

Setting Aside of Arbitral Award : Breach of Natural Justice and Prejudice

MASTER MULIA SDN BHD V SIGUR RUS SDN BHD [2020] 9 CLJ 213

ISSUES

Is the High Court bound to set aside an arbitral award under Section 37 of the Arbitration Act 2005 (“**AA 2005**”) once the Plaintiff established that there was a breach of the rules of natural justice?

Or can the High Court exercise its discretion to maintain the award? If so, what must be taken into consideration in exercising such discretion?

If the Plaintiff established that there was a breach of the rules of natural justice, is the Plaintiff required to further show that such breach lead to some prejudice? If the Plaintiff suffers no prejudice, can the award still be set aside?

These questions were ventilated in the recent Federal Court case of **Master Mulia Sdn Bhd v Sigur Rus Sdn Bhd [2020] 9 CLJ 213**.

BRIEF FACTS

The brief facts of the case, as reported, are as follows:-

- (a) Master Mulia (“**Appellant**”) hired out its vessel to Sigur Ros (“**Respondent**”) for installation of undersea pipelines works in the high sea pursuant to a Charter Party Agreement (“**CPA**”). There is a pipeline installation arm called a Stinger Hitch on the vessel, which was essential to the works.
- (b) The Respondent was to redeliver the vessel on or before the expiry of the charter period on 26.01.2013, failing which, the Respondent was liable to pay a certain daily sum until redelivery.
- (c) The Stinger Hitch was damaged on 09.01.2013 and the Respondent suspended works to carry out temporary repair to the Stinger Hitch in order to complete the remaining works thereafter.
- (d) The vessel was redelivered to the Appellant on 05.03.2013, 37 days after the due delivery date. The Appellant claimed for charter hire up until 22.05.2013, being the date after the vessel had been dry-docked for reinstatement works.
- (e) For the extended period from 22.05.2013 until the vessel was reinstated, the Appellant claimed a sum of USD3,968,279.00. The Appellant also claimed for, amongst others, the costs of reinstating the Stinger Hitch and other claims, including replacement / replenishment of consumables and other equipment on the vessel. The Respondent disputed the claims and contended that the Stinger Hitch was damaged due to its inherent weakness.
- (f) Arising from the dispute, the Appellant initiated arbitration. The Arbitrator decided in favour of the Appellant and the Respondent was required to pay the *“sum of USD3,023,269.52 together with pre-Award interest of USD82,332.33, the sum of RM502,141.47 towards repair and reinstatement of the vessel and post-Award interests”* (**Award**).



HIGH COURT

The Respondent applied to the High Court to set aside the Award pursuant to sections 37 and 42 of the Arbitration Act 2005 (“AA 2005”). The Respondent primarily relied on 2 principal grounds:-

- (i) *“that the Award was issued in breach of the rules of natural justice and, as such, was contrary to public policy under subsections 37(1)(b)(ii) and 37(2)(b)”*; and
- (ii) *“that the Award went beyond the scope of submission to arbitration under subsection 37(1)(a)(iv) of the AA 2005.”*

“The High Court found that the Award was in breach of the rules of natural justice to an extent that s 20 of the AA 2005 on equal treatment of parties was contravened.” However, the Award was affirmed *“principally on the ground that **the respondent failed to show that it suffered actual or real prejudice arising from the breach of the rules of natural justice.**”* (Emphasis added).

COURT OF APPEAL

Dissatisfied, the Respondent appealed to the Court of Appeal. The Appellant did not cross-appeal against the High Court’s findings that *“s 20 of the AA 2005 had been contravened by reason of a breach of natural justice.”*

The appeal was allowed and the Award was set aside. The Court of Appeal *“concluded that there had been a breach of the rules of natural justice sufficient in gravity to set aside the Award.”*

Following the same, the Appellant applied for leave to appeal to the Federal Court.

QUESTIONS OF LAW

Federal Court granted leave on the following questions of law:-

- (1) *“Whether the High Court exercising jurisdiction under s 37 of the AA 2005 is bound to set aside an arbitration award as a matter of course if any of the grounds of challenge under ss 37(1) or (2) is made out by a plaintiff other than a complaint falling under s 37(3)?”*
- (2) *“Where the complaint by the plaintiff under s 37 of the AA 2005 is only in respect of one of three principal issues before the Arbitrator or where the plaintiff’s case is made out only in respect of one out of three issues, whether the High Court is obliged as a matter of law under s 37 to set aside the whole Award?”*
- (3) *“Where a plaintiff has made an application jointly under s 37 and s 42 of the AA 2005 to set aside or vary an Award, and where only part of the Award is found to be bad in law, whether the Court would be entitled to invoke its powers under s 42(2) to set aside the Award in part or to vary it accordingly?”*
- (4) *“Where breach of natural justice is raised as a ground to set aside an arbitration award under s 37(1)(b)(ii) and s 37(2)(b) of the AA 2005, is it sufficient for the plaintiff to prove the alleged breach of natural justice without also establishing that the alleged breach would have made a difference to the outcome of the case?”*



FEDERAL COURT'S DECISION

The Federal Court noted that the “*principal issue in this appeal centres on the interpretation to be given to s 37 of the AA 2005*”, which reads as follow:-

“Application for setting aside

37.(1) *An award may be set aside by the High Court only if –*

(a) **the party making the application provides proof that –**

- (i) *a party to the arbitration agreement was under any incapacity;*
- (ii) *the arbitration agreement is not valid under the law to which the parties have subjected it to, or, failing any indication thereon, under the laws of Malaysia;*
- (iii) *the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present that party’s case;*
- (iv) *the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration;*
- (v) *subject to subsection (3), the award contains decisions on matters beyond the scope of the submission to arbitration; or*
- (vi) *the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Act from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Act; or*

(b) *the High Court finds that –*

- (i) *the subject matter of the dispute is not capable of settlement by arbitration under the laws of Malaysia; or*
- (ii) *the award is in conflict with the public policy of Malaysia.*

(2) *Without limiting the generality of subparagraph (1)(b)(ii) an award is in conflict with the public policy of Malaysia where –*

- (a) *the making of the award was induced or affected by fraud or corruption; or*
- (b) *a breach of the rules of natural justice occurred –*
 - (i) *during the arbitral proceedings; or*
 - (ii) *in connection with the making of the award.*

(3) **Where the decision on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside.”**

The Federal Court noted that in construing any statutes, the Court would apply the plain and ordinary meaning of the statute, before adopting a purposive approach if the words employed in the statute are not clear.

Having examined the manner in which AA 2005 “*fit in the overall scheme of the New York Convention and the Model Law*”, the Federal Court finds that section 37 of AA 2005 is plain and unambiguous and the High Court retains a residual discretion not to set aside an arbitral award even if the ground for setting aside are established:-

“[46] *In our considered view, the opening words of subsection 37(1) which employs the terms ‘may be set aside’ is plain and unambiguous. Subsection 37(1) clearly provides that the High Court retains a residual discretion not to set aside an award even though a ground for setting aside may be made out...*”



Having examined the arbitration enactments in Hong Kong, Singapore and New Zealand as well as the relevant case laws in those jurisdictions, the Federal Court laid down the guiding principles on the exercise of such residual discretion when the application to set aside is grounded on breach of natural justice:-

“First, the Court must consider (a) which rule of natural justice was breached; (b) how it was breached; and (c) in what way the breach was connected to the making of the award;

Second, the court must consider the seriousness of the breach in the sense of whether the breach was material to the outcome of the arbitral proceeding;

Third, if the breach is relatively immaterial or was not likely to have affected the outcome, discretion will be refused;

Fourth, even if the court finds that there is a serious breach, if the fact of the breach would not have any real impact on the result and that the arbitral tribunal would not have reached a different conclusion the court may refuse to set aside the award;

Fifth, where the breach is significant and might have affected the outcome, the award may be set aside;

Sixth, in some instances, the significance of the breach may be so great that the setting aside of the award is practically automatic, regardless of the effect on the outcome of the award;

Seventh, the discretion given the Court was intended to confer a wide discretion dependent on the nature of the breach and its impact. Therefore, the materiality of the breach and the possible effect on the outcome are relevant factors for consideration by the Court; and

Eighth, whilst materiality and causative factors are necessary to be established, prejudice is not a pre-requisite or requirement to set aside an award for breach of the rules of natural justice.”

On the issue of prejudice, the Federal Court finds that the Singaporean position is not applicable in Malaysia as the Singaporean International Arbitration Act requires prejudice to be established before an arbitral award can be set aside on the ground of breach of natural justice. Prejudice is not a prerequisite for setting aside application grounded on breach of natural justice under the AA 2005:-

“...Whilst we appreciate the appellant’s arguments that s 37 should be interpreted in a manner consistent with the underlying policies and objectives of the New York Convention and the Model Law, the courts must be mindful against importing principles advocated by foreign jurisdictions without careful consideration of the foreign law in question and our AA 2005. In this respect, we are bound to agree with the submission of the respondent that the Singapore position is not applicable in Malaysia. We say this because subsections 37(1)(b)(ii) and 37(2)(b)(ii) do not require prejudice to be established; unlike s 48(1)(a)(vi) of the Singapore Act...”

To this end, the Federal Court finds that the *“imposition of prejudice narrows down what is intended to be a wide discretion”* under section 37 AA 2005.

However, although the Court’s discretion to set aside an arbitral award under section 37(1) of the AA 2005 is unfettered, the Federal Court stressed that such discretion must be:-

“..exercised with regard to the policies and objectives underpinning the AA 2005. In particular, due cognizance must be taken of the purposes of encouraging arbitration as a method of dispute resolution and facilitating the recognition and enforcement of arbitral awards.”



ANSWERS TO THE QUESTIONS OF LAW

Having recognised the unfettered discretion of the Courts in Section 37(1) of the AA 2005, the Federal Court answered Questions 1 and 2 in the negative.

The Federal Court declined to answer Question 3 as the Federal Court agreed with the Court of Appeal that “*the breach had materiality and causative effect on the outcome of the arbitration*” and as such, the issue of only setting aside part of the award, i.e. the part of the award which is found to be bad in law, does not arise.

In relation to Question 4, the Federal Court made the following findings:-

“[62] As for Question 4, the issues have already been addressed in the foregoing paragraphs on the guiding principles on the exercise of discretion. As stated, a mere finding of a breach of the rules of natural justice is in itself insufficient. It must be shown that the breach was significant or serious such as to have an impact on the outcome of the arbitration. Prejudice, though, a relevant consideration, is not a requirement.”

Having agreed with the findings of the Court of Appeal, the Federal Court affirmed the Court of Appeal’s decision and dismissed the appeal.

MOVING FORWARD

Following the decision, it is important to note that:-

- (a) The High Court’s discretion to set aside an arbitral award under section 37(1) of the AA 2005 is “*unfettered*”, although such discretion “*must nevertheless be exercised with regard to the policies and objectives underpinning the AA 2005.*”
- (b) Corollary to that, the High Court is not bound to set aside an arbitral award even if a Plaintiff establishes any of the grounds of challenge under sections 37(1) or 37(2) of the AA 2005.
- (c) Where the Plaintiff satisfies the grounds for setting aside under section 37 of the AA 2005 in relation to **part** of the arbitral award, the High Court is not obliged, as a matter of law, to set aside the **whole** award.
- (d) The Federal Court laid down 8 guiding principles on the High Court’s exercise of residual discretion when an application for setting aside is grounded on breach of natural justice.
- (e) Whilst prejudice is a relevant consideration, it is not a prerequisite in setting aside an arbitral award grounded on breach of natural justice.



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