Extension of Arbitration Agreements to Non-Signatories in Switzerland: The Supreme Court Sticks to Her Guns

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In 2019, the Swiss Supreme Court ("Supreme Court") seized two opportunities to confirm and develop its existing case law in relation to the personal scope of arbitration agreements and their possible extension to non-signatories.

Extension to Non-Signatories under the New York Convention

In a first decision, ATF 145 III 199, dated 17 April 2019, the Supreme Court had to decide whether its case law on the extension of arbitration agreements to non-signatories developed under Article 178 of the Swiss Private International Law Act ("PILA") (see previous posts here and here) could also apply in relation to Article II of the New York Convention ("NYC").

In this case, the underlying dispute concerned a distribution agreement between a Slovenian company, as principal, and a Swiss company ("BAG"), as distributor. The distribution agreement was signed by a member of BAG's board vested with individual signing authority, but this person was also a board member, having

individual signing authority, of B. Suisse SA ("BSSA"), a sister company of BAG. This agreement was to expire on 31 December 2014, but the parties continued their business relationship and complied with their obligations until the end of 2015. In 2016, the Slovenian company initiated court proceedings against BSSA in Switzerland in order to recover outstanding amounts. BSSA requested the Swiss lower court ("Court") to declare the claims inadmissible since an arbitral tribunal seated in Ljubljana should have had exclusive jurisdiction over the dispute according to the arbitration clause contained in the distribution agreement.

In its decision, the Court found that BSSA had performed the distribution agreement for several years instead of BAG, thereby manifesting its intent to be bound by this agreement including its arbitration clause. As to the argument raised by the Slovenian company that BSSA could not be bound by the written arbitration clause as it did not sign it, thus failing to meet one of the formal requirements under Article II NYC, the Court considered that such argument infringed the principle of good faith (*venire contra factum proprium*). Indeed, the Slovenian company had actively cooperated without any reservation to the performance of the agreement by BSSA. Finally, the Court affirmed that the parties' conduct amounted to a tacit prolongation of the agreement and the arbitration clause until the end of 2015. In conclusion, the Court found that it lacked jurisdiction and referred the parties to arbitration pursuant to Article II(3) NYC.

The Slovenian company appealed to the Supreme Court in order to vacate the Court's judgment on two grounds: (i) BSSA was not bound by the arbitration clause due to the fact that the formal requirements of Article II(2) NYC were not met and (ii) the tacit prolongation of the distribution agreement did not extend to the arbitration clause in line with the principle of separability.

The Supreme Court noted that the Court's finding that the originally written arbitration clause only bound the Slovenian company and BAG, but not BSSA, was untenable. It recalled that (i) the determination of the parties to an arbitration agreement requires an interpretation of the underlying agreement and the arbitration clause and (ii) it is not admissible to simply rely on incorrect or incomplete party names. However, despite this erroneous finding, the Supreme Court did not remand the case to the Court as it considered that, in any case, there was a binding arbitration agreement between the Slovenian company and BSSA.

With regard to the first argument raised by the Slovenian company, the Supreme

Court found that (i) the formal requirements of Article II(2) NYC correspond to those of Article 178(1) PILA and (ii) the well-established case law relating to the extension of arbitration agreements to non-signatories under Article 178 PILA was thus fully applicable. With that in mind, the Supreme Court concluded that BSSA had intervened in the performance of the agreement for several years and, by such conduct, manifested its intent to be bound by the arbitration clause. The Supreme Court further confirmed that the formal requirements set out in Article 178(1) PILA and Article II(2) NYC were solely applicable to the initial parties to the arbitration agreement, but did not prevent the extension of the latter to non-signatories.

As to the tacit prolongation of the distribution agreement and the arbitration clause, the Supreme Court endorsed the Court's finding that no formal prerequisite was required for the prolongation of an arbitration clause under Article II(2) NYC.

Extension to a State as Non-Signatory

In a second decision, 4A_636/2018, dated 24 September 2019, the Supreme Court had to decide whether a State could be bound by an arbitration clause signed by a State-owned entity under Article 178 PILA.

The underlying dispute arose out of an agreement between two Turkish companies, their joint venture company ("Appellants"), and a Libyan state-owned entity in relation to a pipeline construction project. Following the riots that took place in Libya in 2011, the joint venture company suspended its works and no agreement could subsequently be reached to restart these works. As a result, the Appellants initiated arbitration against the Libyan state-owned entity and the State of Libya. In an interim award on jurisdiction, the tribunal denied jurisdiction in respect to Libya as the latter had not signed the agreement. The Appellants challenged this award in front of the Supreme Court. They invoked that the tribunal wrongly denied jurisdiction in respect to Libya on the grounds that (i) the Libyan state-owned entity and Libya were to be treated as a single entity under Libyan law due to the supervisory role of the State of Libya and (ii) the arbitration clause should be extended to Libya under Swiss law because of its involvement in the performance of the agreement. The Appellants alleged that the landmark "Westland" case (P 1675/1987 dated 19 July 1988), which denied the extension of

an arbitration clause to a non-signatory State, was outdated.

The Supreme Court recalled that it was bound by the tribunal's factual findings, in particular:

1. The Libyan state-owned entity was not entirely financed by the State but also through the sale of water;
2. The involvement of the Libyan Minister of Water became necessary only because Libya was supposed to compensate the Appellants for the machinery and equipment destroyed during the riots in 2011;
3. The Libyan Administrative Contract Regulations were not applicable to the agreement and it was not proven that the State's Audit Bureau participated in the negotiations; and
4. The agreement had neither been reviewed nor authorised by the State's General People Committee or the Prime Minister.

With regard to the incorrect application of Libyan law, the Supreme Court confirmed the tribunal's finding that a substantive law principle according to which Libya or one of its administrative entities can be held liable for the wrongful conduct of a supervised company does not imply that the State submits to the arbitration clause contained in the underlying contractual agreement. Indeed, the Supreme Court considered that a finding of extension of substantive liability had no consequence on the tribunal's jurisdiction and was insufficient to derogate from the jurisdiction of State courts.

As regards the extension of the arbitration clause to non-signatories under Swiss law, the Supreme Court recalled that such extension is admissible only in exceptional circumstances as it derogates from the principle of privity of contracts. Such exceptional circumstances might arise when the non-signatory repeatedly participates in the performance of the agreement and thus expresses by such conduct its willingness to be bound by the arbitration agreement. Based on the tribunal's findings, the Supreme Court found that (i) there was no evidence of Libya's repeated interference in the agreement and (ii) thus Libya never expressed, by conduct, its willingness to become a party to the arbitration clause. Finally, the mere fact that Libya was an authoritarian regime and that the construction project was particularly important to the government at the time of contract conclusion did not create any legitimate expectation that Libya would be a party to the agreement.

Conclusion

These decisions can be considered important in many aspects. First, the Supreme Court confirmed that the mere fact that one party to the arbitration clause is a State-owned entity does not justify the extension of such clause to the controlling State, unless the latter interferes in the negotiations and/or performance of the underlying agreement in such a way that it expresses by such conduct its willingness to be bound by the arbitration clause. Second, the Supreme Court affirmed for the first time that its well-established case law with respect to the extension of an arbitration agreement to non-signatories also applies in relation to Article II NYC.

In conclusion, from a Swiss perspective, the extension of arbitration agreements to non-signatories is admissible if the non-signatory was involved in the negotiations and/or performance of the underlying agreement in such a way that it expressed by such conduct its willingness to be bound by the arbitration clause. This standard is applicable irrespective of the non-signatory involved (*i.e.* State or private entity) and the law applicable (*i.e.* PILA or NYC).