



AUSTRALIA'S HIGHEST COURT APPLIES THE HAND BRAKE TO ARBITRATION: INADEQUATE REASONS RENDER AWARD INVALID

The underlying difference between arbitration and court litigation should be borne in mind at all times.... Though courts and arbitration panels both resolve disputes, they represent fundamentally different mechanisms of doing so. The Court is an arm of the state; its judgment is an act of state authority, subject generally in a common law context to the right of appeal available to parties. The arbitration award is the result of a private consensual mechanism intended to be shorn of the costs, complexities and technicalities often cited as the indicia and disadvantages of curial decision making.

These are the words of the President of the New South Wales Court of Appeal.¹ Almost without exception, the last few years in Australia have seen both legislative and judicial encouragement of the arbitration process.² However, in overturning the Court

of Appeal's decision on an important aspect of arbitration practice (being the circumstances in which a party may appeal to the court from an arbitral award), the High Court, in the *Gordian Runoff* case,³ recently held that the reasons provided by an arbitral tribunal were inadequate such as to amount to a manifest error of law.

The High Court also took the opportunity to take a shot at the suggestion that the arbitral function is purely a private matter of contract, finding that the statutory regime for arbitration in Australia "displays a legislative concern that the jurisdiction of the courts to develop commercial law not be restricted by the complete insulation of private commercial arbitration."⁴ This *Commentary* considers the decision in *Gordian Runoff* and its potential implications for international commercial arbitration in Australia.

BACKGROUND FACTS

The underlying dispute between the parties in *Gordian Run-off* concerned whether reinsurance treaties covered a particular policy and, if not, whether §18B of the Insurance Act 1902 (NSW) operated so as to extend cover to the policy. The reinsurance treaties contained an arbitration agreement.

The details of the dispute are not pertinent to this *Commentary*, except that it should be noted that the subject matter of the arbitration was described by the High Court as complex, involving the construction of insurance contracts and statutory interpretation. It “proceeded along the lines of the conduct of a commercial cause in a superior court.”⁵ There were three arbitrators who proceeded to determine the dispute based upon detailed pleadings that extended to more than 60 pages. The parties were represented by senior barristers; witnesses were cross examined, and there were many documents admitted into evidence.

The arbitral tribunal issued an award in which it accepted the reinsurers’ interpretation of the reinsurance treaties but held that by operation of §18B, the reinsurers were obliged to extend cover.

Section 38 of the Commercial Arbitration Act, 1983 (NSW)⁶ permitted a court to grant leave to review the decision of an arbitral tribunal if there was a “manifest error of law on the face of the award” or there was an error of law, the determination of which would add substantially to the certainty of commercial law. Section 29 of the same act required arbitrators to include in the award a statement of the reasons for making the award. The reinsurers appealed against the award to the New South Wales Supreme Court. This was successful. The New South Wales Court of Appeal overturned the trial judge’s decision.

THE DECISION OF THE HIGH COURT

The errors in the award that the reinsurers identified for the purpose of the appeal to the High Court were that the tribunal:

- Failed to give adequate reasons as to why §18B of the Insurance Act applied; and
- Erred in its construction of §18B of the Insurance Act.

The High Court upheld the appeal from the New South Wales Court of Appeal. It found that the Court of Appeal had erred in not concluding that the arbitrators had failed to give reasons for their conclusion that it was reasonable for the reinsurers to be required to indemnify Gordian within the meaning of a proviso to be found in §18B(1) of the Insurance Act. It also cited their conclusion that considerations of general justice and fairness did not compel the conclusion that the reinsurers should not be required to indemnify Gordian. The arbitrators’ conclusion as to the operation of §18B of the Insurance Act and failure to give adequate reasons for the conclusion amounted to a manifest error on the face of the award—that is, the existence of the error is apparent to the reader of the award.⁷

In considering the exercise of the discretion whether or not to grant leave to review the award, the High Court referred with approval to the balancing act described by Lord Diplock in *The Nema*⁸ as follows:

[T]his, in the case of a dispute that parties have agreed to submit to arbitration, involves deciding between the rival merits of assured finality on the one hand and upon the other the resolution of doubts as to the accuracy of the legal reasoning followed by the arbitrator in the course of arriving at his award, having regard in that assessment to the nature and circumstances of the particular dispute.

The High Court made a number of findings that are likely to affect the practice of arbitration in Australia. Those findings include:

- Arbitrators’ reasons are not necessarily required to be to a “judicial standard.” While no wholly satisfactory formula can be found to flesh out the requirement to give reasons, the adequacy of the reasons will depend upon the nature of the dispute and the particular circumstances of the case.

- In the circumstances of the *Gordian Runoff* case, the High Court held that the arbitrators, having determined that §18B was a critical element in reaching their award, were obliged to explain succinctly why the various integers in that complex statutory provision were satisfied.
- The arbitrators should have, but failed to, indicate the factual findings that supported a finding that a material proviso in the statute was inapplicable, nor did they indicate why it was reasonable in all the circumstances to hold the reinsurers bound to indemnify Gordian. The arbitrators also failed to consider aspects of the reinsurers' pleaded case.
- A "reasoned" award requires arbitrators to explain succinctly why, in light of what happened, they have reached their decision and what that decision is. More was required in this case than a statement of conclusion.⁹
- Failure to provide adequate reasons was a manifest error of law, which enlivened the discretion in §38 of the Commercial Arbitration Act to grant leave to review the award.
- Rather than remitting the matter back to the arbitrators for further reasons (as suggested by the Court of Appeal to be the appropriate remedy), the High Court restored the primary judge's orders setting aside the award.

IMPACT OF THE HIGH COURT'S DECISION

It might be suggested that the impact of the High Court's decision in *Gordian Runoff* is limited because the High Court was considering arbitration legislation that has been superseded.¹⁰ While the successor legislation both domestically and internationally¹¹ requires (unless the parties agree otherwise) that the arbitrators must state the reasons upon which the award is based,¹² at least in relation to international arbitrations, the adoption of the UNCITRAL model law removes the right to seek leave to appeal if there is manifest error of law on the face of the award. This is significant and calls into question what impact *Gordian Runoff* will have on international commercial arbitrations undertaken in Australia.

Despite the changes to the arbitration legislation in Australia, the majority's judgment was, in part at least, driven by policy considerations: that the courts of Australia are required to maintain an active role in the arbitration process to develop commercial law in this jurisdiction so as to ensure that doubtful legal reasoning is able to be corrected. This leaves little doubt that the High Court's decision in *Gordian Runoff* was not intended to be confined to the particular facts and statutory scheme presented to the court in this case.

Article 34(2)(ii) of the UNCITRAL model law permits a party to challenge an award on the ground that it is contrary to the public policy of Australia. A challenge to an arbitral award that fails to give adequate reasons for the findings on the ground that it is contrary to public policy in Australia for commercial disputes to be resolved in such a manner would, to the best of our research, be novel. However, similar to most final courts of appeal, Australia's High Court determines only questions of law of such fundamental importance that they require consideration by the highest court of the land.¹³ That the case might have significant impact upon arbitration practice in Australia in the future is also apparent from the fact that the Commonwealth, the Australian Centre for International Commercial Arbitration, the Australian International Disputes Centre, the Institute of Arbitrators & Mediators Australia, and the Chartered Institute of Arbitrators (Australia) all appeared as amici curiae at the hearing.

While the impact of this decision on international commercial arbitration remains to be seen, it seems likely that:

- Arbitrators are required to give adequate reasons in an award for the conclusions reached;
- The adequacy of the reasons for an award is to be determined having regard to the circumstances of the particular dispute;
- If the subject matter of the dispute involves interpretation of statutory instruments, then the reasons need not necessarily be to a judicial standard but should set out the reasons why the various elements of the relevant statute do or do not apply;

- Awards should be reasoned, meaning that they should set out why, in light of what happened, the arbitrators have reached their decision;
- An arbitrator's failure to provide adequate reasoning in an award makes the award susceptible to challenge by the courts in Australia.

COMMENT

The High Court's decision appears to show a judicial preference for ensuring accurate legal reasoning in awards over the merit of assured finality in the arbitration process. Such a predisposition undermines the perceived benefits of the process. This was described by Heydon J (in his dissenting judgment¹⁴) as follows:

The arbitration proceedings began on 15 October 2004.... This appeal comes to a close seven years later. The attractions of arbitration are said to lie in speed, cheapness, expertise and secrecy.... But it must be said that speed and cheapness are not manifest in the process to which the parties agreed. A commercial trial judge would have ensured more speed and less expense. On the construction point it is unlikely that the arbitrators had any greater relevant expertise than a commercial trial judge. Secrecy was lost once the insurers exercised their right to seek leave to appeal. The proceedings reveal no other point of superiority over conventional litigation. One point of inferiority that reveals is that there have been four tiers of adjudication, not three.

Perhaps more importantly, the High Court decision in *Gordian Runoff* may give rise to a perception that Australia is not an arbitration-friendly environment. Such a perception would be unfortunate. Australia remains a jurisdiction that encourages arbitration. This is apparent from the concerted efforts of the federal and state legislatures to enact legislation designed at encouraging and streamlining the arbitration

process (including being one of only 12 countries to have enacted as domestic law the UNCITRAL model law), the establishment of the Australian International Disputes Centre, and the recent updating of the ACICA (the sole default appointing body in Australia) Rules.

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ENDNOTES

- 1 *Gordian Runoff Limited v Westport Insurance Corporation* [2010] NSWCA 57, at 216.
- 2 See *Jones Day Commentary*, "Arbitration in Australia: How Recent Reforms Have Improved the Conduct of International Arbitration and the Enforcement of Awards" (August 2010), available at www.jonesday.com/arbitration_in_australia/.
- 3 *Westport Insurance Corporation v Gordian Runoff Ltd* [2011] HCA 37.
- 4 Per the majority, French CJ, Gummow, Crennan, and Bell JJ at 19.
- 5 Per the majority, French CJ, Gummow, Crennan, and Bell JJ at 5.
- 6 Which Act governed domestic commercial arbitrations that took place in New South Wales at the relevant time.
- 7 *Ibid* at 42.
- 8 [1982] AC 724 at 739.
- 9 Per Keifel J, at 169-170. This finding is to be compared with the New South Wales Court of Appeal decision of Alsop P, in which he stated that the reasons were adequate "in that they indicate to the parties why the arbitrators reached the conclusion to which they came." [2010] NSWCA 57, at 186.
- 10 The High Court's decision was based upon the construction of the old Commercial Arbitration Act, 1984.
- 11 Commercial Arbitration Act, 2010 (NSW); International Arbitration Amendment Act 2010 (Cth), which enacted the UNCITRAL model law.
- 12 Article 31(2) of the UNCITRAL model law.
- 13 "The High Court as Gatekeeper," the Hon Sir Anthony Macon AC KBE (2000) MULR 31, at 32.
- 14 *Ibid* at 111.