Application to annul recognition and enforcement of two awards dismissed: only blatant violation of right to impartial arbitrator breaches Swiss public policy (Swiss Supreme Court)

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In *Decision 4A_663/2018*, the Swiss Supreme Court refused to annul a decision recognising and enforcing two awards. In doing so, it confirmed that the public policy exception under Article V.2(b) of the New York Convention must be applied narrowly and only a blatant violation of the right to an independent and impartial arbitrator can justify refusing the recognition of an award.

Speedread

In a recently published German-language decision, the Swiss Supreme Court dismissed an application for annulment of a decision of the High Court of Zurich, which had confirmed a Court of First Instance decision to recognise and enforce two International Chamber of Commerce (ICC) awards.

The case concerned a Swiss subsidiary (the respondent) of a Spanish group of companies and a natural person (the appellant), both of which had entered into a share purchase agreement in 2007. A dispute arose and the respondent initiated two ICC arbitration proceedings.

In November 2011, the tribunal rendered two awards ordering the appellant to pay the respondent more than USD 100 million. The president of the ICC tribunal was a partner in a large international law firm in New York. The appellant challenged the president's impartiality before the ICC and he subsequently resigned.

In 2018, the respondent successfully applied for the recognition and enforcement of the two awards in Switzerland. The appellant challenged this decision before the Swiss Supreme Court, alleging that the enforcement and recognition violated Swiss public policy, as per Article V.2(b) of the New York Convention (NYC). In particular, the appellant alleged the president's lack of impartiality because of his law firm's involvement in providing legal assistance to companies pertaining to the same group of companies of the respondent.

The Swiss Supreme Court confirmed that the public policy exception must be construed objectively and restrictively, and based on an analysis of all the circumstances. It recalled its jurisprudence on conflict of interest and notably that one cannot simply overlook the reality of international arbitration and the increasing size of international law firms. Accordingly, the court pointed out that the fact that other lawyers from the arbitrator's law firm performed work for companies pertaining to the same group of companies of one of the parties in the arbitration is not, on the face of it, sufficient to establish a lack of impartiality.

In addition, the fact that the arbitrator's law firm received fees during the arbitration by one party for work performed in relation to companies belonging to the same group of companies of one of the parties in the arbitration, even if considered critical by the Supreme Court, was not sufficient to establish a lack of impartiality. Finally, the Supreme Court left the question open as to whether punitive damages violates Swiss public policy. *(Decision 4A_663/2018 (27 May 2019))*.

Background

Article V.2(b) of the New York Convention (NYC) provides that:

> "2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:
>
> [...]
>
> (b) The recognition or enforcement of the award would be contrary to the public policy of that country."

For further information on the New York Convention, see *Practice note, Enforcing arbitral awards under the New York Convention 1958: overview*.

Facts

The respondent (a Swiss subsidiary of a Spanish group of companies) and the appellant (a natural person domiciled in Brazil that was the sole shareholder of a group of companies) entered into a shares purchase agreement (SPA). In relation to the performance of the SPA, the respondent initiated two International Chamber of Commerce (ICC) arbitration proceedings against a Brazilian company, which acted as guarantor for the appellant in relation to the SPA.

On 21 November 2011, an ICC tribunal rendered two final awards ordering the Brazilian company to pay the respondent over USD 100 million. In both of the ICC proceedings, a partner of a large international US law firm acted as president of the arbitral tribunal.

After the ICC awards were rendered, the appellant challenged the president's impartiality with the ICC, alleging that his law firm had been rendering legal advice to the respondent. The president subsequently resigned from his position.

The appellant and the Brazilian company challenged both awards before the US District Court for the Southern District of New York, which dismissed the application. The US Court of Appeals for the Second Circuit confirmed that decision, and the US Supreme Court declared any further appeal inadmissible.

In enforcement proceedings initiated by the respondent in 2017, a Brazilian court dismissed an application for recognition of both awards, stating that they were contrary to Brazilian public policy.

Previously, on 9 January 2013, the respondent had requested and obtained before the competent court in Zurich the attachment of more than USD 100 million based on the ICC awards. The attachment was executed on 11 January 2013. On 16 January 2013, the respondent sent the appellant an order for payment for CHF 13 million, to which the appellant objected. After the Brazilian company had objected to the order for payment, on 26 February 2015, the respondent filed an application before the competent court in Zurich to obtain:

- The recognition and enforcement of the awards in Switzerland of the awards.
- The dismissal of the objection against the order for payment.

On 18 December 2017, the competent court in Zurich upheld the application, granting recognition and enforcement of the two awards.

On 5 November 2018, the Zurich High Court (court of second instance) dismissed the appellant's application to have the decision of the lower court overturned. Against this decision, the appellant filed an application before the Swiss Supreme Court seeking its annulment and alleging that the lower instance had breached the NYC. It argued that:

- The president of the ICC tribunal lacked impartiality. In particular, the appellant founded its allegations of lack of impartiality on:
    - the long-lasting relationship between the president's law firm and the Spanish group of companies;
    - the high volume of fees (USD 6.5 million) that the Spanish group of companies paid to the president's law firm during the arbitration for work not related to the arbitration;
    - the law firm's participation in corporate transactions involving companies pertaining to the Spanish group of companies;
    - the president's violation of his duty to disclose the relationship between his law firm and the Spanish group of companies;
    - the fact that the president eventually resigned; and
    - the fact that the Brazilian court dismissed the application for recognition and enforcement based on the president's lack of impartiality.
- The order to pay the respondent more that USD 100 million represented punitive damages, unlawful under Swiss law, because the real damage was only USD 18 million.

According to the appellant, the recognition and enforcement of the awards in Switzerland was therefore contrary to the Swiss public policy according to Article V.2(b) of the NYC.

Decision

The Swiss Supreme Court dismissed the appellant's application. The court first addressed the allegation of the president's lack of impartiality, before addressing the argument of the punitive damages under Swiss law.

The president's lack of impartiality

After recalling the restrictive approach to the public policy decisions in the field of foreign court judgments, the Swiss Supreme Court explained that in the context of an *exequatur* decision, the refusal to grant the recognition and enforcement of a foreign award based on Article V.2(b) of the NYC must be construed restrictively and is only justified where there is a blatant breach of fundamental principles of Swiss law. This is often the case in international arbitration where, for instance, a situation listed in the red list of the *IBA Guidelines on Conflicts of Interest in International Arbitration* (IBA Guidelines) occurs.

Under Swiss case law, there is bias and partiality when the facts and the procedural elements at hand generate distrust in the judge's impartiality from an objective point of view. Therefore, it is not necessary that the judge is actually partial because the appearance of partiality is sufficient. The Swiss Supreme Court pointed out that this is also the case in Brazil, while in the US the recognition and enforcement is only refused if the arbitrator was subjectively partial and if this can be proven. The Swiss Supreme Court further recalled that according to Swiss case law, when the judge is also active as a lawyer, that lawyer and the law firm such lawyer works for must be treated as one entity. This is also in line with the provisions concerning conflict of interest contained in professional code of conduct rules and regulations.

The concept of one entity also applies to a certain extent to companies that pertain to the same group. Therefore, there may be a lack of impartiality even though the lawyer who sits as an arbitrator is not providing legal assistance directly to one of the parties in the procedure, but to an individual closely linked to one of the parties, such as in the case of companies belonging to the same group. The Swiss Supreme Court acknowledged that this double "one entity" approach (that is, with regard to the law firm, on the one side, and the group of companies, on the other) can have far-reaching consequences for lawyers acting as arbitrators. With regard to the one-entity approach for a group of companies, the Swiss Supreme Court, in its previous case law, recalled that a strict and systematic application was inappropriate. Rather, it must be analysed whether the relationship between the lawyer acting as an arbitrator (or as a judge) or their law firm, respectively, and an affiliate to the group of companies, entails a similarly closed relationship to one of the parties in the procedure, who belongs to the same group of companies. Thus, if a party to the proceedings is an entity of a group of companies, it cannot, with regard to the arbitrator's impartiality, be treated as if it were one and the same with every affiliate within the group of companies. Rather, an analysis must be conducted based on the specific circumstances and not simply on the basis of the existence of a group of companies.

The same applies in relation to law firms. In this regard, in its decision rendered in 2016, the Swiss Supreme Court pointed out that the increasing size of the law firms cannot be disregarded. Indeed, the fact that a lawyer in the same law firm of the arbitrator is providing or provided legal services to one of the parties in the proceedings is not, *per se*, a situation where the arbitrator lacks impartiality. The Supreme Court confirmed that this approach is in line with Rule 6(a) of the IBA Rules, which provides that the particular circumstances of the case and interest at stake have to be considered (see *Decision 4A_386/2015*, discussed in *Legal update, No conflict and no grounds for revision of Bosch Rexroth v Piacentini award (Swiss Supreme Court)*).

In the present case, the Swiss Supreme Court stressed that the analysis of the alleged lack of impartiality must be done taking into consideration all the factual elements at hand. In particular, because the appellant relied on

different factual elements, each of them had to be analysed separately. In its analysis, the Swiss Supreme Court came to the conclusion that the president's lack of impartiality was unproven due to the below points:

- The fact that the president resigned was irrelevant; only objective criteria were relevant for an analysis of the appearance of partiality.
- The president's law firm provided legal services to a company related to the respondent at a moment when that company was not yet part of the Spanish group of companies. Therefore, this aspect was also irrelevant.
- The president's law firm did not represent a company in the M&A transaction for the acquisition of shares within the Spanish group of companies; the work performed was limited to advising a third entity, namely the US Department of Energy on the shareholders' structure after the transaction. Thus, according to the Swiss Supreme Court, it is difficult to imagine a conflict of interests.
- The (unproven) fact that other lawyers from the president's law firm have had friendly contacts, within an M&A transaction, with lawyers representing a company belonging to the Spanish group of companies, is insufficient to demonstrate the tribunal's president's lack of impartiality.

However, the Swiss Supreme Court found that the payment of fees by one of the parties in the arbitration to the president's law firm during the arbitration proceedings was critical, especially when, such as in this case, the arbitrator has failed to disclose this point. Nevertheless, the Swiss Supreme Court considered that this was insufficient to establish the president's required blatant lack of impartiality and that the payment of fees to the president's law firm, although questionable, was not sufficient to refuse the *exequatur*.

Finally, the Swiss Supreme Court held that the Brazilian court's refusal to recognise and enforce the awards was immaterial. Pursuant to Article V.2(b) of the NYC, a Swiss judge has to determine whether the recognition and enforcement would breach the Swiss public policy, not Brazilian public policy.

Punitive damages and Swiss public policy

The Swiss Supreme Court did not decide on whether punitive damages violate Swiss public policy. It considered that it was not evidenced in the lower court's decision that the respondent's damages only amounted to USD 18 million. As the Swiss Supreme Court is bound by the lower court's factual assessment, it did not admit this additional ground for refusing the recognition and it did not analyse if the recognition and enforcement of a foreign arbitral award granting punitive damages was against the Swiss public policy.

Comment

This decision is important in the area of recognition of foreign awards under the NYC and, in particular, with regard to the lack of impartiality and independence, for various reasons.

First, it reconfirms and firmly establishes the exceptional nature of the public policy defence in Switzerland. Based on a narrower interpretation of public policy, when it comes to enforcement and recognition of a foreign arbitral award, the Swiss Supreme Court will apply a stricter approach than in setting aside proceedings where the compatibility of the foreign law with the Swiss public policy is considered. Only if the Swiss understanding of justice is violated in an unacceptable way will the recognition be refused. However, the decision explicitly leaves open whether such restrictive approach is also justified when the procedural public policy is at stake. In any event, only a blatant violation of the principle of impartiality and independence could justify not recognising a foreign award. In the

present case, no such blatant violation was established. The Swiss Supreme Court states expressly that this would require a situation that clearly falls within the red list of the IBA Guidelines.

Second, the Supreme Court confirms for the first time in the context of arbitration that a systematic "one entity" approach to a group of companies in arbitration is not justified. Rather, the circumstances and interests in each individual case must be taken into account when deciding whether or not the affiliates have to be considered as one entity. This is a very welcome holding for arbitrators sitting in Switzerland and is in stark contrast with a decision of the Paris Court of Appeal of 27 March 2018 in *Société Saad Buzwair Automotive Co c/ Société Audi Volkswagen Middle East FZE LLC, Cour d'appel de Paris, No. 16/09386* (see *Legal update, Paris Court of Appeal sets aside ICC award because tribunal not properly constituted*).

Third, the Supreme Court clarified an earlier decision where it had held that a sole arbitrator was considered to lack the necessary impartiality and independence because he had represented a third party against one of the parties in the arbitration. The rationale was that the negative feelings of a party against its counter party are transferred to the lawyer representing a party. This decision, which was perceived as overly strict, was not applied to the current situation of professional contacts in the context of an M&A transaction and thus interpreted in a welcomed narrow way.

The only problematic circumstance that remained in relation to the involvement of the president's law firm with the respondent was its payment to the president's law firm. Here, the Swiss Supreme Court expressly held that while this was critical, it drew the conclusion that this would not justify the refusal of recognition under the NYC, at least not without a dependency of the law firm. However, it left open whether this situation would have qualified as violating the Swiss public policy in setting aside proceedings.

Overall, the case brings some very useful clarifications and lowers the risk of conflicts with regard to arbitrators who are members of large law firms by confirming that there will be no strict application of the "one entity" approach to members of one law firm. Equally, a case-by-case approach to entities that are members of the same group of companies is now also the established rule for arbitrations in Switzerland and only if there is an additional factor justifying treating the concerned entities of the same group as one entity, will this be done for conflict of interest purposes.

Case

Decision 4A_663/2018 (27 May 2019) (Swiss Supreme Court).

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