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Challenge of Errors in Arbitrators' Awards

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How the dispute arose

The House of Lords has just delivered its decision in *Lesotho Highlands Developments Authority v Impregilo* [2005] UKHL 45, which began its journey through the courts as a case on the scope of arbitrators' powers in respect of currency and interest, but ended up as a consideration of review of arbitrators' awards. It is this latter aspect which is likely to be of relevance to readers of *Asian Dispute Review*.

The Katse Dam in Lesotho, in southern Africa, was a major component of the Lesotho Highlands Water Project, a World Bank funded project largely built by a consortium of international contractors, known as Highland Water Venture (HWV). The contract used was an amended version of FIDIC 4th edition, which contained an arbitration provision incorporating the ICC Rules. A dispute arose following claims by HWV for extra labour costs and other expenses. The ICC arbitration was held in London in 2001 and in 2002, the tribunal, composed of three experienced London-based lawyers, delivered its award, which was in favour of HWV on three of its seven claims. The contractors were awarded £1.6 million (HKD 22,215,156) and £5.96 million (HKD 56,541,524), plus interest.

The clients, the Lesotho Highlands Development Authority (LHDA), challenged

the award under the UK's Arbitration Act, arguing that the arbitrators had exceeded their substantive jurisdiction and/or had been guilty of serious irregularity.

The arbitrators' powers on currency and interest

The basis of LHDA's challenge to the award in summary was that the arbitrators had not applied the provisions of the contract in making the award, either on interest or on the currencies in which the award was made. The latter was significant because Lesotho's currency, the maloti, had suffered serious depreciation in common with the South African rand, to which it is linked.

In the Commercial Court (at first instance) [2003] BLR 98, the judge found for LHDA on both points:

"With great respect to the tribunal, I consider that they did not have the power to make an award in a currency different from that provided for in the contract". Similarly, "for the same reasons as applied to the currency of the award, I consider that the tribunal have exceeded their powers under section 68 of the Arbitration Act and the issue of interest will have to be reconsidered by them having regard to the terms of this judgment". The Court of Appeal, in its decision [2003] BLR 347 of July 2003, upheld this result



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on both grounds. Lord Justice Brooke, giving the sole judgment of a unanimous court, found that the arbitrators were wrong to have departed from the provisions of the parties' agreement: "I therefore agree with the judge that the arbitrators exceeded their powers when they thought that section 48(4) of the 1996 Act gave them any power to depart from what the parties had agreed". "The arbitrators therefore exceeded their powers when they had recourse to what would have been their discretionary powers in Section 49(3) to resolve a matter to which they should have applied the substantive law of the contract".

A different approach in the House of Lords appeal

Neither the Commercial Court nor the Court of Appeal seems to have had much difficulty with their decisions on the LHDA challenge. They saw nothing wrong with such a challenge being brought and were clear that the arbitrators had acted in excess of their powers in the award.

However, HWV, in appealing to the House of Lords, perhaps not surprisingly took a different line of attack. Because this was an ICC arbitration, the parties were taken to have agreed to forego the right to legal challenge of an award. Article 28 provides that "The parties undertake to carry out any Award without delay and shall be deemed to have waived their right to any form of recourse insofar as such waiver can be validly made". The effect of this is that exclusion of legal challenge to the award binds the parties, just as far as the procedural law of the arbitration allows. Under the English Arbitration Act 1996, the right under s.69 to "appeal to the court on a question of law arising out of an award made in the proceedings" is subject to the reservation "Unless otherwise agreed by the parties". So the net effect of the ICC Rule under English law is to exclude challenges "on a question of law arising out of an award". LHDA had not, naturally, applied under s.69. Their challenge was under s.68(2)(b) on the ground of an excess of power.

In the House of Lords, HWV argued that LHDA could not challenge the award at all on the basis of what was actually, they said, an error of law. Morison J had commented at first instance that "The court

is astute to ensure that what is, in substance and reality, a section 69 challenge, for which permission is required, is not dressed up as a challenge under section 68 or 67" but he was satisfied that it was not and the Court of Appeal made virtually no comment on the issue at all.

Despite this background, the House of Lords concentrated largely on this issue. In doing so, they transformed the case into an examination of whether arbitration awards, specifically ICC awards, should be challenged before the courts.

Lord Steyn's approach

The main speech in the House of Lords was given by Lord Steyn. He drew a distinction between an excess of jurisdiction and an excess of powers. He thought the Commercial Court and the Court of Appeal had been wrong to categorise an error of law by the arbitrators as an excess of their jurisdiction: "If it is merely a case of erroneous exercise of power vesting in the tribunal no excess of power under section 68(2)(b) is involved".

Lord Steyn was not, in any event, convinced that the arbitrators had made any such error of law in interpreting their powers in relation to currency and interest.

Referring to the "radical nature of the changes brought about by the Arbitration Act 1996" he concluded that "It is in the arbitration agreement, read with the curial law, in this case the Arbitration Act 1996, that the powers of the tribunal are to be found and not in the underlying contract".

Further, the tribunal could award interest under its general powers under s.49(3) of the Arbitration Act.

Crucially, Lord Steyn also considered what would be the position if he were wrong, so that the arbitrators *had* committed an error of law. He believed that the outcome would still be the same.

This was crucial because the other Law Lords did not agree that there had been no error of law by the arbitrators in the way they had exercised their powers. Lord Hoffmann, while not committing himself on the point, thought it "very likely that the arbitrators did

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make an error of law in calculating the sums awarded in the way in which they did". Lord Scott of Foscote considered that "it might well be that the selection by the arbitrators of historic exchange rates rather than the current ones constituted an error of law". Lord Rodger of Earlsferry took a similar line.

Lord Phillips, the UK's new Lord Chief Justice, who dissented from the overall view of the majority, in holding that the arbitrators had exceeded their powers, was not surprisingly sure that they were wrong in law: "the arbitrators have adopted an approach to currencies that departs from English law ... They expressly stated that section 48(4) gave them a discretionary power which they did not in fact enjoy and then proceeded to purport to exercise that power".

So it may be seen that four of the five Law Lords were of the opinion that the arbitrators had been wrong in law in the exercise of their powers. Yet the result was that the appeal was allowed, the decisions of the two previous courts overturned and the arbitrators' award upheld. Such a dramatic outcome demands further explanation.

The decision explained

With the exception of Lord Steyn's view, (and, as mentioned, he prudently considered the situation if he were wrong), there was general agreement amongst the judges that the arbitrators had made errors, at least in failure to apply the contractual provisions as to currencies in which payment should be made. Taking account of the first instance and Court of Appeal judges, eight out of nine judges who heard the case thought that the arbitrators were wrong.

The ICC Rules exclude legal challenge as much as is permissible under the arbitral law of the country in question. Therefore what is allowable by way of exclusion will vary from country to country. Under English law, the parties are allowed to exclude errors of law from challenge if they agree to do so. By opting for the ICC Rules they had agreed to do so.

The parties could not have excluded an excess of jurisdiction, because the English Arbitration Act does not allow them to do so.

Therefore the crucial point was how to characterise or categorise the error which the arbitrators had made. This is frequently not an easy matter and in this case there were two clear and conflicting views amongst the judges.

The view of five of them (the Commercial Court, the Court of Appeal and Lord Phillips) was that the arbitrators had exercised a power which they did not have. The contract provided for the currencies of the payment and in ignoring it and expressing the award in currencies determined by them, the arbitrators went beyond their powers. That would be reviewable, even under ICC Rules.

The view of the other 4 (namely the majority of the House of Lords) was that the arbitrators have powers, including powers relating to interest and currency of awards. If they do not exercise those powers in accordance with the contract, that is an error of law but not an excess of power. This would not be reviewable under ICC Rules.

The significance of the LHDA decision

The decision of the House of Lords has been greeted by some commentators as creating a benefit for international arbitration and, somewhat melodramatically, as having averted disaster for London as a centre for international arbitration. Their contentions can be summarised as follows. If LHDA were able to challenge the award, this would open the floodgates to challenge of awards in many other cases, where a disappointed party was seeking to re-open the case in an attempt to reverse the outcome. The effect of this, so the argument ran, would be that finality would be lost and confidence in London would be destroyed, since parties would be too fearful of frustration of the process by lengthy and costly court hearings carrying the prospect of an uncertain result. The more extreme version of these arguments suggested that London had already suffered significantly from such an erosion of confidence amongst parties to international disputes.

However, this point of view overlooks certain aspects of the issue.

Hostility to the idea of challenge of arbitrators' awards is based on the perception that the users of

the arbitration system, namely the disputants, will be averse to anything which is detrimental to finality. This is seen as leading to cost and to delay. There is also an implication, although this is not always made explicit, that parties and their legal advisers might exploit the opportunity of challenge in order to frustrate the proper course of events following the award and perhaps to delay the payment of money, even with a very weak case.

This line of argument seems to be overstated. It is an inherent part of the arbitral law of any developed legal system that challenge to an award will be possible in certain circumstances. Finality cannot therefore be the sole criterion. Parties have to be protected against arbitrators who purport to exercise powers which they do not have or who act in bad faith or who produce awards which are incapable of enforcement. So the courts will always be given some scope to allow challenge of awards. Neither ICC nor any other arbitral institution can take that away and it is surely safe to assume that they would not wish to do so. Indeed, the ICC has its own Court of Arbitration which scrutinises awards, although it appears that it may not be suitable for identifying arbitrator errors of this kind. The British Parliament, through the Arbitration Act 1996, entrusted the courts with the task of scrutiny of awards challenged on grounds of serious irregularity. In doing so, it presumably had no fear that the courts would be unable to deal efficiently with any unmeritorious challenges, indeed the English courts are fairly ruthless in doing so. So it is hard to see why there should be a fear that the existence of the possibility of challenge of an award would of itself be an opportunity for exploitation by the unscrupulous. The parties might decide that the arbitrators are best placed to ascertain the facts and agree not to challenge those before any other tribunal, but it is not very radical to see a court as best placed to determine whether the arbitrators have correctly applied the law in exercising their powers.

A better way of looking at the law of arbitration (in every jurisdiction) is as a balance between the attractions of a speedy and robust decision and enforcement which will lead to a swift resolution and protection against occasional error, which even the most experienced arbitrators, being human, may commit.

Conclusion

The *LHDA* case is seen by its supporters as having decided in favour of finality, which they regard as wholly beneficial. This seems too simplistic a view. The actual impact of the case on international arbitration and upon London may not be very significant at all. No convincing evidence has been put forward that London became a less credible centre for arbitration in the two years following the Court of Appeal's decision. Not all arbitral regimes seek to close off challenges like ICC. The UNCITRAL Rules have no equivalent to ICC Article 28, so if an arbitrator goes wrong in law under that regime, a party can challenge the award, under English law amongst others. If there is a serious irregularity, a challenge can be brought under English law, even under ICC Rules, even after the *LHDA* case. No doubt the ICC Court will pick up errors of some kinds and the arbitrators will be requested to review the award. In many cases, of course, arbitrators will not make errors of law and no opportunity for challenge will arise under any jurisdiction.

The net effect of the *LHDA* case appears to be that certain kinds of errors of arbitrators in the exercise of their powers will be protected against review under ICC Rules. This is bad news for a party which suffers loss under the award because the arbitral tribunal has gone wrong. It might encourage that party not to use that arbitral regime, if it is to be unprotected. Finality is a desirable quality of the arbitral system, but not at any price. The House of Lords decision has drawn attention to the tension between finality and protection and will be of interest to those involved in international arbitration for that reason.

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