Arbitration - Austria

Supreme Court defines limits for challenge of arbitrator in set-aside proceedings

Contributed by **Graf & Pitkowitz**

September 12 2013

Background

On June 17 2013 the Supreme Court ruled for the first time(1) on an issue that has been fiercely debated among legal scholars – namely, whether (and to what extent) grounds for challenging an arbitrator can also be raised in set-aside proceedings under the Arbitration Act 2006.

The court ruled that where a challenge becomes known after the arbitration award was issued, only "blatant" grounds can be invoked in set-aside proceedings. When determining whether blatant grounds exist, the court may consider not only domestic law rules for disqualifying judges in the national courts, but also the International Bar Association (IBA) Guidelines on Conflicts of Interest in International Arbitration.

Facts

The respondent ordered from the claimant a firing and flue gas cleaning system that was allegedly defective. The subsequent disputes regarding the defects were resolved in four separate arbitration proceedings. The same three arbitrators constituted the arbitral tribunal in each of the four separate proceedings.

The tribunal dismissed the claim in the fourth proceeding. Within two weeks of the tribunal issuing the award, the claimant filed a challenge against the arbitrator nominated by the respondent. The challenge was raised simultaneously in court proceedings (under Section 589 of the Civil Procedure Code) and with the arbitral tribunal. The arbitral tribunal refused to decide on the challenge, since it considered itself already *functus officio* (ie, discharged from the duties of office). The court dismissed the challenge on the grounds that recourse to challenge proceedings was available only during the arbitration and not after the tribunal had issued its final award. This decision was ultimately confirmed by the Supreme Court on December 17 2010.(2)

Within the three-month time limit after the final award, the claimant also filed a set-aside action. It based its claim on the fact that the arbitrator nominated by the respondent had been a member of the supervisory board of the respondent's grandparent company, a fact that the claimant did not discover until after the award had been rendered. Later in the set-aside proceedings the claimant also asserted that the tribunal's chairman was biased because his law firm had in the past represented the respondent in another matter (unrelated to the arbitration) and drafted a contract between the respondent and its minority shareholder.

First instance decision

The court of first instance dismissed the claim. The court ruled that grounds for challenging an arbitrator that come to the challenging party's attention only after the award has been made

generally cannot be invoked in set-aside proceedings. Only particularly severe and manifest cases of bias would satisfy the high standard for invoking procedural public policy (within the meaning of Section 611(2)(5) of the code) to set aside an award.

In the case at hand, the court concluded that the facts which the claimant had alleged did not meet this standard.

Appellate decision

The court of appeals upheld the judgment of the first instance court. It distinguished between disqualification and challenge of judges in Austrian civil procedure under the Jurisdiction Act.

According to these provisions, a judge is disqualified by the law itself if one of the grounds conclusively regulated in Section 20 of the Jurisdiction Act applies (eg, if the judge or his or her relatives were a party to the proceedings). In contrast, a judge is considered biased and can be challenged if circumstances exist that give rise to justifiable doubt as to his or her impartiality or independence.

In state court proceedings, grounds for disqualification can be invoked at any time, but grounds for a challenge must be raised before the court renders a decision. The court of appeals reasoned that the same principle should also apply to arbitral awards. Otherwise, parties would have an incentive to search for reasons for challenge only after receipt of an unfavourable award.

The court of appeals concluded that none of claimant's allegations met the threshold for disqualification.

Supreme Court decision

The Supreme Court upheld the first instance and appellate decisions and dismissed the claimant's set-aside claim. In its 28-page decision, the Supreme Court first addressed the conflicting views of scholars as to whether, and to what extent under the Arbitration Act, challenges should be permitted after a final award, before dealing with the grounds for challenge raised. In its analysis the court also cited and relied on the IBA guidelines.

Only blatant bias justifies setting aside

When evaluating the grounds for challenge, the Supreme Court referred to the 'old' legal regime, which had been in force before the Arbitration Act came into force. Specifically, it referred to its decision of January 21 2005,(3) in which it had ruled that the challenge of an arbitrator on grounds of bias generally cannot be invoked in set-aside proceedings, even when the relevant facts came to the party's attention only after the award was rendered. In that decision, the court drew an analogy with the principles of state court proceedings and ruled that only grounds for disqualification can justify setting aside an award. It noted that although the act deleted the provisions applicable to state court judges, the underlying legal principle was unchanged.

The Supreme Court discussed different scholars' views on arbitral challenges under the act, in particular:

- the 'wide' view,(4) under which any ground for challenge can be raised in setting aside proceedings; and
- the 'narrow' view,(5) under which only extraordinary reasons can justify setting aside an award.

The court decided to follow the latter view. The court also noted that its conclusion was in line with German arbitration law, which is also based on the United Nations Commission on International Trade Law (UNCITRAL) Model Law.

The court argued that it was necessary to find a fair balance between the principles of impartiality and independence of arbitrators and the equally important principles of stability and security of law. The solution to this conflict as established for state court proceedings should apply equally to arbitration proceedings. Therefore, only blatant cases evidencing a lack of impartiality or independence can be used as a ground for setting aside an award.

The court declined to establish a general rule that would define what constituted a 'blatant' case, except to note that the circumstances would need to be similar to those that would justify disqualification if the case has been brought in the state courts rather than an arbitral proceeding. The court acknowledged that each case must be decided on a case-by-case basis on its own facts. For the first time, the Supreme Court expressly acknowledged the IBA guidelines (even if

the parties did not expressly agree on such guidelines) and stated that they can be taken as guidelines in future cases.

The set-aside claim could therefore be based on either Section 611(2)(4) of the code (defective composition of the arbitral tribunal) or Section 611(2)(5) of the code (violation of procedural public policy).

Analysis of claimant's arguments

The court then evaluated the two grounds for challenge raised by the claimant.

Arbitrator acting as supervisory board member of group company

The court ruled that the fact that the arbitrator was a member of the supervisory board of the respondent's grandparent company was not comparable to any ground for disqualification of state court judges under Section 20 of the Jurisdiction Act. Such a relationship neither qualified as an infringement of procedural public policy nor fell under any item of the non-waivable Red List of the IBA guidelines (in particular, not under Item 1.2). Therefore, the balance of interests did not justify setting aside the award.

However, the court noted in *dicta* that the arbitrator would have been obliged to disclose such information and the relationship would have given rise to justifiable doubt as to his or her impartiality or independence for the purposes of an arbitrator challenge.

Arbitrator's law firm advising in a different matter

With reference to General Standard 6 of the IBA guidelines, the Supreme Court held that the fact that an arbitrator's law firm had formerly represented one of the parties did not automatically give rise to justifiable doubt as to the arbitrator's impartiality or independence. The service was provided in only one matter that had already been concluded and did not concern any of the issues that were the subject of the arbitration. Therefore, the conflict fell under the Orange List of the IBA guidelines, meaning that the arbitrator would have had a duty to disclose such information, but it would not have been sufficient ground for a successful challenge.

Comment

The Supreme Court decision tackles several significant issues.

Under the Arbitration Act (based on the UNCITRAL Model Law), unless otherwise agreed, a party may challenge an arbitrator within four weeks of becoming aware of the circumstances giving rise to the challenge. If the challenge is rejected, the party has the right to bring the case before the state court. Termination of the arbitration proceedings also terminates the arbitrator's assignment (*functus officio*) and a challenge is no longer possible after conclusion of the proceedings.

However, what happens if the grounds for challenge surface only after the close of proceedings? At this stage, challenge proceedings are no longer available (as described above and as tested by the diligent claimant in the case at hand in two separate proceedings).

Can such grounds therefore be raised in an annulment claim? The court accepted and confirmed that cases of bias can be asserted in the course of set-aside proceedings. This is by itself an important development, given that this has been an unsettled issue in Austrian jurisprudence.

More importantly, the decision also settles the hotly debated issue of to what extent arbitrator challenges may be raised after the final award. Although the court's solution to admit only blatant cases of bias in effect limits these cases, it provides a reasonable and appropriate balance between the right of challenge and the stability of arbitral awards.

The limitation of arbitrator challenges following an award is also an effective means to motivate the parties to research diligently any basis for challenge as early as possible, and to assert challenges without delay. In the case at hand, at least the first ground for challenge (ie, the arbitrator's role as a supervisory board member) could probably have been raised in the course of the arbitration, as in Austria all corporate officers are publicly listed.

Under Austrian law, the set-aside claim against an award must be filed within three months. Unfortunately, the court's decision left the question open as to whether that deadline is extended if a ground for bias surfaces only later. The second ground raised (ie, the involvement of the arbitrator's law firm) was in fact only asserted more than a year after the final award. If the court intends to apply similar principles as in respect to state judges, it must also admit challenges after the three-month deadline. However, the law does not mention such cases. This may be the

reason why the court did not dismiss the request outright, but addressed the merits of the arguments.

Although the court relied on Austrian jurisprudence concerning the disqualification of state court judges, the decision also gave adequate account to the distinct function and role of arbitrators. Furthermore, this is the first Supreme Court decision that has expressly cited the IBA guidelines as a valid secondary authority.

For further information on this topic please contact Nikolaus Pitkowitz at Graf & Pitkowitz by telephone (+43 1 401 17 0), fax (+43 1 401 17 40) or email (pitkowitz@gpp.at). The Graf & Pitkowitz website can be accessed at www.gpp.at.

Endnotes

(1) 2 Ob 112/12b.

(2) 6 Ob 228/10p.

(3) 7 Ob 314/04h.

(4) As argued by Rechberger and Melis, Reiner, Torggler, and Rieger and Petsche.

(5) As argued by Hausmaninger, Klausegger and Hanusch, Zeiler and Pitkowitz.

Author

Nikolaus Pitkowitz