

Insights

VALE SA V STEINMETZ: ENGLISH COURT HELD THAT AN ARBITRAL DECISION CANNOT BE RELIED UPON IN PROCEEDINGS BETWEEN NON-PARTIES

Oct 12, 2021

SUMMARY

In a recent English judgment, *Vale SA and others v Steinmetz and others* [2021] EWCA Civ 1987, which concerned the effect that an arbitral award had upon a proprietary claim against a non-party to the arbitration, the Court of Appeal affirmed what is regarded as being a “clear and considered statement of principle”. Save for limited purposes, an arbitral award between A and B generally has no binding effect in proceedings between A and C.

Background facts

Vale SA v Steinmetz related to an arbitral award issued under the LCIA Rules (the “LCIA Award”) which was handed down after a large-scale arbitration which last over five years. A simplified version of the background facts to the substantial arbitration and the subsequent court proceedings is as follows.

Party A (Vale SA) paid certain money, known as the “Initial Consideration”, to Fraudster B (BSGR) under a contract. At least some part of the Initial Consideration subsequently was transferred by Fraudster B to Beneficiary C (Balda and Nysco).

The parties were able to agree on some points of law. It was common ground between the parties that if the contract was voidable for fraud, the innocent Party A’s right to rescind the contract would give rise to an equity, such that upon rescission the payment made by Party A would be impressed with a constructive trust. The parties also accepted that this equity in principle could be asserted against Beneficiary C because they were not good faith purchasers for value without notice of the fraud.

By virtue of the LCIA Award, the contract between Party A and Fraudster B was rescinded for fraudulent misrepresentation. The arbitral tribunal held that Party A was not entitled to the return of

the Initial Consideration based on restitution (by way of *restitutio in integrum*), because the Initial Consideration originally had not been paid to Fraudster B by Party A but by Party A's subsidiary. Instead, the tribunal required and ordered the payment by Fraudster B to Party A of a sum which included the amount of the Initial Consideration as damages for fraudulent misrepresentation.

Fraudster B did not pay any part of the awarded sum to Party A. Party A therefore brought proceedings in court against the related parties including Fraudster B and Beneficiary C. One of the claims brought by Party A was a proprietary claim over assets held by Beneficiary C as recipients of traceable proceeds of the Initial Consideration.

Beneficiary C applied for summary judgment to dismiss the proprietary claim against them on the basis that the proprietary claim was bad in law in the light of the tribunal's decision to reject Party A's restitution claim. The judge dismissed the application and further declared that the LCIA Award did not afford Beneficiary C any defence to Party A's proprietary claim.

Beneficiary C appealed.

The issue before the English Court of Appeal

One of Beneficiary C's lines of argument was that there could be no proprietary claim by way of a constructive trust against Beneficiary C unless Fraudster B also was liable to a restitutionary claim. Beneficiary C's liability was said to be parasitic on the liability of Fraudster B. The LCIA Award already made clear that Fraudster B had no obligation to return the Initial Consideration by way of *restitutio in integrum*. This determination was said by Beneficiary C to constitute a "fact in the world" binding Party A for all purposes. For the present purpose, it meant that Party A had no personal restitutionary claim against Fraudster B and also that no constructive trust had ever come into existence. Therefore, Beneficiary C as transferees of the Initial Consideration could not have been subject to any such trust.

Although the facts of the background arbitration were complex, the Court of Appeal took a step back from the detail and considered the narrow issue of whether Party A was bound by (or, to the same effect, whether Beneficiary C could take the benefit of) the LCIA Award in the court proceedings between Party A and Beneficiary C.

An award between A and B does not bind C

First of all, the arbitral tribunal rejected Party A's claim for restitution on the basis that payment of the Initial Consideration had not been made by Party A but by its subsidiary, but then awarded damages to Party A on the basis that the Initial Consideration was a loss which Party A (not its subsidiary) had suffered. The Court of Appeal agreed with the judge's observation that this part of the arbitral tribunal's reasoning as set out in the LCIA Award was internally inconsistent and impossible to reconcile. The LCIA Award must have been wrong at least to some extent.

Notwithstanding what was said about the correctness of the LCIA Award, the Court of Appeal pointed out that when the parties agreed to arbitrate their differences under the LCIA Rules, they agreed to be bound by the LCIA Award, even if the tribunal may have got the law or the facts wrong.

The Court reiterated that arbitration is a consensual process by which parties agree to resolve disputes by accepting the decision of a tribunal chosen by them or in accordance with an agreed procedure. An award thus produced is final and binding on them (Party A and Fraudster B in this case). It makes no difference whether the award is right or wrong. Just as Beneficiary C had not agreed to be bound by the tribunal's decisions in the arbitration between Party A and Fraudster B, neither had Party A agreed to be bound by any of the tribunal's decisions in any dispute he may have against Beneficiary C.

The Court went on to say that unless the third party (Beneficiary C in this case) can be regarded as a privy of one of the parties (Fraudster B in this case) for the purpose of the doctrine of *res judicata* (which was not a point suggested or pursued by any of the parties), the LCIA Award was final and binding only as between Party A and Fraudster B, and was not binding on Beneficiary C.

Two case authorities, *Ward v Savill* [2021] EWCA Civ 1378 and *Sun Life Assurance Co of Canada v Lincoln National Life Insurance Co* [2004] EWCA Civ 1660, [2005] 2 CLC 664, were cited by the Court in support of its conclusion that, save for limited purposes not applicable to the facts of this case, the LCIA Award between Party A and Fraudster B had no binding effect in proceedings between Party A and Beneficiary C.

Therefore, the Court of Appeal concluded that it was open for Party A to seek to prove, in its court litigation against Beneficiary C, its proprietary claim against Beneficiary C. Party A was entitled to demonstrate that, contrary to the arbitral tribunal's view, it did have a valid personal restitutionary claim against Fraudster B, if this was what was necessary to establish its claim. The LCIA Award did not give Beneficiary C any defence to the proprietary claim made against them.

BCLP's comments

This judgment is a welcome addition to the body of case law which confirms the contractual and consensual nature of arbitration. The nature of arbitration self-evidently excludes claims and disputes as between parties who have not agreed to arbitrate.

Modern commercial transactions often involve more complex factual matrices with more than just two parties to a contract. More often than not, an agreement to arbitrate does not cover each and every relevant party to a project or a transaction¹. In that case, the winning party of an arbitration will not be able to enforce the award as against a stranger to the arbitration, even if that "stranger" in fact may be the most culpable. Similarly, a losing party of an arbitration is not necessarily faced with a dead end, for there possibly are remedies against other relevant but non-contractual parties which are worth pursuing.

Therefore, it is worth emphasising that the consensual process of arbitration is not intended to, and will not, replace completely the court system. Rather, it aims to provide a more suitable alternative for parties who wish to resolve disputes in a more private and controlled manner, along with the other perceived advantages of arbitration such as cross-border enforcement. In this regard, this judgment serves as a reminder of the nature and boundaries of arbitration.

1. Some complex agreements and/or arbitration rules allow for joinder of different arbitrations and/or joinder of parties, but those are exceptions to the general rule.

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