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Bound by Oral Arbitration Agreement. Failing to Object During Negotiations

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In the Swedish case *Profura v. Blomgren* (T 2863-07, Court of Appeals for Western Sweden), from 19 March 2008 known as *Profura v. Stig Blomgren*, an appeal was brought against award according to which the arbitral tribunal had rejected its jurisdiction.[1)] The court found – contrary to the competent arbitral tribunal[2)] – that a binding arbitration agreement had been concluded orally between the parties during the course of a negotiation of a share purchase agreement, despite the fact that no final and binding written share purchase agreement had been signed. The court therefore set aside the award.

The appeal against the award, was based on Section 36 of the Swedish Arbitration Act, which provides that an award may be appealed[3)] (as opposed to a challenge under Section 34) in case the tribunal has declined jurisdiction and failed to determine the issues it was asked to consider (when the tribunal, held a dispute inadmissible or otherwise terminated the proceedings without ruling on the merits of the dispute). The court thus has the final word as to the scope of the jurisdiction of the tribunal, the existence, validity and scope of the arbitration agreement.[4)] In a procedure under Section 36 the case is heard again in its entirety, including the merits. To the extent that the arbitral tribunal has found that it lacks jurisdiction, the judgement of the court will – if the appeal is successful – determine, with res judicata effect, that there is a valid arbitration agreement that applies to the dispute. The court will not remand the case to the same tribunal but a new tribunal must be appointed.[5)]

The case is worthwhile noting, as the court found that an oral arbitration agreement had been entered into which in itself does not rise any eyebrows in Sweden, as Swedish law does not require that the arbitration agreement is in writing.[6)] This is at variance with the Model Law and the New York Convention and many other national arbitration laws. It is worth noting that an arbitration agreement under Swedish law can be concluded both orally, implicitly or tacitly and that parties have been considered bound to arbitrate also based on the contractual practice developed and established between them.[7)] Although the absence of a form requirement does provide for flexibility it also gives rise to concerns and commands caution of contracting parties, in particular if enforcement is to be sought under the New York Convention. One also has to be cautious to draw too far reaching conclusions from this case as it is pronounced by the Court of Appeals of Western Sweden which has very limited experience in arbitration matters and has surprised also

several of those involved.

In its analysis, the court separated the analysis of the conclusion of the main contract as such and then the arbitration agreement as distinct from the main contract – as also the arbitral tribunal did –. The principle of separability is manifest law in Sweden and was explicitly incorporated in the Swedish Arbitration Act of 1999.[8)]

Thus the court first had to determine whether a main agreement (SPA), failing a signed contract, still had been concluded and then if that also meant that, or separated therefrom, or regardless of the main agreement, an arbitration agreement had been concluded as well or nevertheless.

The question was when, and on the basis of what, a binding contract arises between parties who are in the process of negotiating a transaction which lasts for some time. In this case the court noted that there had been numerous drafts exchanged and the main commercial points (in particular the price) were settled and, on the basis of the evidence in the case, the court found that an oral main agreement had been concluded between the parties. However, in this context it should be noted that only one of the parties (Profura) had sent drafts to the other – so there had been no real exchange of drafts – and, even if some common view had been found on the price, none of the representations and warranties had been discussed in any detail.

The court then continued its analysis in order to determine whether the parties, by entering into the main agreement (SPA), also had entered into a binding arbitration agreement. The court's conclusion was that since the arbitration clause had been in the drafts from (NB from one of the parties only) the beginning and, at no time during the negotiations had, the party objecting to the jurisdiction of the arbitral tribunal, made any comments or even less objected to the arbitration clauses as such in the drafts, the arbitration agreement was validly concluded orally as well. In addition, the court noted that Mr Blomgren had made some comments to one of the agreements but not to the arbitral clause therein or in any of the drafts. The court's conclusion is very questionable, as the arbitration agreement had not been the object of any specific discussion or comments, assumingly because Mr Blomgren thought it was premature to comment on the dispute resolution clauses in the drafts and in addition the parties to the agreement that was commented did not include Mr Blomgren himself.

The arbitration agreement under Swedish law is viewed as any other contract, regardless of it having both procedural and civil law effects. Therefore, the principles of interpretation of contracts apply in regard to both its content and how it is entered into i.e. when the binding effect arises. This assumes that there is a meeting of wills to contract. There is some precedent which emphasizes that it has to be particularly clear and evident that the parties agreed to arbitration and not to some other form of dispute resolution. However, the general jurisprudence seems to indicate that there is no support for a doctrine of stricter requirements to apply to arbitration agreements than to other contracts.[9)]

The court seems to have given much weight to and was influenced by the testimonies of the professional advisers, including one lawyer, who witnessed and participated in the negotiations, and confirmed that an agreement had been concluded. The court attributed more weight to these testimonies than the arbitral tribunal did. The court found that the seller simply had accepted an offer orally ("hand shake"). The court found it particularly relevant that nothing in the written documentation evidenced that the seller had raised any objections or made any other comments

that any agreement was subject to any conditions and, thus, there was only a conditional acceptance. The written documentation almost exclusively related to price discussions.

It must however be noted that it was a domestic Swedish case, where both parties were Swedish, and enforcement would be sought in Sweden. The situation would of course be very different if it would have been an international arbitration, where the award eventually might have had to be enforced under the New York Convention and, thus, enforcement could be refused failing a written arbitration agreement.

The case therefore should alert parties to the fact that when a contract is signed, they should be cautious of the effects on agreeing step-by-step on various issues during the negotiations and, in particular, of the main issues during the negotiations, which may be agreed upon orally, unless they make such agreements conditional, with or without handshake, and subject to final written agreement each time.

Although the case must be considered case specific and although it is neither authoritative in regard to Swedish contract law and principles of interpretation nor in regard to a non-party, non-signatory of an arbitration agreement, the court's conclusions are supported by the decision of the Svea Court of Appeals in *State of Ukraine v. Norsk Hydro*[10]. In this case, the court noted that the party not singing or wishing to be bound by an arbitration agreement has to take active steps to make his disagreement known to the other party. Whereas passivity normally would not result in the formation of a contract the case should be distinguished when a party should or ought to realize that the other party believes or assumes that a binding agreement has been concluded. This was the case here. In such a situation, which applies to the *Profura* case, there is an obligation to inform the other party that no such agreement has been formed.

Finally it is noteworthy – and somewhat surprising-, that the court found that, despite the fact that Mr Blomgren was not even a named party to the alleged share purchase agreement with Profura, (although he would have been a party one of the transactions but with another party), the claim brought against Mr Blomgren was considered to have such a connection to the transaction between Profura and the seller that the scope of arbitration agreement extended also Profura's claim against Mr Blomgren on the basis of an alleged overriding oral frame agreement.

It might also be of interest to know that, a subsequent arbitral tribunal, which then was bound by the court's decision on jurisdiction, found that no main agreement had been concluded orally or in writing and dismissed the claim, as had the first arbitral tribunal.[11] This is also what would be the expected outcome. Under normal circumstances parties in this kind of transaction (complexity and value) would typically be entering into a letter of intent which would explicitly provide that any binding effect would be subject to signed formal agreements and thus avoid the problem.

References

?1 Case also commented in Hobér, Kaj, *International Commercial Arbitration in Sweden*, 2011, p. 110.

?2 Including one of the very experienced judge Ingemar Persson, then at the Svea Court of Appeals, now sitting Supreme Court Justice.

?3 The action for an appeal under Section 36 must also be brought to the court of appeals within the jurisdiction of which the respondent resides.

?4 Swedish traveaux préparatoires: SOU (Parliamentary Report) 1994:81 p 295; Prop. (Government Bill) 1998/99:35 pp 238.

?5 Franke, Magnusson et al, *International Arbitration in Sweden: A Practitioner's Guide*, p 238 et seq

?6 Heuman, L, *Arbitration Law of Sweden: Practice and Procedure*, 2003, p 30, 32-33; Swedish traveaux préparatoires: SOU (Parliamentary Report) 1994:81 p 95 ; Prop. (Government Bill) 1998/99:35 pp 67-68.

?7 *Värmeledningsaktiebolaget Radiator v. Skanska AB*, decision by the Svea Court of Appeal made on 15 Nov. 1988 in case no Ö 2840-87, RH 1989:83.

?8 Section 3 of the Swedish Arbitration Act: *"Where the validity of an arbitration agreement which constitutes part of another agreement must be determined in conjunction with a determination of the jurisdiction of the arbitrators, the arbitration agreement shall be deemed to constitute a separate agreement."*

?9 For a further brief description of the formation of contracts refer to Franke, Magnusson et al., *International Arbitration in Sweden: A Practitioner's Guide*, pp. 54 et seq.

?10 Franke, Magnusson et al., *International Arbitration in Sweden: A Practitioner's Guide*, footnote 24 and 25 p 78. See also Hobér, Kaj, *International Commercial Arbitration in Sweden*, 2011, p. 100 et seq (110-111) and Dillén, *Bidrag till läran om skiljeavtalet*, 1933, 140-141.

?11 The subsequent arbitral award is not public.

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