Kluwer Arbitration Blog

Carry on Regardless? The Sulu Case, Arbitrator Authority and Principles of Recognition

Gordon Nardell (Twenty Essex) · Saturday, February 3rd, 2024

On a theoretical level, the ultimate source of an arbitral tribunal's jurisdiction is the parties' consent to refer disputes to arbitration. The source of authority of individual members of a tribunal to exercise that jurisdiction is more nuanced – especially where, in default of agreement on a tribunal, the national court makes the necessary appointments. What happens where the validity of that step is subsequently challenged? If the court rescinds an arbitrator's appointment, does that extinguish the appointee's authority? Or does the competence-competence principle preserve authority to determine the effect of the court's order on the arbitral proceedings – and, potentially, to make an award? If an award is made in those circumstances, how should a court in another jurisdiction approach its validity for enforcement purposes?

The *Sulu heirs v. Malaysia* Saga

That conundrum is at the centre of the high-stakes Sulu heirs' arbitration against Malaysia, presently occupying the courts of several European countries. At its heart is an 1878 Agreement between the Sultan of Sulu – former ruler of parts of the Philippines and the Malaysian State of Sabah – and two European adventurers. The Sultan ceded or leased (exactly which is disputed) the right to exploit territory in return for an annual payment of 5,000 Ringgit, later amended to 5,300. Under the Agreement, disputes were to be "brought for consideration or judgment of [the British] Consul-General in Borneo". The adventurers' interest eventually passed to the British Crown, as did sovereignty over the former Sultanate. Both vested in Malaysia on independence. Until 2013 the Malaysian government maintained annual payments to Filipino nationals identified as heirs of the last Sultan.

In 2017 the heirs, having failed to persuade the UK government to appoint a person to perform the Consul-General's role, gave notice of arbitration. Absent agreement on a tribunal, the claimants applied to the Madrid Superior Court (MSC) which in 2019 appointed Dr. Gonzalo Stampa as sole arbitrator. Dr. Stampa determined a Spanish seat. The arbitration proceeded without active participation by Malaysia, who maintained that the Agreement contained no arbitration clause. In May 2020 Dr. Stampa made a preliminary award accepting jurisdiction.

In June 2021 the MSC decided that the original summons had not been served on Malaysia in accordance with Spanish rules governing proceedings against States. As service of the summons

was a nullity, so too were all subsequent steps including Dr. Stampa's appointment. The claimants made, but discontinued, a fresh application to appoint an arbitrator. They also brought an unsuccessful constitutional appeal (*Amparo*) against the court's decision.

Dr. Stampa, however, purported to continue the arbitration, making a procedural order (PO42) declaring that he remained in office and another (PO44) moving the arbitral seat from Spain to France (the Claimants having obtained *exequatur* of the preliminary award from the Paris *Tribunal de Grande Instance*). Dr. Stampa made a final award in February 2022, ordering compensation of nearly US$ 15 billion on the basis that the appropriate measure was the entire "restitution value" of the right to exploit resources in modern Sabah. The award robustly criticized the 2021 Madrid court developments as an "unauthorised local court intrusion on this ongoing arbitration process, in breach of the principle of judicial non–interference".

In June 2023 the Paris *Cour d'appel* annulled exequatur of the preliminary award. That court has also stayed execution of the final award over Malaysia's set-aside application. Meanwhile the claimants have attempted to enforce the final award in various jurisdictions including the Netherlands, where they applied to the Hague Court of Appeal under the New York Convention (NYC).

Arbitrator Authority: The Hague Court of Appeal's Answer

Even that foreshortened (but unavoidably lengthy) scene-setting reveals a copious range of fascinating issues. For present purposes, though, the issue of interest is that of arbitrator authority. Put simply, if the Superior Court's 2021 ruling was effective to terminate Dr. Stampa's authority as arbitrator, then all subsequent steps – including the purported removal of the seat to France and the final award – ought on first principles to lack legal effect: *ex nihilo nil fit*.

But that outwardly simple analysis raises this question, flowing from the international character of the arbitral and enforcement process: while the position may be settled in the Spanish legal order, how should other legal systems determine the effect of the MSC's decision? Is the answer supplied by universal (or widely accepted) principles of arbitral law, or only by discrete rules applicable in each system?

For an interesting argument for the *ex nihilo* position from general principles, but pre-dating the claimants' enforcement attempts, see this article by Fietta LLP. The Hague Court of Appeal (HCA), refusing enforcement, has now reached much the same conclusion, examining the issue via the rules of recognition of foreign judgments. The HCA based its decision on three grounds, the primary ground being the straightforward proposition that, the MSC having removed Dr. Stampa's authorisation to act as arbitrator, he could not render a valid award (HCA judgment, [6.6] [6.13.1], [6.13.3]). What he rendered in 2022 was an award in form only; it was not an "arbitral award" within the meaning of the NYC.

To determine the effectiveness of the MSC's ruling in the Netherlands legal order, the HCA applied the principles laid down in the Dutch Supreme Court's 2014 *Gazprom* judgment: a foreign judgment is recognized if (i) the foreign court's jurisdiction is based on a ground "generally acceptable according to international standards", (ii) the judgment was reached in a procedure complying with due process and offering sufficient guarantees, (iii) recognition is not contrary to Dutch public policy, and (iv) the judgment is not incompatible with a Dutch judgment between the

same parties or a previous (recognisable) foreign judgment on the same dispute (HCA judgment [6.8]).

The HCA found those tests met. It was "*not internationally unacceptable that the judge who issued a decision can reverse this decision if a procedural error is found*." (HCA judgment [6.9]). The HCA accepted that the MSC had omitted to give the heirs an opportunity to comment on a Foreign Ministry opinion about the service rules, but that did "*not lead to the conclusion that there was no legal process with sufficient guarantees and/or conflict with Dutch public order*", not least because the point could have been raised by *Amparo* (HCA judgment [6.11]).

The principles applied by the HCA are typical of recognition rules in private international law. But are those principles suitable where the decision at issue has impacted on arbitral proceedings? Malaysia submitted that the position should be assimilated to the setting aside of an arbitral award (HCA judgment [4.2.9]). The HCA resisted that analogy: the final award had not been set aside. Rather, it reasoned, the result of the MSC's 2021 decision was that the tribunal was "not properly composed" within NYC Article V(1)(d) (HCA judgment [6.14]).

The Dutch recognition principles share common ground with the approach taken elsewhere to the arbitration-specific question of when recognition should be denied, for the purposes of NYC Article V(1)(e), to a court decision setting aside an award at the seat. (The HCA additionally founded its decision on NYC Article V(1)(e), but on the basis of suspension of the final award). For example, the (generally pro-arbitration) English courts generally recognise such an order even if arguably wrong or procedurally questionable; the order will be disregarded only where there is "*positive and cogent evidence*" of a serious failure to observe due process, such as a decision reached in bad faith or offending "*basic principles of honesty, natural justice and domestic concepts of public policy*" (See *Malicorp Ltd v Government of Egypt* [2015] EWHC 361 (Comm) [22] applying *Yukos Capital SarL v OJS Rosneft* [2014] EWHC 2188 (Comm). See also *Maximov v OJSC Novolipetsky Metallurgichesky Kombina*t [2017] EWHC 1911 (Comm) [15] (and here)). Thus in the arbitral context, these two systems at least – which often set the tone for judicial practice in civil and common law systems respectively – apply *ex nihilo fit nil* unless there has been a fundamental failure of due process in the foreign court's intervention.

Pending Arbitral Proceedings: A Special Case?

But where does that leave the objection – voiced by Dr. Stampa – that the MSC's vice lay in intervening during arbitral proceedings, rather than (as in the case of a set-aside application) following their conclusion?

There is a respectable body of legal opinion to the effect that an arbitral tribunal, faced with an intervention by the authorities at the seat that makes continuation of arbitral proceedings "unduly difficult", may preserve the integrity of the proceedings by moving the seat. In 1989 the *Institut de Droit international* in effect accepted this as a rule of public policy, sometimes dubbed the "von Mehren principle" (see Pierre Lalive "On the Transfer of Seat in International Arbitration" in *Law and Justice in a Multistate World: Essays in Honor of Arthur T. von Mehren* (2002), as well as section III of the Fietta article). The HCA did not directly address this question. Should it have, and would that have made a difference?

On a formal level, the MSC's annulment of its 2019 order made it "unduly difficult" – indeed

legally impossible – for the arbitration to continue as originally constituted: that is, with Dr. Stampa acting under the authority of the 2019 order. But on a substantive level, the court's 2021 "intervention" is far removed from the kind of extreme, illegitimate interference to which the von Mehren principle was addressed. Lalive's examples include the notorious *Himpurna* case involving physical abduction of an arbitrator (see the Fietta article on this point).

It is a moot point whether a foreign court deciding whether to recognise a decision like the MSC's should apply a discrete and additional principle – over and above the general rules on recognition – that once arbitral proceedings are underway, questions of the tribunal's competence should be left to the tribunal itself. But even if such a constraint could in some circumstances come into play, it is unlikely to be engaged absent the wholesale disregard of due process capable of triggering the van Mehren principle and the exceptions in the Dutch, English and many other legal systems to the recognition of foreign judgments in the arbitral context. Those circumstances are unlikely to be supplied by the MSC's 2021 *Sulu* decision, for at least four reasons.

First, that decision was designed to uphold due process by remedying a defect in the original decision. Second, the defect was generated by service rules which are not mere procedural niceties but reflect widely-followed practice, rooted in public international law, governing the impleading of a sovereign State in another's courts. Third, while competence-competence doubtless entitled Dr. Stampa to determine various jurisdictional questions (including whether there was an arbitration agreement at all), those could not logically have included the validity of the MSC's original order under Spanish law. It is difficult to see how competence to determine that lay anywhere but within the court system. Fourth, confronted with evidence of the defect, there was no pragmatic reason for the court to defer acting until completion of the arbitration; better to spare the parties the continuing cost of proceedings destined to be ruled invalid (for other factors pointing in the same direction see the Fietta article).

Does *ex nihilo* always beat competence-competence?

Does that mean that *ex nihilo fit nil* always wins, and that an enforcing court faced with a national decision purporting to rescind an arbitrator's authority mid-proceedings is never obliged to consider questions of this kind? Clearly not – that would go too far. Rather, the point is that the ordinary private international law rules of recognition, such as those applied by the HCA in this case, and by the English courts in cases of set aside awards, provide a principled metric for that question where it arises. Those rules are well capable of accommodating the special features of arbitration – including competence-competence and the van Mehren principle – in those rare cases where they fuel well-founded objections to mid-stream intervention by the national court.

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