Standard of Reasons and Misconduct Under Australian Law

BHP Billiton Limited and Oil Basins Limited [2006] VSC402

Oil Basins Limited and BHP Billiton Limited [2007] VSCA255 (16 Nov 2007)

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On 16 November 2007 the Court of Appeal of the Supreme Court of Victoria Australia upheld the first instance decision of Hargrave J in the case of *BHP Billiton Ltd v Oil Basins Ltd* [2006] VSC 402, thus essentially leaving in place certain provisions of the first instance judgement going to the conduct of arbitration and of arbitrators conducting arbitrations governed under Australian domestic procedural law.

The facts of the case are relatively simple and are fully exposed in the copies of the first instance and Appeal Court judgements following in this journal.

The subject arbitration was between Oil Basins Ltd as Claimant and BHP Billiton Ltd as Respondent.

In essence, the Arbitral Tribunal, made up of two retired Australian superior court judges and a senior American lawyer, published a majority Interim Award dealing with the interpretation and application of the term "Overriding Royalty" as incorporated in a Royalty Agreement governed by New York law, the rights of which were sold, granted and assigned to Oil Basins Ltd (the first instance Defendant through their predecessors) by BHP Billiton Ltd (the first instance Plaintiff through their predecessors) in 1960.

The Interim Award was published on 6 September 2005. This Majority Interim Award of the two retired judges found in favour of the Claimant that royalties calculated, accrued and unpaid by the Respondent on product recovered from the "Blackback" oil field (a relatively new oil field), were payable to the Claimant.

The dissenting arbitrator, an American oil and gas lawyer, opined that a New York Court would not find the term "overriding royalty" established by the subject royalty agreement would extend to apply to a new oil and gas field.

The Chairman of the Arbitral Tribunal, one of the Australian retired judges, unfortunately died some 4 months after the publication of the Interim Award.

The applicable Australian domestic procedural arbitration law[2] relevantly provides at s38 for judicial review of awards. Particularly, at s38.2, the statute allows, with certain caveats, appeal to the court on "any question of law arising out of an award". This provision has been applied by courts in different jurisdictions around Australia, both widely and narrowly

BHP Billiton challenged the Interim Award. They pleaded that (1) the reasons given by the majority of the arbitrators were so manifestly inadequate as to constitute error of law and (2) the

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2 *Commercial Arbitration Act* 1984 (Vic

majority arbitrators had failed to consider and adjudicate upon substantial and serious submissions and evidence to the extent that there was technical misconduct.

The first instance judge found that an element to be considered in assessing the adequacy of an arbitrator's reasons is "the qualification and experience of the arbitrator or arbitrators" exampling that in a "straight forward trade arbitration" a "less exacting standard of reasoning" would apply.

The judge further found that the "arbitrators were under a duty to give reasons of a standard which was equivalent to the reasons to be expected from a judge deciding a commercial case".

An example of alleged inadequate reasons arose in respect of expert evidence on New York law.

The court adopted the principle that it is not sufficient when dealing with competing opinion evidence to adopt a position of preferring the evidence of one expert to that of another. This was not further elaborated but reinforces that the role of the expert must be to edify the tribunal on the basis used to arrive at the expert's opinion such that the tribunal itself in applying that rationale comes to its own opinion which may or may not concur with the expert's opinion.

Section 42 of the governing Act provides that where there has been misconduct by an arbitrator, the court may set aside the arbitrator's award, either wholly or in part.

Misconduct is defined as including "corruption, fraud, partiality, bias and a breach of the rules of natural justice".

The judge found to the effect that inadequate reasons in an award in circumstances where the arbitrators failed to deal with a substantial or serious submission, or with important evidence, amounted to a "technical misconduct".

The first instance court ordered that the Interim Award be remitted for reconsideration. However, as the original tribunal could not be reconstituted or re-empowered because of the death of one of its members, this would necessitate the empanelling of a new tribunal.

On appeal, the Court of Appeal upheld the first instance judgement in effect supporting and adopting the lower court judgement, save that whilst not rejecting the trial judge's dicta on the standard of reasons, did make relevant tempering observations.

The first instance and Appeal Court judgement raise significant issues relating to the conduct of arbitrations governed by Australian domestic procedural law, whether held within or outside Australia.

The autonomy of the parties to form an arbitral tribunal composed of arbitrators with varying skills, knowledge and experience is a fundamental aspect of arbitration. That a tribunal so created may, by its composition, be overall legally neutral, technically neutral and culturally neutral goes to one of the benefits of arbitration.

Whilst the nature of the dispute should dictate or influence the reasons given, for example a quality/quantity dispute submitted to an expert in the subject matter of the dispute, may require simple yes/no answers, where there are complex issues of fact and law unless the parties have otherwise agreed to the contrary, an arbitral tribunal is bound to give adequate reasons and just as importantly to expose its reasoning.

The trial judge's observations to the effect that the more highly legally qualified the arbitrators are the more extensive or complex the reasons must be, whilst not inconsistent with the requirement of a tribunal to give reasons answering only those matters before it, no more and no less, were made obiter and should be recognised as such and without binding effect.

In my view it is not appropriate to include qualifications of the tribunal as a test for adequacy of

reasons. The Court of Appeal recognised that the nature of the dispute and not the nature of the arbitrator should set the standard for reasons.

An award should expose the rationale and the thought process applied by an arbitrator such that an unknowledgeable reader can ascertain and understand how the arbitrator arrived at the ultimate conclusions.

By adoption of the term "technical misconduct" the courts have reverted to the position in Australia pre-introduction of the current *Commercial Arbitration Acts*.

The definition of "misconduct" in the Acts, although not limiting, does not distinguish between culpable and technical or non-culpable misconduct.

It is the nature of the "misconduct" rather than its characterisation that should determine the remedy to be applied however convenient and simple it may be to adopt just two different characters of misconduct.

It is arguable that under the governing statute inadequacy of reasons can be both an "error of law" and "misconduct" at the one time. Certainly failure to give adequate reasons is a breach of a fundamental duty of an arbitral tribunal.

Not dealing with serious and significant submissions without giving appropriate reasons for failing to so deal, given the unlimited definition of misconduct under statute, is certainly open to review by a court.

An affect of these judgements may be an impetus on disputing parties to only have retired judges as arbitrators. Or it may have the opposite affect.

A further element of these judgements and the degree of curial intervention is the affect they may have upon transnational commercial disputants in considering whether or not to choose Australia as a situs for international arbitration.

To be able to choose your tribunal goes to the essence of arbitration. It is hoped that these judgements will not distort the tribunal formation process in Australia or affect that process in other jurisdictions.