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Tesseract and Choice of Law in Arbitration under the Model Law: Beyond Proportionate Liability

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On 7 August 2024, the High Court of Australia ("Court") delivered judgment in the much-anticipated *Tesseract International v Pascale Construction* [2024] HCA 24 in which the Court held that proportionate liability statutes apply in arbitration. This post seeks to draw attention to critical aspects of the decision of Australia's highest court, and suggests that, properly considered, it is profoundly pro-arbitration and bears careful study in its respect for, and adherence to, the international origins of the UNCITRAL Model Law on International Commercial Arbitration ("Model Law").

Background

The underlying arbitration involved a claim by Pascale (the builder) against Tesseract (the engineering consultant) for breach of contract, negligence and misleading or deceptive conduct in respect of building works in the State of South Australia. Tesseract's principal defence denied liability entirely. However, Tesseract contended in the alternative that any damages should be reduced by operation of proportionate liability statutes under the law of South Australia (here and here), by reference to Pascale's contributory negligence brought about by the alleged negligence of a third party in assisting Pascale to prepare its tender.

The operative parts of the proportionate liability statutes limited a respondent wrongdoer's liability to an amount which "the court" considers just having regard to the extent of that person's responsibility for the loss. Importantly, that limitation applied whether or not the other concurrent wrongdoers were parties to the proceedings. Additionally, the statutes required the respondent to notify the claimant of persons believed to be concurrent wrongdoers, protected the respondent from being required to contribute to damages recovered by another concurrent wrongdoer, and enabled third parties alleged to be concurrent wrongdoers to be joined as parties to the proceedings.

The parties agreed to refer a question of law to the Supreme Court of South Australia on whether those proportionate liability statutes applied to a commercial arbitration under the *Commercial Arbitration Act 2011* (South Australia) ("SA CAA") (a statute largely mirroring the Model Law). The Court of Appeal of that court answered the question "No", at [187]ff, having analysed it through the prism of whether those statutes were "amenable to arbitration".

Party Autonomy and Choice of Substantive, Procedural and Curial Law

By a 5:2 majority, and in five separate sets of reasons, the Court upheld Tesseract's appeal and answered the question "Yes", having analysed it through the prism of choice of law under the Model Law. The majority held that in arbitrations, founded as they are on party autonomy, the tribunal must apply the parties' chosen substantive rules of law so long as those rules have the same legal effect when transposed to arbitration, and subject only to notions of arbitrability and public policy under the curial law. Here, the proportionate liability statutes were capable of applying in arbitration without changing their legal effect, and neither arbitrability nor public policy of the curial law (which is informed by the pro-arbitration stance of the Model Law) prevented the proportionate liability statutes from so applying.

The starting point was the parties' choice of *curial* law, since this determined the extent to which, and the limits upon, the parties' choice of *substantive* and *procedural* law, as well as any default choice of law rules in the absence of an express or implied choice.

Here, it was common ground that the applicable *curial* law was South Australia, as the place of the arbitration. Accordingly, the arbitration was one under the SA CAA (and therefore the cognate Model Law provisions). That then provided the statutory architecture for determining applicable *substantive* and *procedural* law.

As to *substantive* law, the underlying contract did not contain any express choice of law clause, but it was common ground that the applicable substantive law was South Australia, whether under s 28(1) or s 28(3) of the SA CAA.

That raised three questions.

First, whether the proportionate liability statutes were substantive or procedural. That question had not previously been analysed, since it had been common ground that the statutes were wholly substantive. Nonetheless, three members of the Court challenged that shared premise, with Gageler CJ at [58]-[64] and Jagot and Beech-Jones JJ at [364] holding that the proportionate liability statutes were partly substantive and partly procedural, and that the choice of substantive law was a choice as to only the substantive aspects, being that part which limited the liability of a respondent wrongdoer, irrespective of whether a third party was or could be joined.

Second, on the premise that the proportionate liability statutes were relevantly substantive, what was the doctrinal basis on which the statute could be recast or "moulded" or "translated" to enable it to be applied to an arbitration and how were those principles to be applied here?

A plurality viewed the question of how a statute could be "moulded" for arbitral application through the lens of the parties' choice of substantive law: Gageler CJ at [56]-[57], Edelman J at [175], Steward J at [235], Jagot and Beech-Jones JJ at [345]-[346] and [353]ff, cf. Gordon and Gleeson JJ at [99]-[100].

Applying that choice of substantive law, Gageler CJ at [56]-[57], [63] and Jagot and Beech-Jones JJ at [293], [345]-[346] and [353]ff held that the proportionate liability statutes could be relevantly "moulded" or "translated" to arbitration since they were capable of so applying in arbitration. Gordon and Gleeson JJ held at [128] that the joinder provisions were not "integral" to the

proportionate liability statute and so their non-application would not relevantly distort the statute. However, in dissent, Steward J held at [264] (Edelman J substantially agreeing at [152] and [184]) that the "carefully calibrated" proportionate liability regime would be "distorted" if only the substantive aspects were applied in arbitration.

Third, it was curial law, and not the substantive law itself, that provided the outer limit to the parties' freedom to choose the applicable substantive rules of law. Since the tribunal has a duty to render an enforceable award, it must have regard to considerations of arbitrability and public policy of the seat: Gageler CJ at [45]-[48], Jagot and Beech-Jones JJ at [290], [337]-[339]. Here, neither consideration prevented the proportionate liability statutes from having essentially the same legal operation in arbitration.

As to *procedural* law, it was again common ground that the parties had made no choice of rules of procedure governing the arbitration. This also meant that the parties had made no choice as to the applicability of the procedural aspects of the proportionate liability statutes (e.g., the joinder provisions): Gageler CJ at [34]. By Art 19 of the Model Law, the choice was therefore one for the tribunal to make: Gageler CJ at [31].

Edelman J saw further significance in this (absence of) choice of procedural law. Together with only an *implied* choice of substantive law, this gave rise to the "natural inference" that the procedure and substance of the proportionate liability statutes did *not* fall within the scope of the parties' implied choice of substantive law. That is because, drawing from the *Fiona Trust presumption*, the parties were not to be taken as having incorporated substantive and procedural rules of law in a manner which required the dispute to be resolved in multiple fora. Each of Gageler CJ at [53] and Jagot and Beech-Jones JJ at [381] disagreed strongly, with the Chief Justice observing that *Fiona Trust* was directed to the problem of determining the scope of the dispute that had been agreed would be settled by arbitration, not to the problem of determining the rules of law chosen by the parties to be applicable to the substance of the dispute.

Key Takeaways

This is a consequential judgment, with significance far beyond the immediate question of the applicability of the specific proportionate liability statutes. The various judgments delve deeply into party autonomy as the bedrock of arbitration, and identify the (chosen) curial law as imposing limitations upon the (chosen) substantive law. The Chief Justice's judgment is a crisp and illuminating exposition of the international origins of Australia's integrated statutory framework for arbitration, containing important statements of principle as to the distinction and interplay between the substantive law, arbitral procedure and the curial law, and a detailed consideration of the most important provisions of the Model Law (Arts 1(2), 8, 16, 19, 28, 34 and 35). It demonstrates a rich and sophisticated understanding of essential features and principles underpinning arbitration under the Model Law.

There are additionally at least four key matters of wider significance that should be noted.

First, substantive, procedural and curial law should be carefully distinguished and separately identified. Plainly, that is critical where different laws have been chosen, but (as this case demonstrates) it is equally critical where all connecting factors point to the same jurisdiction.

Second, under the Model Law there is a need to give effect to party choice as to each of those laws. The choice of substantive law under Art 28 can be as to a whole body of law, or to only certain rules of law. It appears to have been accepted by the Court that parties can expressly opt-out of proportionate liability statutes in their selection of the content of the substantive law to be applied under Art 28. In that sense, as Edelman J noted (at [153]), the conclusion of the majority only represents a default rule. Thus, it appears arguably open to the parties to exclude the operation of proportionate liability laws even where (as in Queensland) they purport to restrict contracting out.

Third, the parties' choice of substantive law is to be respected if the substantive law chosen is capable of being moulded or translated to arbitration so long as the law has the same legal operation in arbitration as in court proceedings. The only outer limits that apply to the chosen substantive law is any limit applicable under the chosen curial law. Through those means, the relatively narrow notions of arbitrability and public policy under the chosen curial law must be considered by the tribunal, although there will be very few situations where those considerations serve to prevent the parties' choice of substantive law from applying.

Fourth, difficult choice of law questions remain as to the proper characterisation of a law as substantive or procedural, since that question was not argued before the Court. Nevertheless, it is clear that one should not assume a statute is necessarily wholly substantive in its characterisation.

Overall, when proper regard is had to the analytical approach taken by the majority, *Tesseract* should be viewed as pro-arbitration. It contains many insightful statements of arbitral principle as to substantive, procedural and curial law, and emphatically respects the principle of party autonomy and the international origins of Australia's arbitration statutes.

The authors (together with Kate Lindeman of Banco Chambers) appeared for the amicus curiae, the Australian Centre for International Commercial Arbitration, in the proceedings before the High Court of Australia.

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