider and does not know or ought to have known that this inside information is (in)directly received by a primary insider, is exempted from criminal sanction. However, administrative proceedings still remain possible if the person knows or ought to have known that the information is inside information.

When applying administrative penalties, no distinction is made between a person who had inside information but did not use it and a person who effectively used it because no causality is required. In the Spector Photo Group case (Case C-45/08), the ECJ held in its judgment on December 23, 2009 that simply possessing inside information is sufficient to constitute insider dealing – no subjective element is required because the prior goal of the legislation is to safeguard market integrity. However the defendant has a right of rebuttal. In case of a crime, the causal link between the possession and the use of inside information must be proven (Article 40§3 of the 2002 Law).

The Enforcement

Compared with criminal prosecution, administrative investigation has multiple advantages. The staff of the Belgian financial supervisory authority, the Banking, Finance and Insurance Commission (CBFA), which has specific competence in financial matters, undertake administrative investigations. The investigation takes place in a more discrete manner and the CBFA has the discretion to impose a fine of twice (treble in case of recidivism) the capital gain, but which may not be less than €2,500 or more than €2.5 million (Article 36§2 of the 2002 Law). A settlement can be proposed (Article 73§3 of the 2002 Law). If condemned by the CBFA, one can appeal to the Brussels Court of Appeal (Article 120 of the 2002 Law), which has full jurisdiction.

The CBFA itself can also transfer the case to the judicial authorities who then can start a criminal prosecution. This may lead to a fine between €275 and €55,000 and the payment of maximum the treble of the capital gained because of insider trading. It may even lead to an imprisonment between 3 months and one year (Article 40§6 of the 2002 Law). During the criminal prosecution, the CBFA can be asked to provide information relating to the case (Article 40§7 of the 2002 Law).

This demonstrates how administrative and judicial authorities cooperate in the enforcement of insider trading. They both have the power to prosecute but they can help each other with the exchange of information.

Furthermore, double prosecution remains possible. The administrative as well as the judicial authorities may charge the same parties with the same infraction of the insider trading regulations without this being considered

an infringement of the *non bis in idem* principle (whereby a person may not be liable to be punished twice for the same infringement). This is because there are two different infringements – the administrative fine is based on Article 25 of the 2002 Law whereby no requirement of causality is needed, whereas the criminal prosecution which is based on Article 40 of the 2002 Law whereby causality is required. Because the constitutive elements of the indictable offences are different, one could be condemned for both infringements without infringing the *non bis in idem* principle. In addition, Article 73 of the 2002 Law stipulates that any prior administrative fine shall be taken into account when a fine is pronounced in a criminal court. This view has been confirmed by the Belgian Constitutional Court on February 24, 1999 in so far the principle of proportionality applies. However, when reading Article 73 of the 2002 Law problems could arise when it is a criminal court that has pronounced a fine before that the CBFA. According to certain Belgian law scholars there is also uncertainty as to the deductibility of the fine based on the capital gains which is pronounced by one of the two authorities, followed by a similar fine pronounced by the other authority.

The Preventive Measures

In order for the authorities and market players to have a better view on the transactions in financial instruments, a set of preventive rules have been installed in the recent years.

The Obligation to Draw up a List of Persons who have Access to Inside Information

Article 9 of the Royal Decree of March 5, 2006 on market abuse (the "2006 R.D.") provides for the requirement for listed companies to list the people who have access to inside information. This list must contain the identity of the people having access to inside information, the reason why these people have access to this information and the date when they got access to this information. The reason for such a list is obvious as on the one hand the authorities want to know who they have to keep an eye on and, on the other hand, listed companies are warned that they have to handle inside information prudently. Furthermore, Article 10 of the 2006 R.D. determines that these lists must be kept updated at all times, when a new person is added to the list, each time there is a change in the reason why somebody has access to inside information and each time a listed person no longer has access to this information. This list must be retained by the company at least five years from the day it was drawn up or updated (Article 11 of the 2006 R.D.).

The Duty to Report any Transactions Carried out by a Person who has Access to Inside Information

The 2006 R.D. also contains a specific obligation for individuals who have managerial responsibility within a listed company and, if such is the case, the people who are closely associated with them. They must notify the CBFA of each transaction they carry out for their own account with respect to the shares or joint financial instruments, like warrants or equity bonds of the listed company. This notice must be given within five business days of the execution of the transaction, unless the value of the transactions in the shares concerned is not more than €5,000 per calendar year (Article 13 of the 2006 R.D.).

Qualified Financial Intermediaries must inform the CBFA if they have any reasonable doubt that a transaction could be considered to be insider trading or market manipulation (Article 16 of the 2006 R.D.). This notification must be given as soon as the intermediary believes a transaction could be considered insider trading or market manipulation (Article 17 of the 2006 R.D.).

Article 3 of the 2006 R.D. contains a non-exhaustive list of criteria which could indicate possible market manipulation. On the contrary, Article 5 of the 2006 R.D. provides a list of criteria which may indicate customary market practices ("safe harbours"). A last exception exists for buyback programs and measures to stabilise the markets in financial instruments: if certain specific conditions are fulfilled, these transactions are not prohibited under the regulation regarding market abuse (Articles 7 and 8 of the 2006 R.D.).

The Information Commitment

To prevent insider dealing, the Royal Decree of November 14, 2007 regarding the obligations of issuers of financial instruments admitted to trade on a regulated market (Belgium or of another Member State of the EEA (the "2007 R.D.")) provides that, to guarantee full transparency, a Belgian issuer of shares must disclose certain information in its annual and semi-annual financial reports (Articles 12 and 13 of the 2007 R.D.).

The annual financial report must contain the audited annual accounts, the annual report and a declaration of the issuers' management responsible for the documents. The semi-annual financial report must contain a shortened financial overview, the interim report and a declaration of the management responsible for the report. Furthermore, Article 14 of the 2007 R.D. stipulates that a Belgian issuer having shares admitted for trading on a Belgian regulated market or regulated market of another Member State of the EEA must publish an interim report during the first half of the financial year and a second interim report during the second half of the financial year.

This regulation aims to provide full transparency for investors and to limit the amount of sensitive financial information kept by the issuer and by certain people who are professionally involved with the issuer. Therefore, Article 10§1 of the 2002 Law stipulates that an issuer of financial instruments which are admitted for trade on a Belgian regulated market must immediately announce any price sensitive information, including changes of meaning regarding previously reported information.

However, the issuer has the possibility to postpone the publication of such information on the condition that this postponement does not mislead the market and that the issuer can guarantee the confidentiality of the inside information. However the decision of this postponement of publication must immediately be reported to the Belgian regulator (Article 10§1, paragraphs 3 and 5 of the 2002 Law).

Conclusion

By implementing a two-track policy combined with multiple precautionary measures, the Belgian legislator aspires to have a better grip on insider dealing transactions which would distort the integrity of the financial markets. Some recent cases, including charges for insider dealing against two well-known Belgian politicians and the imprisonment of two CEOs, have shown that the Belgian authorities are serious about enforcing this legislation.

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PORTUGAL

Civil and Criminal Liability of Directors of Financial Intermediaries under Portuguese Law

BY MIGUEL CASTRO PEREIRA AND ANA SEQUEIRA | ABREU ADVOGADOS

Portugal recently faced two cases of financial intermediaries (banks) that required government intervention (including nationalisation) further to the assessment of gross negligence and wilful misconduct of its directors, leading to significant damages to depositors and shareholders.

Furthermore, the Portuguese banking system and its supervision was also challenged by these facts. Criminal charges were brought against said directors and civil actions have also been started.

This article purports to address the legal regime applicable to directors of financial intermediaries' civil and criminal liabilities under Portuguese law and to demonstrate how these matters should be handled by attorneys representing any of the involved or interested parties.

Who is (Really) Responsible?

Most of the actions of a financial intermediary within the execution of its corporate purpose, are determined by its direction, thus, one might say that all the actions of the company are actions of its directors.

When facing a decision of the corporate body which may be deemed as a crime, should all of the members of said corporate body be criminally responsible or is there any possibility that any of the directors are excluded of such responsibility?

On a collective crime, on which all the parties are liable for the rendered decision, the criminal responsibility shall always be different (even when several directors participate in the same facts), since it depends on the degree of control over the specific facts that each director has, under the general rules of co-participation.

Considering that the criminal responsibility is strictly personal, the fact that the crime was executed within the scope of a collective body does not automatically imply the criminal responsibility of all the members of the collective body, it is necessary to analyse the real contribution of each member to the specific execution of the criminal fact.

The difficulty arises in determining what behaviours are possibly seen as an action or omission that may be attributed to the functional subject – which is part of the collective body – as a personal fact.

In what concerns the facts that are immediately harmful, the simplest cases are those in which the actions of the corporate body are immediately deemed to constitute a type of crime, and there is only one physical person in the corporate body. If the agent executes the action by himself, i.e., acting alone, there are no further questions regarding the legal frame.

In what concerns harmful actions through behaviour of third parties, the questions arising are far more complex, since the harmful fact does not arise from the exclusive action of the corporate body or of its representative; instead, its execution depends on the collaboration of third parties.

Furthermore, the subject may direct a third party to commit the crime (instigation). The subject persuades with intent one or more third parties to commit a criminal action, and the instigated party execute the fact, thus being the criminal action carried out. It's the case of a director that determines another director (ordering the execution of the crime) to either jointly or severally execute the crime and it is voluntarily executed.

The instigation must be direct and it must be performed with intent. The execution can be merely blameful, i.e., the instigated party may act with mere negligence (this fact is relevant for the situations in which the director was instigated).

In what concerns authorship, the author is whoever executes the fact by himself or by means of a third party, or who is a direct part in its execution by joint agreement with another party.

In the mediate authorship, the subject executes the fact by intermediation of a third party. In these cases, the intermediary – the immediate and material executioner – is not responsible since his actions are not harmful. The author, in the cases of the directors, uses the material executioner to perpetrate the crime. The mediate author maintains the control over the executed fact, thus, only whilst the director maintains such domain over the conduit of his collaborators/employees will it be responsible as mediate author.

In the joint authorship by agreement or jointly, the director executes the fact jointly with third parties, being the perpetration of the fact divided among themselves. The agreement does not have to be prior to the execution nor does it have to be express; a mere tacit agreement based on the existence of a conscience and will to collaborate in the perpetration of the criminal objective is enough. If there is no agreement, either express or tacit, there is no joint authorship but parallel authorship.

The Negligence of the Directors of Financial Intermediaries

The problems inherent to negligent crimes are especially relevant considering their frequency in company life.

It is common that the crimes are due to the negligence of any collaborator of the company, which in the exercise of its functions did not act with its duty of care. The question which arises especially in the domain of the company's life, since with the division of work among the collaborators, it must be assessed how can the directors be held responsible for the negligent actions of a third party which is a collaborator of the company, given that besides holding a director responsible, it shall have as a reflex, the imputation of such responsibility to the company, provided that all the conditions for such imputation are met.

Frequently, the director shall be held responsible for the fact as a self fact and not due to the negligent action of a third party.

The negligent responsibility of the directors is not the responsibility for a fact committed by a third party, but as a self fact, since the directors shall only be held responsible by means of a self negligent act – a situation in which the action of the director concurs with that of the collaborator.

It must be noted that in the analysis of the negligent crime structure it is important to distinguish the type of crime that corresponds to the violation of care that the criminal agent, considering its knowledge and personal capacities, is in the condition to render.

In what concerns the immediately harmful actions, it must be noted that as in the crimes of action with intent,

also in the negligent crimes of action, the simpler cases are those in which the conduit of the corporate body immediately executes the criminal action, being the corporate body composed of only one physical person. If the agent executes the fact by himself (i.e., acts alone), there is no doubt as regards the subjective imputation of the crime. All that needs to be considered is the fulfilment of the type of crime and the decision regarding the type of blame of the agent (negligent or deliberate), i.e., the violation of the care that was objectively due by the director, and the care that the agent, pursuant to its knowledge and personal capacities, was in condition to render.

As regards the facts that are harmful through the behaviour of third parties, with exception to the instigator and to the accomplice, a situation of co-participation can be verified in the negligent crimes by action. What is considered for the criminal punishment of the self negligent crimes is that the director of the company intervenes as an agent of the crime.

As a general rule there is no responsibility for the lack of care of a third party, since the law authorises to trust that the third parties shall fulfil their care duties.

It has been understood that the responsibility within the organisation itself implies that the responsible party of the company establishes mechanisms to control the activity of the company, controls that must be rigorous when considering the particulars of the situation at hand.

The omission consists in not carrying out what is due and when such duty is of a company, it is generally a responsibility that falls under the scope of the directors. The omission is not punishable, except if the agent has a duty to act, a situation in which the duty of the functional action is of the directors – and thus fulfilling a duty that is primarily of the company.

The questions of the responsibility by omission arising in the domain of the corporate activity are related to the duty to act in the name of the company, i.e., regarding the existence of the duty by the company, over whose scope such duty will fall under within the company and in a particular way the responsibility in the cases of corporate bodies with a plural composition. Firstly, the corporate body has the duty to act by the company, but when referring the corporate body, the scholars refer to the corporate body members, being such members held responsible due to deliberate or negligent actions, depending on the type of omission.

Over such persons there are duties of vigilance or control and if the violation of such duties falls under their scope, as a deliberate or negligent action, they shall be deemed responsible for the actions of their subordinates, who, due to such violation, committed criminal actions. This situation is one in which the responsibility by omission is verified.

There is no responsibility by facts of a third party, but by a self fact: The omission of the duty of care and vigilance over their subordinates. That said, the mere allegation of not knowing certain facts that occurred is not enough to remove the responsibility.

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The Different Types of Criminal Responsibility of Each Director

BY MIGUEL CASTRO PEREIRA AND ANA SEQUEIRA | ABREU ADVOGADOS

On the basis that criminal responsibility is strictly personal, a case in which a crime is executed in the scope, or with the participation, of a plural corporate body does not automatically imply that the criminal responsibility is of all the members of that corporate body. In cases in which the responsibility is shared by all the members of such corporate body, said members do not have to be held responsible in the same degree; it is possible that some are held responsible as authors and others as accomplices, some may be held responsible for the criminal action with intent and others with negligence.

When the decision to commit a crime arises from a decision of the corporate body, it must be defined how the responsibility of the members of the corporate body is determined, and various hypotheses may arise:

- If all the members of the corporate body vote in the same direction, then all of them will probably be held responsible, being only dependent on the blame of each party, since a situation in which one or more members of the corporate body act without blame may occur or, being the criminal action deliberate, any of them is to be responsible solely by negligent responsibility.
- When any member votes against or does not vote, but the favorable votes are sufficient for the necessary majority for the enactment of the decision, then it is likely that only those that voted favorably will be held responsible for the fact. The members that voted against do not show any criminal intent.
- When the vote, even if contrary to the decision that was rendered, was essential for the validity of the decision itself – as in the case when the participation in the decision of the member that votes against was necessary in order to create the minimum quorum for the decision – the member of the corporate body that voted against must not be considered as an accomplice. By participating in the decision, the member of the corporate body is fulfilling his or her duty, but cannot be held responsible for the decision rendered, since by voting against it, the member is not showing criminal intent.
- The result will be different if the law grants to the member of the corporate body a right to oppose, and such member did not use said right. In this situation, it must be considered that the member is allowing the criminal intent. As a matter of fact, the agent accepts the decision rendered by the majority, since only his omission makes it lawful. The decision rendered by the majority is only possible because that member of the corporate body made it possible by not using his rights. The member is not fulfilling his duty.
- A similar solution to hold a member of a corporate body responsible, is that of the abstaining member, which makes the majority decision possible, since without his presence and abstention, the necessary quorum would not be met. The abstention appears to have the significance of acceptance of the majority decision, irrespective of the decision. The abstention is always the voluntary adhesion to the decision that is rendered.

In the decisions of a corporate body, the issues do not end with the participation in the decision, since there is a second moment: the execution of the decision.

If the decision is not an autonomous crime by itself, but a preliminary phase of the crime, and considering that it is very difficult that the rendering of the decisions within the company are deemed as a preparatory punishable

action, the penal responsibility will only be relevant when the execution of the decision is simultaneously the execution of a criminal fact, i.e., it will only be relevant in terms of how the corporate body created the intent on the perpetrator of the crime, when the decision to commit the crime is externally manifested by the execution. The director may not be held responsible for the criminal action enacted as a consequence of a decision in which said director participated, if through his behavior or vote – as an individual manifestation of will – did not contribute to the execution of the criminal fact.

If all the directors act with intent or negligence, i.e., when there is a criminal intent or negligence by all the directors in the same measure, there are no special issues. Such issues arise when some directors act with intent and others do not, but in such situations it is only necessary to assess the guilt of each of the members of the corporate body.

Concerning the method to determine individual responsibility in the adoption of the decision, it must be noted that frequently the corporate body works based on an interconnected basis with a division of tasks within the body itself, whereby each member has his own circle of activity. The issue arising is solely that of establishing when a decision must be issued, up to which point each member of the corporate body may use the information rendered by other members as a guide, when certain aspects fall within the competence of these members.

The joint direction principle serves the interests of the company and of its shareholders, and tends to assure a higher security and correction of management decisions, but when the possibility of avoiding damage is clear, the prevailing interest of avoiding any damage must overcome the interest of the joint direction. The question now arising is that of the conditions pursuant to which the dissident administrator (when regarding a given decision) is also held liable for the execution of the crime, not due to having participated or not in the corporate body decision, but due to not having stopped the execution of the decision.

The dissident director cannot, as a general rule, be held responsible by action, but he can be held responsible by omission: due to not stopping the execution of the crime perpetrated by the other directors.

The responsibility by omission of the dissident director is grounded on that director's duty of action, in that such duty imposes the non execution of the crime. This duty exists in similar grounds to those of the directors, when regarding the acts of the collaborators/employees of the company, under the authority of such directors. The assurance duty not only exists for the corporate body or bodies, but also over each and every one of the directors.

As a matter of fact, the assurance duties of the directors are not only imposed when they are acting jointly, as a body of persons, they are duties of the corporate body, and as such, duties of all the directors which should ensure that the corporate body fulfills said duties. The same is to say that when considering the particulars of the case, each director should do everything within his reach to stop the execution of the crime.

The accusation will have to prove objectively that the author of the crime had the juridical duty, and effective possibility to stop the result of the crime, and, subjectively, that the director knew its position and the duties related thereto, and that he did not voluntarily execute what was demanded to fulfill their duties, and finally that at least he accepted and foresaw the consequences of his omission.

The person occupying a position of leadership may not be criminally responsible if he opposes expressly the criminal action. If he is a member of a collective body, his individual criminal responsibility is excluded, provided that the member votes against the decision of the corporate body.

The criminal action creates, at the same time, a criminal responsibility and a civil responsibility. The first responsibility fulfills, essentially, general and special prevention (the goal is the avoidance of the execution of new

crimes) and the second has the goal of repairing the damage caused to the victim.

In the case of holding responsible various members of a collective person, as a group of directors of a company, different indemnity obligations are available.

When there are several corporate body members that are deemed as responsible, their responsibility is joint, but the members that did not participate in the act will not be responsible (except in the cases of responsibility by omission: the omission of a duty of action), as well as the members that did not agree with the criminal act.

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Arbitration in Portugal: Main Aspects of a New Legal Regime

BY PEDRO CARREIRA ALBANO | ABREU ADVOGADOS

Statement of Reasons

Despite the adequacy and completeness of Law no. 31/1986, of 29 August – the Arbitration Act ("AA") – which establishes the arbitration regime in Portugal since then (amended by Decree-law no. 38/2003, of 8 March), and represents a notable progress in Portuguese law, which previously did not have a modern legal regime on the matter. However, the truth is that the law has not fulfilled its expectations, not only in terms of the needs imposed by international and domestic commerce, but also compared to arbitration acts in other jurisdictions. Moreover, the framework will have been in existence for 24 years in August, and has failed to keep pace with many of the changes that arbitration has experienced.

Fundamentally, these are the reasons why reform of the law on arbitration as a dispute resolution alternative to courts has long been demanded. Critics wanted to bring the legal regime closer to the "UNCITRAL Model Law on International Commercial Arbitration (the "Model Law"), duly amended to complement local circumstances in Portugal.

In this context, upon request from the Minister for Justice, the Portuguese Arbitration Association presented in March 2009 a draft of a new Arbitration Act (the "draft law").

Therefore, we believe that a brief analysis should be made on what we consider to be the most relevant proposed changes to the Portuguese Arbitration Act.

Finally, a reference will be made to the need for clarification of the "object of the dispute" concept, an issue that is not addressed by the proposed new Arbitration Act.

Main Aspects of a New Legal Regime

One of the main differences between the AA and the draft law on arbitration concerns the issue of *arbitrability*. This no longer depends on the fact that we are before a right or obligation of which parties can dispose of, as provided in section 1, paragraph 1 of the AA, but rather on the economic nature of the right or obligation which is being disputed. Also, this main criteria is now combined with a secondary one related to knowing whether the dispute in question is one which parties are legally allowed to terminate by mutual consent. This means that disputes which do

not involve economic interests, but that parties can solve by settlement, can be referred to this form of alternative dispute resolution, according to section 1, paragraph 2 of the draft law.

One aspect of tremendous practical importance in relation to the arbitral proceedings and one the AA was silent about is that of providing arbitrators with the power to adopt interim measures during the proceedings, to ensure the award's enforceability.

It has been submitted that by granting arbitrators powers to decide their disputes, the parties implicitly (through the implied powers doctrine) provide them with the competence to issue the interim measures required to guarantee the award's efficacy. However, it will be useless to advocate this doctrine, since if parties require any interim measures, the arbitrators may issue them, but the courts will not have any guidelines on how to implement them, as there is no provision in civil procedure law establishing how courts should execute such measures. Arbitrators have no jus imperii, and so they must rely on courts to enforce their decisions (Vd. Manuel P. Barrocas, in Boletim da Ordem dos Advogados no. 46 (Março / Abril de 2007)).

In light of this, the draft law, in line with the provisions added do the Model Law, expressly stipulates that arbitrators have the power to issue interim measures (in line with the more recent Arbitration Acts in Europe (e.g., section 1041 of the German ZPO; section 23 of the Spanish Act, etc.)) and how to proceed in order to enforce them in collaboration with courts.

Another innovation in the draft which ought to be highlighted is the reversal of the default rule on the possibility of appealing the final award.

Section 29, paragraph 1 of the AA establishes that the same appeals that can be made to a judicial decision by the district court are available against an arbitral award. This provision has been highly criticised, as it unjustifiably "judicialises" arbitration, and because the non possibility of appealing awards in the courts is now a rule of private international law. Also, in domestic arbitration, most Arbitration Acts, especially those that were inspired by the Model Law (section 34), do not allow for the appeal of awards unless the parties have stipulated this possibility (*Vd.* Manuel P. Barrocas, *idem*).

Now, the draft law (see section 39, paragraph 3) incorporates precisely the principle of the non possibility of appealing the final award (the award can still be challenged by pleading for its annulment, and this possibility cannot be set aside by the parties beforehand), unless the parties have expressly agreed that the award could be appealed in accordance the applicable procedural law. This legal answer is more in line with the characteristics of arbitration, namely in relation to the fast resolution of the dispute.

As to the request for an annulment of the award mentioned in the draft law (see section 46), which, as it happened with the AA (see section 27), shall only be possible in one of the grounds expressly indicated, to ensure that a final decision about the annulment is reached rapidly, such proceedings do not follow the ordinary process, but rather they are processed like an appeal and, depending on the nature of the dispute, they are presented in the court of appeal; and only one appeal is now permitted.

Lastly, in regards to the recognition and enforcement of the award of arbitral awards rendered outside of Portugal, the draft fully incorporates the regime of the "United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards", and at the same time it attributes competence on these matters to the court of appeal.

As a final comment, it should be noted that the draft law on arbitration is very innovative in relation to the Arbitration Act, in most cases following the provisions of the Model Law and some foreign acts that have implemented it, like the German and the Spanish ones.

The Object of the Arbitration should not be Equated to the Request for Arbitral Proceedings

Although the changes made by the draft law on arbitration are globally on the right track, there is one aspect about the Arbitration Act which has raised great difficulties of interpretation, and therefore should be made clear and exact: the definition of the "object of the dispute", which the draft law does not address.

In accordance with section 11, paragraph 1 to 3, of the AA, the party that intends to commence arbitral proceedings must give notice of that fact to the counterparty, specifying what the object of the dispute is. The other party, in its response, must simultaneously designate the arbitrator that is for her to nominate, and, if she so wishes, declare whether she accepts the delineated object or intends to enlarge it.

It often happens that during those communications the parties are not – and indeed, in most cases they could not be – able to indicate all the claims related to the central question which they wish to bring to the appreciation and judgment of the Arbitral Tribunal (this has to do with the fact that, in most cases, only when the initial petition is being prepared or in the respective statement of defence with counterclaim, as the case may be, which often only takes place several months after the exchange of notices, are the parties able to concretely formulate their pleadings).

The clarification of what is meant by the "object of the dispute" should, thus, be dealt with by the New Arbitration Act, in order to avoid doubts in interpretation which have lead arbitrators to consider out of such object, and consequently out of their consideration, issues that clearly fit in the fundamental question that is being arbitrated, due to the absence of express reference to them in the letters of constitution of the Arbitral Tribunal.

We do not agree with this opinion and therefore propose that a wider notion of "object of the dispute" corresponding to the fundamental issue in dispute is adopted in the New Arbitration Act, allowing the choice of the arbitrator to be made in accordance with its areas of specialty, notwithstanding leaving to the statement of claims made in the initial petition or in the statement of defence, as the case may be, the concrete issues that the parties wish to have examined, in the framework of the previously established object of the dispute.

To provide the reader with an example: A, claiming the default of a given contract signed with B, decides to terminate it. B, denying the existence of sufficient reason for termination by A, commences arbitral proceedings, giving you notice of the arbitrator appointed by him and establishing the object of the dispute in the following way: "assessment of the lawfulness of the termination".

It is asked: if B, in its notice to A, has not specified that, in the event that the termination is considered unlawful, it intended to have A condemned to compensate him as appropriate, would it be legitimate for the arbitrators to decide that, if this claim would then be made in the initial arbitral petition, it could not be assessed because it had not been specified at the time of the notice establishing the "object of the dispute"?

We think not. Indeed, such claim for compensation would always be connected to the declaration of the unlawfulness of the termination; hence there is no good reason for it not to be addressed by the Arbitral Tribunal. This understanding would also allow the several parts of a same dispute to be solved in a single process, which would result in great advantages in terms of the speed of the proceedings, the allocation of resources and cost savings connected with the arbitration.

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Mediation in Portugal

BY JOSÉ ALVES PEREIRA | ALVES PEREIRA, TEIXEIRA DE SOUSA & ASSOCIADOS

2001 saw for the first time the introduction of a new Portuguese law on mediation. Law 78/2001 implemented a system of court-annexed mediation for all cases within a specified monetary value in the jurisdiction of the small claims court. This will include some cases of a commercial nature.

Mediation is defined by article 35 of the said law as follows: "Mediation is an extra-judicial method of dispute resolution, independent in nature, informal, confidential, voluntary and of a non-contentious nature, in which the parties, acting actively and directly, are assisted by a mediator to find, by themselves, a negotiated and amicable solution to their dispute".

As can be seen, the emphasis is on a facilitative method of mediation rather than an evaluative one, and the definition highlights that it is the parties who should to drive the process and not the mediator. The fact that the process is described as being "of a non-contentious nature" stresses the idea that a mediation is not supposed to reflect the court process, but is a completely separate means of dispute resolution.

Before the appearance of such law, mediation and conciliation were practised in Portugal in a completely non-regulated environment and in very limited cases mostly connected with consumer disputes. However, there existed for long time a judicial conciliation procedure, regulated by the Code of Civil Procedure.

Unlike mediation, the provisions governing conciliation are of a general nature rather than applying to specific claims, such as those in the small claims court. Conciliation is characterised as a compulsory attempt to reach a settlement between the parties, which is conducted by the judge.

Conciliation can be distinguished from mediation in a number of ways. First, conciliation is not an optional process but rather one that is imposed on the parties at the discretion of the judge. The conciliation attempt will take place when the judges decide, even if a mediation has already failed or the process is opposed by the parties. Furthermore, unlike mediation, conciliation is not a confidential procedure, as the judge leading the conciliation will go on to hear the case if the conciliation is unsuccessful and the case goes to trial. In the small claims court, the judge promotes conciliation prior to the submission of the case to trial. When the conciliation leads to an agreement, proceedings are ended at an early stage, therefore providing a saving to the parties in terms of both time and expense.

The aforesaid law 78/2001 contains also provisions dealing with the establishment of mediation services, the capacity and duties of the mediators, the rules regarding regulation of mediators (including their qualifications, function and remuneration), the objectives and procedural steps of the pre-mediation and mediation sessions and the issue of confidentially. As yet, mediation has not been enshrined in the Portuguese Code of Civil Procedure, as conciliation is.

The law makes no provision for the consequences of a party's refusal to mediate upon the proceedings. Therefore, a party's refusal to mediate will not result in the judge penalising them with costs sanctions.

There is no statutory definition of confidentiality in the Portuguese system, but Law 78/2001 contains some specific provisions relating to the concept. These provisions are only applicable to the court-annexed mediation scheme at the small claims court. They provide the parameters within which the mediation is confidential, rather than a definition of the term.

Under these rules, the parties must sign in advance a mediation agreement in which they undertake to keep the mediation strictly confidential. The parties, their representatives and the mediator must keep confidential any verbal or written declarations produced during the course of the mediation. In addition, the parties cannot have access to the documents written by the mediator during mediation.

This preserves the confidential nature of the mediation itself, ensuring that the parties are able to discuss their cases with the mediator without fearing that their comments may be seen by the other side.

At the end of the mediation, the mediator is required to report to the court whether settlement was totally, or partially, achieved. No other information relating to the mediation is communicated to the court. This ensures that the parties can negotiate in the confidence that their offers and declarations will not be passed on to the court and later used against them if the case were to proceed to trial.

Finally, the mediator cannot be called as a witness in any claim brought by the parties following the mediation, even if not directly related to the subject matter of the mediation. This guarantees the obligation of continuing confidentiality, so that any information given to the mediator will remain confidential after the event.

The various limitation periods depend upon the specific right, or the nature of claim, in dispute. In general, it is only when a statement of claim is lodged with the court that the limitation period would be interrupted. Mediation procedures will not of themselves suspend the limitation periods.

However, in the specific case of the small claims courts the statement of claim is lodged prior to the pre-mediation and mediation stages. Therefore, the limitation period is suspended for the duration of the court process, which would include the mediation.

Law 78/2001 provides that settlement agreements arising out of mediations must be immediately ratified by the judge and have the same value as a court decision.

Settlement agreements arising out of voluntary mediation outside of the courts have the same value as any other agreement, i.e., contractual. In the event of a breach of the agreement the aggrieved party would be entitled to seek recourse through the courts to obtain an enforceable decision.

The mediation process described by Law 78/2001 provides for a pre-mediation session to take place. The aim of this session is to explain to the parties what mediation is and to evaluate whether they wish to attempt it. This session should take place before the proceedings are submitted to the judge, unless the parties have specifically agreed to waive their right to the process.

If the parties wish to proceed with the mediation then a mediation agreement must be signed and the date for the first mediation session is set. The parties are required to sign both a mediation agreement and a confidentiality agreement prior to the mediation. These agreements include undertakings to keep strictly confidential all verbal or written declarations produced during the mediation and also include an obligation of good faith.

The mediator involved in the pre-mediation session cannot be appointed as the mediator in subsequent mediation sessions of the same case. The court holds a list of all mediators approved for participation in the scheme. The list is compiled by the Ministry of Justice and all on it were specifically selected through a process initiated by the Ministry in 2001. All mediators appointed in the small claims court mediation scheme must have been selected fro the Ministry of Justice list. The parties are able to choose a mediator from the Court list and, in the absence of any agreement, the mediator is appointed by the Secretary of the Court.

The mediators, in cooperation with the parties, will conduct the mediation proceedings. With the consent of the parties, he can hold separate sessions with each side (a “caucus”) in order to facilitate the mediation process.

It is incumbent upon the mediator to evaluate the progress of the sessions and decide on the need to proceed with such sessions. He must dedicate an appropriate amount of time to the mediation bearing in mind the nature and complexity of the dispute.

The law emphasises the facilitative role of the mediator, who is empowered to assist the parties but not to impose a solution upon them. The parties may be accompanied by lawyers, experts, and technicians or other nominated persons, and they are free to stop the mediation at any stage.

If an agreement in reached, it is recorded in writing and signed by all parties, and the mediator, for immediate ratification by the judge. Such an agreement has the same value as a decision taken by the court.

At the present, the above procedure applies only to cases of up to the specified value brought in the small claims court. There is currently a consultation process in place to discuss the results and progress of the scheme. This may well bring about similar developments for cases exceeding €5,000 or in different courts.

After developing the above described civil mediation system for actions up to €5,000, the Portuguese Government decided to create three new schemes of public mediation in order to relieve the courts of the excess of pending suits and at the same time reduce the costs that the parties have to bear with them.

There are three new schemes of public mediation:

- Family Mediation, since 16 July of 2007 and present throughout the national territory. This system was created by Order 18778/2007 of 13 July.
- Labour Mediation, since 19 December of 2006. This system was created through a Protocol of 5 May 2006 signed by the Ministry of Justice, the Trade Unions and Employers Confederations.
- Criminal Mediation, since January 2008. This system is still in probation period for two years in four judicial districts (Porto, Aveiro, Seixal e Oliveira do Bairro). The Criminal mediation was introduced by Law 21/2007 of 21 June.

Family mediation is provided for the following situations: (i) divorce and legal separation; (ii) regulation and alteration of parental responsibility; (iii) authorisation to use the surname of a former spouse; (iv) temporary or permanent alimony payments; and (v) to decide on the family residence.

Labour mediation can be used for disputes dealing with: (i) severance pay; (ii) workplace; (iii) holidays; (iv) working time; and (v) termination of employment agreement. Accidents at work are excluded from mediation.

Criminal mediation may be used on crimes that depend on complaint or private accusation. It is nevertheless excluded on: (i) crimes that depend on public accusation (e.g., homicide or robbery); (ii) crimes with a prison sentence of more than 5 years; (iii) crimes of corruption or fraudulent conversion of public moneys; (iv) whenever the victim is younger than 16 years old; and (v) in summary proceedings as described by law.

Training is mandatory for all those who wish to be mediators in the small claims court mediation scheme. Article 31 of Law 78/2001 lists the criteria that must be fulfilled in order to be a mediator in the court-annexed mediation scheme run in the small claims court. Mediators must be more than 25 years of age and to be in the full possession of all their civil and political rights. Mediators are required to have adequate academic qualification and to be trained under a mediation course recognised by the Ministry of Justice. They must not have been convicted of a crime. Finally, they must be fluent in Portuguese and should preferably be resident within the geographic jurisdiction of the court. The Ministry of Justice organises the accreditation process and manages the mediator list for the scheme.

Outside of the small claims court mediation scheme there is no national rule, or standard, governing the training and accreditation requirements under which mediators have to practise. Post-graduate training courses are available in a number of private universities in Portugal.

Mediators in the small claims court mediation scheme are accepted from every profession requiring a university degree. With the exception of the criteria as stated in Law 78/2001, there are no specific rules to prevent people from acting as mediators.

Law 78/2001 also contains certain rules of conduct for mediators stating expressly that: "In the performance of his functions, the mediator, must act with impartiality, independence, credibility, competence, confidentiality and diligence".

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People's Action: Balancing Efficiency and Justice

BY MIGUEL TEIXEIRA DE SOUSA | ALVES PEREIRA, TEIXEIRA DE SOUSA & ASSOCIADOS

In a globalised world such as the one we live in, the expression "legal transplants", as proposed by Alan Watson, has often been used to designate the transfer of institutes which are characteristic of certain legal systems to other legal systems. Though sometimes one feels that the expression is used on pejorative terms, the truth is that it seems perfectly adequate to describe the transposition of an institute from its original legal system to another system to which it is alien but nevertheless needs it to find the more adequate legal solutions to a certain problem.

For a long time, in the systems belonging to the roman-german family, judicial protection was confined to the rights of a single holder or of specified holders. Following this pattern, the model which grounded the civil procedural laws was either one or some holders of a right litigating against one or some passive holders or defending such right against one or more third parties. This was not the result of the choice of one jurisdiction amongst various options but happened instead because the legal systems did not recognise other subjective situations in need of protection which were not characterised by this individual or limited plural aspect.

This scenario started to change in the post-World War II period, when Western civilizations experienced unprecedented development. One of the consequences of such development was the trend of massive consumption. This led to looking at the consumer not as someone on individual terms but as an anonymous and fungible entity. In fact, if a consumed product appears to be defective, it is immaterial whether it has been acquired by A, B or C since all such entities require the same protection. Equally immaterial is to protect A, B or C from such consumption as all of them also require the same preventive protection.

Another by-product of the industrial development which occurred after the Second World War was environmental aggression. Environmental protection was neglected for long time in exchange for material well-being, but the progressive awareness that environmental devastation and the dilapidation of scarce resources would ruin this well-being and put in jeopardy the future generations has led to an array of legal instruments

aiming to prevent – or at least slow down – baneful actions towards the environment.

Consumption and the environment have revealed the insufficiency of a traditional analysis, based on individual rights or with identified holders. If each and every consumer needs similar protection and if all are harmed by environmental aggressions, then we have an undefined plurality of holders of one same right or, at least, of one same interest. To designate such interests having as holders members of one class or one group but which are incapable of individual appropriation by any one of such members, Mauro Cappelletti (a disciple of Piero Calamandrei) proposed the designation of diffuse interests.

It was in this context, that one of the so-called "legal transplants" occurred, giving expression to a tradition which some consider to go back to the English Middle Age: rule 23 of the V.S. Federal Rules of Civil Procedure establishes, since 1937, a class action, through which, as the name indicates, the interests of the members of a class are protected.

Such class action has waked the interest of some Italian scholars, in particular Mauro Cappelletti, well-known supporter of a social (or "above-individual") conception of the procedure.

As it happens in the transplants done in medical surgical intervention, it is necessary to avoid the rejection of the institute imported from the donor legal system. There is a characteristic aspect of the US class actions which render them difficult to harmonise with the roman-german tradition: it is the admissibility of remuneration of a lawyer through a "quota-litis", or contingency fee system, which renders such lawyer particularly interested in the outcome of a class action and in the amounts which may be obtained through such action by the damaged parties.

Without the impulse normally exercised by the US lawyer, one runs the risk of not finding any holders of a diffuse interest willing to start an action for the protection of one of such interests. Perhaps for this reason, European legislations were generally very cautious in granting legitimacy for the protection of diffuse interests. Following a trend already adopted in some legal systems – namely in the labour and intellectual property fields – most legislations have chosen to grant such legitimacy only to associations, representing holders of a diffuse interests.

Portuguese Law, however, has diverted from this trend. Under art. 52 no. 3 of the Portuguese Constitutional Law, legitimacy to the protection of diffuse interests through a so-called "people's action" is granted not only to associations but also to individual citizens. This aspect makes the Portuguese people's action close to the U.S. class actions. Another aspect which renders similar those forms of collective action is the faculty granted to the holder of the diffuse interest to opt for not accepting his representation by the plaintiffs of the people's action: it is the opting out regime established in article 15 no. 1 of Law 83/95 of 31/8/95. However, the fact of the legitimacy being given, in addition to the holders of diffuse rights, to collective persons having as purpose the protection of such interests, establishes an important difference in relation to U.S. class actions.

The collective actions – that is, the actions such as the class actions or the people's actions – seeking the protection of above-individual interests, are often the sole means available to each one of the interested parties to remedy or prevent a situation. In fact, the little dimension of the interest of each one of the holders of the diffuse interest does not motivate him to introduce an action in court; the dimension of the offense is only significant in a collective perspective, in a perspective which considers all holders of a threatened or violated diffuse interest. In this case, the people's action is a means by which the efficiency is conjugated with justice; such action is the only efficient means to ensure the justice due to each one of the holders of the diffuse interest.

However, it is not always like that. Situations may occur in which the holder of the diffuse interest is harmed in his interests in such a significant way that he has the option either to defend them in an individual action or accept the defence in a collective action. It happens, for instance, in damage caused to health deriving from consumption of a product or from environmental pollution. In such cases, the relationship between efficiency and justice is no longer the same. Because justice would demand the consideration of the situation of each one of the holders of the diffuse interest but the efficiency of the collective action cannot be harmonised with such individual examination. Thus, the collective action, because it must be efficient, cannot ensure all the justice due to each one of the holders of the diffuse interest.

That is the reason why the people's action is still looking for a paradigm closer to efficiency or justice. In any case, it has already become a successful "legal transplant".

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SWITZERLAND

The Swiss Rules of International Arbitration and of Commercial Mediation: Modern Tools for the Settlement of International Disputes

BY MATTHIAS SCHERER AND DOMITILLE BAIZEAU | LALIVE

The Swiss Chambers of Commerce (the "Chambers") have been administering international arbitration proceedings since 1911. Historically, Geneva and Zurich have hosted legions of institutional and *ad hoc* arbitrations and continue to do so. Switzerland also has a long standing experience in the settlement of disputes through other ADR means, including mediation.

Key Features of the Swiss Rules of International Arbitration

In 2004, six Swiss Chambers of Commerce (Basel, Berne, Geneva, Lausanne, Lugano, and Zurich, joined more recently by Neuchâtel) harmonised their procedural rules and adopted uniform rules for international arbitration proceedings, the Swiss Rules of International Arbitration (the "Swiss Rules").

The Swiss Rules can apply to any international arbitration whether the seat is in Switzerland or not (although Swiss arbitration law only applies if the place of arbitration is Switzerland). In addition, the Chambers will administer disputes unless "there is manifestly no agreement to arbitrate referring to" the Swiss Rules. Clauses referring to arbitration "of the International Chamber of Commerce of [Swiss city]", to "the appropriate arbitration board in the Canton of [X]" and to "any arbitration council of Switzerland" have been accepted by the Chambers.

The Swiss Rules are based on the UNCITRAL Arbitration Rules 1976, which are the most popular ad hoc arbitration rules worldwide. They have been adapted and modernised for use in an institutional framework and provide some novel features, namely expedited procedure, joinder and consolidation of proceedings and broad inclusion of set-off defences.

One of the most significant innovations of the Swiss Rules as compared to other institutional rules is indeed the mandatory expedited procedure for small claims (amount of less than CHF 1 million in dispute) provided in Article 42. The expedited proceedings are particularly important in commodity trading where disputes are frequent, and Geneva, like London, is a key hub in this sector. The rules also allow for voluntary expedited proceedings even if the amount in dispute exceeds CHF 1 million.

The mechanism set out in the Swiss Rules ensures speed and cost-efficiency, but also make a clear allowance for the parties' right to be heard and for some flexibility. First, the rules provide for one round of pleadings "in principle", with no time limit set in advance, which means that further briefs may be submitted in appropriate circumstances. Secondly, a single hearing – for the examination of witnesses and for oral argument – has to take place, unless both parties agree that the arbitral tribunal should decide on the basis of the documentary evidence

alone. Thirdly, the expedited procedure applies automatically to all cases where the amount in dispute is below CHF 1 million, but "unless the Chambers decide otherwise, taking into account all relevant circumstances", which circumstances will include the complexity of the case (factual, legal and procedural) and the nature of the relief (e.g., declaratory relief). Fourthly, the case must be heard by a sole arbitrator unless the parties initially agreed and continue to insist on a three member tribunal. Fifthly, there is a six month time limit to render the award which may be extended in exceptional circumstances only, in particular be required where excessive speed would conflict with due process and the parties' right to be heard, typically if a party submits a lengthy expert opinion, or a substantial amount of documentary evidence, which call for more time for the other party to respond. However, contrary to other institutions, the Chambers apply strict control over time limits, and almost all accelerated proceedings are completed within the original six months period. Finally, the arbitral tribunal shall state the reasons upon which it relies in summary form, unless the parties have agreed that no reasons need to be given.

Another key set of features of the Swiss Rules is set out in Article 4 which allows for far reaching consolidation and joinder. First, new cases may be consolidated by the Chambers with an already pending and related arbitration even absent the parties' agreement and even amongst different parties, taking into "all circumstances, including the links between the two cases and the progress already made in the existing proceedings". Secondly, the Swiss Rules allow for the joinder of third parties upon request either of such third party or of a party to the arbitration. The arbitral tribunal decides on the application, again taking into account "all circumstances it deems relevant and applicable" and "after consulting with all parties" (and although not expressly stated, the Chambers) but the parties' consent is not required. In practice, these provisions have been applied and have not yet given rise to insuperable procedural obstacles.

The third significant feature of the Swiss Rules relates to set off defences. As in the UNCITRAL Arbitration Rules, the arbitral tribunal has jurisdiction to hear set-off defences. However, and this is new, this is so "even when the relationship out of which this defence is said to arise is not within the scope of the arbitration clause or is the object of another arbitration agreement or forum-selection clause". Nonetheless, where a counter-claim is brought independently rather than as a set-off, it must be covered by the arbitration agreement on which the main claim is based.

Key Features of the Swiss Rules of Commercial Mediation

In 2007, the Swiss Chambers adopted the Rules of Commercial Mediation of the Swiss Chambers of Commerce and Industry ("Mediation Rules"), thereby offering a complete and uniform set of rules for the resolution of commercial disputes.

Parties can resort to the Mediation Rules in the event that a dispute has already arisen and for future disputes. The seat of the mediation can be in Switzerland or abroad, but the Mediation Rules apply only to "commercial" mediation, and not family mediation or the like.

Like arbitration, mediation requires the consent of all the parties concerned. However, unlike for arbitration, the Chambers may be seized even in the absence of a mediation agreement or any agreement at all. Once the Chambers notify a request for mediation, the other party will have an opportunity to accept to proceed with the mediation, or not, and hence either not reply to the Chamber's notification or, preferably, refuse mediation explicitly.

The parties are free to designate any mediator they choose and there is no closed list. Unless the parties agree

otherwise, a single mediator is appointed. It may sometimes be useful to have two mediators, especially if the parties come from different cultural backgrounds or if the mediator requires a number of skills that cannot be found in a single individual.

Where the parties do not jointly designate a mediator, the Chambers will submit a list of at least three names to the parties, selected after considering the nature of the dispute and the required qualifications. It is advisable for a party who seizes the Chamber with a unilateral request for mediation to identify all the qualifications that may be required (e.g., industry experience, language, nationality). However, it is not advisable that the party name a possible mediator, as, if refused by the other party, s/he will be automatically excluded by the Chambers.

A party who disagrees with a default appointment made by the Chambers has a 5-day time limit to object to the appointment in writing, stating the reasons, which is rather strict. The rules have not been much tested yet, but it is expected that the Chambers will be lenient when considering objections.

All mediators must undertake to comply with the European Code of Conduct for Mediators, which is an attachment to the rules.

Once the mediator is appointed, the Chambers invite he or she to promptly convene the parties to a joint face to face preliminary session, but this is not mandatory. Generally, the parties are free to agree on the manner in which the mediation shall be conducted and will do so in a mediation agreement entered into also with the mediator.

The mediation can be terminated by either party at any time by notification in writing even if no preliminary meeting has been held, i.e., if in effect the mediation has not been properly started.

Finally, a settlement agreement will only put an end to the mediation if it is signed by all the relevant parties. The parties may opt out of this formality.

Two-tier Proceedings: Combining Mediation with Arbitration

The Mediation Rules can be combined with arbitration. They expressly refer to the possibility for the parties to agree in writing at any stage during the course of the mediation to submit all or part of their dispute to arbitration under the Swiss Arbitration Rules. This is simply a reminder to the parties that if mediation fails, arbitration, as opposed to litigation, may be an appropriate alternative. However, this provision does not intend to put in place arbitral tribunals that simply rubberstamp a settlement reached in the mediation. There must be a "dispute" and the submission of a Notice of Arbitration as provided for by the Swiss Arbitration Rules. On the other hand, the parties have the possibility to obtain an award on agreed terms under the Swiss Rules if they settle their dispute during the arbitration.

Somewhat surprisingly, the Mediation Rules (rather than the Swiss Arbitration Rules) also provide that, in case of an arbitration pending under the Swiss Arbitration Rules, not only the arbitrators, but also the Chambers may suggest that the parties mediate the dispute. However, unless the parties agree otherwise, the mediator cannot act as arbitrator, judge, expert, or as representative or advisor of one party in any subsequent proceedings initiated against one of the parties to the mediation. The problem is obviously that the mediator is likely to have obtained confidential *ex parte* information during the mediation.

The Swiss Mediation Rules, like most mediation rules, do not restrict the parties' freedom to initiate litigation or arbitration during the mediation. In fact, in jurisdictions where mediation does not interrupt time limits or where no clear authority to the contrary exists, a party may have to start formal proceedings to preserve its rights.

A restriction may however result from the rules governing the arbitration or litigation itself. For instance, a

court or arbitral tribunal might decide that, unless and until the mediation is initiated, conducted in good faith and fails, arbitration is premature because the right to arbitrate has not yet arisen. This would be an issue as to the validity of the arbitration agreement *(ratione temporis)*. This assumes that the complaining party objects to arbitration from the outset and does not proceed on the merits, and that it participated in good faith in the mediation; any objection would otherwise be considered abuse of right.

Whether the agreement to mediate can be enforced and a failure to mediate in good faith or at all give rise to a damages claim is a highly controversial issue. As a rule, it can be said that the clearer the mediation undertaking, the more likely it will be enforced and its (clear) breach sanctioned.

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The Unified Swiss Code of Civil Procedure: A Major Development in Swiss Litigation

BY SANDRINE GIROUD | LALIVE

The unified Swiss Code of Civil Procedure ("SCCP") will enter into force on 1 January 2011. It will mark one of the most important developments in the Swiss legal order since the unification of the substantive law in civil, commercial, and criminal matters at the beginning of the twentieth century.

Currently, each of the twenty-six cantons has its own code of civil procedure. These codes can differ substantially from each other given the varying influence of the Germanic and French legal traditions prevailing in Switzerland. In addition, the Federal Constitution and several federal statutes also contain procedural rules. Finally, the Swiss Federal Supreme Court has developed unwritten civil procedural law on several basic issues. This multiplicity of rules makes it both onerous and complex to take legal action in Switzerland and has been a source of legal uncertainty. The SCCP aims to eliminate these obstacles by way of a uniform civil procedural law. It is a relatively concise code of 408 articles regulating civil procedure and domestic arbitration. It largely draws on the existing cantonal codes, in particular those of the Swiss-German cantons. Its key features are as follows.

Residual Cantonal Competence: Judicial Organisation

While the regulation of civil procedure is now a federal competence, the judicial organisation remains in the hands of the cantons which are each autonomous in the administration of justice. Cantonal law will thus continue to determine the composition and the jurisdiction of the civil courts, as well as the cost of proceedings. Under the SCCP, cantons are also allowed to create specialised courts, e.g., commercial courts, courts in employment matters, or courts for landlord/tenant disputes. As a result of this cantonal judicial autonomy, it is likely that the existing cantonal practices, e.g., the use of laypersons as judges, will impact the further development of the SCCP.

Jurisdictional Provisions: Place of Jurisdiction in Contractual Matters

The Federal Act on the Place of Jurisdiction in Civil Matters enacted in 2001 now forms part of the SCCP with some minor changes. One of these changes worth noting relates to the introduction of a place of jurisdiction in contractual matters which has been formulated in similar terms to the Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters. Accordingly, proceedings can be commenced before the courts of the place of domicile of the defendant or before the courts of the place of performance of the characteristic obligation under the contract. This ends the distinction that has prevailed in Switzerland between domestic contractual matters and international contractual matters.

Alternative Dispute Resolution Mechanisms: Conciliation and Mediation

The SCCP encourages the settlement of disputes out of court by supplying the parties with two options: conciliation and mediation.

Conciliation proceedings are elevated to a formal procedural step and are now mandatory except in a limited number of cases, e.g. competition or IP matters. The plaintiff can also unilaterally reject conciliation in certain cases, e.g. when the defendant is domiciled abroad. Commencement of conciliation proceedings interrupts any statutory limitation period. Moreover, for disputes below CHF 5,000, the conciliation authority can submit a proposition of decision to the parties which will become final and binding unless one party objects to it within a period of twenty days.

Upon request of all the parties, conciliation proceedings can be replaced by mediation, before or during the course of proceedings that are already pending. Because neither the mediation proceedings nor the qualifications required to be a mediator are regulated by the SCCP, the parties are left to decide upon the mediator and the procedural rules applicable through a mediation agreement. Finally, the SCCP allows the parties to jointly apply for court approval of an out-of-court settlement agreement reached through mediation which, as a result, will have the effect of an enforceable judgment.

These novelties are of a great value and should help relieve the burden on the courts in civil proceedings.

Types of Proceedings: Ordinary, Simplified, and Summary

The SCCP provides for three types of proceedings. Ordinary proceedings apply to pecuniary disputes of high monetary value and to "economic" disputes, i.e., commercial, IP, or competition disputes. Conversely, simplified proceedings apply to small cases, i.e., with a value inferior to CHF 30,000, as well as to matters concerning "social issues", e.g., landlord/tenant disputes, employment disputes and consumer protection. The simplified proceedings are less formal, put greater emphasis on oral submissions and foresee a more active role of the courts. Finally, the SCCP provides for summary proceedings which go even further in terms of simplification and expediency. They apply, in particular, to urgent requests, requests for provisional measures, and also to "clear-cut cases", i.e., cases in which the facts are not in dispute or can be immediately proven, or cases in which the legal issues are straightforward.

Third-Party Interventions

The SCCP offers a wider range of options for third-party interventions. Not only can a party call a third party into the proceedings for assistance, but it can now also join a party by filing a third-party notice. Already in existence

in the cantons of Vaud, Valais, and Geneva, this last form of intervention is being introduced at the federal level for the first time. This should foster time and cost efficiency by avoiding contradictory judgments, making use of procedural synergies and avoiding multiple places of jurisdiction. A typical case for third party notice is where a seller is sued for damages by the buyer and wishes to join the distributor.

Class Action

The Swiss legislator has decided not to introduce the Anglo-American concept of class action. The view was taken that it is contrary to the Swiss legal system which rests on the fundamental principle that only the holder of a legal right can assert that right. It is thus up to the courts to deal with proceedings involving multiple parties by relying on existing procedural instruments, in particular the "association" claim for clubs and organisations and the general consolidation of claims, both of which have a bundling effect.

Provisional Measures: Pre-Emptive Brief

The SCCP now provides a powerful preventive measure for a party fearing the filing of an *ex-parte* injunction against it. The so-called pre-emptive brief allows a party to submit its position in advance to the court. This brief will only be communicated to the opposing party if and when it effectively requests an *ex-parte* injunction and shall remain in effect six months after being filed, after which period it must be renewed or extended if it is to have continued effect. This device will be particularly important in IP and competition matters, but is available in all areas where the issuing of an *ex parte* injunction is to be feared, e.g. freezing order proceedings, exequatur proceedings in relation to a foreign judgment under the Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters (Lugano Convention), or enforcement proceedings of a foreign arbitral award (*see* Domitille Baizeau, "Enforcement of foreign arbitral awards: the Swiss pro-enforcement framework and judicial approach" and Werner Jahnel "Freezing of assets held by foreign parties in Swiss banks").

Recognition and Enforcement of Decisions: Enforceable Deed

Besides the ordinary procedure for the enforcement of judgments, the SCCP now introduces the concept of the enforceable deed. Such deed entitles its holder to directly seek enforcement of the claims it contains in a similar manner to a judgment. This is especially important for creditors who can now benefit from simplified enforcement proceedings. This puts Switzerland in line with the other Contracting States to the Lugano Convention.

Indeed, the recognition and enforcement of foreign court decisions in Switzerland will also be improved by the simultaneous entry into force of the provisions implementing the revised Lugano Convention. These will provide a much needed clarification as to the form of provisional measures under the Lugano regime and will end the divergent cantonal practices in this respect.

Domestic Arbitration

The SCCP also replaces the Intercantonal Concordat on Arbitration which governs domestic arbitration, by providing much needed amendments based on the rules contained in the Swiss Private International Law Act ("PIL Act") which governs international arbitration (Chapter 12), such as the arbitral tribunal's jurisdiction to issue provisional measures, the facilitation of set-off claims, and the possibility to challenge the award directly before the Federal Supreme Court. Furthermore, parties to a dispute subject to domestic arbitration now have

the possibility to directly opt for the application of Chapter 12 of the PIL Act and, conversely, parties to a dispute subject to international arbitration and thus in principle governed by Chapter 12 of the PIL Act can opt for the application of the SCCP and the rules governing domestic arbitration.

Conclusion

The unification of civil procedure in Switzerland, which was first envisaged in 1872 by the Swiss legislator, is finally about to become reality. The SCCP will remove today's barriers which hinder the Swiss legal market in civil matters. Swiss lawyers will be able to provide their services in civil proceedings throughout Switzerland without facing procedural and legal obstacles. In turn, clients will largely benefit from the simplification and increased expediency of the new civil procedure. This historical development will help Switzerland enter the twenty-first century with the necessary tools to make it a competitive forum for litigation.

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Freezing of Assets Held by Foreign Parties in Swiss Banks

BY WERNER JAHNEL | LALIVE

Switzerland is without a doubt among the world's leading banking nations, holding a significant volume of foreign assets in its banks and financial institutions. The freezing of those assets by a creditor might become necessary in order to secure its monetary claims, either through the enforcement of a foreign judgment or arbitral award or by way of a freezing injunction granted as a provisional measure in ongoing court proceedings abroad or in contemplation of proceedings in Switzerland. In the majority of the Swiss cantons, the available measure for securing monetary claims is a freezing order *(séquestre)* obtained under the Federal Debt Enforcement and Bankruptcy Act 1889 ("DEB Act").

Conditions for Obtaining a Freezing Order from the Swiss Courts

The application for a freezing order against monies held in a bank account must be filed before the court at the place where the assets are located. Such place is deemed to be that of the bank's headquarters or that of the bank's subsidiary if the bank's headquarters are not located in Switzerland.

The freezing order will be granted if the creditor demonstrates *prima facie* that: (i) the creditor has a claim; (ii) there exists a ground for a freezing order under the DEB Act; and (iii) there are assets in Switzerland belonging to the debtor.

Regarding the existence of a claim and the grounds for a freezing order, the elements to be proven by the creditor will vary.

If the application is based on a judgment rendered in a Contracting State to the Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters (the Lugano Convention) or on

an arbitral award pursuant to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, all that is required is the filing of the original or certified copy of the judgment or award (and arbitration agreement), together with duly certified translations as the case may be.

However, if the judgment is rendered in a State not party to the Lugano Convention, the creditor has to meet the strict requirements for recognition and enforcement provided under the Swiss Private International Law Act (PIL Act), i.e., (i) the foreign court had jurisdiction; (ii) the decision is final and no ordinary appeal can be lodged; and (iii) its recognition would not be incompatible with Swiss public policy.

If the application is based on an interim measure such as a worldwide freezing injunction rendered by a court in a Contracting State to the Lugano Convention, the creditor must show that the injunction is enforceable in the country of origin; was rendered in *inter partes* proceedings; is not contrary to Swiss public policy; and sufficiently specifies the location of the assets frozen (no "fishing expedition" is allowed). However, if the injunction was rendered in a State which is not party to the Lugano Convention, the application will most probably not be granted; the prevailing view in Switzerland is that recognition of interim measures (including such injunctions) outside the Lugano Convention States is generally excluded. In this case, the creditor could still obtain a Swiss freezing order under the requirements set out below.

Where the application is not based on a judgment or an arbitral award or foreign freezing injunction, the purported creditor can indeed seize assets of debtors not domiciled in Switzerland if it can be shown that: (i) the alleged debt is due and that the alleged debt is not secured *in rem;* and (ii) the claim is based on a recognition of debt or the claim has a sufficient connection with Switzerland, e.g., the debtor's obligation was or is to be performed in Switzerland; the Swiss courts have jurisdiction on the merits; Swiss law is the applicable law to the merits; the litigious contract was concluded in Switzerland in the presence of the parties; however it is not a sufficient connection if the creditor or the debtor is a Swiss national or that the assets to be frozen are located in Switzerland.

In all the above cases, the creditor must demonstrate that the debtor has no domicile in Switzerland, or has no fixed domicile, or is concealing its assets, absconding or preparing to abscond so as to evade its obligations.

In addition, the creditor must also have sufficient evidence that the debtor has assets located within the jurisdiction of the court where the application is filed. The approach varies from one cantonal court to the next, but generally speaking, the more information the creditor has, the more likely is the granting of the freezing order. Swiss courts currently apply a stricter approach to this requirement than in the past, thereby disallowing any form of fishing expeditions.

The Procedure for Obtaining a Freezing Order

A freezing order is issued in ex parte expedited summary proceedings which usually last only a few days or even a few hours if urgency is established by the creditor. The court fees are modest, currently CHF 1,000 to CHF 2,000.

If the court grants the application, it issues a freezing order which is notified to the Debt Collection Office of the place where the assets are located. The Debt Collection Office notifies the creditor and the relevant bank or financial institution, but not the debtor so as to avoid any risk of removal of the assets. It is the bank which then informs the debtor. Meanwhile, the bank is obviously prohibited from disposing of the assets, and will be liable for damages if it does, which operates as a very effective deterrent.

Upon execution of the freezing order, the Debt Collection Office issues a freezing certificate to the creditor which lists the assets attached and provides an estimate of their value.

Following receipt of the freezing certificate, the creditor must pursue the claim within 10 days, generally by requesting a summons to pay from the Debt Collection Office. If the application is not based on a court judgment or an arbitral award, the freezing order will have to be validated by the creditor filing a law suit on the merits of the claim, either before the court which has jurisdiction to hear the claim on the merits, or before the court which granted the freezing order.

On the other hand, following notification of the freezing order, the debtor and the bank have ten days to appeal against the order to the court that granted it. The judge will then initiate *inter partes* summary (i.e., also expedited) proceedings and will examine the likelihood of the existence of the debt.

Proposed Amendment to the Federal Law

The Swiss legislator recently took the opportunity of the revision of the Lugano Convention (which will be implemented in Switzerland at the same time as the new Unified Swiss Code of Civil Procedure due to come into force in 2011) to propose the amendment of certain provisions of the DEB Act dealing with freezing orders. These amendments are subject to a possible request for referendum by the Swiss population until 1 April 2010 and will most probably not enter into force before 2011.

Three key changes are worth noting. First, all the Swiss courts will have to uniformly apply criteria set out in the DEB Act for the granting of freezing orders and temporary attachments will not be available. Secondly, if the debtor is domiciled in Switzerland obtaining a freezing order will be possible on the basis of a foreign or a Swiss court judgment without any further requirements. Thirdly, the court from which the freezing order is sought will have jurisdiction to grant an order regarding assets located within its own canton and within the whole of Switzerland.

Conclusion

To sum up, a creditor who seeks to freeze assets held by a foreign debtor in Swiss banks must simply produce an enforceable judgment or a claim with a sufficient connection with Switzerland as well as detailed evidence regarding the assets to be frozen. Once these conditions are fulfilled, Swiss courts are very efficient in granting freezing orders.

However, the proposed amendments to the relevant law would be a welcomed improvement for creditors seeking to pursue a foreign debtor as they will address difficulties resulting mainly from the shared jurisdiction of different courts as well as their non uniform practice.

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Enforcement of Foreign Arbitral Awards: The Swiss Pro-Enforcement Framework and Judicial Approach

BY DOMITILLE BAIZEAU | LALIVE

Switzerland is one of the leading countries for the conduct of international arbitration. It is also a significant place for the enforcement of foreign arbitral awards, i.e., awards rendered in international arbitral proceedings conducted outside Switzerland. This is primarily due to the large volume of financial assets held by foreign parties in Swiss banks and also to Geneva's role as a centre for commodity trading and related financial transactions.

Whilst the volume of relevant cases is modest (approximately forty cases in the last forty years), Switzerland's track record is rather good: there have been only two instances in the last twenty years where enforcement of a foreign award was denied. In brief, Switzerland can clearly be described as a pro-enforcement jurisdiction and as such should figure on foreign counsel's radar screens when considering asset tracing and enforcement of arbitral awards, and indeed court judgments.

Swiss Legal and Procedural Framework for Enforcement of Foreign Awards

The New York Convention on the Recognition and Enforcement of Arbitral Awards 1958, ("NY Convention") is the cornerstone for the enforcement of any foreign award in NY Convention Contracting States, including Switzerland. In particular it sets out the defences to recognition and enforcement available to a debtor. Pursuant to Article 194 of the Swiss Private International Law Act, it applies directly with respect to any arbitral awards rendered by an arbitral tribunal seated in a country other than Switzerland, even if that country is not a Contracting State to the NY Convention.

Procedurally, the enforcement of arbitral awards entails the availability of debt collection or other enforcement procedures, which in Switzerland are governed in part by Federal statutes and in part by local cantonal procedural rules, soon to be unified.

The enforcement procedure available depends on the nature of the relief awarded. Monetary awards are enforced through summary court proceeding under the Federal Debt Enforcement and Bankruptcy Act 1889 ("DEB Act"). Non monetary awards (orders for specific performance, restitution of a chattel, award or right in real property, and other injunctive relief) call for local cantonal proceedings. Mixed awards must be enforced through two sets of proceedings.

If the debtor is domiciled in Switzerland, the creditor must first request the Debt Collection Office of the place of domicile (which is not a court) to issue a summons to pay the amount due within twenty days. A court application is required only if a formal objection is then filed within ten days by the debtor. The matter will then be heard in summary court proceedings under cantonal procedural law. It is at that point that NY Convention defences can be raised by the debtor.

There are usually three levels of courts in Switzerland (first instance and appeal court at the cantonal level and the Federal Supreme court, where the appeal is more limited and based only on the parties' submissions). The time frame however is reasonable, typically a few months at each level, and the costs are modest and usually awarded to the winning party.

Once the debtor's objection to enforcement has been dismissed by a final court decision, the creditor can go

back to the Debt Collection Office for the continuation of the debt collection proceedings. The process is usually fast, unless the creditor requires the filing of insolvency proceedings against the debtor.

If the debtor is not domiciled but has assets in Switzerland, the procedure is the same except that, as a preliminary step, the creditor must first obtain an attachment or freezing order pursuant to the DEB Act from the court where the assets are located. During such procedure, whether *ex parte* only or followed by *inter partes* proceedings, the judge will only review the compliance of the arbitral award with the NY Convention on a *prima facie* basis (likelihood of a debt). Once the creditor obtains the freezing order, the award may be enforced against those assets through the normal debt collection procedure under the DEB Act as if the debtor was domiciled in Switzerland, as described above.

The Swiss Courts' Approach to Enforcement of Foreign Awards

From the available Swiss courts' decisions and the abundant doctrine (which plays an important role in the Swiss legal system), one can conclude that Switzerland is a pro-enforcement or at least a pro-NY Convention jurisdiction.

Under the NY Convention, as applied by the Swiss courts, arbitral awards will only be denied enforcement if one or more of the defences set out in Article V is established, namely:

- 1(a) Incapacity of a party; invalidity of the arbitration agreement (as defined in Article II(2) of NY Convention "agreement in writing");
- 1(b) Lack of proper notice of the proceedings; inability to present one's case (breach of due process);
- 1(c) Award covering a dispute outside the scope of the arbitration submission;
- 1(d) Arbitral tribunal not composed or arbitral procedure not conducted in accordance with parties' agreement or the law applicable;
- 1(e) Award not yet binding or set aside (challenged) or suspended;
- 2(a) Subject-matter of the dispute not capable of settlement by arbitration (arbitrability); and
- 2(b) Award in breach of public policy.

The burden of proof regarding the availability of the above defences falls to a large extent on the debtor seeking to resist enforcement. The last two defences may be raised by the courts on their own motion (i.e., even if not raised by the debtor) but not the first five, which have to be raised and argued. Notably, even where a defence is proven, enforcement may not be denied if the courts are satisfied that the debtor is acting or has acted in bad faith so that its defence amounts to an abuse of right, typically where the debtor never raised any objection during the arbitral proceedings.

On the specific grounds of Article V, the approach of the Swiss courts can be summarised as follows.

Regarding the requirement for the arbitration agreement to be in writing (Article V.1(a)), the courts do require a signed contract (even if the arbitration agreement may be incorporated by reference) or an exchange of communication (as per Article II.2). However, where those requirements are not met but the evidence clearly shows that the debtor had actual knowledge of the arbitration agreement, due for instance to its past dealings with the same party, the courts have allowed enforcement. The issue is particularly acute in shipping contracts usually concluded through a broker or signed by the carrier and the consignee but not the shipper.

Any defence pertaining to due process (Article V.1(b) & (d)) requires a serious breach, which was raised during the arbitral proceedings.

With respect to the defence of Article V.1(e) – award not yet binding, set aside or suspended – the Swiss courts adopt a predictable and sensible approach, in line with leading NY Convention commentaries. First, the award will be considered as binding even if still open to challenge proceedings in the country of the seat; or if it is not enforceable in that country. Secondly, the award can be enforced if subject to challenge proceedings (although a stay of enforcement may be granted under Article VI NY Convention), but it will not be enforced if it has already been set aside in the country of the seat (unlike in some other countries like France). Finally, the award will not be considered as "suspended" if suspended only by operation of procedural law rather than by a specific court decision.

The concept of arbitrability is very broad under Swiss law, so that the defence of Article V.2(a) (lack of arbitrability) is limited in scope. The defence of breach of public policy (Article V.2(b)) is equally limited, since a very serious breach is required. This defence has only been upheld in one case where the sole arbitrator had been identified in the arbitration agreement and could not be removed (if he was the agreement provided for a penalty of CHF 1 million); yet, he had acted as counsel for both parties on the underlying transaction. Enforcement was denied.

Finally, the Swiss courts tend to avoid excessive formalism when applying Article IV of NY Convention which sets out the documents required for enforcement, namely the authenticated original or certified copy of the award and of the arbitration agreement, together with a certified translation. This is particularly so when the party resisting enforcement does not actually dispute the existence of the arbitration agreement or of the award or the accuracy of a translation. However, caution is required as the approach may vary from one Canton to the next. Whilst an incomplete request can be completed at a later stage (including on appeal), the best approach is to provide, at the outset, all the relevant documents and certified translations, together with evidence that the award is enforceable and not suspended through copies of the relevant foreign legal provisions and even an affidavit of counsel explaining the legal position.

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Switzerland: A Leading Venue for International Arbitration

BY NORADÈLE RADJAI | LALIVE

Switzerland, a neutral country in the heart of Europe, has always been a popular venue for international commercial arbitration. Geneva and Zurich are amongst the four most frequently selected places for ICC Arbitrations worldwide whilst most ICC arbitrators come from Switzerland (ICC Bulletin Vol. 20/No. 1 (Spring 2009), 2008 Statistical Report). The reasons for this are clear from a review of the key features of international arbitration in Switzerland.

Concise Legal Framework Focused on Party Autonomy

Switzerland has adopted an arbitration-friendly law, embodied in Chapter 12 of the Swiss Private International Law Act (the PIL Act). This governs all international arbitrations with a seat in Switzerland, when at least one party does not have its usual place for business or domicile in the country. It is a concise and flexible piece of legislation that accommodates party autonomy, i.e., the parties' own terms in the arbitration agreement, including regarding the qualifications of the arbitrators; the arbitral procedure; the choice (or absence thereof) of specific arbitration rules and other matters.

Arbitrability of Disputes

Any dispute involving "an economic interest" may be the subject of an international arbitration in Switzerland. The Swiss courts interpret "economic interest" broadly and include matters such as competition law issues and expropriation disputes. There is a wide range of disputes referred to arbitration, although disputes most commonly involve construction projects, commodity trading, energy supply and licence agreements.

No Restrictive Requirements for the Arbitration Agreement

In international arbitration proceedings, the arbitration agreement must be made in writing, but this can be by fax or any other means of communication that permits it to be evidenced in writing (Article 178(1) PIL Act). An arbitration agreement is valid if it conforms to any of the following three laws: that chosen by the parties in the arbitration agreement; that applicable to the merits of the dispute; or Swiss law.

Under Swiss law, the main requirement is that the parties intended to submit their dispute to arbitration, which could include the mention of the word "arbitration". This requirement is construed rather widely. The clause must provide an indication of the dispute to be decided by way of arbitration. It is also strongly recommended that a specific Swiss city be designated as the seat of the arbitration and that the language of the arbitration be agreed.

Importantly, as in most arbitration-friendly countries, in Switzerland, the validity of the arbitration agreement itself cannot be challenged on the basis of an alleged invalidity of the underlying contract. Furthermore, the assignment of rights under a contract from the original party to another party usually entails the transfer of the arbitration agreement to the other party, unless the underlying contract itself specifically prohibits assignment.

Support of Swiss State Courts

The Swiss courts' intervention in arbitration is limited to lending support to the arbitrators and the parties. They do not otherwise interfere with the arbitration process. Their role consists essentially in the following:

- Recognition of arbitration agreements by denying the State courts' jurisdiction where there is a valid arbitration agreement (including refusal of jurisdiction if seized of a matter where there is a valid arbitration agreement in place);
- Appointment of arbitrators in the event that a party fails to do so;
- Enforcement of procedural orders issued by arbitral tribunals, including on the taking of evidence;
- Granting interim relief or conservatory measures where such cannot be granted by arbitral tribunals;
- Restricted review of the awards on specific grounds; and
- Enforcement of arbitral awards, whether or not rendered in Switzerland.

Jurisdiction of Arbitral Tribunal

The arbitral tribunal has the jurisdiction to decide whether it has jurisdiction or not *(kompetenz-kompetenz)* and can issue an interim award on its own jurisdiction. The arbitral tribunal's decision on its jurisdiction can generally be appealed before the Swiss Federal Supreme Court, but such an appeal must be filed immediately (Article 190(3) PIL Act).

Arbitral Awards

Arbitral awards must be made in writing, supported by reasons, dated and signed. The arbitral award shall be signed by a majority, or, in the absence of a majority, by the chairman alone (Article 189(2) PIL Act).

Challenges of Arbitral Awards

Switzerland benefits from an expeditious procedure for challenges of arbitral awards.

First, the PIL Act does not allow any appeal on the merits of the award, be it on a question of fact or on a question of law. Second, appeals can be made only on the following limited grounds set out in Article 190 PIL Act:

- The arbitral tribunal was incorrectly appointed or constituted;
- The arbitral tribunal has wrongly decided on its jurisdiction;
- The award has gone beyond the claims submitted to the arbitral tribunal or the arbitral tribunal has failed to decide one of the claims;
- The principle of equal treatment of the parties or their right to be heard in an adversarial procedure has not been observed;
- The award is not compatible with public policy.

A unique feature of Swiss arbitration law is that any setting aside procedures are referred to the highest Court in Switzerland, the Federal Supreme Court, whose decision is final. Applications must be within 30 days of the award being rendered and the decision of the Supreme Court is rendered promptly (within 3 to 6 months on average). This fast-track one-court procedure guarantees the parties a minimal review of the arbitral award. Therefore, the costs of post-award proceedings can be kept to a minimum.

It is possible for non-Swiss parties to expressly exclude, partially or entirely, the challenge of awards (Article 192 PIL Act).

A second means of review of arbitral awards rendered in Switzerland is available under the Swiss Judicial Organisation Act. The procedure (referred to in Switzerland as "revision") is applicable to any court decision and any arbitral award influenced by crime (even in the absence of any conviction), or where a party acquires subsequent knowledge of important facts or key evidence, which existed but could not be discovered before the decision was made or the award rendered.

Flexible Arbitration Procedure

The procedure before the arbitral tribunal may be freely determined. The only statutory requirement is that of due process, in particular the equal treatment of the parties and their opportunity to be heard, which consequently requires that the proceedings be conducted in an adversarial manner. This means that all parties

must be entitled to present their arguments and evidence, although there is no requirement for an oral hearing. The right to be heard does not include a requirement that the award be fully reasoned and address each of the parties' arguments. However, the right to be heard will be violated if the arbitral tribunal fails to draw the parties' attention to issues of law and to facts which it considers highly relevant in order to reach a decision, and which could not be anticipated by the parties, or if the arbitral tribunal fails to hear the parties' arguments on all relevant facts and law before rendering an award on its jurisdiction.

In addition to these minimum requirements, the arbitration proceedings may be subject to institutional rules, such as the Swiss Rules of International Arbitration administered by the Swiss Chambers or the Rules of Arbitration of the International Court of Arbitration of the ICC, if this has been agreed by the parties.

With respect to the venue of the arbitration, arbitral tribunals are free to hold any meeting, hearing or deliberations outside Switzerland, even if the legal seat of the arbitration remains in Switzerland.

The procedure adopted for the gathering of evidence will depend on the legal tradition of the parties and that of the arbitrators, even if the seat of the arbitration is in Switzerland. Generally, as is common practice in international arbitration, all forms of evidence will be admissible including oral testimony by the parties and third party witnesses, expert reports and inspections. Discovery of documents, as is common in US and UK litigation, is not compulsory but is common, even if more limited in scope.

The concept of confidentiality is based on the private character of arbitration proceedings. Whilst the PIL Act does not contain any regulations with regard to confidentiality, some Swiss law commentators suggest that there is an implied obligation to respect the confidentiality of arbitration in Switzerland.

The arbitral tribunal may, at the request of a party, order interim measures (Article 183 PIL Act). However, this power is generally limited to the parties involved in the arbitration and cannot extend to third parties.

Conclusion

Switzerland has for many years been a preferred place for international arbitration. This is no doubt the result of a combination of features unique to Switzerland: political neutrality, a geographically convenient location, a long tradition as the seat of international organisations (e.g., WTO, WIPO, UN, CAS, UNCC), its arbitration-friendly legislation and a well-developed legal system. Switzerland also hosts a high number of experienced Swiss and foreign arbitration practitioners. For all these reasons, Switzerland is often viewed as the best choice of venue when parties include an arbitration clause in an international commercial contract.

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Recent Procedural Developments in Swiss Civil Court Practice

BY DANIEL HOCHSTRASSER AND KARIN BEYELER | BÄR & KARRER

In Swiss state court litigation, a topic which has become increasingly important in recent years is the question to what extent parties have a right to submit briefs and comments to the court without being formally invited to do so. This question is closely related to a party's right to be heard and to present its case to the court which is guaranteed by Article 29 para. 2 of the Swiss Constitution as well as by Article 6 (1) of the European Convention on Human Rights ("Right to a fair trial").

In this respect, it should first be mentioned that in Swiss procedural law (in contrast to common law) the management and conduct of the proceedings are in the hands of the judge, not of the parties. The court has to ensure that the statutory procedural rules of the applicable Code of Civil Procedure and its own orders are complied with. Among these rules is the principle that parties may only submit the briefs which the Civil Procedure Code explicitly provides for (in particular, a statement of claim, answer, reply and rejoinder). Further briefs are only permitted in exceptional cases as defined in the Procedure Code.

For several years, however, there has been a trend that parties amend or extend their written briefs at trial by submitting further, unsolicited briefs in which they try to draw the court's attention to facts and circumstances which they deem to be important for the court's final decision on the merits of the case. Recent case law of the Swiss Federal Supreme Court has also contributed to this development. In implementation of the case law of the European Court for Human Rights pertaining to Article 6 (1) of the European Convention on Human Rights, the Federal Supreme Court has held that as a general principle it is for the parties to decide whether a brief of the counterparty contains new arguments and, therefore, requires further comment.

From this follows that it is not within the court's competence to assess whether a brief of a party contains new arguments which are relevant for the final decision and on which the other party, therefore, wants to comment. Rather, the court has a duty to immediately serve such brief on the counterparty, thereby allowing the counterparty the opportunity to submit its own point of view to the court with regard to the assertions made by the other party in the new brief. If a party is served with a new submission of the other party without being formally invited by the court to file its comments within a certain time-limit, such party must nevertheless give its comments on the new submission *immediately* (if it deems such comment necessary). If it does not react to the counterparty's new submission within an appropriate period of time, the court may legitimately assume that the party has waived its right to comment on the new submission, and the party will, therefore, be precluded from commenting on the new allegations in that submission later in the proceedings.

Another practically important issue is how civil courts must deal with so called "protective writs". A protective writ is an anticipatory brief which a potential respondent submits to the (competent) court in a situation in which the potential respondent anticipates that a claimant will request the court to issue an *ex parte* order against it. In the protective writ, the potential respondent either presents the reasons which speak against the issuance of an *ex parte* order or signals its willingness to appear before court in a hearing. A protective writ is, therefore, a preventive defence against an anticipated motion by another party to the court to issue an *ex parte* order and it is intended to prevent the issuance of such order.

The topic of protective writs often causes confusion among Swiss legal practitioners because until now, the

various civil courts of the 26 Swiss cantons have not followed a uniform practice in this regard. Some courts altogether refuse to receive protective writs. Other courts accept such a writ and serve it on the counterparty mentioned in it (i.e., the potential claimant). This practice basically defeats the purpose of the protective writ since, after having received the writ from the court, the potential claimant will know all the arguments of the potential respondent and it will, therefore, be in a position to either refute these arguments in its request for an *ex parte* order or to base its request on other arguments. Finally, still other courts accept protective writs and simply put them on file for a certain period of time. The writ will only be served on the other party (the potential claimant) if and when that party actually files a request for an *ex parte* order.

In January 2011, the new Federal Code of Civil Procedure will come into effect; it will replace the 26 cantonal civil procedure codes in force today and it will introduce uniform civil procedural rules for all civil courts in Switzerland. In the Federal Code of Civil Procedure, Swiss legislation has followed the third practice mentioned above with regard to protective writs. The new Code explicitly provides that a party which anticipates that an *ex parte* order will be issued against it may preventively explain its position to the court in a protective writ. As from January 2011, all Swiss courts will, therefore, have a duty to accept protective writs, which will only be served on the counterparty if and when that party does, in fact, file a petition for an *ex parte* order. The new Code also provides that a protective writ shall not be taken into account any later than six months after it has been filed.

Finally, another current topic of state court decisions is to what extent procedural law requires the parties to substantiate their factual allegations and denials. The Federal Supreme Court has upheld its practice according to which the parties must specify the essential facts in a *comprehensive and clear* (i.e. *concrete*) manner so that evidence may be taken on them. The respective requirements of substantiation result from the provisions invoked by a party and from the behaviour of the counterparty (in particular, denials). To meet the respective requirements is of paramount practical importance since in all cases where the principle of party presentation applies, all facts that have not been submitted to the court in a sufficiently substantiated manner are *regarded as non-proven*.

Even though it is difficult to circumscribe the requirements of substantiation in a general manner, one may nevertheless point out the most essential issues: in every written brief, the chronology of events should be clear, the factual allegations and legal arguments should be distinctly kept apart, the allegations should be so precise that the court may proceed to take evidence on them, and the factual allegations should cover the legal basis (or bases) of the claim(s).

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Recent and Upcoming Challenges to the Swiss Legal System

BY DANIEL HOCHSTRASSER AND KARIN BEYELER | BÄR & KARRER

Today, the court system in Switzerland is organised separately in each of the 26 cantons. This means that Switzerland has for the time being 26 different Civil Procedure Codes. However, this situation is about to change. By virtue of a popular vote in 2000, the legislative competence in the area of civil procedure has passed from the cantons to the Confederation. Consequently, the 26 cantonal codes will be replaced by a single Federal Code of Civil Procedure whose entry into force is expected for January 2011. The new Code will be a milestone statute for the Swiss litigation practice as it will unify to a large extent civil procedure in Switzerland. The fact that the 26 cantons of Switzerland give up their longstanding systems and institutions, which in fact vary considerably between the cantons, is a major step in a country where federalism is such an important feature of political life.

In the past year and also in the coming months, the challenge for the Swiss legal system has been and still will be to handle the cases resulting from the financial crisis in a competent and expeditious manner. Although the economic situation in Switzerland was healthy up until autumn 2008, it has not been able to escape the present economic downturn, which has affected financial institutions in particular, but also the economy as a whole. The Swiss central bank has slashed interest rates to maintain the country's commercial competitiveness and consumer spending.

Specifically, financial institutions, investment advisers and asset managers see themselves confronted with compensation claims from bank customers who were invested in Madoff Investment Securities. At the time of writing, many of these customers, through their legal counsel, have tried to negotiate an out-of-court settlement for their claims. However, because in many instances these negotiations will fail, state court litigation might follow against the involved institutions and persons for alleged breach of disclosure obligations and of duties to give proper advice.

One of the biggest cases, however, which resulted from the failure of Lehman Brothers and in which potentially hundreds of customers of the bank Credit Suisse could have filed an action against the bank for damages for the losses in their investments in products of Lehman Brothers, could be settled out of court in the course of the year 2009. The bank agreed to pay a total settlement sum of approximately CHF 150 million to indemnify nearly 3,700 Lehman victims.

In the coming months, however, the other big Swiss bank, UBS, could become a target of litigation in connection with its Global Property Fund. The bank had to close the fund in December 2008 because it lacked the liquidity to pay back investors who wanted to exit the fund. In December 2009, the bank decided to wind up the fund. Now, up to 107,000 customers, 20,000 of which are in Switzerland, could be damaged since they were invested in the fund and will not get their investments back. It is to be expected that some of the Swiss customers will start legal action against the bank if no amicable settlement can be reached in this matter.

Still in connection with the financial crisis, it should be mentioned that as of 1 January 2010, the Circular on remuneration schemes of the Swiss Financial Market Supervisory Authority entered into force. The Circular is a reaction to the experience made in recent years that remuneration schemes have a considerable impact on the risk management of financial institutions. The Circular is intended to have a lasting effect on remuneration practices (in particular with regard to variable remuneration) in the financial sector in that remuneration schemes should not create incentives to take inappropriate risks and thereby potentially destabilise the financial system. The Circular

applies to all banks, securities traders and insurance providers. However, implementation of the Circular is obligatory only for firms required to have at least CHF 2 billion in equity capital or as solvency.

Tougher economic times inevitably lead to more disputes and, consequently, to more activity for the legal profession. From a broader forensic perspective, fraudulent reporting and white-collar crime might increase as management struggles to cut costs, cope with fewer staff and increase productivity. As already mentioned, one can particularly observe an increase in disputes in connection with financial accounting activities and with asset management in which, for example, damages claims are raised by bank customers who allege a breach of the duty of care in respect of the management of clients' assets.

The Swiss legal system is expected to recognise the need to collect and electronically disclose case-critical information in advance of complex global cases. Furthermore, there is a growing tendency towards parallel litigation-arbitration, as parties try to gain an advantage by bringing ancillary jurisdictional issues.

At the time of writing, there are no class actions pending in Switzerland. In this connection it should first be mentioned that Swiss procedural law (also not the new Federal Code of Civil Procedure) does not provide for specific procedures dealing with class actions in the style of US class actions. However, if hundreds of practically identical actions are filed with a court, for reasons of economy of proceedings, the court will most likely advance some actions and postpone others which it might, later on, solve by following the decisions found in the earlier cases.

As groups of parties which are involved, in particular, in the above mentioned Madoff and Global Property Fund disputes, are currently attempting to join forces to seek compensation from implicated banks, it remains to be seen how the Swiss judicial system will deal with such mass cases if no out-of-court settlement can be found which will satisfy the damaged bank customers. An increase in class actions is also anticipated where, for instance, there are mass redundancies or damage to multiple holders of certain securities.

Another challenge to the Swiss legal system might come from companies which, when markets further decline, will be less likely to absorb losses themselves, and will be more inclined to seek to hold someone else liable. The Swiss judiciary appears to be more willing to grant injunctions specifically related to asset freezing and seizure, taking a less restrained approach than previously.

Moreover, as in 2009 the number of bankruptcies in Switzerland was as high as never before, this will presumably also result in more litigation, notably in connection with directors' and/or auditors' liabilities claims. Furthermore, unemployment figures in Switzerland are also currently at unprecedented levels; employment disputes are, therefore, likely to increase as a consequence of redundancy programs and claims for wrongful dismissal.

Finally, warranty claims and post-deal disputes may increase as acquired companies and joint ventures falter. However, as the M&A activity level shrinks due to current economic conditions, this increase may be offset by the decline in deals.

As the consequences from the economic downturn will most likely still be felt in 2011, the new Federal Code of Civil Procedure will have to prove itself immediately as it enters into force. In all such civil proceedings as mentioned above, as from 1 January 2011, the new Code will have to be consulted and complied with.

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AUSTRIA

Vienna as a Seat of Arbitration

BY SUSANNE WURZER | CHSH, CERHA HEMPEL SPIEGELFELD HLAWATI

Austria, especially Vienna, has always been an interesting place for international arbitration. Due to its geographic position in the "heart" of Europe, and due to its reputation as a neutral place, companies and corporations from all over the world often agree on arbitration in Austria in their international contracts even if no Austrian party is involved.

The Austrian regulations regarding arbitration are incorporated into the Austrian Code of Civil Procedure ("ACCP"). The current regulations entered into force on 1 July 2006 and brought the Austrian law in line with the UNCITRAL Model Law on International Commercial Arbitration ("Model Law"), although there are also some important distinctions. For this reason, many regulations will be familiar also to lawyers otherwise not perfectly acquainted with Austrian Law – and thus encourage them to use Vienna as a place of arbitration – whereas other regulations might be regarded as new and interesting solutions to well-known issues of arbitration law.

As we all know, the place of arbitration determines such important questions as the validity of the arbitration agreement or the grounds for challenging or setting aside arbitral awards. The purpose of this article therefore is to give practitioners from other jurisdictions a short overview of the most important features of arbitration in Austria.

Arbitrability

Under Austrian Law, any pecuniary claim within the jurisdiction of the courts of law may be made the subject of an arbitration agreement (Section 582 ACCP). The law does not distinguish between domestic and international arbitration or commercial and non-commercial disputes. Corporate disputes are generally arbitrable as well. However, not all kinds of disputes are encompassed. In particular, regarding disputes involving consumers or employees, specific rules apply.

The Arbitration Agreement

Under Austrian law, an arbitration agreement (either a separate agreement or as an arbitration clause within a contract) shall be in writing and must clearly express the intention of both parties to submit the dispute in question to arbitration.

Pursuant to section 583 ACCP the arbitration agreement shall be contained either in a written document signed by the parties or in any other means of communication which ensure a record (including email). Furthermore, a reference in the contract to another contract containing an arbitration clause constitutes a valid arbitration

agreement, if such reference suffices to make the other document part of the main contract.

The necessity of written form not only applies to the arbitration agreement itself, but also to a proxy which entitles to the conclusion of the arbitration agreement. Under Austrian law, a person who is not the legal representative of a company (like a CEO) needs a specific power of attorney for signing arbitration agreements. However, these restrictions do not apply to special agents with a standard proxy *("Prokurist")* and for representatives with a general commercial power of attorney.

Any formal defect of an arbitration agreement is deemed to be cured if a party pleads to the merits of the case without raising the issue of the invalidity of the arbitration agreement. In addition, if a party has relied on the validity of an arbitration agreement at an earlier point in time, it may generally not deny the validity later on.

The Constitution of the Arbitral Tribunal

Generally, the parties are free to agree on the number of arbitrators and the procedure for their appointment. However, party autonomy is limited as section 586 ACCP provides that if the parties have determined an even number of arbitrators, then these arbitrators shall determine a further person as "presiding arbitrator".

The parties are free to agree on the procedure regarding the appointment of the arbitrators. This is, of course, not necessary if they have chosen institutional arbitration like the so-called "Vienna Rules" (of the Vienna International Arbitral Centre of the Austrian Federal Economic Chamber) or the ICC Rules.

If there is no such agreement, the following procedure applies: In case of arbitrations with a sole arbitrator, the court (i.e., the competent court of commerce) will appoint the sole arbitrator upon request of one party, if the parties are unable to agree on the appointment within four weeks. In arbitrations with an arbitral tribunal consisting of three or more arbitrators each party shall appoint the same number of arbitrators and those arbitrators shall appoint the further arbitrator, who shall act as chairman of the arbitral tribunal. If a party fails to appoint an arbitrator within four weeks of receipt of a written request from the other party to do so, or if the other arbitrators do not appoint the chairman within four weeks, the appointment shall be made by the court.

Jurisdiction of the Arbitral Tribunal

Austrian Law expressly recognises the competence of the arbitral tribunal to decide on its own jurisdiction (competence-competence) and also provides for the possibility to render the decision on competence either together with the ruling on the merit in the case or by separate award.

A plea that the tribunal does not have jurisdiction shall be raised not later than at the time of the first submission on the subject matter of the dispute. An objection that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as such matter is raised. Later objections are inadmissible unless the default is sufficiently excused.

Although Austrian law does not explicitly provide for the separability of the arbitration clause, Austrian case law clearly recognises this doctrine. Under this case law, even if the parties claim that a contract is void from the very beginning (or if the contract is terminated), and seek an arbitral award on this issue, the arbitration agreement is not necessarily affected thereby.

The Conduct of the Arbitral Proceedings

Following section 594 ACCP the parties are free to agree on the arbitral procedure, e.g., by referring to arbitration

rules. By agreeing on the procedure for the conduct of the arbitration, the parties must, however, neither violate the mandatory statutory provisions nor the fundamental principles of arbitral procedure.

If the parties do not agree, the arbitral tribunal may conduct the proceedings in such a manner as it considers appropriate. However, the mandatory provisions of the Arbitration Act on the conduct of the proceedings have to be applied by the arbitral tribunal. These provisions regulate only a few important aspects, e.g., the regulation concerning procedural defaults whereby default of the claimant leads to a termination of the proceedings and default of the respondent may neither be regarded as an admission of the claimant's allegations nor hinder the continuation of the proceedings. Another important provision is section 579, which provides that a party is deemed to have waived its right to object to the violations of non-mandatory regulations if it does not object in undue time after having become aware of the failure.

Interim or Protective Measures

Austrian Law provides for the parallel competence of both courts and arbitral tribunals to issue interim and protective measures during arbitral proceedings. The parties therefore have the right to choose to which venue to apply.

Furthermore, Austrian law provides for the enforceability of such measures by arbitral tribunals. These regulations also apply if the seat of the tribunal is not in Austria, which means that also interim measures by a "foreign" arbitral tribunal may be enforced in Austria.

The Arbitral Award

In its award, the arbitral tribunal shall decide the dispute in accordance with such statutory provisions or rules of law as agreed upon by the parties. If the parties have not agreed upon an applicable law, the tribunal shall apply the provisions of law it considers as appropriate.

As a general rule, arbitral awards must be made in writing and signed by all arbitrators (the signature of the majority of all members of the arbitral tribunal shall suffice provided that the reason for any omitted signature is stated). Under Austrian Law, any award (thus also an award on agreed terms) shall state the reasons upon which it is based.

Recourse Against an Award

The Arbitration Act provides a uniform set of rules for recourses against awards and does not distinguish between awards on the merits and awards on jurisdiction. The reasons for setting aside an arbitral award largely correspond to article 5 of the New York Convention and to Article 34 of the Model Law. To give a short overview, Austrian Law recognises the following reasons for setting aside an award:

- relating to the arbitration agreement (e.g., lack of a valid arbitration agreement);
- relating to violations of the right to be heard;
- relating to the scope of the arbitration agreement (e.g., if the award deals with a dispute not contemplated by the arbitration agreement);
- relating to facts which would justify the reopening of court proceedings (e.g., forgery of important documents);
- relating to the constitution and composition of the arbitral tribunal;

- relating to procedural or substantive public policy; and
- relating to arbitrability.

If an award has been issued on a non-arbitrable matter or if an award violates Austrian public policy, this must be considered not only upon assertion by a party, but also ex officio (but, of course, only if the award is challenged by one party at all). All other reasons for setting aside an award will only be considered upon specific application of one of the parties.

Conclusion

As could be shown, Austrian regulations on arbitration are basically in line with the UNCITRAL Model Law. Where Austrian Law differs from the Model Law, the provisions are generally very party and arbitration friendly and safeguard an efficient conduct of the proceedings. All in all, by choosing Vienna, a place with a long tradition regarding arbitration, as the seat of their arbitration, parties can safeguard the applicability of a modern *lex arbitri*.

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Fast Track Arbitration in Austria

BY IRENE WELSER | CHSH, CERHA HEMPEL SPIEGELFELD HLAWATI

International Arbitration proceedings, it has to be admitted, sometimes tend to be lengthy and costly. Therefore, some organisations have developed specific regulations in order to accelerate arbitral proceedings. "Fast Track Arbitration" is a topic more and more "en vogue" in many international arbitration conferences; for example, it was one of the "hot topics" discussed at the Vienna Arbitration Days, a leading conference for international arbitration practitioners, taking place periodically in February. Even though "the" Austrian Arbitral Institution VIAC has not yet developed any specific rules for an expedited procedure, and also the Austrian Arbitration Law remains silent on this issue, we have recently seen quite some cases here in Vienna where arbitral tribunals successfully conducted "fast track" proceedings on the basis of a "procedural order No 1", in which both the Parties and the Arbitrators incorporated all their wishes, rules and maybe also hopes for a speedy procedure. What are the secrets to making fast track proceedings a success, and what are the risks?

Elements of Fast Track Arbitration

Amongst the recognised elements of fast track arbitration, the key element is strict time limits. They apply to the parties as well as to the arbitrators, and cover all stages of the proceedings starting from the nomination of the arbitrators, the mutual submissions of the parties, the presentation of evidence as well as the delivery of the

arbitral award. Furthermore, there is usually a limitation of procedural steps, often excluding an oral hearing and providing for written witness statements only. The use of modern means of communication is definitely essential.

All these elements perfectly comply with Austrian statutory law, which is, generally speaking, built after the UNCITRAL Model Law, and, in Section 594 Austrian Code of Civil Procedure (ACCP), leaves it to the parties to agree freely on the procedure to be followed by the arbitral tribunal; in the absence of such agreement, the arbitral tribunal may conduct the arbitration in any manner it considers appropriate. The principle of fair treatment and the right to be heard do not limit fast track arbitration, but rather encourage the arbitral tribunal to act in a time- and cost-efficient manner. Further, Section 598 ACCP leaves it to the arbitral tribunal to either hold oral hearings or to conduct the proceedings in writing, unless otherwise requested by the parties. Thus, Austrian law has all what is necessary to successfully conduct fast track arbitration proceedings.

Pros and Cons

Even though the idea of conducting an arbitration at high speed is stunning and fascinating, the pros and cons should be carefully outweighed. Not every case is suitable for fast track arbitration.

Advantages of fast track proceedings are not only a speedy procedure as such, but also the concentration on material questions and key evidence. This may lead to negative effects, if there are a lot of side problems to be considered, or if the case is largely dependent on "soft facts" or personal impressions of witnesses that call for the need of being proven by oral statements. As all facts and arguments usually have to be laid on the table at the very beginning, surprises during the proceedings are rare. This, however, leads to the consequence that tactical aspects must step back, because if an argument or a means of evidence is introduced in the proceedings at too late a stage, there is a risk that it will not be admitted any more. On the other hand, there is a wider range of party autonomy. The parties are, in principle, free to adjust the arbitration procedure exactly to their needs and may thus design a tailor-made procedure. On the other hand, this requires the parties to define their needs and expectations at a fairly early stage, if not already in the arbitration clause. This may cause problems, if, at the time when the case goes to arbitration, the parties pursue contrary aims as to the length and complexity of the proceedings. Another crucial advantage is the time-factor – needless to say – that usually makes interim measures obsolete, and, hopefully, the lower costs.

Disadvantages – are there any? It must be admitted that there are. First, fast track proceedings are definitely not suitable if the questions to be solved largely depend on expert opinions. With short time limits of three or six months to be met, it is definitely unrealistic that the arbitral tribunal will find the time to hear experts. Second, in fast track proceedings frequently a lower degree of proof will be deemed sufficient. Preparation efforts for parties and legal counsel are generally demanding and it must not be forgotten that the necessarily short time limits will usually not be extended, even in case of public holidays, unforeseen absences or the like. Another aspect is that it may be hard to find one or more experienced arbitrators who embrace the short time frames that the proceedings entail. The biggest "show-stopper", however, is a defendant who is reluctant to cooperate. Even though the non compliance with strict time-limits or prescription rules will usually be to the detriment of the non-complying party, there is a certain risk that the defaulting party tries to take legal measures against a fast track arbitration award. Also in this respect, however, Austrian law gives comfort to the parties choosing fast track procedures, as outlined below.

Fast Track – No Ground for Rescission of an Arbitral Award

According to Section 611 ACCP, possibilities for a recourse against an arbitral award before state courts are very limited. An application to set aside such award will only be successful in really severe cases. Unlike the UNCITRAL Model Law, not even every deviation in the conduct of the proceedings from the parties' agreement constitutes a ground for rescission, but a challenge would only be successful if the arbitration proceedings were conducted in a way violating Austrian public policy; this will hardly ever be the case with fast track proceedings that have been conducted in accordance with international standards. Inability of a party to present its case is a further – theoretical – ground for rescission, which however, according to Austrian case law and doctrine, would only apply if a party has not been heard at all, and definitely not in case of merely tight time limits.

It must be noted that both of these – theoretical – grounds for setting aside an arbitral award are perfectly in line with the New York Convention on the Recognition and Enforcement of Arbitral awards: According to its Article V, Section 1(b), an award will not be recognised if the party against which it shall be invoked was unable to present its case. According to Article V, Section 2(b), an award that violates the public policy of that country will not be recognised either. Thus, both – theoretical – grounds for rescission of fast track awards under Austrian law fully comply with the grounds for unenforceability under the New York Convention – and will clearly not be fulfilled in case of fast track proceedings that have been conducted *lege artis*.

Future Developments

As Vienna is an important place for international arbitration, Austrian arbitrators have followed the trend of fast track proceedings closely. On the basis of a well-balanced procedural order No 1, quite a few "fast track" proceedings have been successfully completed. Currently, an informal group of arbitration experts think about establishing a new standard for such procedure. But even prior to the establishment of such a new standard-procedure for fast track-arbitration, anyone who decides to try fast track proceedings in Austria will definitely not be disappointed.

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Class Actions: Made in Austria

BY CHRISTINA GLANZER | CHSH, CERHA HEMPEL SPIEGELFELD HLAWATI

For several years there have been attempts to implement a legal framework for class actions into Austrian procedural law which have not come to a successful end so far. Especially the Austrian Code of Civil Procedure (""ACCP") does not contain appropriate provisions for the organisation of mass proceedings, i.e., legal proceedings with a great number of claimants, yet. Although Austrian legal practice has developed so-called "class actions under Austrian law", these "class actions" differ from class actions, for example, in the U.S. legal system, in many ways.

This paper gives an overview of the specifics of the Austrian type of "class actions" and a short outlook on

legislative projects in the area of class actions in Austria.

"Class Actions" under Austrian law

The starting point for the development of "class actions" under Austrian law involved several hundred Austrian tourists in a hotel in Turkey. The tourists suspected the hotel operator of having offered spoiled food and intended to sue the tour operator (who was the contract partner of all the tourists concerned) for damages. None of these individual claims exceeded €2,000. In the light of comparably high legal charges it was rather unlikely that the majority of the tourists concerned would collect their (minor) claims in individual proceedings. Instead, they decided to assign their claims for collection to the Austrian Consumer Association ("VKI") for the purpose of collective assertion against the tour operator. Additionally the VKI called in a finance company which funded the lawsuit and took the litigation cost risk in return for an incentive payment in case of success. This approach allowed the tourists to lodge their comparably minor claims "substituted" by the VKI without any litigation cost risk, which was shifted to the VKI and the finance company respectively. On the other hand the total amount of the collected claims and the prospect of the incentive payment made it attractive for the finance company to fund the lawsuit (Comp. ecolex 2005, 744).

This case can be considered as the hour of birth of "class actions under Austrian law" and has been followed by many others in different areas by now, such as claims for damages of consumers in respect of illegal escalation clauses in loan agreements or in connection with the damages caused by the cable car catastrophe in the skiing area of Kaprun, where over 150 people were killed. Most current example of this Austrian type of class action is the claim brought by the VKI representing several thousand people being potentially damaged by a financial service provider due to incorrect financial advice.

In a nutshell, the Austrian system of "class actions" is accordingly composed of the following elements:

Individuals assign their individual claims to an association for the purpose of filing a complaint in court (joinder of actions according to § 227 ACCP. The consequence of such a joinder of actions is that several claims can be dealt with in just one single lawsuit and a joint judgement can be rendered. A joinder of actions requires that jurisdiction of the court is reserved for all claims and that the same form of proceeding is admissible).

The suing association usually is a licensed company, but can also be an "ad hoc" founded association (Comp. ÖBA 2004, 615). In practice, class actions in Austria are filed by licensed federations such as the VKI or Regional Workers´ Associations.

This system is usually accompanied by the intervention of a litigation finance company which funds the lawsuit in return for an incentive payment (usually 30% of the awarded amount in the case of success).

This approach secures that even minor claims and claims of financially weak claimants can be lodged which might not have been sued individually otherwise in the light of comparably high legal costs. The assignment for collection to an association such as the VKI is a form of a trustee relationship and makes sure that the assignors remain economically entitled to the claims.

Under U.S. law all potential claimants are affected by the court's decision unless they opted out of the collective lawsuit and the action is filed in the name of all potential claimants without appointing them individually. By contrast, in Austria the claimants are free to decide whether to assign their claims for "class action" or to sue them individually. However, even if they join the "class action" the latter still needs to appoint the claimants and their claims individually.

Critical voices argued that the Austrian system of funding the lawsuit by a litigation finance company in return for an incentive payment was not compatible with the Austrian prohibition of quota litis and contrary to public policy. However the Austrian Supreme Court meanwhile confirmed the legitimacy of this system ("class action under Austrian law") with the restriction that all the claims collected have to be based on similar grounds and that the court has jurisdiction in regard of all the claims (See OGH 12.7.2005, 4 Ob 116/05 w.). The Austrian Bar association also confirmed that an Austrian attorney who appeared in a "class action" proceeding acted in accordance with the Austrian conduct rules.

The advantages of class actions are certainly obvious: Similar (legal) questions are clarified consistently in just one lawsuit; in the light of a system of declining legal costs in Austria one lawsuit with a high amount in dispute might be expensive, but still is proportionally cheaper than several lawsuits with minor amounts in dispute.

On the other hand this specific system of class actions in Austria requires the assignment of individual claims to a third party; legal provisions for the organisation of such "mass proceedings" are still missing; besides, in international cases, foreign consumers have to keep in mind that they might lose the benefit of forum actoris according to Art. 15 ff. EuGVVO if they assign their claims to an association (Comp. ecolex 2005, 745f).

Legal rules for collective claims only exist in connection with actions of licensed federations, such as the VKI, the Austrian Federal Economic Chamber and the Federal Chamber of Labour so far (*"Verbandsklage";* see Art. 28 ff. of the Austrian Consumer Protection Act ("KSchG")). However, under the Austrian Consumer Protection Act these federations have basically the sole competence to file actions for injunction in regard of illegal general terms and conditions and therefore are no appropriate legal framework for collective private enforcement. Thus an elementary legal framework for "real" class actions in Austria is not available so far.

Legal Projects for the Organisation of Class Actions in Austria

In 2004 the Austrian Parliament requested the Austrian Federal Minister for Justice to examine potential legislation measures and to discuss amendments to the ACCP to provide a cost-effective and appropriate way to deal with mass lawsuits in Austria. This discussion was opened with a conference held in Vienna in June 2005 and resulted in an amendment draft to the ACCP (Cf. government bill addendum No 89, 24th legislative period of the Austrian Parliament) in 2007, which finally failed obviously because the ideas of the concept and its details diverted too much. However according to the current government program of the coalition parties there are still plans for organising mass proceedings within the Austrian procedural law; this government program already mentions specific conditions, such as a minimum amount of claimants (100 individuals), a minimum amount in dispute (€20,000) and a required deposit bagged by the claimants as a security for the counter party.

Still in the latest amendment to the ACCP, which came into force in 2009, regulations on class actions are not to be found (See Federal Law Gazette I 2009/30 ("ZVN 2009")). The implementation of a legal framework for "real" class actions in Austria in the near future therefore seems to be rather unlikely.

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New Trends in Austrian Litigation

BY MICHAELA SIEGWART | CHSH CERHA HEMPEL SPIEGELFELD HLAWATI

In the past year the Austrian Code of Civil Procedure (the "ACCP") faced two major amendments. Some of the new rules are intended to reduce legal costs as well as the work load of the courts and to speed up proceedings. Other amendments, such as the implementation of the EC regulations no. 1896/2006 and no. 861/2007, are at the same time aimed at a more effective access to justice in European cross-border litigation. The following is a short survey of some of the changes that will be of particular relevance in national and cross-border litigation practice.

Order for Payment Procedure

Already long before the EC regulation no. 1896/2006 created a European order for payment procedure, the ACCP provided for a comparable national order for payment procedure based on the use of standard forms. Similarly to the European procedure, the national procedure applies to the collection of uncontested pecuniary claims. Likewise, the defendant has the option to pay either the amount awarded or to lodge a statement of opposition within the time limit. This statement of opposition has the effect that the order invalidates and that ordinary civil proceedings are initiated. Unlike orders for payment within the scope of the mentioned EC regulation, the Austrian order for payment procedure is not applicable in case the defendant has his seat or main residence outside Austria, so that the national procedure is very often unavailable in cross-border cases. Furthermore, the issuance of an Austrian order for payment is restricted to claims with a maximum value, which was recently raised from €30,000 to €75,000. By contrast, the EC regulation does not provide for comparable limits. The Austrian procedure also differs from the European procedure inasmuch as it applies to pecuniary civil or commercial claims of basically any kind, whereas Art 2 of the EC regulation basically excludes, among others, claims arising from non-contractual obligations. Finally, it should be borne in mind that the national time limit for the lodging of the opposition is 4 weeks of service, whereas the regulation provides for a 30 days limit.

According to the EC regulation no. 1896/2006, the European order for payment procedure established therein should serve as an additional and optional means for the claimant, who remains free to resort to a procedure provided for by national law. Art 26 of the regulation holds that all procedural issues not specifically dealt with therein shall be governed by national law. Accordingly, the Austrian order for payment procedure has been basically retained unchanged. Some supplementary procedural rules were furnished within the system of the ACCP in relation to the European procedure, which provide for the following: at first, the order for payment procedure is centred before the Regional Commercial Court of Vienna that has the exclusive competence to issue the order for payment and also to review the order for payment in exceptional cases according to Art 20 of the regulation. Apart from these cases, further remedies, in particular the right to restitution in integrum, do not apply if the defendant misses the time limit for the opposition.

If a statement of opposition was lodged by the defendant in time, the applicant is requested to name the court having competent jurisdiction within 30 days. In the following, the Regional Commercial Court of Vienna has to either transfer the matter to the court named by the applicant or, in the case of delay, to reject the claim. Considering that the order for payment procedure is based on the use of standard forms and also considering that the defendant is not bound to specify the reasons for contesting the claim in the statement of opposition under the

regulation, the court may request supplementary statements from both parties, in particular from the defendant, before it calls a hearing.

Small Claims Procedure

EC regulation no 861/2007 simplifies and speeds up litigation in small cross-border cases. The regulation establishes a European Small Claims Procedure as an alternative to the existing procedure under the laws of the member states, where the value of a claim does not exceed €2000.

Subject to the provisions of the regulation, the procedure shall be governed by the national law. In this context, Art 548 ACCP clarifies that the national procedural rules applicable depend on the respective matter in dispute. Some supplementary national provisions deal with the procedure following the submission of a counterclaim, with the rendering of a judgement by default and with the review of the judgment pursuant to Art 18 of the regulation.

Legal Aid

In Austrian litigation, legal aid is granted to persons who are unable to meet the costs of proceedings as a result of their economic situation, provided that the conduct of the case does neither appear as wilful nor as manifestly unfounded. Under these circumstances legal aid was also granted to legal bodies and other entities having legal capacity in the past, whereas as of July 1, 2009 only natural persons are entitled to receive legal aid. This amendment intends to avoid the delay of bankruptcy of legal entities and to reduce the risks involved therewith for the opposing party, also considering European trends to decrease the minimum capital funds of legal entities. In any case the restriction to natural persons as receivers of legal aid seems to be in line with the legal system in the majority of European countries and also complies with EC directive no. 2002/8 that establishes minimum common rules relating to legal aid in cross-border disputes.

Appellate Proceedings

Contrary to the proceedings of first instance, appellate proceedings are mainly organised as a written procedure. Following the statement of appeal and the response statement hereto, the appellate court may hold a hearing whenever the court regards it as necessary, e.g., if it has reservations against the consideration of evidence. Until recently, appellate hearings were, aside from small claim procedures, also mandatory as long as none of the parties abandoned it. Speaking from my own experience, there was a tendency to explicitly request an appellate hearing in the statement of appeal even in cases where the hearing was neither required nor even reasonable. As a consequence, the hearing was quite often restricted to a repetition of what had already been pleaded in the statements.

This concept of appellate proceedings has now changed insofar as the appellate court is no longer bound to hold a hearing at the parties' request, but only if the court itself considers it necessary, in particular in regard to the complexity of the case. It may be expected that this amendment will significantly reduce the number of hearings before the appellate courts without changing the proceeding for the worse.

Cost Assessment

Also in Austrian litigation the unsuccessful party bears the adequate and reasonable costs in total or on a pro-rata basis. For this purpose, Art 54 ACCP commits the parties to substantiate the costs incurred and to deliver a

respective schedule in the hearing preceding the court's assessment of costs at the latest. The assessment of costs is subject to separate appeal if the unsuccessful party leaves the decision on the merits uncontested. In the context of cost assessment, the amendment of Art 54 para 1a ACCP will be of particular relevance in practice: With effect from July 1, 2009 the parties are committed to object to the opposing party's costs within 14 days, if they consider certain items unfounded. The court has to assess the costs on the basis of the successful party's schedule as far as they have not been objected to by the opposing party. This provision leaves some scope for interpretation. Legal documents suggest that, failing founded objections lodged by the opposing party, the court may not even verify the schedule and adjudge costs as listed therein. However, meanwhile it has been ruled that this is not true in cases of obvious inadequacy or miscalculation.

Thresholds

Finally, a number of procedural thresholds and maximum amounts were inflation-adjusted in the course of the 2009 amendments, some of them even noticeably above average. Without making a claim to be complete, some modifications may be described, as follows.

Among others, the right to bring an appeal before the Supreme Court basically requires that the value in litigation exceeds certain minimum amounts. These amounts were raised from €20,000 to €30,000 (regarding decisions) rsp. from €4,000 to €5,000 (regarding court orders other than decisions). As yet, the right to appeal against the decision of first instance was restricted in small claim procedures with a value in litigation not exceeding €2,000. This threshold is now raised to €2,700. Furthermore, legal representation before the district courts is now mandatory as soon as the value in litigation exceeds €5,000 (instead of €4,000 as before). As mentioned above the existing Austrian payment order procedure now allows the issue payment orders with a value of the claim not exceeding €75,000 (instead of €30,000 as before).

Conclusion

Summing up, the 2009 amendments implement a number of procedural changes in Austrian litigation, some of which have been triggered by EC law. As the amendments were passed only in 2009, little experience with their effects on litigation is available so far, which is in particular true of the aspect of smooth coexistence of national and European order for payment procedures and small claim procedures. The future practice will show whether the amendments will achieve their objective to simplify, to speed up and at the same time to amend civil proceedings.

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CZECH REPUBLIC

Czech Republic – Arbitration and ADR

BY VÍT HORÁCEK | GLATZOVA & CO.

The Czech Republic is a typical civil law country. In the last twenty years, however, there has been substantial advancement in arbitration, thanks to the development of the business environment and project investments in Czech businesses following industry privatisation. We may have seen thousands of arbitrations in recent years.

There are two major acts regulating litigation and arbitration: the Civil Procedure Code and the Act on arbitration proceedings and enforcement of arbitral awards (the "Arbitration Act"). The Arbitration Act allows for arbitral resolution of disputes only if the subject-matter of the dispute is property or property related matters.

Arbitration and enforcement of arbitral awards coming from foreign countries is a standard practice nowadays and it also has to be stressed that the Czech Republic is already a firm part of the European Union and the European law system.

The Arbitral proceedings are not very complicated and are based on standard arbitration principles known under UNCITRAL or ICC rules. Arbitration therefore represents a relatively reliable way to settle a dispute outside the courts. One further advantage is that arbitral award is generally recognised by local courts.

The Czech Civil Code grants the right to annul/cancel the arbitration award if:

- the award was issued in a case where no valid arbitration agreement was possible;
- the arbitration agreement was invalid or was cancelled or was not applicable to the case;
- the arbitrator was unable or had no right to arbitrate;
- the award was not decided by the majority of the panel;
- one of the parties was not granted the right to arbitrate the case properly;
- the award gives a party an obligation not requested by the claimant or to perform activities not allowed or not possible under local law; or
- there are circumstances in which a civil proceeding can by reopened, i.e.: (i) there are new facts that could not have been used in the previous hearings; or (ii) it is possible to provide evidence not presented in the previous hearings, provided it may provide a more favourable decision for the complaining party in the hearing.

In recent years numerous cases have been brought before Czech courts where there are doubts about the impartiality of the arbitrator or it is argued that there was no possibility of arbitrating the case properly. In general the courts dismiss these cases, with only minor exceptions. It is safe to conclude, therefore, that arbitration awards are standard and will secure the legitimate interests of the disputing parties.

As in other countries, arbitral proceedings may be carried out by and the dispute decided before either permanent or ad hoc arbitral court/arbitrator(s). This issue must be addressed in the arbitration clause (or agreement). The arbitrators are also allowed to decide, if so agreed by the Parties, ex equo at bono.

There are different permanent arbitration courts in the Czech Republic. The most reputable is the Arbitration Court attached to the Economic Chamber of the Czech Republic and the Agricultural Chamber of the Czech Republic. Others include the Prague Stock Exchange Arbitration Court and the Arbitration Court attached to the Commodity Stock Exchange in Kladno.

The Arbitration Court attached to the Economic Chamber and the Agricultural Chamber is the most important arbitration court in the Czech Republic. Hundreds of cases are arbitrated in this court, and most arbitration agreements and disputes are referred to this court. Hearings at this court follow two sets of rules, for international and domestic disputes respectively. Generally, the rules are very straightforward and do not differ substantially. There are provisions that may be of interest of the parties: the possibility or arbitrating in different foreign languages; so-called simplified procedures, where decisions are made on the basis of written documents only or without giving a reason for the arbitration awards; even accelerated proceedings can be applied for, provided extra fees are paid to the Arbitration Court.

As to the interim measures, the permanent Arbitration Courts and Ad hoc Arbitration Panels are very reluctant to issue interim measures in the Czech Republic. The best way to achieve an interim measure is therefore to apply to the civil code to issue an interim measure (preliminary injunction).

In practice, if it is proven that there is a strong reason for assurance of an interim measure, the Czech courts are willing to issue such a decision. Standard preliminary injunctions prohibiting the parties from selling assets or instructing the parties to stop harmful activities for an interim period are issued within seven days of an application to the civil court.

The courts are not, however, very willing to provide interim measures to protect evidence of the parties. It is also not very common and therefore it is not advisable to count on interim measures in the Czech environment.

The Czech Republic is getting more acquainted with alternative dispute resolution (ADR) methods, including mediation. ADR in the Czech Republic has been based on specific agreements linked to specific disputes, and performed on the basis of ad hoc agreement between the parties and arbitrators in such disputes. There is a very specific ADR process linked to EU domain names, and generally domain names called according to ICANN unify the dispute resolution process – UDRP.

The Arbitration Court attached to the Economic Chamber and Agricultural Chamber of the Czech Republic is the dispute resolution centre for ".eu" domain name disputes. This arbitration court also recently became a dispute resolution centre for ICANN for UDRP, top level domain names. These ADR proceedings started from January 2009.

The European Registry of Internet Domain Names (EURid) offers an alternative procedure for solving disputes about ".eu" domain names. This ADR proceeding is facilitated by the Czech Arbitration Court, which administers it in line with the Public Policy Rules for ".eu" of the European Commission (EC Regulation No. 874/2004).

It must be emphasised that this ".eu" dispute resolution proceeding is not an arbitration proceeding but rather a form of alternative dispute resolution. That is, the decision is not issued in the form of an arbitration

award but on the basis of an agreement of the parties to submit the decision to the court and to respect this decision.

Any person or entity may initiate ADR proceedings by submitting a complaint in accordance with the procedural rules. A complaint may be filed: (i) against the holder of the disputed domain name; or (ii) against the registry. The registry means the entity entrusted by the European Commission with the organisation, administration and management of the ".eu" domain designated in accordance with the procedure established in article 3 of EC Regulation No. 733/2002.

The remedies available against the respondent in (i) above shall be limited to either revocation of the disputed domain name(s) or, if the complainant satisfies the general eligibility criteria for registration set out in the aforementioned EC Regulation, the transfer of the disputed domain name(s) to the complainant. The main remedy available pursuant to the ADR rules in (ii) above shall be the annulment of the disputed decision taken by the registry. The panel may also decide, however, that the domain name in question shall be transferred, revoked or attributed.

To conclude, it can be confirmed that the Czech Republic is now a standard civil law country with propriety disputed resolution processes either at the civil court or arbitration and/or ADR matters. Based on the different approach and business knowledge of arbitrators, it is, however, advisable to go through arbitration and all ADR options rather than the rather time consuming route of civil court proceedings.

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SWEDEN

Arbitration in Sweden under Bilateral Investment Treaties and the Energy Charter Treaty

BY ULF HÅRDEMAN AND OLOF RÅGMARK | ADVOKATFIRMAN DELPHI

Sweden is traditionally considered as a good neutral forum for international disputes. The Arbitration Institute of the Stockholm Chamber of Commerce (the "SCC") has long held an established position for so called east and west disputes and is today administrating a significant number of international investment disputes. Nineteen investment disputes had been initiated at the SCC up to the end of 2006 (the very first investment dispute was initiated at the International Centre for Settlement of Investment Disputes ICSID as late as in the 1980s). At the end of 2008, the number of investment proceedings at the SCC had grown to 27 (of which 7 were initiated in the course of 2008). Of these 27 disputes, 19 were requested under Bilateral Investment Treaties ("BITs"), 5 under the Energy Charter Treaty ("ECT") and 3 under contracts between disputing parties.

The possibility for a foreign investor to proceed against the host nation finds its basis in different international treaties or individual investment contracts. These documents contain an open offer of arbitration that the foreign investor is free to accept by requesting arbitration. The offer is often for different institutional proceedings (ICSID, ICC or SCC) but also ad hoc arbitration under the UNCITRAL rules may be available. These documents will also carry the undertakings that the host nation has made for the protection of investors which might be breached by the host nation to the detriment of the investor.

ICSID is an organisation under the World Bank and is an international forum for investment disputes. Some 140 nations are members. Proceedings administrated by ICSID are specific since awards are enforced not under national laws but directly under the ICSID convention and appeals are handled under the ICSID convention by a separate tribunal. Thus, as no local courts are authorised to scrutinise the awards, ICSID awards are considered as somewhat "stronger" than ordinary New York convention awards.

In the course of the 1990s the ECT was created to protect investments within the energy field. Under the ECT the investor may choose between three different arbitration proceedings, under the ICSID rules, under the SCC rules or ad hoc proceedings under the UNCITRAL rules. Thus, Stockholm is one of the available venues under the ECT for investment disputes within the energy field.

The first award issued under the ECT was an SCC award (award 118/2001) in the arbitration *Nycomb Synergetics Technology Holding AB (Nycomb) v. the Republic of Lithuania*. Nycomb had acquired the shares of a Lithuanian company that had constructed a power plant. Nycomb complained that its Lithuanian subsidiary did not receive the correct increased tariff price for produced electricity from the national distribution company. The Lithuanian state was found to have failed in its protection of Nycomb (as indirect investor) and damages were awarded.

The choice of rules can have material effect as the investor must prove that its claim falls under the jurisdiction of the tribunal (as defined by applicable rules). Most BITs do provide quite broad descriptions of protected "investments". That is true also for the ECT. ICSID add certain requirements for the "investment" to qualify under the ICSID rules. In the ECT arbitration under the SCC rules in case *Petrobart Ltd v. Kyrgyz Republic* (SCC case no 126/2003), contractual rights pertaining to the sale of gas was considered a protected investment whereas such rights do not seem to meet the ICSID requirements.

Most BITs do provide for more or less the same protection for foreign investors:

- Most Favoured Nation treatment: The investor shall be treated no less favourable than investors from other nations.
- National treatment: The investor shall be treated no less favourable than investors from the host nation.
- Minimum Standard of treatment (on basis of customary international law) including: (i) Fair and Equitable treatment – The host nation shall not impair, through unreasonable or discriminatory measures, the operations or disposition of the investment by for instance changes in legal rules after the investment decision is made; and (ii) Full Protection and Security – The host nation shall take adequate measures to protect the investor and the investment from wrongful acts of state organs or others.
- Denial of Justice is prohibited as is Discrimination and Expropriation without prompt, adequate, effective compensation. The Investor shall be free to transfer funds and there are limits on the host nation's rights to require investors to adopt inefficient and trade-distorting practices.

Most SCC arbitrations are seated in Sweden although the venue can be anywhere.

The following are general features of Swedish arbitration which form the basis for arbitration proceedings: no special "terms of reference" are drawn up unless otherwise is agreed or provided by the applicable arbitration rules. The principle of "party autonomy" has a strong foothold, and arbitrators decide the case on the basis of the rules of law and the pleadings submitted by the parties. Hence, unless the arbitrators have been expressly given such mandate, the principle of ex aequo et bono or similar principles based on equitability will likely not be applied. The procedure is non-inquisitorial and a Swedish arbitrator is likely to use court precedents and arbitration rulings as an important source of law. Arbitrators cannot administer oaths in Sweden but the Swedish courts are available in support of arbitrations to hear witnesses under oath if required.

The SCC default rule provides for three arbitrators. The chairman is appointed by the SCC Institute. Notably, and unlike many other arbitration institutions, there is no official or binding list of arbitrators. Also, as there are no restrictions as to the nationality of arbitrators, arbitrators from many other jurisdictions appear frequently in Swedish arbitrations. If issues regarding the independence or impartiality of an arbitrator appear upon appointment of the tribunal or during the course of arbitration the arbitrator must disclose any such circumstances. Challenges are determined by the Board of the SCC Institute.

In respect of disputes concerning multiple claimants and/or respondents, the SCC Rules include rules on joint appointment of arbitrators and consolidation of proceedings.

The SCC rules provide for a 6 month time limit for rendering the award as the default rule which may be extended.

Arbitrators have no responsibility for the investigation being sufficient in scope and may not order a party to produce written documents on their own motion. Thus, it is for the parties to supply facts and evidence.

Sweden is party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

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Commercial Litigation in Sweden

BY OLOF RÅGMARK AND SVERKER BONDE | ADVOKATFIRMAN DELPHI

There are three kinds of courts in Sweden: general courts, general administrative courts (dealing with, inter alia, tax matters) and special courts, which determine disputes within special areas, for example, the Labor Court and the Market Court. General courts deal with both civil and criminal matters. They form a three-tiered system; district courts, courts of appeal and the Supreme Court. Review permit (certiorari) is required for all appeals. Whilst the Supreme Court normally grants leave only for the purpose of establishing a precedent to settle an open point of law, the appellate courts will also give leave to appeal for instance if there seem to be reasons to change the decision of the lower court.

The procedural rules governing the work of and disputes before the general courts are set forth in the Swedish Procedural Code *(Rättegångsbalken)* of 1942 and supplementary rules and provisions in a number of acts and decrees.

The numbers and complexity of commercial disputes are increasing in Sweden as elsewhere in Europe. Although the Swedish industry has long preferred arbitration before litigation as a dispute resolution mechanism, also the courts decide an increasing number of commercial disputes each year. Institutional mediations are not very common in Sweden, but mediation is an integral part of court proceedings, in large commercial disputes often by way of a court appointed mediator.

Swedish court proceedings are public and all information in the court files is open to the public. Exceptions can be made by the court for trade secrets and personal and other sensitive information. It is of essence for commercial parties to consider the need for confidentiality when submitting briefs and documents to a court, requesting confidentiality when appropriate.

The Court Procedure

The Swedish Procedural Code is said to have been derived from the Austrian Code of Civil Procedure (of 1895) but is clearly much influenced by Danish and English traditions. The Code provides for an adversarial (non-inquisitorial), oral trial procedural; the proclaimed leitmotifs are “orality”, “immediacy” and “concentration”. The first means that all material on which judgments are to be based must be presented orally, the second that such presentation must be made directly to the court and the third that the main hearing is to be arranged without interruptions.

As is the case with most cardinal principles, they are today partly fictions. In complex cases, preliminary written pleadings may become voluminous and delays between pre-trial meetings may be substantial; written documents and pleadings may be accepted as part of the main hearing by consent of the court as may witness statements. The needs of efficiency has gradually affected and transformed the procedural system and today resulted in a modern procedural order of high flexibility.

A civil action is commenced by the filing by the Claimant with the court of a summons application. The application must state (the Code Ch. 42 p. 2): (i) the (specified) relief requested by the Claimant; (ii) a thorough presentation of the circumstances upon which the action is based; (iii) the evidence offered by the Claimant and what facts each evidence allegedly demonstrate; and (iv) circumstances rendering the court competent (unless apparent). Written evidence shall be filed with the application, the application signed by the Claimant or his lawyer (Power of Attorney to be submitted in original) and a modest court fee paid (for civil cases the ordinary fee is presently 450 kronor, about €45).

Provided that the court deems the application satisfactory, the court issues and serves a summons upon the Respondent, enclosing a copy of the application with enclosures. The Respondent will file a Statement of Defense which should state (the Code Ch. 42 p. 7): (i) procedural objections (such as forum issues, including references to arbitration); (ii) admission or denial of the Claimant's request for relief; (iii) if the request is denied, a thorough presentation of the circumstances upon which the denial is based; and (iv) the evidence offered by the Respondent and what facts each evidence allegedly demonstrate. Written evidence shall be filed with the Statement of Defense and the statement signed by the Respondent or his lawyer (Power of Attorney to be submitted in original). Counterclaims are permissible and should be submitted as early as possible, preferably in connection with the Statement of Defense (the counter claim may be submitted as a set-off defense by the Statement of Defense or by way of a separate application for summons to be joined with the ongoing matter).

The handling of the further proceedings will depend on the complexity of the dispute and the nature of the evidence relied upon. In complex commercial disputes a number of briefs will be exchanged and one or more pre-trial meetings held with the court to prepare for a main hearing.

The Relief Sought

It is fundamental to Swedish judicial procedure that the relief sought by the Claimant – or by the Respondent – is specified. That requirement of *specification* is reflected by the provisions in the Code (Ch. 17 p. 3) that the court may not grant different or more extensive relief than what has been properly demanded by a party. Hence, the parties' prayers for relief have a preclusive effect. These requirements of Swedish law are quite different to those of many other jurisdictions, where the nature of remedies to be obtained is instead left to the discretion of the courts.

The relief may be amended as long as the additional claims are based on essentially the same grounds as the original claim. Thus, there is a critical relationship between the party's allegations – the grounds for the claims as submitted to the court – the prayer for relief and the judgment, which is setting the frames for the proceedings and the court's freedom to rule and which will affect also such issues as the *res judicata* effect of the judgment.

The reliefs normally sought from a Swedish court are performance, either by way of payment of a specified sum of money or of a specific action. Declaratory judgments may also be obtained (although within quite specific frames) as well as injunctions.

Interim Measures

At the interim stage the courts may order attachment (seizure) of property to secure a claim for performance (and, to a lesser extent, declaratory claims) and interim injunctive relief, used to secure a claim for an injunction. Before an attachment or injunction is ordered the applicant will normally have to meet the following conditions: (i) show probable grounds for his claim; (ii) show that time is of the essence and that the property or rights in question is in jeopardy of being removed, destroyed, etc.; and (iii) provide security for any damages caused by the attachment and/or injunction, should his claims ultimately fail. Temporary security measures may be granted *ex parte*. Should the application be made outside of an ongoing proceeding, the applicant must commence legal proceedings (as the case may be, by way of arbitration) within one month from the attachment or injunction order, failing which the order will fall.

There are no general rules permitting a court to grant security for costs as an interim measure. However, should the claimant be a company from outside the EU (or EEA), the respondent may request security for costs, although companies from some jurisdictions are excluded by force of bilateral treaties between Sweden and certain other jurisdictions.

Evidence

A Swedish court may freely evaluate all occurrences in the course of a proceeding; documents or matters submitted as evidence or proof by either party as well as the demeanor of witnesses or the actions of the parties, including their obedience to court orders, claims of privileges, etc. However, although the court may evaluate almost everything: (i) the party carrying the burden of evidence for a specific fact is obliged to identify and specify the evidence relied upon by him to meet that burden; and (ii) the court is expected to identify in its judgment each of the factors relevant for its final conclusion.

The parties are not free to submit new evidence at the appeal stage and the appellate courts do not try cases *de novo* in the true sense of that concept, as for instance witness hearings are presented by way of video recordings and no new questions may be put to witnesses or experts in the appellate court without reasonable cause and excuse.

With regard to witnesses, the general practice is that they are examined under oath by the counsels for the parties. The witness is expected to relate his entire story at once, without interruptions or prompting of the counsels or court, where after questions are put on parts of the story that the counsels or the court finds interesting and in need of further clarifications. Written witness statements are not common but may be accepted by the court if it so finds appropriate provided the consent of both parties. The tendency is that written witness statements are becoming more common, not least in complex matters where both counsels finds it rational to request statements in order to facilitate the preparations of a main hearing.

Experts may be appointed by the parties or by the court. The court's power to appoint experts to assist it on technical or factual matters which require special expertise is discretionary. Costs are borne by the parties jointly or by the party upon whose request the appointment is made. Written reports shall normally be submitted and the expert heard if any party so requests.

Disclosure

Sweden follows the civil rather than common law model of disclosure. Therefore, there is no general obligation to disclose and no "discovery" like in the UK or US. A party can request the court to order disclosure of documents in

the possession of its opponent or of a third party that are of evidential importance, provided they are reasonably identified. Certain documents, such as documents containing trade secrets, are exceptions to this rule. Courts will not permit disclosure or oral testimony on facts which are immaterial or if proof can be adduced by different means at lesser costs and inconvenience. Also "electronic" disclosure is allowed, although not very common.

Privilege is recognised in Swedish law. As disclosure is limited to documents that can be formally admitted into evidence, documents subject to lawyer/client privilege need not be disclosed. Correspondence with a lawyer is usually privileged, as the lawyers' professional confidentiality and that of certain other professionals is protected. Documents produced by in-house lawyers are not usually privileged, except arguably for documents produced while an in-house lawyer is acting for a party in court or in an arbitration.

Costs

Swedish lawyers bill on an hourly basis. Bar and procedural rules provide that fees must be reasonable. Contingency fees are not permitted. Court fees are usually insignificant. The overall cost of litigation depends upon the size and complexity of the dispute, and can obviously vary considerably. "Costs follow the event" so the losing party is generally liable to pay the winning party's costs. Where the parties win and lose on certain points the costs are commonly apportioned between them.

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Commercial Arbitration in Sweden

BY ULF HÅRDEMAN AND POLINA PERMYAKOVA | ADVOKATFIRMAN DELPHI

In comparison with many other countries, commercial disputes in Sweden are settled through arbitration to a relatively large extent. Historical traditions as well as the presence of a modern legislation on arbitration are a few of the many reasons for Sweden's strong position as a venue for international arbitration.

International arbitration in Sweden is conducted either as *ad hoc* arbitration or institutional arbitration under specific rules such as the Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce or the Rules of Arbitration of the International Chamber of Commerce (the "ICC"). Under an *ad hoc* arbitration, procedure is governed solely by the Swedish Arbitration Act of 1999 (the "SAA"). Subject to parties' agreement, other rules such as of the UNCITRAL may be applied as well.

As compared to *ad hoc* arbitration, institutional arbitration gives higher cost predictability and control, supervision in respect of the time-limits of the arbitration, independent control of conflicts of interests, and procedural rules which may be of great practical importance. Among the disadvantages which could be seen in institutional arbitration are the administrative fees to the institution, and also that the parties do not have direct influence on the appointment of the chairman unless otherwise agreed.

The first arbitration legislation was adopted in Sweden as early as 1887 and although Sweden is not a model

law country, the SAA generally follows the UNCITRAL model law and is regarded as a very modern and efficient legislation. Sweden has since long acceded the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and the Swedish court system provides for efficient procedures in connection with the enforcement of arbitration awards in Sweden.

Sweden is regarded as a civil law jurisdiction although Swedish court procedure in some respects shows similarities with the common law tradition. Amongst others, procedure is non-inquisitorial and a Swedish arbitrator is likely to consider court precedents and arbitration awards as an important source of law along with the applicable legislation.

In a Swedish arbitration no special "terms of reference" are usually drawn up unless otherwise agreed or provided by the applicable arbitration rules. The principle of "party autonomy" has a strong foothold, and arbitrators decide the case on the basis of the rules of law and the pleadings submitted by the parties. Hence, unless the arbitrators have been expressly given such mandate, the principle of *ex aequo et bono* or similar principles based on equitability will not likely be applied. Unlike the legislations of some other jurisdictions, the SAA does not give powers to the arbitrators to order witness statements under oath. Swedish courts however provide assistance in hearing witnesses under oath upon request of a party (provided that the arbitral tribunal grants such leave) and also support arbitration as regards granting of interim measures.

Role of the SCC Institute

The Arbitration Institute of the Stockholm Chamber of Commerce (the "SCC Institute") upholds a strong position as one of the leading centres for international arbitration. Traditionally, Sweden has been regarded as a neutral jurisdiction for east-western disputes and the SCC arbitration has become especially popular for disputes involving American, Russian, CIS and Chinese parties. The legal community in Stockholm includes arbitrators of which several are fluent in Russian, and the board of the Arbitration Institute includes American, Russian and Chinese nationals.

The SCC Institute was established already in 1917 as a separate entity within the Stockholm Chamber of Commerce. Amongst others, the arbitration rules of the SCC (the "SCC Rules") include provisions on consolidation, evidence, interim measures and separate award on advance on costs. The latest version of the SCC Rules, which entered into force in January 2010 also provides for the possibility of appointing a so called emergency arbitrator. The aim is to make it possible for parties to request interim measures before the dispute has been referred to an arbitration tribunal, thus bridging the gap between the rise of a dispute and the referral of a case to the tribunal. The SCC Institute also has rules for expedited arbitrations, special rules for insurance disputes and mediation.

The board of the SCC Institute acts also as appointing authority and takes *prima facie* decisions on the existence of a valid and applicable arbitration agreement, decides on advance on costs and extension of time limits for rendering the award. Unlike the International Court of Arbitration of the ICC, the SCC Institute functions solely as an administrative body and is not a court of arbitration. Thus, the procedure does not include any rules for scrutiny of awards by the SCC Institute, and once the matter has been referred to the arbitral tribunal, the SCC Institute has very little involvement in the proceedings. The SCC Rules do not contain any requirements on the terms of reference.

Although the SAA does not provide any time limits for the arbitration, it requires arbitrators to decide cases in a "practical and speedy" manner. In this respect, the SCC Rules provides for a six month time limit for rendering the award.

Arbitrability – Jurisdictional Issues

According to the SAA (Sec.1) any matter on which the parties may reach a settlement is considered arbitrable. A request for relief may include performance claims, declaratory relief as well as the establishment of facts, contract interpretation and gap-filling.

Appointment of Arbitrators

The SAA provides as the default rule that the tribunal shall be composed of three arbitrators, where each party appoints one arbitrator and the arbitrators so appointed appoint the chairman. In case of failing appointments, the Stockholm District Court acts as appointing authority. Quite frequently, however, arbitration agreements designate the SCC Institute or some other body as appointing authority.

As regards SCC arbitrations, the default rule also provides for 3 arbitrators, unless the SCC Institute, taking into account the complexity of the case, the amount in dispute and other circumstances, decides to appoint a sole arbitrator. Unlike in ad hoc arbitrations regulated by the SAA, the chairman in SCC arbitrations is appointed by the SCC Institute. Notably, and unlike many other arbitration institutions, there is no official or binding list of arbitrators. Also, there are no restrictions as to the nationality of arbitrators. Consequently, arbitrators from many other jurisdictions appear frequently in Swedish arbitrations.

Challenge of Arbitrators

If issues regarding the independence or impartiality of an arbitrator appear in connection with appointment of the arbitral tribunal or during the course of arbitration, the arbitrator has a duty to disclose any such circumstances. In this regard, the SAA lists a number of circumstances which always lead to bias. This list of circumstances is not exhaustive. Grounds for challenge include, among other things, contacts between the arbitrator or his law firm and one of the parties, or that the arbitrator has delivered an expert opinion in a parallel case involving one of the parties.

Challenge shall be made within 15 days from the disclosure or when the party otherwise became aware of circumstances giving rise to challenge. In ad hoc arbitrations the challenge is determined by the arbitral tribunal itself unless the parties agreed otherwise. In case of unsuccessful challenge the arbitral tribunal's decision can be appealed to the Stockholm District Court within 30 days. In SCC arbitrations challenges are determined by the Board of the SCC Institute, which decision is final and binding.

Multi-party and Consolidation

In respect of disputes concerning multiple claimants and/or respondents or where the dispute relates to several arbitration agreements the Swedish Arbitration Act does not contain any specific rules which shall be resolved on a contractual basis. The SCC Rules include rules on joint appointment of arbitrators and also provide for the possibility of consolidation of proceedings upon consultation with the parties and the arbitral tribunal. This rule applies in disputes relating to the same legal relationship between the same parties, i.e., in connection with closely connected or associated contracts.

Procedure and Evidence

Swedish arbitration proceedings are non-inquisitorial where the parties shall argue facts and provide evidence. Hence, the arbitrators have no responsibility for the investigation being sufficient in scope and may not order

a party to produce written documents on their own motion. Broad discovery procedures which are ordinary in common law countries are not applied in Sweden. Evidence, both oral and written, is usually summarised in a so called statement of evidence which is submitted in connection with the pleadings of the parties.

Confidentiality

Although arbitration proceedings are generally treated as confidential, the Swedish Supreme Court has ruled that there is no express or implied obligation of confidentiality of the parties under Swedish law. It is therefore advisable to expressly provide for a duty of confidentiality in the arbitration clause. As regards the SCC Institute, the SCC Rules (Art. 46) impose a confidentiality obligation on the SCC Institute itself and the arbitral tribunal but not on the parties.

Costs

Swedish lawyers bill on an hourly basis. Bar rules and the SAA provide that fees must be reasonable. Contingency fees are not permitted. The overall cost of arbitration depends upon the size and complexity of a dispute, and can vary considerably. Swedish law follows the principle "costs follow the event" which means that the losing party is generally liable to pay the winning party's costs as well as the costs of the tribunal and the fees to the institution, when applicable. Where both parties win and lose on certain points the costs are commonly apportioned between them.

Challenge of Awards

According to the SAA as well as the SCC Rules, the tribunal may correct obvious errors in the award and may also, within certain time limits, supplement the award on request of a party in case the tribunal due to an oversight has neglected to determine some issue. Beyond this scope, an award is final and binding and it cannot be appealed under Swedish law. Once rendered, an award may be challenged only on basis of certain procedural irregularities in which case the award can be declared invalid or be set aside in part or in its entirety.

An award is invalid if it rules on a matter which is non-arbitrable, if the award violates public policy or if it is not properly signed by arbitrators. A challenge action to set aside the award may be granted if the issue decided was not covered by a valid arbitration clause, if the award was rendered after the expiration of the time limit for the arbitration (as applicable) or if the arbitrators have otherwise exceeded their mandate. A challenge action can also be successful if the proceedings should not have been conducted in Sweden, if the procedure for appointing the arbitrators was not in accordance with the applicable provisions, if an arbitrator was unable to act due to legal incapacity or if he was not independent or impartial, or, finally, if an irregularity occurred during the course of the proceedings which probably influenced the outcome of the matter and where the party changing the award has not been at fault in this respect.

A challenge must be brought by a party within three months from the date of receipt of the award. Notably, a party challenging an award may not rely on a circumstance which it should have objected to during the proceedings.

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A Comparison of the New SCC "Emergency Rules" with Existing Emergency Procedures

BY JEREMY L. ZELL | ADVOKATFIRMAN VINGE KB

On 1 January 2010, the Arbitration Institute of the Stockholm Chamber of Commerce ("SCC") adopted the latest version of its arbitration rules ("SCC Rules"). The major change from the 2007 SCC Rules is the addition of a new Appendix II, which provides a procedure for appointing an "emergency arbitrator" ("Emergency Rules"). Under the Emergency Rules, parties in urgent need of an interim measure can have an emergency arbitrator appointed and can have the measure granted before the establishment of the arbitral tribunal; indeed, even prior to the submission of the Request for Arbitration.

In adopting the Emergency Rules, the SCC follows other major international arbitration institutions, such as the International Court of Arbitration at the International Chamber of Commerce ("ICC") and the American Arbitration Association ("AAA"). The concept of providing early emergency relief may not be new, but the SCC Emergency Rules are unique in some key respects; a fact demonstrated by comparing the SCC Emergency Rules to the ICC's Rules for a Pre-Arbitral Referee Procedure ("Pre-Arbitral Referee Rules") and Article 37 of the AAA's International Arbitration Rules ("AAA Emergency Rules").

The Emergency Application

The substance required in an application under Article 2 of the SCC Emergency Rules is comparable to the requirements in Article 3.2.2 of the ICC Pre-Arbitral Referee Rules and Article 37(2) of AAA Emergency Rules, but slightly different. All three emergency procedures require, in one form or another, that the party requesting emergency relief identify the opposing party; summarise the dispute; state the type of relief sought and reasons for the relief; and refer to the applicable arbitration agreement. The SCC Emergency Rules, however, require three additional pieces of information.

First, Article 2(i) of the SCC Emergency Rules requires that the requesting party provide the "names and addresses, telephone and facsimile numbers and e-mail addresses" of the parties and their counsel. Article 3.2.2(a) of the ICC procedure only requires the parties' names and addresses and, on its face, Article 37(2) of the AAA Emergency Rules does not even require that much. The SCC's additional requirements are probably related to the methods for notifying opposing parties under the different rules. Under the SCC Emergency Rules, the SCC is charged with notifying the opposing party, while under both the ICC Pre-Arbitral Referee Rules and the AAA Emergency Rules, the party requesting relief is supposed to notify the opposing party and then confirm that the notice was effective.

Second, Article 2(v) of the SCC Emergency Rules requires, among other things, that the requesting party provide comments on the seat of the arbitration and the law or laws applicable to the emergency proceedings. Neither the ICC nor the AAA emergency procedures require similar comments. The additional comments fit with the SCC's overall procedure, however, because Article 5 provides that the SCC Board will determine the seat of the emergency proceedings if the parties do not agree.

Third, and finally, Article 2(vi) of the SCC Emergency Rules requires that proof of payment of the total cost for the emergency proceedings be submitted with the emergency application. The ICC procedure and the AAA

procedure only require proof of payment of the filing fees, but the emergency arbitrators' fees are not required with the application. Another unique characteristic of the SCC Emergency Rules is responsible for this difference. Under Article 10(2) of the SCC Emergency Rules, the application fee and the emergency arbitrator's fee are fixed at €3,000 and €12,000, respectively, regardless of the nature of the emergency relief requested. These fees can be adjusted at the SCC's discretion. Under the emergency procedures of the ICC and AAA, the emergency arbitrators' fees are not set, but determined at a later stage.

Types of Emergency Measures

The emergency measures that an emergency arbitrator can grant under the SCC Emergency Rules are similar to those provided for under the AAA Emergency Rules, but broader than the powers granted under the ICC Pre-Arbitral Referee Rules. Article 1(2), by reference to Article 32(1)–(3) of the SCC Rules, grants the emergency arbitrator the authority to, "at the request of a party, grant any interim measure it deems appropriate" and order the requesting party to provide "appropriate security in connection with the measure". The emergency arbitrator may render his or her interim measure in the form of an order or an award. Similarly, Article 37(5) of the AAA Emergency Rules allows the emergency arbitrator to "order or award any interim or conservatory measure that the emergency arbitrator deems necessary".

Conversely, Article 2.1 of the ICC Pre-Arbitral Referee Rules is more specific in defining the pre-arbitral referee's powers. Such powers include, among other things, the ability to order certain measures that are "urgently necessary to prevent either immediate damage or irreparable loss"; order a party to make "any payment which ought to be made"; order a party to "take any step which ought to be taken according to the contract between the parties"; and order measures which are necessary for preserving or establishing evidence.

Even though the SCC Emergency Rules only generally define the scope of the emergency arbitrator's powers, the powers enumerated in the ICC procedure would almost certainly fall within a SCC emergency arbitrator's power to order measures it "deems appropriate". Therefore, parties can expect to receive the same types of emergency relief as they would expect under the ICC emergency procedure, and probably more.

Timelines

Most notably, the SCC Emergency Rules prescribe well-defined deadlines for the various steps of the emergency procedure and those deadlines are short. Under Article 4(1) of the SCC Emergency Rules, the SCC Board shall "seek" to appoint an emergency arbitrator within twenty-four hours of receipt of the application. Similarly, Article 37(3) of the AAA Emergency Rules requires that an emergency arbitrator be appointed "[w]ithin one business day" of the request. Article 3.4 of the ICC Pre-Arbitral Referee Procedure, on the other hand, permits the non-requesting party eight days to answer the emergency request and the ICC Court's Chairman can only appoint the referee "upon expiry of the time limit set out in Article 3.4," according to Article 4.2.

Of the three emergency procedures, the SCC Emergency Rules provide the shortest period in which the emergency arbitrator must render his or her decision. Article 8 of the SCC Emergency Rules dictates that the emergency arbitrator must make "any decision on interim measures … not later than 5 days" from the date on which the matter was referred to him or her and, under Article 6, the SCC will "promptly" refer the matter after the appointment. Keeping in mind that the SCC must seek to appoint the emergency arbitrator within twenty-four hours, the SCC Emergency Rules allow for approximately one week between the submission of the emergency

request and the rendering of the emergency decision. The SCC may extend the deadline based on the emergency arbitrator's "reasoned request" or otherwise.

Article 37(4) of the AAA Emergency Rules, however, does not set a deadline for rendering an award, but provides that the emergency arbitrator has the discretion to determine the emergency procedure's schedule, including the deadline for rendering the emergency decision. The ICC Pre-Arbitral Referee Rules do set a deadline for the rendering of the emergency decision, but that deadline is longer than the deadline under the SCC Emergency Rules. Under Article 6.2 of the ICC procedure, the referee must render his or her emergency decision within thirty days of receiving the file. The file is transmitted to the referee upon his or her appointment, but, as pointed out above, the referee is only appointed at the end of the eight-day window in which the non-requesting party must submit its answer. Therefore, it could take up to five weeks to receive an emergency measure under the ICC's emergency procedure.

Jurisdiction

Unlike Article 5.2 of the ICC Pre-Arbitral Referee Rules and Article 37(4) of the AAA Emergency Rules, the SCC Emergency Rules do not explicitly permit the emergency arbitrator to rule on his or her own jurisdiction. The SCC Emergency Rules only reference to jurisdiction comes in Article 4(2), which prohibits the SCC from appointing the emergency arbitrator if it "manifestly lacks" jurisdiction. Even if the emergency arbitrator has the implicit authority to determine jurisdiction, that authority is constrained by the five-day deadline for rendering an emergency decision.

Somewhat relatedly, Article 9(3) of the SCC's Emergency Rules provides, "By agreeing to arbitration under the Arbitration Rules, the parties undertake to comply with any emergency decision without delay".

Because the SCC performs only a *prima facie* examination of its jurisdiction; the emergency arbitrator's ability to consider jurisdiction is limited; and the effectiveness of an emergency decision is premised on the existence of a valid arbitration agreement, one party's objection to the SCC's jurisdiction could diminish the effectiveness of an emergency order or award rendered under the SCC Emergency Rules. A party with a colourable argument that it never agreed to arbitrate could theoretically refuse to abide by any emergency decision on the grounds that Article 9(3) is not applicable to it. Of course, this concern only arises in the infrequent event that a party alleges it never agreed to arbitrate.

Conclusion

As of 1 January 2010, parties that submit their disputes to the SCC have the opportunity to obtain interim measures through the appointment of an emergency arbitrator. The SCC Emergency Rules are similar to other existing emergency procedures, but different in certain ways. Most notably, any emergency decision must be rendered in a very short period. This will help parties in dire need of relief, but could pose problems by limiting the emergency arbitrator's ability to consider his or her jurisdiction.

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Fighting in Fog: a Rare Case of a Successful Challenge where an Arbitral Tribunal has Exceeded its Mandate

BY JAMES HOPE | ADVOKATFIRMAN VINGE KB

It is generally accepted that arbitral awards should be final and binding, and they should not be susceptible to challenge in court unless a serious procedural error has been committed. This principle is firmly enshrined in Swedish arbitration law, as it is in most modern arbitration laws around the world. An arbitral award cannot be challenged in Sweden on the substance; it can only be challenged for serious procedural errors as set out in sections 33 and 34 of the Swedish Arbitration Act of 1999.

Nevertheless, if parties are to retain confidence in arbitration as an alternative to court litigation, there need to be sufficient procedural safeguards so as to ensure that arbitration awards that are arrived at unfairly will be set aside (arbitrators are entitled to arrive at the "wrong" result on the substance: that is the price that is paid for a single-instance method of dispute resolution where the parties have excluded all rights of substantive appeal; however, they are not entitled adopt an unfair procedure in doing so). It is notable in this context that parties rarely take up the opportunity, where it exists, to exclude the right of challenge altogether: such waiver provisions exist in a number of jurisdictions, including Sweden (*See* Section 51 of the Swedish Arbitration Act), but they are not generally invoked, for the simple reason that parties wish to preserve the right to complain in cases of procedural unfairness.

In short, justice needs to be seen to be done. But what constitutes justice? Arbitrators have wide discretion to determine their own procedure, but at what point does their procedure cross a line and become unfair? In particular, at what point does the tribunal exceed its mandate?

Systembolaget ./. V&S Vin & Sprit AB, Svea Court of Appeal – 1 December 2009 (T4548-08)

This article concerns a recent case by the Svea Court of Appeal in Stockholm, which is a rare example of a court setting aside an arbitral award where the arbitral tribunal has exceeded its mandate.

By way of a brief summary, this case concerns a Swedish domestic arbitration between V&S, an importer and exporter of alcoholic drinks, and Systembolaget, the state-owned monopoly public retailer of alcohol in Sweden. The case between them arose out of various allegations of bribery by certain individuals, which resulted in Systembolaget terminating its agreement with V&S in certain respects. V&S accordingly commenced arbitration proceedings against Systembolaget, seeking damages for unlawful termination of the agreement.

Systembolaget claimed in the arbitration that it was entitled to terminate the agreement: (i) on the basis of 2002 contract terms between the parties; (ii) on the basis of 1995 contract terms; and/or (iii) on the basis of general contractual law principles permitting termination in the case of material breach of contract.

The tribunal found that none of the claimed contractual provisions were applicable as between the parties – in other words, that none of the particular purchasing terms between the parties had been breached. The remaining question was, therefore, whether Systembolaget had a right to terminate the agreement on the basis of general principles. The tribunal found that the parties had contracted out of these general principles. Accordingly, the tribunal concluded that the termination was unlawful and awarded damages to V&S of some 40 million Swedish crowns, plus costs.

Systembolaget then brought challenge proceedings in the Svea Court of Appeal in Stockholm, seeking to set aside the award on the grounds that the tribunal had exceeded its mandate pursuant to section 34(1)(2) of the Swedish Arbitration Act. In short, Systembolaget claimed that the tribunal had decided the arbitration on the basis of an argument that was never put forward by the parties. The tribunal found that the parties contracted out of general principles of law, but that argument was never made by V&S. (Systembolaget also put forward another ground for setting aside the award, but that ground was not considered by the Court.)

V&S disputed Systembolaget's claim. However, V&S could not claim that it had put forward this argument. The most V&S could say was that this argument could be inferred from the various other complex arguments that there were in the case.

Since the tribunal's determination was based on an argument that was not put forward by the parties, the Court found that the tribunal had exceeded its mandate. Swedish law requires that such an excess of mandate has affected the outcome of the case, and the Court could not rule out the possibility that it had indeed done so. The Court, therefore, upheld Systembolaget's claim and set aside the award in its entirety.

Analysis

It is rare for arbitral awards to be set aside in Sweden. One study of cases between 2002 and 2007 revealed 112 attempts to set aside awards, of which 33 were actually determined by the court and only 2 were actually successful (*See* Christin Brohmé, *The Swedish Challenge Procedure 2002-2007*).

However, this case serves as a reminder that cases can be set aside on procedural grounds in Sweden. Where (as in this case) the complaint concerns the tribunal exceeding its mandate, the court will consider the issue in detail, by reference to the specific arguments invoked by the parties in the case.

Notably, Systembolaget filed no less than three expert legal opinions in support of its claim to set aside the award, by three distinguished professors of law in Sweden – Professor Jan Ramberg, Professor Lars Heuman and Professor Bengt Lindell. These legal opinions are available to the public, since all documents filed with a Swedish court are, as a general rule, public documents. Each of the professors criticises the arbitral tribunal and argues that the award should be set aside.

Professor Jan Ramberg notes that the tribunal found that the 1995 contract terms, together with some further contract terms from 1999, "should be seen as an exclusive regulation between the parties regarding legal measures to be taken in cases of bribery and corruption" (unofficial translation of the original Swedish), but that there had not been any claim by V&S that these matters were "exclusively regulated" in that way or otherwise that general principles of law had been excluded by the parties.

Professor Lars Heuman notes that a basic principle of the right to be heard, as enshrined in section 24 of the Swedish Arbitration Act, is that the respondent must be given the right to defend himself: the respondent must be able to understand the claim that has been made by the claimant and must know what he is to defend himself against. Professor Heuman notes that the tribunal does not make any reference to V&S's position regarding this question of "exclusive regulation". V&S's arguments are set out in some detail in the arbitral award, but after quite careful analysis Professor Heuman concludes that Systembolaget could not have had reason to interpret V&S as arguing that general principles of law had been excluded.

Professor Bengt Lindell in turn refers to Professor Heuman's well-reputed textbook on arbitration in Sweden, in which Professor Heuman likens a situation where the respondent does not know the case that

he has to meet, to the parties being forced to "fight in fog" (Heuman, *Skiljemannarätt,* page 388). Professor Lindell adds that the arbitral tribunal's determination was based upon a factual circumstance that was never formally invoked, or even discussed, in the case.

Against these weighty authorities, it is somewhat curious that V&S did not file any expert legal opinions of its own. V&S pointed out before the Svea Court that it had accepted that there would be a contractual right of termination under the 1995 contract terms in the event of even a non-material breach of contract: thus, V&S argued, the question of the applicability of general principles of law (which would apply in the event of material breach) had in practice become academic. V&S sought to argue that the question of contracting out of general principles was, therefore, irrelevant. Furthermore, V&S sought to re-interpret the tribunal's determination, arguing that the tribunal did not in fact decide that there had been any agreement between the parties to contract out of general principles, but rather that general principles could not be relied upon. However, the Svea Court of Appeal did not accept V&S's interpretation.

It is perhaps of particular relevance in this case that the arbitral tribunal circulated a so-called "recital" (Sw. *recit*) before the hearing. Accordingly to common Swedish practice in domestic arbitration cases, the recital contains the draft text of the final award up until the arbitral tribunal's reasoning in the case, which the tribunal then adds after the hearing. The idea is that the parties are given the opportunity to review and comment upon the arbitral tribunal's description of the background facts and of the parties' respective claims and arguments in the case. As the Svea Court pointed out in its judgment, this practice promotes predictability and it usually helps to prevent potential challenge claims.

However, in this case, the arbitral tribunal's reasoning did not actually follow from the parties' arguments as set out in the earlier, "recital" part of the judgment. Rather than preventing a challenge claim, the recital in this case quite clearly revealed that the tribunal had gone beyond the parties' arguments and had thus exceeded its mandate.

Finally, as an aside, it is somewhat surprising that V&S does not appear to have asked for the case to be remitted to the arbitral tribunal for reconsideration. This possibility exists under section 35 of the Swedish Arbitration Act, but only if one or more parties specifically requests it. One can speculate that it might have been a simple matter for the arbitral tribunal to clarify its reasoning, particularly if (as claimed by V&S) the tribunal actually intended to find that the general principles in question could not be relied upon and that, as clearly argued by V&S in the arbitration, there was in fact no breach of contract that could give rise to a right of termination.

Excess of Mandate as Seen in a Wider International Context

It is rare for arbitral awards to be set aside for excess of mandate in this way, but it is not unknown in other jurisdictions and Systembolaget's arguments could well have found sympathy elsewhere.

In short, Systembolaget's complaint was that it was not given the opportunity to answer the point that general principles had been contracted out of, since that point was not made by V&S. When was such a contract entered into, what were its terms, and where is it evidenced? None of these issues were apparently ever put to Systembolaget.

Coincidentally, a similar situation arose in France last December. On 3 December 2009, the Paris Court of Appeal partially vacated an ICC arbitration award on the basis that the arbitration had been decided on the

basis of a legal principle – the Austrian legal principle of *Geschäftsgrundlage* – which had not been invoked by either of the parties and on which the parties had not been given a chance to comment. (The parties were Engel and Don Trade, but the author has not yet seen a report of the case.)

For a somewhat similar case in England, see *OAO Northern Shipping Co v. Remolcadores De Marin SL ("Remmar")* [2007] EWHC 1821, which concerned an arbitration in which the arbitrators decided the case on the basis of an issue that was neither argued nor discussed in submissions or evidence. Quoting *ABB AG v. Hochief Airport* [2006] 2 Lloyd's Rep 1, para. 70, Mrs Justice Gloster DBE found that: "... the tribunal must give the parties a fair opportunity to address its arguments on all the essential building blocks in the tribunal's conclusion". The judge found that there was a serious irregularity under section 68(2) of the English Arbitration Act, and she accordingly remitted the case to the arbitrators for further consideration.

Another similar case, but where a starkly different conclusion was reached, is the Finnish Supreme Court case of *Werfen Austria GmbH / Polar Electro Europe B.V.,* S2006/716, issued on 2 July 2008. In that case, which concerned a claim for indemnification under a distribution agreement, the arbitral tribunal decided the case on the basis of an adjustment to the contract pursuant to section 36 of the Finnish Contracts Act. However, section 36 was not invoked by either party, and it was applied by the arbitral tribunal *ex officio* without giving the parties the opportunity to comment, make submissions or adduce further evidence. Nevertheless, the Finnish Supreme Court decided, by a majority, that the award should not be set aside. Somewhat surprisingly in an international case, the Court applied the doctrine of *jura novit curia,* by which a court or tribunal is not bound by the legal reasoning invoked by the parties (in contrast to the factual arguments) (for criticism of this case, see *Stockholm International Arbitration Review* 2008, Number 3).

Of course, the danger with all such cases is that permitting these arguments to be raised at all risks jeopardising the finality of arbitral awards. For a case in which the Singapore Court of Appeal took a robust view in not setting aside an award for excess of mandate, see *Soh Beng Tee & Co Pte Ltd v. Fairmount Development Pte Ltd* [2007] SGCA 28. The Court in that case was keen to stress that "... the current judicial climate ... dictates that courts should not without good reason interfere with the arbitral process, whether domestic or international".

Conclusion

To use Professor Heuman's graphic image, "fighting in fog" is dangerous. Even speaking metaphorically, it should not be allowed in arbitration. Parties are entitled to know the case against them, and they should be given the opportunity to deal with it. Parties should be pleased to know that courts are prepared to intervene in such a situation, in order to correct injustice.

Nevertheless, fog is rare, both meteorologically and metaphorically. Such court intervention should be allowed in only the clearest and rarest of cases.

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FINLAND

Resolving Disputes by Arbitration in Finland

BY HEIDI MERIKALLA-TEIR | BORENIUS & KEMPPINEN LTD

Now that New Year's Resolutions have been made and 2010 is already in full swing, it is time to summarise the highlights of 2009 and look forward to the next 12 months. What were the recent developments in the arbitration market in Finland? What are the lessons learned? And what can be expected in 2010?

What Kind of Disputes were Settled by Arbitration Last Year?

It is fair to say that the global financial and economic crisis, or the recession, did not hit the dispute resolution and arbitration market in the same way as it hit many other sectors but it still had some impact on dispute settlement as well.

The number of arbitrations increased significantly during the last year. Even though many clients have expended a lot of time and resources on careful evaluation of a dispute, the chances of winning and the costs related thereto, before commencing arbitration, many eventually decided to proceed anyway. Indeed, regardless of the precarious financial situations of many companies and uncertainty in the market, companies did not hesitate to defend their rights after some initial considerations. In some cases, disputes were settled after the commencement of the arbitration but a significant amount of disputes were also finally settled first by the arbitral award.

According to the statistics of the Arbitration Institute of the Central Chamber of Commerce of Finland (the "Arbitration Institute"), the main arbitration institute in Finland, disputes relating to company acquisitions and supply agreements formed a major part of the disputes that have been settled by the rules of the said institute during 2009. Interestingly, the number of disputes relating to company acquisitions/sale of business increased significantly, from 12% in 2008 to 25% in 2009, with regard to all disputes governed by the rules of the Arbitration Institute. Supply/delivery agreements formed the second largest group of disputes at 12%.

Collection of receivables occupied third place in the statistic with 11%. We know many clients whose invoices have been left unpaid. Surprisingly enough, many of these matters could not be solved by negotiation but rather through litigation or arbitration, in a clear reflection of the unstable market.

What are the Lessons Learned?

As the statistics show, many companies looked at their agreements in more detail during the previous year and sought support for their interpretation of the agreement from attorneys. It appears that when concluding, for example, agreements relating to company acquisitions during the economic boom, the emphasis has not always

been given to clear and unambiguous wording of the agreements. This has resulted in disputes of interpretation that are now being settled in arbitration.

When business is growing and deals are made quickly, the wording of agreements is often of secondary importance to getting a deal that might be crucial for the future business. This is totally understandable but could these disputes be avoided or at least diminished to certain extent? The answer is yes, and it is not necessarily easier said than done.

Would not it be easier to draft agreements if you knew which parts of the agreements are legally more important than the others? Again, yes.

Hopefully the following tips turn out to be useful to those involved with agreements governed by Finnish law. Indeed, by keeping the following main principles in mind, it might be possible to save a coin or too and at least increase the chances of winning a potential dispute.

Under Finnish law, a court as well as an arbitral tribunal should first attempt to interpret an agreement according to its literal wording. If a reasonable interpretation can be concluded from a literal reading of an agreement, such interpretation would normally be adopted. Consequently, great effort should be put on a clear and unambiguous wording of the main articles of the agreement. Sounds self-evident, but based on experience with recent disputes, the focus of the agreements has not always been put in the right place.

If certain articles remain unclear on the basis of the literal reading of the agreement, the court or the arbitral tribunal should then evaluate the preamble and the recitals of an agreement in order to get a better understanding of the objectives of the agreement. The recitals and preamble provide important background information regarding the agreement. Therefore, it is useful to state clearly why and for what purpose the agreement has been initially drafted.

Finally, if further clarification is required in order to interpret an agreement, the court and the arbitral tribunal should look at the intent of the parties to the agreement. If this is not evident on the basis of the recitals and the preamble, it can be evidenced, for example, by the negotiations between the parties, drafts of the agreements, etc. Thus, it is also useful to document to the extent possible the negotiations and discussions between the parties prior to concluding the final agreement.

The main principles seem simple, but they are often forgotten when the deals are put on paper.

What can be Expected from 2010?

The beginning of this year looks busy. Arbitrations commenced during 2009 will at the latest reach the oral hearing stage now. However, there are also new cases in the pipeline and 2010 should follow the previous year in many respects.

As in 2009, it can be expected that clients are rather cost-conscious. Not only do clients require regular cost control from counsels but they also tend to prefer sole arbitrator arbitrations, which is one factor among others affecting the costs of the arbitrations. In fact, according to the statistics of the Arbitration Institute, in 79% of the cases the dispute was settled by a sole arbitrator during 2009.

It should be kept in mind that even if the parties have initially agreed about a dispute settlement by three arbitrators, they can later agree that the dispute shall be settled by a sole arbitrator. Indeed, at least in cases where the interest of the dispute is not significant, it can be advisable to agree on a sole arbitrator. This not only affects the costs of the arbitration but can also speed up the proceedings.

The arbitration proceeding should be considered in its entirety and be structured in a way that best serves the clients' interests. Indeed, flexibility is one of the good features of arbitrations and explains its popularity, which is expected to increase in 2010.

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Costs of Litigation in Finland

BY ANTTI KARANKO | BORENIUS & KEMPPINEN LTD

This article deals with cost issues relating to litigation in Finland. Although civil legal proceedings in a Finnish court may not be particularly expensive from, e.g., an American or British point of view, legal costs are, nonetheless, an issue worth weighing carefully – especially if the financial interest of the case is not considerable.

Generally, the legal costs of a party in a typical Finnish civil court case add up to tens of thousands of euros. Particularly complex cases as well as those which require specific legal knowledge often boost legal costs considerably, especially when the parties retain the services of large corporate law firms, as most often is the case. Naturally, if the case is argued further in a Court of Appeals or the Supreme Court, the parties' legal costs run even higher.

There are several (as a rule, universal) approaches to minimising the legal costs of a corporation but they are not specifically addressed here as they give reason for an altogether separate article. Instead, the general principles relating to the adjudication of the parties' legal costs in Finnish litigation are explained in the following. The article also includes certain practical recommendations for the corporate client to bear in mind both when planning litigation and during the course of the legal proceedings.

Division of Parties' Legal Costs – General Principles

In Finland, the party who loses an "ordinary" civil case (i.e., a case which can be freely settled by the parties) is liable for all reasonable legal costs incurred by the necessary measures of the opposing party. There are some exceptions to this so-called "loser pays rule", however.

If several claims have been made in the same case and some of them are decided in favour of one party and some in favour of the other party, the parties shall, as a rule, be liable for their own costs. If the claim that a party loses has only little significance in the case, such party is, however, entitled to full compensation of his legal costs.

The same principle, i.e., that the parties are liable for their own legal costs, is also applied when the claim of a party is only partially upheld. In such an event, however, full compensation of the legal costs of that party may be ordered if the part of the claim that has not been upheld concerns solely a *matter of discretion* which has little bearing on the amount of the parties' legal costs.

It follows from the aforementioned basic rules on legal costs that it is highly recommended, where possible,

to try to avoid presenting either subsidiary claims or claims which are clearly exaggerated. In any event, when presenting subsidiary claims or considerably large claims (with difficulties in producing conclusive evidence supporting such claims), it is worth bearing in mind that, in connection with a partial victory, the opposite side may be awarded with some of his legal costs.

Attorneys have often disregarded the risks that are involved in presenting several subsidiary claims and/or notably large claims. If an attorney should not raise this issue with the client in the planning stages of the legal proceedings, it is recommendable to specifically discuss the question of the cost risk relating to the proportioning of the claim with the attorney.

Legal Costs and Settlements

In cases which end up in a settlement, the parties also normally agree upon the issue of the parties' legal costs. It is, indeed, highly recommendable to address this issue of costs as well when settling a case. Otherwise the Court has a wide discretion with regard to the division of the parties' legal costs.

In practice, the court normally resolves the issue of unsettled legal costs in a case of settlement by comparing the content of the settlement with the original claims of the parties and decides upon the division of the costs on the basis of the assumption that the claims of the party receiving something in connection with the settlement would have been accepted by the court during the normal course of the proceedings.

To leave the issue of costs outside the settlement creates unnecessary uncertainty – unless the settlement is such that the opposing party agrees to pay the great majority of the original claim. In such a case, it may be tactically wise for the claimant to attempt to settle the case without agreeing upon the costs and leaving the question for the Court to decide.

Compensable Costs

Compensable legal costs must relate to the measures taken in connection with the preparation of the trial and the participation in the proceedings, as well as the fees of the attorney or counsel. In addition, compensation can be paid for the work caused by the trial to the party itself and for the losses directly linked to the trial.

If a party disputes the amount of the claim for legal costs of the opposing party, the Court will then consider the reasonability of the costs. Such consideration takes into account, *inter alia,* the difficulty and the scale of the case, the amount and quality of the work performed and the financial interest and general significance of the case.

The Parties' Own Efforts, Costs and Losses Attributable to the Trial

For some reason (often perhaps the downright ignorance of attorneys), the parties to civil proceedings in Finnish courts quite rarely claim compensation for the parties' own efforts, costs and losses that are attributable to the trial. As a rule, however, a typical civil case, e.g., an action for damages due to breach of contract, requires considerable efforts from the members of the top and mid-level management as well as the legal department and the finance department of the corporations. Compensation for such efforts and loss of time can be claimed from the opposing side.

It is recommend to carefully – and in close detail – document all the internal efforts which have been laid down by the management and the personnel of the corporation which is involved in a civil case as well as the time consumed by such efforts. Together with the financial department of the corporation and/or the corporate accountant, the attorneys handling the case may then calculate a justifiable claim which covers also the amounts

that have been lost by the client in connection with the trial. The more detailed the measures taken and the better founded the argumentation behind the claim are the more likely it is that a claim for compensation of the work and the losses caused by or linked to the trial are awarded by the Court.

It is important to notice that the parties cannot claim any compensation for the distress or the discomfort caused by the trial. Neither can the parties claim – at least not in the form of legal costs – compensation for the loss of profit caused by the trial. Loss of profit can be claimed, however, as an altogether separate claim for damages. The success of such a claim depends greatly on the claimant's ability to produce convincing evidence supporting his assertion that the amount of time and attention consumed by the trial could have been vested in profitable business which, in light of verified past performance of the corporation, would likely have yielded the amount which is claimed from the opposing party in the form of compensation for loss of profit.

Legal Unclearness and Legal Costs

If the legal issues in the case have been so unclear that the losing party can be deemed to have had a justifiable reason to pursue the proceedings, the court may order that the parties are liable for their own costs either in full or in part. This is important to bear in mind when suing a party in a case which is or may become open to various legal interpretations. In such cases, e.g., when there exists diverse legal praxis (or no legal praxis at all) regarding the key legal issues of the case, it is equally important – but regrettably much too often forgotten – also by the respondent to explicitly invoke the legal unclearness of the case.

Adjustment of Unreasonable Costs

If, in view of the circumstances giving rise to the proceedings, the situation of the parties or the significance of the issue, and taking all aspects of the case into account, it would be manifestly unreasonable to render one party liable for the legal costs of the other, the court may on its own motion reduce the payment liability of the party.

In disputes between corporations, adjustment of cost liability is very exceptional. However, when a dispute is between a corporation and a private individual, e.g., a former employee or manager of the company, there is a very real possibility that, even in case of victory, the full legal costs of the corporation may not be awarded.

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Alternative Dispute Resolution in Finland

BY MARKUS KOKKO | BORENIUS & KEMPPINEN LTD

Alternative dispute resolution ("ADR") is a fairly new phenomenon in Finland. We have a strong tradition to solve business disputes in ordinary courts and in arbitration proceedings. There have been, of course, settlements based on negotiations between disputing parties, but we have gained experience on ADR only during the last 10 to 15 years.

The Settlement Procedure of the Finnish Bar Association

Among other things, the Finnish Bar Association provides services that conciliate disputes arising in connection with business life. Settlement procedures can be used only in a dispute in which a settlement is permitted, not, for example, in a dispute that relates to a protected third party interest, such as matters concerning fatherhood or the custody of a child. In practise, the settlement is permitted in all business disputes and, thus, the settlement procedure of the Finnish Bar Association can be used.

The settlement procedure is always based on the voluntariness of the parties and the will to handle the dispute in the settlement procedure. There might be an agreement between the parties that the dispute should be handled in the settlement procedure. It is also possible to make a specific agreement regarding the dispute already arisen.

The parties of the settlement procedure undertake to follow the rules of the settlement procedure of the Finnish Bar Association. In the settlement procedure, the guides concerning the professional ethics of the bar are also complied with to the extent appropriate. The progress of the settlement procedure is not regulated in detail in the rules, which means that the process can be arranged flexibly to each dispute, in such manner as the circumstances and the parties' agreement require. The settlement procedure formally begins with a written notice, compiled by the parties or one of the parties, to a conciliation board. In the real world, the settlement procedure begins so that the mediator meets both of the parties in a joint session, and after that he or she can separately discuss with the parties. Several joint or separate sessions can be arranged if that is considered necessary.

The settlement procedure is led by an impartial and independent mediator who is an attorney of the Finnish Bar Association, who has the training to mediate and who is on the list of mediators of the Finnish Bar Association. The parties can agree upon the mediator and it is also possible, by the joint request of the parties, that the Finnish Bar Association's Settlement procedure board suggests a certain attorney to act as a mediator. If not otherwise agreed, the parties are responsible for the fee of the mediator and other related costs half-and-half. Both of the parties are in a commission relationship with the mediating attorney.

The task of the mediator is to help the parties to find reconciliation to the dispute. Thus, the settlement procedure concerns negotiations that aim for a settlement, aided by a third party. In the settlement procedure the subject can be handled in joint sessions and in private sessions. When the mediator receives certain confidential information in these private sessions, he or she is obliged not to reveal it to the other party. It is not mediator's task to give legal advice to the parties, the parties shall use their own advocates in the process for that purpose. The mediator is not a judge nor can he or she give orders or judgements. However, the mediator can still, with the parties' consent, make an appraisal about the probable decision of the dispute and make a proposal for the settlement to the parties. The mediator can, with the parties' consent, obtain necessary information or hear experts or other persons as well.

The settlement procedure does not end in a judgement, but, when an amicable settlement is reached, in a conciliation agreement. The content of the conciliation agreement is for the parties to decide, and furthermore the conciliation agreement does not necessarily have to be based on law. Participation in the settlement procedure is voluntary and a party can interrupt the procedure at any time without any consequences. Still, the parties do have an obligation to contribute appropriately to the reconciliation process, together with the mediator.

If the settlement procedure ends without a settlement, the dispute will be handled, or the handling will be

continued, in the ordinary court or in an arbitration proceeding. If the dispute is already on the table in an ordinary court or in an arbitration proceeding, the parties can, if necessary, request a postponement to the process due to the settlement procedure. The settlement procedure does not, however, shut out the possibility of a party taking the question under dispute to an ordinary court or to an arbitration proceeding, unless it has been agreed so. Thus, it is possible to have the same question, simultaneously, under settlement procedure, litigation and arbitration proceeding.

The settlement procedure is confidential. The mediator or the parties to the procedure are obliged to keep the settlement procedure confidential. The parties are prohibited from appealing against the proposal, admitting or opinion of a mediator outside the settlement procedure, for example, in a potential litigation or arbitration process.

A solution serving the parties practical interests is quicker and far cheaper to reach in the settlement procedure than in litigation or arbitration proceedings. In Finland the settlement procedure has been used especially in disputes concerning construction and major information technology deliveries where the completion of an unfinished project could be endangered if the business relationship between the parties would be terminated in the middle of the delivery.

The Court-annexed Mediation

The act that concerns mediation in courts came into force in 2007. The mediators in court-annexed mediation are court judges who have had training to act as a mediator. The parties have no possibility to choose or to affect the mediator in court-annexed mediation. The mediation normally takes place in one of the parties' forum domiciles. The court-annexed mediation is inexpensive since the judge will not receive any independent compensation for the mediation. The parties are responsible for their own expenses and for the fees of their advocates.

The court-annexed mediation and the settlement procedure of the Finnish Bar Association are very much alike when it comes to the procedure. The most significant difference is that the court-annexed mediation is usually public. Thus, the potential audience can, by default, be present in the mediation, unless a party to the mediation requests that a part of the mediation will be carried out without the public. The negotiations between the judge and a party to the mediation are nevertheless always prohibited for the public. Since the court-annexed mediation is not completely confidential when it comes to publicity, it is not suitable for, at least not for all, disputes arising in the business world.

The advantage of the court-annexed mediation is that the mediation agreement can be affirmed in the District Court, when the mediation agreement can, as such, be executed by an execution officer, if the adverse party does not comply with the terms of the mediation agreement. Thus, any separate trial due to the breach of mediation agreement is not required.

The mediation ends, if either one of the parties notifies a lack of will to continue the mediation. Also, the judge can end the mediation if he or she, for example, discovers that there is in fact no prerequisite for mediation. After the mediation has failed, the parties are able to take the dispute to a litigation process. If the litigation has been already pending, it will be continued. In post-mediation litigation, the dispute will be handled by a different judge or different judges than in the court-annexed mediation. In the latter litigation, the party has no right to appeal to such matters that the adverse party has brought out in the mediation.

In Conclusion

In Finland, there have been some great expectations towards ADR and the discussion about ADR as a way to resolve disputes has received public attention and the issue is widely discussed between attorneys. Despite all this, ADR has not become too generally used as a dispute resolution tool in the business world. The overwhelming majority of business disputes are still resolved in ordinary courts and in arbitration.

There is only little experience from court-annexed mediation, because the process is fairly new. It is possible to say, however, that when it comes to solving business life disputes, the settlement procedure of the Finnish Bar Association is more recommended, because the confidentiality of the proceeding and the possibility of having an attorney as a mediator who has wide experience about the type of dispute at hand and the business practices in the field that the parties represent.

The success of mediation depends strongly on the parties having a genuine will to reach a settlement. The professional skills of the mediator are another significant factor. Also important is how well the mediator knows the business field of the parties beforehand, and the problems and solutions relevant thereto, and whether the parties feel confident about the mediators' skills and character.

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Jurisdiction in Maritime Disputes

BY ULLA VON WEISSENBERG AND JOHANNA HOLLSTEN | BORENIUS & KEMPPINEN LTD

Sea carriage is dominant in the international transit of goods. Finland's foreign trade is highly dependant on sea carriage, as over 80% of Finland's export and over 70% of the country's import is carried by this mode of transport. The cargo is subject to many risks during transport and, unfortunately, damage to the cargo occurs from time to time.

It is not uncommon that disputes arise when the parties take different views on the carrier's liability for the occurred damage under the contract of carriage. It is then, for many reasons, important to know in what court such disputes can be resolved. If a party wishes to initiate legal proceedings, he will have to identify the court that is competent to deal with his case or, in other words, has jurisdiction. If the claim is presented to the wrong court or if there is a dispute over the question of jurisdiction, the claimant runs the risk of a considerable delay in the proceedings or even of a dismissal of his case because of a lack of jurisdiction.

Given the international character of sea carriage, many different parties from various countries can in some way be involved in the transport, and the goods in transit may pass through several countries. As is the case with other areas of law with a significant international dimension, the issues regarding jurisdiction in maritime disputes are regulated not only in national legislation, but also on an international level through international conventions to which countries are party. In addition, the European Union (EU) imposes its own legislation on

jurisdiction which must be taken into account. Navigating the maze of complicated, partly overlapping regulations and legislation on court jurisdiction, which on some points even may be open to various interpretations, may be a difficult task.

Regulation on Jurisdiction

The Finnish Maritime Code ("FMC") contains provisions on jurisdiction in civil matters concerning carriage of goods by sea. It may be pointed out that the Maritime Codes in the Nordic countries (Finland, Sweden, Norway and Denmark) are almost identical in wording and, therefore, contain uniform provisions on jurisdiction.

Claims in matters covered by the FMC shall be brought before a competent Maritime Court, i.e., one of the district courts, nominated to try maritime disputes.

In a conflict situation between jurisdictional provisions contained in the FMC and international regulations on jurisdiction by which Finland is bound, the latter will prevail. In practice, therefore, the jurisdictional provisions in the FMC as a general rule only become applicable to disputes when both the defendant and the plaintiff are domiciled in Finland or the defendant is domiciled in a country which is not a member of the EU or party to the international conventions regulating jurisdiction.

Of great importance is the so called Brussels I regulation (the Council Regulation (EC) No 44/2001 of December 2000). The regulation lays down rules governing the jurisdiction of courts and the recognition and enforcement of judgments in civil and commercial matters in the Member States of the European Union (EU). It supersedes the Brussels Convention of 1968, which was applicable between the Member States before the regulation entered into force. However, the Brussels convention continues to apply with respect to those territories of Member States that fall within its territorial scope and that are excluded from the regulation. The Brussels I regulation contains some improvements compared to the older convention.

In addition, the Lugano Convention (the Convention on jurisdiction and the enforcement of judgments in civil and commercial matters) from 1988 also contains jurisdictional provisions. The Lugano Convention was recently revised and a new Lugano Convention (now the so called the Lugano II Convention) was ratified by the European Community in 2009. From the point of view of content the new Lugano convention corresponds to the Brussels I regulation. Since the European Community is party to the Lugano II convention, it becomes applicable also in Finland. The convention will, when ratified, apply between the EU Member States and the EFTA (European Free Trade Association) countries (Switzerland, Norway and Iceland).

Furthermore, it may be pointed out that the Arrest Convention (the International Convention for the Unification of Certain Rules relating to the Arrest of Sea-Going Ships) from 1952 entered into force in Finland in 1996. The convention contains provisions on which court shall have jurisdiction to determine a case concerning arrest of a ship upon its merits. The Arrest Convention is a special convention and, thus, as is the case with all special conventions, takes priority over the Brussels I regulation, the Brussels Convention and the Lugano Conventions, which are of more general nature.

Jurisdiction Clauses in the Contract of Carriage

Maritime contracts, i.e., bills of lading and other transport documents used in liner traffic often contain jurisdiction clauses determining the court where legal actions may be instituted. A jurisdiction clause is a provision in a contract that refers disputes arising under the contract to a country, territory or place for hearing and for adjudication.

Jurisdiction clauses should be distinguished from choice of law clauses, as the law of the contract may differ from the country within which disputes are heard.

It is possible to agree that disputes shall be tried by a certain court which would not normally have competence to hear the case. If a jurisdiction clause has been incorporated in a contract, the parties' freedom of choice of the court of jurisdiction is, therefore, limited when a dispute arises. However, this creates foreseeability and firmness in the legal relationship between the parties.

It is possible to agree that in the case of a dispute the parties can choose between many alternative courts. The choice can be tied to certain set conditions. On the other hand a very complicated jurisdiction clause may create uncertainty regarding the determination of the court of jurisdiction.

The freedom of contract regarding the court of jurisdiction is, however, not unlimited. When mandatorily applicable to the contract, the FMC restricts the use of jurisdiction clauses and stipulates that a contract concluded before a dispute has arisen is null and void to the extent it limits the plaintiff's right to have a dispute concerning the carriage of cargo tried before certain courts mentioned in the FMC.

After a dispute has arisen the parties are, however, free to agree on how the dispute shall be dealt with. The jurisdiction agreement must be made in writing.

Jurisdiction clauses are generally recognised by Finnish courts, provided they are binding on the parties, unambiguous, reasonable and not contrary to *ordre public*.

Dispute Resolution through Arbitration

It is common that maritime disputes are resolved through arbitration instead of through litigation in a court. Under Finnish law arbitration agreements must be in writing.

Arbitration clauses are commonly used in charter parties. Although arbitration clauses are not normally included in bills of lading or other documents used for carriage of goods by sea, bills of lading often contain references to charter parties containing arbitration clauses. According to the FMC, arbitration clauses are binding upon the holder of the bill of lading where a bill of lading has been issued pursuant to a charter party containing provisions on arbitration, provided that the bill of lading contains a special annotation that these provisions shall be binding upon the holder of the bill of lading.

Arbitration may offer advantages over court litigation, for instance the process may be faster, private, and the parties can select arbitrators who are experts in the topic in dispute. However, arbitrational proceedings are generally also considerably more expensive than regular court proceedings in Finland and are not subject to appeal.

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POLAND

The Granting of a Temporary Injunction in the Course of Proceeding before a Polish State Court or a Court of Arbitration

BY BARBARA JELONEK–JARCO | KUBAS KOS GAERTNER

The granting of a temporary injunction is an important method for the protection of the rights of an entity willing to pursue its claims before a court. Proceedings concerning the granting of a temporary injunction are a procedural form of interim legal protection and its function in the examination proceedings is ancillary. The purpose of these proceedings is to ensure the efficiency of the verdict issued in the proceedings in which the claimant is pursuing his claim. The possibility of obtaining temporary legal protection prior to the issuance of a legally valid judgment in a case examined by the court is of fundamental importance for the claimant's interests, for whom the injunction means the certainty of satisfaction with the debtor's estate should the judgment accept his claim for a performance. However, it should be underlined that ensuring the enforceability of a judgment by means of enforcement does not exhaust the goals of the proceedings concerning the granting of a temporary injunction. The legal interest in obtaining the injunction may also consist in the situation in which the lack of injunction renders the achievement of the goal of proceedings in the case impossible or severely obstructed – which refers to actions concerning claims other than claims for performance (e.g., establishment of a legal relationship or a right).

The premises and manner for granting the temporary injunction are regulated in the Act of 17 November 1964 – Code of Civil Procedure (the "CCP"). As a principle, an injunction is granted by the state court. However, after the amendment of the CCP that came into force on 17 October 2005, also the claim pursued before an arbitral tribunal may be granted an injunction by a state court or an arbitral tribunal.

In the Polish law, in every civil case that is subject to examination by a state court or an arbitral tribunal the granting of an injunction by a state court may be demanded, whereby the court may grant the injunction prior to the instigation of proceedings or already in the course thereof (Article 730 of the CCP). It follows from the formulation "in every civil case" used in Article 730 of the CCP that the injunction may be order in any litigation and in any non-litigious proceedings. In general, the granting of injunction is subject to a relevant motion which may be submitted prior to instigation of proceedings, simultaneously with the statement of claims (or motion) or in the course of proceedings. Each motion for granting of an injunction should contain the indication of the manner in which the injunction should be granted while in the cases concerning pecuniary claims, the sum of the injunction and substantiation of circumstances grounding the motion should also be indicated. The last requirement as to the content of the motion for granting of injunction results from the premises which are mandatory for the acceptance of the motion. Namely, any party of the proceedings may demand the granting of injunction provided that such party indicates probability of (i) the claim and (ii) the legal interest in being granted the injunction (Article 730.1 of the Civil Code).

The legal interest in being granted the injunction exists in a situation in which the lack of an injunction will render impossible or severely obstruct the enforcement of a judgment issued in the case or will in any other manner render impossible or severely obstruct achievement of the goal of proceedings in the case. Cases in which the demanded legal protection consists in the shaping of a right or a legal relationship usually refer to the elimination of situations in which the legal protection given by the court's judgment comes too late, as a result of which its effects are futile. The purpose of the injunction, therefore, is to ensure the effectiveness of the future judgment.

The competence to grant injunction is held by the court which is competent to examine the case in the first instance.

In principle, the motion for granting of an injunction should be examined at a closed session without the parties' attendance. The decision of the court of first instance issued in the scope of granting of an injunction may be challenged by means of a complaint.

Upon the selection of the manner of the injunction, the court should recognise the parties' or participants' interest so that the entitled party is provided with the due legal protection, yet without excessively burdening the obliged party. If the injunction is granted prior to the instigation of proceedings in the case, the court should also set the time period in which the letter instigating the proceedings should be lodged under pain of the cancellation of the injunction.

The legislator differentiates between the injunction of (i) pecuniary claims and (ii) claims other than pecuniary.

The CCP (Article 747) contains an enclosed list of manners in which the injunction of a pecuniary claim may be granted. The most important are:

- the seizure of chattel, seizure of salary, claim from a bank account or other claim or a financial asset;
- the encumbrance of a property of the obliged party with a compulsory mortgage;
- the establishment of the prohibition to sell or encumber the property for which the land and mortgage register is not kept or for which the land and mortgage register is lost or damaged;
- the encumbrance of a ship or a ship under construction with a marine mortgage.

In turn, if the subject of the injunction is not a pecuniary claim, the court shall grant the injunction in the manner it finds fit, not excluding the manners stipulated for securing the pecuniary claims. In particular, the court may regulate the rights and obligations of the parties or other participants of the proceedings for the duration of proceedings.

In the case of a legally valid return or rejection of the statement of claims or a motion, the dismissal of the statement of claim or a motion or discontinuation of the proceedings, the injunction automatically collapses. In the case of the acceptance of the statement of claims the injunction collapses after one month from the judgment is in force.

The injunction collapses also if it was granted prior to instigation of proceedings and the obliged party failed to advance the entirety or a part of the claims or, alternatively, the advanced claims are different from those secured by means of an injunction.

When a state court decides on the injunction of a claim pursued before an arbitral tribunal, the proceedings are to be held under the rules of CCP. The court competent for the examination of the motion for granting of the injunction is the court which would examine the case in first instance, if the parties have not signed the arbitration

covenant, whereby granting of the injunction is dependent upon the substantiation of the claim an legal interest in granting thereof. In the case of securing pecuniary claims, the court is limited by the list of methods of injunction contained in Article 747 of the CCP. The court may issue a decision on the application of a temporary means of securing a claim only at a party's motion which may be lodged at any stage of proceedings before a court of arbitration.

The proceedings on granting of an injunction before an arbitral tribunal differs significantly from the proceedings held before a state court. An arbitral tribunal may issue, at the motion of the party which indicates probability of the claim pursued, a decision on the application of a method of securing the claims in a manner it finds fit with regard to the subject of the dispute. The manner of the injunction granted by the arbitral tribunal is thus not limited to the list of methods for securing pecuniary claims from the CCP. Also, the indication of probability of the legal interest in being granted the injunction is not required. It is a considerable facilitation for the parties, since the state courts which require the applicant to do so, usually dismiss the motions for the injunction for this particular reason.

The decision of an arbitral tribunal on the injunction is subject to enforcement only after an enforcement clause is appended thereto by a state court. The decision on the granting of an enforcement clause may be challenged by means of a complaint. The state court may refuse to append the enforcement clause to a decision on granting of an injunction issued by a domestic arbitral tribunal for the same reason which may constitute a basis for the refusal to recognise or ascertain the enforceability of a verdict of an arbitral tribunal or an agreement concluded before such court.

Although the obtaining of injunction is advantageous for the applicant, it also entails considerable risk. Namely, if the entitled party who obtained the decision on the injunction further failed to submit a letter instigating the proceedings within a given period of time or withdrew the statement of claims or the motion or if the statement of claims was returned or rejected or the action or the motion was dismissed or the proceedings were discontinued, the other party is authorised to institute an action for compensation of damage caused by enforcement of the injunction against such a party.

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Capability of Settlement by Arbitration

BY MIROSLAW CEJMER | KUBAS KOS GAERTNER

By virtue of the Act dated 28 July 2005 (Code of Civil Procedure, Journal of Laws no. 178, item 1478) a new Part Five (Articles 1154 – 1217) containing extensive regulations on arbitration jurisdiction was introduced to the Code of Civil Procedure ("CCP"). This regulation is based vastly on the UNCITRAL Model Law on International Arbitration of 21 June 1985. However, as regards one of the major elements of the arbitration system, i.e. the so-called capability of settlement by arbitration, the solution suggested in the model act was not taken into account.

The term of capability of settlement by arbitration, or arbitrability, is understood as the possibility of submitting a dispute (with regards to its subject), by the parties, to an arbitration court for examination. Although the model act provides for the capability of settlement by arbitration of all disputes concerning substantive rights of a commercial nature without the necessity of meeting any other requirements, the Polish legislator used the conservative construction that was abandoned recently in Germany and Austria, i.e., the countries whose legal orders are one of the sources for Polish legislation. Namely, a requirement was introduced that renders the capability of the settlement of a dispute by arbitration dependent upon the meeting of an additional criterion – the possibility of conclusion of such an agreement between the parties before the court in a given case. Furthermore, it has been made in a very imprecise manner which leads to a large dissonance in stances presented in the literature as well as considerable uncertainty in legal practice.

The current situation is highly unsatisfactory, especially considering that ascertaining whether a given dispute is capable of being settled by arbitration directly affects the recognition or enforcement of an arbitration award under the provisions of the New York Convention (United Nations Conference on International Commercial Arbitration, Convention on the Recognition and Enforcement of Foreign Arbitration Awards, New York, 10 June, 1958) or, in cases in which this Convention is inapplicable, on the basis of relevant provisions of the CCP, or alternatively, the setting aside of an award of an arbitration court issued within the territory of Poland.

Under the previous legislation, the subject of examination by an arbitration court could only be disputes concerning substantive rights, except for cases involving alimony and those remaining within the sphere of the labour law, however limited to situations in which "the parties were capable of making obligations independently" (thus provided by the repealed provision of Article 697.1 of the CCP. Under the amendment of 28 July 2005 it has been superseded by the current regulation of Article 1157). The restriction of the objective scope of such cases to only those referring to substantive rights had a very specific exception in the Polish legal practice, namely the jurisdiction of arbitration courts could not include corporate relationships concerning resolutions on organisational shareholders' rights, which were groundlessly assessed as not having a property related nature. The reason for this was the stance of the Supreme Court – although often criticised, yet still in force – pursuant to which the subject of the resolution is of decisive importance for the examination of the nature of the corporate dispute.

Announcements of the intention to modernise and liberalise the Polish arbitrations law gave rise to a hope that legal solutions in line with the direction indicated by the model act would be adopted. Meanwhile, the new regulation of Article 1157 of CCP stipulates that "unless set forth otherwise by a specific provision, the parties may submit disputes concerning substantive rights or dispute concerning legal rights in which an agreement before a court may be concluded, to the jurisdiction of arbitration courts, except for cases concerning alimony". In consequence, one of the very few issues that are clear is the maintenance of the lack of capability of settlement by arbitration of disputes concerning alimony. In light of the entire statutory regulation, it should also be indisputable that cases which are not of a civil nature are incapable of settlement by arbitration (inadmissibility of civil legal action).

On the other hand, it is beyond any doubt that the scope of cases that may be subject to examination by arbitration courts has been extended to cases under the labour law. However, the arbitration covenant concerning such disputes may be made only after the dispute arises (see Article 1164 of the Code of Civil Procedure.). Furthermore, it is indicated that the capability of settlement by arbitration was extended to disputes concerning

legal rights, provided that the mentioned eligibility for settlement may be ascribed to them which is a separate problem that has not been solved yet. The new regulation, or more specifically, the circumstances and the declared purposes behind its introduction, supported the hitherto dominant view as to the capability of settlement by arbitration of disputes concerning bills of exchange as well as disputes under consumer agreements. However, this is where the issues that are relatively clearly interpretable end.

The major dispute that arose over the new regulation refers to the finding whether the criterion of eligibility for settlement refers only to disputes concerning legal rights or also to disputes concerning substantive rights. Presently, the wrong stance seems to be prevalent – that the capability of settlement by arbitration of all disputes – concerning both legal and substantive rights – depends upon their eligibility for settlement.

It seems that the relatively conservative Polish judicature shall not attempt to release disputes over substantive rights from the additional premise of capability of settlement by arbitration in order to render them capable of examination by arbitration courts. Hence the deliberations, for now, seem to concentrate on the insufficiently analysed term of capability of settlement by arbitration. The attempts taken in the doctrine hitherto prove that it will be difficult to achieve a relatively commonly accepted understanding of this construction. As a result, a conservative construction seems to follow pursuant to which the issue at hand is allegedly the same capability to dispose of the subject of the dispute by the parties as the one mentioned in the previous regulation of Article 697.1 of the CCP.

Doubtlessly, the lack of capability of settlement by compromise - and in consequence, the capability of settlement by arbitration - takes place when provisions of the law clearly foresee so, for example in the event of Article 47712 of the CCP, which excludes the conclusion of a compromise *in cases in the scope of social insurance,* as well as Article 47711 of the CCP, which does not allow for a conclusion of a compromise agreement *in cases on the recognition of provisions of the model agreement as unlawful.* Moreover, it is a common conviction that the lack of capability of settlement by compromise is also recognised as a succession to the circumstances resulting from the nature of a given legal relationship or right, expressed, among others, in the fact that the basing of the verdict on the recognition of the statement of claims is impossible. In this context, non-property marital relations (divorce, the annulment of marriage) marital status rights or parental custody, are enumerated.

The consequences of the above are specifically unsatisfactory for supporters of opening arbitration to the widest possible scope of the cases, specifically for corporate disputes, and for the ascertainment of the invalidity or the reversal of a resolution of the meeting of stockholders of a capital company. For this reason, some of the supporters of the recognition of the arbitrability of these disputes have tried to substantiate their statements by means of granting Article 1163 of the CCP the nature of *legi speciali* towards the general principle of the code. This provision constitutes that the arbitration covenant, included in the articles of association (statute) of a commercial company, regarding disputes from the company relationship binds the company as well as its shareholders. The Supreme Court dispelled any hope of such an interpretation of the new provisions by rejecting the above opinion in the resolution of 7 May 2009 (the resolution of 3 judges of the Supreme Court, file reference no. III CZP 13/09 included in the Lex program, under no. 493962). The Supreme Court stated that the provisions of Article 1163 of the CCP do not prejudge on the capability of settlement by arbitration of any of the categories of disputes from the company relationship, and only, in referring to the issue of the form of the arbitration covenant, allow for covering by the statutory arbitration clause also of those shareholders, who acceded to the company at a later stage and did not sign the articles of association (statute).

Questioning the capability of settlement by compromise of some of the categories of corporate disputes results in uncertainty regarding the capability of settlement by arbitration also in the case of disputes on the exclusion of a shareholder from a limited liability company, as well as the dissolution of a limited liability company. In this context, an issue of a more general nature, not settled unanimously appeared, namely whether the demand of establishment of the legal relationship or the law as well as the demand for shaping the legal relationship may constitute the subject of the settlement of a court of arbitration. The reply to a question posed in such a manner should be, in principle, affirmative.

The best solution for the problems connected with attributing the capability of settlement by arbitration to many significant categories of disputes would be the determination by the Supreme Court that the criteria of the capability of settlement by compromise refers solely to non-property disputes. The legislative materials constituting the basis for the making of a relevant historical interpretation of the provisions of the CCP seem to deliver the necessary arguments for this. Since it is difficult to expect such a settlement, it seems that the intervention of the legislator will be necessary at some point in the near future. It is impossible to accept a situation, in which a fundamental change on the part of the legislator, instead of leading to the development and modernization of the law, means, in practice, stagnation and the deepening of the pre-existent disputes as well as uncertainty in transactions.

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The Conclusion of an Agreement and Ex Culpae in Contrahendo Liability in the Polish Law

BY JULITA ZAWADZKA | KUBAS KOS GAERTNER

Agreements are a basic source of creation of obligational relationships in the Polish law. The provisions of the Polish Civil Code dated 23 April 1964 provide for three manners in which the conclusion of an agreement may occur as well as the liability for the non-performance of an agreement and the so-called pre-contractual liability.

The conclusion of an agreement may occur in the manner of the acceptance of an offer, negotiations and in the manner of a tender or auction.

The conclusion of an agreement in the manner of offer acceptance takes place by making an offer and its subsequent acceptance. The offer contains the proposition of the conclusion of an agreement of a specific content. It must contain all the relevant provisions of the prospective agreement so that its conclusion may take place by simple acceptance of the offer. In the Polish law, the offeror is normally bound by their offer for a specific period of time. The offer constitutes the right of the offeree to unilaterally conclude the agreement by means of acceptance of the offer.

The conclusion of the agreement takes place if the acceptance of offer is made within the period in which the offeror is bound by their offer. This period may be defined by the offeror in the offer itself and if the offeror fails to

do so, the offer made in the presence of the other party or by means of direct communication ceases to be binding after it has not been immediately accepted.

The agreement shall be concluded only if the offeree accepts the offer in its entirety. For if the offeree accepts the offer with certain reservations or conditions, such declaration of the offeree actually constitutes a new reciprocal offer. Also, if the acceptance of the offer takes place after the expiration of the period of time in which the offeror is bound thereby, such declaration is regarded as a new offer.

In the relationships between the entrepreneurs, an offer may be cancelled before the agreement is concluded if the declaration on its cancellation was submitted to the offeree prior to the sending of a declaration on the acceptance of the offer by the latter party. However, the offer cannot be cancelled, if it has been provided in its content that the offer is irrevocable or if the time period for acceptance of the offer has been specified therein.

Another manner of the conclusion of an agreement is the tender or auction. The tender is a competition between written offers, whereby the auction is a tender carried out in a verbal manner. As regards some types of agreement, certain specific provisions prescribe an obligatory conclusion of an agreement in the manner of a tender.

The tender and auction procedure is commenced by the organiser's announcement in which they specify the time, place, subject and conditions of the auction or tender, or indicates the manner in which one may become acquainted with these conditions. The tender may be of a limited nature in which the invitation to make the offers is sent only to a specific group of potential counterparties, or of an unlimited nature in which any person may present their own offer in the tender. The same refers to auctions.

The organiser may subsequently alter the conditions of the tender or auction, but only if they reserved the right to do so in the content thereof. The announcement and conditions of the tender/auction are thus binding for the organiser from the moment of their publication. They are also binding for anyone who decides to enter the tender/auction – from the moment the offer was made and in pursuance with the announcement of the auction or tender.

The offer made in the course of an auction ceases to be binding when a more favourable offer is made by another auction participant, whereby this issue may be regulated somewhat differently in the auction conditions. The conclusion of the agreement as a result of an auction principally takes place when the status of a "winning bid" (pl. *przybicie*) is granted to the auction's participant who made the best offer. If, however, it is necessary to meet other requirements stipulated by the law (e.g., permit of an administrative authority, specific manner of the conclusion of the agreement) in order for the agreement of a given kind to be valid, the placement of a "winning bid" does not automatically result in the conclusion of the agreement, but effectuates a pre-contractual agreement between the parties which means that the organiser of the auction and the participant whose offer was accepted may pursue the agreement to be concluded.

In the case of a tender, its participants submit written offers to the organiser within the time period prescribed thereby in the announcement. Subsequently, in the place and time specified by the organiser the opening of the offers and selection of the most favourable offer takes place, or the ascertainment that none of them met the requirements set out by the organiser. In such case, the tender remains unresolved. The offer made in the course of the tender ceases to be binding when another offer is chosen or the tender is closed without the selection of any offer. However, this issue may be regulated differently in the tender conditions.

The organiser of the tender or auction may render the admission of participants to the tender or auction dependent upon payment of a specific sum or granting a security for payment of such sum to the organiser (the

so-called bid bond). If the participant of the auction or tender, despite selection of their offer, will evade the conclusion of the agreement whose validity depends upon meeting specific requirements prescribed in the law, the auction or tender organiser will have the right to retain the bid bond or pursue compensation concerning the security. In other cases the paid bid bond is subject to immediate return and the given security expires. If, in turn, the auction or tender organiser evades the conclusion of the agreement, the participant whose offer was selected may pursue the payment double the bid bond amount or compensation of the damage.

The organiser and participants of a tender have the right to demand the court to invalidate the agreement if a party to this agreement, another participant or a person acting in cooperation therewith, affected the result of the auction or tender in a manner violating the law or good practices. The authorised person may submit a claim for the invalidation of such an agreement only within one month from the date on which it learned of the reason for invalidation of the agreement, however, not later than one year after its conclusion.

Finally, the third manner of the conclusion of agreements is the negotiations. The Civil Code contains an interpretation rule pursuant to which the agreement is concluded in this manner if the parties achieve a settlement in regard of all its provisions that were the subject of negotiations, and not only the provisions that were substantially relevant. It is important that these negotiations must be carried out in order to conclude a specified agreement. By entering into the negotiations, the parties may also declare that they do so only to prepare the draft agreement, yet its conclusion will require a separate action to be performed after the determination of the content of the agreement.

The negotiations are closely connected to the institution of the letter of intent which, as in common law countries, is used also in the Polish legal system. This institution has not been regulated in the Polish law in any scope. The letter of intent is neither deemed the declaration of will to conclude an agreement nor the offer to conclude the agreement within the meaning presented above. Thus, it does not create any right on the part of its addressee to enter into agreement by means of its acceptance. It only constitutes a declaration of one party stating the current status of relationships between the parties and the will to carry out further negotiations aimed at conclusion of a specified agreement.

In the case in which the party which sent it withdraws from the negotiations without giving important reason or if it carried out negotiations with violation of good practices, the addressee of the letter of intent is entitled to pursue the compensation of the damage he suffered as a result of disloyal conduct of the partner in negotiations.

The legal basis for institution of such claims lies in the Civil Code which provides that the party which initiated or carried out negotiations with violation of good practices, particularly without the intention to enter into an agreement, is obliged to compensate the damage suffered by the other party hoping for the agreement to be concluded. Although this provision refers directly to the negotiated manner of agreement conclusion, it is assumed that the *ex culpae in contrahendo* liability refers also to damages incurred in connection to other manners of agreement conclusion.

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The Multitude of Entities in Polish Civil Proceedings and the Institution of Class Action Suits

BY RAFAL KOS | KUBAS KOS GAERTNER

The Polish civil procedure differentiates between two types of proceedings at the case examination stage:

- so-called litigious proceedings (disputable) and
- non-litigious proceedings (non-disputable).

In the case of non-litigious proceedings, the number of parties that may participate in the proceedings is theoretically unlimited – apart from the applicant, the status of a party in the proceedings (i.e., a participant) may be obtained by any person interested in the case who proves that the outcome of the proceedings affects the scope of their rights or obligations.

In the case of litigious proceedings, there are always two parties in the proceedings – the claimant and the defendant. There are no other parties, while in certain situations it is prescribed in the proceedings that several persons may jointly hold the status of the claimant or defendant. Such a situation is referred to as joint participation in a dispute.

Pursuant to the provisions of the Polish Code of Civil Procedure, several persons may appear in one case in the capacity of claimant or defendant as so-called substantive joint participants if the subject of the dispute involves their joint rights or obligations that are the same or possess the same actual and legal basis. In turn, if the basis of their joint appearance is the fact that the claims or obligations are of the same kind and stem from the same actual and legal basis, what we are dealing with is a so-called formal joint participation.

Substantive joint participation in some cases may be of a qualified nature, i.e., if a case may be instigated only against several persons jointly – such kind of joint participation is referred to as mandatory joint participation.

In the proceedings, each joint participant acts on their own behalf. However, in a case in which it follows from the nature of a disputable legal relationship or from a provision of the law that the judgment should refer *indivisibly* to all joint participants (such situation is referred to as uniform joint participation) the procedural actions of active joint participants are, as an exception, effective towards those that are passive. Nevertheless, the conclusion of an agreement, the waiver of a claim or the admission of a claim requires the *consent of all* joint participants.

As an exception, in litigious proceedings, apart from the parties, also an additional participant may appear, namely a *side intervener*. This is a person who holds a legal interest in the case being resolved favourably for one of the parties. The intervener may join the case independently or be summoned to take part in the proceedings in such capacity by the court, subject to the motion of a party.

Basically, a side intervener is authorised to all procedural actions admissible in a given case status, while the only requirement is that they should be compliant with the actions and declarations of the party which the intervener joined. Only the situation of a so-called autonomous side intervener is different. An autonomous side intervener is a participant for whom the judgement will have a direct effect in the relationships between him and the party opposing the party which he joined (since this is what follows from the nature of a disputable

relationship or a provision of the law). In such case, the side intervener may submit declarations that contradict the stance of the party which he joined, whereby the conclusion of an agreement in such proceedings, the waiver of the claim or recognition of the claim requires his consent as well.

Finally, it may also happen that a third party lodges a claim concerning an object or a right regarding which a case between the claimant and the defendant is already pending before the same court (in which case the claim is lodged against both the claimant and the defendant). Such person becomes the main intervener, a quasi-claimant, whereby the defendants are both the initial claimant and the defendant.

A revolutionary change in disputable proceedings in terms of the number of persons participating in the proceedings is the recently passed *act on the collective pursuit of claims* (the draft act has been passed by both chambers of the Polish Parliament; the "Act"). This Act is purported to transplant the institution known in the American law as *class action* and in the European law model as *collective claim* to the Polish civil litigation system.

The Polish regulation is similar to regulations adopted in other EU countries; proceedings are instigated by one collective statement of claims within which the protection of individual interests of multiple injured parties as a result of one event is performed; this mechanism is designed to work within the framework of the so-called *"opt-in"* model; it is assumed in the *"opt-in"* mechanism that a judgment issued as a result of the statement of claims lodged shall be binding *only* for the injured parties who expressly and unequivocally manifested their will to take part in such proceedings through clear indication of their will to participate in the said proceedings.

Deciding on the "opt-in" model in all categories of cases, especially in so-called mass litigation cases, the Polish legislator ignored the fact that: (i) this model is more expensive and less efficient than the American "opt-out" mechanism, since more entities may interfere in the litigation; (ii) it may turn out to be ineffective in light of some typical models of social behaviour – the general public, and more specifically consumers are unlikely to join collective claims due to the costs and time as well as complexity of the procedure in such cases; (iii) the person joining the collective action acknowledges the fact that the defendant shall not pay full compensation, since – based on the statistics – it is almost certain that not all consumers will join the litigation which means that this model will not allow for achieving the preventive effect against entities guilty of unfair market practices; and (iv) it may result in discrepancy of judgment in factually identical cases, since persons who will institute individual cases may lose, despite the fact that – for example – the collective claim was successfully won.

The Act is of procedural nature; it does not interfere in the substantive-law principles of compensation, namely those that refer, e.g. to the manner of adjudication (valuation) of compensation, causal connection, etc.

In comparison to the American *class action* model, the Act lacks a clear statutory effectiveness premise *(numerosity)* for the institution of a collective claim. A relatively low number of 10 persons has been assumed as the minimum number of participants. It should be noted, as already mentioned above, that the Polish CCP stipulates some institutions of "collective" pursuit of claims. Thus, the non-introduction of additional criteria for the admissibility of a collective claim seems to be an error in light of the fact that the already existent legal solutions may be no less effective.

The Act adopts a rule of representation, i.e. it allows one entity – the representative – to act in collective proceedings in favour of and with effects on the sphere of rights of other entities. Thus, there are certain

similarities to the solution applied in America. In the formal procedural sense, only the representative is a claimant – a party to the proceedings. All other members of the group for whom the class action is a manner of pursuing their subjective rights do not hold the status of a party in the proceedings (although in the substantive-law meaning, they still are parties) which means that they are deprived of the party's rights in such group proceedings except for the listed dispositive and substantive acts.

A person that would like to become a member of the group should "prove" or at least "substantiate" their right to participate in the group. The Acts stipulates that the claimant may oblige a member of the group to lodge additional evidence and explanations.

In group proceedings the Court shall issue a decision concerning the "composition of the group" after the defendant raises charges as to the said "composition". It is stipulated in the Act that decisions as to the group composition shall be subject to appeal by means of a complaint.

The proceedings will have four stages:

- stage one (initial) – the examination of the admissibility of a collective claim concluded with the issuance of a court decision on the examination of the case in the manner of group proceedings or a decision on the rejection of the collective claim (so-called *certification*);
- stage two – the formation of the final group, the determination of the group participants in the proceedings, the objective and subjective scope of the proceedings, including the obligatory announcement on the institution of a claim in group proceedings;
- stage three – essentially means the examination of the case as to its merits, including joint proceedings as to evidence as well as issuance of the verdict, and
- stage four – the performance of the judgment; in the case of the adjudication of pecuniary service in favour of individual members of the group (subgroup), the excerpt from the verdict specifying the amount due constitutes an enforcement title.

The initiative to introduce the institutions of group proceedings to the Polish civil procedure should be regarded very positively, although some of the regulations in their current shape will require further analysis and amendments made by the legislator.

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BELARUS

International Commercial Arbitration in Belarus

BY ALEXEY ANISCHENKO | SORAINEN

Until recently, arbitration was not perceived by commercial people and business lawyers in Belarus as a real alternative to resolution of commercial disputes in state courts. Presently, the International Arbitration Court of the Belarusian Chamber of Commerce and Industry (BelCCI; hereinafter the "IAC") remains the only permanent arbitration institution operating in Belarus authorised to consider commercial disputes involving both national and foreign parties.

There were a few reasons for the relative unpopularity of arbitration in Belarus. First of all, Belarus does not have a long-lasting legal tradition of effective use of alternative dispute resolution. Due to the state-dominated economy, most commercial (or, as they are called in the legislation, "economical") disputes were naturally "kept" within the state system.

Second, and most importantly from a practical perspective, resolving commercial dispute in Belarusian commercial courts is cheap and quick. In that respect Belarus is unique. While dispute resolution lawyers in the rest of the world are arguing whether arbitration is still a better alternative to litigation as regarding cost and timing, their Belarusian colleagues never had such a dilemma. Under existing commercial procedural legislation and established practice the decision on commercial dispute is normally rendered within 1.5 months upon submission of the claim, with a very limited number of exceptions. All four instances, including supervisory instance of the Supreme Commercial Court, could be passed through within half a year. The costs of commercial litigation in most cases are lower than arbitration costs.

Third, there was a certain information vacuum on ADR in general and particularly on international arbitration. The IAC is weak in marketing and promoting its activity and did a little to change the situation and to promote itself on either a national or international scale. There is still no effective website of the IAC (there is only a webpage on the website of the Belarusian Chamber of Commerce and Industry). One can find very limited information on the IAC, especially in foreign languages. Until recently the IAC was not active enough in conducting seminars and conferences to promote itself and arbitration in general among the Belarusian and the foreign legal and business community. The IAC has also been criticised for lack of transparency to the public that certainly did not build up enough confidence in the institution among its existing and prospective users.

Nonetheless, according to unofficial sources (the IAC does not publish statistics) the IAC considers roughly 70-80 cases per year, which is a relatively significant number when compared with arbitration institutions in CIS and Baltic States. It is strongly believed by the local professional community that in coming years the caseload will grow and the IAC will increase its adjudicatory role on both a national and international scale. Why is that?

On the national level the key driver could be the overload of the state commercial courts due to the economic downturn (up to 150% increase of the caseload has been reported) and the extreme need to develop alternative dispute resolution means. It is expected that a new law on arbitration may be introduced to facilitate arbitration of domestic disputes. In addition, there is a growing interest in arbitration among public and practicing lawyers in particular. It was a very progressive step for the IAC to start publication of its awards, in particular through a major provider of legal databases.

Most of the potential is on the international front. The vast majority of cases settled by the IAC (up to 90%) are of an international nature; domestic disputes traditionally form only a minor part of the caseload. Nationality of the parties varies considerably but most represented are parties from Russia, Ukraine, Poland, Kazakhstan and the Baltic States. And in the current difficult times there is certainly a great chance to promote the IAC for the settlement of middle and small-sized disputes between eastern and western businesses.

Several factors shall be taken into account by foreign and local legal counsels when choosing Belarus as an arbitration forum.

First and foremost it is the arbitration friendly environment. The basement is the Law of the Republic of Belarus No 279 dated 9 July 1999 "On International Arbitration Court (Tribunal)" that follows rather closely the 1985 UNCITRAL Model Law. The actual version of the Rules of the IAC adopted in 2000 and last amended in 2009, although not being perfect, provide all necessary means for experienced arbitration counsel to defend its case before the arbitration tribunal established under the auspices of the IAC. Yet there is an ongoing work carried out with joint efforts of local and foreign professionals to ensure the Rules meet modern arbitration standards.

As Belarus is a party to the New York Convention on Recognition and Enforcement of Foreign Arbitration Awards and the European Convention on International Commercial Arbitration, no major traps and problems with enforcement shall be expected. The only two important issues to be carefully considered when entering into a commercial relationship with the state or state-owned companies are the concepts of public policy and sovereign immunity that are not well-established and construed rather broadly by the state courts.

Secondly, it is again the issue of costs and timing. Contrary to comparison with local commercial courts the IAC will certainly be cheaper and more expedite than any of its potential rivals in Russia, Ukraine, Poland and the Baltic States. The difference is much higher when compared with leading European institutions. By way of example arbitration costs of handling a MEUR 1 case in Minsk by a panel of three arbitrators established under the IAC Rules will cost roughly 4 times less than in Stockholm under the auspices of the Arbitration Institute of the Stockholm Chamber of Commerce that was historically considered the best foreign venue on post-soviet territory.

The Rules are not only modest with the scale of fees; they also provide a great degree of flexibility on costs. According to the Rules all expenses incurred during the arbitration proceeding are divided into :(i) arbitration fee (including registration fee); and (ii) costs related to arbitration proceedings. The registration fee, which is an integral part of the arbitration fee, amounts to €150. It is fixed and non-refundable. The rest of the arbitration fee depends progressively on the claimed amount. The costs related to arbitration proceedings include travel and other expenses, incurred by arbitrators; payments to witnesses, experts and specialists and other expenses of the arbitral tribunal. It shall be also noted that VAT (now 20%) shall be levied on all payments due to the IAC.

All decisions on costs and their allocation between the parties are left to the tribunal. By general rule the tribunal awards the winning party the reimbursement of all arbitral expenses incurred from the party that lost

the dispute or divides them between the parties proportionally if the claim was upheld in part. Compensation of legal costs could also be awarded. If one of the parties acted in bad faith the tribunal may oblige to compensate additional expenses of the other party caused by misconduct. The arbitral tribunal can also refuse reimbursement of costs related to arbitral proceedings if it decides that they were unreasonable or excessive.

As a general rule the arbitration proceedings may only be commenced upon the receipt of the arbitration fee by the IAC, but the claimant may apply to the Chairman of the IAC for the permission to pay down to 50% of the arbitration fee first and if such permission is granted, to pay the rest before the first hearing takes place.

According to the Rules, the amount of the arbitration shall be decreased by 30% if the dispute is settled by a sole arbitrator, provided that in all cases the arbitration fee shall be not less than €700. If the same dispute shall be reconsidered by the IAC in case of setting aside or refusal in recognition and enforcement of the initial arbitral award, the amount of the arbitration fee is decreased by 50%.

If arbitration proceedings were terminated after payment of the arbitration fee, 75% of the paid amount of the arbitration fee shall be refunded if that happened before the establishment of the tribunal or 50% after the establishment of the tribunal but before the first arbitration hearing has taken place.

The Rules require the tribunal to consider the dispute and render the award within not more than 6 months from the time of its formation. In practice, the IAC endeavours to ensure observation of this time-limit, but not always successfully. It is seldom that the IAC is able to deliver an award earlier. If the case is complicated the award is sometimes rendered and released to the parties sometimes in about a year from the commencement of arbitration. Still, that is not the worst case scenario when compared with other institutions.

The scrutiny of the award by the Chairman of the IAC could be one of the reasons for possible delays but the IAC affirms that usually it takes no more than one week for the Chairman of the IAC to accomplish the scrutiny procedure and certify the award as stipulated in the Rules. But on the other hand such a scrutiny may be considered as an institutional advantage ensuring the quality of the awards. It shall be noted here that the IAC awards are set aside in Belarus only on very rare occasions. There are no available statistics on recognition and enforcement of the IAC awards abroad, but no major problems have ever been reported.

Finally, such factors as overall liberalisation of the economy and legal regime for doing business, substantial increase of the private sector, improved infrastructure (airport, hotels, translation services), should not be underestimated. In that regard, existing visa requirements remain the only “technical” impediment for foreign parties to welcome the choice of the IAC from a pure “logistic” perspective.

It is, of course, time and practice which will have the final word on perspectives of international arbitration in Belarus. Much will depend on if the approach of the Belarusian commercial courts remains “arbitration-friendly”, particularly in relation to interim measures of protection, recognition and enforcement. But if the current positive trend does not change, Minsk will certainly become a visible spot on the global international arbitration map in the very near future.

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Enforcement of Foreign Judgments and Arbitral Awards in Belarus

BY ALEXEY ANISCHENKO AND MARIA YURIEVA | SORAINEN

Belarus is often perceived as a "closed" or "unfriendly" jurisdiction to foreign judgments and arbitral awards. However available statistics shows the opposite. According to the Supreme Commercial Court of the Republic of Belarus, there was no single refusal to recognise or enforce a foreign arbitral award or foreign judgement in 2008-09. At the same time, a considerable number of application were returned to the applicants for mere procedural technical reasons: failure to submit all documents, required by law and/or lack of proper certification and/or translation of documents, non-payment or improper payment of state fee, etc. Particularly in 2008, 31 applications on recognition and enforcement of foreign judgements and arbitral awards rendered in Ukraine, Russia, Moldova, Sweden, Poland, Latvia, Lithuania, Austria and other European countries, as well as the US, were filed with commercial courts in Belarus. Sixteen of them were satisfied whereas the other fifteen were returned because of the aforesaid procedural defects. In order to help potential applicants to avoid such mistakes, this article will briefly describe the legal framework and procedure of recognition and enforcement of foreign judgements and arbitral awards in Belarus and will identify the main traps that may impede successful enforcement.

Legal Framework

Rules on enforcement of foreign judgments and arbitral awards in Belarus are determined at both national and international level since Belarus is party to a number of bilateral and multilateral international treaties dealing with recognition and enforcement issues. There is also a dual system on the national scale:

- Foreign judgments and arbitral awards arising out of commercial (economic) disputes and insolvency cases are recognised and enforced in Belarus in commercial courts according to the procedures set by the Commercial Procedural Code of the Republic of Belarus dated 15 December 1998 (as amended; the "ComPC").
- Foreign judgments arising out of other civil disputes involving individuals, family or labour cases are recognised and enforced in Belarus in civil courts according to the procedures set by the Civil Procedural Code of the Republic of Belarus dated 11 January 1999 (as amended; the "CivPC").

There is an important difference between the two: the ComPC stipulates that recognition and enforcement of a foreign judgement or arbitral award could be granted on two grounds, namely if it is provided by an *international treaty* to which Belarus is a party or on the basis of *reciprocity principle*. So far, the latter principle was rarely used in practice and there were only few reported cases on successful recognition of German, Estonian and French court decisions in Belarus on the basis of reciprocity. CivPC, however, does not consider reciprocity as a ground for recognition and enforcement. In the absence of a respective international treaty, recognition and enforcement of such a foreign judgment or arbitral award that relates to civil (non-commercial), labour or family disputes in Belarus shall not be possible. Still, foreign judgments and arbitral awards that do not require enforcement are in principle recognised in Belarus if no objections are raised by the counterparty. Such objections are to be submitted with the court within a month from the date the counterparty knew that the application for recognition was filed with the court.

Belarus is a party to a number of international treaties that provide for mutual recognition and enforcement of foreign judgements. There are several regional conventions involving CIS countries:

- Convention for Settlement of Disputes Connected with Commercial Activities (Kiev Convention) of 20 March 1992;
- Convention on Legal Assistance and Legal Relations on Civil, Family and Criminal Matters (Kishinev Convention) of 7 October 2002;
- Convention on Legal Assistance and Legal Relations on Civil, Family and Criminal Matters (Minsk Convention) of 22 January 1993.

Besides that, Belarus has ratified bilateral agreements for legal assistance on civil matters with 11 countries, namely with China, Cuba, Czech Republic, Finland, Hungary, Iran, Italy, Latvia, Lithuania, Poland and Vietnam.

With regard to foreign arbitral awards provisions of the 1958 UN Convention on Recognition and Enforcement of Foreign Arbitration Awards (New York Convention) are applicable.

Procedure

Both in commercial and in civil courts, recognition and enforcement shall be granted upon examination of a written application for recognition filed with the court. Foreign judgments and arbitral awards are not to be reviewed *per se* by Belarusian courts provided that all of the procedural requirements have been met. Belarusian courts would accept jurisdiction of the foreign court provided that the case is not within the exclusive competence of Belarusian courts under Belarusian legislation or the international treaty to which Belarus is a party. There are no major procedural differences between procedures at civil and commercial courts.

Applications for recognition and enforcement shall be submitted to a commercial court of first instance at the place where the debtor resides or, if such place is not known, at the place where the debtor's property is located.

The application for recognition and enforcement of a foreign judgment or arbitral award shall indicate the name and place of residence of the foreign court or arbitral tribunal (in the latter case composition of the panel shall also be indicated); names and places of residence of the applicant and the debtor; information about the foreign judgement or arbitral award and a precise request for its recognition and enforcement. There are no legal requirements for special allegations (e.g., that the judgment is not against public morality, that the judgment is no longer appealable, etc.) to be included in the application.

The set of documents to be attached to the application slightly differs depending on whether recognition and enforcement of foreign judgement or arbitral award is being sought. The application for recognition and enforcement of foreign judgement shall be accompanied with the following documents:

- certified copy of the foreign judgment;
- certified copy of the document confirming the judgment came into force or that it is subject to be performed prior to it comes into force unless this information is given in the body of the judgment;
- certified document confirming the debtor was timely and properly notified on the litigation in a foreign court;

- certified document confirming the authorities of the signatory (power of attorney, etc.);
- document confirming the copy of the application was forwarded to the debtor;
- certified translation of the documents listed above into Belarusian or Russian language; and
- document, verifying payment of state fee (that currently amounts to approximately €85).

The application for recognition and enforcement of a foreign arbitral award is to be submitted along with:

- certified original or copy of the foreign arbitral award;
- original arbitration agreement (or its properly certified copy);
- certified translation of the documents listed above into Belarusian or Russian language; and
- documentary proof of payment of state fee.

In case the application is submitted by a foreign company, an extract from trade register and/or official document confirming its legal status and capacity should also be submitted.

The commercial court must consider the application and render its ruling no later than within one month from the date of filing the application, regardless of whether it is opposed or unopposed. The application is considered in an open court hearing with both parties being notified. If a party fails to appear in a court hearing that will not prevent the court from considering the application and rendering its ruling.

Belarusian legislation does not permit to refuse recognition or enforcement on the merits. The ComPC essentially follows article V of the New York Convention also in regard to foreign judgements of state courts. Thereby Belarusian commercial court may refuse recognition and enforcement of a foreign judgment or arbitral award only if:

- the judgment (arbitral award) has not come into force;
- the party against which the judgment (arbitral award) was rendered had not been timely and properly notified on place and time of the court hearing or was not able to present its case for other reasons;
- the dispute falls within the exclusive jurisdiction of Belarusian courts;
- there is a valid decision of a Belarusian court on the same dispute between the same parties regarding the same subject and on the same grounds;
- a Belarusian court considers the same dispute between the same parties regarding the same subject and on the same grounds and respective proceedings commenced at the Belarusian court earlier;
- the limitation period for enforcement has expired and was not restored; and
- the enforcement would contradict public policy of the Republic of Belarus.

The ruling of a commercial court of the first instance (whether positive or negative) enters into force immediately upon being declared but can be appealed to the cassation and/or supervisory instances of the Supreme Commercial Court of the Republic of Belarus.

If recognition and enforcement were finally granted, the applicant receives an enforcement court order that will have the same legal effect and will be executed under the same execution procedure as enforcement court orders issued following domestic judgments.

Finally it shall be noted that if the applicable international treaty contains different procedural provisions it shall prevail over national procedural legislation.

Potential Pitfalls

Yet there are number of local specifics that shall be taken into account by foreign parties when having a dispute that may end up in the need of recognition and enforcement in Belarus.

First of all, one should know that Belarus recognises and enforces only final foreign judgements and arbitral awards. Interlocutory decisions or court rulings granting interim measures will not be recognised and enforced. Very recently the Cassation Instance of the Supreme Commercial Court of the Republic of Belarus overturned the ruling of Minsk Commercial Court whereby it granted recognition and enforcement of the ruling of Vilnius Commercial Court on granting interim measures against a Belarusian respondent based on certain provisions of the bilateral treaty on mutual legal assistance between Belarus and Lithuania. The higher instance decided to opt for narrow interpretation of the treaty and essentially ignored reciprocity principle as Lithuanian courts in the same situation will recognise Belarusian court rulings on interim measures of protection.

Second of all, according to the ComPC only the party to original proceedings can file application for recognition and enforcement. Therefore if there is a cession the assignee might need a separate ruling from the court (tribunal) that rendered the judgement (award) to confirm procedural substitution. It is even more important to know when there is an arbitration agreement in place, that Belarusian law does not recognise cession of arbitration agreement in principle. Therefore if the arbitral award was rendered in a dispute between the parties different from the parties to the original arbitration agreement and the subsequent cession was not accompanied by a new arbitration agreement than there is a high risk that Belarusian commercial court will refuse recognition and enforcement as contradicting to public order.

Finally, in each particular case, especially those involving state and state companies, the issues of exclusive jurisdiction, state immunity and arbitrability shall be carefully analysed. There were several cases when commercial courts used those concepts to deny recognition and enforcement. For example, in 2005 the Supreme Commercial Court refused recognition and enforcement of several arbitral awards against a state-owned company on the ground that it may be contrary to the interests of the state and other creditors in pending insolvency proceedings and therefore it would be against public policy.

Apparently, the best way to minimise the indicated and other possible risks is to consult with a local adviser well in advance, not only just before filing an application for recognition and enforcement of the given judgement or arbitral award, but rather when jurisdiction clause is being negotiated by the parties.

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LATVIA

The Law and Practice Regarding Securing of the Court Claims in Latvia

BY EDGARS BRIEDIS | SORAINEN

This article will address the court practice of Latvian courts concerning the application of temporary measures in order to secure the claims brought before the courts by claimants. It will be analysed whether court practice actually complies with the legal rules allowing securing of the court claims and how such court practice impinges upon the principle of legal certainty and the flow of day-to-day business activities of the defendant. It also will be analysed whether any recent changes in the court practice regarding application of temporary measures can be noticed within Latvian court practice.

The Latvian law provides that the grounds for securing the court claim are factual circumstances that indicate that enforcement of an eventual judgment in the future might be difficult or even impossible.

There are two types of these circumstances. The first are attributable to the behaviour of the debtor or, in other words, are intentionally created by the debtor with the aim of avoiding fulfilment of the contractual obligation. An example of such circumstances is the sale of assets performed by the debtor or change of the place of business without notifying the creditor. As noted, such circumstances could serve as the ground for securing the claim only if the aim of the debtor is to avoid fulfilment of the contractual obligation. Often it is practically difficult or even impossible to determine the real intention of the debtor hidden behind one or another activity. Therefore, in practice, intention of the debtor often is derived from the objective eventual effect of its activities on enforcement of the eventual judgment. In other words, if the nature and consequences of the activities of the debtor are such that enforcement of eventual judgment might be difficult or even impossible then it is likely that the court will secure the claim.

The second type of these circumstances covers those not being dependent on debtor. An example of such circumstances is existence of damages that, unexpectedly, of course, have been borne by the debtor. The idea is that such damages result in decrease of the total amount of assets the debtor has which, in its turn, might make it difficult to satisfy all possible claims of the creditors. If the debtor was not insured against such damages then the fact that the debtor has suffered damages is even stronger ground to argue that the claim of the creditor should be secured.

There could be many other different circumstances that can serve as the ground for request to apply a preliminary measure in order to secure the court claim. However, any of these circumstances can be classified as either dependent or independent from the intentions of the debtor. In the meantime, it is always up to the court to assess these circumstances and to decide whether the circumstances of the particular matter give reason to believe that enforcement of eventual judgment will be difficult or even impossible and thus to apply

a temporary measure.

The Latvian law allows application of the temporary measure as a security means not only when the court proceedings are already pending but also before initiation of the court proceedings. Moreover, the application of the temporary measure can be requested also if the obligation of the debtor is not due yet.

The problem, however, is availability of the information. Namely, the question is whether the creditor is aware of the circumstances that allow requesting application of the temporary measure. Knowledge of these circumstances is important as, according to the general principle of law, the creditor has to prove the existence of these circumstances. If the creditor does not know about these circumstances, he can neither substantiate the request to apply a temporary measure nor produce evidence necessary to prove existence of these circumstances.

The request to apply a preliminary measure, therefore, might be successful only if three following stages have been completed. First, the collection of information about the financial and business status of the debtor is performed. Second, this investigation reveals information about facts that obviously could be a good ground to request application of a preliminary measure. Finally, this information is adequately explained within the application addressed to the court.

Very often, however, the creditor who wants to collect the debt is willing to request application of the preliminary measure but does not possess information on whether the necessary circumstances for such procedural measure indeed exist. If the creditor does not have this information then the request addressed to the court is based on allegations rather than on facts supported by evidence as required by the law.

In this context, interesting information has been revealed by the survey of court practice made by the Supreme Court of Latvia. This survey covers the court cases decided in 2006 and 2007 and, among other issues, addresses the application of the temporary measures. Interestingly enough, the Supreme Court has found (although, theoretically possible that Supreme Court decides issues related to application of temporary measures, most often, those are first instance courts and appellate courts that decide on these issues) that lower instance courts are of the opinion that when the creditors seeks for temporary measure during the pending court proceedings there is no need to produce any evidence supporting the point of view that the enforcement of the eventual judgment might be actually difficult or impossible in the future. Instead, it is enough that the creditor is in doubt that the defendant will have sufficient assets to pay the debt.

As we can see, there is a difference between the test where existing circumstances that indicate that enforcement of the eventual judgment might be actually impeded or made impossible are required and the test where only doubts of the debtor are required in order to apply a preliminary measure. The first test is objective while the second test is subjective. If in the case of the first test application of a preliminary measure objectively would safeguard interest of the creditor, then in the case of the second test application of a preliminary measure still would safeguard the interest of the creditor but in the meantime it would be objectively ungrounded. It would be ungrounded because decision on application of a preliminary measure would not be based on any circumstances indicating that enforcement of eventual judgment might be actually difficult or impossible in the future. If such indications do not exist, there should not be ground to think that enforcement of eventual judgment will be actually difficult of even impossible. In other words, temporary measures are not merely for satisfaction of the creditor's willingness to safeguard recovery of the debt but rather to satisfy such creditor's willingness if there are objective reasons to believe that if the claim will not be secured the actual recovery of the debt might be fruitless.

The approach of the first instance and appellate courts discovered in the above-mentioned survey of the

Supreme Court of Latvia has been criticised by the Latvian practitioners of law. Such criticism has been fairly based also on the argument that existing court practice in application of temporary measures which is based on the test of the creditor's doubts disrupts the legal certainty and predictability of legal decisions in certain common situations.

Disruption of the legal certainty creates a business environment where even the merchants and companies who have and, most likely will have, sufficient funds during the disputes can never be sure that these assets and money in bank accounts are seized during the court disputes because the court has applied temporary measure. Such seizure of assets can not only be a significant obstacle for further business activities of the defendant but also could paralyse the business activities of the defendant which, in turn, can result in a necessity to pay late payment interest and contractual penalties to other creditors.

Thus, even if the managers of the company are duly and diligently doing their job and asking for the opinion of legal counsel on whether envisaged activity creates a risk to be subjected to any temporary measure and even if the answer of the legal counsel is that objectively there is no ground to apply a temporary measure, there is always a risk that temporary measure can be applied for the mere doubts of the creditor will be sufficient ground for that according to the practice of Latvian courts. It is worth noting that the creditor's subjective view almost always is that there is a doubt regarding the ability of the eventual debtor to satisfy the claim.

However, the recent case law of Latvian courts on application of temporary measures indicates that the courts have started to assess the eventual influence of the applied protective measures on the flow of the debtor's day-to-day business. As a result of that, some courts tend to apply a protective measure that is less harmful for the eventual debtor's business activities but still ensures actual enforcement of the eventual judgment in the future.

Unfortunately, not all courts in Latvia employ this approach. For some courts, a creditor's doubts still can be a sufficient ground to apply a temporary measure in order to secure the claim. Therefore, one still could argue that legal certainty in Latvian court practice is lacking, which is so important for businesses trying to manage their legal risks.

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Management Liability in Latvia

BY IEVA BERZINA-ANDERSONE | SORAINEN

Management liability is an important tool of corporate governance regulation, which aims to ensure that managers of a company do their best to perform their duties in the interest of the company. If the managers fail to do their duty with respect to the company, they may face a certain liability. This tool is effective, if the company in practice can receive satisfaction from its management members who have failed to fulfil their tasks. In Latvia, since 2002 there is sufficient legal framework to establish management liability. Managers are expected to act in the best interests of the company and be dutiful and loyal. If they do act unlawfully, the company can claim from them the

losses caused. Unfortunately, in practice the Latvian courts have been reluctant to find managers liable for losses caused to the company, perhaps due to the lack of precedents and sufficient practice.

In Latvia, management liability applies to the management board members of commercial companies, i.e., persons who are entitled to represent the company within the daily management, as well as to the supervisory board members, i.e., persons who are supervising the management board and often approve strategic decisions of the company. The Latvian Commercial Law provides that these managers of the company must always act as good and dutiful masters. They are jointly responsible for losses caused to the company due to their unlawful actions. The company may claim the management liability subject to a shareholders' decision to do so, if the following preconditions apply: there have been unlawful actions by the management, the company has suffered losses, and there is a causal link between the unlawful management actions and the suffered losses. Moreover, the law provides strict liability, which means that the management's fault for the losses caused by their actions is presumed, and the managers bear the burden of proof to bring the evidence to the contrary. Claims may be brought not only against the current managers, but also against the previous management.

The Commercial Law does not elaborate further, what it means to be a good and dutiful master. However, the notion of a dutiful master is used also in the Latvian Civil Law. The cross-reference to the provisions of this law hints that such a master must not allow even a slight negligence, not even speaking about gross negligence or wilful misconduct. The legal writings suggest that the management duty includes an obligation to follow the law, the articles of association of the company, to act in accordance with the shareholders' decisions, as well as to be loyal to the company and its shareholders. The loyalty duty includes that managers must act in good faith and primarily in the interests of the company, not in their own interests. Even if their own interests would conflict with the interests of the company, they have to put the company's interests forward.

All of this looks very promising when written in the law and discussed in legal writings. However, it is important that management liability may be efficiently litigated and enforced by the court. Up to now, the situation in Latvian courts with respect to management liability claims is far from satisfactory.

As a main problem, there have not been many management liability claims in the Latvian courts. Thus, the courts lack precedents and experience in deciding such claims. To our knowledge, there have been virtually no cases against supervisory board members, and few cases against management board members.

Moreover, the single case, which according to publicly available information has been reviewed by all three court instances, is not very instructing, as the claim was dismissed due to formal reasons and perhaps improper preparations by the claimants (e.g., the shareholders' meeting had not approved the raising of the claim). There have been more cases reviewed by lower instance courts, but it is difficult to make any complete summaries of the practice, as only selected court decisions are publicly available in Latvia (others are fully available only to the parties of the case).

In addition, it often seems that the courts are unwilling to apply management liability in cases, where the unlawful activity of the management is not straightforward and the losses are more an indirect than direct consequence of management's actions. Thus, in 2007, an appeal instance court rejected a claim against a manager for the losses caused by the penalties to the company imposed by the tax authority. The court considered that the liability of the manager for these penalties is not established. This finding seems unfounded, as it was evident from the case that the penalties were imposed due to improper accounting (the management is responsible for accounting supervision) and failure to appeal the tax authority's decision.

In another notorious case adjudged in 2009, the first instance court rejected a claim against a manager for the losses caused to the company by excessive lease payments and a resulting necessity of the company to terminate this lease agreement and pay a contractual penalty. The management had not only concluded a disadvantageous lease agreement on behalf of the managed company, but had also used their powers by concluding this lease agreement with a company owned by them. It was clear from the facts that the provisions of the lease agreement were beneficial only for the landlord company owned by the managers, and very strict and disadvantageous (including exceptionally high lease payments and large contractual penalties) for the lessee company managed by these managers. The court, however, established that the cause of losses was not clear and that it was not prohibited per se for a manager to conclude an agreement on behalf of the managed company with a company owned by him. However, the court failed to analyse that by these actions the managers clearly were in breach of the duty of loyalty towards the company represented.

There have been also some cases with positive results for the claimant company, but they have included quite clear and uncomplicated violations, such as damage caused to the company's property.

Nevertheless, an overall trend is that the Latvian courts have been reluctant to analyse more complicated cases of management liability and, in case of doubt, tend to adopt an approach more favourable to the accused managers than to the company. This, however, should not encourage Latvian managers to act recklessly against the represented company by hoping that the courts will continue being friendly and fail to enforce the management liability efficiently. As noted above, the Latvian law provides sufficient legal framework for the management liability. Recently there have been more writings both in the legal doctrine and in general media stressing the duties of management and pointing out the potential liability. It may be reasonably believed that the courts will gain more experience on the topic and thus there should be more successful outcomes for claimant companies, provided that the claims are sufficiently grounded.

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Choosing Between Mediation, Arbitration and Litigation in Cross-Border Disputes – Latvian Perspective

BY AGRIS REPSS | SORAINEN

When determining what type of dispute resolution should be considered when entering into a contractual relationship, which potentially might need adequate dispute resolution mechanisms, as well as when planning strategy in an already existing dispute in Latvia, a number of legal and practical aspects should be taken into account. A proper choice of the dispute resolution venue might enhance the prospects of a successful result and ensure a more efficient litigation.

If swiftness of dispute resolution is crucial, one should know that state court proceedings in Latvia might take a long time. Even a simple commercial dispute could last more than three or four years until a final judgment is

rendered in Riga. Courts outside the capital are not so overloaded and it takes less time, but still one should not expect a speedy process. This drawback of the Latvian judiciary might lead to believe that alternative dispute resolution mechanisms such as arbitration and mediation could be a potential solution.

Arbitration in Latvia, on the other hand, has its peculiarities. It is important which arbitration institution is chosen in Latvia, because only a few arbitration institutions are capable of resolving complex commercial cross-border matters. There are more than a hundred registered institutional arbitrations in Latvia. Most of them are so called "pocket arbitrations" of some companies, banks, debt collection agencies, law firms with closed list of arbitrators, which restrict the appointment of arbitrators outside that list. Many of these small institutional arbitrations are more like profit driven instruments for getting the required award. One should not expect legally well reasoned award in these arbitrations. Therefore it is important to check the background of the arbitration institution which is being considered in Latvia.

Arbitral awards are final and are not subject to legal review or setting aside process. Only at the enforcement stage can one raise objections if due process has not been observed. Given this aspect of arbitration, sometimes the possibility to appeal court judgments and decisions might be an important argument in deciding whether to refer disputes to state courts in Latvia as opposed to arbitration. It is understandable that a foreign company might be concerned about local bias in courts and in arbitration in Latvia. Therefore, in practice, when risks and interests of the parties substantiate it, it is advisable to consider choosing an arbitration institution outside Latvia.

Applicable law is another aspect that might determine the choice of dispute resolution method in a cross-border deal. Should the parties consider applying a law other than Latvian law to their contractual relations and possible disputes, one should bear in mind that neither Latvian courts nor arbitration institutions have an established tradition and practice in applying foreign laws. Apart from practical difficulties and additional costs that the application of foreign law might involve, which is similar in all jurisdictions, there are no established traditions, practices and methods of how the courts and arbitrations act when they are faced with the application of foreign law. Although there are procedural rules in Latvian law that deal with the application of foreign law, there are many issues that require more established practices in order to have some degree of legal certainty. Therefore, the choice of applicable law should always be considered together with a potential venue and dispute resolution method, for it is the court or arbitration that will eventually need to apply the law. There is no guarantee that the foreign law will be interpreted and applied the same way as it is applied and interpreted by the courts or arbitration of the country of its origin.

Mediation could be a feasible solution, because it is a less institutionalised dispute resolution method and can be well applied in cross-border disputes. An important advantage of mediation is that it is aimed at amicable settlement of a dispute and often helps the parties not only avoid judicial proceedings but also preserve business relations. Unfortunately, until recently there has been certain reluctance in accepting mediation as a feasible dispute resolution method in commercial matters in Latvia due to the lack of certain traditions in commercial culture. There is also lack of trained mediators.

Even if mediation is seriously considered, parties in disputes often wish that there is still some element of adjudication in mediation whereby a mediator would say a final word on what should be a solution of the dispute. Such an approach and understanding of mediation is not uncommon in other jurisdictions as well. Mediation where the mediator not only facilitates the settlement but uses some elements of adjudication could be exercised by a court. It is known as an integrated mediation model, whereby a judge during the court process would try to

find a possibility for parties to amicably settle by combining elements of adjudication and mediation process. For such a model, special legislation is necessary, which currently is not available in Latvia. Therefore the courts, although welcome to do so, usually do not engage in facilitating settlement in civil and commercial disputes.

It has been recognised by the Latvian government as well that alternative dispute resolution methods in civil and commercial disputes that are aimed at settlement of disputes are not well developed in Latvia and do not satisfy the needs of the commercial community. Often court adjudication is deemed as the only solution in civil and commercial disputes. The above described peculiarities of arbitration institutions in Latvia have resulted in considerable distrust in arbitration as a good alternative to dispute resolution in courts. Although there are a number of government supported initiatives in introducing and developing various mediation models in Latvia, little progress is noticeable to date. Nevertheless, some development in facilitating mediation will take place because Latvia, like all EU Member States, is obliged to implement the EU Directive 2008/52/EC on certain aspects of mediation in civil and commercial matters.

Nonetheless, regardless of the lack of legal framework for mediation in Latvia, parties are free to detail and elaborate in their contracts mediation as the dispute resolution method. Such agreement should address the process of how the mediator will be chosen, and certain procedural time frame and rules of mediation process, costs of mediation, the termination of mediation process if parties cannot reach a settlement, and how the settlement is exercised if it is achieved.

All in all, when choosing a dispute resolution method in Latvia, one should consider that the lengthy court proceedings could substantially delay the resolution of the dispute. Arbitration institutions in Latvia should be chosen with great care and caution. Most of the institutional arbitrations are not suitable for resolving cross-border disputes in Latvia and have closed lists of arbitrators. Therefore, sometimes independence and neutrality of arbitrators might become an issue. While mediation is advisable when the parties are willing to seek settlement, it must be noted that there are no traditions of mediation in Latvia, and there is a lack of trained mediators. It is not unusual that a Latvian party when discussing mediation as a possible dispute resolution method might wish that there is still some element of adjudication in mediation, whereby a mediator would say a final word on what should be the solution of a dispute.

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LITHUANIA

Court System of Lithuania

BY REGINA DERKINTYTE | SORAINEN

After restoring the independence of the Republic of Lithuania on 11 March 1990, it has been realised that the national legal system also needs reform. The essential step towards a modern court system was taken on 25 October 1992 when the Constitution of the Republic of Lithuania was adopted in a Referendum. In accordance with Chapters VIII and IX of the Constitution, justice in the Republic of Lithuania shall be administered by the following courts: the Constitutional Court, courts of general competence and specialised courts.

The new Constitution has introduced a four level court system of general competence that was functioning in Lithuania before occupation: the Supreme Court of Lithuania, the Court of Appeal of Lithuania, district courts and regional courts. This system began functioning as of 1 January 1995 and remains unchanged to date.

Further significant changes were made in 1998. The reform vested the authority to hear cassation claims solely by the Supreme Court of Lithuania, instead of five regional courts, the Court of Appeal of Lithuania and the Supreme Court of Lithuania.

Another significant stage in the history of Lithuanian courts' development is considered to be the establishment of specialised administrative courts. Article 111 of the Constitution provides that specialised courts may be established for the hearing of administrative, labour, family and other related cases. On 1 May 1999 a three level system of administrative courts began to function, which comprised 5 regional administrative courts, the Higher Administrative Court and the Division of Administrative Cases in the Court of Appeal of Lithuania. After a couple of years the last two institutions were reorganised into the Supreme Administrative Court of Lithuania.

The Constitutional Court

The Constitutional Court of the Republic of Lithuania shall guarantee the supremacy of the Constitution of the Republic of Lithuania in the legal system as well as constitutional legality by deciding, according to the established procedure, whether the laws and other acts adopted by the Parliament are not in conflict with the Constitution and whether acts of the President of the Republic and the Government are not in conflict with the Constitution or laws. The Court has played a substantial role in the development of the Lithuanian legal system, declaring a number of national laws unconstitutional.

The Constitutional Court consists of 9 justices appointed for a single nine-year term. Only Lithuanian citizens of an impeccable reputation, who are trained in law, and who have served for at least 10 years in the legal profession, or in an area of legal education are eligible for appointment. Usually, notable legal scholars and highly experienced judges qualify for the position. Every three years, one-third of the Constitutional Court is reconstituted.

Courts of General Competence

District Courts

District courts are the first instance courts of general competence that hear the most cases. Currently, there are 54 district courts in Lithuania. They are the first instance for: (i) civil cases where the disputable sum amounts up to LTL 100,000 (about €28,962); (ii) criminal cases (except felonies); (iii) cases of administrative offences (assigned to its jurisdiction by law); (iv) cases assigned to the jurisdiction of mortgage judges; and (v) cases relating to the enforcement of decisions and sentences. Judges of a district court also perform the functions of a pre-trial judge, an enforcement judge, as well as other functions assigned to a district court by law.

Usually, the case is heard by one judge; however the Chairman of the court may assign a board of three judges for cases that are exceptionally difficult and complex.

District court should consist of at least two judges. The Chairman of the court performs dual functions: on one hand, he has the same judicial powers as any other judge of the district court, and, on the other hand, he is superior to all administrative personnel, such as secretaries, registrars etc., that have to ensure suitable functioning of the court.

Bearing in mind that a four level court system is mainly seen in big federal states, this system does not completely perform its functions in a small state such as Lithuania, as the courts of higher instance deal with a significantly smaller number of the cases compared to those heard by district courts.

Regional Courts

A regional court is first instance for criminal and civil cases assigned to its jurisdiction by law and appeal instance for judgments, decisions, rulings and orders of district courts.

As regards first instance for civil cases, regional courts hear disputes over LTL 100,000 (about €28,962) and cases regarding insolvency, restructuring, public procurement, copyright and other specific issues provided by laws and Code of Civil Procedures. Vilnius Regional Court has an exclusive jurisdiction to hear cases related to the Law on Trademarks and the Law on Patents.

Currently there are five regional courts functioning in five major cities of Lithuania.

The Chairman of a regional court organises and controls the administrative activities of district courts and their judges within the territory of his activities in accordance with the procedure prescribed by law.

If a dispute is brought to a regional court as a first instance, usually one judge hears the case. When the appeal is submitted, as a rule the case is heard by a board of three judges.

Rulings of regional courts may be appealed to the Court of Appeal of Lithuania, if regional court was a first instance and to the Supreme Court of Lithuania if regional court was an appeal instance for the case.

The Court of Appeal of Lithuania

Despite the fact that this court serves as an appeal instance for decisions that were adopted by regional courts as courts of first instance, the Court of Appeal of Lithuania has a specific jurisdiction: it hears requests for the recognition of decisions of foreign or international courts and foreign or international arbitration awards and their enforcement in the Republic of Lithuania, as well as performs other functions assigned to the jurisdiction of this court by law.

The Chairman of the Court of Appeal supervises and administers regional courts and their judges in accordance with the procedure prescribed by law.

Decisions of the Court of Appeal may be revised only by the Supreme Court of Lithuania.

The Supreme Court of Lithuania

The Supreme Court of Lithuania is the only court of cassation instance for reviewing effective judgements, decisions, rulings and orders of the courts of general jurisdiction.

Cassation is an extraordinary form of exercising supervision over the legitimacy of judicial decisions and it is applicable only in exceptional cases defined by the Codes of Criminal and Civil Procedure that establish the grounds for cassation; therefore, a very limited number of cases is heard by the judges of this court. As the Supreme Court hears cases exclusively on questions of law, a cassation appeal must be based not on the arguments of a factual character but only on the application and interpretation of law. In order to decrease the number of ungrounded claims, the special Reception Office is assigned in order to decide the admissibility of the cassation.

After amendments of Law on Courts were adopted in 1998, the Supreme Court of Lithuania has been assigned as the only court that hears cases under cassation procedure. This implies a certain duty to this court: the objective of the Supreme Court, as a court of cassation, is to ensure uniform court practice of courts of general jurisdiction in the state by means of precedents formulated in the cassation rulings. Moreover, the Supreme Court not only summarises and revises the practice of the courts, it also consults the judges of the lower instance courts on general matters.

Another important function of the Supreme Court is its participation in deciding on disputes over jurisdiction between the courts of general jurisdiction and the administrative courts.

The Supreme Court of Lithuania consists of 37 judges – the President of the Court, Chairmen of the Criminal and Civil Divisions and judges in both Divisions.

Cases before the Supreme Court are normally heard by a panel of three judges. In the instances where a cassation case involves a complicated issue of interpretation or application of laws, the President of the Supreme Court, the Chairman of the relevant Division, or a panel of judges may forward the case to be heard by an extended panel of seven judges or by a plenary session of the relevant Division.

Administrative Courts

Regional Administrative Courts

A regional administrative court is the court of special jurisdiction established for hearing complaints (petitions) in respect of administrative acts or omission by entities of public and internal administration.

Regional administrative courts hear disputes in the field of public administration, deal with issues relating to the lawfulness of regulatory administrative acts, tax disputes, etc.

Pre-trial procedure may be followed before applying to an administrative court. In this case disputes regarding individual legal acts or actions taken by entities of public administration are investigated by municipal public administrative dispute commissions, district administrative dispute commissions and the Chief Administrative Dispute Commission.

Currently there are 5 regional Administrative courts in Lithuania.

Supreme Administrative Court

The Supreme Administrative Court is first and final instance for administrative cases assigned to its jurisdiction by law. It is an appeal instance for cases concerning decisions, rulings and orders of regional administrative courts, as well as for cases involving administrative offences from decisions of district courts. The Supreme Administrative Court is also instance for hearing, in cases specified by law, of petitions on the reopening of completed administrative cases, including cases of administrative offences.

The Supreme Administrative Court develops a uniform practice of administrative courts in the interpretation and application of laws and other legal acts.

National Courts Administration

Since 1st May 2002 a new institution that is independent from the executive authorities – the National Courts Administration – has been established in order to ensure the efficiency of the court system, its governance and organisation of work as well as independence of judges.

The main activities of the National Courts Administration are to secure courts' organisational autonomy, to ensure the close interrelations among courts and institutions of self-governance of courts, to contribute to the fluent formation of the judiciary, to organise a centralised system of material-technical supply to courts; to implement the strategy of common court information system, etc.

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The Interim Measures in Lithuanian Judicial Civil Proceedings

BY DAINIUS CICELIS | SORAINEN

In order to protect violated rights, every person has the right to seek judicial protection. This subjective right is ensured in both the European Convention on Human Rights and Fundamental Freedoms and in local legal acts of Lithuania: the Constitution, the Code of Civil Proceedings. However, it is not enough to have a subjective right that a court formally stipulates. Article 5 of the Code of Civil Proceedings of the Republic of Lithuania (the "Code") defines that any interested person is entitled to apply to court for the protection of his/her subjective right or interest that is damaged or disputed. Thus, the main purpose of the judicial (civil) procedure is to ensure real protection of person's subjective rights, and not just to have them formally stated by court decision.

With this end in view, the Lithuanian legislative deeds establish certain ways to achieve these objectives. One of these ways is application of measures ensuring execution of future court decisions. According to the Code this institute is called "interim measures". The main purpose of this institute is to ensure that the court's decision to be taken in the examination of civil case will actually be enforced. Additionally, interim measures secure evidences and also impact on the debtor (defendant) in a preventive way, by forbidding him/her to perform certain actions. Absence of such measures may give rise to a situation where the debtor (defendant) after becoming aware of the

civil proceedings initiated against him/her may intentionally transfer his/her property to third parties whereupon the recovery of such property may become impossible as third party is to be treated as fair owner of property. In order to avoid this situation, the creditor (the plaintiff) is given the opportunity to ask the court to apply certain procedural injunctions called interim measures to the debtor by limiting his/her entitlement to dispose of his/her property etc.

Types of Interim Measures and Principles of Application

The existing Code provides a wide range of interim measures, which can be used as single ones or in combination, applying a few of them at once. The most frequently used interim measures are as follows: (i) arrest of defendant's real estate; (ii) arrest of movable property, including money or property rights held by the defendant or to third parties; (iii) injunction against participation in certain transactions or taking certain steps; (iv) ban on other individuals to transfer assets or to pursue other obligations to the defendant; and (v) the obligation to take steps to prevent damage. Some interim measures are applied quite rarely, e.g., a ban on the defendant to leave their domicile, detention of defendant's property and administration of defendant's property. In addition, some special laws may permit other interim measures to be applied. For example, copyright protection cases may be subject to the interim measures provided for in the Law on Copyright and Related Rights of the Republic of Lithuania. Thus, such interim measures as a ban on distributing illegal copies of intellectual property may be applied.

Applicants are certainly free to choose on their own what kind of interim measure they may require when requesting the court to apply interim measures to the defendant. However, the court applying interim measures must conform to certain principles and rules established in the legislation. For instance, the court may impose interim measures on an amount that is not substantially bigger than the amount of a claim, e.g., the court cannot seize account capital exceeding the amount of a claim. The second principle is that the interim measures should be selected in a cost effective manner. This means that application of interim measures should not disturb the normal person's activity and this is especially pertinent to legal entities. Furthermore, it should be emphasised that if the final result of a case is negative (i.e., claim is dismissed), the defendant has the right to seek recovery of damages caused by the application of interim measures requested by the plaintiff. This opportunity is also provided for in the Code.

Moreover, the defendant is entitled to ask the court to oblige the plaintiff to put down a deposit on the defendant's losses, if any, ensuing due to the interim measures applied. Sometimes the court requires providing a bank guarantee issued in favour of the defendant instead of putting down a deposit. Those remedies should prevent the plaintiff from a potential procedural rights abuse, especially when the claim filed to the court obviously has no substance.

The arrest of a defendant's assets listed in the public registries (i.e., real estate, movable assets such as automobiles and the like) entails limitation on the owner's rights to dispose of that property, and this must be recorded in public registries – the Real Estate Register (supervised by the state enterprise REGISTRŲ CENTRAS), the Motor Vehicle Register (supervised by the state enterprise REGITRA).

Usually, interim measures are applied after the initiation of civil proceedings, i.e., as soon as the court receives a claim, case-related documents, and plaintiff's application for applying interim measures.

However, in some cases there may be situations that require taking immediate steps to secure future claim and its objectives. In such cases the Code allows applying interim measures prior to lodging a claim and opening

a case. The person requesting interim measures must, before filing a claim to court, indicate the reasons why the action was not filed immediately and motivate if such a matter of urgency for applying interim measures exists; he/she should also substantiate his/her request with underlying evidence. In addition, a person must pay half of the stamp duty for the filing of the claim. If a dispute is related to assets, standard stamp duty in civil proceedings is up to 3 percent from the claim amount, however it may vary (decrease) in some cases and that depends on the amount of claim and the chosen procedure. Finally, in case the court applies interim measures before starting the case procedures, the applicant has to submit a claim to the court within 14 calendar days. Otherwise, the court may cancel the interim measures applied earlier.

It should be noted that court may apply interim measures not only where the dispute is pending in court, but also for disputes pending in arbitration. This opportunity is provided by the Law on Commercial Arbitration of the Republic of Lithuania. The court of the Republic of Lithuania may apply interim measures before the beginning of arbitration proceedings or in the course of the arbitration process. The plaintiff's request in such case should be submitted to the district court according to the defendant's (the debtor's) domicile, unless the parties to the arbitration agreement decide otherwise. The interim measures established by foreign arbitration can also be enacted in the Republic of Lithuania but such a ruling must be admitted by the Lithuanian Court of Appeal, and it is allowed to run in accordance with analogy of Article 817 of the Code and Articles 12 and 20 of the Law on Commercial Arbitration. However, it must be acknowledged that similar precedents are sufficiently rare in the Lithuanian case law, since a practice to settle disputes by arbitration in Lithuania is not yet widespread.

The Procedure for Application of Interim Measures

A person seeking interim measures from court usually has to provide the court with separate application for interim measures or this application may be included in a claim. Article 144 of the Code clearly states that in the absence of such a request the court may impose interim measures on its own initiative only in exceptional cases, i.e., only if it is necessary to protect the public interest. Article 148 of the Code clearly states that application for interim measures has to be resolved by the court within 3 calendar days as from the date of receipt of the request by the court. The question whether this time limit is reasonable may be discussed. In our point of view, such a term for evaluation of situation, analysis of documents provided as well as for drafting of the court ruling is too short. Reality shows that due to quite objective reasons this term is a bit longer (especially taking into account that the days-off are also included in the term, which is quite illogical). In deciding whether to impose interim measures such requests must be communicated to the defendant, but in reality most often the issue is resolved without notifying the defendant. Of course, the question may arise whether those proceedings are in accordance with the principle *audiatur et altera pars* (i.e., hear the other side). However, another – the balance of interests – principle must be followed as well. In many cases, when a person applies to the court, he/she intends to have the violated rights protected and recovered. Therefore, we suppose that it would be unfair and wrong against the applicant to give the law breaker additional time limits for encumbering execution of a future court decision.

According to Article 145 of the Code, the application of interim measures is subject to appropriate court ruling, which must be reasoned. The defendant is given an opportunity to appeal against this ruling. Basically, the court must specify the basis allowing it to apply interim measures. Currently, the case law of Lithuania specifies that court is not required to have the proof that threats for the future execution of court decision exists at the moment of issuing the interim measure related ruling. In fact, a likelihood of risk is a sufficient ground for applying interim

measures (see the ruling of Lithuanian Court of Appeal issued on 19 November 2009 (case No 2-1320/2009), the rulings of same court issued on 12 November 2009 (case No 2-1321/2009), on 24 April 2009 (case No 2-304/2008). Thus, the plaintiff does not really need to prove that a threat of judicial decision necessarily appears in the performance, it is sufficient to determine the likelihood of such an event. The prevailing case law in Lithuania is currently presuming that a large amount of claim increases the likelihood of any risk that the court's decision cannot be executed or its execution can be encumbered. The law does not define the amount which is considered as significant, so this criterion is subjective in nature and depends largely on the court (judge's) estimation. Of course, the presumption mentioned above is not absolute. The court should evaluate both the documents submitted and the related circumstances, and decide whether, in light of the defendant's financial resources, it must be concluded that the amount of claim is high and may cause difficulties in fulfilling the potential court decision. If the evidence proves that the value of the assets, revenues available for capital and the other property of the defendant are sufficient and the amount of the claim is relatively small, it denies the existence of the presumption mentioned above and the objective threat for execution of future decision.

The court ruling regarding the interim measures comes into force after its adoption. However, the defendant may appeal against this ruling to a higher court within 7 calendar days. It should be noted also that the appeal against ruling does not suspend execution of the ruling as the execution of such ruling is urgent. The court ruling regarding the interim measures is physically enforced by the state empowered person – a bailiff. A bailiff usually locates and describes the debtor's property, evaluates it, as well as appoints a person responsible for the safety of the property and the like.

The interim measures applied by the court are valid until the court decision is adopted and executed in full amount (where the claim is satisfactory). If the claim is dismissed, interim measures should be cancelled after the effective date of a respective court decision.

In summary, it should be emphasised that the importance of interim measures should not be undervalued as they are one of the most significant remedies to ensure execution of the court decision in reality.

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Simplified and Accelerated Procedures in Lithuanian Code of Civil Procedure

BY LAURA CEREŠKAITE-KINCIUVIENE | SORAINEN

For many people, litigation is associated with a long, difficult and expensive procedure during which the court follows a whole set of rules. These rules are designed to ensure that each party has equal opportunities to present its case to the court and to make sure that the judge applies the principle of a fair trial in his decisions.

Lithuania, as in most EU member states, has, however, introduced simplified and accelerated procedures in which these rules are relaxed. There are three main ways of resolving disputes in a simplified procedure according

to the Lithuanian civil process law:

- firstly, when the claim is not contested by the defendant – the so-called "Order for payment" or "Court order" procedure;
- secondly, when the value of the claim is below a certain threshold – so-called "Small Claims" procedure; and
- thirdly, when the claim is based on written evidence – so called "Documentary procedure".

The simplification of rules in the simplified proceedings concern all phases of a procedure, e.g., the rules which lay down the form by which a claim can be introduced, or on whether or not you need to employ a lawyer. Also rules concerning the time frame in which the parties can present their arguments, concerning the necessity of a hearing or on how evidence is to be taken are simplified. This is also the case for rules with respect to the question of the litigation costs, and of whether there is a possibility to appeal against the judgment.

The obstacles to obtaining a fast and inexpensive judgment are exacerbated in cross-border cases. This has been followed at the European level by Regulation (EC) No 861/2007 of the European Parliament and of the Council of 11 July 2007 establishing a European Small Claims Procedure. This gives citizens and businesses all over Europe a speedy and affordable civil procedure for claims of under €2,000, which is uniform in all EU member states and in all procedural steps from the commencement of the procedure to the final enforcement of the judgement.

The objective of such a procedure is to facilitate access to justice. The distortion of competition within the internal market due to imbalances with regard to the functioning of the procedural means afforded to creditors in different EU member states entailed the need for legislation that guarantees a level playing-field for creditors and debtors throughout the European Union.

Court Order Procedure

The court order proceedure is the most simple, fast and inexpensive procedure in Lithuanian civil process law. Usualy it is to be used in order to collect debts. The stamp duty payable for application for court order equals one-quarter of the amount payable for the lawsuit in ordinary court proceedings. When the debtor presents objections to the court order, the creditor may defend his rights according to the rules of documentary proceedings or ordinary court proceedings. However in this case the creditor must pay the deficient part of the stamp duty. The amount of the stamp duty in the ordinary court proceedings will differ depending on the amount of the claim and is calculated in the manner established by laws but in no case will exceed LTL 39,000. If the creditor does not file a lawsuit after the debtors objection, the stamp duty paid during filing the application for a court order is not refunded.

Creditors should present the model form application to the court. The creditor is entitled to request the court to apply interim measures for securing the claim. Following such a request, the court may pass a ruling regarding the interim measures for securing the claim only if the non-application of these measures would make the enforcement of a future court judgment impossible or more difficult.

The court issues the court order and only then informs the debtor about the case, inviting him to present objections to the court order within 20 days from the notification of the case. The debtor's objections to the court order may be motiveless. If the debtor presents objections to the court order, the court order does not come into force. In this case the creditor may defend his rights according to the rules of documentary proceedings or ordinary court proceedings. The court order also does not come into force if the court fails to serve it upon the debtor.

Should the debtor not present the objections to the court order, the court order becomes final and enforceable. In this case neither appeals, nor the cassation appeals may be presented.

The creditor may apply for the court order only if:

- the subject of a dispute is connected with pecuniary claims (in labour cases only disputes regarding indemnification for loss may be resolved under this procedure) or adjudgement of movable property; and
- the debtor resides in Lithuania or the registered office of the debtor is situated in Lithuania and the place of residence of the debtor is known.

Small Claims Procedure

The small claims proceedings applies when the value of the claim is below LTL 1,000. In this procedure the court has a right to decide at its own discretion what procedure is to be applied in the case. The case shall be examined in the verbal court hearing in exceptional cases on one of the parties' request.

Documentary Procedure

Documentary procedure lies between court order procedure and ordinary court proceedings. The plaintiff should present the lawsuit for the issuance of the preliminary decision to the court. The court adopts the preliminary decision and only then informs the defendant about the case. The defendant may present objections to the preliminary decision within 20 days from the notification of the case. The defendant's objections to the preliminary decision should be reasoned. If the defendant presents the objections to the preliminary decision, the dispute shall be resolved on its merits. If the defendant does not present the objections to the preliminary court decision, the preliminary court decision becomes final. In this case neither appeals, nor the cassation appeals, may be presented.

The person may protect his rights in documentary proceedings only if:

- the subject of a dispute is connected with pecuniary claims (in labour cases only disputes regarding indemnification for loss may be resolved under this procedure), adjudgement of movable property or securities, or claims arising from agreements on lease of real property in connection with eviction of tenants;
- all claims are based on written evidence; and
- the defendant resides in Lithuania or the registered office of the defendant is situated in Lithuania.

In documentary proceedings it is not allowed to change the subject or ground of a lawsuit, to increase the amount of the claim or present the counterclaim.

The stamp duty payable for a lawsuit filed according to the rules of documentary proceedings equals half the amount payable for a lawsuit in ordinary court proceedings. Even if the defendant presents the objections to the preliminary decision, the plaintiff does not have to pay the deficient part of the stamp duty.

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Arbitration in Lithuania and Proceedings in the Vilnius Court of Commercial Arbitration

BY RENATA BERZANSKIENE | SORAINEN

Arbitration has good potential to progress as an attractive alternative means of dispute resolution for businesses, given the optimal cost of arbitration, rising awareness of arbitration, and efforts from arbitration enthusiasts and the VCCA. Lithuanian businesses are not presently used to solving commercial disputes by way of arbitration. In 2008, fewer than thirty commercial arbitration cases were solved in the Vilnius Court of Commercial Arbitration. This number may be regarded as minimal in comparison to over 100,000 civil cases per year that are dealt with by state courts.

As for commercial arbitration in Lithuania, practically everything centres on one institution: the Vilnius Court of Commercial Arbitration (the VCCA). It was founded in 2003 by merging the two main Lithuanian arbitration institutions which had operated before, namely the Arbitration Court at the International Chamber of Commerce Lithuania (established in 1997) and the Vilnius International Commercial Arbitration (established in 1996). This merger resulted in a concentration of knowledge and skills related to commercial arbitration in "one place", and the results are excellent.

It should be noted that the founders and the main stakeholders of the VCCA are the most prominent business associations of Lithuania: the Association of International Chamber of Commerce Lithuania (ICC Lithuania), the Association of Lithuanian Banks, the Lithuanian National Road Carriers' Association LINAVA, the Association of Lithuanian Chambers of Commerce, Industry and Crafts, the Lithuanian Confederation of Industrialists, and the Association INFOBALT, the Lithuanian Lawyers' Association. Such a make-up of authoritative stakeholders is believed to promote reliability and quality of service. Moreover, it most probably adds up to quite stable statistical results, in terms of the number of arbitrations per year.

There are three other institutions that come forward with arbitration in Lithuania, but they are not officially incorporated as "permanent arbitration institutions" in accordance with the Law on Commercial Arbitration of the Republic of Lithuania and there is no official information on their practice. *Ad hoc* arbitrations also emerge from time to time but those are rare. When considering whether to choose an *ad hoc* or institutional arbitration, one should note that *ad hoc* arbitration might prove to be effective only where an agreement on all the issues concerning the whole mechanism of arbitration between the parties exists. However, it is very difficult to reach such agreement in cases where a dispute has already arisen. Therefore, *ad hoc* arbitration is advisable only in exceptional cases.

Currently, arbitration in Lithuania is undergoing a surge in popularity. This conclusion takes into account the following statistics: 20 cases were initiated in 2008, whereas 39 cases were initiated in 2009; 14 cases were completed in 2008 and 26 cases in 2009. Such growth in the number of arbitrations could be explained by the fact that more and more obstacles for efficient litigation arise in Lithuania and with better awareness of arbitration.

The major problem with litigation in Lithuania is that courts are overloaded. According to the unofficial statistics one judge in Vilnius Regional Court *(Vilniaus apygardos teismas)* has a load of approximately 400-500 hundred cases to be heard as first instance and a load of approximately 100 cases to be heard as second instance per year. Enormous overload causes many problems and concerns of case hearing quality, as judges do not have

enough time to prepare for the case hearings and usually do so only during the preparatory hearings.

Furthermore, insolvency cases and other cases requiring special knowledge are usually heard by judges without adequate knowledge and qualification. This situation is a result of introducing a computerised system in Lithuanian courts.

Another noticeable development concerning litigation in Lithuania is the lengthy time of litigation. Although it might take 2-3 years to litigate a case through all the three instances, official statistics shows that only about 6 percent of all cases at courts of first instance are tried for much longer than 6 months.

Questions of Law

As for the legal environment of commercial arbitration, Lithuania adopted the Law on Commercial Arbitration more than a decade ago, in 1996. It is based on UNCITRAL Model Law on International Commercial Arbitration (1985) (the "Model Law"). The Model Law provisions apply to international as well as national arbitration. Soon the Law on Commercial Arbitration will be changed substantially and the draft of the new law prepared by arbitrators, VCCA and the Ministry of Justice is already presented to the Ministry of Justice for further adoption.

In accordance with the Code of Civil Procedure (Para. 2-6 Art. 137), a valid arbitration agreement precludes from bringing the dispute to state court if the defendant objects. If the defendant does not object, the case is heard in the state court. Such an objection should be expressed in the first response to the claim or earlier if the court asks the defendant to present an opinion on the question.

An arbitral award becomes effective and may be enforced after its adoption. No cases may be initiated in state courts on the same grounds after they were dealt with in the arbitral award.

Arbitral awards are enforced according to the same rules as judgments of state courts. For the enforcement, a writ of execution is needed. In national arbitration cases the execution writ is to be issued, on the request of a party, by the state court located in the same place as the arbitral tribunal. A ruling in which the court issues or refuses to issue a writ of execution may be appealed against to the regional court. In addition, the recourse (cassation appeal) to the Supreme Court of Lithuania is possible.

Applications for the setting aside of an arbitral award may be filed on the same grounds that are provided for by the UNCITRAL Model Law (Para. 2 Art. 34). Such applications should be presented to the Court of Appeal of Lithuania. A decision of this court is also subject to cassation appeal to the Supreme Court of Lithuania.

Such wide facilities to challenge arbitral awards attract criticism. Diminishing a possible number of recourses against arbitral awards may well constitute a trend towards possible future legislation reform.

Lithuania is a party to the 1958 New York Convention on Recognition and Enforcement of Foreign Arbitral Awards. By ratifying this convention Lithuania made a declaration that it would also recognise foreign arbitral awards adopted in the non-member states of the Convention on the grounds of reciprocity. This provides for easy recognition of international commercial arbitration awards adopted abroad.

A request for the recognition and permission to enforce a foreign arbitral award is heard by the Court of Appeal of Lithuania. They give time for the defendant to present an opposition. Oral hearing is arranged, but non-appearance of one of the parties or both does not preclude the court from deciding the matter. On average, it takes several months from the lodging of the application to ruling the decision of the Court of Appeal of Lithuania. This decision is subject to recourse (cassation) to the Supreme Court of Lithuania one month after its adoption. In general the Supreme Court of Lithuania decides a matter in half a year.

To the extent a foreign award is recognised and allowed to be enforced, the Court of Appeal of Lithuania issues a writ of execution upon the request of an interested party. The law does not provide for a possibility to appeal against the decision to issue a writ of execution in case of a foreign arbitral award, which was officially recognised and allowed to be enforced in Lithuania.

Below are the main steps for arbitration according to the Rules of the VCCA.

Filing the Claim

If the Claimant wishes to have recourse to arbitration, the arbitration proceedings can be initiated by filing a claim with the VCCA and paying the registration fee.

If the claim amount is, for example, €700,000, an arbitration fee will be approximately €20,000. The arbitration fee is paid in equal parts by both parties. If the Claimant refuses to pay its part of the arbitration fee, the Defendant will be obliged to do it. The prevailing party's arbitration costs may be covered by the losing party, yet this should be indicated in the arbitral award and in fact it is a quite common practice.

The arbitration proceedings are deemed to commence when the claim complying with the requirements is filed with the VCCA, unless the parties agree otherwise. The claim should contain detailed contact information of the parties and their representatives as well as references to the disputed agreement and agreement of parties to settle it via arbitration process.

Language of the Proceedings

Generally the language of the proceedings is indicated in the arbitration clause. It depends on a particular situation but the majority of cases in the VCCA are solved in the Lithuanian and English languages. Most arbitrators are Lithuanian nationals and an arbitration process in the local language is more acceptable to them. The award is also rendered in Lithuanian, yet it may be translated. Moreover, assuming that representatives of the parties will also be Lithuanian nationals, the Lithuanian language would be the most preferable to all. Finally, the process of enforcing the award will take place in Lithuania, thus having the proceedings and award in Lithuanian will make execution more convenient and efficient. However, if parties opt for the English language, the VCCA and the arbitrators will be happy to work in this language.

Number of Arbitrators

In the majority of cases the arbitral clause provides that the Arbitral Tribunal will consist of three arbitrators. In the arbitration with three arbitrators each party appoints one arbitrator within a fixed period of 30 calendar days and the two thus appointed arbitrators, not later than within 10 calendar days, appoint the third arbitrator who will preside over the Arbitral Tribunal and act as the presiding arbitrator. If the parties make a request, the VCCA sends them a list of arbitrators approved by the VCCA, but the parties retain the right to select arbitrators who are not included in that list.

Each Party is entitled to appoint one arbitrator, who will then jointly appoint the presiding arbitrator.

Arbiters are appointed by the Chairman of the VCAA in the following cases:

- if a party fails to appoint the arbitrator within a fixed period of 30 calendar days;
- if the two arbitrators appointed by the parties to the dispute fail to agree on the third arbitrator within 10 calendar days from the date of appointment of the last arbitrator.

The Chairman of the VCCA appoints an arbitrator from the list of arbitrators and such decision is final and cannot be appealed. The best situation in these cases (as in all others) is when two arbitrators manage to agree on the presiding arbitrator.

Interim Measures

It is advisable to request application of interim measures (arrest of immovable property and if its value is not sufficient, then the bank accounts, etc.) otherwise it might be difficult to enforce the award, if the sums claimed are high and/or the financial stability of the defendant is doubtful. Under such circumstances the application should be submitted to Vilnius Regional Court, if the value of the claim is more than €33,000 (LTL 100,000) and the defendant is located in Vilnius. It is recommended to submit the application after the arbitration proceedings have commenced, i.e., the claim is already filed to the VCCA.

After receiving such request, the court within three calendar days (in practice it takes one to two weeks) passes out a ruling whether to apply interim measures. The ruling is subject to appeal at the Appeal Court.

Hearings

A party to the dispute or the Arbitral Tribunal may call for a preliminary hearing. A preliminary hearing resolves the issues that were not agreed on by the parties in their arbitration clause: procedures and time limits for the exchange of documents, kinds of evidence and the procedure for their collection, the date, time, place, call witnesses and rules of the procedure governing the main hearing, clarification of the claims and reply to the claim.

The main hearing is audio recorded and a statement of the hearing is drawn up. Every party to the dispute may familiarise with the contents of the statement and receive its copy.

Arbitral Award

The Arbitral Tribunal must substantively resolve the dispute by rendering an award not later than within a period of 6 months after the case is transmitted to the Arbitral Tribunal. In exceptional cases this period may be prolonged. The final award is made within as short a time as possible after the main hearing is held but no longer than 20 calendar days after the last main hearing.

Before signing the final award, the Arbitral Tribunal must submit it in a draft form to the VCCA in order for it to assess whether the award complies with the formal requirements of the VCCA. After receiving the draft award, the VCCA submits its assessment within a period not exceeding 10 days. As it was written above, the arbitral award is binding on the parties and has the same judicial power as a judgment of a court; therefore it will be brought to action with the same legal means.

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ASIA PACIFIC

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AUSTRALIA

Legal Privilege

BY NORMAN LUCAS | CLAYTON UTZ

Legal privilege is a right to maintain confidences. In general, it protects certain oral or written confidential communications that have passed between a client and his or her legal advisers from compulsory disclosure (Note that helpful statements about the general principles of legal professional privilege can be found in *In the matter of Southland Coal Pty Ltd (rec & mgrs apptd)(in liq)* [2006] NSWSC 899 at [14] and in *AWB Limited v Honourable Terence Rhoderic Hudson Cole (No 5)* [2006] FCA 1234 at [44]).

At common law, legal privilege is known as "legal professional privilege". When the uniform *Evidence Acts* were introduced in 1995 in Federal jurisdictions and certain States, including NSW, privilege was renamed "client legal privilege". This emphasises that privilege belongs to the client, not the legal profession.

This has, however, created a situation where two sets of laws operate in the area of privilege in *Evidence Act* jurisdictions. In broad terms, the uniform Evidence Acts govern privilege issues on occasions when evidence is adduced at trial, while the common law governs questions concerning privilege which arise pre-trial, except to the extent otherwise provided by statute or rules of court.

Rationale for Legal Privilege

The rationale for privilege is to promote the better administration of justice by:

- encouraging freedom of consultation between clients and their legal advisers and full disclosure to the adviser of the relevant circumstances; and
- encouraging the production of information for the purposes of litigation.

Evidence Act

Sections 118 and 119 of the *Evidence Act* create a privilege for confidential communications made, and prepared, for the dominant purpose of a lawyer providing legal advice or legal services relating to actual or anticipated litigation.

The "purpose" referred to in sections 118 and 119 is the purpose which led to the making of the communication or the preparation of the document.

Common Law

Elements of the Privilege

There are three elements necessary to establish legal professional privilege over communications passing between

legal adviser and client:

- The communications must pass between the client and the client's legal adviser;
- The communications must be made for the dominant purpose of enabling the client to obtain legal advice, or for the purpose of actual or contemplated litigation; and
- The communications must be confidential.
- It is the actual *communication* that is privileged from disclosure.

Dominant Purpose Test

The High Court adopted the dominant purpose test for common law privilege in *Esso Australia Resources Ltd v Commissioner of Taxation (Cth)* (1999) (201 CLR 49; as expressed by Barwick CJ in *Grant v Downs* (1976) 135 CLR 674 at 677) as distinct from the sole purpose test.

The purpose, or intended use, for which a document is brought into existence is a question of fact: *Singapore Airlines v Sydney Airports Corporation & Anor* [2004] NSWSC 380 (7 May 2004), upheld on appeal in [2005] NSWCA 47 (9 March 2005); *Waterford v The Commonwealth* (1987) 163 CLR 54 at 66. The "dominant" purpose is the paramount purpose: *Mitsubishi Electric Australia Pty Ltd v Victorian Workcover Authority* (2002) 4 VR 332, 336-337 [10], Batt JA. Where there are competing purposes, it is a question of fact whether in any case any one purpose "dominated": *Sparnon v Apand Pty Ltd*. (1996) 68 FCR 322, 327-328, Branson J. If two purposes were of equal weight, one would not dominate the other: *Sparnon; AWB v Cole* [2006] FCA 571 at [118]. In practical terms, it will often be a matter of instructions from the client to ascertain the "purpose" for which a document was brought into existence.

Ordinarily the relevant purpose is the purpose of the person who creates the document embodying the relevant communication. In the case of a corporation, the relevant purpose is that of the corporation regardless of the particular employee or employees through whom it was articulated. Ordinarily, the corporation's purpose or purposes may be gathered from the individual purposes of particular employees acting within the scope of their authority: *Singapore Airlines v Sydney Airports Corporation & Anor* [2004] NSWSC 380 (7 May 2004).

Where a communication is not made or prepared for the dominant purpose of providing "professional legal services" relating to legal proceedings, the privilege does not apply. For example, there will be no privilege if a communication is with a lawyer acting in a non-legal capacity (that is, an accountant, a company director or a friend, where "legal advice" is not being provided).

Similarly, there is recent NSW Court of Appeal authority for the proposition that a solicitor's response to an audit request letter does not attract legal professional privilege because it is not prepared for the dominant purpose of the client being provided with professional legal services (*Westpac Banking Corporation v 789Ten* (2005) 55 ACSR 519).

In the Federal Court case of *Hoy Mobile Phones Ltd v Allphones Retail Pty Ltd* [2007] FCA 933 (21/6/07), Tamberlin J held that documents were privileged despite being created for dual legal and commercial purposes. The plaintiff claimed that the documents, created during a period when the parties were trying to resolve their dispute through mediation, were created for non-privileged purposes such as investigating facts to formulate a business strategy for dealing with the parties ongoing commercial relationship. Tamberlin J stated that taking steps to mediate a dispute did not mean that the dominant purpose of records created was

not seeking legal advice or assistance or for use in reasonably anticipated litigation. He noted that parties may seek to negotiate a resolution while at the same time contemplating and preparing for litigation.

In House Counsel

How do these principles relate to in-house lawyers?

General Principles

Oral or written confidential communications between in-house counsel and their employer should be protected by legal professional privilege provided the communications meet the following requirements:

- they are made for the dominant purpose of giving or receiving legal advice or of conducting actual or anticipated litigation;
- the professional relationship of lawyer and client is maintained between counsel and the employer, ensuring independent advice; and
- counsel is qualified and entitled to practise law, and is subject to the duty to observe professional standards and the liability to professional discipline (See the High Court decision of *Waterford v Commonwealth* (1987) 163 CLR 54, a case which involved in-house counsel in a government department. See also the recent decisions in *Vance v McCormack* (2004) 154 ACTR 12 (first instance – Crispin J.) and [2005] ACTCA 35 (Court of Appeal), *Australian Hospital Care Pty Ltd v Duggan* [1999] VSC 131, and *Southern Equities v Arthur Andersen* [2001] SASC 398).

For legal professional privilege to apply to communications made by in-house counsel, counsel should be acting in a professional or legal capacity and the advice should be of a legal nature (In *Waterford v Commonwealth* (1987) 163 CLR 54, for example, parts of documents which dealt with policy advice given by in-house counsel were released because those parts were held to be outside the scope of LPP). There are conflicting views on whether counsel *must* also hold a current practising certificate, but on any view it remains a very relevant factor in determining whether privilege exists (In *Vance,* for example, Crispin J. held at first instance that a practising certificate was essential. This decision was reversed in the Court of Appeal. In Queensland, the effect of holding a current practising certificate is detailed in the *Legal Profession Act 2007,* which states that in-house government lawyers do not require a current practising certificate so long as they are engaged in government legal work (s44) (See also definitions in s12). Corporate in-house counsel will be required to hold a practising certificate, in order to avoid breaching section 24 of the Act). Where the *Evidence Act* applies, the recently expanded definition of "lawyer" in section 117 indirectly clarifies that it is not strictly necessary for a practising certificate to be held (by linking that term to "Australian lawyer", which requires admission).

In one formulation, the court suggested that in-house lawyers should be: "...persons who, in addition to any academic or other practical qualifications, [are] listed on a roll of current practitioners, [hold] a current practising certificate, or [work] under the supervision of such person" (See *Waterford v Commonwealth* (1987) 163 CLR 54).

The requirement of independence means that the advice provided by in-house counsel must not be influenced by their loyalties or duties to their employer (Emilios Kyrou, "Legal professional privilege for general counsel wearing two hats", (June 2000) 42 *Law Society Journal* 42).

Privilege and General Counsel with Dual Roles

There is a recent trend of appointing in-house counsel of public companies to dual roles. For example, general counsel may also occupy the role of company secretary, senior manager or director.

It is important to note that even if the job title suggests that the person is solely a legal adviser, this is not, of itself, conclusive (See *Southern Equities*).

Since legal professional privilege only protects communications made by a lawyer while acting in the capacity as lawyer, a general counsel wearing "two hats" must be careful when signing off on internal communications that are intended to be protected by legal professional privilege (Emilios Kyrou, op.cit.). Also, when giving advice, general counsel must be independent of their company (Ibid). Failing to observe these two requirements may prevent sensitive documents from being protected by legal professional privilege (Ibid).

A claim for legal professional privilege over a document prepared by general counsel who wears two hats may suffer challenges on two main bases:

- that the document was prepared by counsel in a management capacity rather than a legal capacity; or
- that general counsel is not truly independent of the employer (Ibid. See also *Southern Equities*).

In-house counsel and their employers will be more susceptible to challenges relating to independence if:

- general counsel is also a director of the company;
- general counsel's remuneration is linked to the performance of the business; or
- general counsel owns shares in the company (Ibid).

An important decision, underscoring the need for careful consideration of the contents of the documents in question, is *Seven Network Limited v News Limited* [2005] FCA 142. In that case, Tamberlin J, *inter alia*:

- refused a claim for privilege in respect of a document prepared by a lawyer (the Chief General Counsel of News Ltd), marked "privileged and confidential", and recording the contents of a meeting between the internal lawyer and their external lawyers. He held it did not satisfy the dominant purpose test;
- refused a claim for privilege in respect of a draft report (prepared by the internal lawyer), commenting on a letter from the other side, and marked "Privileged – prepared for the purpose of obtaining legal advice in relation to threatened legal proceedings". In the Judge's view, the content of the document was a summary of a commercial position and not within a legal context such as to attract privilege.

Conversely, Sundberg J in *Rio Tinto Ltd v Commissioner of Taxation* [2006] FCA 1200, allowed a claim for privilege in relation to certain documents evidencing communications between in-house counsel and the chairman of the board. Although it was accepted that a "corporate governance" purpose was found to attach to the communications, Sundberg J held (at [39]) that this was "not the dominant purpose of the communications...but rather...the context in which the legal advice was given". Moreover, the documents related to "certain pro forma matters to be attended to by the board" for particular purposes including to enter a specific legal transaction. Sundberg J concluded that though these documents were not formal legal opinions, they could constitute legal advice (at [39]).

Conclusion

Privilege will generally apply to the work product of in-house lawyers. However, the more varied nature of the work performed by in-house lawyers as compared to external lawyers necessarily provides more scope for such privilege claims to be challenged. In-house counsel must ensure they are independent of their employer and be alive to the capacity in which they are acting when undertaking their functions.

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Social Networking, Social Death? Managing Your Business' and Staff's Reputation in a Web 2.0 World

BY NORMAN LUCAS, TOBY MULLEN AND SHOMAICE ZOWGHI | CLAYTON UTZ

Social networking sites and other user-driven Web 2.0 sites can bring out the best and worst in people, especially those who have an axe to grind. Being clear about acceptable online behaviour by staff, and being proactive, can minimise the risks.

Why Your Online Reputation is Important

In recent years there has been a dramatic rise in the use of social networking sites (e.g., Facebook, Myspace and Twitter) and other user generated Web 2.0 sites (eg. blogs, forums and Wikipedia, or any site which allows its users to interact with other users or to change website content, in contrast to non-interactive websites where users are limited to the passive viewing of information that is provided to them) by Australians. For example, between May 2007 and October 2009, the number of Australian Facebook users reportedly grew from a few thousand to around 8.1 million. Some of the statistics are simply amazing – in October 2009, Facebook, YouTube and Wikipedia had unique Australian audiences of 8.1 million, 5.8 million and 5.2 million respectively, and Facebook alone now accounts for a staggering 29% of all time spent online by Australians, according to the Sydney Morning Herald citing Neilson NetView.

This explosion of social networking and other Web 2.0 sites has changed the way the internet is used. What was once a passive tool, used to view or download information posted by others, is now an interactive forum where anyone with internet access can influence website content and share their views with the world. Once, disparaging comments either were made by a person within his or her limited social networks (for example, down the pub with their friends) or subject to screening by publishers (e.g., newspaper editors or online media outlet managers) conscious of the risks of publishing defamatory material. However, these days, emboldened by a false sense of online anonymity or a lack of thought for the repercussions, everyday web users are just as likely to individually post disparaging material on one of these websites.

The fact that this material is posted online can magnify the damage and complicate the issues, because of:

- the larger size of online social networks;

- the difficulties in pinpointing who is behind the creation of online material, and, in some cases, the difficulties in having it removed (sites like Facebook and Myspace often require you to get a court-issued subpoena before they will hand over material such as the IP addresses of users who post defamatory material. By this time, millions of people might have read the offending material);
- the accessibility of the material to prospective customers, employers and business associates (e.g., through Google searches); and
- the more permanent nature of online content (most content leaves an online footprint, which, even after the disparaging material is removed, may be accessed for years to come through other sites).

Most Common Forms of Online Attack

The most common forms of online attacks include the creation of fake profiles (especially on Facebook and MySpace), false and damaging Wikipedia entries, the creation of negative common interest groups on social networking sites (e.g., where ex-employees exchange disparaging comments about their former company or boss), damaging parodies on You Tube, negative comments on online discussion forums, blog entries and the comments in the readers comments sections at the end of online news stories.

While these kinds of online attack can be perpetrated by anyone on anyone (even former High Court Judge, The Hon. Michael Kirby, fell victim to a fake and defamatory profile on MySpace in 2007) some of the most common perpetrators of such attacks can include disgruntled ex-employees, former business associates, consumers, former friends and those with a political axe to grind.

What Steps can You take to Respond to, Minimise or Prevent Damage to Your Online Reputation?

While some organisations choose to block the use of sites such as Facebook at work, often on productivity or network performance grounds, doing so could result in an employee backlash and won't solve the reputational issues these sites raise. After all, employees are only one source of reputational risk and they could still post disparaging material from home or elsewhere.

Below are some other steps which may be more effective in managing your online reputation:

- *Insert non-disparagement clauses in contracts* – Having a contractual term which prevents employees, former employees or business partners from making disparaging statements overcomes many of the problems with traditional causes of action (see below). It is important to ensure that the clauses can be enforced after the underlying contractual relationship ceases.
- *Implement clear internet usage policies for employees* – Aside from making employees think twice before engaging in unwanted behaviour on these sites, good internet usage policies will: (i) make it easier to seek recourse against employees who do breach them; and (ii) lower the risk of being held vicariously liable for any harmful online behaviour your employees engage in, such as harassment and cyberbullying, defamation or breach of copyright. These policies should form part of your company's employment contracts. Ideally, your employees should also be educated regarding these policies and the risks and consequences of their online behaviour, and reminded of these policies regularly (e.g., by a pop up prompt when they sign on to the network).
- *Act first: create positive and accurate online postings/profiles* – The first step many prospective employees, customers or business associates take to find out about a company (or a person) is to conduct an internet

search. While most businesses already have websites, creating further positive images on the net (e.g., by adding an accurate entry on Wikipedia or an official profile on a social networking site) can improve your online reputation and minimise the impact on your overall online reputation caused by any other negative posts/profiles.

- *Manage/close unofficial groups* – It is common for employees or ex-employees to create unofficial company related groups – places where members can post or exchange information – on social networking sites (for example, MySpace currently has over 47 000 Companies/Co-workers groups registered globally). These groups are not necessarily designed to harm the company or its reputation. Often they are created simply to socialise or stay in touch with colleagues and former colleagues. However, they can lead to an irrepressible number of comments, tags and posts which can be negative, defamatory or unprofessional. If you see an unofficial group page relating to your company on a social networking site, consider asking the administrator if it can be merged into an official group. Alternatively, request to be added as an administrator, so you can monitor and moderate any false, misleading or defamatory content.
- *Be conscious of your privacy settings on personal profiles* – Having a publicly accessible personal profile on a social networking site comes with risks, including having your personal details and photos used to create fake/defamatory profiles, having negative comments posted about you or being tagged in embarrassing photographs seen by your work colleagues. Measures you can take to manage this risk include setting your profile to private (i.e., only making it accessible to "friends") and limiting the access certain friends (e.g., colleagues and business associates) to certain parts of your personal profile (e.g., particular photo albums).
- *Monitor your online reputation* – Simply add your or your company's name to one of the many useful online tools such as Google Alerts, Tweetbeep, Trackur, MonitorThis or Wikipedia's Watchlist. The sooner you notice an attack on your online reputation, the sooner you can respond to it and minimise the damage.
- *If you see something harmful on one of these sites, remove it or contact the site* – Social networking sites cannot monitor all the content published on their site. However, they all have terms and conditions and, if notified of content that breaches these, they will often remove it. Reporting/editing mechanisms vary from site to site. On Facebook, the easiest way to remove inappropriate content on your profile page is to delete it yourself by clicking the "Remove" link next to the relevant content, or, if that is not possible, to report it by clicking the analogous "Report" link. On Wikipedia, you can revert pages, report vandalism or edit the page yourself. If in doubt about the procedures relating to a particular site, email/contact the site administrator directly. It should be noted that simply contacting the site and requesting the material be removed, may not work if the content you want removed does not breach their terms and conditions.
- *Contact the person making the disparaging statements* - They may remove it voluntarily.
- *If all else fails, you can still sue* – Just because material is published by an individual online doesn't mean that the usual legal actions do not apply. For example, in 2008, a UK executive successfully sued a former friend for defamation and misuse of private information, after the former friend created a fake Facebook profile and a group called "Has Mathew Firsht lied to you".

There is no doubt that publishing defamatory material on a social networking site would also be actionable by individuals in Australia. In fact, we have started to see individuals commence actions based on such material.

In 2008 a Melbourne man was forced to publish apologies in two major newspapers over comments made on Facebook, and in 2009 a Western Australian woman launched a claim for defamation and breach of confidence over fake profiles and personal photos published on Facebook and adultfriendfinder.com.

The major obstacle to such actions for businesses in Australia is that profit-seeking companies with more than 10 employees are now statutorily barred from suing for defamation. Companies may rely on other causes of action, such as injurious falsehood or misleading and deceptive conduct, but each of those cause of action faces its own issues. With injurious falsehood, there are difficulties in proving malice and actual damage to your business. With misleading or deceptive conduct, the major issues are that the impugned conduct must occur "in trade or commerce" and that media organisations are generally exempt as "information providers". In the light of these complications and limitations, the best approach for most companies is to support an individual employee's action for defamation or, if it is available, to enforce a non-disparagement clause.

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Restraint Clauses in Employment Contracts

BY DAVID LEGGATT AND JAMES HUTCHINS | DLA PHILLIPS FOX

In the competitive business environment, restraint clauses in employment contracts are close to many hearts. Employers and employees naturally seek to protect their respective interests. Australia has become a home for many employees of international companies, many of whom have restraint clauses in their employment contracts. This article discusses the enforceability of restraint clauses in Australia, with a view to the commercial imperatives of employers and employees of international companies operating in Australia.

Who Says What?

Employers like restraint clauses. Employees don't. Why does each side say what they say?

Employers say that it is only fair to uphold restraint clauses. They want a return on their investment in employees. Employers spend time and money developing employees and their customer/supplier relationships, often supporting employees' endeavours before they perform profitably. In addition, the promise of loyalty during and after the employment contract is often a key element of the bargain struck on the resources, privileges and remuneration extended to the employee.

On the other hand, employees say restraint clauses are unfair. The bargaining power between employer and employee is often unequal. During employment, employees generally devote most of their expertise, time and energy to the employer and once the employment relationship finishes, that "asset" is no longer the employer's to exploit or to sterilise.

Australian Law on Restraint Clauses

Australian common law on restraint clauses in employment contracts developed from English law. Since the late 19th century, there has been a presumption that restraints of trade are invalid.

To enforce the restraint clause, the employer must show that the restraint is reasonable. Reasonableness, and therefore enforceability, is assessed by considering: (i) whether the clause is intended to protect some "legitimate interest" of the employer; and (i) whether the extent of the restriction is greater than is necessary to protect that "legitimate interest".

While Australian courts consider "fairness" in each case, they are ultimately guided by the extent of the employer's interests and whether there is a legitimate reason for the restraint to be imposed.

Types of Information to be Protected

The interests usually protected by employment restraint clauses include confidential information and customer or client relationships.

Regardless of the restraint clause, the employer's confidential information will be protected by the courts if the confidential information can be specifically identified and shown to have been gained in confidential circumstances. Importantly, courts will also require the employer to show that there is an actual threatened misuse of confidential information.

What constitutes "confidential" information is a vexed question, and the answer to that question will depend on the circumstances of each case. Generally, it will be difficult for a business to protect business methods and practices. However, "trade secrets" such as certain formulae, processes, customer information, pricing or costing information are generally considered to be confidential and worthy of protection by the courts as the property of the former employer that is not to be exploited by an outgoing employee.

Australian courts have not settled on a satisfactory definition of "trade secret" but academics suggest that the term includes "any information of a business or commercial nature which has been kept relatively secret".

As stated above, whether information is confidential will be a question of fact that must be considered against the context in which the dispute arises.

The duty not to compete extends to not soliciting the employer's customers during employment. This includes compiling or memorising lists of customers for personal use. Even if lists are not going to be used, or if the custom is not to be transferred, until after the employee's departure, there remains a duty not to solicit. But in cases where the former employee merely responds to approaches from a customer, the promise not to "solicit" customers is not broken. In any case, it will be practically difficult to monitor communications between former employees and customers unless the customer is forthcoming with information.

Information relating to an employer's suppliers may also be protected. In NSW, information about potential suppliers of hand tools for resale in Australia was considered sufficiently confidential as to justify a post-employment restraint of the use of that information.

The "owner" of the information or relationships and therefore whether the employer has a "legitimate interest" in the information, is often contentious. Some tests that have been applied in the past have shown that this issue is not capable of being tested by any single, watertight test.

For example, employers have argued that if the information or customer lists/information needed to be written down, then they were impliedly the "property" of the employer which the employee would be prevented from

using in future competition.

However, this test is fickle, as it depends on the individual employee's capacity for retention of information and ignores the reality that whether something is written down says nothing of how or by whom it was generated.

"Reasonable" Restraints

Clearly, employers will seek to obtain the widest possible protection available to them. But if a restraint clause is too broad in terms of the information it protects, the conduct it prohibits or the timing and geographical reach of the clause, then it will be struck down by Australian courts as being unreasonable.

Reasonableness depends on three factors: (i) the nature and extent of the activities from which the employee is required to abstain; (ii) the area in which those activities must not occur; and (iii) the duration of the restraint. The factors are considered together, not in isolation. For example, where the area of restraint increases, the duration of the restraint must decrease in order to be reasonable and enforceable.

Importantly for those who operate in dynamic industries, the reasonableness of the restraint is assessed at the time the restraint was agreed, not the time at which the alleged restraint occurred. For this reason, commentators suggest that employers should renegotiate restraint clauses regularly for employees who have been working for considerable periods of time, especially if there has been a shift in the duties being carried out by the relevant employee.

It is unclear in Australia whether or how the assessment of reasonableness will be influenced by the fact that a contract was made in another country.

Worldwide restraints are generally not upheld, because courts take the view that no matter how extensive the employer's business activities, it is hard to show that activities in one part of the world can cause damage everywhere else in the world. However, an early Australian decision upheld a trans-Tasman restraint where the employee was a general manager with access to much of the company's confidential information.

Further, the increasing prevalence of multinational corporations, the burgeoning integration of international customer / supplier relationships and certain industry-specific factors may begin to sway courts to the view that international restraints are reasonable and enforceable.

For example, if a contract is made overseas with a company operating a global business with an employee who is intimately involved with the global operations of the company, a worldwide restraint may pass the "legitimate interest" and reasonableness tests and therefore be enforceable.

Consequences for Breach of Restraint Clause

The legal remedies available for a breach of the duty not to compete or to misuse confidential information includes damages equal to the amount of the loss caused by the breach or an injunction to prevent apprehended misdeeds.

Clearly, calculating damages is often difficult because it is not easy to reliably ascertain the commercial "value" of a customer relationship or of confidential information, not to mention identifying the precise losses that were caused by the breach. In reality, an award of damages will only ever compensate for loss that has already occurred and will almost certainly fail to fully compensate the successful party.

While an injunction may prevent future damages, the efficacy of injunctions will depend on the duration and scope of the injunction and the enforceability of injunctions may be limited to the information flowing to the

person who seeks to enforce the injunction, not to mention the restrictions on enforceability of orders across jurisdictions.

Conclusion

Australian law on restraint clauses in employment contracts follows the common law principle that enforceability relies on the legitimate interest protected by, and reasonableness of, the clause. This depends on whether the employer has a "legitimate interest" and whether the restriction is apt, but not more than necessary, to protect that "legitimate interest". The legitimacy of the interest will depend on the relationship or information in dispute and how those came to exist. While there is a general reluctance to enforce restraints for large geographical areas, the onset of globalisation and certain industry-specific factors may provide impetus for more far-reaching restraints to be enforced.

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Consulting Expert v. Expert Witness – Double the Chance of Success or Double the Cost?

BY DAWNA WRIGHT, JON ROWELL AND NATALIE QUINN | MCGRATHNICOL

The work of a forensic accountant is varied and can include investigating financial fraud, valuing businesses, tracing the proceeds of crime, advising on post-acquisition disputes and quantifying loss and damage arising from contractual disputes or other events.

Historically, much of this work was undertaken in the capacity of an expert witness, where the expertise of the accountant is ultimately tested in Court and where the expert has an overriding duty to the Court to be impartial.

In recent years however, there has been an increasing trend for forensic accountants to be engaged as consulting experts, either in place of, or in addition to, an expert witness.

There are a number of reasons as to why this trend has emerged, and is continuing to gain traction, including the need for accounting assistance prior to the commencement of formal litigation proceedings, the realisation that financial analysis is valuable in formulating litigation strategy, and most importantly, the potential need to keep an accounting expert witness "clean" and impartial. This trend has been highlighted both by changes in standards guiding the work of forensic accountants, as well as by recent Court judgements commenting on the work of expert witnesses.

This article considers the distinction between the two roles, the advantages of using a consulting expert, and other considerations if an expert is engaged to perform both roles.

Expert Witness

In Australia, the *APES 215 Forensic Accounting Services* standard was released by the Accounting Professional and Ethical Standards Board (APESB) in December 2008 and became effective from 1 July 2009. It now provides

a clear distinction between Consulting Expert Services and Expert Witness Services, which was not detailed in the preceding authority.

The role of an expert witness is explained in APES 215 as someone who may express opinions to the Court "..... on matters such as whether technical or professional standards have been breached, the amount of damages, the amount of an account of profits, or the amount of a claim under an insurance policy."

As indicated in the Federal Court of Australia expert witness guidelines and in APES 215, an expert witness has an overriding duty to assist the Court impartially on matters relevant to his or her area of expertise – and not to assist or advocate for the party by whom he or she is retained.

Consulting Experts

As evidence of the emerging trend, APES 215 helpfully now "defines" the role of a consulting expert, which has previously been referred to in Australia as a dispute consultant, a "shadow" expert, or a "dirty" expert. It characterises a consulting expert service as an accountancy service provided in the context of a matter that may, or will, be brought before a Court, excluding that service of an expert witness, lay witness or investigation service. "It includes acting as an advisor, an arbitrator, mediator, member of a professional tribunal, expert in an expert determination, referee or in a similar role".

A consulting expert is generally engaged as an advisor to the legal team and its client. As indicated by APES 215, the role can be wide-ranging. A consulting expert is free to advise its client in the knowledge that they are not subject to the impartiality restrictions encountered by an expert witness, as they will not be required to give evidence in Court. Consequently, they are able to advise on financial issues impacting the strategy of their client's case and highlight potential pitfalls, subject to the boundaries of the APESB *"Code of Ethics for Professional Accountants"*.

When is it Advantageous to use a Consulting Expert?

The benefits of engaging a consulting expert in a dispute have lead to the increase in their use in Australia. The key advantages are:

- conducting financial analysis early to avoid costly "surprises" arising in the latter phases of a litigation;
- obtaining expert assistance when formulating a litigation strategy;
- maintaining an expert witness' impartiality and limiting their exposure to discrete issues; and
- the opportunity to obtain a second opinion, or "stress test" opinions, on complex matters;

In our experience, disputes involving complex issues often require the assistance of a consulting expert, particularly in the early stages. The requirement for expert witnesses is then considered once the legal team's strategy is further progressed and specific issues have been identified. The various ways in which a consulting expert may assist in the "pre-trial" phases of a dispute are listed below.

Readiness (Planning, Negotiation)

- financial "fact finding";
- conducting financial analyses for the purposes of legal strategy;
- providing input to the drafting of, and response to, pleadings and damages sections of a Statement of

Claim;

- assisting in determining which issues may require financial experts, and in formulating their instructions;
- calculating preliminary estimates and "scenario analysis" of potential damages outcomes;
- performing analyses for the purposes of settlement negotiations or mediation either within or outside of the litigation process.

Response (Discovery, Expert Evidence)

- assisting with collating relevant financial documents and identifying discovery required from other parties;
- assisting the legal team analyse and validate financial information obtained from its client prior to discovery;
- reviewing other parties' discovery to identify financial evidence that may support or be detrimental to their client's case.
- assisting with the briefing of expert witnesses;
- preparing financial information which is to be used by expert witnesses; and
- playing "devil's advocate" to critique and "stress-test" the opinions of the expert witnesses.

The above list is not exhaustive but provides an indication of how much the consulting expert's role can extend beyond the more traditional role of expert witness.

When Consulting Expert Becomes Expert Witness

There is a clear distinction between the roles of a consulting expert and expert witness. However, sometimes these roles can become blurred or overlap. Consequently, in practice, the roles of the consulting expert and expert witness need to be carefully considered, well defined and constantly monitored.

There are high profile examples of where a Court has questioned the objectivity of an expert witness resulting in the exclusion from trial of that expert's written report and evidence. The expert has either been found to have crossed the line by advocating their client's case too strongly, or has acted as an advisor in formulating strategy.

Australian Securities and Investments Commission v Rich [2005] NSWCA 152 (ASIC v Rich) is an example of a recent decision in Australia where a large proportion of an expert's report was held as inadmissible due to the expert and his team performing an investigating role in the matter prior to being engaged as an expert witness. The Court considered whether the expert was able to disregard the broader information known to him about the matter in determining his expert opinion.

It has become increasingly difficult for expert witnesses to provide advice on financial issues needed by lawyers, without risking objectivity and independence. Especially on large, protracted and/or complex matters, this restriction can prove a challenge for the legal team as it is faced with difficult financial issues in determining and executing their legal strategy, not to mention the day to day management of the financial information being produced by the client. To ensure objectivity is maintained at all times, an expert that is ultimately expected to act as an expert witness should not be involved in these aspects.

In addition, where it is initially thought that only one expert will be required, the role should be closely monitored for any changes in circumstances over the course of the engagement that may give rise to a conflict in

adherence to the Court expert evidence guidelines down the track.

But will the use of a separate consulting expert double the cost to the client? In our experience, it does not – as the work of the consulting expert will generally need to be performed in any event. Importantly, the use of a consulting expert will often save time and costs by identifying the key financial issues up-front. This can facilitate an early settlement – avoiding the need for an expert witness altogether, as many matters are not expected to go the distance to a trial. But for those matters where it is necessary to prepare for the event that it will end up in Court, the financial analysis performed by the consulting expert will have laid the groundwork for the expert witness to arrive at their opinion more efficiently. It will also allow the client to remain focussed on its business and not become consumed by reviewing and preparing financial information for the legal team.

The costs, benefits and risks of each option must be assessed on a case by case basis. While there are times when it is advantageous to have the two roles performed by a single expert, there are many others where the benefits of using a separate consulting expert can far outweigh the costs.

Conclusion

There is a clear distinction between the roles of a consulting expert and expert witness. However, in long-running and complex litigation the distinction can become blurred. Both roles play an important part in the process, so the issue becomes whether or not they should be performed by separate experts. There is no "one size fits all" solution – a case-by-case assessment is required as there are different risks and advantages associated with either choice in each particular matter. But whichever way the initial decision falls, it is important that the roles of any experts are not only clearly defined at the outset, but also closely monitored through various stages of an ever-changing environment in order to minimise the risk – and costly consequences – of disregarded expert evidence.

Dawna Wright and Jon Rowell are Partners and Natalie Quinn is a Director at McGrathNicol Forensic.

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CHINA

Chinese Company Litigation

BY ZHANG BAOSHENG AND CHENG SHIGANG | KING & WOOD

This article looks at examples of two kinds of disputes which arise frequently in Chinese company litigation: disputes over control of the company's official seal, financial seal and business licence (sometimes referred to as the company "chops") and disputes over changes to the company's incumbent legal representative. The frequency of these disputes highlights the importance of the company chop and the legal representative under Chinese company law.

Example I – The Company Chops

In China, a fight over possession of a company's official seal, financial seal and business licence often corresponds to a fundamental dispute over who has the right to control the company.

For example, in a recent case, "A" was the owner of 80% of the shares in a family-owned Hong Kong pharmaceutical company. The Hong Kong company in turn was the sole owner of a wholly-foreign-owned trading company in Tianjin, near Beijing. "B" was the daughter of A and A appointed B as the legal representative and general manager of the Tianjin company, to ensure that it was controlled by one of his relatives. B had possession of the Tianjin company's official seal, financial seal and business licence.

When, some time later, A's wife passed away, a dispute arose between A and B about who should inherit his wife's estate. After the dispute arose, A removed B from her position as the legal representative and general manager of the Tianjin company. However, B refused to give up possession of the company's official seal, financial seal and business licence and withdrew funds from the company's bank account, causing a great loss.

In that case, A was advised that he could take legal action requiring B to return the official seal, financial seal, business licence and other important items to the company. A was also advised that he could take property preservation measures by which the court would freeze the assets wrongfully transferred out of the company by B.

Given the special relationship between A and B, it was also suggested that A consider negotiating first to ease the conflict. Before the litigation came to an end, A and B entered into a settlement agreement and B delivered-up possession of the company chops and other important items to A.

Analysis

In China, the person who has possession of a company's official seal, financial seal and business licence is the one who can, in practice, exercise control over the company.

An imprint of the official seal must be affixed to any contracts which the company enters and to any court documents filed on behalf of the company in domestic litigation. An imprint of the financial seal must be affixed to bank documents each time the company deposits, withdraws or pays money to third parties. The business licence is the official legal certificate which entitles the company to engage in business.

The company official seal, financial seal and business licence are, in theory, company property. Legally speaking, they are not the property of any individual one of the company's shareholders. However, since third parties can rely on imprints of the company official seal, financial seal and presentation of the company's business licence as evidence of the company's authority, a shareholder or other person in practical control of the company will have exclusive control over these items. In some cases, they might use the company official seal, financial seal and business licence in a way that harms the interests of the company, and of the other shareholders.

In theory, the wrongful use of the company official seal, financial seal and business licence is a kind of tort against the company. Under Article 152 of the PRC Company Law (2005), the company itself has the right to commence legal proceedings for the return of the company properties and for other relief. However, failing that, under the same provision of the PRC Company Law, any of the company's shareholders may take action instead. As mentioned in the example above, the people's court may order interim relief, if requested, in the form of a property preservation order freezing property under the defendant's control, pending the outcome of the legal proceedings.

Example II – The Legal Representative

If a dispute requires legal proceedings to be commenced against a company's existing legal representative, the process can be difficult, because the legal representative has a special kind of authority under Chinese company law.

In a recent case, a Mr. Wang was the legal representative of a Chinese limited liability company. Shareholder "A" transferred his shares in the company to shareholder "B" and the change of shareholding was duly registered. However, Mr. Wang, who was personally loyal to Shareholder A, refused to return the company official seal, financial seal, business licence etc. and refused to cooperate in registering the company's new legal representative, preferring to remain in the position himself.

Shareholder B was to hold a shareholders' meeting and board meeting to formally appoint the new legal representative. With the shareholders' and board meeting resolutions as proof of the company's corporate will, B was able to initiate legal proceedings using documents signed by the new legal representative and to obtain, as a result, an order from the court confirming the new legal representative's appointment.

Analysis

Under the PRC Company Law, a company must assign one person as its "legal representative". The legal representative is the person ultimately, legally responsible for the exercise of the company's rights and the performance of the company's duties in accordance with the law. This person is usually the chairman of the company's board of directors or the company's general manager.

Within its internal legal structure, the relationship between the company and the legal representative is one of employer and employee. Therefore, in theory the legal representative can be appointed and removed by the passage of board meeting or shareholder meeting resolutions, as appropriate.

However, in the context of the company's interactions with third parties, the acts of the legal representative

bind the company. The legal representative's authority arises by operation of law and, once appointed, he or she requires no separate authorisation to act in the company's name. As a result, the company may not use the lack of any internal corporate authorisation to defeat a claim by any third party who has relied on a legal representative having authority to act in the company's name.

The legal representative is also the person who has the right to participate in civil proceedings on behalf of the company and, in practice, the People's Courts consider the local Administration for Industry and Commerce ("AIC") registration record as prima facie evidence of the true identity of the company's legal representative.

If the company has changed its legal representative, but has not amended its AIC registration removing the incumbent legal representative's name and replacing it with the name of the new legal representative, then it can be difficult for the company's newly-appointed legal representative to initiate civil proceedings in the company's name, in the event that such a step becomes necessary.

There are often valid reasons why a company's legal representative is changed. For instance, the change might be necessary because of changes to the company's role in a group or operational structure or because of a change of the company's shareholders. However, in some cases, the incumbent legal representative will simply refuse to step down and will not cooperate in the amendment of the company's AIC registration record either. Under those circumstances, who has the right to initiate legal proceedings on behalf of the company is a matter of much debate.

In our view, an AIC registration merely confirms the identity of the company-appointed legal representative and places that appointment on record; it does not affect the company's right of internal governance. Therefore, if the company has appointed a new legal representative in accordance with the law, administrative regulations and the company's articles of association, then the newly-appointed legal representative has been lawfully appointed and may exercise the civil rights of the company, including participating in legal proceedings. That is the case even if the company's AIC registration record has not been amended. Our view was confirmed in litigation of the case cited above.

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The Sanlian Case – Recognition and Enforcement of a Chinese Monetary Judgment in the United States

BY ARIEL YE AND GE YAN | KING & WOOD

With the exception of those dealing with divorce and custodial issues, it is rare for judgments issued by Chinese courts to be recognised and enforced in the United States. Therefore, it was a significant event when, in the matter of *Hubei Gezhouba Sanlian Industrial Co., Ltd. et. Al. v. Robinson Helicopter Co., Inc., 06-01798 (C.D. Cal 2009)* (the "Sanlian Case"), United States District Court Judge Florence-Marie Cooper decided to enforce a monetary judgment of almost US$6.5 million awarded by the Higher People's Court of Hubei Province (the "Higher

Court"), China, against Robinson Helicopter Company, an aircraft manufacturer based in Torrance, California ("Robinson").

Case History

Hubei Gezhouba Sanlian Industrial Co., Ltd. ("Gezhouba") was the owner of a model R-44 helicopter manufactured by Robinson. Hubei Pinghu Cruise Co., Ltd. ("Pinghu") was the owner of a river cruise boat from which the helicopter had been operating. On Tuesday, March 22, 1994 the helicopter crashed into the Yangtze River, causing the death of three people. The crash was the result of a production defect in the particular Robinson R-44 model and in March 1995, the two Chinese companies sued Robinson in the Superior Court of the State of California claiming negligence, strict liability and breach of implied warranty. Robinson demurred, arguing that the Peoples' Republic of China had an independent judiciary which followed due process of law and that a Chinese court would have jurisdiction over the case. The California Superior Court agreed, and the suit was dismissed on the grounds that China was a more convenient forum. However, as a condition for dismissal of the California lawsuit, Robinson agreed to toll the statute of limitations and to abide by any judgment rendered by a Chinese court.

In 2001, after an attempt to submit the case to arbitration in the United States failed, the Chinese companies decided to commence civil proceedings against Robinson in the Higher Court in Hubei. A three-judge panel was formed, and among other things, it properly notified Robinson of the date set down for trial, March 25, 2004, in accordance with the provisions of the *PRC Civil Procedure Law* and Article 5(a) of the *Hague Convention on the Service Abroad of Judicial and Extrajudicial Documents in Civil or Commercial Matters*. Robinson failed to appear on that date but the trial continued. After assessing the evidence submitted in due course by the plaintiffs, the three-judge panel found that the fatal helicopter crash had indeed been the result of manufacturing defects in the Robinson R-44. Finally, in December 2004, the Higher Court issued a judgment awarding damages, costs and interest equivalent to US$1.9 million and US$4.5 million in favour of Gezhouba and Pinghu respectively *(Hubei Gezhouba Sanlian Industrial Co., Ltd., et.al. v. Robinson Helicopter Company Inc., Case No (2001) E-Min-Si-Chu-1),* (the "PRC Judgment").

Since the PRC Judgment was rendered by a court of first instance, Robinson had an automatic right of appeal under the *PRC Civil Procedure Law* which, as a party without domicile in the PRC, it had to exercise within 30 days of service. However, Robinson did not exercise its right of appeal in the PRC courts, and as a consequence the PRC Judgment became final and enforceable under PRC law. Because Robinson was a party without domicile in the PRC, the plaintiffs were entitled, in principle, in accordance with the *PRC Civil Procedure Law,* to apply for recognition and enforcement of the PRC Judgment directly to the foreign court with jurisdiction over Robinson's assets.

There is no treaty and there are no reciprocal arrangements between the U.S. and China with respect to the mutual recognition and enforcement of judgments issued by each other's courts in civil and commercial matters. However, in the U.S., the general principles of comity and recognition of foreign money judgments have been codified in the *Uniform Foreign Money Judgments Recognition Act* ("UFM-JRA") and the state of California has adopted the provisions of the UFM-JRA in its *Code of Civil Procedure*.

Notwithstanding this, the plaintiffs' initial efforts to obtain recognition of the PRC Judgment in the U.S. were rejected. In enforcement proceedings before the United States District Court for Central District of California, Robinson argued, and presiding Judge Cooper agreed, that the PRC Judgment was void because California Law

rather than PRC Law applied to the statute of limitations, which had expired before the Chinese proceedings were commenced. However, the plaintiffs appealed Judge Cooper's decision to the U.S. Court of Appeals for the Ninth Circuit which ruled that the Chinese proceedings were not time-barred. This was so, according to the Court of Appeals, because Robinson's agreement to toll the statute of limitations in the original California Superior Court proceedings remained in place. The Court of Appeals also found that recognition and enforcement of the PRC judgment would not offend California's public policy against stale claims.

The Enforcement Decision

On remand to the California Central District Court, Judge Copper again heard argument from the parties concerning recognition and enforcement of the PRC Judgment. At the bench trial on June 2 and 3 2009, Robinson argued, contrary to its original position, that the Chinese legal system does not provide impartial tribunals or procedures compatible with the requirements of due process. However, finding no evidence that the Higher Court's decision lacked either impartiality or due process, Judge Cooper ruled that the PRC Judgment was "final, conclusive and enforceable under the laws of the People's Republic of China" deciding on August 12, 2009 that "Plaintiffs are hereby entitled to the issuance of a domestic judgment in this action in the amount of the PRC Judgment, with interest calculated as set forth in the PRC Judgment."

Legal Analysis

The UFM-JRA has been adopted as law by the majority of the U.S. states. Under the UFM-JRA "Foreign Money Judgment" means any judgment rendered in a jurisdiction outside the U.S. and its territories which has the effect of granting or refusing the recovery of a sum of money. Under the law of states which have adopted the UFM-JRA, a Foreign Money Judgment is subject to a limited-scope inquiry before it can be recognised and enforced as a domestic money judgment. A defendant challenging recognition of a Foreign Money Judgment may not retry issues of liability or damages, but is instead limited to the due-process type defences enumerated in the UFM-JRA.

As a mandatory condition, a Foreign Money Judgment must be final, conclusive and enforceable under the law of the jurisdiction in which it was rendered. In addition, a U.S. court applying the UFM-JRA must be satisfied of that the foreign court: (i) has rendered its judgment under a system that provides impartial tribunals or procedures compatible with the requirements of due process; (ii) has personal jurisdiction over the defendant; and (iii) has subject matter jurisdiction over the controversy.

A U.S. court applying the UFM-JRA may also take into consideration any of the following circumstances: (i) that the defendant received sufficient notice of the proceedings; (ii) that the judgment was not obtained by fraud; (iii) that the judgment is not repugnant to the enforcing court's public policy; (iv) that the judgment is not in conflict with another final and conclusive judgment; (v) that the judgment is not inconsistent with an ADR agreement between the parties; (vi) where jurisdiction is based on personal service alone, that the foreign tribunal was not a seriously inconvenient forum; and (vii) whether or not the foreign court reciprocally recognises judgments from the U.S. However, it is not necessary for a U.S. court to consider any of these discretionary factors when making a decision to enforce a foreign monetary judgment under the UFM-JRA.

In the Sanlian case, the California District Court found that the PRC judgment involved the recovery of a sum of money, the PRC judgment itself was final, conclusive, and enforceable under the laws of the PRC, and service was proper. As California's law adopting the UFM-JRA applied to the case, and no evidence was put

forward that any of the mandatory conditions for recognition had not been fulfilled, the plaintiffs were entitled to a domestic judgment. The uniform principles governing recognition of Foreign Money Judgments in the U.S. do not discriminate against any particular jurisdiction of origin. As a result, Chinese litigants can rely on U.S. legal authority pertaining to the recognition of Foreign Money Judgments originating from any country in order to determine whether a judgment from China will be granted domestic recognition and enforcement under a given set of facts.

While cases under the UFM-JRA abound, cases specifically addressing recognition of Foreign Money Judgments entered in China are still relatively few. Together with the modernisation of everything else in the People's Republic, its judicial system is rapidly developing. Therefore, it is increasingly likely that when deciding whether to recognise a Foreign Money Judgment entered in China, a U.S. court will conclude that China's judicial system provides impartial tribunals and comports with traditional western notions of due process. As Judge Cooper noted, there was no evidence advanced in the Sanlian case to show that the PRC courts lack impartiality or due process. Importantly, Judge Cooper noted in her Findings of Fact and Conclusions of Law that the requirements of due process are interpreted broadly when the procedures of a foreign tribunal are at issue. Under U.S. law, a foreign legal system will be seen as compatible with the requirements of due process as long as its procedures do not offend basic concepts of fairness.

Conclusion

If future Chinese monetary judgments otherwise meet the mandatory requirements of the UFM-JRA, there is very little to distinguish them under U.S. law from Foreign Money Judgments entered in jurisdictions with well-established reputations for impartiality and due process such as the courts of England, Australia or Canada, as demonstrated in the Sanlian Case. Litigants domiciled in the U.S. but defending claims in the PRC courts should take note of the California District Court's recent findings.

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Litigating the Non-Competition Obligation – Risks and Responses for Senior Officers

BY LIU XIANGWEN | KING & WOOD

Multinational corporations ("MNCs") tend to focus on a single industry or sector when investing in China, either by creating a greenfield investment or by strategically acquiring or merging with businesses that are already established in the local market. It is standard operating procedure for MNCs to appoint one senior officer to the board of directors or as the general manager of several or even all of their Chinese operating companies.

This practice is especially evident in private equity investments and it has its advantages. First, it allows MNCs to simplify the management structure in their Chinese operations. Secondly, it allows them to save on human resource costs and thirdly, it allows them to implement business policies consistently.

However, the practice is starting to be challenged in the Chinese courts. The leading example occurred recently when a Chinese company ("the Chinese side" or "Party A") filed legal action in the Intermediate People's Court of Guilin against the senior officer of a well-known MNC ("the Foreign side" or "Party B"). Party A's complaint stemmed from the fact that Party B had placed several of its senior officers on the boards of directors of its Chinese joint ventures with Party A, as well as on the boards of many companies owned or invested in by Party B other than those which were established as joint ventures between Party B and Party A.

Party A filed its complaint in the courts in several Chinese cities where the parties had set up joint ventures. Thereafter, beginning in November 2007, the Chinese courts began to issue judgments which ordered Party B's senior officers to resign from their positions in the parties' joint ventures and to pay compensation for the damage which they had caused by serving at the same time as the directors or senior officers of competing companies. The decision of the Intermediate People's Court of Guilin (the "Guilin Case") is one example of the Chinese courts' decisions which focused on breaches of Article 149, Paragraph 5 of the PRC Company Law. The Guilin Case was part of a larger sino-foreign joint venture dispute involving Party A and Party B that ended with a settlement in late 2009.

Case History

Between 1996 and 2006, Party A and Party B established 39 joint venture companies in China. One of the companies, ("Guilin Co") was established in July 2000 as a joint venture between Party A (33%), one of Party B's Singaporean subsidiaries ("Sing Co") (51%), and a minority local investor (16%).

In December 2005, Sing Co appointed Mr. F, one of Party B's senior financial officers, to be a member of Guilin Co's board of directors. At the same time, Party B and several other Party B subsidiaries appointed Mr. F as a director of more than a dozen other companies that were not part of the group of joint ventures between Party A and Party B, but still operated in the same industry as Guilin Co.

The other companies that Mr. F served as a director included manufacturers of several big national consumer brands. All of the companies, whether joint ventures between Parties A and B or otherwise, manufactured products similar to Guilin Co's for local consumption.

Over more than a decade the joint ventures were successful and profitable. However, in 2007 the Chinese side and the Foreign side fell into dispute over long term strategic control of their 39 joint ventures. The dispute resulted in the parties filing more than 50 separate litigations and arbitrations in forums around the globe.

During the dispute, Party A and the local minority investor in Guilin Co filed a shareholder's derivative action against Mr. F with the Guilin Intermediate People's Court (the "Guilin Court"). In their statement of claim, Party A and the local investor asked the court to order Mr. F to resign from Guilin Co.'s board of directors, and requested an order prohibiting him from concurrently holding the same position at more than a dozen competing companies. They also requested an order that Mr. F pay any damages that he was found to have caused to Guilin Co. by concurrently serving on the boards of directors of Guilin Co's major competitors.

The Guilin Court's Decision

Based on the evidence adduced, the Guilin Court had little difficulty in finding that the Mr. F had violated Article 149, Paragraph 5 of the PRC Company Law.

Article 149 of the PRC Company Law provides that: "The directors and senior officers of a company shall not: ... (5) take advantage of their positions to obtain for their own benefit or the benefit of others any business opportunities that belong to the company or to engage in the same type of business as that of the company for their own account or for the account of others without approval of the shareholders' meeting or the shareholders' general meeting".

The Guilin Court focused on two key issues in deciding whether Mr. F had violated his duty not to compete under Article 149, Paragraph 5 of the PRC Company Law. Firstly, it considered whether Guilin Co.'s board of directors had approved Mr. F serving as the director or manager of other companies. Secondly, it looked at whether the other companies on whose boards Mr. F was serving were involved in the same industry as Guilin Co or not.

The Guilin Court had no difficulty in relation to the first question, finding that Guilin Co.'s board of directors had not given Mr. F approval to serve at the same time as a director or manager of other companies owned or invested in by Party B.

As to the second question, the Guilin Court found that Mr. F had served as a decision maker and was at the same time extensively involved in multiple companies' operations, and that some of the companies competed aggressively against Guilin Co. The Guilin Court also found that Mr. F held positions in multiple companies that shared the same or similar business scopes, sold the same or similar types of products, used the same or similar mode of sales, had the same or similar markets, and asked the same or similar prices for their products as did Guilin Co. As a consequence, the companies were considered to be in competition with one another, and accordingly, the Guilin Court found that Mr. F was prohibited from serving the other companies in the absence of Guilin Co's approval.

Analysis

The Guilin Court's findings show that Chinese courts can look further than a company's registered business scope in order to determine whether it and another business are the same or similar. Indeed, Chinese courts may look at any relevant factors which illustrate that the companies are in competition with each other. For example, the Guilin Court looked at factors such as the types of products which the companies made, the modes of sales the companies employed, each company's geographic sales markets, and the prices the companies charged for their products.

The Guilin Court's decision also shows that because Chinese law presumes that a company's directors are active participants in that company's operational decision making process, Chinese courts may infer that if a director serves in competing companies then he or she has in fact participated in a form of unfairly competitive conduct that is prohibited by Article 149, Paragraph 5 of the PRC Company Law.

Risks for Senior Officers

A company's directors and managers face a number of risks if they choose to serve as the directors or managers of multiple companies in the same industry or business sector. If the nature of that service is ever challenged in litigation using the Chinese court system then: (i) The director or manager may be forced to give up one or

more of his or her positions; (ii) the director or manager could be forced to give up any income that he or she has gained in violation of the statutory non-compete obligation (the company that is considered to be the victim of the director or manager's conduct will be entitled to receive all of the illegal income that the director or manager has made); and (iii) The director or manager may be held liable for any damages that he or she has caused to the victim company.

The Guilin Court penalised Mr. F in all three of these ways.

Responses for Senior Officers

The Guilin Case helps to show that, in China, when business runs smoothly the practice of appointing one key staff member to directorial or managerial positions in several companies does not raise a serious issue. However, if a dispute does occur (especially a dispute over strategic control) then directors and managers who serve multiple businesses are easy litigation targets.

Litigants do not have a difficult burden of proving their claims in these situations, because they merely need to show that: (i) a director or senior manager has been appointed to serve multiple companies that can be said to compete in the same or similar industries; and (ii) that the plaintiff company did not give its approval.

By contrast with the previous company law (1993), the PRC Company Law (2005) clearly establishes that as long as the shareholders' meeting or the board of directors meeting (in the case of a joint venture company) has approved the director or manager's service in a competing company, then the director's statutory non-competition duty to that company has been waived. Thus, Article 149, Paragraph 5 of the current PRC Company Law does indeed provide a lawful way for directors and senior managers to serve multiple companies which may be technically considered to be in competition with one another.

It is recommended that if an MNC requires the same key staff to serve senior managerial or directorial positions in multiple Chinese companies, then the MNC should be proactive and ensure that formal approval is obtained, in the manner prescribed by the law. If a major dispute occurs and no such approval has been obtained, as the Guilin Case demonstrates, it may be easy for a litigant in local court proceedings to prove that a breach of Paragraph 5, Article 149 of the PRC Company Law has occurred.

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Enforcement of ICC Awards in China

BY LIU YUWU AND XU XIANHONG | KING & WOOD

The people's courts play an important role in the enforcement of international arbitral awards in China. They must recognise and enforce arbitral awards made by foreign arbitral institutions unless a reason for non-enforcement applies under international treaties which China has concluded or to which China is a party or in accordance with

the principle of mutual reciprocity. There is also a pre-reporting system which requires the lower people's courts to obtain confirmation from a higher-level court of any decision not to enforce an international arbitral award. Many cases exist in which parties have sought to enforce ICC awards in China and this article looks at several examples.

Enforcing ICC Awards in China – The Theoretical Framework

Article 25.3 of the ICC Rules provides that "The award shall be deemed to be made at the place of the arbitration and on the date stated therein".

Therefore, an ICC award can be deemed to be made in Mainland China when the place of arbitration is in Mainland China, for example Beijing or Shanghai. Alternatively, an ICC award can be deemed to be made outside Mainland China if the place of arbitration is not in Mainland China for example, Paris or Hong Kong.

If the award is made in Mainland China, can we assume that it shall be deemed a "domestic award" under Chinese law and is enforceable in China pursuant to Chinese law? And if the award is made outside of China, can we assume that it shall be deemed "foreign award" under Chinese law and thus enforceable in China pursuant to the New York convention? To answer these questions, we must refer to the PRC Civil Procedure Law (revised in 2007) which classifies arbitral awards into three categories:

- Category A: award made by an arbitral institution established according to Chinese law (Article 213).
- Category B: award made by foreign-related arbitral institution of the PRC (e.g., CIETAC) (Article 258).
- Category C: award made by a foreign arbitral institution (Article 267).

To enforce a Category A award, the applicant may apply for enforcement to the competent people's court. The court may dismiss the application for enforcement if any of the following matters is proved: (i) the parties had neither included an arbitration clause in their contract, nor subsequently reached a written arbitration agreement; (ii) matters decided in the award exceed the scope of the parties' arbitration agreement or are beyond the authority of the arbitration institution; (iii) the composition of the arbitral tribunal or the arbitral procedure did not conform to statutory procedure; (iv) the main evidence for ascertaining the facts was insufficient; (v) the law was applied incorrectly; and (vi) one or several arbitrators acted corruptly, accepted bribes, practiced graft or made an award that perverted the law.

To enforce a Category B award, the applicant may apply for enforcement to the intermediate people's court of the place where the party subject to enforcement resides or where its property is located. The court may dismiss the application for enforcement if any of the following matters is proved: (i) The parties had neither included an arbitration clause in their contract nor subsequently reached a written arbitration agreement; (ii) the person against whom the application is made was not requested to appoint an arbitrator or to take part in the arbitration proceedings or the person was unable to state his opinions due to reasons for which he is not responsible; (iii) the composition of the arbitration tribunal or the arbitration procedure was not in conformity with the rules of arbitration; (iv) matters decided in the award exceed the scope of the parties' arbitration agreement or are beyond the arbitral authority of the arbitration institution; (v) the people's court determines that enforcement of the award would be against the public interest.

To enforce a Category C award, the applicant may directly apply to the intermediate people's court of the place where the party subject to enforcement resides or where its property is located. The people's court must handle the matter pursuant to international treaties concluded or acceded to by the People's Republic of China or in accordance

with the principle of reciprocity. China ratified the New York Convention on December 2, 1986 with reciprocity and commercial reservations. People's courts must recognise and enforce arbitral awards made by foreign arbitral institutions if the conditions in the New York Convention (or, where applicable, in arrangements such as the Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong SAR (1999)) and in the domestic law are satisfied.

To enforce an award made in Hong Kong, the applicant needs to make its application in accordance with the Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong SAR reached in June 1999, under which the courts of Mainland China have agreed to enforce the awards made in Hong Kong and vice versa.

Enforcing ICC Awards in China - In Practice

The following are examples of how these classifications have been applied by the people's courts to ICC awards. However, note that unlike common law jurisdictions, the system of judicial precedent does not exist in China. Therefore, the people's courts are not bound by their own earlier decisions or by the decisions of other people's courts.

Example 1 - "Arbitration: 15.3 ICC Rules, Shanghai Shall Apply."

A, a German company, and B, a Chinese company, had entered into a contract in December 2000, which contained a clause providing "Arbitration: 15.3 ICC Rules, Shanghai shall apply".

A dispute arose during the performance of the contract and B filed an action with the local people's court. In April 2003, A submitted the dispute to the ICC for arbitration. B raised an objection to the ICC's jurisdiction over the dispute and A maintained that the arbitration clause was valid and binding.

Thereafter, A filed an action with the local people's court, requesting it to confirm the validity of the arbitration clause. However, both the Wuxi Intermediate People's Court and the Jiangsu Higher People's Court determined that the arbitration clause was invalid, and submitted the question to the Supreme People's Court for confirmation. The Supreme People's Court replied in July 2004: "...Since the arbitration clause does not contain an express agreement on selection of arbitral institution, it shall be ruled invalid."

In March 2004, the ICC made an award in favour of A and in August 2004, A applied to the Wuxi Intermediate People's Court for recognition and enforcement of the award.

The Decision of the People's Court

The Wuxi people's court found that the ICC award in question had been made by the ICC and had been affirmed by its secretary general, hence it was a "non-domestic award" as defined in the New York Convention. Since the New York Convention applied to the award, the court decided that it must review the award in order to decide whether to enforce it. Upon completing its review, the court found that the arbitration clause had been ruled invalid by a competent people's court, so that the award fell within the meaning of Article V.1(a) of the New York Convention, that is: "the parties to the agreement referred to in article II 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".

As a result, the application for enforcement of the award was dismissed.

Example 2 - ICC Arbitration in Paris

C, D and E, three foreign companies, and F, a Chinese company, entered into a joint venture agreement in December 1995, which contained a clause providing for ICC Arbitration in Paris. A joint venture company was established but several disputes arose between the joint venture company and F, which F litigated successfully in the people's courts. As F had obtained favourable judgments in each case it was able to freeze part of the joint venture company's bank accounts and stock-in-trade.

Thereafter, C, D and E submitted a request for arbitration to the ICC, alleging that F had breached the joint venture agreement. F responded, and extensive issues were dealt with during the ICC proceeding, including in relation to the operation of the joint venture company, the matters disputed in the previous people's court cases between the joint venture company and F, the property reservation measures taken by F in each case and other matters.

As a result, in 2007, the ICC made an award materially in favour of C, D and E. F refused to perform as directed in the award. So C, D and E, as applicants, applied for recognition and enforcement of the award before the Jinan intermediate people's court, in Shandong province in China.

The Decision of the People's Court

The Jinan people's court found that the ICC award was made in Paris, noting that both France and China are signatories of the New York Convention, hence the New York Convention applied. The court went on to find that the decision in the award exceeded the scope of the arbitration clause, in violation of Article V.1(c) of the New York Convention, that is: "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 decision 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 may be recognized and enforced".

As a result, the application for enforcement of the award was dismissed.

Example 3 – "The Place of Arbitration is Hong Kong"

G, a Hong Kong company, and H, a Chinese company, entered into a sales contract in June 1998, which provided: "any request for arbitration shall be submitted in Hong Kong. The arbitration shall be conducted according to ICC Rules and British law". A dispute arose during the performance of the contract and G submitted the dispute to the ICC for arbitration.

The ICC made an award in October 2001which expressly stated that "the place of arbitration is Hong Kong", and G applied to the Taiyuan intermediate people's court in Shanxi province in China for recognition and enforcement of the award.

The Decision of the People's Court

In the opinion of the Taiyuan people's court, the award was not consistent with the parties' arbitration clause, the composition of the arbitral tribunal was not consistent with the arbitration clause, the arbitral tribunal did not give H the chance to sufficiently present its counter-claims during the arbitration and the award was against the public interest. The Shanxi Higher People's Court upheld the lower court's decision, although with different reasons, and submitted the matter to the Supreme People's Court for its confirmation. (Both courts applied criteria for refusing enforcement that are contained in Article 7 of the Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong SAR (1999)).

The Supreme People's Court replied that since the award was made by the ICC, an arbitral institution established in

France, and since both France and China are signatories of the New York Convention, the convention applied. Therefore, it directed the Taiyuan people's court to review the case based on the New York Convention and not based on the 1999 Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong SAR as it had done. The Supreme Court also stated that the reasons for refusal of recognition and enforcement submitted by the Shanxi Higher People's Court do not constitute appropriate reasons under the New York Convention.

Finally, the lower court was instructed to review the case.

Example 4 – "The Arbitration Commission of International Chamber of Commerce Seated in Beijing"

J, a Swiss Company, and K, a Chinese company, entered into a sales contract in January 2003, which contained a clause providing that "all disputes arising from or in connection with this contract shall be submitted to the arbitration commission of International Chamber of Commerce seated in Beijing and in accordance with CISG". A dispute arose during the performance of the contract and J submitted the dispute to the ICC for arbitration in September 2005.

The ICC rendered an award in Beijing in September 2007 in favour of J and in December 2007, J applied to the Ningbo intermediate people's court in Zhejiang province, China, for recognition and enforcement of the award.

In response, K submitted the following defence: by conducting arbitration in Mainland China, the ICC has violated Chinese law; the real intention of the parties' arbitration agreement was for CIETAC arbitration (this is because CIETAC is also known as the Court of Arbitration of the China Chamber of International Commerce); and K was unfairly treated in the ICC arbitration, since it was not duly notified of the appointment of the arbitrator or of other matters during the arbitration.

The Decision of the People's Court

The Ningbo people's court found that K had failed to raise any objection to the validity of the arbitration clause within the time limit provided by law, and noted that the ICC had determined the arbitration clause as valid in its award. Thus, K's objection to the validity of the arbitration clause was not considered justified. The court found that the ICC award involved was a "non-domestic award", and thus the New York Convention applied to it. Accordingly, the court found, there was no evident reason for refusing the recognition and enforcement of the award.

As a result, the application for enforcement was granted.

Recent Development

On January 5, 2010, in a very recent development, the Supreme People's Court has issued a Notice which states specifically that in cases where an applicant applies for enforcement of arbitral awards made in Hong Kong by the ICC, the people's courts shall review the award according to the Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong SAR (1999). Interestingly, the Notice stands in contrast to the directions given to the Taiyuan people's court in example 3 cited above.

It is now clear that awards made in Hong Kong by the ICC shall be enforceable in Mainland China under the 1999 arrangement. This is in keeping with the promotion of Hong Kong as an international arbitration centre.

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HONG KONG

Expert Evidence under the CJR

BY TREVOR DICK | ERNST & YOUNG

Hong Kong's Civil Justice Reform legislation (the "CJR") was implemented on 2 April 2009. The reforms include amendments to the existing Rules of the High Court (the "New Rules") which promote active case management on the part of the Courts and are intended to address perceived problems with regard to the neutrality of expert witnesses and the excessive and unnecessary use of expert evidence.

This article outlines certain decisions handed down by the Courts that pertain to the provision of expert evidence under the New Rules and considers the likely practical consequences of the CJR for expert witnesses, and those instructing experts, going forward.

Expert Directions

Under the New Rules the parties are required to identify in their Timetabling Questionnaire (which is to be submitted within 28 days of the close of pleadings) the names of their expert witnesses and the specific issues to which their evidence will relate. A mere reference to adducing expert evidence "limited to the issue of quantum" will not be sufficient. In *Kam Hing Trading -v- The People's Insurance Company of China (Hong Kong) Limited* (HCA1062/2008, 27 July 2009) Madam Registrar Queeny Au-yeung noted that: "... defining the issues which the expert should give his opinion on will prevent lengthy reports addressing different issues. The Summons should not just state that the expert should give evidence on e.g. the loss suffered by the plaintiff as pleaded in the statement of claim. Pleadings can be lengthy and the expert should not be left to define for himself the questions he needs to answer. Rather, the parties should endeavour to agree on a list of issues for the expert. Such issues should preferably be framed as yes or no or 'multiple choice' questions ... The expert can then provide his opinion around the framed issues."

Practitioners can expect the Courts to take the requirements of the CJR in connection with the framing of instructions for expert witnesses seriously. A well thought out framework identifying the scope of the expert evidence should reduce the risk that the parties' experts produce reports that address totally different issues like "ships that pass in the night".

However, it is often the case that the issues that are pertinent from an expert's perspective are not the same as those that might be initially flagged up for the expert's attention. Case theories evolve over time and are shaped by the factual evidence. In complex matters parties might consider instructing experts in a consulting capacity at the pre-action stage to assist with the gathering of evidence that is pertinent to quantum and to ensure that the scope of the expert evidence is appropriately identified in the Expert Directions.

Statements of Truth

All expert reports must be verified by a Statement of Truth, given by the expert. The Statement of Truth is a declaration that the expert believes that the facts stated in his or her report are true and the opinions he or she has expressed are honestly held. Failure to sign a Statement of Truth may render an expert's opinion inadmissible and any party who makes a false statement in a document which has been verified by a Statement of Truth may be found in contempt of Court.

The wording of the Statement of Truth is as follows: "I believe that the facts stated in this [Expert Report] are true and the opinion expressed in it is honestly held".

The CJR apparently requires that the expert declare his or her belief that *all* facts that appear in his or her report (whether or not they are within his or her knowledge) are true. This raises a potential problem for the expert. The facts in many disputes are heavily contested. An expert who is engaged after the fact is generally not in a position to provide factual evidence. Accordingly, wherever possible the expert should base his or her opinion on contemporaneous documents from which the necessary facts can be determined. If the expert requires assistance in interpreting those documents then he or she should refer to the evidence of the factual witnesses or, if necessary, to appropriate assumptions that he or she may be asked to adopt by his or her instructing solicitors. Any suggestion that the expert is making findings of fact should be avoided.

The importance of the Statement of Truth was emphasised by a decision handed down by Hon Rogers VP in *Tong Kin Hing v Autron Mauritius Corp* ([2009] HKEC 1696). In that case the Plaintiff alleged that there had been a breach of fiduciary duty in connection with the granting of certain loans but the Plaintiff neglected to reveal that he had approved the majority of the loans. The Plaintiff's Counsel conceded that the Statement of Claim was defective in this regard but argued that the Plaintiff should nevertheless be given an opportunity to amend. The Court found that: "The requirement of a statement of truth is important. Its purpose is to focus the mind of the relevant party and to deter sloppy or speculative pleadings and prevent dishonest cases being put forward. It is a very important part of the Court's process in applying the Rules … Having broken faith with the Court by failing to observe what is now a fundamental rule designed to achieve the objectives of the Court process [the Plaintiff] is in no position to seek the indulgence of being allowed to reconstitute the present action rather than having to start anew."

So far as we are aware there have not yet been any cases before the Hong Kong Courts dealing with defective Statements of Truth given by experts. However, the above decision underlines the importance attached to these statements by the Courts.

Single Joint Experts

The Court now has the power to direct that, in appropriate circumstances, expert evidence be given by a Single Joint Expert ("SJE").

In *Total Market Limited v Crosby Wealth Management* (HCA2168/2008, 27 July 2009) Madam Registrar Queeny Au-yeung considered an application for expert directions on quantum. The issues to be addressed in the expert evidence in that matter pertained to the calculation of the losses suffered by the Plaintiff as a result of an alleged "Error Trade" in securities by the Defendant on the Plaintiff's behalf. The Court found that: "Having considered the issues, the securities prices and interest rates should not be controversial. The formula for calculation of the value of the securities is not in dispute. The expert evidence is much a mathematical exercise. I am of the view that an SJE will be sufficient for this case."

This decision underlines the Court's willingness to appoint SJEs in circumstances where the issues that are being

determined are relatively non-contentious and there is likely to be little room for differences of opinion between impartial experts.

What is the reaction of the Court likely to be in a situation in which the evidence adduced by an SJE is challenged by the parties? There is guidance in England & Wales on this eventuality in the matter of *Daniels v Walker* ([2000] 1 WLR 1382) in which Lord Woolf allowed the appeal of a party who wished to adduce its own expert evidence in addition to that of an SJE. He held that the joint instruction of an expert was merely the first step in obtaining expert evidence and that in a substantial matter, and if good reasons were given, the Court should permit a party to instruct its own expert.

Mediation

Under the CJR the Courts have a duty to encourage litigants to settle their disputes through the use of alternative dispute resolution ("ADR") procedures such as mediation. Practice Direction 31, which aims to assist the Courts in discharging this duty, became effective on 1 January 2010. In accordance with the Practice Direction all parties to Court proceedings (unless otherwise exempted) must at close of pleadings file a Mediation Certificate stating whether they are agreeable to mediation and, if not, the reason why.

Mediation can be particularly effective when the parties have an ongoing commercial relationship that it is in their mutual interest to preserve. The role of the mediator is not to impose a decision or to judge the merits of the case but rather to guide the parties to their own settlement. The result of a mediation will not necessarily represent the likely outcome of the case had there been a trial. The mediator helps the parties to achieve a settlement by focusing on what can be done to move forward rather than on who is at fault.

Parties will benefit from involving their experts in the mediation process. A quantum expert can provide a damages model into which potential concessions or compromises by one or other of the parties can be fed in order to determine the probable financial effect of the various settlement scenarios that might be explored during a mediation.

Conclusions

The key impact of the CJR on expert evidence is likely to be in relation to the amount of work that will need to be done at the outset of a potential litigation. The days when parties could delay instructing an expert until the eve of the trial are hopefully behind us. Experts should expect to play an enhanced role in giving pre-action advice; providing early views as to quantum issues under dispute; and assisting with the discovery process.

SJEs are unlikely to be a feature of complex commercial litigation. To the extent that SJEs are used in relation to highly contentious issues, this might lead to the emergence of shadow experts in Hong Kong thus adding to, rather than reducing, the total costs.

Statements of Truth are to be taken seriously and experts will need to carefully consider the appropriateness of declaring their belief in the truth of facts supplied by those instructing them.

The Court has a duty to encourage parties to use ADR procedures where appropriate. It will be necessary for experts and those instructing them to consider how their skills can best be applied in the ADR process.

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INDIA

Overcoming Anti-Corruption (FCPA) Challenges in India

BY ANAND S. DAYAL | KOURA & COMPANY

Cross-border investment transactions face many risks. These include opaque accounting practices, labour and environmental liabilities, pending and threatened litigation, and regulatory ambiguity. But perhaps the biggest risk may be violations of the US Foreign Corrupt Practices Act ("FCPA") and the Prevention of Corruption Act ("PCA") in India. Often there are existing violations or questionable practices that come to light only after the acquisition is complete. In addition to past violations, there is the risk of ongoing violations; given the prevalence in India of a culture of bribery. This article provides guidance on dealing with the legal issues in overcoming these challenges.

FCPA and Legal Framework in India

The FCPA contains anti-bribery and accounting control provisions. These provisions prohibit "US persons" from paying or offering to pay "anything of value" to any "foreign official" with the "corrupt purpose" of obtaining business. "US persons" is a term that is defined in the statute to include; all business entitles organised in the United States; all individual US citizens and residents; all companies listed on the US stock exchanges, including foreign issues; and foreign persons acting within the United States. The accounting control provisions apply only to publicly listed companies, which also include foreign issuers. This means that Indian companies who have issued American depositary receipts are also subject to the accounting control provisions of the FCPA.

Besides the FCPA, compliance with the anti-corruption laws in India is required. While there is a robust framework of anti-corruption laws and investigating agencies in India, their enforcement record is spotty, particularly against corruption in high places. Also, the scope and focus of Indian anti-corruption laws is different. Compared to the FCPA, Indian law is both under inclusive in some respects and over inclusive in other respects; which presents challenges in fashioning a compliance strategy. It is critical therefore to have an understanding of Indian anti-corruption laws and investigating agencies.

Prevention of Corruption Act, 1988

The Prevention of Corruption Act, 1988 deals primarily with curbing corruption within government agencies and authorities. It prohibits the taking of a bribe or any other gratification by a public servant. One of the objects of the 1988 Act (which is a re-enactment of earlier legislation) was to make the existing anti-corruption laws more effective by extending the scope of the term "public servant" by bringing within its sweep each and every person who holds an office by virtue of which such person is required to perform any public duty. In addition, the PCA

takes into its ambit any one who acts as a tout or intermediary in facilitating the offence of corruption.

To prosecute a public servant, it is necessary to obtain prior approval of the Central Government or State Government in the case of Central and State Government employees (as applicable) and, in the case of any other person, the authority competent to remove the accused from office. This approval requirement poses a significant challenge in prosecuting offences under the PCA. Corruption cases brought against high public officials inevitably become politicised, resulting in a dismal record of actual convictions in such cases. More successful are prosecutions against middle and lower level government employees, who often lack political patronage.

Investigation Agencies Dealing with Corruption

Central Vigilance Commission (CVC)

The CVC was established for the purpose of inquiring into and investigating offences under the Prevention of Corruption Act by certain categories of public servants of the Central Government, corporations established by or under any Central Act, government companies, societies and local authorities owned or controlled by the Central Government.

The CVC is comprised of a Central Vigilance Commissioner and not more than two Vigilance Commissioners. Their appointment is intended to be apolitical and bi-partisan. Accordingly, the Commissioners are appointed by the President of India upon the recommendation of a committee comprised of the Prime Minister, the Minister of Home Affairs and the leader of the opposition in the Lok Sabha (Lower House).

Chief Vigilance Officer (CVO)

At the organisational level, the vigilance function is discharged by the CVO in that organisation. The primary responsibility for maintenance of ethical purity, integrity and efficiency in the organisation vests, as the case may be, with the secretary of the concerned ministry, or the head of the department, or the chief executive of the public sector enterprise. Such person however is, in the discharge of vigilance functions, assisted by the CVO. The CVO acts as a special assistant or advisor to the chief executive, and reports directly to him in all matters relating to vigilance. The CVO heads the vigilance division of the organisation concerned and provides a link between this organisation and the Central Vigilance Commission and the Central Bureau of Investigation.

The Chief Vigilance Officers in all government departments and organisations are appointed after prior consultation with the Central Vigilance Commission, and no person whose appointment in that capacity is objected to by the Commission may be so appointed.

Central Bureau of Investigation (CBI)

The CBI was established in 1963, as the successor organisation to the Delhi Special Police Establishment (DSPE); but with an enlarged charter. The DSPE was made one of the six divisions of the CBI, namely the Investigation and Anti-Corruption Division.

Superintendence of the CBI/DSPE vests with the Central Vigilance Commission in so far as it relates to the investigation of offenses under the Prevention of Corruption Act, 1988. The CVC may give directions to the CBI/DSPE for purposes of discharging their investigative responsibilities. However, the CVC cannot require the CBI/DSPE to investigate or dispose of any case in any particular manner. The CVC may review the

progress of investigations conducted by the CBI/DSPE into offenses under the Prevention of Corruption Act, and it may review the applications pending with the competent authorities for sanction of prosecution under the said Act.

Directorate of Enforcement

The Directorate of Enforcement is responsible for enforcement of the Foreign Exchange Management Act, 1999 and the Prevention of Money Laundering Act, 2002. It is under the administrative control of the Department of Revenue in the Ministry of Finance.

The Directorate of Enforcement is not directly responsible for the enforcement of anti-corruption laws; that is the domain of the CVC. The Directorate however becomes indirectly involved in anti-corruption prosecution efforts because the payment and receipt of bribes often involves violations of the foreign exchange and anti-money laundering regulations. These violations are often easier to prove than offences under the Prevention of Corruption Act.

Compliance Challenges in India

Culture of Acceptance of Bribery

Corruption is often viewed as a normal part of the business process in India. Local partners are often not sensitive to the need for compliance with anti-corruption laws, and poorly trained employees may assume a "when in Rome" attitude. Although US companies may not be directly involved in such payments, they are nonetheless liable under the FCPA. The FCPA prohibits corrupt payments through intermediaries. Intermediaries may include joint venture partners or agents.

No Exception for Facilitating Payments

The FCPA contains an explicit exception to the bribery prohibition for "facilitating payments" to facilitate or expedite "routine governmental action". There is however no such facilitating payments exception under Indian anti-corruption laws. Bribery is not permissible under any circumstances. This means that certain conduct, which is acceptable under the FCPA, may violate Indian law. This creates a trap for the unwary.

Prevalence of Public Sector in Commerce

Public sector enterprises comprise a significant portion of industry in India, including the petroleum sector, the steel, nuclear and defence industries, larger banks and financial institutions, and the insurance industry. Given the size and scope of public sector activities, commercial dealings with and investments in public enterprises are common.

The officers and employees of public enterprises are "public servants" for purposes of the PCA and "foreign officials" under the FCPA. Accordingly, all commercial dealings with such enterprises whether as vendor, customer, joint venture partners and investors must be conducted such as to stay clear of prohibitions under these anti-corruption laws. Often innocuous actions, such as inviting prospective buyers to overseas factory visits to witness equipment tests, providing free product or services at festivals to employee groups within the public enterprise and routine business hospitality could raise anti-corruption compliance concerns.

Avoiding Corruption Liabilities

A significant number of anti-corruption enforcement actions have arisen in the context of a merger or acquisition involving non-US entities. Even without regulatory action, fraud and illegal acts pose a barrier to operational efficiency for a strategic or financial buyer. For a foreign investor, the post-acquisition discovery of a fraudulently enhanced revenue stream will not only erode company profitability but will also adversely impact exit realisation and internal rate of return.

To avoid being held liable for corrupt third party payments, US companies are encouraged to exercise due diligence and to take all necessary precautions to ensure that they have formed a business relationship with reputable and qualified partners and representatives. Such due diligence may include investigating potential foreign representatives and joint venture partners to determine if they are in fact qualified for the position, whether they have personal or professional ties to the government, the number and reputation of their clientele, and their reputation with the US Embassy or Consulate and with local bankers, clients and other business associates.

In addition, in negotiating a business relationship, the US firm should be aware of so-called "red flags", i.e., unusual payment patterns or financial arrangements, a history of corruption in the particular industry, a refusal by the foreign joint venture partner or representative to provide a certification that it will not take any action in furtherance of an unlawful offer, promise, or payment to a foreign public official and not take any act that would cause the US firm to be in violation of the FCPA, unusually high commissions, lack of transparency in expenses and accounting records, apparent lack of qualifications or resources on the part of the joint venture partner or representative to perform the services offered, and whether the joint venture partner or representative has been recommended by an official of the potential governmental customer.

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SINGAPORE

Singapore: An Insight into the eDiscovery Landscape

BY ROGER CLAY | ERNST & YOUNG

In common with countries like the United States, United Kingdom and Australia, Singapore recently published new rules to assist parties to litigation in managing their electronic discovery (e-discovery) requirements. Practice Direction No.3 of 2009 – Discovery and Inspection of Electronically Stored Documents, as an opt-in framework, provides legal practitioners and the courts with the necessary guidance when dealing with electronically stored information ("ESI") or electronically stored documents as referred to within the direction.

ESI differs from traditional "paper based" documents for a variety of reasons, some examples being; ESI volume ordinarily would be expected to be considerably larger, ESI is volatile and can be easily altered or deleted, ESI contains certain "hidden" information termed metadata including, for example, creation dates, authors, tracked changes and ESI offers additional searching and filtering options due to its electronic state.

During the e-discovery lifecycle a number of different phases of work exist. Briefly these are:

- *Information Management* – The proactive management of company records and information prior to the commencement of litigation.
- *Identification* – With reference to the scope of the matter being reviewed, the process of identifying where within the data universe and under whose custody, relevant information resides.
- *Preservation and Collection* – Preservation can be achieved through the use of hold notices or suspending data purging. Collection is the process of gathering the ESI for later processing and may include disk imaging, forensic data extractions or merely physically taking possession of a backup tape.
- *Processing, Analysis and Review* – During this phase the collected data is extracted into a useable format, filtered according to scope requirements i.e., date, keywords, author, etc., then hosted in a review platform for assessment as to relevance, privilege, confidentiality, etc.
- *Production* – Those documents relevant to the case, minus excluded material (i.e., privileged material) are produced to the opposing parties in litigation.
- *Presentation* – This involves the tendering of relevant documents as evidence before the court.

Singapore

Like a number of countries navigating their way through e-discovery issues, Singapore has relied on traditional protocols and case laws to provide guidance. As other countries have experienced, there is a gap between what traditionally is available as guidance and the requirement for new rules and protocols to assist in providing for smoother, less burdensome discovery.

With this in mind, Practice Direction No.3 of 2009 – Discovery and Inspection of Electronically Stored Documents came into effect on 1 October 2009. This direction, issued by the Supreme Court of the Republic of Singapore, is provided as an opt-in framework rather than a mandatory procedure and is one of the first such legal guidance documents issued within the Asia area.

One key focus of the direction is to encourage early collaboration and agreement on a discovery protocol. This includes the scope of the discovery, schedule, format of data and manner of delivery. If agreement cannot be reached, parties can apply to the court for an order. The court will require a draft protocol and evidence of good faith collaboration prior to making a determination.

Electronic discovery introduces a raft of complex issues which either did not exist or were not as serious when compared with traditional paper based discovery. One such issue is the burden which is attached to electronic discovery. The Singapore Practice Direction highlights the key factors which should be considered when balancing the requirement for discovery against the burden attached to it. Considerations include the value of the claim and the financial position of each party along with the complexity of the matter and the number of electronic documents involved.

As a general guide, depending on the platform used for review, it is expected that a reviewer can review between 1-2,000 items per day. An item includes an email, multipage document or any other electronic document one would expect to find. This might sound like a lot of information however 1 GB of email may contain around 10,000 items. This means it will take one person up to 10 days to completely review a 1 GB email container. It will be appreciated, therefore, that once discovery is extended to multiple custodians and archival data along with readily available information (such as live email), the cost of review time can add up sharply. Getting parties to focus on the burden of financial cost early in the case therefore allows them to make strategic assessments without having committed to an expensive course of action.

Specifically the direction recognises that on occasions discovery can be more costly for one side than the other. Although costs are to be borne by the party doing the discovery, the direction also acknowledges the courts' power to shift or apportion costs to prevent injustice or abuse of process.

Without regurgitating the Practice Direction in granular detail, it does cover a large number of the challenge areas faced by parties to litigation. This includes management of duplicate items, existence of privileged material, inspection of information and format of production copies. Of particular note however, the direction does recognise that file metadata may be of importance and also native copy production where required.

Although a relative newcomer in the world of electronic discovery when compared to the United States and United Kingdom, the Singapore courts have recognised the increasing need for parties to review electronic material and manage the challenges associated with it. Within the Asia region, Singapore markets itself as a premier location for commercial trade and arbitration. The release of the Practice Direction together with statutes and case laws shows that the Singapore legal system is flexible enough to recognise and address the growing and developing challenges of technology. Recognising and acting on these issues assists in reaffirming Singapore's strategic position in Asia as a regional business centre.

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An Overview of International Arbitration in Singapore

BY ALVIN YEO | WONGPARTNERSHIP LLP

Singapore has long been supportive of international arbitration. It ratified the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("New York Convention") in 1986. In 1991, it established the Singapore International Arbitration Centre ("SIAC"). In 1994, it passed the International Arbitration Act ("IAA") which adopted the UNCITRAL Model Law on International Commercial Arbitration ("Model Law") as law. Arbitration, as a method of dispute resolution, has also been favourably regarded by the Singapore courts which have consistently adopted a pro-arbitration stance. This article will provide an overview of these key aspects, namely, the SIAC, the IAA and the role of courts vis-à-vis international arbitration.

The IAA

The IAA defines an "international arbitration" as an arbitration where:

- at least one of the parties has its place of business outside Singapore;
- the subject matter of the dispute is closely connected with a country outside Singapore; or
- a substantial part of the contractual obligations is to be performed outside Singapore.

An arbitration agreement must be in writing. A clause in the main contract is sufficient, and electronic documents will be recognised. In addition, if a contract refers to a document containing an arbitration clause, this will be sufficient provided that the contract is in writing and the reference is such as to make that clause part of the contract.

The IAA does not specify any mandatory procedural rules, and parties are free to agree on the procedures to be followed by the arbitral tribunal in conducting the proceedings. If the arbitration agreement is silent, or parties are unable to agree on a set of procedures to apply, the default rules set out in the Model Law apply.

Singapore courts have recognised that arbitration is confidential in nature. Confidentiality is recognised as an essential corollary to privacy in arbitration and, accordingly, is a term that the courts will imply into the arbitration.

Unlike domestic arbitration where parties may seek to appeal to the courts on a question of law, for international arbitrations there is no right of appeal as such to a court against an award made by an arbitral tribunal. Under the IAA, an award may only be challenged by way of an application to have it set aside. The grounds for setting aside an award are:

- the party to the arbitration agreement was under some incapacity;
- the arbitration agreement is not valid;
- the party making the application was not given proper notice of the appointment of an arbitrator or of the proceedings and was unable to present his case;
- the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration;
- the composition of the arbitral tribunal or the arbitral procedure is not in accordance with agreement of the parties;

- the making of the award was induced or affected by fraud or corruption;
- the breach of the rules of natural justice has occurred;
- the subject matter of the dispute is not capable of settlement by arbitration; or
- the award is contrary to public policy.

As Singapore has ratified the New York Convention, an arbitral award made in Singapore will be enforceable in most other jurisdictions. To further assist in the enforcement of awards, as some foreign courts require that the awards be duly authenticated before allowing the awards to be enforced, the IAA has recently been amended to provide for the authentication of arbitration awards on a non-mandatory basis.

This amendment was among several others that came into effect on 1 January 2010. These came about as part of the Singapore government's practice of regularly reviewing the IAA to ensure that it remains relevant and up-to-date. The amendments also include the introduction of a new provision that gives the Singapore courts power to grant interim orders in arbitrations held outside of Singapore. The section specifically provides that the court will be empowered to make such orders whether or not it relates to a matter that is justiciable before a Singapore court. The orders that may be made include orders to freeze the assets of parties. This amendment brings Singapore in line with the position in the UK and New Zealand.

The SIAC

Since the establishment of the SIAC in 1991, it and Singapore have become increasingly popular choices in the region for international arbitration. From a mere 37 cases in 2000, the SIAC administered some 70+ cases in 2008. Part of the attraction would be due its panel of arbitrators who come from 30 countries spanning all five continents. This breadth of expertise is matched by its depth as many of the arbitrators on the panel are recognised worldwide as experts in their field. The Board of Directors of the SIAC is chaired by Professor Michael Pryles and both it and the SIAC's Council of Advisers are made up of international practitioners.

This level of expertise has meant that the SIAC has revamped its services, processes, and rules to match best practice in international arbitral institutions. The SIAC Rules were recently revised and updated and are increasingly being adopted in international transactions. The key provisions of the SIAC Rules provide as follows:

- Parties may nominate arbitrators, and their nominations are subject to confirmation by the Chairman of the SIAC. Failing agreement, the Chairman will appoint the arbitrators.
- The default seat of arbitration is expressly provided to be Singapore, although parties may agree on another seat of arbitration. Generally speaking, the seat of arbitration determines the applicable law of the arbitration. However, if the arbitration is to be conducted in Singapore, it is both simpler and more convenient for the law governing the arbitration to be Singapore law.
- The arbitration process is commenced by one party notifying the other and the SIAC that there is a dispute to be arbitrated. Upon the appointment of an arbitrator (or an arbitral tribunal) and the filing of statements by both sides, the arbitrator/tribunal is required to draw up a Memorandum of Issues. This memorandum will define the issues to be decided in the award. This practice, which is similar to that used in arbitrations conducted under the international arbitration rules of the International Chamber of Commerce ("ICC"), helps to narrow issues and also to plan the arbitration proceedings.

- The tribunal has wide powers to control and move forward the arbitral proceedings. These include ordering inspection and discovery, making interim orders and granting injunctive relief for the preservation of evidence and the freezing of assets, allowing other parties to be joined in the arbitration, making an award notwithstanding one party's default of compliance with the arbitral process, and ordering the provision of security.
- Once the tribunal has made a decision, a draft award must be drawn up and sent to Registrar of the SIAC for approval. This is similar to arbitrations conducted under the ICC, and the Registrar may draw the tribunal's attention to issues of substance.

The SIAC Rules also provide that the tribunal may rule on its own jurisdiction where the existence or validity of the arbitral agreement is disputed by one party. More recently, the Singapore Court of Appeal in *Tjong Very Sumito & Ors v Antig Investments Pte Ltd* [2009] SGCA 41 held that the arbitral tribunal, and not the court, is the proper authority for determining whether a dispute is a "dispute" within the meaning of the governing arbitration agreement.

The Role of the Courts

In *Tjong Very Sumito & Ors v Antig Investments Pte Ltd,* the Court of Appeal also emphasised that: "Courts should ... be slow to find reasons to assume jurisdiction over a matter that parties have agreed to refer to arbitration. It must also be remembered that the whole thrust of the IAA is geared towards minimizing court involvement in matters that the parties have agreed to submit to arbitration."

While the risk of a local court intervening to frustrate an arbitration is low, Singapore courts may and have intervened at the parties' request to *assist* arbitration proceedings. However, the courts' approach in this regard is that their processes not be used to bypass the arbitral tribunal or abused to gain a procedural advantage, but only to support the arbitration. Accordingly, as a general rule, the courts have indicated that their help should only be sought when "arbitration is inappropriate, ineffective, or incapable of securing the particular form of relief sought". Such situations include the following:

- where third parties over whom the arbitral tribunal has no jurisdiction are involved;
- where matters are very urgent; or
- where the court's coercive powers of enforcement are required.

Indeed, the Court's consistent pro-arbitration attitude was also expressed in another 2009 Court of Appeal decision, *Insigma Technology Co Ltd v Alstom Technology Ltd* [2009] SGCA 24 where it stated: "Given the inherently private and consensual nature of arbitration, our courts will ordinarily respect the principle of party autonomy and give effect to (workable) agreed arbitration arrangements in international arbitration..."

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MIDDLE EAST

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MIDDLE EAST

Arbitration and Mediation in the Arab World – A Growing Phenomenon

BY NASSER ALI KHASAWNEH AND VICKY SFEIR | KHASAWNEH & ASSOCIATES

Alternative dispute resolution (ADR) mechanisms in the Arab world have been growing hand in hand with the resurgence of various countries as members of the fast growing club of successful emerging markets. The flexibility of arbitration, mediation and other ADR methods, as well as their speed, efficiency and confidentiality, have made them more attractive to investors and parties in contracts of an international nature. Consequently, a significant number of Arab countries have been busy updating and enhancing their laws and regulations on arbitration and mediation in particular. There is momentum behind ADR in the region.

Furthermore, the global economic downturn has led to a significant increase in the number of disputes in various sectors, and this in turn has provided an impetus behind the need to enhance the procedures applied by the various arbitration centres in the Arab world.

This development is not solely linked to the realities of modern commerce. In fact, the conciliatory approach and the notion of deferring to a neutral and objective personality for a decision, that ultimately underline all forms of ADR, are well steeped in Arabic and Islamic traditions. There are at least two verses in the Koran that sanction the notion of arbitration and mediation. Furthermore, one of the most famous stories of the Prophet Mohammad's early life involved him being chosen by feuding tribes, who could not agree on a vital element of the reconstruction of the Ka'aba, to resolve the dispute. The Prophet bridged the gaps between the quarrelling parties by suggesting an original solution that was essentially a win-win for all. Other examples of arbitration and mediation abound in Islamic history.

At the outset let us distinguish between mediation and arbitration. There are a number of differences between those two mechanisms. Firstly, these methods differ in terms of the role of the appointed third party; in arbitration, an arbitrator is like a judge and his or her decision is final, whereas in mediation, the mediator works to try and bridge the differences between the parties and move them closer a settlement or conciliation. In a sense, mediation is the preferred option when the parties are still attempting to resolve their differences in a way that would allow them to continue their working relationship; whereas, arbitration is usually sought in order to reach a final determination on the overall dispute at the end of the relationship. Secondly, the authority of an arbitrator is much wider than that of the mediator. Thirdly, there are differences in terms of time limits, and venue considerations, between the two methods. In essence, arbitration is an attempt to replicate the judicial process but in a manner that is more specialised and streamlined. Mediation is a process whereby the parties agree to nominate a third party who would be tasked with trying to find common ground between the parties and resolve their differences, usually through the organisation of

meetings which are of a rather informal nature, at least in comparison with arbitration proceedings.

Finally, one of the main advantages of mediation is that it is far less costly than arbitration. In fact, it can be said that the costs of arbitration are its Achilles heel.

One of the most significant trends is the adoption of laws that deal specifically with mediation. In Jordan, the Law on Mediation for the Resolution of Civil Disputes was adopted in 2006. The law organises the process of judicial mediation that takes place at the Court of First Instance. In accordance with Article 3 of the said law, the presiding judge may, upon the agreement of the parties or further to their request, refer the dispute to a mediating judge or a private mediator for the purposes of amicable resolution of the dispute. The mediator is then obliged by law to complete the mediation process within three months of the date on which the dispute was referred to him or her.

A similar development has taken place in the Emirate of Dubai, in the United Arab Emirates. By virtue of Dubai's Law No. 16 of 2009, a Mediation Centre was established. The Mediation Centre will be annexed to Dubai's Courts. The Centre is entrusted to review types of disputes that are defined by its Chairman. Disputes will be reviewed and amicably resolved through a number of experts, under the supervision, of the concerned judge, within a period that would not exceed one month from the date of the attendance of the parties before the judge.

The creation of such centres in Jordan and the UAE, as well as the existence of various mediation mechanisms through international organisations such the World Intellectual Property Organization's Arbitration Centre, is likely to lead to a surge in the use of mediation as a method for the amicable resolution of disputes. This would be a welcome development, as it would entail the effective resolution of so many disputes in a conciliatory and timely manner, well before the matter escalates to reach a court room or an arbitration panel.

As for arbitration, we have also seen a number of positive trends in this regard in the Arab world. On the one hand, the trend towards the effective adoption of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Arbitration Convention) has solidified. The New York Arbitration Convention mainly enshrines the principle that a properly made arbitration award in one member country must be binding and enforceable in another member country, unless the award can be rejected on the basis of certain grounds for refusal of enforcement, which are narrowly defined in the Convention. The Convention also confirms the principle that if a court is presented with a dispute which the parties had agreed to refer to arbitration, then the court must refer the matter to arbitration upon the request of one of the parties.

Historically, the rate of adoption of the New York Arbitration Convention in the Arab world has been good. Jordan was amongst the first countries to adopt the Convention, which came into effect in 1959. Almost all Arab countries have since joined, with Kuwait joining in 1978, Saudi Arabia in 1994 and, more recently, the United Arab Emirates in 2006.

The challenge is to ensure that the exceptions that would allow a member country to refuse the enforcement of an arbitral award are applied in a strict and narrow manner. Under Article V(2)(b) of the Convention, the enforcement of an arbitral award may be refused if "the recognition or enforcement of the award would be contrary to the public policy of that country". The parameters of what a country regards as "public policy" can be wide. In Saudi Arabia, an arbitration agreement or award is respected provided that it is not contrary to the principles of Shari'a law. Such a limitation falls within the "public policy" exception, but the key lies in the way such an exception is applied.

In the UAE, Articles 235 and 236 of the Civil Procedures Law (Federal Law No. 11 of 1992) confirm the principle that foreign arbitral awards will be enforced in the country, provided a number of conditions are met. These include procedural issues such as the proper notification and representation of the parties before the arbitral tribunal that

issues the decision in the foreign country. Also, UAE courts may refuse the enforcement of a foreign arbitral award if it contradicts a previous judgment already issued by a UAE court or if it includes elements that "contradict public policy or morals".

While in the past "public policy" exceptions have been defined in a wide manner that allowed courts to reject a number of foreign arbitration awards in various Arab countries, there is a discernible trend towards limiting the use of this exception, and applying it only in clear cases of contravention of the country's moral or public policies.

Furthermore, in the recent past, various Arab countries have upgraded their arbitration laws to be in line with international best practices. This is evidenced by the increasing use of the United Nations Commission on International Trade Law (UNCITRAL) Model Law on International Commercial Arbitration. This model law was drafted by the UNCITRAL with a view to assisting countries that seek to improve their laws in such a way as to ensure the best possible procedures for commercial arbitration. For example, Egypt adopted Law No. 27 in 1994, the Commercial Arbitration Law, which is based on the UNCITRAL Model Law. This aimed to enhance arbitrations procedures and resolve complications that arose under the provisions that dealt with arbitrations in the Egyptian Code of Civil and Commercial Procedures and provide a law dedicated to arbitration. Also, in 1994, Bahrain adopted a new international arbitration law (Decree no. 9/1994) that was based on the UNCITRAL Model Law. In 2008, Syria issued an arbitration law that is based on the Model Law as well.

The UAE is also presently considering a new Federal arbitration law and it is widely reported that the new law would be based on the UNCITRAL Model Law. Once enacted, the new Federal arbitration Law will replace the existing provisions in the Civil Procedures Law.

Finally, there is no greater proof of the growing popularity and importance of arbitration than the increasing use of existing arbitration centres in the region, and the founding of new centres. The Dubai International Arbitration Center (DIAC), whose rules are UNCITRAL based, has proven to be an excellent success. The number of cases that the DIAC is handling has been growing at a very impressive rate. According to one report, while the number of new cases with the DIAC in 2008 was 100, there had been 180 new cases registered with DIAC by August 2009. The Cairo Regional Center for International Commercial Arbitration, which was established in 1979, continues to be a great success.

Earlier in January, Bahrain announced the launch of Bahrain Chamber of Dispute Resolution, in partnership with the American Arbitration Association. It is reported that the Chamber will operate what is being called an "arbitration free zone."

In conclusion, various Arab countries have engaged in an active process of upgrading their arbitration laws and those dealing with other alternative dispute resolution mechanisms. Arab arbitration centres are growing in significance, as more parties resort to the use of their services. These important developments can only serve to facilitate the infrastructure supporting international commercial contracts in the Arab world and, in turn, this will have very positive effects on investment and business growth in our region.

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UNITED ARAB EMIRATES

Alternative Dispute Resolution in Dubai

BY CHRISTOPHER MILLS AND ALEXANDRIA TILL | CLYDE & CO LLP

Mandatory Requirement to Attempt an Amicable Settlement

Law Number 16 of 2009, "Establishing the Centre for Amicable Settlement of Disputes" (the "Law"), was issued by Sheikh Mohammed in his capacity as the Ruler of Dubai in September 2009 and established the Centre for Amicable Settlement of Disputes (the "Centre"). The Law became effective from the day of promulgation and publication in the official gazette; however, in practice the Centre is not yet operational. The Law as promulgated, applies to those disputes under the jurisdiction of the Courts of Dubai, and thus excludes the DIFC Court.

Containing 16 articles, the Law creates a mandatory requirement for the Centre to examine disputes, whatever be their nature or values involved. Pursuant to the Law, no dispute that falls under the Centre's broad ambit will be filed before a court of law until it is tried by the Centre (Article 6). Those cases to which the government is a party, and/or necessitating a temporal order or summary proceedings will be exempted. Also exempted will be cases that do not fall under the existing jurisdiction of courts and those filed before the issuance of this law (Article 4).

The party filing the dispute will be required to pay a fee, yet to be set. Half of such fee will be returned where amicable settlement is reached. Upon filing, the limitation periods for the matter will be suspended (Article 9).

The Law stipulates that the disputes will be presented before the Centre, where a panel of competent jurists led by a judge will try to settle them amicably (Article 5). The Centre will summon the disputing parties or their legal attorneys, will study their documents and exhibits as well as other evidences, and offer reconciliation between them for reaching an amicable settlement of their disputes. The panel may also call on other experts to submit their opinion on technical matters (as to which the parties will bear the cost burden of- Article 11).

The Centre will review the matter and give a decision, in the form of a "reconciliation order" within one month of the date that the litigants appear before it. The Law does not provide details on whether this date accrues from the first meeting of the parties or the last, and it is expected that such information will become apparent through the procedures to be issued by the Chairman of the Centre (Article 8). It is understood that the reconciliation order can be accepted at face value, or negotiated, and is enforceable once signed and approved by a competent judge (Article 12). In the event that the parties do not settle, the dispute shall be transferred to a court of competent jurisdiction to issue judgment (Article 13).

While the concept of amicable settlement prior to the issue of formal proceedings is not new to the UAE, the mandatory requirement to participate in the same is. For example, many cases coming before federal judges are first referred to a conciliation desk (those cases arising in the Emirates of Dubai and Ras Al Khaimah are exempt). However, in such a case, the respondent to the dispute can elect to participate in the conciliation or proceed

straight to litigation.

The mandatory nature of the Centre combined with the absence of an appointed Chairman and procedures for the Centre being promulgated, creates a large number of unresolved issues relating to the Centre. Foremost of these is the lack of clarity surrounding the issue of fees and costs associated with the Centre, and who will bear the burden of these. It is also not clear what powers the Centre and those appointed to it will have with regard to disclosure of documents, and what will occur to those parties that are in contempt of the Centre and its procedures.

In an effort to combat the lack of information currently available, we are aware that cautious advocates are addressing letters of application to commence proceedings to the Centre but that the Courts are currently stamping the same and instructing the advocates to register the case as normal before the Court Registration Section. This procedure will assist in defending any arguments that the case should be dismissed as the matter has not been referred to the Centre in accordance with the procedure set out in the Law.

Mediation

Mediation is a voluntary, non-binding, and private dispute resolution process in which a trained neutral person – the mediator – helps parties to a dispute, or other impasse between them, try to reach a negotiated settlement for themselves, with or without the assistance of their own professional advisers.

Mediated settlement can only come about on the authority of the parties concerned as the mediator has no authority to make a binding determination. If a settlement is reached, the agreed terms may form part of an enforceable contract.

Many of the well known institutions which deal with dispute resolution have mediation procedures, for example, the Centre for Effective Dispute Resolution ("CEDR"), the International Chamber of Commerce ("ICC") and the London Court of International Arbitration ("LCIA").

Alternatively, the parties are able to agree on their own procedure and terms, which are set out in an ad-hoc Mediation Agreement and which include terms empowering the mediator to, for example, direct timeframes and extensions of time, instruct on the submission of documents and detail costs.

Whilst mediation is extremely common in the United Kingdom and United States, it has only recently gained popularity in Dubai and the UAE. In particular, international companies familiar with the additional costs and time incurred in proceeding to arbitration or other legal processes are moving towards mediation as a viable option. The success of mediation does, however, rely on the skills of a mediator to successfully negotiate a resolution and the commitment of parties to settle their conflicts.

The Government of Dubai identified property disputes as an area which could benefit from mediation and as such a "Special Judicial Committee" (which had been referred to in the Media as a Mediation Centre) was established by Law No.30 of 2007 to resolve real estate disputes. Due to the large influx of cases it received, the Committee could not process the cases in a timely manner.

Law No. 28 of 2008 addressed the above referred situation by granting authority to the Real Estate Regulatory Authority (RERA) to determine Real Estate disputes (as referred to in Article 11 of the Law No.13 of 2008, and amended by Law No. 9 of 2009) prior to their review by the Courts.

Subsequent to the promulgation of Law No.13 of 2008 as amended by Law No. 9 of 2009, RERA have attempted to play the role of an informal mediator in property disputes- seeking an amicable outcome for

both parties. This has had mixed results, in part, due to the lack of policy governing mediation and the varied grounds by which RERA suggestions are made. It is hoped that the Executive Regulations to Law No.9 of 2009 will provide greater clarity to the Real Estate Community. These were expected to be released in 2009 but have been delayed.

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Arbitration in Dubai

BY CHRISTOPHER MILLS AND ALEXANDRIA TILL | CLYDE & CO LLP

Arbitration as a forum for alternative dispute resolution in the Emirate of Dubai continues to grow. The Dubai International Financial Centre London Centre for International Arbitration (DIFC-LCIA) and Dubai International Arbitration Centre (DIAC) have both seen a dramatic rise in cases.

This article does not explore the different considerations that should be given to drafting clauses for arbitration in Dubai, but rather looks to the steps required to navigate the proceedings once arbitration has commenced, and the ratification and execution of the Award once rendered.

Arbitration in Dubai is protected by, and in the absence of any other rules referred to in the arbitration clause is governed by, Articles 203-218 of Federal Law No.11 of 1992, The Civil Procedure Law of the UAE (the "Law"). Once an arbitration is underway (in accordance with the Law or the rules of the clause), the proceedings are protected by Article 203 (5) of the Law. This provides, in translation into English, that: "If litigants agree to arbitrate a dispute, no case may be lodged for such dispute before the Courts. Nevertheless, if a party lodges a case without considering the arbitration clause and the other party does not object at the first hearing, the case may be heard and the arbitration clause shall be considered null and void."

If a party wishes to rely upon an arbitration clause, as a defence to proceedings commenced against them in the UAE courts, they must raise a jurisdictional defence at the first hearing and seek an Order to stay the proceedings. If they fail to do so they will be seen as having accepted the jurisdiction of the courts and the arbitration clause will be deemed waived.

There are also regulations concerning arbitration and disputes arising out of contracts to which the Dubai Government or any of its subsidiary departments is a party. These are set out in Law No.6 of 1997 (for example, Government departments must seek leave of the Ruler prior to entering into international arbitration).

For those who are drafting arbitration clauses, it is important to note that a draft Arbitration Law has been circulated, but is not yet in force. We would recommend that parties check the status of the draft law, prior to finalising clauses. While the UAE is not among the countries in the region that have adopted the Model Law of the United Nations Commission on International Trade Law for Arbitration (the UNCITRAL Model Law), a review of the translation into English of the draft law leads us to believe that the drafters of the UAE Arbitration Law have looked at the UNCITRAL Model Law for some guidance in their drafting.

Ratification and Execution of an Award issued in the UAE

Pursuant to paragraph 1 of Article 217 of the Law an "Arbitrator's rulings may not be contested in any way". Notwithstanding this, there are a number of steps that must be undertaken prior to an Award being able to be relied upon in, Dubai and the UAE.

An Award must be ratified in order for it to have the standing of a final judgment. The process of conversion occurs through the Court of First Instance. An application for ratification of the Award is made to the Court through the normal process of submitting a Statement of Claim along with supporting documents to be filed and the court fee. The Court will then review the papers, and consider the application. This review process may take a number of hearings, particularly if the application is contested.

Should an opposing party wish to contest the application, they can apply to have the Award annulled. Consideration is supposed to only be given to those challenges that are procedurally based, as opposed to merit based challenges. An opposing party is able to contest an Award pursuant to Article 216 of the Law at paragraphs 1 and 2. An excerpt from which states: "1...(a) If [the Award is] given without a deed of arbitration or if based on an invalid deed, or if lapsed through prescription, or if the arbitrators have exceeded the limits of the deed. (b) If the ruling has been given by arbitrators not appointed according to the law, of if given by some of them without being so empowered in the absence of the others, or if given under a deed of arbitration in which the subject of the arbitration is not stated, or if given by someone not competent to agree to arbitration or by an arbitration who does not fulfil the legal requirements. (c) if there is something invalid in the ruling or in the procedures affecting the ruling."

Article 210 (1) further states that in the absence of an agreed time limit, that an Award shall be rendered within 6 months of the first hearing. Should an Award not be rendered in this time frame the parties may file a dispute in the Court of First Instance.

In order to prevent the above listed challenges, prior to an application for ratification being made, a check should be made:

- that the time limits stated, if any, within the arbitration clause or rules were adhered to. In the event there was no limit, and the parties did not agree to an extension, that the Award was rendered within 6 months of the first hearing.
- that the Award is delivered, signed, to the parties no less than 5 days from when the Award is issued by the arbitrator.
- on the authority of the individual issuing the power of attorney (POA), ensuring they had the ability to enter Arbitration and delegate the same to the lawyers engaged;
- that the Award has been signed on each page by those issuing it;
- that the Award has been issued in the UAE, pursuant to Article 212 (4) of the Law; and
- that other challenges have been considered (including those related to: witness testimony, time extensions, issue of the Award within the 6 month time frame, proportionate sums/costs awarded, and whether an independent expert reviewed the party appointed experts statements etc.).

It should be remembered that as ratification can only occur through the court, while judgment at the Court of First Instance level is considered "final" for enforcement purposes, the opposing party holds the ability to automatically appeal the judgment to the Court of Appeal.

Once the Award has been ratified, an application for execution can be made. This procedure takes place in a separate department of the Court. Judges are specifically assigned to the Execution Court assisted by an Execution Bailiff and administrative staff at the Execution Department to administer the execution and enforcement of judgments and orders including the provision of notice to the other party that the Award is to be enforced.

Ratification and Execution of a Foreign Award

Article 235(1) of the Law provides: "Judgments and orders issued in a foreign country may be executed in the UAE in the same conditions prescribed in the law of that country to execute the judgments and orders issued in the State."

While historically difficult to ratify and execute a foreign award in the UAE, the UAE is now a signatory to the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, the International Convention for the Settlement of Investment Disputes (more commonly known as ICSID), the Agreement on Enforcement of Court Judgments, Delegations and Judicial Notices in the GCC States and the Riyadh Judicial Cooperation Agreement. Furthermore, the UAE has a number of bilateral arbitration enforcement arrangements in place with, amongst others: India, France, Egypt, Jordan and Syria.

Ratification of a foreign award is carried out through the same process as ratification of a domestic award, however, the likelihood of it being successfully ratified (and executed) without challenge will vary, depending on whether the country of issue is a member to any of the bilateral treaties referred to at paragraph 2.3.1.

Judges tend to ensure, during the ratification process, that an arbitration award satisfies UAE procedural law, as well as foreign procedural law. Further, the court will often ensure that the losing party was properly summoned to attend the hearing, and that service was properly given, especially where the arbitration award was given in default. The court will also require cogent evidence that the foreign award is final and good for execution before the court of the country in which the award was made. Should they desire, often UAE Courts can rely upon Article 20 of the Law to ensure they have jurisdiction: "With the exception of real actions (actions in rem) concerning real estate located abroad, [UAE] courts shall have jurisdiction to hear actions lodged against a national and a foreigner having domicile or place of residence in the State."

As long as this remains the case, enforcement of foreign awards in the Dubai Courts will be fraught.

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Litigation in the United Arab Emirates – Are You or Your Client at Risk?

BY CHRISTOPHER MILLS AND ALEXANDRIA TILL | CLYDE & CO LLP

A contract or bill of lading containing a law and jurisdiction clause providing for any disputes to be resolved in a particular forum, will not necessarily protect your client from litigation in the United Arab Emirates (UAE) or the jurisdiction of the Courts therein. UAE courts guard their jurisdiction jealously and the jurisdiction of the UAE

courts is a matter of public policy.

For example, both Federal Law No.26 of 1981 (the Maritime Code) and Federal Law No.11 of 1992, The Civil Procedure Law of the UAE (the "Law") contain provisions dealing with jurisdiction. Put simply, this means that if the event giving rise to a dispute involves a connection with the UAE, it is likely that a claimant will be able to invoke the jurisdiction of the UAE courts unless governed by an arbitration clause.

Should you or your client be involved in a dispute in which the UAE Courts would have jurisdiction, it is important to understand some of the costs that may be incurred. This article briefly outlines how jurisdiction of the courts is determined and the basic level of costs that can be expected should proceedings be initiated in Dubai.

Jurisdiction

The UAE Courts tend to guard their jurisdiction jealously (Federal Law 11 of 1992, Articles 20-22 of the Law (The Civil Procedure Code)). For example, the presence of the assets of a defendant in the UAE, in many cases, will be grounds for the UAE Courts to seize themselves of jurisdiction in a case.

In summary, pursuant to Article 21 of the Law, the UAE courts will assume jurisdiction when:

- one of the parties is domiciled in the UAE;
- the claim concerns an asset which is located in the UAE;
- the claim concerns a contract under which the contractual obligation should have been or was performed, concluded, executed, completed or relevant payments were made in the UAE;
- the claim is in respect of insolvency, which has been declared in the UAE;
- the claim is against a UAE national or expatriate who is domiciled in the UAE; and
- the claim concerns a party who is employed in the UAE.

Within each of the seven emirates of the UAE there are two types of courts:

- Civil courts which broadly have exclusive jurisdiction over civil, commercial, banking and maritime matters; and
- Sharia courts broadly have exclusive jurisdiction over family law matters.

However, both the civil courts and the Sharia courts have non-exclusive jurisdiction in respect of criminal proceedings although (in practice) most criminal matters are heard by the civil courts.

In both sets of courts, the codified provisions of the law of the UAE will apply. However, in the absence of any specific legislation, Islamic Sharia will be applied. Since it is likely that the majority of practitioners reading this article will only, if ever, be involved in the civil courts, the article will concentrate on the civil courts.

The local court at the place where the defendant is to be found will always have jurisdiction for the proceedings. Occasionally, however, it may be perceived to be in claimants' interest to issue proceedings in their own country. One of the obvious advantages to issuing proceedings in, for example, England, is familiarity with the English legal system and recoverability of costs incurred in a successful action. The pursuit of proceedings outside the country of domicile of the defendant, however, may not achieve the desired result because there may be no reciprocal agreement with the UAE for the execution of judgments obtained in the foreign country. The UAE has bilateral agreements with few countries outside of the GCC region.

Execution of Foreign Judgments

Should the UAE courts not have jurisdiction, and/or a judgment is received elsewhere, the UAE courts will, in certain circumstances, recognise a judgment of a foreign court if the criterion set out in articles 235-238 of the Law are met as follows:

- that the UAE courts did not have jurisdiction in the dispute;
- that the foreign court had the requisite jurisdiction under the applicable international rules to hear the dispute;
- that the defendant in question had been summoned to appear and had duly appeared before the foreign court;
- that the judgment is final under the law of the court issuing the same; and
- that the judgment does not conflict with any judgment or order previously issued by a UAE court and is not contrary to the public morals or order of the UAE.

Whilst Article 235 (1) of the Law provides that foreign judgments or orders may, in principle, be enforced in the UAE courts on a reciprocal basis, Article 235 (2) sets out certain minimum requirements which must be met. It is these requirements which often prove to be a stumbling block in the enforcement of a foreign judgment. Article 235 of the Law provides, in the translation into English: "(1) Judgments and orders issued in a foreign country may be ordered to be enforced in the State of the United Arab Emirates on the same conditions as prescribed in the laws of that country for the enforcement of similar judgments and orders issued in the State. (2) An enforcement order shall be applied for under normal litigation procedures to the Court of First Instance within whose jurisdiction the enforcement is required. Enforcement may not be ordered until the following has been verified: (a) That the State courts do not have jurisdiction in the dispute in which judgment has been given or the order made, and that the foreign courts which issued it have jurisdiction therein under the international rules for legal jurisdiction prescribed in their laws; (b) That the judgment or order has been issued by a court having jurisdiction under the laws of the country in which it was issued; (c) That the opposing parties in the case in which the foreign judgment has been given have been summoned to appear, and have duly appeared; (d) That the judgment or order was final under the law of the court which issued it; (e) That it does not conflict with a judgment or order previously issued by a court in the State and contains nothing in breach of public morals or order in the State."

Attempts to enforce a foreign judgment against assets of a defendant that are situated in the UAE tend to fail on the jurisdictional grounds found in 235 (2) (a), because the UAE Courts would often regard themselves as having had jurisdiction to hear the original claim. For this reason, the enforcement of foreign judgments is nearly always unsuccessful.

Codified System of Law

The UAE has a codified system of law. The core codes, which will deal with most international trade, shipping and commercial disputes, are:

- Federal Law No.11 of 1992, the Civil Procedure Law of the UAE
- Federal Law No. 5 of 1985, the Civil Code of the UAE
- Federal Law No. 26 of 1981, the Maritime Code of the UAE (the Maritime Code)

- Federal Law No. 18 of 1993, the Code of Commercial Practice
- Federal Law No. 10 of 1992, the Law of Proof and in Civil and Commercial Transactions (Law of Evidence)
- Federal Law No. 3 of 1987, the Penal Code of the UAE
- Federal Law No. 35 of 1992, the Penal Procedures Code

Litigation procedure in the UAE is governed by the Civil Procedure Code and the Law of Evidence. The Penal Code plays a more active role in the litigation framework than in many common law countries due to the overlap between civil and criminal causes of action in the Middle East (for example, a bounced cheque is a criminal offence). Familiarity with the aforementioned Codes is required in order to progress substantive claims.

Timescale

There are three stages in the litigation process in UAE. The first stage is the Court of First Instance. There is an automatic right of appeal to the Court of Appeal. Finally, the highest court (depending on which jurisdiction the action is being brought) is the Court of Cassation or Federal Supreme Court. In Dubai, it is the Court of Cassation. This final court, however, will hear issues relating only to matters of law, and not matters of fact.

The time scale will vary between Emirates but in Dubai it is possible to obtain an enforceable judgment in one year to 18 months. In general, we would expect that a minimum of six months and a maximum of 12 months is required to obtain a Court of First Instance Judgment, depending on whether the court decides to appoint an expert to review the evidence and provide a report to the court.

If a judgment of First Instance is appealed, Courts of Appeal would normally take between 3 and 6 months to render a judgment. As mentioned above, on points of law, it is possible to make a final appeal to the Court of Cassation, which could take a further two to three months to hand down a final judgment.

It is also worthwhile highlighting that the execution of a final judgment can also, sometimes, be time consuming, notably when there is a need to file an application to request that attached assets belonging to the losing party are sold at an auction.

Court Fees and Other Costs

Approximately 3.75% of the amount of the claim, subject to a maximum of AED15,000 must be paid to the Court to initiate an arrest or attachment in Dubai.

For substantive proceedings, the court fees in Dubai are 7.5% of the amount of the claim with a cap of AED30,000. In the other emirates, the court fees on the arrest are only AED1,000 and for the substantive suit the fee is 5% of the amount of the claim with a cap of AED30,000.

Court fees paid by a successful litigant may be recoverable from the losing party as part of the judgment.

Lawyers' Fees

Unfortunately, lawyers' fees are not recoverable, save to an entirely nominal extent (perhaps the equivalent of a few hundred dollars).

Translation Fees

As Arabic is the language of the Courts, all documents should be submitted in Arabic, with the translation completed by a Ministry of Justice approved legal translator (typically AED100-150 per page). The cost of translation is generally not recoverable in proceedings.

Court-appointed Experts

Appointed Judges have the discretion to appoint an Expert to assist them in the review of the subject matter including: documentation, contract documentation and to meet the parties to establish the background facts. The court expert will be directed by the court to produce a report in respect of liability and quantum. In our experience, the recommendation of the court expert is highly influential and invariably becomes the decision of the court. However, it can take many months for the expert to carry out his investigations and produce a report. Court appointed Experts are paid for by the parties to the dispute.

Bearing the above in mind, it is important when a dispute arises between contracting parties, that litigation and the costs involved therein are considered as an option but not the sole option.

Conclusion

Bearing the above in min d, it pays to know where the companies that you are doing business with are domiciled, and to consider where you are executing your contracts. When disputes occur, do not presume because a governing law clause will protect you, check the geography of the incident itself... and if in the UAE review the above again.

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SYRIA

Arbitration in Syria

BY NAYIRI BOGHOSSIAN| KHASAWNEH & ASSOCIATES AND HUSSEIN KHADDOUR | SYRIAN LEGAL BUREAU

Arbitration as a dispute resolution mechanism applies to both national and international transactions. However, it is more commonly used for various reasons in contracts of an international nature. The main argument in support of arbitration in international contracts is the fact that parties belong to different jurisdictions. Hence, they tend to prefer arbitration over the judicial route as one party may not trust the neutrality and the capacity of the court systems of the other. In such circumstances, the parties would opt for arbitration as they perceive it to be a more adequate mechanism to judge their conflict. Of course, one should add to that the fact that arbitration is, generally-speaking, a faster method of dispute resolution compared to the judicial track, or at least it should be.

Due to the international nature of arbitration, there have been legislative instruments dealing with arbitration in the form of international conventions or model laws. International conventions aim at ensuring enforcement of arbitral awards issued in another country while model laws provide an example that a country can follow while issuing its national arbitration law. This has been the case with Syria where the legislature has recently issued the Arbitration Law no. 4 of the year 2008 ("Law"). Syria chose the UNCITRAL Model Law on International Commercial Arbitration as a basis to draft the Law (in fact, the Law replicates the Model Law in almost every aspect but includes certain differences, the examination of which is beyond the scope of this article). Even though the Law is relatively recent, the concept and practice of arbitration in the country dates back a few decades. In fact, legislation governing arbitration has been in place since the 1950s as part of the Procedures Law no. 84 year 1953. But the Syrian legislature, in line with the trend towards modernising the laws in the country during the last few years, issued a law specially governing arbitration. This move was necessitated by Syria's desire to encourage foreign investment. A country wishing to penetrate the international business arena must adapt its dispute resolution systems to international standards and expectations. The adoption of the Law reflects the moves that the country is making towards economic liberalism. It was necessary for the country to update, upgrade and enhance its arbitration provisions in order to take them from the realm of national arbitration, applicable to contracts among local parties, to the international realm where it would be applicable to contracts of an international nature.

When we look at previous legislation governing arbitration, we note articles 506 to 534 of the Procedures Law. The Law cancels these articles and replaces them. Under the definitions chapter, we note that the Law extends the application of the Law to international commercial arbitration by stating the conditions under which arbitration would be considered international. The Law then clearly states that it applies to all arbitration proceedings which take place in Syria and to international commercial arbitration proceedings which take place abroad, if the parties choose to apply the Law. This broadening of scope is the one of the most salient features of the Law as the previously

applicable provisions under the Procedures Law lacked such a provision. They did not touch upon what constitutes an international commercial arbitration and stipulated that the award should be issued in Syria. Otherwise, it would be treated as a foreign verdict. Under the Law, international commercial arbitration is arbitration where the subject of the dispute is related to international commerce, even when the arbitration proceedings take place in Syria. This occurs in one of many instances; if the principal place of business of the parties are located in different countries, if the parties are located in the same country but the arbitration seat, or the execution of a substantial part of the contract, or the location that is the most closely linked to the dispute is outside the country of common residence of the parties, or if the dispute is linked to more than a country.

The Law is a comprehensive piece of legislation as it examines all aspects related to arbitration. It covers issues related to the form and conditions of an arbitration agreement, the composition, appointment and challenge of the arbitral tribunal. It covers in detail the conduct of arbitral proceedings, the form and content of the award, recourse against it and the execution thereof. The Law also includes a chapter on arbitration centres. It allows the creation of permanent arbitration centres in the country.

As mentioned above, the Law replaces articles 506 to 534 of the Procedures Law. However, the Law stipulates that arbitration agreements that were concluded prior to the entry into force of the Law shall continue to be subject to the provisions that were in place on the date of their conclusion, i.e., the articles set out in the Procedures Law.

The Law states that it does not apply to disputes relating to contracts of the administration, which should remain subject to the provision of article 66 of the Contracts Law no. 51 year 2004. This does not exclude arbitration in administrative contracts, as arbitration was introduced in connection with many of the public sector contracts through previous legislation.

Syria has also been a member of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards which was executed in 1958 ("New York Convention") and aims at ensuring recognition of arbitral awards in a manner that does not discriminate against foreign arbitral awards and ensures non-domestic arbitral awards are enforced within a member country in the same manner as national awards. In addition, Syria has also concluded bilateral agreements with many countries for the execution of arbitral awards.

The issuance of the Law is a further sign of Syria's commitment towards reinforcing and encouraging a modern business environment, and a further step towards enhancing Syria's legal environment in line with international standards. The implementation of the Law combined with the legal heritage of Syria, where arbitration rules have been in place for half a decade now, as well as the adherence of Syria to the New York Convention and other international agreements, will ensure that the practice of arbitration is improved over the next few years. It is necessary now to put in place arbitration centres that have sufficient resources both in terms of financing and expertise. It is very important to choose carefully the panel of arbitrators to be appointed to ensure they are well versed in the world of international arbitration. If careful steps are taken towards the creation of arbitration centres that meet the international standards and the necessary environment is developed in the country, we do not see a reason why Syria cannot have a national centre that would become one of the best arbitration centres in the region.

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AFRICA

SOUTH AFRICA

Constitutional Court of South Africa Lends Strong Support to Arbitration

BY JOHN BRAND AND EMMYLOU WEWEGE | BOWMAN GILFILLAN

The South African Constitutional Court has held that section 34 of the South African Constitution does not apply to arbitration and the Court has given strong support to arbitration.

Section 34 of the South African Constitution states that "everyone has the right to have any dispute that can be resolved by the application of law decided in a fair public hearing before a court or, where appropriate, another independent or impartial tribunal or forum".

The Supreme Court of Appeal had previously considered the application of section 34 in private arbitration in the case of *Telcordia Technologies Inc v Telkom SA Ltd 2007 (3) SA 266 (SCA)*. Harms JA held that although section 34 does apply to private arbitration, when parties agree to arbitration, to that extent they waive their rights in terms of section 34. In reaching this conclusion he referred to the judgment of the European Court of Human Rights in *Souvaniemi v Finland (ECHR case number 31737/96)* which held that Section 6 of the European Convention of Human Rights is applicable to private arbitration.

Case: Lufuno Mphaphuli and Associates (Pty) Ltd v Andrews and Another 2009 (6) BCLR 527 (CC); CCT 97/07) [2009] ZACC 6; 2009 (4) SA 529 (CC)

Lufani Mphaphuli and Associates (Pty) Ltd, an electrical infrastructure contractor, was the main contractor on an Eskom project for the electrification of certain rural villages in Limpopo. Mphaphuli subcontracted some of the work on the project to Bopanang Construction CC. Bopanang vacated the site early and a dispute arose between the parties concerning the work undertaken by Bopanang and whether either party was liable to make payment to the other.

During April 2003 Bopanang issued a High Court summons claiming payment for work done and also launched an urgent application for a temporary interdict preventing Eskom from paying Mphaphuli. The proceedings were settled on the basis that an interim interdict would be issued and that the dispute between the parties would be referred to arbitration. In October 2003 the parties entered into a written arbitration agreement. On 23 August 2004 the arbitrator published his award in favour of Bopanang. Bopanang applied to the High Court to have the award made an order of court. The application was opposed by Mphaphuli, which also filed a counterclaim to have the award set aside. A primary argument by Mphaphuli was that the arbitrator had held "secret meetings" with Bopanang and therefore, it had not been accorded a fair and impartial hearing. The High Court and the Supreme Court of Appeal found in favour of Bopanang.

Mphaphuli appealed the decision to the Constitutional Court. The court dismissed the appeal and upheld the award. The majority judgment was delivered by O'Regan ADCJ. She held that section 34 has no direct application to private

arbitration. In deciding this she drew a distinction between the wording of section 34 and the manner in which private arbitration is conducted. Private arbitration is ordinarily not held in public, nor can it ordinarily be said that arbitrators have to be independent in the way that courts and tribunals must be.

As there is no direct application of section 34, by choosing private arbitration, the parties do not waive their rights in terms of section 34 but instead choose not to exercise them. Despite this, she held that the Constitution was still relevant to private arbitration. First, the Constitution has an indirect effect in terms of section 39, which obliges the court to promote the spirit, purport and object of the Bill of Rights when interpreting statutes or developing the common law. Secondly, an arbitration agreement will be null and void to the extent that it is contrary to public policy in relation to the values of the Constitution. Further, she held that in interpreting arbitration agreements, it should be accepted that when parties submit to arbitration they submit to a process intended to be fair, highlighting that fairness is one of the core constitutional values.

O'Regan held that scrutiny of arbitration awards is to be done in terms of section 33(1) of the Arbitration Act 42 of 1965. She reasoned that the Constitution requires a court to construe these grounds reasonably strictly in relation to private arbitration.

On the facts, O'Regan held that the arbitration agreement in this case required the arbitrator to adopt an informal, investigative method of proceeding and not a formal, adversarial one.

The minority judgment was delivered by Kroon AJ (Nkabinde J and Jafta AJ concurring). Kroon AJ agreed with the decision in *Telcordia* and held that section 34, and particularly the requirement of "fairness" within it, applies to private arbitration.

On the facts, he found that the arbitrator had committed certain gross irregularities and therefore, concluded that the appeal should have been upheld and the arbitration award set aside.

Conventional wisdom both in South Africa and abroad is that it is unsafe to have the seat of arbitration in South Africa because of concerns that the judiciary may not provide necessary support to the process and to the enforcement of awards.

This case contradicts that perception. It is a strong statement of support for arbitration by the highest court in South Africa.

O'Regan emphasised the benefits of private arbitration which lie in its flexibility, cost effectiveness, privacy and speed. She stated that "in determining the proper constitutional approach to private arbitration, we need to bear in mind that litigation before ordinary courts can be a rigid, costly and time-consuming process and that it's not inconsistent with our constitutional values to permit parties to seek a quicker and cheaper mechanism for the resolution of disputes".

She emphasised that parties are free to subject their disputes to private arbitration voluntarily and to "determine what matters are to be arbitrated, the identity of the arbitrator, the process to be followed in the arbitration, whether there is an appeal to an arbitral appeal body and other similar matters".

Finally, O'Regan also referred to the powers of the court to interfere in the arbitration process. She noted that international and comparative law suggests that "courts should be careful not to undermine the achievement of the goals of private arbitration by enlarging their powers of scrutiny imprudently".

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The Duty to Mediate Commercial Disputes in South Africa

BY JOHN BRAND | BOWMAN GILFILLAN

Mediation is well established in South Africa as an effective method of resolving labour disputes, family disputes and community disputes. In many instances it is not possible to get to court without exhausting mediation. There are also at least forty statutes which in one way or another encourage mediation.

In this context it is surprising that, until recently, mediation was seldom used in the commercial arena. There are a range of possible reasons for this but perhaps the primary one was the belief that there was no need to mediate such disputes. Recent pronouncements from the highest courts in the land are however likely to change this situation and make it difficult for parties not to mediate.

In the case of *Port Elizabeth Municipality v Various Occupiers* 2005 (1) SA 217 (CC) the Constitutional Court said that "one of the relevant circumstances in deciding whether an eviction order would be just and equitable would be whether mediation has been tried. In appropriate circumstances, the courts should themselves order that mediation be tried". In 2007 in another eviction case in the Constitutional Court, *Occupiers of 51 Olivia Road,Berea Township, and others* v City of Johannesburg and others, Case CCT 24/07 (2008) ZACC 1 in 2007, the Court urged the parties to mediate their dispute and it endorsed the agreement reached in mediation in its ultimate judgment.

In June 2008 the High Court in Johannesburg urged the parties to mediate in a case involving the suspension of the CEO of the South African Broadcasting Corporation. The Court however stopped short of ordering the parties to mediate.

Perhaps the strongest encouragement for commercial mediation came in August 2009 when the High Court in Johannesburg held in an as yet unreported case of *Brownlee v Brownlee* that the failure by attorneys in that case to advise their clients to go to mediation at an early stage should be visited by the Court's displeasure. The Court limited the costs that the attorneys could recover from their clients to those that they could tax on the party and party scale and thereby deprived them of their full attorney and client fees. The case was one that involved the dissolution of a marriage, parental rights, maintenance and the division of the joint estate.

The court relied on the Rules of the High Court which require that one of the matters which must be considered at a pre-trial conference is whether a dispute should be referred to mediation. The attorneys in the case had no hesitation in answering the question in the negative.

The Judge said "I am given to understand that in England the all but obligatory recourse to mediation has profoundly improved the process of dispute resolution. Parties resolve their problems so much more cheaply as a result and the burden on the court rolls has been considerably lightened. Informed estimates put the success rate of mediation at between 80% to 90%". He went on to say "mediation can produce remarkable results in the most unpropitious of circumstances, especially when conducted by one of the several hundred people in this country who have been trained in the process. The success of the process lies in its very nature. Unlike settlement negotiations between legal advisors, in themselves frequently fruitful, the process is conducted by an independent expert who can, under conditions of the strictest confidentially, isolate underlying interests, use the information to identify common ground and, by drawing on his or her own legal and other knowledge, sensitively encourage an evaluation of the prospects of success in the litigation and an appreciation of the costs and practical consequences

of continued litigation, particularly if the case is a loser".

In relation to the case under consideration the Judge held that "in the process of mediation, the parties would have had ample scope for an informed but informal debate on the levels of their estates, the amount of their incomes and the extent of their living costs. Nudged by a facilitative intermediary, I have little doubt that they would have been able to solve most of the monetary disputes that stood between them. The saving in time and legal costs would have been significant and, once a few breakthroughs had been made, I have every reason to believe that an overall solution would have been reached. Everyone would, in the process, have been spared the burden of two wasted days trying to settle in Judge's chambers and four further days in which the minutia of assets and liabilities and income and expenses were interrogated."

Just one month later, in the unreported case of *Gluckman v Chiert and Another*, the High Court in Johannesburg directed the disputing parties to enter mediation regarding all of the issues in dispute between them. The Court nominated a mediator and prescribed time limits for the mediation and that the costs of the medication should be borne equally by the parties. The dispute concerned seven swamp cypress trees situated along the common boundary between the partys' properties. The dispute was successfully mediated and the litigation was avoided.

These cases and statutes indicate that there is a growing recognition by the South African judiciary and legislature of the important role that mediation can and should play in the civil justice system. It is also clear that in some cases the risk now exists that attorneys who do not advise their clients appropriately about the benefits of mediation or that parties who unreasonably refuse to mediate may be deprived of their costs. The parties also run the risk in certain circumstances of being refused a hearing by the court until they have mediated.

This judicial and legislative support for mediation as well as the inherent merits of the process are likely to ensure that it will soon become an integral part of commercial dispute resolution in South Africa.

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The 2009 Bilateral Agreement for the Promotion and Reciprocal Protection of Investments between Zimbabwe and South Africa

BY JOHN BRAND AND MIEKE KRYNAUW | BOWMAN GILFILLAN

On 27 November 2009 the government of the Republic of South Africa and the government of the Republic of Zimbabwe signed a Bilateral Agreement for the Promotion and Reciprocal Protection of Investments ("BIPPA") in Harare, Zimbabwe. In terms of the agreement's preamble the two countries entered into the agreement because they both desire to create favourable conditions for greater investment by South African investors in Zimbabwe, and Zimbabwean investors in South Africa.

The agreement was driven by the belief of both governments that the BIPPA would itself encourage investment, and that this stimulation of individual business initiative will increase prosperity in both Zimbabwe and South Africa. Through signing the BIPPA, both governments aim to signal to investors that investment is encouraged

and that both governments recognise the need for internationally recognised protection of investors and investments.

Negotiations relating to the content of a bilateral agreement between Zimbabwe and South Africa have been ongoing since 2002. Although theoretically a reciprocal agreement, the agreement was largely signed to make provision for the South African business community's interest in investment opportunities in Zimbabwe, particularly in the agro-processing sector, telecommunications, mining and infrastructure.

South African investors, who remain Zimbabwe's largest African trading partner, have in the past been anxious about investing in Zimbabwe because of the high levels of uncertainty about the protection of their investments, particularly the protection of property rights. The BIPPA aims to allay this uncertainty. The Department of Trade and Industry also made it clear that a driving factor behind South Africa's aiding of the recovery of Zimbabwe's economy was to alleviate the burden placed on the South African Government resources by Zimbabwean immigrants.

Notwithstanding the intent to encourage investment in Zimbabwe, the agreement can be used by Zimbabwean investors to invest in South Africa. At face value this may seem unlikely but a possible unintended consequence of the agreement is that foreign investors from anywhere in the world can use Zimbabwe as a conduit to invest in South Africa and South Africa as a conduit to invest in Zimbabwe under the protection of the agreement. This is a consequence of the inclusion of juristic persons in the definition of "investor" in the agreement without any requirement that the juristic person has effective economic activity in the country of incorporation.

Arthur Mutambara, Zimbabwe's Deputy Prime Minister, seems to appreciate this as he said that the agreement had worldwide significance and application and represented a bill of investment guarantees to any willing investor and further that Zimbabwe had "signed the BIPPA, not with South Africa, but with the world. The BIPPA lays out the fundamental conditions that we are also going to offer the rest of the world".

The agreement had been set to be signed in March 2009 but was delayed due to a disagreement over a clause which dealt with the issue of the security of previous South African investments in Zimbabwe, particularly property rights. Article 11 of the BIPPA, titled the "Scope of the Agreement" was the contentious clause.

On 13 November 2009 it was reported that the South African Minister of Trade and Industry, Rob Davies, had indicated that a compromise has been reached which provided security of tenure for all existing and new South African investments in Zimbabwe but excluded historical claims arising from the land reform process undergone in Zimbabwe. This land reform process included expropriation by the Zimbabwean state without compensation of large numbers of farms, including farms belonging to South Africans. According to Davies the aim of the BIPPA was to provide security in future for any South African investor in any sector, including agriculture. This security would create certainty for investors in Zimbabwe that would help with the economic recovery and stabilisation of that country which would contribute to political stability. However, the aim of the BIPPA was not to "reopen old wounds" which is why, according to Davies, it was impossible for South Africa to negotiate a retrospective clause relating to property rights.

This outcome did not however meet with approval from all sectors in South Africa. Although organisations such as AgriSA supported the idea of an investment protection agreement, it believed that the lack of proper consultation by the South African Government jeopardised the legitimacy and legality of any proposed bilateral agreement while the Zimbabwean Commercial Farmers Union said that it would be a huge mistake to sign the agreement as it had "serious flaws".

Prior to the scheduled signing of the agreement on 27 November 2009, AfriForum, a South African civil society organisation, brought an urgent application in the North Gauteng High Court in Pretoria, South Africa, to prevent the South African government from signing the agreement. The application was brought by AfriForum on behalf of a South African farmer, Louis Fick , who owned a confiscated farm in Zimbabwe.

The applicants argued that the so-called "exclusion clause" was discriminatory and therefore unlawful and the proposed agreement was in contravention of the South African Constitution, international law and the rulings of the Southern Africa Development Community ("SADC") Tribunal, specifically *Mike Campbell (Pvt) Ltd and Others v Republic of Zimbabwe* [2008] SADC (T) 02/2007 (28 November 2008) and *William Michael Campbell and Another v The Republic of Zimbabwe* [2009] SADC (T) 03/2009 (05 June 2009). The Zimbabwean Government does not recognise either of these SADC Tribunal rulings which held that Zimbabwe's expropriation process had discriminated against the applicants on the ground of race, that fair compensation is payable to the applicants for the properties which had been compulsorily acquired and that Zimbabwe was in breach of a number of its SADC Treaty obligations. The second ruling held Zimbabwe in contempt of the first ruling.

An out of court settlement was reached between the parties and this agreement was then submitted to the Court which made it an order of Court. In terms of the order, it is recorded that the aim of the BIPPA is to create legal and other remedies for South African citizens "over and above existing remedies in terms of international law". Furthermore the South African Government and Minister of Trade and Industry gave their assurance that the BIPPA "does not affect existing rights or remedies in terms of other sources of international law, in particular those in terms of the Treaty of the Southern African Development Community (SADC)". Lastly, the order notes that the SADC Tribunal rulings are not affected by the BIPPA and that the South African Government respects the rulings and orders of the SADC Tribunal and that it undertakes to honour the rulings in terms of its own obligations under the SADC Treaty. The outcome of the settlement was that the matter was removed from the roll with no order as to costs and the signing ceremony scheduled for 27 November 2009 went ahead.

The signed agreement applies to "all investments, whether made before or after the date of entry into force of [the] Agreement, but shall not apply to any property right or interest compulsorily acquired by either Party in its own territory before the entry into force of this Agreement". The contents of the BIPPA are otherwise largely standard. This is surprising as in a government position paper on BITs in 2009 the South African government had proposed major changes to BITs in the future to make them less biased in favour of investors.

The BIPPA will come into force thirty days after the last notification by both Governments that their respective constitutional requirements for entry into force have been fulfilled. It will then remain in force for a period of ten years and thereafter it will remain in force on an annual basis until written notification of termination by either government and a period of 12 months after such written notification has elapsed.

Neither Government has yet made public that its constitutional requirements for entry into force have been fulfilled, thus the BIPPA currently remains unenforceable.

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NIGERIA

Arbitration in Nigeria – Recent Developments in Nigeria's Statutory Framework

BY FUNKE ADEKOYA | AELEX

Arbitration in Nigeria is essentially governed by the Arbitration and Conciliation Act [CAP A18 LFN 2004], a modified Federal enactment of the UNICTRAL Model Law on Arbitration law. Although some States have their own Arbitration Laws, which are not UNICTRAL based, as a matter of practice most parties specify the Federal Act as governing their disputes. Its main objective is to provide a unified legal framework for the settlement of commercial disputes by arbitration and to make applicable the Convention on the Recognition and Enforcement of Arbitral Awards (the New York Convention) to any international arbitration award made in Nigeria or any other contracting state. Consequently most provisions of the UNICTRAL Model Law form part of the Nigerian legislation. Although the Act governs both domestic and international arbitration, its mandatory arbitration rules apply only to domestic arbitration, as parties may choose the rules to govern international arbitration proceedings.

Disputes arising out of criminal matters, illegal and void contracts, or leading to a change of status of the parties are not "arbitrable". The test is whether the dispute can be compromised lawfully by way of accord and satisfaction.

Subject to the agreement of the parties, the tribunal shall decide whether the proceedings shall be conducted by holding oral hearings or on the basis of documents or on both and can also administer oaths or take affirmations of parties and witnesses. Cross examination is allowed.

Unless otherwise expressly agreed by the parties, there is an implied duty of confidentiality with respect to arbitral proceedings. The Rules specifically provide that "Hearing shall be held in camera unless the parties otherwise agree". Disclosure in subsequent proceedings may be permitted with the consent of the party who produced the information or by an order of court. Arbitral proceedings will not be protected by confidentiality if the parties agree otherwise.

As a matter of practice, parties tend to limit disclosure to submission of written witness statements and copies of exhibits to be relied upon. The extent of discovery practice will depend on the procedural rules chosen by the parties. Unless otherwise agreed by the parties, the tribunal has the power to make an order of discovery against the parties.

There are no limits on remedies that are available in arbitration.

By Sections 30 and 48 of the Act; except where a challenge to an award is based on procedural issues which amount to misconduct or may have resulted in lack of fair hearing, the court has no power to intervene in proceedings. Section 23 of the Act also empowers a court to order a *subpoena ad testificandum* or *duces tecum* to

compel the attendance of a witness to testify and/or produce documents.

There is no right of appeal under the Act. However, a party may challenge an award or request the court to refuse recognition or enforcement. In line with the UNCITRAL Model Law, grounds for setting aside or refusal of recognition include where the award contains decisions on matters not covered by the submission; where the arbitrator has misconducted himself; there is incapacity of a party; the arbitration agreement is invalid under the law agreed by the parties or where the award is against public policy.

On 18th May 2009 the House of Assembly of the Lagos State enacted for Lagos State an Arbitration Law [Law No 10 of 2009] and by Law No. 8 of 2009 also established a Lagos Court of Arbitration. The new Arbitration Law [which is also closely modelled on the Arbitration and Conciliation Act] is to apply to all arbitration within Lagos State except where the parties have agreed that another arbitration law shall apply. The Law has made substantial changes to the legislative framework for conducting arbitration proceedings in Nigeria. As parties generally make the Arbitration and Conciliation Act the applicable law, it will take a while before the impact of the new provisions of the State Law is noticed. This paper will highlight areas where this and other new legislation will affect the current statutory framework for conducting arbitrations in Nigeria.

Parties have autonomy in the selection of arbitrators with a default provision in the Arbitration and Conciliation Act for the appointment of three arbitrators where the agreement is silent on the number, however the default provisions in the Lagos Law provides for the appointment of a sole arbitrator. If the Lagos Law is chosen as the relevant Law or where the parties are silent on which Law to apply, a sole arbitrator will resolve the dispute.

An arbitrator can grant preliminary or interim relief by way of an interim award. This may be a conservatory order, order for sale of perishable goods or order to provide security for costs.

A court may grant interim relief although the Act does not specify under what circumstances. However a recent court decision has stated that a court cannot grant preliminary relief before the arbitration panel has been established, unless a substantive relief is also sought. The State law addresses this by specifically empowering a court before which an application to stay court proceedings brought in respect of a matter which is subject to arbitration the power to grant such interim and supplementary orders as it may deem necessary.

The definition of a party, in the State legislation for purposes of an application for stay, as including anyone claiming through or under the party to the arbitration agreement is another departure from the current law and the effect of this remains to be seen.

There are no special provisions in the Federal legislation regulating multiparty arbitrations in Nigeria (either arising under the same agreement or different agreements) being consolidated in one proceeding. Because arbitration is consensual, parties must agree to consolidate claims or allow third parties to join arbitral proceedings as co-claimants or co-respondents. The Lagos Law however specifically provides for consolidation of concurrent arbitral proceedings.

The Legal Practitioners Act of Nigeria restricts foreign lawyers from practising law in Nigeria unless granted a warrant in respect of particular court proceedings. Since the arbitrator or the representative of a party need not be a lawyer it is unclear whether this restriction would apply to arbitration proceedings. To address this issue, the Lagos Law specifically seeks to open arbitration practice to non Nigerians by providing specifically that nationality shall not be the basis for disqualification as an arbitrator [not though as counsel]. Since the law applies whenever Lagos State is the venue for the arbitration unless the parties agree otherwise, the effect is that non Nigerians may be appointed arbitrator even in domestic arbitrations.

There are no provisions in the Federal Act governing interest unlike the State Law which specifically grants the arbitral tribunal power to award interest, order security for costs and exercise a lien over its award until fees are paid.

The Act simply provides that an award may be challenged by an application to the court but without providing for the procedure to be followed. In contrast, the Lagos Arbitration Law has Rules governing the procedure for making arbitration applications to court.

The Lagos Court of Arbitration Law seeks to provide a forum for administered arbitration within Lagos State, as it is empowered to issue Arbitration Rules, although none have yet been issued since the Court is yet to take off. The function of the Court is stated as being to promote resolution of disputes in the territory of Lagos State by arbitration and other alternative dispute resolution mechanisms. The Lagos Court of Arbitration when functional will provide administered arbitration proceedings. It has power to establish an arbitral tribunal in respect of any dispute referred to it and will maintain a panel of neutrals which shall consist of Arbitrators, Mediators as well as other experts with special skills and experience in specialised areas for this purpose.

The Nigerian courts have given full recognition to the importance of arbitral procedures and the enforcement of awards arising there from. The High Court (Civil Procedure) Rules of Lagos, Rivers, Ogun States of Nigeria effective in 2004, 2006 and 2009 respectively and the High Court (Civil Procedure) Rules of the Federal High Court Territory, Abuja all provide for mandatory pre-trial conferences during which the presiding judge is to promote amicable settlement of the dispute by alternative dispute resolution or refer the case to court annexed arbitration using a "Multi-Door Court House" structure. These multi door court house systems are dispute resolution centres established by and responsible to the State Judiciary and which provide an avenue for the conduct of arbitration and other ADR proceedings.

Matters in a Multi-Door Court House environment may be initiated through court referrals – where litigation has been commenced, the pre-trial Judge will stay the matter and refer it to the centre for resolution; if resolved the matter is then referred back to the court for entry of the agreement as a consent judgment. Additionally disputes which may or may not be the subject matter of litigation are filed directly at the Multi-Door Court House for settlement by one or both parties to the dispute; and direct intervention (where of its own initiative the Multi-Door Court House directly intervenes in a dispute in the public domain by inviting the parties to explore settlement at the centre.

At the State level, there seems a clear trend towards providing an attractive venue for arbitration [both domestic and international] as a viable alternative to contentious litigation. The picture is not so clear at the Federal level however as pending before the National Assembly are various bills to amend the current Arbitration and Conciliation Act. One bill seeks to prohibit Nigerian entities from using foreign substantive law for settling their arbitration disputes or from hosting their arbitration disputes outside Nigeria if the dispute itself arose from Nigeria. The thinking is to ensure that arbitration of Nigerian disputes should be by Nigerians and in Nigeria. In so far as these amendments if passed may restrict the concept of party autonomy which is the central attraction of arbitration, they may turn out to be counter-productive.

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Appealing a Decision in Nigeria

BY NNAMDI KINGSLEY ORAGWU | PUNUKA ATTORNEYS & SOLICITORS

The principles of justice and fairness imply that decisions affecting the rights or liabilities of persons should not be absolute in the first instance but can be reviewed on appeal to a higher body than the original decision maker. There are different kinds of decisions. Decisions may emanate from administrative, regulatory, judicial, arbitral or other dispute resolution, disciplinary or regulatory procedures. Thus decisions could be court judgments, decisions or orders of administrative tribunals, award of arbitration tribunals, decisions of regulatory bodies or even decisions of traditional rulers. Different principles and procedures govern appeals against each kind of decision. However, this paper focuses mainly on appealing judicial decisions.

The judicial powers of the Federal Republic of Nigeria are vested in the courts. The hierarchy of courts in Nigeria is set out by the Constitution and includes courts of first instance and appellate courts. The hierarchy of Nigerian courts is such that judicial decisions are subject to scrutiny at different levels with the aim of ensuring that justice is upheld. The appeal process under Nigerian law is regulated by statute and appeals flow from the courts below to those above in the chain. Statutes and Rules of Court regulate issues of time, place and procedure for appeal.

This Paper shall discuss the appeal process and the requirements of a valid appeal arising from court proceedings.

An appeal is the resort to a superior court to review the decision of a lower court or bodies intended to correct a perceived injustice or error committed. This is because an appeal by its nature is a continuation of the prosecution of the original cause or matter which is the subject of the appeal. See *Ogundiani v. Araba* [1978] 11 N.S.C.C. 334 @ 347. The position as upheld by the courts is that a party should not be seen to put forward in the appellate court a case different from what he canvassed at the trial court. See *Ohiaeri v. Akabueze* (1992) 2 NWLR (PT. 221)1 @ 20.

In Nigeria, the right of a litigant to appeal, the jurisdiction of the appellate court to entertain such appeals and the procedure to be followed are strictly regulated by the constitution and other Statutes.

The various State High courts can in the exercise of the appellate jurisdiction hear and determine all appeals from the decisions of the Magistrate courts in the Southern State – whether original or appellate and those of the District Courts in the North – in the exercise of the original jurisdiction. See Section 59 of the Magistrate Court Law of Lagos State, 2003.

The procedure is by filing a notice of appeal in the Magistrate or district court that gave the decision .The notice of appeal and all copies must be signed by the appellant or by his Legal practitioner .The Appendix to each of the Rules of Court contain a form of notice of appeal and an appellant is required to adopt the form with such variation as circumstances may require.

The notice of appeal must be filed at the registry of the lower court (the magistrate court) and should contain the following:

- The suit number of the proceedings from which the appeal arose;
- The name of the parties;
- The date and substance of the decision;
- The ground of appeal which shall be stated clearly and succinctly. (Each ground of appeal shall be set out separately and where a ground of appeal alleges an error in law, the nature of such error shall be stated. The

ground of appeal may simply state that the decision of the lower court is against the weight of evidence. This is otherwise known as the omnibus ground).

- The appellant's address for service within jurisdiction and
- The name of the legal practitioner (if any), representing the appellant.

Appeals may also arise from the original or appellate decisions of the High Court and these are to be determined by the Court of Appeal as provided under Section 240 of the 1999 Constitution of the Federal Republic of Nigeria (the "Constitution"). The Court of Appeal under this section also has exclusive jurisdiction to hear appeals from the Sharia Court and Customary Courts of Appeal.

Appeals may be as of right or with leave of Court. Appeal as of right means that the person who is appealing has an automatic right to contest the decision. While appeal with leave means that the approval of the Court (original or appellate court as the case may be) by an application for that purpose is required.

Section 241(1) of the 1999 Constitution of Nigeria clearly laid out the circumstances when appeals from the High Courts to the Court of Appeal can be as of right. They are:

- final decisions in any civil or criminal proceedings before the Federal High Court or a High Court sitting at first instance;
- where the ground of appeal involves questions of law alone, decisions in any civil or criminal proceedings:
- decisions in any civil or criminal proceedings on questions as to the interpretation or application of this Constitution;
- decisions in any civil or criminal proceedings on questions as to whether any of the provisions of Chapter IV of this Constitution has been ,is being or is likely to be, contravened in relation to any person;
- decisions in any criminal proceedings in which the Federal High Court or a High Court has imposed a sentence of death; and
- decisions made or given by the Federal High Court or a High Court: (i) where the liberty of a person or the custody of an infant is concerned; (ii) where an injunction or the appointment of a receiver is granted or refused; (iii) in the case of a decision determining the case of a contributory or officer under any enactment relating to companies in respect of misfeasance or otherwise; (iv) in the case of a decree nisi in a matrimonial cause or a decision in an action determining liability, and (v) in such other cases as maybe prescribed by any law in force in Nigeria

Also, based on Section 244 and 245 of the Constitution appeals lie as of right to the Court of Appeal from any decisions of the Sharia Court of Appeal and the Customary Court of Appeal in civil proceedings concerning Islamic or customary law. Section 246 of the Constitution allows appeals as of right to the Court of Appeal from the decisions of the Code of Conduct Tribunal, National Assembly Election Tribunal and the Governorship and Legislative Houses Election Tribunal on the question of the validity of the election or terms of office of a person.

While Section 242 of the Constitution stipulates that outside the circumstances laid out under Section 241, other appeals to the Court of Appeal shall be with leave.

Some legal practitioners have found themselves swimming in murky waters with regard to the above provisions in two respects. First is the distinction between a final decision and an interlocutory decision for the purpose of appeal. Second is the determination of whether the grounds of appeal are on points of law alone or on points of

mixed law and fact or on points of facts alone.

In determining the nature of an appeal as whether one of law or of fact the grounds of appeal and the particulars are to be considered and not just the label placed on the ground of appeal by the appellant. See *Bwai v. U.B.A. Plc. [2002] 4 NWLR (pt. 758) 692*. Thus an appeal labelled as one on ground of law may upon examination of the particulars actually be an appeal on ground of fact or one on ground of mixed fact and law.

The test to determine whether an order or decision is final or interlocutory is to look at the order made and not the proceedings and to see whether the entire case or proceeding has been brought to its finality or whether there are still other issues or matters to be resolved in subsequent litigation. See *Excel Plastic Industries Limited v. FBN PLC [2005] 11 NWLR (PT. 935) 59*. Thus a judgment after the hearing of the entire case is a final decision as it finally determines the matter but at the same time a decision upon a simple application challenging the court's jurisdiction may be final if the application succeeds as it may also determine the matter.

A single point of law is enough to sustain an appeal even where other grounds are bound to be incompetent for failure to seek leave. See *Bwai v. U.B.A. Plc.* (supra).

Section 243 of the Constitution spells out persons who can appeal against a decision to include a party, an interested party with leave of court, an accused person in a criminal proceeding and the Attorney General of the Federation or the states when prescribed. Where there are two or more appellants, an appeal will be competent if one or more of them has or have the competence to appeal. See *Mobil Producing (Nigeria) Unlimited v. Monokpo [2003] 18 NWLR (PT. 852) 346*.

The procedure for appealing to the Court of Appeal is by filing a notice of appeal at the lower court (the court that gave the decision being contested). The notice of appeal and all copies must be signed by the appellant or by his Legal practitioner except for criminal matters where each appellant is required to personally sign a separate notice of appeal. See *Uwazurike v. Attorney General of the Federation [2007] 8 NWLR (PT. 1035)1*. The Appendix to the Court of Appeal 2007 contains the various forms of notice of appeal for civil and criminal matters and an appellant is required to adopt the form with such variation as circumstances may require. An appellant may file more than one notice of appeal. See *N.B.A. V. Chukwumeife [2007] 8 NWLR (PT. 1035)221*.

A respondent who is not satisfied with the decision appealed against and wants a reversal of the judgment or a part of it must file a notice of appeal. This is referred to as a cross appeal and will be argued with the appeal of the appellant. On the other hand a respondent who did not appeal from the decision of the court below, but desires to contend on appeal that the decision of that court should be varied, either in any event or in the event of the appeal being allowed in whole or in part, must give notice to that effect, specifying the grounds of that contention and the precise form of the order which he proposes to ask the court to make in that event, as the case may be. This is called a Respondent's Notice. See Order 9 of the Rules.

The proceedings and documents relied upon in the matter at the lower court are transferred to the Court of Appeal by a process called "transmission of records". These records are compiled either by the Registrar of the lower court or the appellant within a period of 90 days. See Order 8 of the Court of Appeal Rules 2007(the Rules). Failure to compile and transmit the records of appeal is good ground for the respondent to apply for the court to dismiss the appeal. See Order 8 Rule 18 of the Rules. Once the records of appeal are compiled and transmitted the appeal is deemed to have been entered and the lower court loses jurisdiction over the proceedings. See *Ogunremi v. Dada [1962] 1 A.N.L.R. 657; Denton-West v. Muoma [2008] 6 NWLR (PT. 1083) 418*.

After the transmission of the records of appeal the appellant is given 45 days to file his brief of argument at the

court of appeal, while the respondent upon the receipt of the appellant's brief shall have thirty days to respond by filing the respondent's brief of argument. When the appellant is served with the respondent's brief of argument he shall if necessary be allowed fourteen days to file a reply brief. See Order 17 of the Rules. After all briefs have been filed and served, the court will proceed to hear the appeal and deliver its judgment.

The Supreme Court has exclusive jurisdiction over appeals from the Court of Appeal. Appeals lie to the Supreme Court from decisions of the Court of Appeal whether interlocutory or final. Such appeals maybe as of right or with leave. See Section 233(1) of the Constitution.

Section 233(2) of the Constitution provides that an appeal shall lie as of right in the following cases:

- where the ground of appeal involves questions of law alone, decisions in any civil or criminal proceedings before any Court of Appeal;
- decisions in any civil or criminal proceedings on the questions as to the interpretation of the Constitution.
- decisions in any civil or criminal proceedings on the question as to whether the provisions of Chapter IV of the Constitution has been, is being or is likely to be contravened in relation to any person,
- decisions in any criminal proceedings in which any person has been sentenced to death by the Court of Appeal or which the Court of Appeal Has affirmed A Sentence of death imposed by any other court;
- decisions on any question: (i) whether any person has been validly elected to the office of President or Vice-President or Vice-President under the Constitution; (ii) whether the term of office of the president of Vice-President has ceased; and (iii) whether the office of the President or the Vice-President has become vacant;
- Such other cases as may be prescribed by an Act of the National Assembly.

However, Section 233(3) of the Constitution provides that "Subject to the provisions of subsection (2) of this Section, an appeal shall lie from the decisions of the Court of Appeal or Supreme Court". In determining the nature of the right of appeal to the Supreme Court, whether the appeal is against a final or interlocutory decision is of little consequence.

The courts are strict as to the time frames for appealing against decisions. An appeal against an interlocutory decision must be filed within fourteen days while that against a final decision must be filed within three months. See Section 24(2) of the Court of Appeal Act (CAP. C 36) Laws of the Federation of Nigeria (LFN) 2004 and Section 27(2) of the Supreme Court Act (CAP. S 15) LFN 2004.

Conclusion

Understanding the appeal process is a vital part of efficient justice delivery. The lack of understanding of the appeal process has remained an albatross of several appeals which have failed to meet the strict requirements of a valid appeal. Appealing decisions requires a good grasp of the substantive and procedural law of the subject matter of the case as well as the grounds of appeal permitted by law.

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The Use of Expert Witnesses

BY OMONE FOY-YAMAH | PUNUKA ATTORNEYS & SOLICITORS

Expert witnesses are useful witnesses in civil or criminal litigation as well as in arbitration. Expert witnesses give expert opinion in specialised areas of a case or dispute, which are not ordinarily within the knowledge or competence of the judge or adjudicator. Thus the role and duty of an expert witness is to assist the court or tribunal in arriving at the true facts and position regarding technical issues within his area of expertise.

The independence of an expert witness is an important factor in determining the credibility and weight to be attached to the expert opinion. Expert witnesses may be appointed by the court or arbitral tribunal, or they may be appointed by the parties themselves. Where the court appoints an expert, the independence of the expert is easier to maintain since his primary duty is owed to the court in the first place, and he would usually give a single opinion on the questions he is called upon to give his opinion. But where parties appoint expert witnesses, questions of independence and bias may arise as there is the tendency for the expert witness to be loyal to or biased towards the party who appoints and pays him. However, the independence and credibility of party appointed experts, can be maintained by various rules, practice and procedures, some of which will be highlighted in this Article.

Making the best use of expert witnesses depends on a number of factors. These factors include knowing when to use an expert witness, determining or narrowing the issues on which expert opinion is required, finding the right expert, interviewing the expert and preparing the expert report (where written statements are adopted), ensuring and maintaining expert independence, assessing the expert fee structure, and so on. In all, the paramount duty of the expert to assist the court, rather than the parties should be upheld.

A witness is generally not allowed to give his opinion as to the existence or non-existence of any fact in issue. Witnesses are called only to state facts observed by them but not draw inferences from facts. The general rule of evidence is that the opinion of any person is irrelevant and inadmissible. See section 66 of the Evidence Act, Cap E14 Laws of the Federation of Nigeria 2004. Thus the use of expert witnesses is an exception to this general rule.

Experts may be used in civil or criminal litigation, arbitration and in expert determination which is another form of alternative dispute resolution. In civil litigation, a judge may before or during trial, order or direct that expert witnesses be called and may specify the number of such expert witnesses. See for instance Order 32 rules 2 & 3 of the High Court of Lagos State Civil procedure Rules 2004.

In arbitration, unless otherwise agreed by the parties, the arbitral tribunal may appoint one or more experts to report to it on a specific issue to be determined by the arbitral tribunal. See section 22 of the Arbitration and Conciliation Act Cap A18 Laws of the Federation of Nigeria 2004. Thus experts may be appointed by the court or arbitral tribunal or by the parties themselves. A single expert may be appointed to give an opinion on the matters in dispute, or two or more experts may be appointed to give joint or separate opinions. It is suggested that appointing a single expert will avoid unnecessary costs and inevitable bias associated with multiple experts.

When to Use an Expert

In legal parlance, an expert is any person who is specially skilled in the field he is called upon to give an opinion. However, it is the court that determines whether or not a witness can be regarded as an expert. Ordinarily, an expert should not give opinion on the ultimate issue which involves the application of a legal standard such as negligence or breach of contract.

This is for the judge or adjudicator to infer from the law and facts. An expert opinion should not be a substitute for the judge's opinion, but should merely assist the judge or adjudicator in forming an opinion in areas which are ordinarily not within his training and experience. Thus expert evidence is not usually admitted on questions of credibility of a witness even where the witness is a child. See *A.G. Federation v. Abubakar* (2007) 10 NWLR (Part 1041) 37.

The Evidence Act in sections 57 to 61 provides occasions on which expert witnesses may be used. These include issues relating to a point of foreign law, native law or custom, science or art, or identity of handwriting or finger impressions. For instance a medical doctor may be called as an expert in cases of forensic medicine such as time of death or cause of death while a structural engineer may be called as an expert in construction contracts. A handwriting expert may be called to prove that a person wrote or signed a document (see section 57 of the Evidence Act Cap E14 Laws of the Federation of Nigeria 2004). However, by section 61 of the Evidence Act, a lay person who is familiar or acquainted with a person's handwriting may also be called to prove that a person wrote or signed a document.

However, it is not in all cases of foreign law, science or art that it is necessary to use an expert. It has been held that statistical analysis does not fall within the items contemplated in section 57 (1) of the Evidence Act. See A.N.P.P. v. Usman (2008) 12 NWLR 9 (Part 1100) 26. Also, in arbitration it may be unnecessary to use expert witnesses where the arbitral tribunal is made up of experts in the matters of dispute. Sometimes an arbitration clause may stipulate that the arbitrator should be an expert or have some level of qualification in the subject matter of the contract. But the fact that an arbitrator is knowledgeable in the field of dispute does not preclude the right of parties to call expert evidence.

Finding the Right Expert

Finding the right expert is a key determinant of the usefulness of the expert's evidence. The first task in finding a suitable expert is to determine the issues on which the expert opinion is required. Once the issues are determined, it would be necessary to find a person who has specialised knowledge of the issues identified. An expert must possess knowledge and information on the issues on which he is called upon to give an opinion, beyond that which is ordinarily available. This means that the expert must be specifically trained in those areas. Thus the educational background of the expert is very relevant in determining if he is suitable for the case. In this regard, his academic background as well as his professional training and experience should be considered. If the expert has international qualifications and experience, it is an added advantage as he would be able to answer jurisdictional related issues.

Apart from having technical knowledge and skill, a good expert should have a good grasp of general human experience since his opinion may be challenged on a wide variety of natural occurrences and he may be asked to draw conclusions from certain ideal situations during cross examination.

A good expert must be able to make sharp, clear analysis of the facts with which he arrived at his opinion and must be able to react to surprises on trial. Thus he must have good language and communication skills and must be reasonably intelligent to foresee the goal of cross examination. Closely connected to this is whether the expert has any previous experience testifying in court, although even if he doesn't he could be well prepared.

The time schedule and availability of the expert is also important as the expert would apart from physically attending proceedings to give evidence, be required to attend meetings before trial. An expert who is always out of jurisdiction or whose schedule will not allow appropriate consultation may pose a challenge. However, modern information technology help to reduce these challenges as telephone conferences and e-mail communications can be used. But then these forms of communications are not entirely safe for expert consultation because of the level of confidentiality which ought to be maintained. It is advisable to have face to face consultations with the expert before trial.

Cost is another factor to consider in choosing an expert. Usually experts give their opinion for a fee and the fee would vary depending on the scope of the expert opinion required, his level or years of experience, the region where the trial is being conducted, travel cost, and so on. It is important to strive to minimise expert cost without necessarily compromising quality. Exorbitant expert fees should be avoided as this could be a basis for challenge of an expert's independence and credibility. The client should be involved in the selection of an expert particularly in the area of cost since he would usually pay the fees.

Preparing the Expert Report

Preparing a good and relevant expert statement requires not just presenting the expert's ideas as recounted by him, but preparing it in an acceptable and admissible form. In Nigeria, the ordinary rules of evidence would apply to an expert's written opinion sworn on oath, except of course the rule against opinion evidence. Thus an expert opinion should not contain facts or opinion given to the expert by some other person who is not called in evidence. His opinion should be restricted to matters peculiarly within his knowledge as an expert. Any opinion outside this limit is inadmissible. See A.N.P.P. v. Usman (2008) 12 NWLR (Part 1100) 28.

An expert opinion should state the expert's qualification and satisfy the court that he is an expert on the subject in which he is giving his opinion. The expert's Curriculum Vitae and qualifying certificates should also be produced as evidence of his expertise. The expert opinion must also state clearly the reasons or basis of the opinions expressed and this would usually be the basis on which the expert may be cross examined and would enable the court or tribunal to determine the relevance of the opinion and the weight to be attached to it. If an opinion is based on doubtful grounds or unrealistic assumptions, it may be irrelevant and inadmissible, and if it is admitted, little or no evidential weight will be attached to it.

In addition, the expert's written statement should contain an acknowledgment of his duty to the court and also a declaration of the expert's independence in relation to the parties and the dispute. Compliance or adherence with this duty and independence of the expert should run through the expert's statement and should be evident in its form. In Nigeria, there are no specific rules or guidelines on the format of expert reports as regards the independence and duty of an expert. In New South Wales, the Uniform Civil Procedure Rules 2005 (rule 31.17(f) introduced by the new Division 2 with effect from 8 December 2006) requires a declaration of the duty of an expert witness to the court and the parties in proceedings. Also, under the said Rules, an expert witness cannot give evidence and his expert opinion or report will not be admitted in evidence unless he has declared his adherence to the Expert Witness Code of Conduct set out in schedule 7 to the rules. In international arbitration, the IBA Rules on Evidence. Article 6.2 provides for a statement of independence to be submitted by all tribunal-appointed experts before accepting an appointment, but there is no such provision in respect of party – appointed experts. The *Chartered Institute of Arbitrators (CIArb) Protocol for the Use of Party Appointed Expert Witnesses in International Arbitration* however provides Guidelines to facilitate a tribunal's assessment of the independence and usefulness of party-appointed expert witnesses. One of such guidelines is that an expert's written opinion should contain the following expert declarations:

- An acknowledgement that the expert's duty in giving evidence is to assist the arbitral tribunal to decide the issues in respect of which expert evidence is adduced, and that the expert has complied with and will continue to comply with that duty;
- A confirmation that the expert is independent of the appointing party;
- A confirmation that his opinion is independent, objective and unbiased, and has not been influenced by the

pressures of the dispute resolution process or by any party to the arbitration;

- A confirmation that all matters upon which the expert has expressed an opinion are within the expert's area of expertise;
- A confirmation that the expert has referred to all matters which the expert regards as relevant to the opinions the expert has expressed and has drawn the attention of the tribunal to all matters of which the expert is aware, which might adversely affect the expert's opinion;
- A confirmation that the expert considers the opinion to be complete and accurate and constitute the expert's true , professional opinion; and
- A confirmation that if the expert subsequently considers that the opinion requires any correction, modification or qualification, the expert will notify the parties to the arbitration and the arbitral tribunal forthwith. See Article 4.5(n) and Article 8, CIArb. Protocol for the Use of Party Appointed Expert Witnesses in International Arbitration.

The above objectives can be achieved by a proper consultation process with the expert and it is important that the client is involved in this process.

It is suggested that Nigeria should take a cue from the above guidelines in accessing the independence of expert witnesses.

When the preparation of the expert written statement is complete, the expert signs the statement (and forensic report if any) which is usually then filed as his evidence. The expert must appear in court to testify or adopt his written evidence and be cross examined as to his qualifications, experience and credibility of his opinion to enable the court determine the evidential value of his opinion. The evidence of an expert will amount to hearsay and may be inadmissible where the expert gives his opinion in writing and is not called as a witness. See A.N.P.P. v. Usman supra.

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Assessing the Potential Outcome of a Pending Case

BY NNAMDI K. ORAGWU AND IGE ASEMUDARA | PUNUKA ATTORNEYS & SOLICITORS

The outcome of a civil or criminal case cannot be determined with mathematical accuracy. Although it is usual to expect that a good or simple case would ultimately turn out successful, several factors may produce an unexpected outcome. Several factors may be responsible for the unexpected outcome of a case and the impact of such factors may be seen right from the initial conceptualisation and presentation of the case up to trial and final judgment.

The potential outcome of a case is best assessed from the lawyer or attorney's perspective. This assessment requires good knowledge of the law and facts and it is indeed, the first task which the lawyer (or attorney) must undertake before setting out on a case. If from a proper evaluation of the facts and law, he does not foresee any chances of success, the lawyer or attorney may not set out to litigation, but may advise his client and seek other alternative ways of resolving the case. Thus the lawyer or attorney plays a significant role in the outcome of a case. But then, the court, judge or adjudicator also plays an important

role in the potential outcome of a case for no matter how well the lawyer or attorney has conceptualised and presented the case, the court or judge has the final say. Although the doctrine of judicial precedent may provide some indication of which side the case should tilt, the court must in the application of the doctrine, sift through the facts and determine what it classifies as material and what decisions of the superior courts are applicable. Here, the personal orientation and experiences of the judge are important factors that may influence the judge's decision and create uncertainty in the outcome of the case. In this regard, the lawyer or attorney must be alert in knowing and understanding the judge in order to employ the appropriate skill and tactics that would bring a successful outcome.

This Paper therefore attempts to assess the potential outcome of a case from the attorney's perspective. In doing this, a general overview of the facts of the case, the law as it applies to the case (including judicial precedents which sometimes create uncertainties contrary to widespread belief), the strategy of the attorney, understanding the personal idiosyncrasies and dispositions of the judge as well as the prevailing social and economic atmosphere and other ancillary issues will be examined. A detailed discussion of these issues will make for good understanding of the subject matter.

There is no gainsaying the fact that each attorney has a style or employs an approach that is peculiar to him in prosecuting a case. Yet, an attorney's style, no matter how fantastic it appears, operates and becomes productive only within the framework of the facts of the particular case. Thus, the fact of a case is a major determining factor in assessing its potential outcome. No matter how ingenious an attorney may be, if the facts of the case turn against his client, he can only struggle helplessly like a lumberman that uses the blunt edge of an axe. He may find solace in technicalities but that will not confer on him judgment on the merit. Therefore, the facts of the case is fundamental to getting a positive final result and the Supreme Court acknowledged this when it said that "facts are important in every case before the court as they are the fountain head of the law." *Abubakar v. Joseph (2008) 13 NWLR (Pt. 1104) 307 at 343*.

Because facts relate to the state of things or relation of things as seen, observed and/or perceived by the parties (section 2(1) of the Evidence Act, CAP E14 LFN, 2004), they can hardly be changed but, an ingenious Attorney may be able to present a rather obscure and difficult fact in a vividly clear and simple manner. This does not, however, radically change the facts but may put on it a different outlook – a benefit a litigant enjoys in hiring a skillful attorney. To the extent that a good presentation puts a new and better outlook on the facts before the court, the Court of Appeal's observation in *C.G.G. (Nig.) Ltd v. Amaewhule* (2006) 3 NWLR (Pt. 967) 282 at 297 that "facts are static and whatever may be our wishes, our inclinations, they cannot alter the state of facts and evidence" becomes limited. In other words, although facts have been held to be static, stable, certain or definite and not affected by one's inclination, it is not out of place to say that good presentation, which is a product of wishes, inclination and thought processes, does affect it.

Since facts do not run the judicial atmosphere in isolation, it is important that the place of law as a telescope for assessing the future dimension of a case is not underestimated. As a matter of fact, facts are only aligned with law. Good facts without legal authorities supporting them will at best only unsuccessfully appeal to the sympathy of the court and at worst makes counsel's submission otiose and dry. Law has several sources ranging from the Constitution to other Nigerian statutes and subsidiary legislations, the Received (and extended) English Law of which the Statutes of General Application is an offshoot; the principles of Common Law and the doctrine of Equity, Customary Law of which Islamic Law is treated as a sub-sect and very importantly, Case-Law commonly referred to as Judicial Precedent. A sound knowledge of these various sources of the law and a tactful and proper application of them to the available sets of fact makes for good outcome of a pending case.

The main essence of approaching a court when dispute arises is for the court to give an interpretation of the law, in the light of the facts presented before it, *for juria novit curia,* i.e., *the court knows the law*. More often than not, an Attorney or even an ordinary man on the street knows the wordings and letterings of the law but the court may give its interpretation

to the law different from the other observer's perspective. That is why Justice Oliver Wendell Holmes of the Realist School would say that, "law is not a brooding omnipresence in the sky but the prophecy of what the court says and nothing more pretentious…"

This underlies the importance of judicial decisions. In order to ensure certainty, judges have developed the act of law-making through the doctrine of *Stare Decisis (meaning, stay by the decision),* and judicial precedent as a source of law is thereby institutionalised.

Today, Judicial Precedent is arguably the most important legal prism through which the potential outcome of a case can best be assessed as a previous decision of court on similar facts can give an assessor a clue as to the likely result of an instant one in view of the fact that judges are mandated to stay by the previous decisions. There is therefore an element of certainty that comes with Judicial Precedent. But this element of certainty which is the beauty of Judicial Precedent appears to have been tinkered with as there are conflicting decisions of Superior Courts on the same issues, a situation which puts the lower courts in tight corners in making decisions on matters of similar facts. Two of the Nigerian Supreme Court cases which have highlighted such conflict are the cases of NEPA V. Edegbenro [2002] 18NWLR (PT. 798) 79 and Onuorah v. K.R.P.C Limited [2005] 6 NWLR (PT. 921) 393 (both highlighted such conflict in their effort to determine the issue of whether it is the State High Court or the Federal High Court that has jurisdiction to determine matters involving the Federal Government or any of its agencies, an issue which is recurrent till date). So, it is almost impossible to predict or give an infallible pre-judgment assessment of the outcome of a pending case.

In an attempt to remove the uncertainty created by conflicting decisions of Superior Courts on the same issues, the courts have unsuccessfully devised a guideline on what to do. Even on this, the courts are divided. In *Aseimo v. Abraham* (1994) 8 NWLR (Pt.361) 191 at 212 – 3 the Court of Appeal sitting in Port-Harcourt held that "where there are two conflicting decisions of the Supreme Court, the Court of Appeal is free to choose which of the two decisions it is to follow". The same decision was reached by the Ibadan Panel of the Court of Appeal in *ECU-Line v. Adelekan* (2001) 10 NWLR (Pt. 721) 261 at 281 in stronger terms thus: "where authorities of equal standing are irreconcilably in conflict, a lower court has the freedom to pick and choose between them". But, the Court of Appeal in its earlier sitting at Benin had held that "where there appears a conflict in two previous decisions of the Supreme Court on the same points or issue, as in this case, *the Court of Appeal is bound by the latter decision and must follow and apply it*." Okpozo v. Bendel Newspaper Corp. (1990) 5 NWLR (Pt. 153) 652. The above decisions demonstrate the extent of the conflict that has bedeviled the doctrine of *stare decisis* as a mirror for assessing the potential outcome of a pending litigation.

Be that as it may, it is candidly opined that, *Okpozo's case* seems to present a better approach than *Aseimo and ECU-Line's* cases. The reasons are clear. Firstly, the latter decision would appear to have considered the earlier one. Indeed, part of the principles of our law is the doctrine of judicial notice set out in Section 74 of the Evidence Act by which the courts are presumed to be aware of an earlier decision. Secondly, the idea that a lower court confronted with conflicting decisions should "pick and choose" seems to confer discretion on the court and discretion is alien to *stare decisis* principles. Thus, the Supreme Court has held in *Amaechi v. I.N.E.C.* (2008) 5 NWLR (Pt. 1080) 227 at 379 that "the application of the principles of *stare decisis* or judicial precedent does not involve an exercise of judicial discretion at all. It is what must be done i.e. it is mandatory". However, it seems that the line of thought of allowing the courts to pick and chose when there are conflicting decisions before them has taken a more solid footing. Without losing sight of our main task in this discourse, may it be stated that judicial precedent seems to have been diminished by the inconsistence of the administrators of justice in giving decisions on similar questions submitted to them.

It is also very important that one considers the skills and competence of the attorney who handles the matter when

assessing its potential outcome. An attorney's skill is usually brought to bear on the case starting from the presentation in the pleadings and conduct of trial to the final determination of the suit. Hiring a sound, diligent and tactful attorney then becomes extremely necessary for a party seeking favourable outcome. A litigant is responsible and completely bound by the kind of counsel he hires; the counsel's tactics are his tactics, the counsel's mistakes are his mistakes. The conduct of a case lies wholly with counsel. As a matter of fact, it is only where there are procedural irregularities that mistakes of counsel are not visited on his clients. Where it is shown that the error relates to the conduct of the case, the litigant is bound by the conduct of his case as it relates to the competence of his counsel. The rule should be "caveat client". *Trans Nab Ltd. V. Joseph (1997) 5 NWLR (Pt. 504) 176 at 197 – 8, i.e.,* once a litigant chooses a counsel, he should permit him once seised of the case to conduct it in the manner of his professional ability.

Having considered the Attorney's skills and strategies, one must remember that a lot depends on the judge whose duty it is to adjudicate on the matter. Apart from the fact that the judge is controlled largely by the position of the law relating to the facts of the particular case, his personal idiosyncrasies and disposition also have much influence on the direction the matter goes. There is definitely no dearth of examples, in either our legal system or elsewhere, of how Judge's background and disposition comes to bear on their judgments. Up till today, the decision of Blackburn J. of the Court of Exchequer Chambers in the celebrated case of *Rylands v. Fletcher* (1868) LR 3 HL 330 is still been debated in both social and academic circles not mainly because it established strict liability without negligence but because of the experience and disposition of the judge coupled with the then prevailing public concern for such matter.

Indeed, even judges themselves admit outside the courtroom that their idiosyncrasies, training, personal experience and disposition affect the decisions they give on cases presented before them. Judge Posner who wrote recently in the Havard Law Review admitted that: "It is no longer open to debate that ideology (which I see as intermediary between a host of personal factors, such as upbringing, temperament, experience, and emotion-even including petty resentments toward one's colleagues – and the casting of a vote in a legally indeterminate case, the ideology being the product of the personal factors) plays a significant role in the decisions even of lower court judges when the law is uncertain and emotions aroused. It must play an even larger role in the Supreme Court, where the issues are more uncertain and more emotional and the judging less constrained". See "The Supreme Court (2004) Term Foreword: A Political Court", (2005) 119 Harv. Law Rev. 32 at 48-9.

So, is the background, training, general outlook and life philosophy of our judges reflected in their judgment? See Markesinis and Deakin's TORT LAW; 6th Ed. (2008) p.77. To this extent, the judge is a factor in assessing the potential outcome of a pending case.

Furthermore, the prevailing social, economic and political atmosphere also influences the direction a pending litigation goes. For instance, it would be difficult for the Courts to annul election results in the 1999 Elections when the country was struggling to get off the hostile grip of the military.

By and large, even when an assessor knows all these factors and reckons with them, it is not an easy task telling the potential outcome of a pending case yet this feat is an integral part of a lawyer's task before embarking on long and torturous litigation journey.

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OFFSHORE

JERSEY

Enforcement of Foreign Judgments in Jersey

BY NIGEL SANDERS | OGIER

Before any party launches into litigation, the kind of questions that will be asked will include: will it be worth it? What is there to be gained if I win? Can I enforce any judgment? That is perhaps more the case in times of recession where funds are tight and the prospects of throwing good money after bad in terms of what are likely to be hefty legal costs are wholly unwelcome. The purpose of this article is to outline the ways in which judgments of foreign courts can be enforced in Jersey.

Overview

Clearly, it is impossible to give a template that can be applied to any given judgment, as much will depend on the nature of the judgment, from where it emanates and the kind of assets that are being targeted for enforcement. However, there are some broad principles that can be stated in order to provide a would-be litigant with a flavour of how any overseas judgment might be viewed by the Jersey Courts should enforcement efforts be made.

The starting point is that Jersey is a distinct and independent jurisdiction – there are certain circumstances where certain judgments can be registered and enforced directly by reason of reciprocal enforcement provisions, but they are limited. Accordingly, in many instances it will be necessary for the judgment debtor to commence fresh proceedings in Jersey seeking a "localised" judgment which gives effect to the original judgment of the foreign court.

Recognition – Registration and Enforcement

Enforcement by way of registration of a foreign judgment is provided for in Jersey pursuant to the Judgments (Reciprocal Enforcement) (Jersey) Law 1960 (the "1960 Law"). The 1960 Law sets out criteria that must be met and also provides that only judgments from superior courts of reciprocating countries will be recognised.

Which Countries and Courts are Covered?

Dealing with the latter point first, reciprocating countries and their superior courts are listed in the Judgments (Reciprocal Enforcement) (Jersey) Act 1973 and comprise the following:

- England and Wales – House of Lords, Court of Appeal and High Court;
- Scotland – Court of Session and Sheriff's Court;
- Northern Ireland – the Supreme Court of Judicature; and
- Isle of Man (the Hugh Court of Justice).

The question of what is a superior court judgment as regards the English Courts received judicial scrutiny in the case of *In re Hardwick* [1995] JLR 245 in which the Royal Court in Jersey held that notwithstanding that an English County Court judgment had been transferred to the High Court in England for enforcement purposes, the fact that the "original" judgment (the phrase used in the 1960 Law) was not of a superior court of England, the judgment could not be recognised. That decision has recently been doubted by the Royal Court of Guernsey in *Manches LLP v Inter Global Financial Limited* (9 September 2009) in which a County Court judgment that had similarly been transferred to the High Court for enforcement purposes was capable of being registered pursuant to the relevant Guernsey legislation, which is materially identical to the 1960 Law. The Judge of the Royal Court of Guernsey was persuaded to follow Isle of Man authority (*Kreisky (trading as Video Vision Broadcast) v Stapleford Flying Club Limited* [1990-92] MLR 236) in which a position contrary to that in *In re Hardwick* had been adopted. It is generally thought that the Jersey position may well be decided differently should the matter be considered by the Royal Court again.

What is the Criteria for Registration?

The 1960 Law sets out criteria for enforcement which are typical and reflect the basic common law position. To be capable of registration, the judgment has to be

- Final and conclusive (a judgment can be "final and conclusive" even though an appeal in the foreign court is pending or possible, although any such appeal will be relevant to an application to set aside registration); and
- In respect of a money sum which has not been wholly satisfied (other than for a tax or similar charges, or a fine or other penalty).

The judgment has to post-date the coming into effect of the Jersey Act confirming reciprocal status of the country and the judgment creditor must apply to the Royal Court for registration within six years of either the date of the judgment itself or, where the judgment has been appealed, the date of the last judgment in the appeal proceedings.

The procedure for the registration is set out in detail in relevant Rules (the Judgment (Reciprocal Enforcement) Rules 1961). Applications are required to be supported by affidavit evidence. Notice of registration is required to be served on the judgment debtor following which applications to set aside can be made on certain grounds (including lack of jurisdiction, fraud and failure to comply with the requirements of the 1960 Law) within specified periods (which can be extended). Naturally, enforcement steps cannot be taken until the period has expired or any application to set aside has been dealt with.

Enforcement at Common Law

Money Judgments

As regards the courts of countries outwith the Act (in essence non-UK superior courts) where registration is not available, money judgments may be enforced by commencing fresh proceedings in Jersey on that original judgment. The right to enforce such a judgment arises on the basis that the judgment of a foreign court of competent jurisdiction imposes an obligation on the judgment debtor to pay the judgment debt, and is therefore

not dependent on principles of comity or reciprocity (*Showlag v. Mansour* [1994] JLR 113 at 118 (Privy Council)). Whilst Article 10 of the 1960 Law grants the States of Jersey the power to bar the enforcement of judgments from countries which do not reciprocate (i.e., which give Jersey judgments substantially less favourable treatment than Jersey affords its judgments), to date no Act has been made under this Article.

As the 1960 Law codified the existing common law position relating to enforcement, the present common law rules largely mirror those described above. In summary, to enforce a foreign judgment *in personam* at common law, the judgment must be:

- final and conclusive;
- for a debt or definite sum of money (but not payable in respect of taxes or similar charges or a fine or other penalty);.
- given by a court of competent jurisdiction; and
- but must not be impeachable on the grounds of fraud, or contrary to public policy, or natural justice.

In practice, the key question is usually whether or not the foreign court had jurisdiction. This will be determined by the Royal Court according to Jersey law. The foreign court will be held to have jurisdiction over the judgment debtor if, for example, he was physically present and served with the foreign process within that court's territorial jurisdiction, he voluntarily appeared in the foreign proceedings to contest the action on it merits, he was the plaintiff or counterclaimed in those proceedings, or he expressly agreed to submit to the foreign court's jurisdiction (for instance, in a contractual jurisdiction clause).

Where the above criteria are met, the defences available to a judgment debtor are limited, and the Jersey Court will not readily enquire into the merits of the original action, nor review the measure of damages awarded.

Non-Monetary Judgments

The decision in *Brunei Investment Agency v Fidelis Nominees Limited* [2008] JRC 152 (16 September 2008), was a significant one from the Jersey Courts last year. In it, the Court held that a final and conclusive non-monetary judgment obtained in the courts of any territory deemed to have jurisdiction in accordance with the principles of private international law as applied by Jersey law, may in appropriate circumstances be recognised and enforced by the Jersey court without a substantive re-examination of the merits. The case arose in the context of seeking to enforce a judgment for specific performance of a settlement agreement in the long-running litigation involving Prince Jefri Bolkiah. The rule that only monetary judgment could be enforced had stood for some 200 years and was reflected in Rule 35.1 of Dicey Morris & Collins. However, the Jersey Court (following Canadian and Caymanian jurisprudence (in *Pro Swing Inc. v. Elta Golf Inc.* 2006 SCC 52 and *Miller v Gianni* [2007] CILR 18 respectively) held that the time for change had come and the old rule should be adapted for the modern age where remedies such as specific performance are important. However, the Jersey Court have did not give any specific guidance as to what constitutes "appropriate circumstances", and each case will be treated individually on its facts.

Other cases in Jersey in the past 12 months or so in the area of trust law have similarly been concerned with the basis upon which non-monetary judgments may be recognised and given effect to. In *Elder v Stock* [2009] JRC 034 (25 February 2009) the Royal Court considered Rule 35.1 in the context of enforcement of a Judicial Settlement (i.e., court approved resolution) from Liechtenstein regarding assets held in Jersey. The Court concluded that that

was essentially equivalent to a judgment and as it was essentially for a monetary sum and met other requirements (finality and jurisdiction) it would be enforced.

In *The Matter of the IMK Family Trust* [2008] JRC 136 (15 August 2008), which was appealed to the Jersey Court of Appeal and reported as *Representation of Aaliya Mubarak* [2008] JCA 196 (19 November 2008) the question of the recognition of an English judgment purporting to alter the terms of a Jersey trust was considered. A detailed consideration of the trust law regarding such a situation is beyond the scope of this article (and has been the subject of a number of cases in the past few years). However, the Court did consider the 1960 Law and concluded that it did not apply (the judgment not being for a monetary sum); further, on the basis of provisions of the Trust (Jersey) Law 1984, the judgment of the English Court purporting to vary a Jersey trust could not be enforced and recognition and enforcement purely on the basis of comity was also rejected. The Court confirmed that the proper approach to this issue is for a trustee to seek directions from the Jersey Court as to whether effect should be given to the judgment, and in doing so enable the Court to consider the interests of the beneficiaries as a whole.

Conclusion

The fact that Jersey is party to very few treaty arrangements concerning enforcement demonstrates the limitations on enforcement measures available, but either under statute (for UK judgments) or by applying the common law, where Jersey has shown itself to be attuned to modern commercial needs, there are ways and means of seeking to enforce foreign judgments in Jersey. The giving of effect to foreign judgments in which purport to vary or alter Jersey trusts is a topic that has seen much judicial comment in the past years but now appears to be clearly stated by the Court of Appeal. Even where judgments fall outside the 1960 Law and common law principles, there is still the prospect that they may nevertheless be recognised by the Jersey Court as conclusive between the parties in all proceedings founded on the same cause of action, and may be relied upon by way of defence or counterclaim in any such proceedings.

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BRITISH VIRGIN ISLANDS

Developments in the Eastern Caribbean Supreme Court, Commercial Litigation and the Litigation Marketplace

BY IAN THOMPSON | FTI CONSULTING

There have been notable recent developments in the Eastern Caribbean Supreme Court system, which are significant both for the British Virgin Islands ("BVI") and the Eastern Caribbean region as a whole. This reflects the fact that commercial litigation matters – particularly in the BVI – are increasing in number, complexity and value, which has led in turn to significant expansion in the litigation marketplace.

The Eastern Caribbean Supreme Court

The Eastern Caribbean Supreme Court was established by the West Indies Associated States Supreme Court in 1967. It comprises nine Eastern Caribbean States and, prior to the developments described below, consisted of the High Court and the Court of Appeal. Its headquarters are in Castries, St Lucia, and it has offices in each of the member states.

The New Commercial Court

The BVI is one of the nine member States, and it has recently seen the opening of a state-of-the-art Commercial Court, which houses the new Commercial Division of the Eastern Caribbean Supreme Court. The Commercial Court will hear commercial matters from all nine States, which comprise Anguilla, Antigua & Barbuda, Dominica, Grenada, Montserrat, St Kitts & Nevis, St Vincent & the Grenadines and St Lucia, as well as the BVI.

As part of the Eastern Caribbean Supreme Court system, the Commercial Division will adhere to the mission of its parent body, namely to provide for members a system of justice that is accountable and independent, and administered by officers in a prompt, fair, efficient and effective manner.

In order to be heard, claims must have a value of more than $500,000, and/or concern commercial, insolvency, trust, business arrangements, dissolution, or matters of a similar nature. While most of the cases heard relate in some way to the BVI's financial services industry, local and regional business disputes are also heard.

The addition of the Court will not necessarily drive business to the territory, since few if any set out to have a commercial dispute. However, it is nonetheless important, for both the BVI and the Eastern Caribbean as a whole, to have an institution which provides litigants access to a specialised tribunal and procedural rules. In relation to its rules, a detailed practice direction was brought into force at the end of 2009, which provides for the efficient hearing of large and complex matters.

The Court officially opened on 30 October 2009, having heard cases since May 2009. At the opening of the Court, Acting Justice of Appeal, His Lordship, the Honourable Justice Michael Gordon QC, said that since the establishment of the Commercial Division in May, there had already been 6 full trials, 45 heavy applications and 120 short applications. This clearly illustrates just how much work there is.

The BVI as a Financial Centre, and the Increase in Litigation

The BVI is one of the largest offshore financial centres in the world, with over 850,000 companies having been incorporated there. The existence of such a large number of companies has itself led to substantial growth in commercial litigation, although this has also been fuelled by the global economic downturn and the ever increasing complexity of businesses, and offshore structures in particular.

Where once litigation in the BVI frequently concerned straightforward shareholder disputes, now long-running, multi-jurisdictional actions involving billions of dollars and appeals to the Privy Council are commonplace. Some of the largest Madoff feeder funds are registered in the BVI, and almost every law firm on the island is engaged with Madoff matters of one sort or another.

In addition to Madoff-related matters, the Commercial Court has already heard disputes involving oil and gas concerns in Indonesia, the division of family assets in Russia, and insolvency matters in relation to assets in Brazil, Hong Kong, China, Europe and the United States. This illustrates the considerable geographic scope, as well as the calibre, of the matters before it.

It is worth pointing out, however, that all these developments must be good for the other member States of the Eastern Caribbean Supreme Court, and not just the BVI. That their disputes are being heard in such a high profile and sophisticated environment can only create more confidence in the judicial system, and therefore be beneficial for those jurisdictions too.

The First Judge of the Commercial Court, and the Need for Speed

It is significant that the first Judge of the Commercial Court is Mr. Justice Edward Bannister QC, formerly a leading commercial silk at 3 Stone Buildings. Mr Justice Bannister will be responsible for supervising the establishment and organisation of the new Commercial Division, presiding over all stages of litigation up to and including trial, and assisting in the development of rules of procedure and practice as referred to above. That an eminent silk was chosen for the job illustrates the level at which the Court is expected to operate.

In a recent interview with the publication “Business BVI”, Mr Justice Bannister said the following about how he hopes the Court will function: “I want the Court to attract as much new business as possible and to be as user-friendly as possible. Apart from being courteous, this means hearing cases as quickly as possible and getting decisions out as speedily as I can. Parties have normally invested a huge amount of money and they want to know what the answer is. My judgements tend to be short, but I aim to get them out in a matter of days, not weeks. I regard speed as very important.”

These sentiments echo the words of the Honourable Chief Justice Hugh Rawlins who, in marking the opening of the new 2009/2010 law year, made the following remarks about the new Commercial Division: “This Division is intended to specialize in and bring a new and dynamic dimension to cross-border litigation…The aim of this division of the Court is to facilitate the speedy and efficient resolution of commercial cases in our system, in a manner that permits the Court to maintain a competitive international profile.”

However, it is not just the Court that has to work fast. Despite the increase in complexity of litigation matters, they nonetheless move at remarkable speed. In complex, multi-jurisdictional fraud cases, time is measured in days and weeks, not months; liquidators need to move swiftly to recover assets; and clients often require an initial response within hours from accountants on the ground, working alongside litigators.

Growth in the Litigation Marketplace, and the Likely Consequences of Change

Given the increase in litigation – both in volume and complexity – it is unsurprising that the litigation marketplace is growing. Established firms in the BVI such as Harneys, Conyers Dill and Pearman, Maples and Calder, Walkers and Forbes Hare have all expanded their litigation departments, and two new firms have recently arrived in the territory: Withers is the first onshore law firm to venture offshore (primarily owing to the increasing number of onshore matters that have an offshore element or elements), and Lennox Paton, a leading Bahamian practice, has also recently arrived.

Times, therefore, appear to be changing in a number of ways: matters are becoming more complicated, there are more of them and they are being heard in a more sophisticated environment than was previously the case. Given these developments, it seems likely that the need for litigation, insolvency, forensic accounting and financial investigation specialists in the BVI and the wider Caribbean can only increase.

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