NATURAL JUSTICE IN INTERNATIONAL COMMERCIAL ARBITRATION: *TCL AIR CONDITIONER (ZHONGSHAN) CO LTD V CASTEL ELECTRONICS PTY LTD*

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International Commercial Arbitration is increasingly becoming the preferred means by which contractual parties whose relationship is transnational in nature choose to have their disputes resolved. The Australian judiciary has confirmed its minimal role in the arbitral process in the case of TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd (2014) *232 FCR 361. The court for the first time in Australia addressed how a party may succeed in having an arbitral award being refused enforceability or set aside on the basis of a denial of Natural justice in the proceeding. This case note comprehensively reviews the decision and tracks its judicial reception and impact on the judicial landscape in Australia.*

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I INTRODUCTION

The growth of International Commercial Arbitration currently spreading across Australia is not to be understated. Recent legislative amendments,[1]

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[1] The *International Arbitration Act 1974* (Cth) was amended on 6 July 2010 to give effect to the changes made to the *United Nations Commission on International Trade Law Model Law on International Commercial Arbitration* in 2006.

inaugurations of arbitration institutions and case law are indicative of this expansion.

In 1975 Australia became a signatory State[2] to the *Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (NY Convention). To give effect to Australia's obligations under the NY Convention the Commonwealth Parliament enacted the *International Arbitration Act 1974* (Cth) (IAA). As well as the IAA, the UNCITRAL *Model Law on International Commercial Arbitration* (Model Law)[3] has the force of law in Australia.[4] Together these two instruments provide the legislative framework for the regulation of international arbitration in Australia.

The global rise of international commercial arbitration has seen a corresponding increase in Australian case law in the field, and thus an increasing focus on the IAA. Commentators have recognized this rise as reflecting a 'heightened awareness of Australia's legal framework'[5] concerning International Arbitration. *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361 (TCL Air Conditioner) is one such case that interprets the IAA. This paper is a critical analysis of TCL Air Conditioner, which was the first case to analyse the circumstances in which an alleged denial of natural justice could justify a Court, under the IAA, in setting aside or refusing to enforce an arbitral award.[6]

II FACTUAL BACKGROUND

TCL Air Conditioner was heard in the Full Court of the Federal Court of Australia by Allsop CJ, Middleton and Foster JJ. Section 18(3)(c) of the IAA conferred jurisdiction on the Federal Court of Australia to hear the matter. TCL Air Conditioner (Zhongshan) Co Ltd (TCL) was a Chinese based

[2] *Contracting States*, New York Arbitration Convention <http://www.newyorkconvention.org/countries>.
[3] Scholars have noted the Model Law as beneficially serving as a '…template aimed at harmonizing and modernizing national arbitration legislation' for those nations which are signatory States to the NY Convention. See for example, Monichino, Nottage and Hu, 'International Arbitration in Australia: Selected Case Notes and Trends' (2012) 19 AUIntLawJl 181, 181.
[4] *International Arbitration Act 1974* (Cth) s 16(1).
[5] Monichino, Nottage and Hu, above n 5, 184.
[6] Only this aspect of the decision will be analysed in this Note.

company in the business of manufacturing air conditioning (AC) units.[7] Castel Electronics Pty Ltd (Castel) was an Australian based company that entered into a contract with TCL. The contract stipulated Castel as the exclusive distributor of TCL-manufactured AC units in Australia.[8]

A dispute arose between the parties when it surfaced that TCL had been selling in Australia for 4 years AC units it had manufactured, albeit the units not bearing its brand.[9] Castel asserted that such business activity on TCL's part breached the contractual term conferring exclusivity upon the former to rights of distribution.[10] As the dispute could not be mutually resolved, the contract provided for arbitration as the means by which to settle it.[11] In December 2010 the appointed arbitration panel, following a 10 day hearing, delivered an arbitral award in Castel's favor in the amount of $2,874,870.00, with an additional $732,500.00 in costs.[12]

Castel then sought to enforce the award pursuant to Article 35(1) of the Model Law.[13] TCL resisted Castel's action to enforce pursuant to Article 36(1)(b)(ii) and moved to have the award set aside pursuant to Article 34(2)(b)(ii). TCL also relied on ss 8(7A) and 19(b) of the IAA[14] as the basis for its claims.[15] TLC submitted the award ought to be set aside[16] or not be enforced[17] as being in conflict with or contrary to the public policy of Australia,[18] on the basis that the arbitral panel did not afford it natural justice during the hearing. TCL appealed to the Full Court after being unsuccessful at first instance.

[7] *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361, [2].
[8] Ibid.
[9] Ibid [4].
[10] Ibid.
[11] Ibid [2].
[12] Ibid [3].
[13] For the trial decision, see *Castel Electronics Pty Ltd v TCL Air Conditioner (Zhongshan) Co Ltd (No 2)* [2012] FCA 1214.
[14] As well as *International Arbitration Act 1974* (Cth) s 8(7A).
[15] *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361, [6].
[16] *Model Law* Art 34(2)(b)(ii).
[17] Ibid Art 36(1)(b)(ii).
[18] The abovementioned *Model Law* articles relied upon by TCL owe its origin to the *NY Convention* art V(2)(b).

III Appeal Grounds

TCL did not allege bias in the arbitrators. It would have been a difficult argument to make given the panel was constituted of Dr Gavan Griffith AO, the Hon Alan Goldberg AO and Mr Peter Riordan SC. The only limb of natural justice considered by the court was the fair hearing limb.

TCL contended that it was 'denied an opportunity to present evidence and argument'[19] on findings which together enabled the arbitrators to quantify the financial detriment caused to Castel as a result of TCL's breach.[20] It was argued that the quantum of damages was calculated in the absence of probative evidence.[21] The issue falling for determination was whether the content of natural justice in the context of the IAA extended to the allegations made by TCL.[22]

In determining whether natural justice had been afforded TCL asserted that the proper approach was to examine the facts of the case afresh and revisit in full the questions which were before the arbitrators in order to evaluate whether or not probative material supported the factual conclusion.[23] The Full Court rejected this approach for the reasons below.

IV Legal Principles and Factual Application

A *Limited Scope of Public Policy Defense*

The Court provided a detailed analysis of the discussions and extrinsic legislative material leading to the creation of the NY Convention, the Model Law and the IAA, including what each of those instruments entailed.[24] In this respect, the Court appeared to be employing a contextual statutory interpretation technique to enable it to gain a holistic understanding of the legislative framework with which it was dealing. The phrase 'public policy', appearing in all three instruments, was given particular attention.[25] Drawing

[19] *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361, [7].
[20] Ibid [33] - [41].
[21] Ibid [8].
[22] Ibid [11].
[23] Ibid [8].
[24] Ibid [57] - [67].
[25] Ibid [64].

upon the legislative history of the NY Convention, the Court stated the phrase did not refer to 'particular domestic national public policy',[26] but rather denoted 'a concept recognizing the international place of the NY Convention and the need for public policy to be restricted to be State's most basic, fundamental principles of morality and justice'.[27] The Court also referred to Article 18 of the Model Law as ensuring fairness in arbitration hearings.[28]

The court supported its initial construction with an analysis of international jurisprudence dealing with similar legislation to the IAA.[29] Such authorities, though not binding upon Australian Courts, are of persuasive value due to the transnational provenance of international arbitration and the need to maintain 'a degree of international harmony and concordance of approach'.[30] After an in depth analysis of the case law[31] the Court found the weight of authority endorsed the phrase 'public policy' as being intended by its drafters to be '…limited to the fundamental principles of justice and morality of the state'.[32] To this effect, the Court was verifying that its narrow interpretation of 'public policy'[33] was one which had widespread support.

B *Requisite Natural Justice for Enforceable Arbitral Awards*

The Court then considered how natural justice sits against this narrow construction of public policy, an issue that had not yet been addressed by Australian courts. After exploring the legislative background of sections 19(b) and 8(7A) of the IAA,[34] the Court held that a breach of the rules of natural justice was listed in the IAA as a circumstance in which an arbitral award might be in conflict with or contrary to the public policy of Australia 'to avoid confusion' and 'any doubt' that it was not such a circumstance.[35] Therefore, the meaning of 'public policy', found in the Model Law and elsewhere as a defense

[26] Ibid.
[27] Ibid.
[28] Ibid [67].
[29] Such foreign legislation is also based on the Model Law and NY Convention.
[30] *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361 [75]. Such an approach is said to accord with section s 2D of the *International Arbitration Act 1974* (Cth) and Art 2A of the *Model Law*.
[31] Ibid [75] - [80].
[32] Ibid [76].
[33] An interpretation also given in other Australian authorities, see ibid [80].
[34] Ibid [71].
[35] Ibid [73].

to resist enforcement or as grounds to set aside an award, was not in any shape or form altered as a result of the introduction of those IAA provisions.

Appreciating this permitted the Court to articulate natural justice as falling '…within the conception of a fundamental principle of justice, being… equated with, and based on, the notion of *fairness*'.[36] The effective and efficient running of the international arbitration system in Australia was at the forefront of the Court's mind.[37] As their Honors importantly noted, the Model Law embraces a system which places 'independence, autonomy and authority into the hands of arbitrators'.[38] Similarly, it was noted elsewhere that arbitral hearings and resulting awards 'should not be scrutinized with an overcritical or pedantic eye'[39] or with undue legality, but rather ought to be reviewed with 'commonsense'.[40] Maintaining a workable balance between the finality of arbitral awards and appropriate judicial interference required, in the Court's view, courts to act '…prudently, sparingly and responsibly, but decisively when grounds under Articles 34 and 36 are revealed'.[41]

The Court held that the rules of natural justice in this context do not require arbitrators to have probative evidence to support their factual findings, nor are they required to show logical reasoning to support factual conclusions.[42] If the court was to make these inquiries it would have to re-agitate the proceedings and go over the panel's findings and this would severely undermine the arbitration system in Australia.[43] In this respect, the distinction between a factual evaluation of available evidence and a complete absence of supporting material should not be blurred.[44] The rules of natural justice cannot be 'broken' in a minor and technical way.[45] The natural justice ground will not

[36] Ibid. For example, for a finding to be deemed to be in breach of the rules of natural justice for want of probative evidence, the Court noted the fact or facts upon which the finding of the arbitral panel was based must have been critical, have never been the subject of attention at the hearing and the finding must have been made without the parties taking advantage of the chance to address it, see ibid [83].
[37] Ibid [109].
[38] Ibid.
[39] *Colin Joss & Co Pty Ltd v Cube Furniture Pty Ltd* [2015] NSWSC 735, [47].
[40] Ibid.
[41] Ibid [109].
[42] Ibid [54].
[43] Ibid.
[44] Ibid.
[45] Ibid.

be made out unless it is shown that some real unfairness or practical injustice occurred.[46]

C *Application of the Principles to the Case*

TCL bore the onus to show, in a succinct manner, that there was a meaningful breach of the rules of natural justice such that it suffered real unfairness or real practical injustice.[47] This was, in the circumstances, found by the Court not to have been discharged by TCL. It was essentially seeking a re-hearing of the facts, an approach which unacceptably worked to 'undermine the object of facilitating the expeditious and fair enforcement of awards'[48] in international arbitration. TCL was misusing the court's judicial review function by 'dressing up'[49] its complaints regarding the factual findings as an allegation concerning 'asserted procedural unfairness'.[50] In the Court's view, the arbitrators calculated a damages amount after carefully evaluating the available evidence, as opposed to engaging in mere guesswork.[51] In dismissing the appeal, the Court concluded that TCL '…received a scrupulously fair hearing in a hard fought commercial dispute',[52] and so TCL could not avail itself of the established 'no evidence' rule of natural justice. As Chief Justice Menon of Singapore relevantly stated in a recent judgment, courts should resist the temptation to offer parties '…a second chance to canvass the merits of their respective cases'.[53]

V JUDICIAL RECEPTION

The utility and strength this decision of the Full Court of the Federal Court holds in Australia is best gleaned through an analysis of subsequent case law in which it has been considered. The Supreme Court of Victoria in *Robotunits Pty*

[46] Ibid [55].
[47] Ibid [153]. This is a position of which is shared by the Singaporean Judiciary, see for example *CRW Joint Operation v PT Perusahaan Gas Negara (Persero) TBK* [2011] SLR 305, 342-343.
[48] *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361 (16 July 2014), [81].
[49] Ibid [53].
[50] Ibid.
[51] *TCL Air Conditioner (Zhongshan) Co Ltd v Castel Electronics Pty Ltd* (2014) 232 FCR 361, [163].
[52] Ibid [167].
[53] *AKN v ALC* [2015] SGCA 18, [37].

Ltd v Mennel (2015) 297 FLR 300 at [13] – [14] and in *Cameron Australasia Pty Ltd v AED Oil Ltd* [2015] VSC 163 at [19] was guided by the notion promulgated by the Federal Court of the need to pay due deference to international judgments in order to maintain international uniformity in the area of International Arbitration.

In New South Wales, *Aircraft Support Industries Pty Ltd v William Hare UAE LLC* [2015] NSWCA 229 involved a direct application of the principles laid down by the Federal Court. A sub-contract existed between the appellant, an Australian company, and the UAE based respondent which provided for the respondent to perform certain construction work in exchange for payments from the appellant.[54] A letter was sent from the appellant to the respondent detailing the final amount, money already paid in satisfaction of this and the dates by which retention monies would be released.[55] A dispute[56] arose regarding the appellant's failure to pay the second installment of retention monies by the date stipulated in the letter.[57] In accordance with the contract, the dispute was settled by arbitration in the UAE after which an award was made in favor of the respondent prompting the respondent to seek enforcement of the award in Australia under the IAA.[58] The appellant, in resisting enforcement, contended the sent letter was not executed in accordance with the required formalities and so could not constitute a variation to the sub-contract or indeed bear any legal character.[59]

The appellant argued that this submission was not considered by the arbitral tribunal and accordingly the award was contrary to the public policy of Australia as there was a breach of the rules of natural justice. The primary judge,[60] with whom the appeal division of the Supreme Court of New South Wales agreed, applied the TCL Air Conditioner case to find the appellant had not demonstrated it had suffered any practical unfairness or injustice.[61] It was duly noted that the arbitral panel had dealt adequately with each of the

[54] *Aircraft Support Industries Pty Ltd v William Hare UAE LLC* [2015] NSWCA 229, [3].
[55] Ibid.
[56] Among others raised.
[57] *Aircraft Support Industries Pty Ltd v William Hare UAE LLC* [2015] NSWCA 229, [3].
[58] Ibid [6].
[59] Ibid [39].
[60] See *William Hare UAE LLC v Aircraft Support Industries Pty Ltd* [2014] NSWSC 1403, [111].
[61] *Aircraft Support Industries Pty Ltd v William Hare UAE LLC* [2015] NSWCA 229, [44].

appellant's arguments which were clearly articulated.[62] However, the appellant failed to substantiate clearly its main contention beyond merely raising it in its pleadings.[63] The arbitral tribunal had no obligation to deal with unsupported assertions.[64] The foreign award was found not to be infected with any material breach of the rules of natural justice and was thereby capable of being enforced so far as the second installment of the retention monies was concerned, with the sent letter amounting to a binding settlement.

Another noteworthy New South Wales case is *Colin Joss & Co Pty Ltd v Cube Furniture Pty Ltd* [2015] NSWSC 735. All Australian States have enacted uniform arbitration statutes dealing with the subject matter in the domestic context. Similar to the IAA, the New South Wales Act allows for the setting aside of arbitral awards made in conflict with the public policy of the State.[65] Significantly, the Court here extended the applicability of the principles expressed in the TCL Air Conditioner case to the domestic arbitration arena by requiring the aggrieved party to demonstrate real unfairness or real practical injustice by reference to the established rules of natural justice. In providing further content to this principle, the Court stated that the public policy ground to set aside an award '…is not concerned with mere procedural imperfections but with a negation of rights which our legal system recognizes as being fundamental and therefore matters of public policy'.[66]

VI Conclusion

In TCL Air Conditioner the Federal Court clarified an ambiguous area of the law that had not yet had the benefit of judicial attention. The case placed Australia in line with its foreign counterparts. For this reason it seems unlikely that the High Court of Australia would depart from the reasoning adopted by the Federal Court should s19(b) of the IAA be revisited in that forum. A study of TCL Air Conditioner demonstrates how courts vested with jurisdiction under the IAA are tasked with crucial supervisory functions, the limits of which

[62] *William Hare UAE LLC v Aircraft Support Industries Pty Ltd* [2014] NSWSC 1403, [103].
[63] *Aircraft Support Industries Pty Ltd v William Hare UAE LLC* [2015] NSWCA 229, [44] - [45].
[64] Ibid [46].
[65] *Commercial Arbitration Act 2010* (NSW) s 34(2)(b)(ii).
[66] *Colin Joss & Co Pty Ltd v Cube Furniture Pty Ltd* [2015] NSWSC 735, [46].

must be strictly observed in respect of the setting aside, non-enforcement or non-recognition of awards.

TCL Air Conditioner confirms that the collective effect of the IAA, the Model Law and the NY Convention is to encourage courts not to stifle the integrity, finality and certainty of the arbitral finding process. As Allsop CJ stated extra-curially, the Australian judiciary, in the context of International Arbitration decision-making, needs to continue to display an assistive, supportive and sympathetic attitude in respect of the arbitration process and to exercise reasonable restraint where appropriate.[67] TCL Air Conditioner is a prime example of the Australian judiciary adopting a pro-arbitration stance[68] and taking a proactive stride in bolstering the country's 'reputation as a strong arbitral jurisdiction'.[69] This case will also inform future decisions on the topic as well as provide great assistance to lawyers in advising clients as to the merits of challenging the legality of an arbitral award on public policy grounds given the high threshold imposed.

[67] Allsop J, International Arbitration and the Courts: The Australian approach in CIArbs Asia Pacific Conference 2011 *Investment & Innovation: International Dispute Resolution in the Asia Pacific* (2011), 7.
[68] Chung L, Stollery J and Christlo E, *Australian Court Upholds Primacy of the Arbitral Fact Finding Process* (*Herbert Smith Freehills*, 17 July 2014) <http://hsfnotes.com/arbitration/2014/07/17/australian-court-upholds-primacy-of-the-arbitral-fact-finding-process/> viewed 12 February 2016.
[69] Croft, above n 65.