“Any Party May Submit the Dispute to Binding Arbitration”: the Privy Council Examines the Option to Arbitrate

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Introduction

The Privy Council, the final Court of Appeal for a considerable number of current and former Commonwealth countries and British Overseas Territories, has recently given a judgment of wide interest to arbitration practitioners and those looking to draft arbitration clauses in their agreements. In January this year, the Privy Council found in Anzen Limited and others v Hermes One Limited (British Virgin Islands) [2016] UKPC1 that a clause that provided that any party “may” submit a dispute to an arbitration would entitle a party against whom litigation had been commenced to a stay of proceedings, even where that party had not referred the matter for arbitration.

Background

The parties were shareholders in a BVI company. Clause 19.5 of the relevant shareholders’ agreement provided that, in the event of an unresolved dispute, “any party may submit the dispute to binding arbitration”. A dispute arose and the respondent commenced litigation in the BVI. The prospective claimants then applied for a stay of proceedings under the Arbitration Ordinance 1976 (British Virgin Islands), the relevant arbitration legislation in the BVI. In other words, the “First Party” to act had commenced litigation and not arbitration, but the “Second Party” wanted to stay those legal proceedings so that they could refer the dispute to arbitration. The Lower Court rejected the Second Party’s application. This was because the Second Party had only asked to refer the dispute to arbitration but had not formally commenced arbitration.
The Second Party appealed to the relevant Court of Appeal, but the Court of Appeal agreed with the Lower Court. They then appealed to the Privy Council, who allowed the appeal. That decision is the focus of this blog.

Three Possible Interpretations

The Privy Council considered that the key to the appeal lay in the proper construction of the clause’s wording: “any party may submit the dispute to binding arbitration”. It then identified three rival interpretations of that clause, calling them Analyses I, II and III, before ultimately rejecting Analyses I and II and ruling that Analysis III was the most appropriate.
Before choosing Analysis III, the Privy Council rejected Analysis I and Analysis II.

Analysis I was that the Clause prevented the First Party from commencing litigation at all. Under that first Analysis, a clause that said either party "may" arbitrate required the parties to refer their dispute to arbitration – the word "may" being interpreted as meaning the same thing as "shall". In rejecting this analysis, the Privy Council considered a wealth of cases from various jurisdictions which interpreted the above wording.
Analysis II was that the First Party was permitted to commence litigation, but subject to the Second Party's right to request that the matter be referred to arbitration instead. In such a case, the Second Party was required formally to commence arbitration proceedings in order for the courts first seized to stay the proceedings pending before them. This is what the BVI Courts had found in first instance and on appeal. The Privy Council found this analysis to be incongruous, preferring instead Analysis III.
Analysis III was that the First Party was permitted to commence litigation subject, again, to the Second Party's right to request that the matter be referred to arbitration instead, but the Second Party could obtain a stay by either (i) formally initiating arbitration proceedings, or (ii) by requesting arbitration proceedings to be commenced, or (iii) simply by applying for a stay. This is what the Second Party had in fact sought to do in this case. Where there is a choice between litigation and arbitration, commencing litigation will not prevent the Second Party from seeking a stay for arbitration, even where arbitration had not been commenced.
It is perhaps a little surprising that the court did not contemplate at all as an alternative interpretation of the word "may", the possibility that there is no agreement, but an agreement to agree. The usefulness of inserting such a clause would of course be questionable (because it cannot be specifically enforced in certain jurisdictions), but this interpretation would be closer to a literal interpretation of the word "may".

The Privy Council Opts For The Third Analysis

The Privy Council gave strong reasons for rejecting Analysis I, and with them a comprehensive and helpful overview of the current position regarding arbitration clauses expressed in terms of choice, election or option. This analysis will be of use to practitioners across many jurisdictions as the Privy Council drew from a wide selection of cases. In English law, the Privy Council cited Lobb Partnership Ltd v Aintree Racecourse Co Ltd [2000] CLC 431, where Colman J said that that such a clause strongly indicated that it would be open for the First Party to refer a dispute to arbitration if he chose to do so and that if he did so, the Second Party would be bound to accept that reference. The Lobb Partnership decision is consistent with the Canadian case of Canadian National Railway and others v Lovat Tunnel Equipment Inc (1999) 174 DLR (4th) 385, and the same reasoning was used in the Singapore High Court, in WSG Nimbus Pte Ltd v Board of Control for Cricket in Sri Lanka [2002] 3 SLR 603. The Privy Council also addressed a few cases in the United States that suggested "may" gave a mandatory meaning to arbitration clauses so that an agreement that a party "may" use arbitration had the same effect as one that said a party "shall" use arbitration if a party wanted to commence proceedings. These cases were said to have unpersuasive reasoning, and that they were decided in a non-commercial context.

This consistency of approach in construing these types of arbitration clauses is supportive of general principle. Clauses "depriving" a party of the "right" to litigate should be clearly worded and there is an obvious difference between a promise that a dispute shall be submitted to arbitration and a provision that a dispute may be submitted to binding arbitration. However, it could be said that at this point the court assumed the questionable view that litigation is somehow superior to arbitration and that it is the preferred option for users, who should therefore not be "robbed" of their sacrosanct right to litigate. This assumption is plainly inconsistent with empirical research on the matter, which demonstrates that the vast majority of businesses prefer arbitration over litigation for their cross border disputes.

This left the Privy Council with a choice between Analyses II and III.

Analysis II was said to be incongruous. Although this analysis purported to give each party a right to have a dispute submitted to arbitration, it allowed in fact the First Party to commence litigation and then only required the dispute to be referred to arbitration if the Second Party had formally initiated arbitration. If the Second Party is in fact a respondent with no counterclaims, that Second Party would only be able to seek a declaration of no liability, and no positive relief. This option may not be appealing given the costs involved in commencing arbitration. In sum, Analysis II would not make commercial sense.
This left Analysis III, which the Privy Council considered to be the better view. The Privy Council noted that there was no doubt that the court, under s.6(2) of the Arbitration Ordinance, had power to order a stay pending arbitration even though neither party has actually submitted, or will necessarily ever submit, the dispute to arbitration. In other words, submitting a dispute to arbitration was not inextricably linked to the actual commencement of arbitration. This position was decided by the House of Lords in Channel Tunnel Group Ltd v Balfour Beatty Construction Ltd [1993] AC 334. The Privy Council was therefore comfortable with Analysis III, where the Second Party would be permitted to seek a stay despite not actually initiating arbitration proceedings.

The Privy Council also considered Analysis III to be a better view on principle – parties to arbitration are under mutual proceedings to co-operate in the pursuit of the arbitration. The arbitration process is one underpinned by consent. In that regard, a notice that triggered the mutual agreement to arbitrate fit better into a consensual scheme than one which required the artificial construction and commencement of arbitration in respect of a cross-claim. Analysis III allows a party wishing for a dispute to insist on arbitration before or after the other party commenced litigation, without itself having to commence arbitration if it did not wish to. But court did not go on to ask what true practical benefit this might have. In the vast majority of cases in real life a party will submit its dispute to arbitration by commencing proceedings: either by filing a request to arbitration with the relevant institution, or by sending a Notice of Arbitration in an ad hoc arbitration context.

Conclusion

Anzen Limited helps those desiring of arbitration faced with litigation proceedings, but in circumstances where the arbitration clause provides only an option for arbitration instead of litigation. The Privy Council's decision bolsters the arbitration process, and, at least in theory, reinforces both its consensual nature and its relevance even in circumstances where the arbitration route is only expressed as an option. In reaching its decision, the Privy Council also clears up the proper construction of such arbitration clauses and sees both a consistency across jurisdictions and with general principles.
The Privy Council's decision is likely to be received in three ways by the arbitration community. First, the importance of clearly drafting arbitration clauses must be noted – parties and counterparties to contracts will be on notice that close drafting is required to ensure that the desired result is reflected in writing. Secondly, arbitration practitioners will welcome the Privy Council's decision. Where there is a choice between litigation and arbitration, commencing litigation will not prevent the Second Party from referring the dispute to arbitration. Thirdly, practitioners may be disappointed that despite its support of the arbitration process, the Privy Council gave its judgment in terms that still assumes the primacy of litigation, and in terms that failed to address the real-world, practical considerations of its analysis.