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Jurisdictional Decision Finding that an FAI Arbitration Clause in a Draft Agreement was Valid and Binding on the Parties

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Introduction

It is not unusual that parties to FAI arbitration proceedings raise various jurisdictional objections before the Finland Arbitration Institute ("FAI") and, provided that FAI will nonetheless allow the arbitration to proceed, subsequently also before the arbitral tribunal. Such objections come in all shapes and sizes. For example, respondent may dispute the existence of an arbitration agreement on the grounds that the main contract in which the alleged arbitration cause is embedded is merely a draft which was neither finalized nor accepted by the parties and which is therefore not binding on them. The following case from the recent FAI practice serves as an example of how an arbitral tribunal seated in Finland addressed this question under Finnish law.

Background of the dispute

An Irish company A had entered into negotiations with a Finnish company B with a view to signing a business contract. During the negotiations, the parties had exchanged various drafts of the agreement, all of which contained an arbitration clause providing for arbitration under the FAI Arbitration Rules ("FAI Rules"). The clause read as follows: *"Any dispute, controversy or claim arising out of or relating to this Agreement, or the breach, termination or validity thereof shall be finally settled by arbitration in accordance with the Arbitration Rules of the Finnish Central Chamber of Commerce."*

Once a dispute arose between the parties, A commenced FAI arbitration proceedings against B. In its answer to A's request for arbitration, B raised a jurisdictional plea, contending that there was no valid and binding arbitration agreement as the parties had never signed and accepted the alleged main agreement in which the purported arbitration clause was inserted. On the other hand, B also noted that, in the event that FAI allowed the arbitration to proceed, B agreed with A's proposal that there should be a three-member arbitral tribunal and that the seat of arbitration should be Helsinki, Finland.

Applying the *prima facie* jurisdictional test set out in Article 14 FAI Rules, FAI was satisfied that there may exist a valid FAI arbitration agreement binding on the parties, thereby allowing the arbitration to proceed and constituting a three-member arbitral tribunal as agreed by the parties. As B upheld its jurisdictional objection before the arbitral tribunal, the latter chose to determine the question of jurisdiction by issuing a separate jurisdictional decision at the outset of the

proceedings. In its decision, the arbitral tribunal found that there was a valid and enforceable arbitration agreement binding on the parties. Below is a summary of the reasons for the arbitral tribunal's decision.

Reasons for the arbitral tribunal's decision

(i) It is a well-established and fundamental principle of law that an arbitration agreement is a separate and independent agreement even when incorporated into a contract. Further, the validity and enforceability of an arbitration agreement is not dependent on the validity or enforceability of the underlying contract meant to be covered by the arbitration agreement.

(ii) It follows from Section 3 of the Finnish Arbitration Act (967/1992; "the Act") that a valid and enforceable arbitration agreement may exist even in the absence of a contract signed by both parties. The Act does, however, impose a requirement that an arbitration agreement must be in writing. According to Section 3, it may be formed by correspondence, or by exchange of telegrams or telex messages, or documents exchanged in another corresponding manner. Also a mere reference to a document containing an arbitration clause is sufficient to conclude a valid arbitration agreement.

(iii) A submits that it has sent the draft agreement containing the above-quoted arbitration clause to B for signing, but B failed to sign and return it to A. However, B never objected to the arbitration clause, and both parties have since then acted in accordance with the terms of the draft agreement.

(iv) A also submits that on *[date]*, B's officer Ms. X sent an email to the officers of A, as well as to other officers of B, proposing that an arbitration clause be incorporated into the draft agreement. The wording of the arbitration clause proposed by Ms. X was identical with the one that A had originally suggested to B.

(v) Furthermore, on *[date]*, Ms. X sent to the officers of both companies by email a slightly revised draft agreement, which contained yet again an arbitration clause of similar wording.

(vi) In light of the evidence produced to the arbitral tribunal, both parties have – allegedly by ordinary mail, and in any case by email (constituting "in another corresponding manner" in the meaning of Section 3 of the Act) – exchanged messages expressing their willingness to agree on an arbitration agreement of identical wording. Neither party has raised any objections.

(vii) Based on this documentary evidence, and applying Section 3 of the Act, a valid and enforceable arbitration agreement has been formed between the parties.

(viii) lt is, however, another issue whether or not the claims to be made and the relief sought in these proceedings are covered by the arbitration agreement so formed (*scope of the arbitration agreement*). Such objections may be raised first once A has submitted its Statement of Claim with sufficient specification. Once so submitted, B may raise objections that any of the claims made are not within the scope of the arbitration agreement.

Commentary

In the above-cited case, the arbitral tribunal determined the validity of the arbitration clause on the basis of the law of the seat of arbitration, i.e. Finnish law. It is well-known that the choice-of-law question is approached differently in different jurisdictions. At the risk of oversimplification, in

civil law countries, the law of the seat is typically decisive in this regard, whereas in many common-law jurisdictions, the validity of an arbitration clause is generally determined not by application of *lex arbitri* but by the law governing the underlying contract.

It also appears that arbitral tribunals and courts in different countries address differently the issue of whether, and under what conditions, an arbitration clause in a draft agreement may be deemed binding on the parties. For example, in its recent judgment in *BCY v BCZ* [2016] SGHC 249, the High Court of Singapore ruled (in contrast to the sole arbitrator appointed by the ICC Court in the preceding ICC arbitration proceedings) that an arbitration clause in an unexecuted draft Sale and Purchase Agreement ("SPA") was not valid and enforceable under New York law, which was the governing law of the (draft) SPA and which both the sole arbitrator and the High Court also found to govern the (purported) arbitration agreement. According to the High Court, there was no objective evidence of the parties' mutual intention to be bound by the arbitration agreement in the absence of a properly executed underlying SPA, considering that a party is entitled to make any amendments to the contract, including the arbitration agreement, before it is signed.

The case *BCY v BCZ* has been previously commented upon in the Kluwer Arbitration Blog by Khushboo Shahdadpuri. As noted by the author, despite the outcome of the Singapore High Court's judgment, each case will turn on its own merits, and there may well be circumstances that would reflect parties' intention to be bound by the arbitration agreement independently of, and/or prior to, the underlying contract. In fact, in a recent decision concerning the validity of an arbitration clause in a draft contract, the Swiss Supreme Court came to a different conclusion than the Singapore High Court in BCY v BCZ (Swiss Supreme Court, 4A_84/2015, February 18, 2016). The facts of that case can be briefly summarized as follows (see also comment by Tavernier Tschanz).

The seller had asked the buyer to sign a "frame contract" for their business relationship. The draft contract provided that it was governed by Swiss law and that any disputes in relation to the contract shall be finally resolved in accordance with the Swiss Rules of International Arbitration. In the course of their negotiations, the parties exchanged modified versions of the draft contract; in the last two versions, the arbitration clause remained unchanged. However, the parties never signed a final contract, and the buyer refused to pay to the seller the advance payment as required by the terms of the draft contract.

Once the seller launched arbitration proceedings against the buyer, the latter raised a jurisdictional objection for lack of a valid arbitration agreement. The sole arbitrator appointed by the Court of the Chamber of Commerce of the Canton of Ticino found that, although the underlying contract was not signed by the parties, a valid and binding arbitration agreement had nevertheless come into existence. The buyer challenged the jurisdictional award, but the Swiss Supreme Court sided with the sole arbitrator: it held that the parties had validly agreed on an arbitration agreement during the negotiations of their main contract, regardless of the fact that they had ultimately failed to sign a final main contract. While noting that a mere exchange of draft contracts containing an arbitration clause would not normally suffice to constitute an arbitration agreement binding on the parties, the Supreme Court went on to state that there are certain "additional qualified circumstances" that can still confer jurisdiction upon an arbitral tribunal to resolve claims based on the underlying (draft) contract. According to the Supreme Court, these include (i) instances where the parties have previously concluded several contracts containing the same arbitration clause; (ii) the parties' objectively understandable interest to opt for arbitration (e.g., neutral forum/language and confidentiality); and (iii) the exchange of drafts establishing the parties' common will to enter into

an arbitration agreement (e.g., where the arbitration clause remains unchanged in subsequent drafts), irrespective of the outcome of the negotiations regarding the main contract.

Final remarks

The above-stated serves to illustrate that the question of the validity and binding effect of an arbitration clause in a draft agreement remains a "hot topic" in international arbitration. It defies easy answers, and will depend on case-specific circumstances. Such circumstances will require careful analysis and assessment of the arbitral tribunal and – should the tribunal's positive jurisdictional award be challenged – of competent state courts.

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