Kluwer Arbitration Blog

Kompetenz-Kompetenz: Should the Arbitral Tribunal Exclusively Determine Whether a Right to Arbitrate Has Been Waived?

Huw R Watkins (Victorian Bar) · Wednesday, April 5th, 2023

Under the UNCITRAL Model Law and the laws of many 'arbitration friendly' jurisdictions, courts must refer a matter subject to a valid and operative arbitration agreement to arbitration if requested by a party within the relevant time period.

The principle of *kompetenz-kompetenz* prescribes that an arbitral tribunal may determine its own jurisdiction (which necessarily includes the validity of any agreement to arbitrate). However, when is it appropriate for a Court to step in and should all matters be referred to the Tribunal in the first instance? The recent decision of the Full Federal Court of Australia (the **Full Court**) in *Instagram Inc v Dialogue Consulting Pty Ltd* [2022] FCAFC 7, addresses this point (and others).

Importantly, the decision reinforces that Australian Courts are not afraid to address nuanced questions of foreign law where appropriate.

Background

The decision was an appeal from the decision of Justice Beach[1)] refusing to stay the principal proceedings because of a waiver of the arbitration agreement through participation in the litigation.

The principal proceedings related to an application for injunctive and declaratory relief in respect of the removal of Dialogue's access to the Facebook and Instagram platforms following allegations that Dialogue had breached the Terms of Service through its use of user data.

Instagram's 2013 Terms of Service provided for arbitration pursuant to the American Arbitration Association's rules for arbitration of consumer related disputes. The terms further provided that the governing law was the law of California.[2)]

The key parties to the dispute were: Dialogue, who provided clients with an automated content publication service; and various Facebook (rebranded as "Meta") and Instagram entities (the **Meta Parties**).[3)]

The proceedings were commenced in April 2019 and had a significant procedural history by the

time the application for a stay of the proceedings was brought on 9 April 2020.[4)]

Grounds of Appeal

The key ground of appeal considered by the Full Court was whether the primary judge was correct in finding that the Meta Parties had waived their right to arbitrate. This was challenged on the following basis:

> (a) that *kompetenz-kompetenz* principles dictated that the primary judge refer the matter to arbitration for determination (ground 1);
> (b) that the primary judge erred in failing to follow uncontradicted expert evidence that prejudice was an essential element of waiver under US Law (grounds 2 and 3); and
> (c) that the primary judge should have found that Dialogue did not suffer prejudice under US law and that the Meta Parties did not waive their right to arbitrate (grounds 5 and 6).[5)]

Grounds 2 and 3 were dismissed by the Court on the basis that the primary judge had, in fact, found prejudice even though he concluded it was not essential.

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While both parties accepted that the judge had a discretion whether or not to determine the operability of the arbitration agreement, Meta argued that his Honour failed to consider the complexity of the US law question relating to waiver (in particular, relating to whether or not prejudice was a necessary element) when he exercised his discretion. The Full Court rejected this and found that:

> (a) the issue of the content and uncertainty of the US law authorities on waiver and the necessity of prejudice was comprehensively explored in cross-examination despite the lack of responsive expert evidence; and
> (b) the judgment engaged with this complexity of the US law and thus it could not be concluded that Justice Beach had failed to consider this in deciding to exercise his discretion.[6)]

Prejudice

Meta's expert (Judge Ware) gave evidence in the primary proceeding that relevant factors to establish prejudice included:

> (a) whether the public policy advanced by arbitration (namely, the efficient and cost-effective resolution of disputes) had been undermined; and
> (b) whether the judicial process had been used to gain something not available to the applicant in arbitration.

The Full Court accepted that his Honour was correct in finding prejudice of the requisite standard required by US law. In particular, they found that Meta had:

(a) filed two defences which did not rely upon the arbitration agreement;
(b) applied 12 months into the proceeding for the stay, causing significant expense and delay;
(c) obtained the benefit of mandatory court processes through:

(i) notices to produce;
(ii) requests for further and better particulars; and
(iii) discovery,

that would not have been available to the same extent in arbitration.[7)]

One argument that was raised by the Meta Parties is where there is a mix of arbitrable and non-arbitral matters prejudice is harder to establish. This is because many of the steps would be taken in any event (regardless of any failure to seek a stay in favour of arbitration).[8)] While this proposition was not disputed, the Court found that:

(a) the submissions lacked substance where Meta was seeking a stay of the entire proceeding (i.e. there would be no parallel proceedings of arbitrable/non-arbitrable claims)[9)]; and
(b) Meta had enjoyed the benefit of court processes only available in court proceedings for both arbitrable and non-arbitrable claims.[10)]. This included the issue of Notices to Produce which resulted in the review and production of a significant volume of documents over several months.

Commentary & Conclusion

The Full Court's decision serves as a reminder of a number of key points:

(a) The requirement to stay proceedings that are the subject of arbitration only 'bites' once the Court is satisfied that there is a valid and operative arbitration agreement.
(b) While *kompetenz-kompetenz* allows a tribunal to determine questions affecting its own jurisdiction it does not mandate it. The Court retains a discretion which it will exercise in appropriate circumstances. In this respect, Justice Beach decided that it was more appropriate for him to make a final determination rather than defer to the Tribunal.
(c) The Court would appear more likely to exercise its discretion where:

(i) there are issues of Australian law (in this case, statutory unconscionability and unfair contract terms) or other issues which the Australian Court considers itself better placed to determine;
(ii) choice of law questions could result in the application of Australian law; and
(iii) the materials necessary to make the determination are already before the Court (including in this instance, expert evidence as to the state of the relevant foreign law).[11)]

(d) Australian Courts are not deterred from considering and applying uncertain foreign law. In this regard, the Court unambiguously remains the final arbiter on the foreign law question before it. It will be assisted but not bound by experts qualified in the relevant jurisdiction.
(e) Where the Court does decide to exercise its discretion, establishing that the discretion has miscarried to the requisite standard will be difficult. This can be done by, for example,

showing that extraneous or irrelevant matters have affected the decision (not the case here), a mistake has been made as to the facts (not the case here) or a material consideration has not been considered (in this instance, being the 'uncertainty of foreign law'). As should be apparent, this is not an easy hurdle to clear.

(f) A party wishing to rely upon an arbitration agreement to stay proceedings must act promptly and should not seek to obtain the benefit of court processes before seeking a stay. While the Court's compulsory processes may provide ready access to potentially forensically useful evidence that may be difficult to obtain via arbitration, the potential cost (waiver) is high. In this respect, it is worth remembering that the Tribunal often has power to order document disclosure, and that the Australian Courts can be approached for orders in support of the arbitration (noting that often the Tribunal's consent is necessary (such as for subpoenas)).

References

[1] *Dialogue Consulting Pty Ltd v Instagram Inc* [2020] FCA 1846.

[2] [2022] FCAFC 7, [11]-[12].

[3] Facebook acquired Instagram in 2012 and rebranded its business 'Meta' in October 2021.

[4] The procedural history is recounted in paragraphs [16] through [28] of the judgment.

[5] [2022] FCAFC 7, [48].

[6] [2022] FCAFC 7, [56].

[7] [2022] FCAFC 7, [86]-[88] and [102]-[104].

[8] See, for example, [92] of the judgment.

[9] [2022] FCAFC 7, [95].

[10] [2022] FCAFC 7, [96].

[11] (2020) 291 FCR 155, [197]-[201].

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