

Arbitration and third parties.

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QUEEN MARY UNIVERSITY OF LONDON

SCHOOL OF INTERNATIONAL ARBITRATION

ARBITRATION AND THIRD PARTIES

By

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Thesis for the degree of Doctor of Philosophy

London, 2008

Under the supervision of:
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Acknowledgments

I often thought that writing the acknowledgments would be the easiest part of the thesis. After all, this was the moment I have been rehearsing the most during my Ph.D years. I was wrong. This is mainly because it is a overwhelming task involving a great deal of emotional retrospection. It requires me to review all the good and, most certainly, the bad times I have naturally been through all these years of research and writing. All these moments that I thought I had made a breakthrough but I was wrong, again and again. All these moments that my initial excitement about one of my ideas or my arguments was quickly replaced by an erosive feeling of doubt. There was not a single instance that I thought of quitting. But there were several moments of scepticism and uncertainty for the final outcome. It has been, indeed, a long, tiring and very often lonely experience. But it was an experience that was absolutely worth going through.

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ABSTRACT

ARBITRATION AND THIRD PARTIES

Stavros Brekoulakis

Modern international transactions have become extremely complicated, requiring the participation of several parties for the delivery of large-scale projects. However, multiparty commercial projects are invariably executed through several bilateral contracts providing for bilateral dispute resolution arrangements. Some of the contracts might include a jurisdiction clause, certain others might provide for arbitration, while others may not contain any dispute resolution provisions at all. This practice leads to “jurisdictional fragmentation of the multiparty commercial project” where the several parties of a single business plan will fall under the jurisdiction of different adjudicatory fora. Thus, a dispute arising between two persons bound by an arbitration agreement in connection with the multiparty project will have to be resolved exclusively by arbitration between these two parties. Other persons cannot take part in the resolution of the dispute, even if they play an active role in the actual business project, and thus have an interest in the outcome of the dispute. These persons will remain *third parties* both to the arbitration agreement and the arbitral award.

This study focuses on the role and the interests of the wide group of third parties exhibiting an interest in the dispute pending before a tribunal between two genuine parties. The thesis, in particular, examines *whether arbitration agreements* can affect persons which are not contractually bound by these agreements. In addition, the thesis explores whether *arbitral awards* can affect persons that have not participated in the arbitration proceedings

The thesis challenges the prevailing contractual approach to the issue of arbitration, focusing exclusively on the contractual characteristics of arbitration agreements. According to this view, the main question is whether a non-signatory can be contractually bound by an arbitration agreement. The study demonstrates that focusing exclusively on the contractual nature of arbitration agreements obscures the real issue here, which is whether arbitration agreements may have any jurisdictional implications vis-à-vis ‘third parties’. Accordingly, the thesis takes a jurisdictional approach, and argues that the discussion should be focused on the dispute and on any implications this may have to third parties, rather than on the requirement of consent to arbitration agreements.

Regarding the effect of arbitral awards on third parties, the thesis argues for a third-party effect of arbitral awards specially designed for the needs of international arbitration. More specifically, the case is made for the application of an arbitral effect different from that of *res judicata*, both in terms of quality and intensity, but that is nevertheless conclusive. It is also suggested that the third party effect of an arbitral award should be analogous to the degree of substantive association between the genuine and the false third parties. This is consistent with the basic premise of the whole thesis: the relations between several parties, in terms of jurisdiction and more generally in arbitration procedure, should correspond to the extent of association between those parties, in terms of substantive rights, interests and liability.

TABLE OF CONTENTS

INTRODUCTION	4
<i>Arbitration and third parties: setting out the framework of the discussion.....</i>	<i>4</i>
<i>Scope of the thesis- Research questions</i>	<i>7</i>
<i>Theoretical Background of the discussion on arbitration and third parties- suggestions of the thesis</i>	<i>9</i>
First, the concept of “false third parties”	9
Second, the effect of arbitration agreements upon third parties.....	10
Third, the effect of arbitration awards upon third parties	14
<i>Research methodology.....</i>	<i>16</i>
<i>Structure of the thesis</i>	<i>17</i>
PART I: PARTIES AND ARBITRATION AGREEMENTS.....	19
CHAPTER 1: GENUINE PARTIES TO ARBITRATION AGREEMENTS- NOTION AND RELEVANCE TO THE THESIS	20
1.1 Agency - representation.....	21
1.2. Assignment.....	22
1.3 Succession - novation	24
1.4 Specific consent to arbitrate and genuine parties to arbitration agreements	24
CHAPTER 2: THE NOTION OF FALSE THIRD PARTIES.....	28
2.1 Different groups of false third parties	29
2.2 String construction contracts.....	32
2.3 Web-type construction contracts	41
2.4 Guarantees and other security agreements	43
2.5 Several companies with close corporate links: the case of the “group of companies” in particular.....	49
CONCLUSIONS OF PART I	55
PART II: ARBITRATION AND THIRD PARTIES: THE CONTRACTUAL APPROACH.....	57
CHAPTER 3: THIRD-PARTY MECHANISMS	60
3.1 Third-party mechanisms and consent.....	60
3.1.1 Equal treatment of the several co-respondents or co-claimants in the constitution of the tribunal.....	62
3.1.2 Effective interpretation of multiparty arbitration clauses	63
3. 2. Third-party mechanisms in arbitration rules and laws	64
CHAPTER 4: EXTENSION DOCTRINES- THE DOCTRINE OF EQUITABLE ESTOPPEL.....	68
4.1 general Overview of the doctrine	68
4.2 Commentary on the doctrine: content and conditions of application	69
4.2.1 The application of the doctrine presupposes a thorough analysis of the dispute and its factual circumstances	69
4.2.2 Moving away from its equitable origins: the “intertwined factor” and the conditions for the application of the doctrine	70
4.2.2.1 First, the dispute between the signatory and the non-signatory party must be intertwined with the contract between the signatories	72
4.2.2.2 Second, the non-signatory party must have close contractual or corporate links with one of the signatory parties.....	77
4.2.2.3 Concluding remarks on the intertwined version of the equitable doctrine....	78
4.2.3 Equitable estoppel doctrine and consensual origins of arbitration.....	79
4.2.4 The court rather than the tribunal will determine whether the dispute between the signatory and the non-signatory party is arbitrable or not	82

CHAPTER 5: THE DOCTRINE OF GROUP OF COMPANIES.....	84
5.1 <i>OVERVIEW OF THE doctrine</i>	85
5.2 <i>Legal basis of the doctrine</i>	86
5.3 <i>Conditions for the application of the doctrine</i>	88
5.3.1 First, the group corporate structure.....	92
5.3.2 Second, active role of the non-signatory companies in the negotiations, performance or termination of the contract.....	94
5.3.3 Third, legitimate impression of the co-contracting party that the non-signatory companies are genuine contracting parties	95
CHAPTER 6: CRITIQUE ON THE EXTENSION DOCTRINES	98
6.1 <i>Positive contribution of extension doctrines</i>	98
6. 2 <i>Conceptual inefficiencies of the extension doctrines</i>	99
6.2.1 The extension doctrines fail to distinguish between the different types of third parties.....	99
6.2.2 Limitations of the extension doctrines based on consent (consensual extension doctrines)	100
6.2.2.1 Deduction of implied consent is not always justified.....	102
6.2.2.2 Specific arbitral consent is required for the non-signatory to be bound by the arbitration agreement.....	104
6.2.2.3 Misapplication of traditional principles of contract law in the context of the extension doctrines.....	110
6.2.2.4 Conclusions on the extension doctrines based on consent	112
6.2.3 Limitations of extension doctrines not based on consent (non-consensual extension doctrines)	113
6.2.4 The extension doctrines and the “writing requirement”	118
6.3 <i>Conclusions on the extension doctrines and the contractual approach</i>	120
PART III: THE SUGGESTION FOR A JURISDICTIONAL APPROACH TO THE ISSUE OF THIRD PARTIES AND ARBITRATION.....	123
CHAPTER 7: THE CONCEPTUAL PREMISES OF THE JURISDICTIONAL APPROACH: EFFECTIVE ARBITRAL JURISDICTION AND EXTRA-CONTRACTUAL JURISDICTION	127
7.1 <i>The extra-contractual lis pendens effect of arbitration agreements in the context of multiparty relationships</i>	127
7.2 <i>National courts and extraterritorial jurisdiction: the case for application by analogy in the context of arbitration</i>	134
CHAPTER 8: THE UNDERLYING PRINCIPLES AND RATIONALE OF THIRD-PARTY MECHANISMS	139
8.1 <i>The importance of third-party mechanisms in international arbitration</i>	138
8.1.1 Third-party mechanisms and functional equilibrium between substance and procedure in multiparty relationships	140
8.1.2 Efficiency in arbitration: regulating overlapping parallel proceedings.....	142
8.1.3 Third-party mechanisms and the interests of the several parties to arbitration..	144
8.2 <i>Comparative analysis of third-party mechanisms in the context of national and international litigation: underpinning rationale and general principles</i>	146
8.2.1 Overview and different groups of third-party mechanisms	146
8.2.2 Policy analysis of the third-party mechanisms: distinctions and underpinning rationale	153
8.3 <i>Conclusions of Chapter 8</i>	164
CHAPTER 9: THIRD-PARTY MECHANISMS IN THE CONTEXT OF ARBITRATION AND THE PRINCIPLE OF PROCEDURAL PARTY AUTONOMY	165
9.1 <i>Relevance of the principle of procedural party autonomy</i>	165

9.2 Procedural party autonomy, as a rule, will prevail over third-party mechanisms .	167
9.3 Third-party mechanisms in the context of multiparty projects where parties are contractually interrelated but not strongly associated in substantive terms	170

CHAPTER 10: THE EXCEPTIONAL CIRCUMSTANCES WHERE THIRD-PARTY MECHANISMS SHOULD APPLY IN ARBITRATION176

10.1 The fundamental role of the pending dispute for the determination of the jurisdiction of a tribunal	174
10.2 Co-liability or community of rights between the several parties as a threshold for extra-contractual jurisdiction and third-party mechanisms	179
10.2.1 First: co-liability resulting from the contractual arrangements of the several parties	178
10.2.2 Second: co-liability resulting from the applicable substantive law	187
10.2.3 No lower threshold than co-liability or community of rights and duties warrants extra-contractual jurisdiction and third-party mechanisms	190

CHAPTER 11: FINAL REMARKS ON THE JURISDICTIONAL APPROACH.....201

11.1 applying third-party mechanisms in arbitration: The third party remains a party not bound by the arbitration agreement	201
11.2 Examining the dispute at the stage of determination of the jurisdiction does not lead to prejudgment of the merits of the dispute	203
11.3 Practical relevance of the jurisdictional approach	205
11.3.1 The law applicable to the validity and the interpretation of the arbitration agreement	205
11.3.2 Jurisdiction in accordance with the jurisdictional approach is determined on a basis closer to commercial reality	210

CHAPTER 12: THE EFFECT OF AN ARBITRAL AWARD AND THIRD PARTIES IN INTERNATIONAL ARBITRATION215

12.1 THE ARBITRAL EFFECT	217
12.1.1 Legal Framework Regarding Arbitral Effect	218
12.1.2 National Regimes on <i>Res Judicata</i> : Differences and Constituent Elements	220
12.1.2.1 Differences	220
12.1.2.2 Constituent Elements of <i>Res Judicata</i>	218
12.2 RES JUDICATA AND THIRD PARTIES	220
12.2.1 The “Same Parties” Requirement: Rule and Exceptions	220
12.2.2 False Third Parties: The Problem	223
12.2.2.1: Solutions in the context of litigation: unification and harmonisation mechanisms	224
12.2.2.2 Solutions in the context of Arbitration	228
12.3 THE SUGGESTED THIRD-PARTY ARBITRAL EFFECT	230
12.3.1. Examination of the Suggested Effect	234
12.3.2 Characteristics of the Third-Party Arbitral Effect- Distinction from <i>Res Judicata</i>	234
12.3.3 Requirements of the Arbitral Effect	236
12.3.4 The Parties Affected	238
12.4. THE LEGAL BASIS OF THE EFFECT OF AN INTERNATIONAL AWARD	245
12.5. CONCLUSION	248

CONCLUSIONS250

Remarks on existing views on arbitration and third parties	246
Suggestions of the thesis on “arbitration and third parties”	254

Table of cases and awards	267
Bibliography	284

INTRODUCTION	4
<i>Arbitration and third parties: setting out the framework of the discussion.....</i>	<i>4</i>
<i>Scope of the thesis- Research questions.....</i>	<i>7</i>
<i>Theoretical Background of the discussion on arbitration and third parties-</i>	
<i>suggestions of the thesis</i>	<i>9</i>
First, the concept of “false third parties”	9
Second, the effect of arbitration agreements upon third parties	10
Third, the effect of arbitration awards upon third parties	14
<i>Research methodology</i>	<i>16</i>
<i>Structure of the thesis</i>	<i>18</i>

INTRODUCTION

ARBITRATION AND THIRD PARTIES: SETTING OUT THE FRAMEWORK OF THE DISCUSSION

The study of the interrelation between arbitration and third parties is an integral part of any discussion touching upon elements of arbitration. This owes to the very definition of arbitration as a consensual dispute resolution mechanism binding only those persons that have unequivocally consented to an arbitration agreement.¹

The contractual foundations of arbitration constitute the fundamental difference between arbitration and litigation. In litigation the capacity to become a party to court proceedings is determined on the basis of interest(s). Provided that it is subject to the territorial jurisdiction of the particular national court,² a legal or a natural person is entitled to commence court proceedings whenever it needs to protect its legal or financial interest.³

¹ See J. Lew, L. Mistelis and S. Kroell, *Comparative International Commercial Arbitration*, (Kluwer Law International 2003), para 7-3 et seq; P. Fouchard, E. Gaillard and B. Goldman, *On International Commercial Arbitration*, E. Gaillard and J. Savage (eds.) (1999), para. 498.

² Which is usually determined on the basis of the domicile, residency or even presence of the defendant.

³ See in US Federal Rules of Civil Procedure, r.17:

“Parties Plaintiff and Defendant-

Capacity (a) Real Party in Interest:

Every action shall be prosecuted in the name of the real party in interest”

Cf English Civil Procedure Rules (CPR) r.19.6:

“Representative parties with same interest:

(1) Where more than one person has the same interest in a claim—

(a) the claim may be begun; or

(b) the court may order that the claim be continued.

By contrast, in the context of arbitration, it is generally accepted that the capacity to take part in proceedings is exclusively determined on a contractual basis.⁴ Entering into an arbitration agreement is the indispensable requirement for a person to participate into the arbitration proceedings and be bound by the resulting arbitral award.

The principle of procedural party autonomy provides parties with the freedom to determine in their contract the circle of the persons that can participate in the arbitral proceedings. Parties not bound by an arbitration agreement, i.e. third parties, are excluded from the arbitration process. Any legal or financial interest that a third party might have in the dispute between the parties bound by the arbitration agreement is in principle irrelevant.

The principle of procedural party autonomy and the contractual foundations of arbitration make arbitration a very flexible dispute resolution mechanism, allowing the parties to establish a dispute resolution mechanism in accordance with their commercial needs. This has proved a significant advantage of arbitration over litigation, and it has contributed to the increasing popularity of the former amongst members of the international commercial community, particularly in the last thirty years.

By the same token, in the context of multiparty commercial relationships, the contractual, and thus relative, nature of arbitration frequently leads to unfavourable results. Modern international transactions have become extremely complicated, requiring the participation of several parties for the delivery of large-scale projects. For example, a typical construction project will usually involve, apart from the employer and the main contractor, an engineer and/or an architect, several subcontractors, suppliers, financiers and possibly more commercial parties. Multiparty situations may also result from finance and security agreements, such as guarantees, indemnities or performance bonds, where a bank, an insurance company or a protection and indemnity association will come into play providing security for the main contract exclusively concluded between two other parties. Particular mention should also be made to the modern corporate structure of multinational companies. Nowadays the typical form of business organisation views large corporations carrying

by or against one or more of the persons who have the same interest as representatives of any other persons who have that interest”.

⁴ Russell, *On Arbitration*, D. Sutton, J. Gill, M. Gearing (23rd ed. Sweet & Maxwell London 2007), para 3-002.

out their affairs through a number of subsidiaries in several countries. Thus, several companies (affiliates, or subsidiary companies, or officers, directors, stockholders and members of that legal entity) of the same group will often take part in the execution of a contract concluded by only one company of the group.

However, multiparty commercial projects are invariably executed through several bilateral contracts rather than through a single agreement applicable to the several parties to the project. Accordingly, the several bilateral substantive contracts will usually provide for bilateral dispute resolution arrangements. Some of the contracts might include a jurisdiction clause, certain others might provide for arbitration, while others may not contain any dispute resolution provisions at all. Even those contracts, including jurisdiction or arbitration clauses will usually fail to provide for the same national court or the same type of arbitration. Thus, it often happens that the several parties make jurisdictional arrangements on a bilateral basis, against the backdrop of a multiparty commercial project. In other words, the parties will opt for *a scheme of several bilateral proceedings* rather than a single set of multiparty proceedings. This practice leads to what is called, here, “jurisdictional fragmentation of the multiparty commercial project”, which occurs when the several parties of a single business project are subject to the jurisdiction of different adjudicatory fora.

Thus, a dispute arising between two persons bound by an arbitration agreement in connection with the multiparty project will have to be resolved exclusively by arbitration between these two parties, which for the purposes of the thesis are named *genuine* or *original parties* to an arbitration agreement and arbitration proceedings. Other persons than the genuine parties cannot participate in the resolution of the dispute, even if they play an active role in the actual business project, and, therefore, they have an interest in the outcome of the dispute. These persons will remain *third parties* both to the arbitration agreement and the arbitral award between the genuine parties.

Therefore, procedural fragmentation leads to a *discrepancy* between the circle of persons taking part to the resolution of a dispute by arbitration, and the circle of persons not entitled to participate therein despite the fact that they have a legal and financial interest in the dispute.

To give some examples:

- A guarantor may remain outside the arbitration between a creditor and a debtor. This may be the case despite the fact that this arbitration may well

determine that the guaranteed debt has been extinguished, in which case the guarantor would cease to be liable.

- A subcontractor may not take part in the arbitration between an owner and a contractor, although this arbitration may well determine that the work actually delivered by the subcontractor is defective.
- A team of stockholders may not take part in the arbitration between the corporation and another party, although the arbitration may find against the corporation with considerable financial repercussions for the stockholders.

Conversely, the parties to the arbitration process are denied the chance to confront other parties that play an active role in the actual business project:

- A parent company of one of the parties to an arbitration agreement would stay out of the arbitration between its subsidiary and the other genuine party, although the parent company might have taken a decisive role in the performance of the contract.
- A guarantor would stay outside the arbitration between the creditor and the principal debtor, although, the arbitration might well determine that the guaranteed debt exists, in which case the creditor would have an obvious interest in seeing the guarantor be bound by the award.

Consequently, jurisdictional fragmentation of multiparty commercial transactions excludes parties with a significant interest in a particular transaction from taking part in the resolution of the disputes arising out of this transaction. Additionally, it leads to multiplicity of legal proceedings, either arbitral or judicial, which in turn, may result in a considerable waste of legal and financial resources. More importantly, though, jurisdictional fragmentation may result in inconsistent, if not conflicting, decisions. This outcome will eventually frustrate parties' expectations from arbitration and may well undermine the tribunal's main goal, namely the effective resolution of the dispute.

SCOPE OF THE THESIS- RESEARCH QUESTIONS

This study focuses on the wide group of third parties with an interest in the dispute pending before a tribunal between two genuine parties. Third parties of this group are not bound by an arbitration agreement, but they are not strangers to the dispute and

the arbitration proceedings either. Since their interests are related to the outcome of the dispute, any factual or legal determination in the arbitral proceeding may well affect their legal position. Therefore, third parties having an interest in the dispute between to other parties bound by an arbitration agreement are labelled by the thesis “false third parties”. The main research questions that will be addressed here are:

- The role and the *interests* of false third parties
- Whether an *arbitration agreement* can have an effect on any persons not contractually bound by it
- If yes, under which circumstances this would come into effect and what potential results would arise
- Whether an *arbitral award* can affect any person that has not participated in the arbitration proceedings
- If yes, what would the specific conditions and possible outcomes of such circumstances be

Generally speaking, the thesis explores whether it is possible for arbitration to interact with persons that are neither contractual parties to an arbitration agreement, nor parties to arbitration proceedings. Ultimately, the thesis tests *the consensual boundaries of arbitration*.

Thus, the thesis will not be looking into cases where all the parties involved in the same commercial project have consented to arbitration. Even in situations when consent to multiparty proceedings is not disputed, several issues may well arise. For example, matters with regard to the constitution of the tribunal, the allocation of the costs of the arbitration or the conduct of the arbitral proceedings will often arise in the context of multiparty arbitrations. However, these issues are in the periphery of the conceptual boundaries of this work, and therefore, they will only briefly be mentioned in the thesis.

Equally, the thesis will not focus on matters that, although touch on arbitration and involve more than two parties, predominantly relate to general contract law. Thus, for example, problems concerning the succession of arbitration agreements or the conclusion of arbitration agreements by an agent are more relevant to general principles of succession applicable to all substantive contracts than to principles of arbitration law. Accordingly, they will only shortly be discussed in the first Chapter of

the thesis, but they will not be examined any further. The discussion in the thesis is based on the assumption that a third party has not consented to arbitration.

THEORETICAL BACKGROUND OF THE DISCUSSION ON ARBITRATION AND THIRD PARTIES- SUGGESTIONS OF THE THESIS

Arbitration and third parties, or multiparty arbitration as is usually referred to, is one of the most pervasive topics in arbitration law and practice. However, in spite of the extensive relevant literature, the issue is far from settled. In particular, further study pertains to three relative areas, namely the notion of “false third parties”, the effect of arbitration agreements upon third parties and the effect of arbitration awards upon third parties. At this stage, it is useful to explain and briefly discuss the existing theoretical background of these issues and, at the same time, outline the main suggestions of this study, which will be then presented in analytical detail in the main part of the thesis.

First, the concept of “false third parties”

It is essential to establish a theoretical basis for defining the notion of “false third parties” as opposed to that of third parties in general. Strictly speaking, every person not bound by an arbitration agreement is a third party. However, not all third parties would be relevant in an arbitration between the two original parties. Only third parties that have a legal or financial *interest* in the dispute pending before the tribunal may be relevant, namely the “false third parties”.

Thus, the interest that a third party may have in the pending dispute is a *key factor* to determine which persons are pertinent to the discussion on arbitration and third parties. From this perspective, the thesis explores in detail the notion of “false third parties”. The aim here is to canvass the interests of false third parties, and, on that basis, distinguish between different types of false third parties. The analysis takes a *substantive viewpoint*, focusing on the association between the genuine and the false third parties, in terms of contractual rights, duties and liabilities. In the light of the findings of this analysis, it will be argued that we should distinguish between two groups of false third parties: those that share the same rights, duties and liabilities with the genuine parties to the arbitration, and those that are merely contractually interrelated with them. It will be shown that the interests of the former in the

arbitration between the two genuine parties are stronger and, thus, more relevant than the interests of the latter.

This distinction is essential for the purposes of the thesis, as it provides the conceptual grounds for the working hypothesis of the thesis, namely whether arbitration agreements and arbitral awards may have any effect upon false third parties depends on the degree of the association between the genuine and the false third parties, in terms of substantive liability and interests.

Second, the effect of arbitration agreements upon third parties

To date, the legal discourse and arbitral practice have opted for two different viewpoints on this matter. The first suggests that arbitration agreements cannot have any impact whatsoever on any person who has not clearly consented to arbitration, as this consent is evidenced by their signature. According to this view, non-signatory parties are total strangers to an arbitration agreement and the ensuing proceedings between the signatories.

The second stance proposes that arbitration agreements, as substantive contracts, may be “extended”, under certain circumstances, even to persons that have not signed them. This is the view taken by what is called in the thesis “extension doctrines”, the most prominent of which are the “group of companies” doctrine in the European continent and the “equitable estoppel” in the USA. According to extension doctrines, signature should be distinguished from consent to arbitrate. Thus, it is possible under certain conditions for non-signatories to enter into an arbitration agreement, notwithstanding the fact that they have failed to sign it. In the context of “group of companies” doctrine, in particular, it has been argued that the existence of consent of a non-signatory party to arbitrate may even be presumed.

As will be demonstrated, neither of the above mentioned views succeed in giving satisfactory answers to the problem of arbitration agreements and third parties. This is largely because they both take a strict contractual approach to the issue, focusing exclusively on the contractual characteristics of arbitration agreements. In this contractual context, the main question is whether a non-signatory, rather than a *stricto sensu* third party can be contractually bound by an arbitration agreement. As will be explained, not even the extension doctrines challenge “consent” as an indispensable requirement for the participation of the non-signatory party to the arbitration between

the signatories. The core argument of the extension doctrines is merely that signature on an arbitration agreement is not the only means to assert consent to arbitrate.

Effectively, the whole discussion on arbitration agreement and third parties, until now, is limited to issues of “signature” and “evidence of consent”. In other words, from the viewpoint of the prevailing contractual approach, the debate on arbitration and third parties relates only to the boundaries of the arbitration agreement as a substantive contract. Thus, this discussion is mainly related to contract law and principles of contract interpretation, rather than arbitration law. In the context of the prevailing contractual approach, arbitration agreements are exclusively viewed as ordinary substantive contracts.

The thesis examines the contractual approach in detail and at the end, demonstrates its theoretical and practical limitations. The attention is particularly focused on the extension doctrines the conceptual premises of which, the thesis argues, are undermined by a conceptual contradiction: although they adhere to the requirement of consent, they violate fundamental principles of contract law and contract interpretation as they effectively establish presumptions for the existence of the intention of the non-signatories to arbitrate.

If arbitration agreements are exclusively viewed as ordinary substantive contracts, any discussion on arbitration agreements and third parties is necessarily rendered superfluous or contradictory in terms. From a strict contractual viewpoint, an arbitration agreement, as any other ordinary contract, have inherent constraints: they bind only those persons that have clearly consented thereto. In such terms, consent constitutes the indispensable requirement for a person to be bound by an agreement, and can neither be substituted nor presumed. In other words, in this contractual context there is no room for third parties to come into play at all.

By contrast, the thesis argues that a jurisdictional approach to the issue of arbitration and third parties should be adopted. Arbitration agreements have important jurisdictional effects. Arbitration law is not, and should not be viewed merely as an advanced version of contract law. Arbitration agreements differ from ordinary contracts in that they provide tribunals with significant jurisdictional powers. These jurisdictional powers are necessary for the tribunal to achieve their primary goal, namely the authentic *determination of the dispute at hand*. Focusing exclusively on the contractual nature of arbitration agreements obscures the real issue, which is

whether arbitration agreements may have any *jurisdictional implications vis-à-vis third parties*.

The thesis does not dismiss the relevance of contractual foundations of arbitration. However, it does argue that the issue of third parties in arbitration can be better addressed, if the focus is shifted from the contractual nature of arbitration agreements to their *jurisdictional effects*. In particular, it is suggested that the focus should be shifted from whether arbitration agreements as ordinary contracts may bind third parties to whether arbitral tribunals may assume jurisdiction over third parties and if so, under what circumstances. In this jurisdictional context, the *dispute* pending before the tribunal rather than the arbitration contract is the key factor to determine the boundaries of the jurisdiction of the tribunal.

In the light of this jurisdictional approach, the thesis focuses on the dispute and on any implications this dispute may have for third parties, rather than on the requirement of consent to arbitration agreements. On this premise, the thesis examines whether a tribunal may assume jurisdiction over parties not bound by an arbitration agreement and under which circumstances this can be feasible.

More specifically, the concept of *effective arbitral jurisdiction* is introduced, which comes as a necessary corollary of the jurisdictional approach. According to the concept of effective arbitral jurisdiction, a tribunal should be able to assume as much jurisdiction as is necessary for a tribunal to achieve its main goal, namely the determination of the pending dispute. Therefore, it is argued that a tribunal in order to assert its jurisdiction should not only examine the contractual scope of an arbitration agreement but it should also take into account the full implications of the pending dispute. This is particularly necessary when third parties are integral part of the dispute pending before the tribunal. Indeed, as will be demonstrated, when the pending dispute necessarily implicates third parties, arbitration agreements may produce jurisdictional effects *that stretch beyond their contractual boundaries and the parties thereto*. In fact, it is argued that arbitration agreements may have *collateral jurisdictional effects on third parties*.

Since tribunals should be able to assume as much jurisdiction as is necessary for them to resolve the pending dispute and since arbitration agreements may stretch beyond their contractual origins, the thesis concludes that it is possible for a tribunal to assume *extra-contractual jurisdiction*. As will explained, extra-contractual jurisdiction can be achieved in practice by the application of third-party mechanisms,

which constitute the procedural means for a tribunal to assume jurisdiction over a third party by way of joinder, interpleading, intervention or consolidation.

To prevent misinterpretation, this argument is delimited by a caveat: it is only in *extremely exceptional circumstances* and *with particular caution* that a tribunal should assume extra-contractual jurisdiction. Furthermore, the thesis by reference to national procedural systems, determines the exceptional character of extra-contractual jurisdiction and third-party mechanisms. Nevertheless, the principle of the argument is established: extra-contractual jurisdiction is not incompatible with arbitration, and therefore tribunals *may* assume jurisdiction over third parties.

Once the principle is set out, the thesis addresses some equally important issues: first, it examines whether the tribunal *should* assume extra-contractual jurisdiction and apply third-party mechanisms. Here, the thesis embarks on a policy-oriented analysis, which demonstrates that third-party mechanisms are necessary in the context of international arbitration. As will be shown, there are important policy reasons suggesting that arbitration despite its contractual basis should not remain a closed system, reserved only for parties that have agreed to an arbitration agreement. Instead it should be a dispute resolution system, which -under particular circumstances- should be open to pertinent third parties. A procedural system of communication between the genuine and third parties should be established in arbitration.

Secondly, it explores *the rationale behind third-party mechanisms* as procedural tools, and looks into the way they operate and the purposes they serve. The exploration of these questions takes place against a comparative background of several national litigation and regional procedural systems. Again here, it is suggested that the key-element for the operation of third-party mechanisms is the pending dispute and its implications for the third parties.

In particular, it will be shown that the extent to which a third party may participate in the proceedings between two original parties is directly relevant to the *degree of association between the third party and one of the original parties, in terms of substantive liability and interests*. Here, the rule is: the closer the substantive association between the original and the third party, the more effective third-party mechanisms are provided by procedural systems. More specifically, third-party mechanisms of *compulsory character* are provided when the third party and the original parties are *strongly associated in substantive terms*, whereas third-party mechanisms of *permissive character* are provided when the third party and the

original parties are *contractually interrelated but not strongly associated* in substantive terms.

The findings of this analysis are then tested on arbitration against the background of the principles prevailing in arbitration and, in particular, the *principle of procedural party autonomy*. The question here is whether extra-contractual jurisdiction and third-party mechanisms are compatible with the freedom of the parties to determine the forum and the procedures for the resolution of their disputes in the way it best serves their commercial interests (procedural party autonomy). It is argued that in the majority of the cases the principle of procedural party autonomy should prevail, rendering third-party mechanisms inapplicable to arbitration. As will be demonstrated, the right of the parties to opt for a scheme of several bilateral proceedings rather than third-party mechanisms should be observed, even if this scheme would result to the jurisdictional fragmentation of the multiparty relationship. Jurisdictional fragmentation, despite its unfavourable consequences, should be accepted as a legitimate collateral inconvenience.

However, as already indicated, the thesis argues that there are exceptional circumstances where third-party mechanisms should take precedence over procedural party autonomy. It is suggested that this should happen whenever the third parties are *strongly interrelated* with the parties to the arbitration, so that third and genuine parties are *co-liable or co-holders of rights and duties*. As will be demonstrated, in such a case the several parties (third and genuine) constitute *an inseparable unit in terms of jurisdiction*. This jurisdictional unit, due to the strong substantive interrelations of the several parties, should not be separated and, thus, should prevail over the scheme of bilateral dispute resolution agreements of the several parties. Therefore, it is concluded that the tribunal should be able to assume jurisdiction over the whole jurisdictional unit, consisting of the several genuine and false third parties.

Third, the effect of arbitration awards upon third parties

This issue has been relatively overlooked since the interest of academic doctrine and jurisprudence has focused principally on the effect of arbitration agreements rather than the effect of arbitral awards upon third parties. The sole viewpoint here is that arbitral awards should be equated to national decisions. Accordingly, the question of whether the arbitration award may have any sort of impact upon third parties depends on the national provisions regarding *res judicata*. As will be shown, national

provisions invariably provide that the *res judicata* effect is strictly limited to the persons taking part in the proceedings. The only persons, apart from the parties to the proceedings, which are bound by the *res judicata* effect of a national judgment and, therefore, an arbitral award are third parties with *identical* interests with the parties to the proceedings, namely the *privies* to the parties to the proceedings.

The thesis challenges the prevailing view on the grounds that it overlooks the differences, in nature and purpose, between international awards and national decisions. Most importantly though, the prevailing view fails to accommodate the systemic problems arising in international arbitration with regard to multiparty commercial relationships.

Instead, the thesis argues for a *third-party effect of arbitral awards* specially designed for the needs of international arbitration. The case is made for the application of an arbitral effect different from that of *res judicata*, both in terms of quality and intensity, which is nevertheless conclusive.

Accordingly, it is argued that arbitral awards should be able to affect a wider circle of third parties than the one affected by national judgments. A wider arbitral effect would compensate for the lack of unification mechanisms at an earlier stage analogous to the mechanism provided in the context of litigation. It is suggested, in particular, that arbitral awards should somehow affect the false third parties rather than just the privies to the parties in the proceedings.

However, it is noted that the substantive links between the privies and the original parties to the proceedings are stronger than those between the false third parties and the original parties. Therefore, it is argued that the third-party arbitral effect vis-à-vis false third parties should be different and certainly less drastic than the *res judicata* effect upon privies. This suggestion accords to the overarching argument of work here, namely that *the procedural relationships between several parties must correlate to their relationships in substantive terms*.

More specifically, it is submitted that arbitral awards should have both conclusive and preclusive effects on false third parties. Thus, the preclusive effect of the award between two parties will prevent the re-litigation of any factual and legal issue that might arise again in the second set of proceedings between a false third party and one of the parties in the first set of proceedings. In addition, the conclusive effect of the award between two parties will provide the logical and legal basis for the second forum, be that a national court or an arbitral tribunal, to reach a decision in

accordance with the determination of the first award. Applied in this way, the combination of preclusive and conclusive effects of an arbitral award will harmonise the several sets of proceedings, in the context of a multiparty relationship, and it will ensure that any conflicting awards are avoided.

Despite its conclusive and preclusive consequences, the third-party arbitral effect suggested here is less effective than the *res judicata* effect. The award will merely *affect rather than bind* a false third party, and, therefore, any issues in terms of due process will not arise. The award given in proceedings between the two genuine parties will not be able to be enforced by or against the false third parties. Thus, this third-party effect will not pre-empt rights or duties of the third party. A second trial will still be indispensable for the claims of the third party to be determined.

RESEARCH METHODOLOGY

The basic methods employed in this study were research and qualitative analysis of primary and secondary legal sources, including national and international laws and rules, case law of national courts and arbitral tribunals, and academic treatises.

More specifically, as far as arbitration rules are concerned, the rules of all the major arbitration institutions are examined. Attention, of course, is particularly focused on the United Nations Convention on Recognition and Enforcement of Foreign Arbitral Awards of 1958 (the New York Convention), the international arbitration treaty that has been enjoying an unprecedented success, and has been immensely influential to the development of arbitration doctrine and practice.

In terms of national jurisdictions, the research takes an international comparative viewpoint. The legislation and case law of different countries are reviewed, although emphasis is especially placed on England, the USA, France, and to a lesser extent on Switzerland, Germany and the European Union. The selection of the above jurisdictions was mainly made for two reasons. First, it provides equilibrium between common and civil law legal traditions. Second, it covers almost all the major arbitration centres with advanced arbitration laws and procedural systems.

The following notes should also be made with regard to the methodological approach of the thesis:

First, as already indicated, despite the fact that the literature on “third parties in arbitration” is extensive, the discussion is still largely open. Additionally, regulation

on the topic is lacking in a national, regional or international level. Accordingly, the analysis performed here is policy orientated, whereas the final suggestions go beyond black letter law.

Secondly, the analysis on arbitration agreements draws to some extent on material regarding jurisdiction agreements. Arbitration and jurisdiction are very similar, if not identical, in nature, while they also have the same objective. In particular, they are both of contractual origins and they both serve procedural party autonomy. Procedural party autonomy provides the parties with the ability to choose in advance the forum that suits them best, instead of having their disputes resolved by the default forum, which in many cases is difficult to predict. Arbitration and jurisdiction agreements give effect to procedural party autonomy and, thus, constitute fundamental tools for commercial parties to establish an effective dispute resolution policy. Therefore, case law on jurisdiction agreements is occasionally used to support, by analogy, suggestions regarding arbitration agreements.

Similarly, part of the research focuses on national and regional civil procedural systems. It is true that arbitration is in many respects a very different adjudicatory system from litigation, and an arbitral tribunal will normally try the case differently from a national court. Nevertheless, both arbitral tribunals and national courts are, in principal, equal adjudicatory fora vested with the same power: jurisdiction to determine the dispute and issue an authoritative binding decision. Therefore, in jurisdictional terms, national courts and arbitral tribunals perform a very similar function.

Accordingly, the thesis makes an in-depth comparative analysis of national litigation systems with regard to the participation of third parties in court proceedings. The aim of this comparative study is to reveal the rationale behind third-party mechanisms in dispute resolution systems in general. The outcome of this analysis is used as a policy guideline in order for the thesis to determine the right impact of arbitration agreements and awards upon third parties.

It should be highlighted that the thesis merely seeks guidance from the study of litigation procedural systems to arbitration. It does not suggest the *ad hoc* application of litigation systems to arbitration. Due attention is always paid to the existing differences between the two dispute resolution systems.

STRUCTURE OF THE THESIS

The thesis is divided into three parts.

Part I consists of two chapters and focuses on the notion of third parties and false third parties in particular. Chapter 1 looks into some particular types of parties, whose status in relation to arbitration agreements is not clear. This is in particular the case for a principal, when an arbitration agreement is concluded by an agent; an assignee, after the assignment of an arbitration agreement; a consignee in a bill of lading containing an arbitration agreement; a successor in a contract containing an arbitration agreement. It is argued that, although they are some times taken as third parties, the above persons should be considered *genuine parties* rather than third parties, because they will be contractually bound by an arbitration agreements by reference to rules of contract law.

Chapter 2 then focuses on “false third parties”, which *ratione personae* define the scope of this study. Here the attention is focused on the different types interests of “false third parties”. Thus, false third parties are distinguished into two groups on the basis of the difference in the degree of association between the genuine and the false third parties, in terms of contractual interests and liability. The chapter examines each group in detail and presents some typical examples of false third parties, which are then used throughout the thesis as case studies.

Part II consists of four chapters, dealing in detail with the prevailing contractual approach to the issue of arbitration and third parties. Chapter 3 explains the role of consent in this contractual approach and gives a brief overview of the existing arbitration laws and rules relating to third-party mechanisms. Chapter 4 and 5 explore the two most important extension doctrines: the doctrine of “Equitable Estoppel” developed in USA, and the Continental doctrine of “Group of Companies”. Chapter 6 further discusses the extension doctrines adopting a more critical stance. This chapter highlights the conceptual and practical limitations of the extension doctrines and of the contractual approach in general. The discussion in Chapter 6 will demonstrate that a different approach to the issue of arbitration and third parties needs to be adopted: the jurisdictional approach that will be presented in Part III.

Part III is the largest part. It consists of six chapters and it puts forward the main suggestion of the thesis: the substitution of the contractual with a jurisdictional approach to the issue of arbitration and third parties. Chapter 7 presents the

conceptual premises of the suggested *jurisdictional approach* and introduces the concept of *effective arbitral jurisdiction*, according to which a tribunal should be able to assume as much jurisdiction as is necessary for the tribunal to determine the pending dispute. Here, particular attention is focused on the role of the “dispute” for the determination of the jurisdiction of the tribunal. It is argued that whenever the dispute has jurisdictional implications for third parties, arbitral tribunals may assume extra-contractual jurisdiction over third parties and apply third-party mechanisms.

While Chapter 7 establishes the principle that a tribunal *may* assume extra-contractual jurisdiction, Chapter 8 addresses some equally important issues: first, it examines whether the tribunal *should* assume extra-contractual jurisdiction and apply third party mechanisms, and secondly, it explores *the rationale behind third-party mechanisms in general*. The exploration of these questions takes place against a comparative background of several national litigation and regional procedural systems, where various third-party mechanisms such as joinder, consolidation, intervention, are examined in detail under the light of national case law.

The findings on the rationale behind third-party mechanisms as procedural tools is applied in the next two chapters to arbitration against the backdrop of the particular principles prevailing in arbitration and, in particular, the principle of procedural party autonomy. More specifically, Chapter 9 shows that in the majority of the cases the principle of procedural party autonomy should prevail, rendering third-party mechanisms inapplicable to arbitration. Jurisdictional fragmentation, despite its unfavourable consequences, should be accepted as a legitimate repercussion of procedural party autonomy.

However, Chapter 10 argues that there are exceptional circumstances where third-party mechanisms should take precedence over procedural party autonomy. It is suggested that this should happen whenever the third parties are strongly interrelated with the parties to the arbitration, so that third and genuine parties are *co-liable or co-holders of rights and duties*.

Chapter 11 makes the final remarks on the jurisdictional approach and discusses its practical relevance and advantages over the contractual approach, whereas in Chapter 12 the attention is shifted from the arbitration agreements to the arbitral awards. In particular, the chapter examines first the effects that arbitral awards may have on third parties and second the legal basis of the arbitral effect at an international level.

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PART I: PARTIES TO ARBITRATION AGREEMENTS

The aim of Part I is to define the notion of false third parties and delimitate the group of persons that are relevant for the discussion on arbitration and third parties and, therefore, for the purposes of this study.

Chapter 1 distinguishes the group of false third parties from that of genuine parties to arbitration agreements. The focus here is on particular types of persons whose status in relation to arbitration agreements is not clear. This is, for example, the case with a principal, whenever an agent concludes an arbitration agreement, an assignee, after the assignment of an arbitration agreement, a consignee in a bill of lading containing an arbitration agreement and a successor in a contract containing an arbitration agreement. These types of persons are sometimes regarded as ‘third parties’. However, the thesis revisits this view, arguing that all persons, such as the above, who are bound by an arbitration agreement by reference to general principles of contract law should be regarded as genuine rather than third parties to an arbitration agreement. In effect, the question of which parties are contractually bound by an arbitration contract is a matter that mainly relates to contract law, and, therefore, it falls outside of the scope of this work. Here, the only question pertinent to arbitration law is whether *separate consent to arbitrate is required* for the above types of persons to become bound by the arbitration agreement included in a substantive contract, or general consent to the latter as a whole would suffice. Chapter 1 look into this issue in the light of the principle of separability and the principle of autonomy of arbitration agreements.

Chapter 2 differentiates the notion of false third parties from that of third parties in general. Strictly speaking, every person not bound by an arbitration agreement is a third party. However, not all third parties would be relevant in an arbitration between the two original parties. Only third parties that have a legal or financial *interest* in the dispute pending before the tribunal may be relevant, namely the “false third parties”. Thus, based on the criterion of interest, Chapter 2 explores in detail the notion of “false third parties”, focusing on their association with the genuine parties, in terms of contractual rights, duties and liabilities.

CHAPTER 1: GENUINE PARTIES TO ARBITRATION AGREEMENTS- NOTION AND RELEVANCE TO THE THESIS	20
1.1 Agency - representation	21
1.2. Assignment	22
1.3 Succession - novation	24
1.4 Specific consent to arbitrate and genuine parties to arbitration agreements.	24

CHAPTER 1: GENUINE PARTIES TO ARBITRATION AGREEMENTS- NOTION AND RELEVANCE TO THE THESIS

Arbitration agreements must meet specific requirements of formal and substantive validity. While the formal requirements are determined by specific arbitration provisions,¹ the substantive requirements of validity of arbitration agreements are governed by ordinary principles of contract law.² As a rule, any individual or corporate body validly entering into an arbitration agreement becomes a party thereto.³ In effect, the question of whether a person is a party to an arbitration agreement is relevant to principles of contract rather than arbitration law. Therefore, it would be fair to argue that arbitration law becomes pertinent only after contract law rules have irrevocably determined which parties are contractually bound by an arbitration agreement.

Naturally, thus, the discussion about which persons are bound by an arbitration agreement in accordance with principles of contract law is only peripheral to this study, which principally focuses on jurisdictional issues related to arbitration rather than contract law. Although the issue of substantive validity of arbitration agreements and the requirement of consent, in particular, are touched upon in many chapters, the scope of the thesis goes beyond them.

¹ For example United Nations Convention on Recognition and Enforcement of Foreign Arbitral Awards, at New York, 1958 (hereafter NY Convention) Art.II(2), or English Arbitration Act 1996 (hereafter EAA) s.5, UNCITRAL Model Law on International Commercial Arbitration (hereafter Model Law) art.7(2) etc.

² J.Lew, L.Mistelis and S.Kroell, *Comparative International Commercial Arbitration*, (Kluwer Law International 2003), para 7-34 et seq; G.A. Born, *International Commercial Arbitration*, (Kluwer Law International 2nd ed. 2001), chapter 3; Williston, *On Contracts*, (4th ed), ed. R. Lord, (WestGroup 2001) para 57:1.

³ Russell, *On Arbitration*, D. Sutton, J. Gill, M. Gearing (23rd ed. Sweet & Maxwell London 2007), para 3-002.

Nonetheless, it would be useful to look briefly into some particular types of parties, whose status in relation to arbitration agreements is not clear. This is in particular the case for a

- Principal, when an arbitration agreement is concluded by an agent
- Assignee, after the assignment of an arbitration agreement
- Consignee in a bill of lading containing an arbitration agreement
- Successor in a contract containing an arbitration agreement

The above types of persons are sometimes incorrectly regarded as ‘third parties’. However, as this section shows a principal, an assignee, a consignee and a successor should be considered *genuine* rather than *third parties* to arbitration agreements, since they are contractually bound by the arbitration agreements by reference to rules of contract law. Here, the term “genuine party” equally applies to persons who have not personally concluded an arbitration agreement, but who nevertheless are bound by it in accordance with general principles of contract law. More specifically.

1.1 AGENCY - REPRESENTATION

Here the position is reasonably straightforward. It is a well-established principle in the theory of contract law that the person in whose name and on whose behalf the contract was made is bound by all the rights and obligations deriving from this contract.⁴ An agent is not ordinarily liable under the contract he executes on behalf of his principal, so long as his agency is disclosed.⁵ This fundamental principle of agency will equally apply to arbitration agreements. As is generally accepted both by legal discourse and case law, it is the principal rather than the agent who is entitled to enforce an agreement to arbitrate by referring the dispute to arbitration in his own name.⁶ It is clear, thus, that the principal becomes the

⁴ Bowstead and Reynolds, *On Agency*, 17th ed. (Sweet & Maxwell London 2001), p. 67.

⁵ The agent will be personally liable only in case it has undertaken an independent duty, see *Westmoreland v Sadoux*, 299 F.3d 462 (5th Cir. 2002); *Interbras Cayman Co. v Orient Victory Shipping Co., S.A.*, 663 F.2d 4, 6-7 (2nd Cir. 1981); *A/S Custodia*, 503 F.2d at 320; *Carl Fisser and Martha Fisser v International Bank*, F.2d 231 (2nd Cir. 1960) at 233-38; *Keystone Shipping Co. v Textport Oil Co.* 782 F.Supp. 28, (NYDC 1992) at 31-32.

⁶ P. Fouchard, E. Galliard and B. Goldman, *On International Commercial Arbitration*, E. Gaillard and J. Savage (eds.) (Kluwer Law International 1999), para. 498; M. Mustill and S. Boyd, *Commercial Arbitration*, (2nd ed. Butterworths London-Edinburgh 1989 and 2001 Companion) p. 136; Domke, *On Commercial Arbitration*, (NY 1993) p.125.; Williston, *supra* n. 2, para 57:19.

For case law in the US see *Berlage Co. v Littlejohn & Co.*, 20 App Div 2d 697, 698, 247 NYS2d 58, 60, affd 15 NY2d 530, 254 NY2d 122, 202 NE 2d 566 (1964); *Rieger v Elco Coat Co.*, 34Misc 2d 359, 228 NYS2d 242 (1962); *David v Merrill Lynch, Pierce, Fenner and Smith, Inc.*, 440 N.W.2d 269 (N.D. 1989); *Westmoreland v Sadoux*, 299 F.3d 462 (5th Cir. 2002); *Merrill Lynch Inv.*

genuine party to the arbitration agreement from the time this agreement is concluded, while the agent is in essence a third party thereto.

1.2. ASSIGNMENT

Although was disputed for some time, it is generally accepted nowadays that arbitration agreements can be transferred by way of assignment.⁷ Thus, after the assignment of the main contract including the arbitration agreement is completed, the assignee is entitled to enforce the arbitration agreement *on its own name* and *in its own right*. In other words, the assignee becomes a *genuine party* to the arbitration agreement. This is the view taken by the courts in several countries. This is for example the case in England,⁸ the USA,⁹ France,¹⁰ Switzerland¹¹ and other jurisdictions.¹²

Managers v Optibase, Ltd 337 F.3d 125 (2nd Cir 2003); *Contra Pritzker v Merrill Lynch, Pierce, Fenner & Smith, Inc.* 7 F.3d 1110 (3rd Cir 1993) holding that not only the principal was bound under terms of a valid arbitration clause but also its agents, employees, and representatives.

In France it also is accepted that the principal rather than the agent is bound by an arbitration agreement, see Cass. 2e civ., Oct. 14, 1987, *Ampafrance v. Wasteels*, 1988 Rev. Arb. 288, with note J.-L. Goutal.

The same is accepted in arbitral case law: ICC award case no 6519 of 1991, 118 (1991) *J.D.I (Clunet)* 1065.

In England, see *Charles M Willie v Ocean Laser Shipping* [1999] 1 Lloyd's Re. 225, for an example of the relationship between agent and principal in the context of arbitration.

⁷ See, in general, D. Girsberger and C. Hausmaninger, "Assignment of Rights and Agreement to Arbitrate", (1992) 8 Arb Int'l 121; S. Jagusch and A. Sinclair, "The Impact of Third Parties on International Arbitration –Issues of Assignment" in L.Mistelis and J.Lew (eds), *Pervasive Problems in International Arbitration*, (Kluwer Law International 2006) Chapter 15; see also VV Veeder "Towards a possible solution: Limitation, Interest and Assignment in London and Paris", in A. van den Berg (ed) *Planning Efficient Arbitration Proceedings: The Law Applicable to Arbitration*, (ICCA Congress Series No.7, Kluwer Law Arbitration International 1996) p. 268 et seq.

⁸ At one time English courts considered arbitration agreements as personal covenants, rejecting the possibility of their assignment: *Cottage Club Estates v Woodside Estates*, [1928] 2KB 463. This position changed in *Aspell v Seymour* [1929] W. N. 152 and *Shayler v Woolf*, [1946] Ch 320, where courts recognized arbitration agreement's assignability. This was further accepted in *Montedipe v JTP-Ro Jugotanker (The Jordan Nicolov)*, [1990] 2 Lloyd's Rep. 11 and in *Schiffahrtsgesellschaft Dedlev Von Appen v Voest Apline Trading*, [1997] 2Lloyd's Rep 279; however, see the recent *The London Steamship Owners v Bombay Trading (The Felicie)* [1990] 2 Lloyd's Rep. 21, where Phillips J expressed doubts about the assignability of arbitration agreements: "I am driven to the conclusion that there is no wholly satisfactory explanation for the basis upon which [...] by assignment *inter partes* the transferee acquires the right and obligation to arbitrate in his own name". Note that under English law (s.82(2) Arbitration Act) the assignee is considered to be a person "claiming under or through a party to the [arbitration] agreement" (although in essence the assignee claims *instead (in place of)* rather than *under* or *through* the assignor); see also R. Merkin, *Arbitration Law*, (Lloyd's London 1991), para.1.37 and 2.33; Mustill and Boyd, *supra* n.6, p.137 et seq.

⁹ *Star-Kist Foods v Diakian Hope*, 423 F.Supp.1220 (C.D.Ca 1976); *Asset Allocation and Management v Western Employer*, 892 F.2d 566 (7th Cir.1989); *Asset Allocation and Management v Western Employer*, 892 F.2d 566 (7th Cir.1989).

¹⁰ Cour de cassation, 5 January 1999, *Banque Worms v Bellot*, (2000) Rev. Arb. 85, with note Mayer; Cour de cassation, 8 February 2000, *Soc. Taurus Films v les Films du Jeudi*, (2000) Rev. Arb. 280, with note Gautier: « la clause d'arbitrage international s'impose à toute partie venant aux droits de

However, unlike the principal, the assignee becomes a genuine party to an arbitration agreement only after the assignment of the arbitration agreement is completed rather than from the time of its conclusion. It is the assignor who is the original real party to the arbitration agreement. However, according to the most convincing view, once the assignment is completed, the assignor ceases to be a party to an arbitration agreement,¹³ since he also ceases to be a party to the substantive contract containing the arbitration agreement.¹⁴

The same applies to the case of an arbitration agreement contained in a bill of lading. Here, a consignee, according to the prevailing view, is considered an assignee of the shipper.¹⁵ Accordingly, the former by holding the bill of lading becomes the new genuine party to the arbitration agreement incorporated thereto, taking the place of the shipper.

l'un des contractants) [...] la convention d'arbitrage stipulée dans le mandat [...] devait recevoir application à l'égard des mandataires substitués»; Cour d'appel de Paris, 28 January 1988, (1988) *Rev Arb* 565; Cour d'appel de Paris, 25 November 1999, *SA Burkinabe des ciments et matériaux v soc. Des ciments d'Abidjan*, (2001) *Rev Arb* 165; see also Delebecque, "La transmission de la clause compromissoire", 1991 *Rev. Arb.* 19, 26 arguing that arbitration agreements are incidental to the substantial claims.

¹¹ See cases of Swiss Tribunal Fédéral: *Muller v Bossard*, (1977) 103 II AFT 75, and *Clear Star v Centromor*, (1991) 8(2) J Int Arb 21.

¹² The same is accepted in Sweden, see for example, Sweden Supreme Court of Sweden, Oct. 15 1997, *MS Emja Braack Shiffahrts v Wärtsilä Diesel Aktiebolag*, (1998) *Rev Arb* 431, with note Jarvin, and in Greece AΠ 176/1976, (1976) *NoB* 706; ΕφΑθ 4830/1977, (1978) *ΕΛΔ* 720; ΕφΑθ 1343/1995, (1998) *Δ* 473, and, Μαντακου, *Η Καταρτιση της Συμφωνίας Διαιτησίας στη Διεθνή Συναλλαγή*, (Αθήνα 1998), p. 260.

¹³ See *Read v Brown* (1889) LR 22 QBD 128; *The Jordan Nicolov*, *supra* n.8; See also Jagusch-Sinclair, *supra* n.7, para 15-22. However, there is US authority, holding that the assignor may still enforce the arbitration agreement against its original co-contractor, on the condition that the assignee would be the person entitled to any rights arising out of the award *American Renaissance Lines v Saxis*, 502 F2d 674 (CA2 1974). Cf also Lew-Mistelis-Kroell, *supra* n.2, par.7-57, arguing that the extent to which the assignor remains bound by the arbitration agreement is primarily an issue of interpreting the arbitration agreement.

¹⁴ It is the assignee, rather than the assignor or both jointly, that will be liable vis-à-vis its original co-contractor after the assignment. See *The Jordan Nicolov*, *supra* n.8, Hobhouse J: "The legal assignment extinguishes the legal cause of action of the assignor against the party liable so that the assignor cannot thereafter himself ask for an award against the party liable" and "...a joint award could not be right since on any view there was no joint right in the plaintiffs, ie the charterers and insurers; only one or the other could be entitled to an award".

¹⁵ Cf R. Goode, *Commercial Law*, 2nd ed. (Penguin 1995), p.1075: "...the consignee or indorsee becomes the statutory assignee of the shipper's rights under the carriage contract..." (referring to both Bills of lading Act 1855, s.1 and Carriage of Goods by Sea 1924, s.2). See Also Rémond-Gouilloud, "Des Clauses de Connaissances Maritimes Attribuant Compétence à une Juridiction étrangère; Essai de Démystification", (1995) *DMF* 339.

For the various theories regarding the legal nature of a consignee see Rodière, *Traité General de droit Maritime, Affrètement et Transport*, (1968) par 408; Rodière et du Pontavice, *Droit Maritime*, 11^e éd (Précis Dalloz 1991) par 359; Rémond-Gouilloud, *Droit Maritime*, 2^e éd (1993) par 610; note Goutal on *Mediterranean Shipping*, (1995) *Rev Arb*, at 624.

1.3 SUCCESSION - NOVATION¹⁶

Here the position is also relatively straightforward. Whenever a person succeeds either by law or by contract in the rights and obligations of another person, who is a party to an arbitration agreement, the former becomes the new party to that arbitration agreement.¹⁷ As in the case of assignment, here the original party cannot enforce the arbitration agreement, as he no longer has any status in the contractual relationship.¹⁸ Thus, a successor takes the place of the original party to the arbitration agreement and becomes a genuine party thereto.¹⁹

1.4 SPECIFIC CONSENT TO ARBITRATE AND GENUINE PARTIES TO ARBITRATION AGREEMENTS

Agency, assignment and succession are sometimes wrongfully considered as cases involving third parties.²⁰ However, as was explained, a principal, an assignee, a consignee and a successor are genuine parties to an arbitration agreement by reference to rules of contract law. These persons become parties to the substantive contract and, therefore, genuine parties to the arbitration agreement included therein. Thus, the question of whether these persons are entitled to take part to arbitration proceedings is effectively a matter of *consent* which will be exclusively determined by rules of contract law and general principles of contract interpretation. In this discussion, arbitration law is largely irrelevant.

In this discussion, the only question pertinent to arbitration law is whether *separate consent to arbitrate is required* for the above persons to be bound by the arbitration agreement in the main contract, or general consent to the main contract as a whole would suffice. Here, arbitration principles such as the principle of ‘separability’ or the principle of ‘autonomy of arbitration agreements’ will come into play. According to

¹⁶ Novation is a contract that transfers both rights and obligations from one of the original parties to a new party, whereas an assignment is a contract where the original party transfers only contractual rights.

¹⁷ See *Smith v Pearl Assurance Co Ltd*, [1939] 1 All ER 95; *Oakland Metal Co Ltd v D Benaim & Co Ltd*, [1953] 2 Lloyd’s Rep 192; *Socony Mobil Oil Co Ltd v West of England Ship Owners Mutual Insurance Association Ltd (The Padre Island)* [1984] 2 Lloyd’s Rep 408.

¹⁸ Mustill and Boyd, *supra* n.6 p. 137; the same B. Hanotiau, *Complex Arbitrations, Multiparty, Multi-contract, Multi-issue and Class Actions*, (Kluwer Law International 2005) para 35; The same has been held in arbitral case law: see for example ICC award no.7154 of 1993, 121 *JDI (Clunet)* 1059.

¹⁹ Cf *Damon Compania Naviera S.A. v Hapag-Lloyd International S.A. (The Blankenstein)*, [1985] 1 Lloyd’s Rep. 93; [1985] 1 W.L.R. 435.

²⁰ See for example, Mustill and Boyd, *supra* n.6, dealing with agency, succession and assignment under “Chapter 8: Arbitration and Third Parties”.

one view, evidence for *distinct intention to arbitrate* of a principal, an assignee etc is required rather than just evidence for general intention to be bound by the main contract.²¹ Otherwise, this view argues, the principles of separability and ‘autonomy of arbitration agreements’ would be violated, and the independent status of the arbitration agreement from the main contract would be undermined.

However, the prevailing view in arbitration is that *general consent* of the above persons to the whole transaction would be enough for them to become parties to the arbitration agreement too. This is especially the case with regard to assignment where the rule of “automatic transfer of the arbitration agreement” seems to prevail in the context of international transactions, in particular.²² According to this rule an

²¹ See for example Cour de cassation, 6 November 1990, *Fraser v Compagnie Euorpéene de Pétroles*, (1991) Rev Arb., p. 73, holding that:

“an arbitration clause remains subject to the principles of privity of contracts and cannot therefore circulate in a chain of contracts, unless the parties have expressly provided otherwise” (translation by the author)

The same was held by the Paris Cour d’appel, 22 March 1995, *SMABTP v Statinor*, (1997) Rev Arb., p.550 in the context of assignment; cf also Article 1989 of the French Civil Code that forbids the agent to bind the principle with an arbitration agreement unless there is express mandate for that:

“an agent may act only within the scope of its mandate, and the power to settle disputes does not confer a power to enter into arbitration agreements”. (“Le mandataire ne peut rien faire au delà de ce qui est porté dans son mandat; le pouvoir de transiger ne renferme pas celui de compromettre” note that in French “compromettre” means both “reach a settlement” and “agree to resort to arbitration”).

For the US see *Lachmar v Trunklin LNG*, 753 F 2d 8 (2d Cir 1985).

For arbitral case law, see the Award of the Foreign Trade Arbitration Commission of the USSR Chamber of Commerce and Industry, 9 July 1984, *All Union Foreign Trade Association (“Sojuzneftexport”) v Joc Oil Ltd*, (1993) XVIII YBCA, p. 92.

²² Lew Mistelis and Kroell, *supra* n.2, par. 7-52 and see also Jagusch and Sinclair, *supra* n. 7, para 15-50; cf. however, Girsberger- Hausmaninger, *supra* n.7, p.136, who argue that a uniform international substantive rule on this issue does not exist; see also Fouchard-Galliard-Goldman, *supra* n.6, par.707 *et seq.*, who argue that on the one hand the *express acceptance* of the assignee is required for the completion of the assignment, but on the other hand that this express acceptance should be presumed. In the context of agency, Fouchard Galliard and Goldman argue that a liberal approach should be taken so that a general authorization to the main contract would suffice for principal to be bound by the arbitration agreement signed by the principal, *supra* n.6, para 468.

In England, see *The Jordan Nicolov*, *supra* n.8, “...the assignee is bound by the arbitration clause in the sense that he cannot assert the assigned right without also accepting the obligation to arbitrate”.

In the US see for example the *Star-Kist Foods v Diakian Hope*, *supra* n.9; *Asset Allocation and Management v Western Employer*, *supra* n.9; contra *Lachmar v Trunkline*, 753 F.2d 8 (2d Cir.1985), on the basis that an arbitration agreement confers duties as well as rights, requiring the acceptance of the co-contractor. In Switzerland, for example, see the *Clear Star* case, *supra* n.11. In France, for example, see Cour de cassation, *Banque Worms v Bellot* and Cour d’appel de Paris, *SA Burkinabe des ciments et matériaux v soc. Des ciments d’ Abidjan*, *supra* n.10: «une cession de créance ou de contrat implique nécessairement la transmission par le cédant au cessionnaire du bénéfice de la clause compromissoire, laquelle est indissociable de l’économie du contrat initial»....(contra *Fraser v Compagnie européenne des Pétroles*, 6 November 1990, (1991) Rev Arb. p.73 where the Cour de cassation held that an arbitration agreement, contained in a contract between an intermediate seller and its buyer in a chain sale could not be enforced by former against the ultimate buyer who had not accepted whatsoever the arbitration clause); the same view in Delebecque, “La transmission de la Clause Compromissoire”. (1991) Rev Arb. p.25. In Sweden, for example, see *MS Emja Braack*

arbitration agreement, due to its subsidiary character is transferred automatically to an assignee alongside the substantive rights of the contract.²³ The rule of automatic assignment effectively means that no *specific consent of an assignee to arbitrate* is required. An assignee will be bound by an arbitration agreement automatically. Otherwise it would be possible for the assignee to escape an otherwise valid arbitration clause unilaterally by the mere fact of the assignment.²⁴ Similarly, no previous consent of a debtor to arbitrate with the specific assignee is required either. Therefore, a debtor cannot argue that it has agreed to arbitrate specifically with the assignor “but not with some outsider”.²⁵ The automatic transfer of an arbitration agreement can only be prevented if the latter has been concluded in view of a specific assignor (*intuitu personae*). However, arbitration agreements are in general considered not to be personal covenants (*intuitu personae*).²⁶

The rule of “automatic transfer of the arbitration agreement” applies equally to bills of lading. Although there is a view arguing that a consignee must be aware of the arbitration agreement and must specifically accept the arbitration agreement before he takes delivery of the goods,²⁷ the prevailing view dispenses with the prior consent

Shiffahrts v Wärtsilä Diesel Aktiebolag, *supra* n.12. In Greece, a decision of a court of first instance, ΠολΑθ 2690/1976, (1977) *NoB* 220, held *in obiter* that a notice to debtor rather than the consent of the debtor would suffice.

²³ The *intuitu personae* arbitration clause can either be provided expressly in the contract or be inferred from the factual circumstances surrounding the contract, see Fouchard Galliard and Goldman, *supra* n.6, para 720 et seq. An arbitration agreement could be *intuitu personae* for example when an arbitration agreement provides for a personal appointment of an arbitrator by the assignor, see Corbin, *On Contracts*, (1951 Supplement 1991) par.892. See also the US cases *Star-Kist Foods v Diakian Hope*, *supra* n.9; *Asset Allocation and Management v Western Employer*, *supra* n.9. See also the position taken by the Swiss Tribunal Fédéral in: *Muller v Bossard*, and *Clear Star*, *supra* n.11., which, in the context of assignment, reaffirmed the *ancillary* character of the arbitration agreement to the substantive rights and held that a conditional prohibition of the assignment of the substantive rights was also covering the arbitration agreement; in the same vein, Werner, “Jurisdiction of Arbitrators in Case of Assignment of an Arbitration Clause”, (1991) 8(2) *J Int Arb*, p.13. Cf also the *Shayler v Woolf*, *supra* n.8, by Lord Greene M.R “the arbitration clause also follows the assignment of the subject matter of the contract”.

²⁴ See the *MS Emja Braack Shiffahrts v Wärtsilä Diesel Aktiebolag*, *supra* n.12 and *Hosiery Mfg Corp v Golston*, (1924) 143 NE 779; 238 NY 2d 22; cf Girsberger and Hausmaninger, n.7, p.138.

²⁵ Mustill and Boyd, *supra* n.6, p.138.

²⁶ See *Shayler v Woolf*, *supra* n.8, at 324 and the *MS Emja Braack Shiffahrts v Wärtsilä Diesel Aktiebolag*, *supra* n.12; cf Lew, Mistelis and Kroell, *supra* n.2, par 7-53 and Jagusch – and Sinclair, *supra* n.7, para 15-14.

²⁷ See in the context of arbitration clauses Cour de cassation, *Mediterranean Shipping v GAFL assurance et autres*, 20 June 1995, (1995) *Rev Arb* 622, with note Goutal who criticizes the decision. and Cour de cassation, *The navire Stolt Osprey*, 29 November 1994, (1995) *DMF* 218, note Tassel. in the context of jurisdiction clauses. In the past, US courts have held, on different grounds, that arbitration agreements stipulated in a bill of lading are not opposable to the consignee. The argument was that these arbitration agreements were negated by US COGSA s.3(8), on the ground that they were unduly limiting the liability of the shipowner, eg *Indussa Corp. v SS Randborg*, 377 F.2d 200 (SC 1967). However, the US courts now take the opposite view, see the following note.

of the consignee.²⁸ Thus, arbitration agreements are transferred to the holder of the bill of lading automatically together with the substantive rights on the goods. Otherwise, the negotiability and commercial effectiveness of the bill of lading would be compromised.²⁹

It follows from the above that the principle of separability or “autonomy of arbitration agreement” does not create any theoretical difficulties to the automatic transfer of the arbitration agreement. In effect, an assignee, a consignee or a successor ‘gets into the shoes’ of the original party to the main contract *as a whole*. Therefore, the former assumes the contractual position of the latter in exactly the same terms, which of course include the arbitration clause. In all the above cases, the transfer of an arbitration agreement is mainly linked with the transfer of the substantive contract including the arbitration agreement and, therefore, it remains predominately a question of contract law. Accordingly, the thesis will not discuss the issue of ‘genuine parties’ to arbitration agreements any further. It will focus on the impact of arbitration upon persons not contractually bound by arbitration agreements. The following section defines the notion of ‘third parties’ and determines which particular groups of persons will be examined by the thesis.

²⁸ In the US, courts require only the *actual notice* of the consignee rather than its consent; see for example *Amoco Oil Co. v. M.T. Mary Ellen*, 529 F. Supp. 227 (S.D.N.Y. 1981); *Vimar Seguros y Reaseguros S.A v Sky Reefer*, 29 F.3d 727 (1994 U.S. App.); affirm. by 515 U.S. 528 (U.S. S.C. 1995) *Japan Sun Oil v M/V Maasdijk*, 864 F.Supp.561 (U.S. Dist. 1995); *Japan Sun Oil v M/V Maasdijk*, 864 F.Supp.561 (U.S. Dist. 1995).

In England see *The Rena K* [1978] 1 Lloyd's Rep. 545 *The Nerano* [1994] 2 Lloyd's Rep. 50, upheld [1996] 1 Lloyd's Rep. 1 (C.A.); *The Delos* [2001] 1 Lloyd's Rep. 703.

The same in Greece, (Ολ)ΑΠ 8/1996, (1997) ΕΕμπΔ 85; (Ολ)ΑΠ 236/1986, 17 ΕΕμπΔ 290; ΕφΘες 1602/1983, 25 ΕΕμπΔ 311.

The same view has been taken by the European Court of Justice (ECJ) in the context of jurisdiction clauses: 19 June 1984, C-71/1983, *Partenreederei Tilly Russ v Haven*, [1984] ECR 2417.

²⁹ See note Goutal on the *Mediterranean Shipping*, above note, at p.626. Cf also Rémond and Gouilloud, *supra* n.15.

CHAPTER 2: THE NOTION OF FALSE THIRD PARTIES

Chapter 2: The notion of False third parties	28
2.1 Different groups of false third parties	29
2.2 String construction contracts	32
2.3 Web-type construction contracts	41
2.4 Guarantees and other security agreements	43
2.5 Several companies with close corporate links: the case of the “group of companies” in particular.....	49
Conclusions of Part I	55

As already mentioned, not every third party falls under the scope of this work. The thesis focuses on “false third parties”, i.e. third parties with an interest in the dispute between two other persons bound by an arbitration agreement.

False third parties are typically found in the context of multiparty contractual relationships, which are jurisdictionally fragmented. Jurisdictional fragmentation occurs when several parties involved in a single commercial project conclude different bilateral dispute resolution agreements. Thus, a person participating in a multiparty commercial project may be left unable to participate in the arbitration proceedings between two other persons involved in the same project, if the former is not party to the arbitration agreement binding the latter. In other words, persons with an active role and a significant interest in a project might not be able to take part in the resolution of the dispute arising out of the project, the outcome of which might affect their own interests. These persons cannot take part in the determination of the dispute since they are not parties to the arbitration agreement, which has exclusively been concluded between two other persons (genuine parties). Nevertheless these persons are not strangers to the dispute between the genuine parties, as they are closely involved in the execution of the project from which the dispute arises. Hence, they can be named *false third parties*.

This chapter examines in detail the notion of false third parties. The analysis takes a substantive viewpoint, focusing on the contractual rights, duties and liabilities of the several parties involved the same commercial project. From this substantive perspective, the chapter distinguishes between two different groups of false third parties: those who share the same rights, duties and liabilities with the genuine parties

to the arbitration, and those who are merely contractually interrelated with them. It will be shown that the interests of the former group in the arbitration between the two genuine parties are stronger and, thus, more relevant than the interests of the latter group. Furthermore, the chapter looks into each of the two groups in detail and presents some typical examples of false third parties. These typical examples are used throughout the thesis as case studies in order to test and demonstrate its main arguments.

The emphasis on the substantive status of the parties is a key point for this work. As will be argued in Part III, there is a direct relevance between the substantive and the jurisdictional status of the several persons in a multiparty commercial relationship: the closer the several persons are associated in substantive terms the less likely is for them to be separated in terms of jurisdiction. Whenever several persons constitute a substantive unit, they should also be regarded as a jurisdictional unit, and, therefore, they should be subject to the jurisdiction of a single adjudicatory forum. Therefore, the findings on the interests of false third parties and their substantive association with genuine parties will provide the conceptual basis for the final suggestions of the thesis regarding the impact of arbitration on third parties. In fact, the analysis performed here provides the groundwork for the whole thesis.

2.1 DIFFERENT GROUPS OF FALSE THIRD PARTIES

Depending on how closely they are associated with the genuine parties, in terms of interests and liability, the false third parties may be distinguished in the following two groups:

The first group includes persons that are *strongly associated* with a genuine party to an arbitration agreement or arbitral proceedings, in terms of contractual interests and liability. Here, genuine and false third party will have *concurrent interests* in the pending dispute and the commercial project they are both involved in. In particular, genuine and false third party will usually be *co-liable* or *co-holders of rights or duties* (community of rights and liability). They will typically be *joint* or *joint and severally liable* vis-à-vis the other genuine party to the arbitration proceedings.¹ These two

¹ Joint or indivisible rights or obligations may occur in two cases. First, when the object of the obligation cannot be actually divided; this is the case, for example, when two persons undertake the same obligation with regard to the same property. Second, when the parties have expressly agreed to

types of liability, joint and joint and several, are similar in that in both cases the co-promisors are jointly rather than cumulatively liable, so that the performance of the obligation by one promisor will discharge all them.² It should be noted however, that the terms “joint” and “joint and several liability” have a very strict technical meaning which varies, sometimes significantly, from jurisdiction to jurisdiction. Thus, for the purposes of the thesis, which adopts an international viewpoint, reference to ‘joint’ or ‘joint and several’ liability should be understood as a reference to ‘co-liability’. Typical examples of this group are:

- Co-holders of rights in property³
- Partners in a legal entity⁴
- Persons involved in the making and transfer of the same negotiable instrument (e.g. promissory notes, bills of exchange, bonds etc).⁵

undertake an obligation jointly. In either case, each of the promisors is liable for the whole performance. For more details on joint obligations:

In England, see Halsbury’s, *Laws of England*, (Lexis Nexis Butterworths 2007), para 1080;

In the US, see Restatement (Second) Contracts, para 289;

In France see Bacache in Rép. Civ. Dalloz (2007), *Indivisibilité*, art.1217-1225; cf also French Code Civil art. 1217 « L’obligation est divisible ou indivisible selon qu’elle a pour objet ou une chose qui dans sa livraison, ou un fait qui dans l’exécution, est ou n’est pas susceptible de division, soit matérielle, soit intellectuelle ».

On the other hand, *joint and several liability* arises when two or more persons join in the same instrument in making a promise to the same person, and at the same time each of them individually makes the same promise to that same promisee. Joint and several liability is similar to joint liability in that the co-promisors are not cumulatively liable, so that the performance of the obligation by one promisor will discharge all them.

For more details on joint and several liability:

In England, see Halsbury’s, *ibid*, para. 1079.

In the US, see Restatement (Second) of Contracts, para 288.

In France, see Tourneau and Julien, in Rép. Civ. Dalloz (2007), *Solidarité* ; cf also Code Civil art. 1197 « l obligation est solidaire entre plusieurs créancier lorsque le titre donne expressément à chacun d’eux le droit de demander le paiement du total de la créance, et que la paiement fait à l’un d’eux libère le débiteur, encore que le bénéfice de l’obligation soit partageable et divisible entre les divers créanciers ».

² See Halsbury’s, *ibid*, para 1079.

³ For example, two purchasers of real property will joint and several obligors under the agreement of sale, see *Converse v James*, 89 Hawai’i 461, 974 P.2d 1051, (Hawai’i App. 1997).

In France a typical example of such type of liability will come from when several people share property rights, such as servitudes réelles (real servitude i.e. a burden imposed upon one estate in favor of another estate of another proprietor).

⁴ For example, in the US, section 15 of the Uniform Partnership Act provides that partners are liable jointly and severally for tort or breach of trust, but jointly on partnership contracts: see also *Bullis v Bear, Stearns & Co Inc*, 553 N.W.2d 599 (Iowa 1996).

In England see the Partnership Act 1890 s 9; The liability of the partners of a firm on contracts entered into by the firm is joint, not joint and several cf also Halsbury’s, *supra* n.1, para 1083.

⁵ For example, the maker, the acceptor or drawer or indorser of the same negotiable instrument.

In the US, see section 3-118(e) of the Uniform Commercial Code that provides that “unless the instrument otherwise specifies” two or more persons who sign commercial paper as maker, acceptor or drawer or indorser and as part of the same transaction are jointly and severally liable.

The second group includes persons that are contractually linked but not *strongly associated* with a genuine party to an arbitration agreement or arbitration proceedings, in terms of contractual interests and liability. Here, genuine and false third party will have related but not *concurrent interests* in the pending dispute and the commercial project they are both involved in. In particular, genuine and false third party will be contractually linked but they will not be sharing the same rights or duties. They will not be co-liaible vis-à-vis the other genuine party to the arbitration agreement and the proceedings. Either they will be *liable in the alternative* or *one of them only will be liable* vis-à-vis the other genuine party. Here, the contractual obligations of genuine and false third party relate to the same commercial project. However they will *assume distinct duties to deliver distinct performances*. In short, genuine and false third party will be “commercial partners” but not co-liaible or co-holders of the same rights and duties. Consequently, although contractually associated, the degree of their association, in terms of contractual interests and liability will be lesser than in the first group.

Typical examples of this group are:

- Several persons contractually linked by bilateral contracts with regard to the *same construction project*. Here, the several persons may be linked
 - Either, in several *string contractual relationships*, where for example an owner is contractually related with a contractor who in turn is contractually related with a subcontractor.⁶
 - Or, in *web type contractual relationships*, where an owner is contractually related an architect/engineer, a contractor and a financial institution regarding the same construction work.
- Several persons contractually linked in the context of *security agreements*. A typical example here is the contractual relationships between a creditor, a debtor and a guarantor.

In England, the makers of a promissory note may be liable on it either jointly, or jointly and severally, according to the tenor of the note; but the acceptors of a bill of exchange can only be liable jointly: see the Bills of Exchange Act 1882 ss 6(2), 85; *cf* Halsbury's, *supra* n.1, para 327.

⁶ String contractual relationships can also be found in the context of commercial transactions with regard to the same goods: the typical example here would be the consecutive transactions between the manufacturer, the wholesaler, the retailer and the consumer. Thus, any suggestion made by the thesis in connection to construction string contracts will be equally applicable by analogy to the case of string transactions between the manufacturer, the retailer and the consumer.

- Several *corporate entities with close corporate links*, as for example the links between the several companies belonging in the same group.

Arbitration agreements are very frequently used in the context of all the above types of contractual relationships that involve several parties. Naturally, thus, the question of whether, for example, a subcontractor will be bound or in some way affected by an arbitration agreement or arbitral proceedings between an owner and a contractor arises very often. The same question arises

In the context of web-type construction contracts: will a contractor, for example, be bound or affected by an arbitration agreement or proceedings between an owner and an architect?

In the context of security agreements: will a guarantor be bound or affected by an arbitration agreement or arbitral proceedings between a debtor and a creditor?

In the context of several companies with close corporate links: will a parent company be bound by an arbitration agreement or proceedings between a subsidiary and another party?

In more general terms, the question here would be whether a false third party (in the above scenarios: a subcontractor, a contractor, a guarantor or a parent company respectively) would be bound or in any way affected by an arbitration agreement or proceedings between the genuine parties?

These questions are directly relevant to arbitration law and they will be in the heart of the discussion in this study. However, the exploration of these questions from an arbitration viewpoint requires first an analysis of the substantive status of the several parties involved in a commercial multiparty relationship. This is the aim of the following sections.

2.2 STRING CONSTRUCTION CONTRACTS

Due to the increase in specialisation and technology in the construction industry, the completion of a construction work will invariably require the participation of more than two persons. In a typical construction project several different professionals may get involved: an owner, a contractor, a quantity surveyor, a civil or structural engineer, an architect, a project manager, a architectural or engineering consultants, several subcontractors (e.g. substructure subcontractor, superstructure subcontractor, mechanical and electrical subcontractor), suppliers, sureties and others.

The above persons will usually get linked in pairs by way of several bilateral agreements rather than a single multilateral one. Typically, the several bilateral agreements will take the form of a contractual chain: an owner will enter into a contract with a contractor, who in turn will enter into a contract with a subcontractor, who may then agree with a supplier or another subcontractor and so on.

The use of substantial subcontracts has become a general practice in construction industry nowadays. The proliferation of subcontracts in the last decades is due to the fact that contemporary construction industry becomes geographically dispersed and increasingly complex in terms of technology. Construction projects may require different types of skills, services and materials from different countries of the world. It is more economical for a contractor to employ local specialised subcontractors in view of a particular construction project each time than to keep permanently employed craftsmen in all of the necessary trades within each region of activity.⁷ The use of subcontracts is commercially suitable for an owner too. The latter only needs to enter into a single contract and obtain a single price for the whole work. In general, the use of several subcontracts is considered more efficient than one multilateral contract for the completion of the project. Complicated problems of multiplicity of contracts and liability, which would arise if the works were to be carried out by various contractors each separately employed by an owner, are avoided by the execution of several bilateral contracts.⁸

A subcontractor may either be selected by or agreed with an owner under nomination arrangements in the main contract itself (*nominated subcontractor*),⁹ or be left to the commercial discretion of the main contractor (*domestic subcontractor*).¹⁰ By getting the owner involved in the selection of a subcontractor, the main contractor seeks to minimise its own liability for defective work or other failures of the performance of the subcontractor. However, as is generally accepted, it is the main contractor that will be invariably liable under an express or implied obligation in the

⁷ J. Murdoch and W. Hughes, *Construction Contracts*, (3rd ed Spon Press 2000), para. 19.1.

⁸ Hudson's, *Building and Engineering Contracts*, (11th ed Sweet & Maxwell London 1995), para.13-022; see also F. Nicklisch, "Multi-Party Arbitration and Dispute Resolution in Major Industrial Projects" (1994) 11(4) *J. Int'l. Arb.*, p. 69 et seq.

⁹ Hudson's, *supra* n.8, para 13-002; I.N.D. Wallace, *Construction Contracts: Principles and Policies in Tort and Contract*, (Sweet & Maxwell London 1986), Ch. 21; Murdoch- Hughes, *supra* n. 7, para 20.1 et seq.

¹⁰ Murdoch- Hughes, *supra* n.7 para 19.4.

main contract for any default work performed by subcontractors.¹¹ Indeed, under the principle of “chain liability” the main contractor, whether or not personally in default, remains fully liable to the owner for any default of the sub-contractor.¹² The same principle, will in turn entitle the main contractor to hold a defaulting subcontractor responsible for his own damages.¹³

In general, it can be argued that the principle of chain liability sums up the delicate balance between the several contractual relationships in the case of string contracts: although contractually interrelated, the several bilateral contracts maintain a substantive degree of autonomy. This is evidenced in more detail by the following.

On the one hand, the *several string contracts are interrelated*. Thus, both the contract between an owner and a contractor and the one between a contractor and a subcontractor have the same subject matter: *construction works on the same project*. The construction work of the specific project is the common denominator of both contracts, as it constitutes the commercial cause underpinning both agreements. In essence, the subcontract is concluded in view and in the light of the main contract. Hence, the main contract and the subcontract very often contain cross-references, resulting to a ‘direct communication’ in contractual terms between the two agreements. This is achieved by various ways. For example, subcontracts frequently incorporate parts of the main contract by way of express reference thereto.¹⁴ Also, subcontracts are very often drafted on the same contractual pattern of the main contract, a practice called drafting on *back-to back terms*. Some institutions well known in the construction industry have issued standard forms of subcontracts to be used in tandem with the standard forms of contracts issued by the same institution. For example, the International Federation of Consulting Engineers (FIDIC) has issued the FIDIC (Red Book) Conditions of Subcontract to be used back-to-back with the provisions of the FIDIC (Red Book) Conditions of Construction Contracts.¹⁵

¹¹ Murdoch- Hughes, *supra* n.7, para 19.5.2.

¹² *Young & Marten Ltd. v McManus Childs Ltd*, [1969] 1 AC 454; Hudson’s, *supra* n.8, para 13-002 et seq.

¹³ Hudson’s, *idem*; Murdoch – Hughes, *supra* n.7, para 19.3.

¹⁴ Without incorporation the terms of the main contract would not apply to the subcontractor, even if the terms are well known to both the contractor and the subcontractor. Also, imprecise or generic references, such as “the sub-contractor shall be deemed to have notice of all the provisions of the main contract” will not have a full-scale incorporation effect. See Hudson’s, *supra* n. 8, para 13-100 et seq.

¹⁵ The FIDIC (Red Book) Conditions of Construction Contracts is widely used in international construction practice and has obtained an international acceptance in the construction industry. It provides an international norm or standard by which construction works and contracts are

Similarly the Federation of Civil Engineering Contractors (FCEC) has issued a standard form of subcontract for use on contracts based on the Conditions of Contracts issued by the Institution Civil Engineers (ICE).¹⁶

All these standard forms of subcontract are filled with express references to the corresponding standard forms of the main contract. For example, in the FIDIC conditions of subcontract:

- Sub-clause 4.1 provides for the duty of the contractor to provide the subcontractor with a copy of the main contract. Sub-clause 4.1 adds that the subcontractor shall be deemed to have full knowledge of the main contract (except details of the contractor's price)
- Sub-clause 4.2 provides that the subcontractor shall generally have all the obligations and liabilities of the contractor under the main contract in relation to the subcontract works. In particular it reads:

“save where the provisions of the Subcontract otherwise require, the Subcontractor shall so design (to the extent provided for by the subcontract), execute and complete the Subcontract Works and remedy any defects therein that no act or omission of his in relation thereto shall constitute cause or contribute to any breach by the Contractor of any of his obligations under the Main contract. The Subcontractor shall, save as aforesaid, assume and perform hereunder all the obligations and liabilities of the Contractor under the Main Contract in relation to the Subcontract Works”
- Subclause 7.provides that when the subcontractor is delayed in the execution of the subcontract works, he shall be entitled to extension of time for completion if the delay is due to any circumstances in regard to which the Contractor is entitled to receive an extension of his time for completion of the Main Work under the Main Contract
- Subclause 7.3 provides that the main contractor has to notify the subcontractor of all extensions of time obtained under the main contract, which affect the subcontract¹⁷

determined. Thus, even when it is not incorporated into a particular contract it is generally accepted as a point of reference in construction contracts and works.

¹⁶ See also the Joint Contracts Tribunals (JCT) standard conditions of subcontract issued for use on contracts based on Intermediate Form of Building Contracts (IFC) 98.

- Also Clause 8 and 9 of the FIDIC subcontract provide that, as regards instructions and variations, the subcontractor shall have similar rights and duties vis-à-vis the contractor to those owed by the contractor vis-à-vis the employer.

Moreover, significant rights or duties of the subcontractor vis-à-vis the contractor are often hinged upon rights and duties of the latter vis-à-vis the employer. For example, the liability of the main contractor to make payments to subcontractor is frequently conditioned upon the certification of the sums in question by the owner's architect or engineer under the terms of the main contract.¹⁸ In the same vein, architects often indicate in their certificates for interim payments to the main contractor what proportion of the sums so certified is referable to nominated subcontractors.¹⁹

In addition, it is not unusual that the subcontract will contain "pay if and when paid" clauses, which provide that the subcontractor will be entitled to be paid the balance of the subcontract price only if and when the contractor has been paid by the employer under the main contract. This kind of clauses are rightly criticised and are expressly excluded by some standard forms of subcontracts, including the FIDIC subcontract provisions for example.²⁰ This is because "pay if and when paid" clauses largely hinder ultimate recovery of the subcontractor and totally shift the risk of the employer becoming insolvent to the latter who is not a in contractual terms with the employer.²¹ Nevertheless, they are not unusual in the construction industry, especially in construction subcontracts in the countries of South-east Asia.²²

Although in principle no privity exists between the employer and the subcontractor, there are cases where either person will be entitled to a direct

¹⁷ J. Winter "The FIDIC Conditions of Subcontract and the UK FCEC 'Blue Form' of contract", (1997) 14 ICLR, p. 435, who argues that by virtue of this provision any extension of the main contract should automatically extend the subcontract too, although this is not expressly provided in the provision.

¹⁸ Hudson's, *supra* n. 8 para 13-108.

¹⁹ Hudson's, *ibid*, para 13-121.

²⁰ See Sub-clause 16.5.

²¹ The crucial question here is whether "the pay if and when paid" clauses hinge the *liability* of the main contractor vis-à-vis the sub-contractor upon the payment of the former by the owner; see further on this, Hudson's *supra* n.8, para 13-108 et seq and Murdoch –Hughes, *supra* n.7, para 19.6.1: the prevailing view in the US case law is that such clauses do not mean that the subcontractor will be paid if the main contractor is ever paid. This construction is accepted in order to ameliorate the consequences of such clauses, see for example *Thomas J Dyer co v Bishop International Engineering Co.*, 303 F 2d 655 (1962).

²² Murdoch – Hughes, *supra* n. 8 para 19.6.1.

contractual claim against the other. For example, the main contract may expressly provide that the employer has to pay the subcontractor directly, deducting the sums paid from the amount due to the main contractor.²³ Such a contractual provision will give the subcontractor the right to sue the employer directly. The same will apply, whenever the applicable substantive law expressly provides that the employer may be directly liable to the subcontractor. This is the case under French law²⁴ and the law of some of the countries influenced by French law.²⁵

Similarly, the employer will be entitled to a direct *contractual claim*²⁶ against the subcontractor, in case the latter provides the employer with a direct warranty on the work.²⁷ Direct warranties are often provided in construction contracts and are even included in some standard forms of construction contract.²⁸ Faced with an action from the employer, the subcontractor may raise defences arising out of the contract between the contractor and the subcontractor, or even defences arising out of the main contract between the contractor and the employer.²⁹

The contractual interrelation between the main contract and the subcontract means that a dispute arising out of the former is likely to refer to the same factual and legal issues as a dispute arising out of the latter. Thus, for example, the issue of causation or liability will probably arise in both disputes. Likewise, defects or delay in the work of the subcontractor will affect the liability of the contractor vis-à-vis the employer, and

²³ Hudson's, *supra* n. 8 para 13-121.

²⁴ Law No. 75-1334 of December 31, 1975. See further on this, C. Seppala, "French Law on Subcontracting" [1991] *ICLR*, p. 78.

In Swiss law see F Chaix and S. Marchand, "The right of Recourse of an Employer against a Subcontractor", (1998) 15 *ICLR*, p. 21: there is no specific provision in Swiss law providing for a direct claim/relationship, but they argue that the Code of Obligations art. 339(3) ("if the agent has assigned the obligation to a third person (...) the Principal may bring any claims which he has against his agent directly against the third person") regulating the relationships between agent-principal and the third party should be applied by analogy to the contractors for work and materials.

²⁵ See for example, Algerian Code art. 565, Egyptian Code art. 662, Libyan Code art. 661.

²⁶ The other option will be of course that the employer files tort claims against the subcontractor, in which case the employer must establish that the subcontractor owes him a duty of care, see in *Henderson v Merrett Syndicates Ltd*, [1994] 3 All ER 506 HL; Halsbury's, *supra* n. 1, para 48 and Hudson's, *supra* n. 8, para 13-042 et seq.

²⁷ *Greater Nottingham Co-operative Society Ltd. v Cementation* [1988] Q.B. 71; see also Halsbury's, *supra* n.1. para 47 and Chaix – Marchand. *supra* n. 24. p.227. According to Hudson the direct warranties provided by the subcontractor to the employer entirely subvert the no-privity subcontract objective of the English nomination system. Hudson's, *supra* n. 8 para 13-055.

The same will apply when the manufacturer provides for warranty in the context of string contracts regarding the same goods.

²⁸ See for example in the RINA/JTC standard form: "exécution sans défaut".

²⁹ However, the subcontractor cannot invoke the defences based on the personal relationship between the contractor and subcontractor, see Chaix - Marchand. *supra* n. 24. p. 223 et seq.

the amount of damages owed by him against the employer.³⁰ In case the contractor is found liable for works actually constructed by the subcontractor, the former will most likely sue the latter. It follows, that the interests of the contractor and the subcontractor in the project and the outcome of the proceedings between the contractor and the employer are *closely related*.

On the other hand, *the several string contracts remain distinct*. As a matter of principle there is no privity between the employer and the subcontractor.³¹ Even, when the subcontractor is nominated or selected by the employer, the main contractor is not regarded as the agent of the owner.³² Acceptance by the employer of work done by a sub-contractor does not establish or even imply a contractual link between these two persons.³³

The principle of no privity between the employer and the subcontractor in effect means that the economic risk and the contractual duty of performance of the main contract rest entirely on the main contractor. The latter rather than the subcontractor will be held liable for defective work performed by the subcontractor.³⁴ Equally, unless otherwise is expressly provided in law or in contract, the employer will not be liable to pay the subcontractor directly for work done or materials supplied with regard to the main work.³⁵

The principle of no privity applies even to back-to-back standard forms of contract and subcontract. Thus, the FIDIC Subcontract provides in Sub-clause 4.3 that:

“Nothing herein shall be construed as creating any privity of contract between the Subcontractor and the Employer”;

While, Sub-clause 4.4 provides that:

“If the Subcontractor commits any breaches of the Subcontract, he shall indemnify the Contractor against any damages for which the Contractor becomes liable under the Main Contract as a result of such breaches. In such

³⁰ Hudson's, *supra* n. 8, para 8-169.

³¹ Unless the contractor assigns the subcontract to the employer, see FIDIC (Red book) clause 4.5: Assignment of Benefit of subcontract. See also Murdoch- Hughes, *supra* n. 7, para 19.3; Hudson's, *ibid*, para 13-016; Wallace, *supra* n. 9, para 21-02 et seq; Halsbury's, *supra* n. 1, para 47. Cf *Davies & Co (Shopfitters) Ltd v William Old Ltd* (1969) 67 LGR 395.

³² See Murdoch- Hughes, *supra* n. 7, para 20.3 et seq and 20.4.1; Chaix- Marchand, *supra* n. 24, p. 223. See also *Hampton v Glamorgan*, [1917] A.C. 13; *Vigers Sons & co Ltd v Swindell*, [1939] 3 All ER 590.

³³ Halsbury's, *supra* n. 1, para 47.

³⁴ Murdoch - Hughes, *supra* n.7, para 19.5.2.

³⁵ See the seminal decision in *Hampton v Glamorgan*, [1917] AC 13.

event, the Contractor may, without prejudice to any other method of recovery, deduct such damages from monies otherwise becoming due to the Subcontractor.”³⁶

The reason the parties draft the subcontract in back-to-back terms with the main contract is to ensure that the two contracts will be compatible and, thus, more effective. However, back-to-back terms by no means break the contractual autonomy of the main contract and the subcontract. The performance promised by the contractor to the employer is different from that promised by the subcontractor to the contractor, despite the fact that both performances concern the same project.³⁷

The rights, duties and liability of the contractor in the main contract can never correspond exactly to those of the subcontractor in the subcontract.³⁸ This is because, the flow of the contractual rights and duties of the employer stops at the contractor. Unless there is an express provision in the subcontract, benefits that the contractor might obtain from the main contract cannot be passed over the subcontractor.³⁹

In *Lafarge Redland Aggregates Ltd. v Shephard Hill Civil Engineering Ltd.*⁴⁰ the subcontract contained a preamble making express references to the main contract:

“Whereas the contractor has entered into a contract (hereinafter called ‘the main contract’) particulars of which are set out in the First Schedule hereto”
and

³⁶ Cf also the SEA art.29(2) Rule 118 providing that “Dans l’exécution de ses travaux, le sous-traitant n’a rapport contractuel qu’avec l’entrepreneur”.

³⁷ Nicklisch, *supra* n. 8, p. 68-69.

³⁸ Hudson’s, *supra* n.8, para 18-116.

³⁹ See *Mooney v Henry Boot Construction Ltd* [1996] 80 B.L.R. 66; 53 Con. L.R. 120; see also the *Balfour Beatty Construction Ltd v Kelston Sparkes Contractors Ltd*, (No.2) 2001 WL 753373, where the subcontractor claimed part of the sum awarded by an arbitral award to the contractor against the employer. Although the sum was awarded to the contractor for delay and disruption to planned drainage arrangements which were works *undertaken by the subcontractor*, it was disputable whether the subcontractor was entitled to any portion of this sum. This was the case in spite of the fact that, first the contract (a I.C.E. Standard Form of Contract for Civil Engineering Works,) and the subcontract (a F.C.E.C. Standard Form of Subcontract) were designed as back-to-back contracts; second the subcontract expressly provided in cl.10(2) for the contractor to take all reasonable steps to secure from the employer such contractual benefits, if any, as might be claimable in accordance with the main contract ‘on account of any adverse physical conditions or artificial obstructions or any other circumstances that may affect the execution of the subcontract works’, and that on receiving any such benefits the contractor was to pass on to the subcontractor a fair and reasonable proportion. Finally the Court of Appeal decided that the subcontractor was entitled to *a fair and reasonable proportion* of the sum that the contractor was awarded by the employer. However, H. Lloyd J at first instance had held that clause 10(2) was merely providing for a procedural rather than a substantive claim.

⁴⁰ [2000] 1 W.L.R. 1621 (L).

“whereas the subcontractor having been afforded the opportunity to read and note the provisions of the main contract (other than details of the contractor's prices thereunder), has agreed to execute upon the terms hereinafter appearing the works which are described in the documents specified in the Second Schedule hereto and which form part of the works to be executed by the contractor under the main contract.”

Despite the above references to the main contract the House of Lords noted that:

“These provisions have an important bearing on the contractual relationship between the contractor and the subcontractor. But it is not, and could not be, suggested that by entering into the subcontract with the contractor the subcontractor was entering into a contractual relationship of any kind with the employer”⁴¹

And also that:

“The only contract which binds the employer is his contract with the contractor under the main contract. The only contract which binds the subcontractor is his contract with the contractor under the subcontract. The doctrine of privity of contract inhibits the formation of any kind of implied contractual relationship between the employer and the subcontractor.”⁴²

The same was held in the ICC award case no 6230 of 1990. Here, the subcontract included a clause providing that:

“in the internal relationship the subcontractor will take upon himself and bear all obligations and risks arising from the contract to be concluded between the [employer] and [contractor] in such a way as if the subcontractor had concluded a direct contract with the [employer] for his scope of supply and services”⁴³

Nevertheless, the tribunal was clear noting that the above provision was a “risk shifting” clause that should be construed narrowly since under Swiss construction law, applicable to both the main contract and the subcontract:

“(a) the subcontract is treated as an independent contract vis-à-vis the main construction contract.

⁴¹ *Ibid.*, at 1626.

⁴² *Ibid* at 1623.

⁴³ Unpublished.

(b) the subcontractor is not a person employed by the contractor for the performance of an obligation

(c) Provisions of a main construction contract do not become automatically valid vis-à-vis the subcontractor simply because the contractor made an obligation to the owner to adopt such provisions of the main contract in the subcontract

(d) there are no direct legal relationship between the owner and the subcontractor”

In the light of the above analysis, it is concluded that the several string contracts, *although interrelated remain separate*. Despite the fact that the general legal position of the subcontractor is in many ways affected by that of the contractor, the liability of the former is as a matter of rule from those the liability of the latter.

2.3 WEB-TYPE CONSTRUCTION CONTRACTS

Here the position is usually more straightforward than in the case of string contracts. The two contracts, the one between the employer and the architect or engineer (*the A/E contract*)⁴⁴ and the other between the employer and the contractor (*the building contract*), will be related in many ways. However, the autonomous character of each contract is even clearer than in the case of string contracts. More specifically:

On the one hand, the two agreements are in principle *connected*, since the building contract is normally concluded *in light* of the A/E contract. The contractor undertakes the duty to construct the work in a “workmanlike manner” *in accordance with* the design specifications provided in the A/E contract. The latter sets out in detail the plans, the drawings, the materials and the working methods required to be followed for the construction of the work.⁴⁵

⁴⁴ Architects undertake the duty to design the building and, usually, to supervise and administrate the work until its final completion. The duties of the engineers, although not always the identical are similar to those of the architects as far as the design and supervision of the work is concerned; cf the description given by the Institution of Civil Engineers (ICE) for the profession of civil engineer as “the art of directing the great sources of power in nature for the use and convenience of man” (found in Hudson’s, *supra* n. 8, para 2-016.

⁴⁵ Hudson’s, *ibid.* para 4-080.

Moreover, the A/E undertakes the duty to administer the building contract. Thus, the A/E is continuously involved in the construction work, having to decide whether the work done by the contractor is acceptable or not.⁴⁶

The building contract itself often requires the A/E to take a number of actions in connection with the construction work, in all of which the A/E owes a duty of care to the owner. Thus, for example, the A/E will undertake the duty to order variations, or check the contractor's final account on completion.⁴⁷

The intersection of the two contracts, in terms of substantive rights and duties means that whenever the work turns out to be defective the question of whether there is a construction or design default inevitably arises. Therefore, the same legal and factual issues will come up in a dispute arising out of the A/E contract and a dispute arising out of the building contract. For example, the issue of whether the plans and drawings in the A/E contract were followed by the contractor will be directly relevant to both contracts and the disputes arising out thereof. The same applies to the question of whether the plans, drawings or other instructions were given by the A/E to the contractor *in time*; or whether the fact that a supplier or a sub-contractor, nominated by the A/E had refused to complete the work, affected the progress of the contractor's work; or whether further instructions that had been given by the A/E constitute *variations*, that would entitle the contractor to additional payment. Thus the courts or tribunals will have to pay considerable regard to the provisions of the building contract, which the A/E has agreed to supervise and administer, in order to ascertain the duties owed by the A/E to the employer.⁴⁸

It is, therefore, evident that the A/E and the building contract are typically interconnected. Accordingly, the interests of the contractor and the A/E are related to those of the employer. Thus, for example, in proceedings between the employer and the A/E, the contractor has an interest in seeing the employer succeeding in its claim against the A/E. Otherwise the employer will most likely turn against the contractor. Equally, the A/E will have an interest in seeing the employer succeeding in its claim against the contractor. More generally, in the context of web-type construction contracts, the legal position of the third party, be that the architect or the contractor, will be associated to that of the "middle man" employer.

⁴⁶ Hudson's, *ibid*, para 2-058.

⁴⁷ Hudson's, *ibid*, para 2-198.

⁴⁸ Hudson's. *supra* n. 8, para 2-004.

Notwithstanding the above, the main and the building contract remain *distinct agreements*. The A/E and the contractor assume separate duties vis-à-vis the employer, stemming from different bilateral contracts. The A/E is solely bound by the A/E contract, often concluded a considerable time before the main building is concluded.⁴⁹ A/E and contractor are in no contractual relationships.⁵⁰ Termination of the contractual relationship between the employer and the A/E has no legal effect to the contractual relationship between the employer and the contractor, and vice versa. Consequently, the liability of the contractor vis-à-vis the employer is distinct from that of the A/E. Contractor and A/E will normally be liable vis-à-vis the employer *in the alternative* rather than jointly. Apart from exceptional cases,⁵¹ the latter is usually free to elect to sue one over the other.⁵²

It follows from the above that, despite the fact that they are in many ways interrelated, the A/E and the building contracts remain largely separate and autonomous.

2.4 GUARANTEES AND OTHER SECURITY AGREEMENTS

Very often, parties in their commercial transactions arrange for the security of the performance or the debt assumed therein. Thus, in accordance with the terms of the main contract, a third party will provide security for the performance of the transaction in a separate agreement (the '*security agreement*'). This third party may be a bank, an insurance company, protection and indemnity association or other guarantor. Naturally thus, security arrangements lead to multiparty situations: a third person comes into play providing security for the contract exclusively concluded between two other parties.

The terms 'security agreements' and 'suretyship' are generic terms covering different types of contracts, such as guarantees, indemnities or performance bonds.⁵³ Hence, the term 'surety' will be used, here, collectively referring a person providing

⁴⁹ Hudson's, *supra* n. 8, para 2-005.

⁵⁰ See for example *Davies & Co (Shopfitters) Ltd v William Old Ltd* (1969) 67 LGR 395. Hudson, however, argues that there is an *implied warranty duty* of the A/E vis-à-vis the contractor not to exceed his actual authority the breach of which will result to the liability of the A/E against the contractor, see Hudson's, *supra* n. 8, para 2-080.

⁵¹ Where the employer may sue both the contractor, for construction fault, and the A/E for supervisory negligence (concurrent liability), see *Townsend v Stone Toms & Partners* (1984) 27 BLR 26.

⁵² See *Campbell Flour Mills v Bowes and Ellis* (1914) 32 O.R. 270.

⁵³ G. Andrews and R. Millett, *Law of Guarantees*, (3rd ed. Sweet & Maxwell London 2000), para. 1.01

security in all the above types of security contracts. In principle, the term can be also used with regard to insurance contracts. However, for the purposes of the thesis at least, guarantees, indemnities or performance bonds should be distinguished from insurance contracts. The latter provide security for a person “against damage caused by contingencies *other than the non-performance* by another person of obligations or duties owed to the insured.”⁵⁴ Therefore, insurance contracts are not usually concluded *in view of a contract between two other persons*. Thus, unlike the other security agreements, insurance contracts will not necessarily lead to multiparty situations. Accordingly, the main attention of this section will focus on guarantees, indemnities and performance bonds, while insurance contracts will be relevant only in cases the damage is caused by a third party, as, for example, in the case of an accident.

On the one hand the main contract and the security agreement are interwoven. In fact, the two contracts are more closely interrelated than in the case of the several string or web-type construction contracts. Guarantees, indemnities and performance bonds perform similar commercial functions in providing compensation to the creditor for the failure of a third party to perform his obligations.⁵⁵ The security is provided in view of the debt or the performance undertaken in the main contract. Compensation in accordance with the security agreement will be provided only if the performance in the main contract is not fulfilled. The non-performance of the main contract is, thus, a condition precedent for the performance of the security agreement.

This, in principle, applies to all the above three types of security contracts, although the interrelation will be stronger in the case of guarantee than in the case of indemnity or performance bond. This is because in a guarantee contract⁵⁶ the

⁵⁴ Andrews- Millett, *ibid*, para. 1.08.

⁵⁵ Halsbury's, *supra* n. 1, para 343.

⁵⁶ Defined in Halsbury's, *ibid*, para 101, as “an accessory contract by which the promisor undertakes to be answerable to the promisee for the debt, default or miscarriage of another person, whose primary liability to the promisee must exist or be contemplated. For other definitions of a guarantee contract. In England See also *Re Conley, ex p Trustee v Barclays Bank Ltd*, *Re Conley, ex p Trustee v Lloyds Bank Ltd* [1938] 2 All ER 127 at 130 (CA).

In the US, see *Madison County Farmers Ass'n v. American Employers' Ins. Co.*, 209 F.2d 581 (8th Cir.1954); *W. T. Rawleigh Co. v. Warrington*, 39 Del. 366, 199 A. 666 (1938): “[s]uretyship may be defined as a contractual relation whereby one person engages to be answerable for the debt or default of another.” See also Restatement (Third) of Suretyship & Guaranty (1996) § 1 et seq.

In France, see Code Civil art.2288 (as amended by the recent Ord. No346 of 23 March 2006): « Celui qui se rend caution d'une obligation, se soumet envers le créancier à satisfaire à cette obligation, se le débiteur n'y satisfait pas lui-même »: see further Delebecque, in *Rèp. Civ.* (2007), Cautionnement, art.2288 et seq.

guarantor undertakes an obligation that is *dependent upon and collateral* to the main obligation, while in an indemnity⁵⁷ or a performance bond⁵⁸ the promisor undertakes *an original and independent obligation* to save the promisee from any loss caused by the claims of third parties.⁵⁹

Thus, the *guarantee and the main contract present a unique interrelation*. This is particularly evidenced by the following.

First, *the obligation* of the debtor in the main agreement is the main reason that security is provided in the security contract.⁶⁰ The obligation of the surety to perform instead of the debtor is activated only in case the latter fails to perform its own obligation. Secondly, under a contract of guarantee, the guarantor assumes a secondary *liability* to the creditor for the default of another who remains primarily liable to the creditor.⁶¹ The surety is liable only to the extent that the debtor is.⁶² For the surety to be held liable, the liability of the debtor must in any case exist or be contemplated.⁶³ Thirdly, the duration and the validity of the guarantee contract depend upon the duration and the validity of the main contract.⁶⁴ Fourthly, the surety is entitled to invoke against the creditor all the defences arising out of the main

⁵⁷ Indemnity, on the other hand, is a contract by one party to keep the other harmless against loss caused to him by the conduct of third parties see for example, *Yeoman Credit Ltd v Latter*, [1961] 2 All ER 294 at 296, CA, per Holroyd Pearce LJ.

In France, there is the autonomous guarantee or guarantee on first demand (*garantie à première demande*), see Civil Code, art. 2331: « La garantie autonome est l'engagement par lequel le garant s'oblige, en considération d'une obligation souscrite par un tiers, à verser une somme soit à première demande, soit suivant des modalités convenues ».

⁵⁸ Performance bonds fall, in general, under the definition of indemnity, Halsbury's, *supra* n.1, para 343. This is particularly the case for performance bonds "on demand" as opposed to performance bonds "on default". The former can be called without proof of breach of contract by the contractor or of loss or damage suffered by the employer, whereas the latter operate as guarantee and requires proof of default on the part of contractor, see further, J. Jenkins and S. Stebbings, *International Construction Arbitration Law*, (Kluwer Law International 2006) p.47.

⁵⁹ Halsbury's, *supra* n.1, para 343.

⁶⁰ *Lakeman v Mountstephen* [1874] L.R. 7 H.L. 17, at 24: "there can be no suretyship unless there is a principal debtor. Nor can a man guarantee anybody else's debt unless there is a debt of some other person to be guaranteed".

⁶¹ *Yeoman Credit Ltd v Latter*, *supra* n.86; *Goulston Discount Co Ltd v Clark* [1967] 1 All ER 61 CA; *Argo Caribbean Group Ltd v Lewis* [1976] 2 Lloyd's Rep 289 at 296, CA, per Orr LJ.

⁶² *Andrews- Millet*, *supra* n.85, par.1.04 and *Wardens and Commonalty of the Mystery of Mercers of the City of London v New Hampshire Insurance Company*, [1991] 3 J.I.B.F.L. 144. Cf also *The London Lion*, [1980] 2 Lloyd's Rep 456 (CA) that held that the letter of undertaking was a contract subsidiary and secondary to the shipbuilding contract.

In the US. see Restatement (Third) of Suretyship & Guaranty (1996) para 15(b).

⁶³ See, Halsbury's, *supra* n. 1, para 101. See also French Civil Code art.2298 « La caution n'est obligée envers le créancier à le payer qu'à défaut du débiteur ».

⁶⁴ See in French Civil Code art. 2289 « La cautionnement ne peut exister que sur une obligation valable»; *Andrews - Millet*, *supra* n. 82, par.6.01; cf *Jowitt v Callaghan* [1938] 38 N.S.W. 512 and *Vision v Churchfield Leasing* [1988] B.C.L.C 623.

contract, except the ones that are personal to the debtor. This is the rule under both common⁶⁵ and civil law.⁶⁶ Finally, any collateral supplied by the principal obligor to secure the duty to reimburse the secondary obligor also secures the principal obligor's duty to the secondary obligor to perform the underlying obligation.⁶⁷

The above apply particularly to guarantee which, as already noted, is considered a contract dependant and ancillary to the main contract.⁶⁸ Nonetheless, the situation does not significantly differ in indemnities or performance bonds. Here, as in the case of guarantee, the creditor when suing the surety must prove that he has suffered a loss *due to the principal's non-performance*. In other words, the difference between guarantees on the one hand and the indemnities and performance bonds on the other is that in the former compensation is due only if the principal debtor is found *liable* for non-performing, whereas in the latter compensation is due irrespective of whether the principal debtor is found liable for non-performing or not. In both cases, however, compensation under the security agreement follows the non-performance of the main contract.⁶⁹

Thus, in all security agreements, the surety undertakes an obligation *in view of the obligation* undertaken by the debtor in the main contract. This is why the surety has to pay *exactly the same amount of money or to perform exactly the same the performance* that the debtor failed to pay or perform.⁷⁰ Hence, the creditor can only be paid once, either by the debtor or the surety. When the secured obligation is fulfilled the security contract is brought to an end, and the creditor does no longer have any

⁶⁵ A.L. Corbin, *On Contracts*, Int. ed. (Lexis Nexis 2002) and 2004 Spring Cumulative Supplement , par. 937; The same in Restatement, (Third) of Suretyship & Guaranty (1996) para 34.

⁶⁶ In France, see Civil Code art. 2313 « La caution peut opposer au créancier toutes les exceptions qui appartiennent au débiteur principal, et qui sont inhérentes à la dette; Mais elle ne peut opposer les exceptions qui sont purement personnelles au débiteur » ; see also Civ 1st, 1 June 1983, (1984) D, p.152, with note Aubert.

In Germany, see Civil Code art.768 and in Greece, see Civil Code art.853 and Βρέλλης, in ΕρμΑΚ Γεωργιάδη-Σταθόπουλου αρ.853.

⁶⁷ Restatement (Third) of Suretyship & Guaranty (1996) para 25.

⁶⁸ *Mountstephen v Lakeman* (1871) LR 7 QB 196 at 202. See also; *Lougher v Molyneux* [1916] 1 KB 718. The same is accepted in France, see Com. 26 Jan 1988, *Bull Civ.* IV, no 49 : « La cautionnement est une obligation accessoire à l'obligations du debater envers le créancier ».

⁶⁹ *Sampson v Burton* [1820] 4 Moo. C.P.515: "The surety is under a secondary obligation which is dependent upon the default of the principal and which does not arise until that point".

⁷⁰ Corbin, *supra* n.94, par 926: "one who guarantees payment of the debt of another person, may undertake a separate obligation, but he nevertheless always promises the *same performance* as the principal debtor. This is the case even where the guarantor limits the amount of his liability". The same is accepted in Greece, see Βρέλλης, in ΕρμΑΚ, Γεωργιάδης-Σταθόπουλος Αρθρο 847.

claim against either the debtor or the surety.⁷¹ This is also why every jurisdiction provides that the surety is entitled to recover his payment from the debtor once he performs the secured obligation (*subrogation*).⁷²

It follows from the above, that first, the legal position of the surety is *strongly interwoven* to that of the debtor and secondly, *the interests of these two parties vis-à-vis the creditor are closely related*.

On the other hand, though, the interests of the surety remain dissimilar to those of the creditor. The legal status of the surety is distinct from that of the debtor. In particular, the security contract and the main contract are two separate bilateral agreements rather than one multiparty agreement.⁷³ The *obligations* undertaken by the surety and the debtor are different: the surety does not promise to deliver the performance undertaken by the principal; he promises to cover the *risk* that this performance is not delivered.⁷⁴ The obligation of the surety is to repair the damage caused by the failure of the debtor to perform. In *Lee v Yano*⁷⁵ it was noted that:

“a guarantor does not promise the same performance as the principal debtor. While a principal debtor promises to pay a specified amount, a guarantor promises to pay that amount only if it cannot be collected from the principal debtor.”

Moreover, as is generally accepted no privity exists between the surety and the debtor. Surety and debtor do not constitute one person in law, and therefore they are not jointly or jointly and severally liable to the creditor.⁷⁶ This particularly applies to

⁷¹ Halsbury's, *supra* n.30, para 187-188: “Where the guaranteed obligation is properly discharged by performance, the obligations of a guarantor of that obligation are also thereby discharged¹. Similarly, the guarantor will be discharged where the underlying contract is discharged by frustration before the time for performance”; see also Corbin, *supra* n.13, par.931 and 947; Restatement (Third) of Suretyship & Guaranty (1996), para 39; see also *Union M.L. v Handford*, 12 S.Ct.437 (U.S. 1892). It should be noted that in performance bonds provided with regard to construction projects the surety is not discharged until the architect or engineer has issued a certificate that the work has been completed to his satisfaction, *Eshelby v Federated European Bank Ltd* [1932] 1 KB 423, CA: the liability of the surety does not arise if the contractor fails to show entire completion.

⁷² In England, see Halsbury's, *supra* n.30, para 226. In the US, see Restatement (Third) of Suretyship & Guaranty (1996) para 27. In France see Code Civil, art. 2305 et seq.

⁷³ Cabrillac et Mouly, *Droit des Sûreté* (Litec 1990), par. 327; Simler, *Le Cautionnement* (Litec 1982), par. 44.

⁷⁴ Cabrillac et Mouly, *idem*; E. Loquin, “Arbitrage et Cautionnement”, (1994) *Rev. Arb.*, p.236. cf also Simler, *ibid*, par. 232.

⁷⁵ 93 Haw.142, 997 P.2d 68, (Intermediate Ct. App.2000) at 74.

⁷⁶ See for example, *Rawstone v Parr* (1827) 3 Russ 539 at 541 and the more recent *Moschi v Lep Air Services Ltd* [1973] AC 331 (HL). The same is accepted in France, unless the guarantor has expressly undertaken a joint and several obligation with the principal (caution solidaire) see Code Civil art,

indemnity, where liability of the indemnitor vis-à-vis the creditor is *primary* rather than ancillary to liability of the debtor. Here, the surety undertakes to *indemnify* the creditor in case the debtor does not perform. In other words, he undertakes the obligation to make good a loss suffered by debtor's failure to deliver rather than to deliver what the debtor has promised. Therefore, the liability of the surety is accepted to be independent rather than joint or joint and severally with the liability of the debtor.⁷⁷

In the same vein, the English Court of Appeal held in *McAlpine Construction v Unex*,⁷⁸ that, unless an express wording to the contrary is stipulated in the suretyship contract, the liability of the surety is, in principal, independent from that of the debtor. In this case, a clause was inserted in the suretyship contract⁷⁹ in question providing that

“[...] the Guarantor (a parent company of the employer) shall not be under any greater liability to the Contractor (the creditor) than the Employer (the principal debtor) would have been liable in contract pursuant to the express terms of the (main construction) Contract”.

Despite the fact that the liability clause in the suretyship contract was directly referring to the main contract and the debtor's liability (as the maximum limit of the surety's liability), the court held that wording was not explicit enough to link the liability of the surety to that of the principal debtor. Thus, this view concludes, the surety and the principal debtor are neither joint nor joint and several obligors vis-à-vis the creditor, since a joint liability requires that more obligors promise the same performance.⁸⁰

The same applies to performance bonds, which constitute a binding contractual undertaking given by a person to pay a specific amount of money to a named beneficiary, in case the principal fails to fulfil his contractual obligation to the beneficiary.⁸¹ Therefore, the contractual obligations arising under such bonds are

2298 a fin. The same also in Greece, see Βρελλης, in ΕρμΑΚ, Γεωργιάδης-Σταθόπουλος Άρθρο 847 para 33.

⁷⁷ Andrews-Millet, *supra* n.82, par 1.13. See also *Western Credit Ltd v Alberry* [1964] 2 All ER 938 (CA) and *Stadium Finance Co Ltd v Helm* (1965) 109 Sol Jo 471 (CA).

⁷⁸ *McAlpine Construction v Unex*, [1994] 38 Con LR 63 (CA).

⁷⁹ Which the court held, to be a contract of indemnity although the form of contract employed by the parties bore the title “guarantee contract”, *ibid*, at 66.

⁸⁰ *Lee v Yano*, *supra* n. 94, at 73: “a guarantor is not a co-obligor or a joint and/or several obligor with the principal obligor”.

⁸¹ Andrews-Millet, *supra* n. 82, para 1.16; see also Halsbury's, *supra* n. 30, para 359.

separate from, and not dependent on, those existing under the main contract.⁸² As has been noticed, the obligations assumed by a bank under the performance bond are analogous to those assumed by a confirming bank to the seller under a documentary credit.⁸³

This, in effect, means that, unlike guarantors, the person securing the debtor's obligation by an indemnity or a performance bond will remain liable even in the event that the main agreement is void or unenforceable.⁸⁴ Similarly, an insurer under an insurance contract undertakes a primary rather than a secondary obligation vis-à-vis the insured. Thus, the liability of the insurer is accepted to be independent from that of the liability of the third person.⁸⁵

In the light of the above it is concluded that the relationship between the surety and the debtor is a *unique, sui generis one*: their interests are related albeit distinct. The liability of the surety is affected by, or in the case of guarantor directly depended upon, the liability of the debtor. However, surety and debtor are by no means co-liable vis-à-vis the creditor. Due to the warranty nature of a security agreement, the legal status of the surety is interrelated by that of the debtor. However, surety and debtor are not parties in privity.

2.5 SEVERAL COMPANIES WITH CLOSE CORPORATE LINKS: THE CASE OF THE "GROUP OF COMPANIES" IN PARTICULAR

Although not far from new, the idea that a corporation carries out business through a number of subsidiaries in several countries has become now the typical form of business organization.⁸⁶ The role of 'subsidiaries' has become central to the way

⁸² This is particularly the case with "performance bonds on demand", see *supra* n. 87. See also *Themehelp Ltd v West* [1996] QB 84 (CA); *Wahda Bank v Arab Bank plc* [1996] 1 Lloyd's Rep 470 (CA).

⁸³ See Halsbury's, *supra* n. 30, para 359 and *United City Merchants (Investments) Ltd v Royal Bank of Canada* [1983] 1 AC 168 at 184 (HL). However, performance bonds, unlike letters of credit, do not provide any security to the issuer: see *Potton Homes Ltd v Coleman Contractors Ltd* (1984) 28 BLR 19 (CA). Also, the principle "of strict compliance", applicable to letters of credit according to which the payment is allowed only if the documents, conforming precisely to the terms of the letter of credit, are presented to the bank does not apply to performance bonds: see *Siporex Trade AS v Banque Indosuez* [1986] 2 Lloyd's Rep 146.

⁸⁴ *Yeoman Credit v Latter*, [1961] 2 All ER 294.

⁸⁵ Halsbury's, *supra* n. 1, para 110.

⁸⁶ See, in general, T. Hadden, *The Control of Corporate Groups*, (Institute Advanced Legal Studies-University of London 1983); P. Muchlinski, *Multinational Enterprises and the Law*, (Blackwell London 1999); P. Blumberg, *The Law of Corporate Groups, Procedural Law* (Little Brown and Company 1983); P. Blumberg, *Tort, contract, and other common law problems in the substantive*

international commerce is conducted nowadays. Trade operations very often split between a number of holding companies, or expand through the acquisition of established businesses, which they later incorporate into their group.⁸⁷ The several companies belonging in the same corporate group will usually have a wide range of interconnected relationships. However, each of them will typically have been established as a separate legal entity. Thus, the close financial or business links between the several companies belonging in the same group are not reflected in the formal legal structure of a multinational, as a group of several separate legal entities. There are clear advantages in terms of taxation and efficient business management for a multi-company international group to adopt a 'separate corporate personality' structure.

Although the traditional structure of a group of companies will be that of a parent company with several subsidiaries or sub-subsidiaries, groups may take different legal structures, depending on the business objectives of the group and the legal models available under the law of the state in which the different companies reside. In particular they may take the form of groups based on contract, or equity based corporate groups, joint ventures between independent firms, informal alliances, publicly owned multinationals and supranational forms of international business.⁸⁸ Moreover, a group of companies will very often consist of companies of various nationalities, which gives the group a multinational character and makes the issue of liability within the group even more complicate.

In any case, the groups will adopt the legal form that provides them with the maximum operational flexibility, which makes the groups commercially effective, and promotes international business in general. In most countries, the current trend in the national legislation regarding multinationals is moving towards a flexible, friendly regime for multinational groups.⁸⁹ This typically happens in developing countries in which the adoption of flexible company legislation is considered important for these countries to attract internationally mobile projects. The same, however, applies to all major industrial countries whose laws recognise the principle of 'limited liability' and

law of parent and subsidiary corporations: Substantive Law of corporate groups, (Little Brown and Company 1987); P. Blumberg, *On Corporate Groups*, (Aspen 2004); J. Dine, *Governance of Corporate Groups*, (CUP 2000); J. H. Dunning, *Multinational Enterprises and the Global Economy*, (Addison Wesley, 1992).

⁸⁷ Hadden, *ibid*, p. 10.

⁸⁸ Muchlinski, *supra* n. 86, p. 62; see also Dine, *supra* n.86, p.39 et seq.

⁸⁹ Cf Muchlinski, *ibid* 115, p. 9.

‘separate corporate personality’.⁹⁰ The adoption of a more liberal legal regime on group of companies, reflected on the rule of separate corporate personalities, has proved to some extent beneficial for the growth in the world economy, as it encourages investment even in relatively risky ventures.⁹¹

In England the principle was established very early in *Salomon v Salomon & Co Ltd*,⁹² and has since been accepted to a large extent consistently. In *Adams & Ors v Cape Industries plc & Anor*, the English Court of Appeal was clear that:

“Our law, for better or worse, recognises the creation of subsidiary companies, which though in one sense the creatures of their parent companies, will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities.”⁹³

And that:

“we do not accept as a matter of law that the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law”⁹⁴

In the US the rule is that, although shareholders were not immune from liability for corporate obligations at common law, the principle of limited liability and separate

⁹⁰ See OECD, Report on International Investment and Multinational Enterprise-Responsibility of Parent companies for their subsidiaries, (1980).

⁹¹ See Easterbrook and Fischel, “Limited Liability and the Corporation” (1985) 52 *U.Chi.L. Rev.* 103 et seq, who argue that the beneficial impact of the principle of limited liability and the entailing principle of separate liability between a parent and a subsidiary on capital markets outweighs the losses from its imperfections. From an political and ideological perspective, the argument for market driven economies has been now largely established as the prevailing and most effective economic practice. This has been particularly the case after the collapse of the Eastern Bloc in the late 1980’s and early 1990’s and the abandoning of state led economic policies even by countries such as China or Russia.

⁹² [1897] AC 22, HL. See more recent cases in *Adams & Ors v Cape Industries plc & Anor.*, [1990] B.C.C. 786 (CA) and *Ringway Roadmarking v Adbruf* [1998] 2 BCLC 625.

⁹³ Per Slade LJ at 820.

⁹⁴ *Ibid* at 826.

legal personality has been the cornerstone of corporate law since the nineteenth century, and is reflected in the legislation of every state.⁹⁵

This was characteristically noted in *Intergen N.V. v Grina*:

“the principle of limited liability ...[is] the corner stone of corporate law”⁹⁶

Similarly, in *DeBreceni v. Graf Bros. Leasing, Inc*⁹⁷, it was underlined that:

“Limited liability allows individuals to take a calculated risk when they engage in the investment and entrepreneurial ventures central to a capitalist economy. If the venture fails, corporate shareholders lose only their interest in the corporation, not their homes or life savings.”⁹⁸

This principle has been accepted by arbitral tribunals too. Thus, the tribunal in the ICC case no.11160 of 2002 stressed that:

“The Respondents have also explained in the record that Respondent 1 was organized with the specific purpose of qualifying for an exemption from the Value Added Tax introduced in Venezuela. This is perfectly lawful and valid business purpose. Contrary to what the Claimant believes, there is nothing devious or fraudulent about it.”⁹⁹

However beneficial as it might have been, the principle of separate liability has been criticized for shifting the risk from the corporate owners to involuntary third parties. In fact, the argument goes, by reference to the principle of separate liability, the multinational groups evade liability altogether and accumulate extreme power, which on some occasions they have abused.¹⁰⁰

⁹⁵ See the Revised Model Business Corporation Act (1984) para 6.22(a), expressly limiting shareholder liability to payment of the consideration for which the shares were authorized to be issued or payment of the consideration specified in the subscription agreement. It further provides that a shareholder is not personally liable for the acts or debts of the corporation except as provided in the articles of incorporation or except by reason of a shareholder's own acts or conduct.

⁹⁶ 344 F.3d 134 (1st Cir. 2003) at 150.

⁹⁷ 828 F.2d 877, 879 (1st Cir.1987) at 879.

⁹⁸ See also, indicatively, *Mills v USA Mobile Communications, Inc.*, 190 W Va 209, 438 SE2d 1 (1993); *Silva v Kinsho Intern. Corp.*, 210 F Supp 2d 241 (SD NY 2000); *Dorsky Hodgson & Partners, Inc. v National Council of Sr. Citizens*, 766 A2d 54 (DC 2001); *Bujol v Entergy Services, Inc.*, 922 So 2d 1113 (La 2004); *Salatin v Trans Healthcare of Ohio, Inc.*, 170 F Supp 2d 775 (ND Ohio 2001); *Drilltec Tech., Inc. v Remp*, 64 SW3d 212 (Tex App 2001); *Reeves v Mohawk Factoring, Inc.*, 261 Ga App 629, 583 SE2d 487 (2003); *Rowland v Franklin Career Services, LLC*, 272 F Supp 2d 1188 (D Kan 2003).

See also in more details the analysis of the principle and its limitations in the seminal work of Prof. P. Blumberg, *The law of Corporate Groups, Substantive Law*, *supra* n. 86.

⁹⁹ 16 (2005) 2 *ICC Bull.*, p.100.

¹⁰⁰ Indeed, there is growing concern over the fact that the growing power of big multinational groups has in many occasions been abused, in terms of corruption or human rights. The effects of the multinational groups upon the underdeveloped or developing countries have also raised questions

The discussion on whether or not the principle of separate liability has created the legal environment for multinationals to accumulate and abuse their power goes beyond the scope of this work. What is necessary to note, here, is that a strict application of the principle would distort commercial reality: the several companies belonging in the same group maintain very close corporate links. In strict business terms they constitute a trading unit. It is often the case that the several companies will share the same financial or human resources: officers, premises, contract details, bank accounts intellectual property rights etc. In addition they will operate under the same business plan, working closely together on a day-to-day basis on the same commercial projects.¹⁰¹

Thus, in many jurisdictions there have been attempts to restrain the principle of separate legal liability. In this regard, the main thrust of group liability theories and legislation is the same: to treat the several companies of the same group as a unit and hold either the parent company or the group as a whole liable for acts or omissions of the another company of the group.

In particular, in common law countries a parent company may be held liable under the doctrine of piercing the corporate veil, which however applies only as a matter of exception and under strict conditions.¹⁰²

In the US, where case law concerning the principle is extensive, the courts will mainly pierce the corporate veil of the subsidiaries and hold a parent company liable only when the former has been under the complete control of the latter or has been used as a 'sham' or a 'fraud' formalities.¹⁰³ Here, the courts will review a big list of various factors in order to determine whether the corporate veil should be pierced. They will examine for example:¹⁰⁴ the funds that have been channelled from the

since the 1970's. The argument for more transparency and disclosure in the way multinational groups operate has gained more ground lately. See in particular, J. Dine, *Companies, International Trade and Human Rights*, (CUP 2005).

¹⁰¹ See more details on that in Chapter 5 below.

¹⁰² In *Kodal Ltf v Clark* [1903] 1 KB 505, for example, it was held that a 98 per cent controlling interest in a company does not itself give rise to an agency relationship so as to treat the parent and subsidiary as one enterprise. Other similar theories on parent liability developed by the US courts are the alter ego theory, the identity theory, the instrumentality theory. All these theories are not fundamentally different than the doctrine of piercing the corporate veil and in many cases apply interchangeably, see K. Hofstetter, "Parent Responsibility for Subsidiary Corporations: Evaluating European Trends", (1990) 39 *Int'l Comp. L.Q.*, at p. 592, n. 130.

¹⁰³ See for example in R. Clark, *Corporate Law*, (Aspen Publishers 1986) p. 71-74.

¹⁰⁴ For this, see in general J. Purver, "Liability of Parent Corporation for Acts of Subsidiary", 16 *Am. Jur. Proof of Facts* 2d 67, and indicatively from case law: *Trustees of Nat. Elevator Industry Pension, Health Benefit and Educational Funds v Lutyk*, 332 F.3d 188 (3d Cir. 2003); *Thrift Drug*,

debtor corporation from the dominant stockholder; whether the companies of the group have failed to observe corporate formalities; whether a company of the group suffers from gross undercapitalization; the circumstances under which a debtor company of the group has been bankrupted; whether the corporation is merely a facade for the operation of the dominant stockholder.

In England, the courts will also review similar factors for the application of the doctrine. Thus, they will particular examine whether the owner exercised complete domination over the corporation with respect to the transaction at issue (objective factor) and whether that such domination was used to commit a fraud or wrong that resulted in the plaintiff's injury (subjective factor).¹⁰⁵

Civil law jurisdictions, where the doctrine of piercing the corporate veil is unknown, provide also for exceptions from the principle of separate legal liability. Germany has traditionally been the most progressive jurisdiction in this respect.¹⁰⁶ The German Act on stock corporations,¹⁰⁷ for example, provides that a parent company must integrate its subsidiary, when the parent owes more than 95% of the latter. In this way, parent and subsidiary become jointly and severally liable for any claim a third party creditor might have against the subsidiary. Although its scope is narrow and, therefore, its impact is limited, the German Act on stock corporations is a characteristic example of legislation where the several companies with corporate links are treated as group rather than as separate corporations.¹⁰⁸

In France, in the context of bankruptcy proceedings, it is provided that the assets of a parent company and its subsidiary are integrated, if the parent company has been de facto directing (“dirigeant de fait”) the subsidiary.¹⁰⁹

To conclude, in the context of corporate law, the principle of limited liability and accordingly the principle of separate liability between the parent and its subsidiary remain the rule internationally. Therefore, the several companies in the same group

Inc. v Universal Prescription Adm'rs, 131 F.3d 95 (2d Cir. 1997); *Bridas S.A.P.I.C. v Government of Turkmenistan*, 345 F.3d 347 (5th Cir. 2003).

¹⁰⁵ See *DHN Food Distributors Ltd v London Borough of Tower Hamlets* [1976] 3 All ER 462, see also Dine, *supra* n. 115, p.48 et seq.

¹⁰⁶ Blumberg, *Substantive Law*, *supra* n.115, p. 642.

¹⁰⁷ “Aktiengesetz”.

¹⁰⁸ See more in Hofstetter, *supra* n. 133, and M. Schiessl, “The liability of corporations and shareholders for the Capitalization and obligations of Subsidiaries under German Law” (1987) *Northwestern Int. Law & Bus.*, p. 480.

¹⁰⁹ Loi, 1985, 25 January, no 85-98, Redressement et liquidation judiciaires: art 180; see further, Roger Houin “Les Groupes de société en droit français”, in K. Hopt (Ed.), *Groups of Companies in European Laws, Legal and Economic Analyses on Multinational Enterprises*, (1982), p. 45-58.

are generally accepted to be distinct legal entities with separate interests. Nonetheless, it is also accepted that the several companies of the same group are typically strongly interconnected in terms of corporate links and commercial interests. This is why many jurisdictions provide for limited exceptions from the principle of separate liability.

CONCLUSIONS OF PART I

The analysis in the Part I demonstrated:

- First, that any person bound by an arbitration agreement as an ordinary contract, by reference to rules of contract law is a genuine party to that arbitration agreement. The term “genuine party” equally applies to persons, who have not personally concluded an arbitration agreement, but who nonetheless are bound by this agreement in accordance with general principles of contract law. This is in particular the case for a
 - Principal, when the arbitration agreement is concluded by an agent
 - Assignee, after the assignment of an arbitration agreement
 - Consignee in a bill of lading containing an arbitration agreement
 - Successor in a contract containing an arbitration agreement
- Second, false third parties are not contractually bound by an arbitration agreement concluded by two other persons (genuine parties), but who nevertheless are involved in the same commercial project with the genuine parties and, therefore, they have a significant interest in the dispute arising out of the project between the genuine parties.
- Third, false third parties can be distinguished in two different groups depending on how closely a false third party is associated a genuine party, in terms of interests and liability.
 - The first group includes false third parties that have concurrent interests with one the genuine parties and are co-liaible with them vis-à-vis the other genuine party to the arbitration agreement.
 - The second group includes false third parties that are contractually linked but not co-liaible with one of the genuine parties to the arbitration agreement. Here, the genuine and the false third party have related but

not concurrent interests in the pending dispute and the commercial project they both take part in.

- Fourth, the Chapter focused on some typical examples of false third parties of the second group, and provided a detailed analysis of their substantive relationships with the genuine parties. The analysis confirmed that the substantive relationships between several parties in the context of *construction contracts*, *security agreements* and *group of companies* are closely interrelated but still distinct.

PART II: ARBITRATION AND THIRD PARTIES: THE CONTRACTUAL APPROACH

The previous chapter distinguished between two different groups of “false third parties”, depending on the degree of association between genuine and false third parties, in terms of substantive liability and interests. The focus of attention was, in particular, on the rights and duties resulting from the contractual relationships between each of the groups of false third parties and genuine parties, and the way in which these rights and duties become intertwined. As has been shown, false third parties are typically involved in the same commercial project with the genuine parties and, therefore, they have a significant interest in the dispute arising out of the project between the genuine parties. Therefore, false third parties may not be strangers to the arbitration between the genuine parties.

Many questions arise in this context. Should the arbitration process between two original parties remain an exclusive system, reserved only for those persons who have consented thereto? Alternatively, should the arbitration process affect the position of the false third parties? Is any kind of communication between arbitration and false third parties compatible with the contractual character of arbitration? Should there be any third-party mechanism applicable to international arbitration?

To date, the discussion on arbitration and third parties has been limited to issues of “consent”. A strict *contractual approach* to the subject has been adopted by legal discourse and case law focusing exclusively on the contractual characteristics of arbitration agreements as substantive contracts.

From this contractual viewpoint, the answers to the above questions depend on whether a person is bound by an arbitration agreement as an ordinary contract or not. Any party not bound by an arbitration agreement, i.e. third party, may not take part into the arbitration process irrespective of any legal or financial interest that this third party might have in the dispute between the parties bound by an arbitration agreement. Therefore, according to the contractual approach, third-party mechanisms, such as joinder, intervention or consolidation, may not apply to arbitration unless all the relevant parties are bound by an arbitration agreement. This approach is echoed in the vast majority of the existing arbitration rules and arbitration laws, which usually hinge the application of third-party mechanisms to arbitration proceedings on the condition

that both genuine and third parties to an arbitration agreement have consented to the joinder or the consolidation.

Consequently, according to the prevailing contractual approach, the discussion on arbitration and third parties relates only to the boundaries of the arbitration agreement as a substantive contract. Within this contractual approach two different views have been suggested.

According to the first, arbitration agreements cannot have any impact whatsoever on any person, who has not clearly consented to arbitration, as this consent *is evidenced by his signature*.¹ Thus, only those persons that have *signed* the arbitration agreement will have the right to take part in arbitration proceedings. Conversely, any person who has not signed an arbitration agreement is regarded as a total stranger to the arbitration process, which may affect only the signatory parties. This view is quite straightforward relating to the formal requirement of signature and, thus, the thesis will not explore it any further.

By contrast, particular attention will be given to the second view taken by what is known as “extension doctrines”. According to the extension doctrines, it is possible under certain conditions for non-signatory parties to enter into an arbitration agreement, notwithstanding the fact that they have failed to sign it. As is argued, the arbitration agreement between two signatory parties may be “extended” to non-signatories. Hence, the thesis refers to these doctrines as “extension doctrines”. As will be shown, the extension doctrines do not challenge “consent” as a requirement for the participation of the non-signatory party to the arbitration between the signatories. The core argument of the extension doctrines is that signature on an arbitration agreement is not the only means to assert consent to arbitrate. Consent, which is necessary for a non-signatory party to participate in the arbitral proceedings, may be inferred, or even presumed by reference to other factual circumstances. Therefore, extension doctrines are in accord with the prevailing contractual approach.

This Part examines the contractual approach in detail. Chapter 1 explains the role of consent in this contractual approach and gives a brief overview of the existing arbitration laws and rules relating to the third-party mechanisms. Chapter 2 and 3 explore the two most influential and intellectually intriguing extension doctrines: the

¹ For example, O. Sandrock, “Extending the Scope of Arbitration Agreements to Non-Signatories”, in *Arbitration Agreement – Its Multifold Critical Aspects*; (1999) ASA Special Series No 8, p.167 and O. Sandrock, “Arbitration Agreements and Group of Companies” (1993) 27 *International Lawyer*, p. 945.

doctrine of “Equitable Estoppel” developed in the USA, and the Continental doctrine of “Group of Companies”. Chapter 4 further discusses the extension doctrines adopting a more critical stance. This chapter highlights the conceptual and practical limitations of the extension doctrines and the contractual approach in general. The discussion in Chapter 4 will demonstrate that a different approach to the issue of arbitration and third parties needs to be adopted: the jurisdictional approach that will be presented in Part III.

Chapter 3: Third-party mechanisms.....	60
3.1 Third-party mechanisms and consent	60
3.1.1 Equal treatment of the several co-respondents or co-claimants in the constitution of the tribunal	62
3.1.2 Effective interpretation of multiparty arbitration clauses	63
3. 2. Third-party mechanisms in arbitration rules and laws.....	64

CHAPTER 3: THIRD-PARTY MECHANISMS

3.1 THIRD-PARTY MECHANISMS AND CONSENT

There is a plethora of legal discourse and case law relating to third party mechanisms, particularly consolidation, in the context of international arbitration.¹ The prevailing view as taken by the majority of the authorities is that third-party mechanisms are not applicable to arbitration.² This view is generally based on two arguments.

¹ See I. Dore, *Theory and Practice of Multiparty Commercial Arbitration*, (Graham & Trotman/Marinus Nijhoff London/Dordrecht/Boston 1990); Multiparty Arbitration, ICC (ed.) (1991); G. Bernini, *Arbitration in Multi-Party Business Disputes*, in *Yearbook Commercial Arbitration* (Kluwer Deventer 1980) p.291; Commission on International Arbitration, Final Report on Multiparty Arbitrations, Paris, June 1994, by the Working Group under the Chairmanship of M. Jean-Louis Delvolvé, in (1995) 6 *ICC Bull.* 26 (“Delvolvé Report”); G.A. Born, *International Commercial Arbitration*, (Kluwer Law International 2nd ed. 2001), chapter 10; P. Level “Joinder of Proceedings, Intervention of Third Parties, and Additional Claims and Counterclaims”, (1996) 7(2) *ICC Bull.* 38; P. Fouchard, *Multi-Party Business Disputes*, Institute of International Business Law and Practice, ICC Doc. No. 359, 1980, p.57; F. Nicklisch, “Multi-Party Arbitration and Dispute Resolution in Major Industrial Projects”, (1994) 11(4) *J.Int.Arb.* 57; M. Platte “When Should an Arbitrator Join Cases?” (2002) 18 *Arb.Int* 67; V.V.Veeder “Muplti-party disputes: Consolidation under English Law; *The Vimeira- a Sad Forensic Fable*”, (1986) *Arb.Int.* 310, S. Strong, “Intervention And Joinder As Of Right In International Arbitration: An infringement Of Individual Contract Rights Or A Proper Equitable Measure?” (1998) 31 *Vand.J.Transnat'l.L.* 915, T. Stipanowich, “Arbitration and the Multiparty Dispute: The Search for Workable Solutions”, (1987) 72 *Iowa L. Rev.* 473; A. Mourre, “L’intervention des Tiers à l’Arbitrage”, (2000-2002) *Les cahiers de l’arbitrage, Recueil*, Vol. I, 100.

² Bernini, *ibid*, p.295; Devolve Report, *ibid*, para 5; J. Lew, L. Mistelis and S. Kroell, *Comparative International Commercial Arbitration*, (Kluwer London 2003), para 16-74; G.A. Born, *International Commercial Arbitration*, (Kluwer Law International 2nd ed. 2001), chapter 10; Fouchard *idem*; Nicklisch *idem*; A. Redfern and M. Hunter, *Law and Practice of International Commercial Arbitration*, by N. Blackaby and C. Partasides (eds) (Kluwer Arbitration Law 2004) at 3-73., E. Gaillard, *Pré-rapport sur l’arbitrage multi-partite et la consolidation de procédures arbitrales connexes*, The International Law Association Report of the Sixty-Third Conference, Warsaw, 1988, p. 480; R. Wallace, “Consolidated Arbitration in the US: Recent authority requires consent of the parties”, (1993), 10(4) *J.Int'l Arb.*, p.5; Leboulanger, “Multi-Contract Arbitration”, (1996) 13(4) *J.Int.Arb.* 43; Platte *supra* p.77; M. de Boisseson, *Le droit francais de l’arbitrage interne et international*, (G.L.N 1990) p.264 ; E. Loquin, « Arbitrage et cuationnement », *Rev Arb.* 1994 p. 247.

The principal argument relates to the contractual character of international arbitration. The principle of arbitration's contractual character has acquired among scholars the status of a sacred doctrine, which would forbid any third-party involvement in the exclusively bilateral arbitration process, unless all relevant parties have consented thereto either expressly³ or impliedly.⁴

The second argument emphasises the practical problems that usually result from the participation of third parties in arbitration proceedings. Third-party mechanisms will, normally, make arbitral proceedings more complicated, which in turn will make arbitration more expensive and time-consuming.⁵ Issues concerning confidentiality⁶ or, even, the payment of the arbitrators⁷ will also arise when third parties intervene in arbitration. Therefore, the prevailing contractual view is that a person not bound by an arbitration agreement, i.e. a third party, cannot participate into the arbitration process.

If the parties want the application of third-party mechanisms to their arbitration resulting to multiparty proceedings they have to provide for them in the arbitration agreement. The principle of procedural party autonomy gives the parties the freedom to design multiparty proceedings specifically designed to accommodate the particular

For case-law, see in France: Cour d'Appel de Paris, December 19, 1986 *O.I.A.E.T.I v Sofidid*, (1987) Rev.Arb. 93; Cass., Nov. 8, 1982, *Société Burmeister et Wain Engineering Cie. Lit. v. Société Ceusot Loire et al.*, (1984) *Clunet* 151.

In England: *Oxford Shipping v Nippon Yusen Kaisha*, [1984] 3 All E.R.835; *Abu Dhabi Gas Liquefaction [ADGAS] v Eastern Bechtel*, [1982] 2 Lloyd's Rep. 425, where the courts opted for a concurrent hearings rather than consolidation, see at 1061 where Watkins LJ noted that the consolidation would be "the ideal solution" but concluded that such a solution was impossible in the absence of the parties' consent.

In the US see, indicatively, *United Kingdom v Boeing*, 998 F.2d 68, 74 (2nd Cir. 1993); *American Centennial v National Cas.*, 951 F.2d 107, 108 (6th Cir. 1991); *Baesler v Continental Grain*, 900 F.2d 1193, 1195 (8th Cir. 1990); *Del E. Webb Constr. v Richardson Hosp. Auth.*, 823 F.2d 145, 150 (5th Cir. 1987); *Weyerhaeuser v Western Seas Shipping*, 743 F.2d 635, 637 (9th Cir. 1984).

³ Stipulated in a multiparty arbitration agreement, binding all the several parties or expressly provided in the several arbitration agreements with cross-references. On some occasions, there may be an *ad hoc* agreement between the original parties and the third party providing for participatory rights (see Merkin, *supra*, para 15-1 and *Hoesch Export v Hansa Projekt Transport (The World Umpire)* [1990] 1 Lloyd's 374.

⁴ Implicit consent may usually be inferred in case of several contracts with 'back-to-back' arbitration clauses providing for arbitrations with identical characteristics. If the several arbitration clauses differ in their main terms, for example they provide for different institutions or different applicable law, implicit consent will be impossible to be inferred there even if the several contracts are inextricably intertwined or even have a uniform economic character, see Berger, *International Economic Arbitration*, (Kluwer 1993) p. 295; Platte, *supra* n.1, p.71; Nicklish, *supra* n. 1, p. 60 and 71.

⁵ M. Schwartz, "Multiparty Disputes and Consolidated Arbitrations: An Oxymoron or the Solution to a Continuing Dilemma?" (1990) 22 *Case.W.Res.J.Int'l L.* p.341 Nicklish, *supra* n. 74, p.64.

⁶ See *Oxford Shipping v Nippon Yusen Kaisha*, [1984] 3 All E.R.835; also M. Collins, "Privacy and Confidentiality in Arbitration Proceedings", (1995) 30 *Tex.Int'l.L.J.* 121; Nicklish *supra* n.1, p.69.

⁷ See Strong *supra* n. 1, p.931.

needs of their commercial agreement. Thus, the several parties may incorporate multiparty dispute resolution clauses in the several contracts, conferring jurisdiction over the several parties on a single arbitral tribunal. In this regard, the parties have the exclusive discretion to provide for the application of third-party mechanisms, be that consolidation or intervention or joinder. This is a well-established right of the parties particularly in the context of international business transactions and, accordingly, courts and arbitral tribunals must honour parties' preference to multiparty proceedings.

The case where the several parties provide for multiparty proceedings in their arbitration agreement is a clear-cut case of multiparty arbitration and should not raise any difficult issues. Whether or not several parties have consented to multiparty proceedings, in these cases, is a matter of interpretation of the relevant arbitration agreements. Strictly speaking, when several parties conclude multiparty arbitration agreements, all the several parties are genuine rather than third parties. Therefore, the thesis will not examine in detail the matter of multiparty arbitration agreements. It is for the sake of completion, that the next two sessions will briefly look into two issues that often arise in the context of dispute resolution clauses providing for multiparty proceedings: first, the issue of equal treatment of the several co-respondents or co-claimants in the constitution of the tribunal and, second, the issue of effective interpretation of these clauses.

3.1.1 Equal treatment of the several co-respondents or co-claimants in the constitution of the tribunal

The issue of equal treatment of the several parties in the constitution of the tribunal has been the subject matter of an exhaustive discussion in literature, particularly in the last decade.⁸ The well-known decision of the French Cour de cassation in the *Siemens AG v Dutco Construction Co.* case⁹ laid down the theoretical premises of the discussion. It should be briefly reminded that in Dutco, upon threats by the ICC Court to appoint an arbitrator on behalf of the several respondents, the latter jointly nominated an arbitrator. At the same time, however, they reserved their right to challenge the appointment procedure. The two co-respondents argued that their interests in the particular case were conflicting and, therefore, each one of them

⁸ See indicatively Platte *supra* n.1, Lew-Mistelis-Kroell, *supra* n.2 para 16-11 et seq.

⁹ Cass. (France) 7.1.1992, [1994] *ADRLJ* 36.

should have been given the right to appoint its own arbitrator. The highest court of France held that the appointment procedure had violated the principle of equality of the parties in the appointment of arbitrators, which is a matter of public policy. Thus, the Cour de cassation disapproved of ICC's practice under its previous rules to allow for one side to choose its own arbitrator while obliging the other party to agree on a single arbitrator despite their conflicting interests. The Dutco dictum was not unanimously acclaimed. There have been voices of concern, noting that it is not always workable to provide every party involved in a multiparty arbitration with the right to appoint its own arbitrator.¹⁰ Nonetheless, the principles set out by the French Cour de cassation have been in general accepted by the arbitration community. As has rightly been observed: "the French Cour de cassation simply requires that all the parties should have the same rights with regard to the appointment of the arbitrators, not that they should all have a right to appoint "their" arbitrator".¹¹

Accordingly, many arbitration institutions modified their rules in accordance with the Dutco principles, providing at the same time for a more workable solution. In particular, the new arbitration rules give the multiple claimants and respondents the opportunity to nominate a single arbitrator, but in case they fail to do so, the institution will appoint the tribunal on behalf of both the sides.¹² This solution is in general considered the best possible compromise in the delicate issue of the equal treatment of the several parties in the appointment of arbitrators.¹³

3.1.2 Effective interpretation of multiparty arbitration clauses

As regards the issue of the effective interpretation of the multiparty arbitration clauses the following notes should be made. In practice, the parties often fail to draft clear dispute resolution clauses, explicitly providing for multiparty proceedings. Thus, very often the several parties instead of concluding one multilateral arbitration agreement will conclude several bilateral contracts, containing bilateral arbitration clauses, with no cross-references. In such cases, it is difficult to infer multilateral

¹⁰ Lew-Mistelis-Kroell, *supra* n. 2, para 16-12; also Redfern and Hunter, *supra* n.2 para 3-71; B. Hanotiau, *Complex Arbitrations, Multiparty, Multi-contract, Multi-issue and Class Actions*, (Kluwer Law International 2005) para 443 et seq; E. Schwartz, "Multi-Party Arbitration and the ICC: In the Wake of Dutco" in (1993) 10 *J.Int.Arb.* p.16.

¹¹ P. Fouchard, E. Galliard and B. Goldman, *On International Commercial Arbitration*, E. Gaillard and J. Savage (eds.) (Kluwer Law International 1999) para 792.

¹² ICC art.10, LCIA art.8, Swiss Rules art. 8 paras 3-5, AAA-ICDR art. 6.

¹³ See Hanotiau, *supra* n.10, para 444: "it seems that in general, all situations of this type have managed to find an appropriate solution, through discussion with the parties".

consent for multiparty arbitration proceedings, even if the several contracts are drafted in view of the same commercial project, and the arbitration clauses are drafted in identical terms.¹⁴

Whenever the contractual provisions of the parties are ambiguous or unclear, the courts will normally apply general contract interpretation principles to lift the ambiguity and give effect to the agreement of the parties. Thus, provided that the clauses are otherwise valid in terms of form and substance, courts and tribunals will favour an effective interpretation, which accords with the obvious commercial purpose of the agreement.¹⁵

3. 2. THIRD-PARTY MECHANISMS IN ARBITRATION RULES AND LAWS

Even if the parties have failed to provide for multiparty proceedings in their arbitration agreements, third-party mechanisms may still apply by reference to the applicable *lex arbitri*. This section gives a brief overview of the arbitration rules and laws regarding third-party mechanisms. As will be shown, the vast majority of the arbitration rules and the national laws adhere to the prevailing contractual approach providing that third-party mechanisms, such as joinder or consolidation, may not apply to arbitration unless all the relevant parties have given their consented thereto.

Starting from the arbitration rules, there are only few of them providing for third-party mechanisms. In general, the majority of the arbitration rules leave the exclusive decision on such a delicate issue to the parties. For example, no relevant provision is

¹⁴ Nicklisch, *supra* n. 2, at p. 71; *contra* Platte, *supra* n.1, p. 68 et seq.

¹⁵ See for example *Antaios Compania Naviera v Salen Rederierna* [1985] AC 191 at 201; *Manai Investments v Eagle Star* [1997] AC 749 at 771; *Siruis International Insurance Company v FAI General Insurance Limited* [2004] UKHL 54.

found in the ICC,¹⁶ the AAA ICDR,¹⁷ the UNCITRAL Rules,¹⁸ the Stockholm Chamber of Commerce Arbitration Rules (2007),¹⁹ or the CIETAC Rules.²⁰

When arbitration rules expressly provide for third-party mechanisms, they usually require consent of all the relevant parties (genuine and third ones). This is, for example, the case with the Vienna Rules²¹ or the Netherlands Arbitration Institute rules.²²

There are only a few exceptions to the principle requiring consent of all the relevant parties for the application of third-party mechanisms. For example, in some institutional rules, such as the LCIA, the CEPANI or the Swiss Rules, consent of all the parties is not required for the consolidation of two pending arbitrations between several parties, or the joinder of a third party. In these cases, the decision for the consolidation or the joinder is entrusted either to the arbitral tribunal or the administration body.²³ This “interventionist approach” is more frequent in arbitration

¹⁶ ICC art.10 refers only to the constitution of the arbitral tribunal in a case where there are multiple claimants or respondents. This provision was inserted after the *Dutco* case in order to preserve the equal treatment of the several parties in nominating the party-appointed arbitrator, see above n.10.

¹⁷ The policy of the American Arbitration Association is to permit consolidation of proceedings only in cases in which all parties agree thereto, or a court orders consolidation (Consolidation of Arbitration Proceedings, Lawyers’ Arbitration Letter no.37, American Arbitration Association); *cf* Strong, *supra* n.1: p. 932: “The AAA’s experience has been that joinder is more likely in vertical disputes (such as those involving an owner, a general contractor, and a subcontractor) than in horizontal disputes (such as those involving an owner, a contractor, and an architect).”

¹⁸ The drafters of UNCITRAL Rules as of UNCITRAL Model law thought it best to avoid dealing with the issue of participatory rights and leave it to party autonomy; see in general (in the context of UNCITRAL Model law) the First Working Group Report A/CN.9/216 para. 37.

¹⁹ Art.13(4) is a similar provision to ICC art.10 referring to the constitution of the tribunal, see note above, whereas art.11 is on consolidation of several claims between the same parties.

²⁰ Art.24 is also similar to ICC art.10.

²¹ Art.10. Vienna rules will also permit joinder in cases where the substantive applicable law “positively provides that the claim is to be directed against several persons” (art.10(1)(a)). For more detail on the importance of the substantive applicable law on application of the participatory mechanisms see below Chapter 6.

²² Art.41.

²³ For example see LCIA art.22.1(h) where the tribunal will decide, upon the application of a real party whether a third party will be joined in the arbitration. LCIA require only the consent of the applicant and the third party, but not the consent of the other real party.

In the CEPANI Rules art.12, the decision on consolidation, at the request of a party or the tribunal or upon the CEPANI’s own motion, will be taken by the CEPANI’s appointment committee or the chairman of the tribunal.

In the Swiss Rules the decision for consolidation of two proceeding is taken by the administrative body (Chambers) (art.4(1)), whereas the decision for intervention or joinder is taken by the arbitral tribunal (art.4(2)).

In the Japanese Commercial Arbitration Association Rules, the participation of a third party in pending arbitration proceedings requires the consent of the parties to the arbitration (r.43). For multiple related claims to be consolidated in the absence of the written consent of all the relevant parties, it is required that the administration of the arbitral tribunal determines that consolidation is

rules related to specific industries, such as construction,²⁴ commodities,²⁵ securities²⁶ or maritime.²⁷

National arbitration laws also opt for party autonomy, the majority of which avoids to include any fall back provisions, let alone any mandatory ones, providing for third-party mechanisms. Indeed, no relevant provisions can be found in the US Federal Arbitration Act,²⁸ the Swiss PILA, the French NCCP, the German ZPO or the Model Law.²⁹

Even when national laws expressly provide for third-party mechanisms, they usually take the contractual approach, requiring the agreement of all the parties, original and third, to multiparty proceedings. This is the legislative model followed for example by the EAA,³⁰ and the Belgian Judicial Code,³¹ where the final decision on the application of the joinder or intervention needs to be taken by the tribunal. Some other national laws empower the national courts rather than the tribunal to

necessary (r.44). Consent is not required only when the multiple requests for arbitration come out of the same agreement.

²⁴ For example, the AAA Construction Industry Arbitration Rules and Mediation Procedures (Including Procedures for Large, Complex Construction Disputes) R-7 (consolidation) or the AAA New Jersey Residential Construction Lien Arbitration Rules, s.5. (Joinder).

²⁵ For example, the US National Grain and Feed Association, s.5 (f)-(e).

²⁶ For example, the AAA Supplementary Procedures for Securities Arbitration s.2 or the NASD Uniform Code of Arbitration s.10314(d) or the New York Stock Exchange Arbitration Rules s.612(d).

²⁷ For example, the London Maritime Arbitration Association, s.14(b)(concurrent proceedings) or the Society of Maritime Arbitrators (NY) Arbitration Rules, s.2 (consolidation).

²⁸ S.4, which authorises actions to compel arbitration, does not grant a court the authority to consolidate proceedings unless the arbitration agreement provides for consolidation (*Glencore v Schnitzer Steel Products*, 189 F.3d 264 (2d Cir.1999)); cf however, *Robinson v Warner*, 370 F.Supp.828 (D.R.I. 1974), ordering the consolidation of two AAA arbitrations between an owner and a contractor, on the one hand, and the same owner and the architect on the other, pursuant to s.4 FAA.

²⁹ For the reasons see the First Working Group Report A/CN.9/216 para37 (*supra* n); cf also Dore, *supra*, n.1 chapter 3 for an extensive analysis of the multiparty issues in the UNCITRAL context in general.

³⁰ S.35: consolidation or concurrent hearings between two arbitral proceedings on the agreement of all parties involved therein. The Advisory Committee on the EAA rejected a proposal to include provisions for a court-ordered compulsory consolidation: "In our view it would amount to a negation of the principle of party autonomy to give the tribunal or the Court power to order consolidation or concurrent hearings. Indeed it would to our minds go far towards frustrating the agreement of the parties to have their own tribunal for their own disputes. Further difficulties could well arise, such as the disclosure of documents from one arbitration to another. Accordingly we would be opposed to giving the tribunal or the Court this power. However, if the parties agree to invest the tribunal with such a power, then we would have no objection" (Report on the Arbitration Bill by the Departmental Advisory Committee on Arbitration Law, February 1996, para.180).

³¹ Art.1696(bis) provides for intervention and joinder on the basis of first a new arbitration agreement between the third party and the real ones, and second the unanimous consent of the arbitral tribunal. Consensus of all the relevant parties is required also by the Netherlands Code of Civil Procedure art.1045 for joinder or intervention of a third party.

decide whether a third party will take part in the arbitration proceedings, although they still require the consent of the all relevant parties as an indispensable condition.³²

Only as a rare exception arbitration laws deviate from the contractual approach, and provide for compulsory third-party mechanisms ordered exclusively by national courts, even without the unanimous consent of the relevant parties. The classic example here is the Netherlands Code of Civil Procedure art.1046,³³ which provides for compulsory consolidation to be ordered by the President of the Amsterdam District Court.³⁴

Finally, an interesting approach is taken by the New Italian Arbitration Law: echoing analogous provisions in Italian litigation proceedings, art. 816 *quinquies* distinguishes between “voluntary intervention or joining” of a third party, which will be admissible only with the agreement of the third party and the original parties with the arbitrators’ consent, and the intervention or joining of a third party who is considered to “be necessary by law” (*litisconsorzio necessario*), which will always be admissible, irrespective of the consent of the original parties to the arbitration proceedings.

³² For example, Utah Code Ann.s.78-31a-9; California s.1297.272; Canada, British Columbia s.21; Texas s.172.173.

³³ This provision was enacted to accommodate the construction industry in Netherlands. The latter, however, has not been entirely satisfied with the final result and the way art.1046 has been applied in practice, see Jacomijn van Haersolte-van Hof, “Consolidation under the English Arbitration Act 1996: A view from the Netherlands”, (1997) 13 *Arb. Int.* p. 427.

³⁴ Similar provisions can be found in HK Arbitration Ordinance s.6.B (consolidation or concurrent hearings) and s.7 (interpleading) both applicable for domestic arbitrations; New Zealand Arbitration Act s.2 (Second Schedule); Australia, Queensland s.26; see also the US Revised Uniform Arbitration Act s.10 (however, in case the arbitration agreement expressly prohibits consolidation, the court would have no power to violate the agreement, s.10(c)); and a number of US national state laws: Washington RCW s.7.04A.100 (consolidation); Georgia arbitration code: 9-9-6(e) (consolidation); Alaska AS 09.43.370 (consolidation); South Carolina S.C. Code Ann. s.15-48-60 (joinder).

CHAPTER 4: EXTENSION DOCTRINES- THE DOCTRINE OF *EQUITABLE ESTOPPEL*68

4.1 general Overview of the doctrine	68
4.2 Commentary on the doctrine: content and conditions of application.....	70
4.2.1 The application of the doctrine presupposes a thorough analysis of the dispute and its factual circumstances	70
4.2.2 Moving away from its equitable origins: the “intertwined factor” and the conditions for the application of the doctrine	70
4.2.2.1 First, the dispute between the signatory and the non-signatory party must be intertwined with the contract between the signatories	73
4.2.2.2 Second, the non-signatory party must have close contractual or corporate links with one of the signatory parties.....	77
4.2.2.3 Concluding remarks on the intertwined version of the equitable doctrine	79
4.2.3 Equitable estoppel doctrine and consensual origins of arbitration	80
4.2.4 The court rather than the tribunal will determine whether the dispute between the signatory and the non-signatory party is arbitrable or not.....	82

CHAPTER 4: EXTENSION DOCTRINES- THE DOCTRINE OF *EQUITABLE ESTOPPEL*

4.1 GENERAL OVERVIEW OF THE DOCTRINE

The doctrine of equitable estoppel in its traditional meaning reflects the general legal principle of *non-venire contra factum proprium*, found in Roman Law and known in many contemporary civil law jurisdictions.¹ According to the doctrine, a party is prevented from asserting rights against another party, when the latter justifiably relied on the conduct of the former and changed his position to his detriment as a result of such reliance.² The principle, as its name indicates, has an equitable character, which makes it difficult to delineate.³

In arbitration the doctrine has developed a specific meaning applicable to non-signatories in the context of jurisdictionally fragmented multiparty projects with

¹ E. Gaillard, “L’interdiction de se contredire au détriment d’autrui comme principe général au droit du commerce international”. (1985) *Rev. Arb.*, p. 241; Cf also B. Hanotiau, *Complex Arbitrations: Multiparty, Multi-contract, Multi-issue and Class Actions*, (Kluwer International 2005) para.41, who notes that the equitable estoppel doctrine is primarily an Anglo-American concept which will rarely apply *per se* in a commercial arbitration in a truly international context, let alone in Continental Europe.

² See *First Union Commercial v Nelson, Mullins, Riley & Scarborough (In re Varat)* 81 F.3d 1310, (4th Cir.1996) at 1317; and *Lowery v Stovall*, 92 F.3d 219 (4th Cir.1996) at 223.

³ *Grigson v Creative Artists Agency*, 210 F.3d 524, 527 (5th Cir.2000), per J Dennis (dissenting): “[N]early anything can be called estoppel. When a lawyer or a judge does not know what other name to give for his decision to decide a case in a certain way, he says there is an estoppel”

regard to construction works,⁴ secured agreements,⁵ or string sales contracts.⁶ Thus, the US courts have repeatedly estopped signatory parties to arbitration agreements from initiating court proceedings against non-signatory parties, ordering signatories submit their dispute with the non-signatories to arbitration. In the majority of the case the doctrine has been employed by the US courts to estop the *signatory party* “from avoiding arbitration with a non-signatory.”⁷ However, on various occasions the doctrine has equally been applied to estop the non-signatory *party from avoiding arbitration with the signatory party*.⁸

⁴ This was the case, for example, in *Hughes Masonry v Greater Clark County School Bldg*, 659 F.2d 836 (7th Cir. 1981); *McBro Planning & Development Co v Triangle Electronic Construction*, 741 F.2d 342, 343 (11th Cir. 1984); *Smith/Enron Cogeneration v Smith Cogeneration Int'l*, 198 F.3d 88 (2d Cir. 1999).

⁵ For example in *Choctaw Generation v American Home Assurance*, 271 F.3d 403 (2nd Circ.2001) or in *Ex Parte Napier*, 659 F.2d 836 (7th Cir.1981).

⁶ *International Paper v Schwabedissen Maschinen & Anlagen GmbH*, 206 F.3d 411 (4th Circ. 2000).

⁷ *Smith/Enron Cogeneration v Smith Cogeneration Int'l*, *supra* n. 4, at 98; *Thomson-CSF v American Arbitration Ass'n*, 64 F.3d 773 (2d Cir. 1995) at 779; *Choctaw Generation v American Home Assurance*, *supra* n. 5.

The US case law with regard to equitable estoppel doctrine has caused extensive discussion on the issue, particularly in the last decade. See, for example, B. Hanotiau, *Complex Arbitrations*, *supra* n. 1, para 41 et seq.; J.M. Townsend, “Non-Signatories in International Arbitration: an American Perspective”, in *International Arbitration 2006: Back to Basics?*, ICCA International Arbitration Congress (Kluwer Law International 2007); Williston, *On Contracts*, (ed Richard Lord) 4th Ed, (West Group 2001), Ch. 57:19; J. Douglas Uloth -J. Hamilton Rial, “Equitable Estoppel As A Basis For Compelling Nonsignatories To Arbitrate: A Bridge Too Far?” (2002) 21 *Rev. Litig.*, p. 593; J. Douglas Uloth -J. Hamilton Rial, “Enforcing Arbitration Against Nonsignatories” (2002) 65 *Tex. B.J.*, p. 802; H. Warren Knight et al., *Arbitration By and Against Nonsignatories*, in *California Practice Guide: Alternative Dispute Resolution*, (1998) paras 5:261-5:288; Jeff DeArman, “Resolving Arbitration's Nonsignatory Issue: A Critical Analysis of the Application of Equitable Estoppel in Alabama Courts”, (1998-1999) 29 *Cumb.L.Rev.*, p. 645; Dileo, “The Enforceability Of Arbitration Agreements By And Against Nonsignatories” (2003) 2 *Journal of American Arbitration*, p. 31; Charles Lee Eisen, “What Arbitration Agreement? Compelling Non-Signatories To Arbitrate” (2001) 56 *Disp. Resol. J.*, p. 40.

⁸ See for example *Denney v BDO Seidman*, 412 F.3d 58 (2nd Cir 2005); *International Paper v Schwabedissen Maschinen & Anlagen GmbH*, *supra* n. 6; *American Bureau of Shipping v Tencara Shipyard S.P.A.*, 170 F.3d 349, 353 (2nd Cir. 1999); *In re Weekley Homes*, 180 S.W.3d 127, (S.C Tex. 2005); *Carlin v 3V*, 928 S.W.2d 291, 296 (Tex. App.1996) and *Merrill Lynch, Pierce, Fenner & Smith v Eddings* 838 S.W.2d 874 (Tex. App.1992); *Matter of VMS*, 26 F.3d 50, 52 (7th Cir. 1994); *Deloitte Noraudit A/S v Deloitte Haskins & Sells*, F.3d 1060, 1064 (2d Cir. 1993); *Amkor Tech. v Alcatel Business Systems*, 278 F.Supp.2d 519 (E.D.PA.2003); *Nova Hutt A/S v Kaiser Group Int'l*, 307 B.R.449 (Del. 2004); *E.I. DuPont de Nemours v Rhone Poulenc Fiber & Resin Intermediates, S.A.S.*, 269 F.3d 187, 200 n.7 (3d Cir. 2001). *Cf* the wording in *Jones v Genus Credit*, 353 F.Supp.2d 598 (U.S.D.C. Maryland 2005), at 602:

“The law is clear that a non-signatory to an arbitration agreement may enforce (or be bound by) the agreement’s terms where the claims against the signatory and the non-signatory are based on the same facts and are inherently inseparable.” (emphasis added).

Cf also *Griffin v Beach Club II Homeowners Association*, 384 F.3d 157 (4th Cir 2004), where a real party tried to compel a third party to arbitrate (motion denied on other grounds). *Contra Thomson-CFS v American Arbitration Association*, *supra* n. 7, where the Court rejected the application of the doctrine to third parties.

4.2 COMMENTARY ON THE DOCTRINE: CONTENT AND CONDITIONS OF APPLICATION

The following observations should be made regarding the content of the doctrine as well as its conditions of application

4.2.1 The application of the doctrine presupposes a thorough analysis of the dispute and its factual circumstances

Courts in order to apply the doctrine must first carefully examine the rights and duties arising out of the interrelated contracts between the several parties. This examination under the equitable estoppel theory must be particularly thorough by comparison with the usual fact-finding analysis. In *Choctaw Generation v American Home Assurance*,⁹ for example, the Second Circuit noted characteristically:

“We carefully reviewed the relationship among the parties, the contracts they signed (or did not), and the issues that had arisen, to arrive at the conclusion that the controversy was arbitrable” [...] “The tight relatedness of the parties, contracts and controversies is easily demonstrated by a (necessarily tedious) review of the contract terms in dispute between and among the parties, and the parties' competing analyses of them.”¹⁰

Similarly in *Ex parte Isbell*, the court stressed that:

“Any case coming before this Court that involves the right of non-signatories to compel arbitration will [...] be peculiarly fact-specific and will require a penetrating analysis of the facts and an application of traditional contract principles”¹¹

4.2.2 Moving away from its equitable origins: the “intertwined factor” and the conditions for the application of the doctrine

As was indicated, the estoppel doctrine has equitable roots. Applied in its traditional meaning, the doctrine would prevent a party that has gained a *direct benefit* from a contract including an arbitration clause from avoiding arbitration. As courts have emphasised:

⁹ 271 F.3d 403 (2nd Circ. 2001).

¹⁰ *Ibid* at 406.

¹¹ 708 So. 2d at 577-78 (Ala.1997).

“To allow [a plaintiff] to claim the benefit of the contract and simultaneously avoid its burdens would both disregard equity and contravene the purposes underlying enactment of the Arbitration Act.”¹²

The US courts have several times applied the doctrine on this equitable basis. For example, in *Deloitte Noraudit A/S v Deloitte Haskins & Sells*,¹³ a Norwegian accounting firm was estopped from denying its obligation to arbitrate under an arbitration clause included in a memorandum agreement, which the firm had not signed, when the firm had accepted the benefits of the Agreement through its continuing use of IP rights, namely the name of the firm.

Likewise, in *American Bureau of Shipping v Tencara Shipyard*,¹⁴ the doctrine was applied to estop yacht owners (non-signatories) from refusing to arbitrate under an arbitration clause in a contract between the yacht’s builder and a ship classification society (signatories), when the yacht owners had received lower insurance rates and has acquired the ability to sail under the French flag due to the contract.

Equitable considerations also underpinned *International Paper v Schwabedissen Maschinen & Anlagen GmbH*.¹⁵ Here the buyer of industrial saw was precluded from asserting that, as non-signatory party, it was not bound by the arbitration clause included in the contract for the sale of the saw between distributor and manufacturer, when the buyer’s claims against manufacturer were based on and arose out of that contract. The Court noted that:

“A non-signatory is equitably estopped from refusing to comply with an arbitration clause when it receives a direct benefit from a contract containing an arbitration clause”¹⁶

However, on many other occasions, the US courts have given the doctrine a dynamic meaning, which seems to have diverged from its traditional equitable origins. In this context, the courts have attached less importance to whether the party avoiding the arbitration agreement has gained a *direct benefit* from a contract including the arbitration clause, and more importance to two other factors:

¹² *Avila Group, Inc. v Norma J. of California*, 426 F.Supp. 537, 542 (S.D.N.Y.1977) (also cited in *International Paper*, *supra* n. 6); *Cf Tepper Realty v Mosaic Tile*, 259 F. Supp. 688, (S.D.N.Y.1966) at 692: “In short, [plaintiff] cannot have it both ways. [It] cannot rely on the contract when it works to its advantage, and repudiate it when it works to [its] disadvantage”.

¹³ 9F.3d 1060 (2d Cir. 1993).

¹⁴ 170 F.3d 349 (2nd Cir. 1999).

¹⁵ 206 F.3d 411 (4th Cir. 2000). *Cf also Ex parte Isbell*, 708 So.2d 571 (Ala.1997).

¹⁶ *Ibid* At 418: “A non-signatory is equitably estopped from refusing to comply with an arbitration clause when it receives a direct benefit from a contract containing an arbitration clause.

- First, the degree to which the *dispute* between the non-signatory and the signatory party is *intertwined* with the contract between the two signatories
- Second, the degree to which the non-signatory is *interrelated* to the signatory parties

Here, the courts have given emphasis to the “intertwined” factors, rather than to equitable considerations. In fact, there have been cases where the courts have made no reference to the term “equitable estoppel” at all.¹⁷ Instead the “intertwined factor” has evolved as the decisive criterion for determining whether a signatory to a bilateral arbitration agreement must arbitrate with a party that has never consented to this arbitration agreement.¹⁸

In detail, the two key-elements under the intertwined version of the estoppel doctrine are:

¹⁷ No reference to “equitable estoppel” is found in *Choctaw Generation v American Home Assurance*, *supra* n. 5; *McBro Planning & Development Co v Triangle Electronic Construction*, *supra* n. 4; *Ex Parte Napier*, *supra* n. 5; *Denney v BDO Seidman*, *supra* n. 8.

¹⁸ It seems that the key-phrase “intertwined with the underlying contract obligations” was first added to the traditional equitable estoppel doctrine by the Seventh Circuit in *Hughes*. The Court in this case basically applied equitable considerations, and it is not clear whether it was in its intention to expand the doctrine (J. Douglas Uloth -J. Hamilton Rial, argue in the negative, *supra* n. 7, p. 609). In any event, this phrase was used in *McBro Planning Development v Triangle Electrical Construction*, *supra* n. 4 applied in *J.J. Ryan & Sons v Rhone Poulenc Textile*, 863 F.2d 315 (4th Cir.1988); and *Smith/Enron Cogeneration v Smith Cogeneration International*, 198 F.3d 88 (2nd Cir. 1999) and finally achieved full recognition in *Choctaw Generation v American Home Assurance*, *supra* n. 5271 F.3d 403 (2nd Cir.2001).

The existence of a different kind of estoppel theory than the traditional equitable one is also recognized in *Thomson*, where after referring to the equitable estoppel, the Court referred to the theory of intertwined contracts noting, that “Several courts of appeal have recognized an *alternative estoppel theory* requiring arbitration between a signatory and nonsignatory”, *supra* n 7, at 779. It continues: “As these cases indicate, the circuits have been willing to estop a signatory from avoiding arbitration with a nonsignatory when *the issues the nonsignatory is seeking to resolve in arbitration are intertwined with the agreement that the estopped party has signed*” (emphasis added). However, at the end, the Court in *Thomson* rejected that theory “‘close relationship’ and ‘intimate []’ factual connection provide no independent basis to require a nonsignatory of an arbitration agreement to arbitrate with a signatory, and therefore that a nonsignatory cannot be bound without receiving a ‘direct benefit’ from or pursuing a ‘claim [...] integrally related to the contract containing the arbitration clause.’” *Thomson-CSF*, 64 F.3d at 778-80.

The same approach can be found in *Fluor Daniel Intercontinental v General Electric*, (1999) WL 637236 (S.D.N.Y.), at 5-6.

International Paper, *supra* n. 6 also refers to the intertwined theory as opposed to the traditional equitable estoppel theory, but it avoided examining the issue any further (although applied the equitable benefit recognizes the existence of the intertwined relationships). See 418 n.6.

Cf J. Douglas Uloth -J. Hamilton Rial, *supra* n. 7, p. 611: “as courts later began to focus on the Seventh Circuit’s use of the phrase ‘intertwined with the underlying contract obligations’, a new ‘intertwined claims’ equitable estoppel theory was born”.

4.2.2.1 *First, the dispute between the signatory and the non-signatory party must be intertwined with the contract between the signatories*

Here, the courts will examine the dispute between the non-signatory and the signatory party in the light of the contract between the signatories, which includes the arbitration agreement.

For example, in *Choctaw Generation v American Home Assurance*, a construction company had entered into a series of contracts with the owner, under which the contractor had to provide engineering and construction services, the performance of which were secured by a letter of credit provided by a surety company. An arbitration agreement was included in the construction contract between the owner and the contractor, whereas the letter of credit (the security contract) had no arbitration agreement. The Second Circuit found that the dispute between the surety and the owner was strongly intertwined with the underlying construction contract since it

“concerns the duty to replenish a letter of credit maintained under the Construction Contract, and requires a ruling as to whether that duty is independent of certain others in the context of the Construction Contract as a whole”¹⁹

The court also held that:

“The underlying dispute between [the contractor] and [the owner], concerning [the owner’s] entitlement to liquidated damages, is now in the early stages of arbitration, and *entails the construing of a dozen provisions of the Construction Contract*. The immediate dispute in this action between [the owner] and [the surety], concerning whether [the owner] can compel immediate replenishment of the letter of credit to fund the liquidated damages, *turns upon many of the same provisions*”²⁰

The Court, therefore, concluded that:

“The controversy presented on this appeal [between the owner and the surety] is linked textually to the Construction Contract, and its merits are bound up with the dispute now being arbitrated between [the owner] and [the contractor]”²¹

¹⁹ *Choctaw*, *supra* n. 5, at 406.

²⁰ *Idem*.

²¹ *Ibid*, at 407.

In *McBro Planning Development v Triangle Electrical Construction*,²² a construction manager contracted with the owner of a hospital with regard to renovation work on the hospital, while an electrical engineer executed a separate agreement with the owner to perform electrical work on the same hospital. The electrical engineer filed a suit before the US courts against the construction manager, alleging that the latter had harassed and hampered its electrical work. The construction manager invoked the arbitration clause included in its contract with the owner and moved for an order to compel the electrical engineer to arbitrate with it.²³ The Eleventh Circuit, indeed, ordered the electrical engineer to arbitrate the dispute with the construction manager as it found that the rights and duties of the construction manager with regard to the construction work were entangled in the underlying contractual relationship between the owner and the electrical engineer:

“Although the contract [between the owner and the contractor] disclaims any contractual relationship between the [construction manager] and [the contractor], the general conditions of that contract are replete with references to the [manager’s] duties as construction manager, on behalf of the owner, as regards supervision of the project, for which [contractor] was a contractor. [...] *The contractor’s claims are ‘intimately founded in and intertwined with the underlying contract obligations’*” (emphasis added)²⁴

The court made extensive reference to the terms of the construction contract to illustrate the tight interrelation between the dispute in question and the underlying contract. In particular, under the contract for construction

“The construction manager would be ‘engaged to manage the construction of the Project’”

and the

“Authority to act on behalf of the Owner, and to schedule and coordinate work of contractors, to process payment applications and to reject nonconforming work, and even giving contractor reasonable veto over owner's

²² *Supra* n. 4.

²³ The contract between the electrical engineer and the owner also included an arbitration clause. The District Court had taken this arbitration clause into account as an alternative basis for compelling the engineer to arbitrate with the construction manager, see *McBro Planning v Triangle Elec. Constr.*, No. 82-C-1577-S, Memorandum of Opinion (N.D.Ala., Oct. 14, 1982).

²⁴ *Supra*, n.4, at 344.

choice of new construction manager and referring any dispute thereon to arbitration”²⁵

Hence, the Court concluded that:

“In short, the construction manager's duties on behalf of the owner are so broad that a contractor-owner contract inevitably involves a close contractor-construction manager relationship”²⁶

In *Hughes Masonry v Greater Clark County School Bldg*,²⁷ in factual and legal circumstances almost identical to those in *McBro*, the Seventh Circuit, on the one hand referred to equity principles,²⁸ but on the other focused on the close interrelation between the terms of the contractual relationships of the several parties.

More specifically, a construction manager entered into an agreement with an owner who had also concluded a contract with a masonry company with regard to the same construction project (the building of two schools). The masonry company filed an action against the construction manager for intentional and negligent interference with its contract with the owner. The construction manager invoked the arbitration clause incorporated in the contract between the owner and the masonry company and moved for an order to compel the masonry company to arbitrate its dispute with it. The Seventh Circuit referred the masonry company to arbitration with the construction company. The court noted that:

“In substance [the masonry company] is attempting to hold the [the construction manager], to the terms of the agreement [between the masonry company and the owner]”²⁹

and that the masonry company's

“complaint is fundamentally grounded in the [the construction manager's] alleged breach of the obligations assigned to it in the agreement [between the masonry company and the owner]”³⁰

²⁵ *Ibid* at 344, n.8.

²⁶ *Idem*.

²⁷ 659 F.2d 836 (7th Cir.1981).

²⁸ *Ibid*, at 839 “it would be manifestly inequitable to permit [the masonry company] to both claim that [the construction manager] is liable to [the masonry company] for its failure to perform the contractual duties described in [the owner-masonry company] agreement and at the same time deny that [the construction manager] is a party to that agreement in order to avoid arbitration of claims clearly within the ambit of the arbitration clause”.

²⁹ *Ibid*, at 838.

³⁰ *Idem*.

The Court here, as in *McBro*, referred to the underlying contract between the owner and the masonry company to demonstrate the close interrelation between the dispute at hand and the underlying contract. The Court, in particular, underlined:

“that the agreement [between the masonry and the owner] set forth various duties that the [construction manager is] to perform on behalf of the owner, including:

the scheduling and coordination of the masonry company’s work on the project

the processing of masonry’s payment applications and the certification of masonry company’s work for payment by the owner

the authority to approve original and revised work progress schedules prepared by the masonry company

the authority to approve masonry company’s operations on the project sites and to determine whether materials and equipment used by the masonry are defective.”³¹

The Court added that:

“The masonry construction ‘shall indemnify ... the Construction Manager for certain damage claims arising out of the negligent acts or omissions of the masonry or its agents.’”³²

In *Sunkist Soft Drinks v Sunkist Growers*,³³ the licensor of a trademark filed a claim against the parent company of the licensee for improper interference with the license agreement. The parent company although a non-signatory party to the arbitration clause, incorporated in the license agreement, filed a motion to compel the licensor (signatory party) to arbitrate the dispute with it. The Eleventh Circuit was satisfied that:

“The nexus between [the licensor’s] claims and the license agreement, as well as the integral relationship between [the licensee] and [the licensee’s parent company], leads us to the conclusion that the claims are *intimately founded in and intertwined* with the license agreement.”³⁴

³¹ *Ibid.*, at 839.

³² *Ibid.*

³³ 10 F.3d 753 (11th Cir. 1981).

³⁴ *Ibid.*, at 758; see too *Fluor Daniel Intercontinental, Inc. v Gen. Elec. Co.*, *supra* n. 18, at 6.

In *Ex Parte Napier*,³⁵ the dispute arose out of the purchase of a mobile home. In addition to a retail installment contract with the seller, the buyer entered into separate contracts with an insurance company and a finance company. Only the contract between the buyer and the seller included an arbitration clause. Nevertheless, the buyer was compelled to arbitrate the dispute not only with the seller but also with the insurance and the finance company. The Court pointed out that:

“[claimants’] claims against the signatory defendants and those against the nonsignatory defendants are sufficiently intertwined that all claims must be arbitrated.”³⁶

4.2.2.2 Second, the non-signatory party must have close contractual or corporate links with one of the signatory parties

The application of the doctrine requires that the non-signatory party is closely linked to at least one of the signatory parties. This link is usually *contractual*. Thus, for example, the non-signatory and signatory parties may have executed a construction agreement, as in *McBro* and in *Hughes*, or a purchase agreement as in *Ex Parte Napier*, or a secured agreement as in *Choctaw*.

In some other cases the non-signatory party may have *corporate links* with one of the non-signatory parties. The two interrelated parties may be affiliates or have a parent-subsidary relationship. A corporate relationship of this type is naturally based on *community of interests*³⁷ between the signatory and the non-signatory, which will usually result in stronger links than those between the signatory and the non-signatory in the context of a typical contractual relationship.³⁸ The courts have, indeed, considered corporate relationships between a non-signatory and a signatory party as a decisive factor for applying the intertwined version of estoppel doctrine.³⁹

³⁵ 723 So.2d 49 (Ala 1998).

³⁶ *Ibid*, at 53.

³⁷ See J. Douglas Uloth -J. Hamilton Rial, *supra* n. 7, p. 620.

³⁸ *Pritzker v Merrill Lynch, Pierce, Fenner & Smith*, 7 F.3d 1110 (3d Cir.1993) The Court in this case relied on traditional agency theory to apply an arbitration clause incorporated in the broker agreement between a pension plan trustees and a broker, to the financial consultant and the broker's sister company (non-signatories): “Relying on *Barrowclough*, we noted that arbitration agreements may be upheld against non-parties where the interests of such parties are directly related to, if not congruent with, those of a signatory”, at 1121. *Cf* See also Williston, *supra* n. 7, para 57:19.

³⁹ This remark brings the ‘estoppel theory’ close to the ‘group of companies doctrine’, discussed in detail in the next Chapter.

In *Sunkist* the Court based its decision to apply the doctrine, *inter alia*, on “*the integral relationship*” between a licensee [signatory] and its parent [non-signatory] company.⁴⁰

In *Smith/Enron Cogeneration v Smith Cogeneration Int’l.*,⁴¹ the Second Circuit referred to “*the identity of interests*” between the parent company (non-signatory) and its subsidiaries (signatory) to conclude that Smith Cogeneration International, as a parent company, was bound by the arbitration agreement that its subsidiaries had signed.⁴²

In *J.J. Ryan & Sons v Rhone Poulenc Textile*,⁴³ the Fourth Circuit stated:

“When the charges against a parent company and its subsidiary are based on the same facts and are inherently inseparable, a court may refer claims against the parent to arbitration even though the parent is not formally a party to the arbitration agreement. As the Fifth Circuit explained under similar circumstances, ‘If the parent corporation was forced to try the case, the arbitration proceedings would be rendered meaningless and the federal policy in favor of arbitration effectively thwarted.’ *Sam Reisfeld & Son Import Company v S. A. Eteco*, 530 F.2d 679, 681 (5th Cir. 1976)”

⁴⁰ “The nexus between Sunkist’s claims and the license agreement, as well as the *integral relationship between SSD [licensee] and Del Monte [licensee’s parent company]*, leads us to the conclusion that the claims are ‘intimately founded in and intertwined with’ the license agreement. Therefore, we hold that Sunkist is equitably estopped from avoiding arbitration of its claims” [emphasis added], *Sunkist supra* n. 32, at 758.

⁴¹ 198 F.3d 88, 98 (2d Cir. 1999).

⁴² In a complicated factual background, Smith Cogeneration International and Enron Int’l agreed to create a joint venture regarding the construction and operation of an electrical power plant. To this end an affiliate of SCI and an affiliate of Enron entered into a limited partnership agreement. The parent companies (SCI and Enron) assigned their interests in the Power Purchase Agreement to the limited partnership, which effectively took over the construction and operation of the power plant. It was the arbitration agreement included in this last agreement that Enron invoked in order to compel SCI to arbitrate their dispute. The Court, indeed, compelled SCI to arbitration with Enron, referring to the theory of piercing the corporate veil, and, additionally, to the intertwined estoppel theory. At 97 the Court noted characteristically:

“The identity of interests between petitioners and the current Enron signatories to the 1994 Agreement [...] is nowhere more apparent than on the assignment instruments themselves: the signatures of the assignors in the assignments from ACF and ER to EDR and EDRO are the same as the signatures for the assignees. Similarly, virtually all the correspondence between SCI and the various Enron petitioners is mailed to the same address in Texas, ‘c/o Enron Development Corp.’ Perhaps most telling is SCI’s own reference to the various Enron companies in its complaint in the Dominican Lawsuit as the ‘Enron Group,’ ‘affiliates,’ and ‘Enron’”.

⁴³ 863 F.2d 315, 320-21 (4th Cir.1988), at 320-321. In this case, four affiliates of a manufacturer (Rhone Poulenc Textile) concluded an exclusive distribution agreement, including an arbitration clause, with a subsidiary of a distributor (Ryan). The subsidiary assigned the contract to the distributor, which brought an action against the manufacturer and its affiliates. The manufacturer, although a third party, invoked the arbitration agreement in the distribution agreement and moved to compel the distributor to arbitration.

4.2.2.3 Concluding remarks on the intertwined version of the equitable doctrine

The above overview of the relevant case law shows there has been a growing acceptance of the “intertwined factor” as the key element for the application of the estoppel doctrine in the context of arbitration and third parties. It can be argued that the intertwined version of the doctrine now qualifies as a valid version of the equitable estoppel doctrine in its own right. This is not to suggest that there has been a total shift from the traditional equitable estoppel doctrine to the intertwined version.

At present, it seems that both versions of the doctrine are applied by US courts, as is evidenced by the most recent case-law,⁴⁴ although there are signs lately that the US courts are concerned about the non-consensual character of the intertwined version.⁴⁵ In any case, it is too early to say whether both versions will advance in parallel or whether one of the two will be preferred to the other.

It should be noted, however, that the “intertwined” version, for all its theoretical problems⁴⁶ is closer to commercial reality than the traditional equitable version is. As the above overview of the relevant case-law showed, the courts will usually apply commercial standards and business sense in order to determine whether the dispute between the non-signatory and the signatory is “intertwined” to the contract between the signatory parties, or whether two non-signatory and the signatory have sufficient contractual or corporate links. The intertwined version, thus, has a dynamic character that follows commercial developments and business practice, while the strictly equitable version of the doctrine is based on equitable rather than commercial considerations. Characteristically, equitable principles or considerations are too subjective to define and, thus, the strictly equitable doctrine is conducive to legal and commercial uncertainty.

⁴⁴ For the *equitable interpretation* of the doctrine see, for example, *Griffin v Beach Club II Homeowners Ass'n*, 384 F.3d 157 (4th Cir 2004); *In re Weekley Homes*, 180 S.W.3d 127, (S.C Tex. 2005); *In re FirstMerit Bank, N.A.*, 52 S.W.3d 749 (Tex. 2001); in *Employers Ins. of Wausau v Bright Metal Specialties, Inc.*, 251 F.3d 1316, 1322 (11th Cir. 2001). The Court found that the plaintiff enjoyed the advantages of the contract and, therefore, must be subject to the contractual duty of arbitration.

For the *intertwined interpretation* of the doctrine, see for example, *E.G.L. Gem Lab v Gem Quality Institute*, No. 97-7102, 1998 WL 314767 (S.D.N.Y. 1998); *Fluor Daniel Intercontinental v General Electric*, *supra* n. 18; *Usina Costa Pinto S.A. Acucar e Alcool v Louis Dreyfus Sugar Co.*, 933 F.Supp. 1170, 1179 (S.D.N.Y.1996); *Jones v Genus Credit*, 353 F.Supp.2d 598 (Maryland. 2005); *Denney v BDO Seidman*, *supra* n. 8; *JLM Industries v Stolt-Nielsen SA*, 387 F.3d 163, 177 (2d Cir.2004) (quoting *Choctaw Generation Ltd. v Am. Home Assurance Co.*, *supra* n. 5; see also *Contec Corp. v Remote Solution*, 398 F.3d 205, 209 (2d Cir.2005).

⁴⁵ See J.M. Townsend, “Non-Signatories in International Arbitration: an American Perspective”, paper in Conference of the International Council for Commercial Arbitration, Montreal 31 May-3 June 2006, p.10. See also Ch.6.2.3 below.

⁴⁶ As will be explained in detail in Chapter 6.

4.2.3 Equitable estoppel doctrine and consensual origins of arbitration

The intertwined version of the equitable doctrine has been applied on a non-consensual basis.⁴⁷ In determining whether the dispute between the non-signatory and the signatory party should be referred to arbitration, the courts have not been examining whether the parties have actually indented to arbitrate or not. Here, the courts have applied the doctrine against persons that were not contractually bound by the arbitration agreement. Strictly speaking, the “non-signatory party”, here, is not a party to the arbitration agreement at all. It is a person not bound by the arbitration agreement, i.e. a third party, rather than merely a non-signatory.

In *Choctaw*, for example, the Court, although held that the dispute between the surety and the owner had to be referred to arbitration, made clear that the term “party” included in the arbitration agreement in the contract between the genuine parties “is a defined term that includes only [the creditor] and [the debtor]” and by no means the non-signatory surety.⁴⁸

The same position was adopted in *Mc Bro*. Here, the Eleventh Circuit, although ordered the contractor (the non-signatory party) and the construction manager (the signatory party) to arbitrate, denied that the two parties had any contractual, substantive or arbitration, relationships. The contractor was subject neither to the bilateral substantive nor to the bilateral arbitration agreement between the construction manager and the owner. The Court mentioned that:

“The Triangle-St. Margaret's [Contractor-Owner] contract lists McBro as construction manager, but the contract itself constitutes an agreement between St. Margaret's as hospital owner and Triangle as contractor That contract also states, in its general conditions [...], that ‘nothing contained in the Contract Documents shall create any contractual relationship between the Construction Manager [McBro- Real party] and the Contractor [Triangle-Third party].’ The arbitration clause, [...], of the same contract [between the real parties, the owner and the Construction manager] refers to the ‘parties’ or the ‘other party.’ Similarly, the McBro-St. Margaret's [the real parties] contract is an agreement between those two parties; it makes no mention of Triangle as contractor.”⁴⁹

⁴⁷ Dileo, *supra* n.7, at 34, calls equitable estoppel a “quasi-contract theory”.

⁴⁸ *Supra* n. 5, at 405.

⁴⁹ *McBro*, *supra* n. 4, at 343.

It follows that the intertwined version of equitable doctrine places more emphasis on the intertwined factor, as shown in the previous section, than on whether the signatory and non-signatory party have actually agreed to arbitrate. Therefore, it can be argued that the intertwined version of the *estoppel doctrine distances arbitration from its consensual origins*. In fact the doctrine to some extent “*objectifies*” arbitration.

By contrast, the equitable version of the estoppel doctrine has been consistently applied on consensual premises. Here, the US Courts will take into account both equitable and consensual considerations in order to decide whether the non-signatory and signatory parties have to submit their dispute to arbitration. The fact that the non-signatory relies on the substantive clauses of the contract that includes the arbitration agreement reveals consent of the non-signatory to the substantive contract and, therefore, to the arbitration agreement incorporated therein. In *Deloitte Noraudit A/S v Deloitte Haskins & Sells* the Court noted:

“We conclude that Noraudit [the non-signatory] is bound by the arbitration section of the 1990 Agreement. Noraudit failed to object to the Agreement when it received it and offers no persuasive reason for its inaction. In addition, Noraudit knowingly accepted the benefits of the Agreement through its continuing use of the name ‘Deloitte’. Thus, Noraudit is estopped from denying its obligation to arbitrate”⁵⁰

Indeed, the courts in applying the equitable version of the estoppel doctrine will examine whether the non-signatory is *contractually bound by the arbitration agreement as an ordinary contract*.

For example, in *American Bureau of Shipping v Tencara Shipyard*,⁵¹ the Second Circuit noted that:

“Our first task is to determine whether the Owners of the “Tag Heuer” [the non-signatory] can be bound to arbitrate with ABS [the signatory] even though they never signed the arbitration agreement.”⁵²

Here, the non-signatory party is, in essence, *a regarded as a party that has consented to the arbitration agreement*. It is, therefore, a *genuine party the arbitration agreement*, despite the fact that has failed to sign it. In this regard, the courts have

⁵⁰ *Supra* n. 8, at 1064.

⁵¹ 170 F.3d 349 (2d Cir. 1999).

⁵² *Ibid.*, 353.

repeatedly distinguished consent to arbitration from the signature requirement. In *International Paper v Schwabedissen Maschinen & Anlagen GmbH*⁵³ the Fourth Circuit mentioned that:

“[A] party can agree to submit to arbitration by means other than personally signing a contract containing an arbitration clause” and

“[A] party can agree to submit to arbitration by means other than personally signing a contract containing an arbitration clause.”⁵⁴

4.2.4 The court rather than the tribunal will determine whether the dispute between the signatory and the non-signatory party is arbitrable or not

The decision of whether a signatory party must arbitrate its dispute against a non-signatory party will not be referred by the US courts to the arbitral tribunals. Nor will the national courts wait for this issue to be examined by the tribunal first. Instead, the courts will make the decision themselves, after they have thoroughly examined the factual circumstances of the dispute, as shown above.

Outside the US, it is open to question whether the national courts should be engaged in a full review of the existence and validity of an arbitration agreement and, thus, a full review of the tribunal's jurisdiction before the tribunals have first considered the issue.⁵⁵ The prevailing view is that the courts should, indeed, be entitled to proceed to such a full review⁵⁶ although in some jurisdictions the courts are limited to a *prima facie* review, before the tribunal has examined its own jurisdiction.⁵⁷ In the US, the courts have consistently engaged in a full review of the arbitration agreement, which includes the issue of whether a person is a party to the arbitration agreement.⁵⁸ Here two brief notes should be made:

First, this practice of the US courts to engage in a full review of the arbitration agreement rather than refer the issue to the tribunals must be accepted as the right approach to the issue. Otherwise, it is doubtful whether the tribunals would be able to

⁵³ 206 F.3d 411 (4th Cir. 2000).

⁵⁴ *Ibid.*, at 416, and *Deloitte Noraudit A/S v Deloitte Haskins & Sells*, *supra* n. 8, at 1063.

⁵⁵ See more on this J. Lew- L. Mistelis- S. Kroell. *Comparative International Commercial Arbitration*, (Kluwer Law International 2003), para 14-49 et seq.

⁵⁶ See, for example, Model Law art.8, which according to the prevailing view entitles the courts to a full review of the existence or validity of the arbitration agreement. The same is provided in the EAA s. 9 (Cf also EAA s.32).

⁵⁷ See for example French NCCP art.1458(2).

⁵⁸ *Interocean Shipping Co. v National Shipping & Trading Corp.*, 462 F.2d 673, 677 (2d Cir. 1972); *McAllister Bros., Inc. v A&S Transp. Co.*, 621 F.2d 519, 524 (2d Cir. 1980).

assume jurisdiction over the non-signatory on the basis of the doctrine of equitable estoppel. Research indicates that no arbitral award has applied the estoppel doctrine, in either of its versions. It could be argued that if tribunals were to apply the estoppel doctrine, they would apply it in a US domestic arbitration only, provided that the applicable substantive law would recognize the estoppel doctrine in the context of third parties to an arbitration agreement.⁵⁹ It is doubtful that the estoppel doctrine would be applied in an arbitration outside the US, not least because the non-US jurisdictions are not familiar with the doctrine and, therefore, the award would face a serious risk of either being annulled.

Second, the review by the US courts will not extend to the merits of the dispute. The determination will be limited to whether the dispute between the non-signatory and the signatory party should be referred to arbitration or not. Inevitably, the determination of the jurisdiction will touch upon issues relevant to the merits. This is particularly the case under the “intertwined version” of the equitable estoppel. Here, as shown above, the courts will normally undertake a thorough analysis of the dispute and its factual circumstances, in order to determine whether the dispute between the non-signatory and the signatory is “intertwined” to the contract between the signatory parties, or whether two non-signatory and the signatory have sufficient contractual or corporate links. This analysis, however, will never pre-empt the decision of the tribunal on the merits.

In *Choctaw*, for example, where the Court first examined in detail the rights and duties of the owner, the surety and the contractor,⁶⁰ the Court concluded:

“We therefore do not reach the many substantive and procedural issues addressed in the district court’s careful and comprehensive opinion. We vacate that judgment solely to clear the way for rulings on the merits in arbitration, and we remand for the framing of an order directing arbitration”⁶¹

⁵⁹ US state laws that recognize the equitable doctrine in arbitration is for example, Louisiana law, see *Lakeland Anesthesia v CIGNA Healthcare of Louisiana*, 812 So. 2d 695, 702 (La. Ct. App. 2002) where the Louisiana Appellate court stated that Louisiana courts recognize that equitable estoppel may bind third parties to an arbitration agreement although it did not apply the doctrine to the facts of the instant case; or Texas Law, see *In Re Weekley*, *supra* n. 8. at 131.

⁶⁰ *Supra* n. 5 at 406

“We carefully reviewed the relationship among the parties, the contracts they signed (or did not), and the issues that had arisen, to arrive at the conclusion that the controversy was arbitrable”

⁶¹ See *Choctaw*, *supra* n. 5, at 404.

Chapter 5: the doctrine of Group of Companies	84
5.1 Overview of the doctrine	85
5.2 Legal basis of the doctrine	87
5.3 Conditions for the application of the doctrine	88
5.3.1 First, the group corporate structure	92
5.3.2 Second, active role of the non-signatory companies in the negotiations, performance or termination of the contract	94
5.3.3 Third, legitimate impression of the co-contracting party that the non- signatory companies are genuine contracting parties	95

CHAPTER 5: THE DOCTRINE OF GROUP OF COMPANIES

This chapter examines the ‘group of companies’ doctrine, arguably the most prominent, and controversial of the extension doctrines. The idea that large multinational groups, operating through several subsidiaries, associated or holding companies, should be regarded as a whole rather than as strictly independent legal entities was originally developed in the context of company and tax law.¹ Indeed, under the law of many countries, groups of companies are treated as one unit for tax and accounting purposes.²

The doctrine has, however, acquired a particular relevance in the context of international arbitration: it has been employed mainly by international arbitral tribunals as the theoretical basis for the ‘extension’ of arbitration agreements signed by one or more of the several companies to non-signatory parties in the same group. The ‘group of companies’ doctrine was introduced into arbitration by the seminal award in *Dow Chemical v Isover-Saint-Gobain*,³ and has subsequently been developed as one of the most challenging theories in the area. For more than two

¹ The accounting profession has developed techniques and practices of consolidated group accounting since 1930’s, see T. Hadden, *The Control of Corporate Groups*, (Institute Advanced Legal Studies-University of London 1983), p. 2. For a detailed account on the development and regulation of group of companies or multinational enterprises see P. Muchlinski, *Multinational Enterprises and the Law*, (Blackwell London 1999).

² In England for example see s. 258 of the Companies Act 1985.

³ Interim award in ICC case no. 4131 of 1982, *Dow Chemical v Isover-Saint-Gobain*. (1984) Rev. Arb. 137; (1983) 110 Clunet 899, with note Derains. It should be mentioned, however, that even before the *Dow Chemical* award, arbitral awards had been making tentative references to the ‘group of companies’ notion and its important role for the jurisdiction of the tribunals in the context of international arbitration. See, for example, the ICC case no. 2138 of 1974, ICC Arbitral Awards 1974-1985 (Y.Derain and S.Jarvin), p.934; ICC case no. 1434 of 1975, *ibid*, p.263; ICC case no. 2375 of 1975, *ibid*, p.257 and (1985) Rev.Arb., p.583.

decades, the doctrine has been the subject matter of extensive literature, and has repeatedly been dealt with by arbitral tribunals and national courts in different jurisdictions.

Despite the fact that it has been widely debated for many years, the discussion on the group of companies is by no means settled yet. Thus, the thesis revisits the ‘group of companies’ doctrine and provides an analysis of its conceptual characteristics. This chapter first gives a brief overview of the history and the legal premises of the doctrine. It then studies the relevant case law of arbitral tribunals and national courts. Finally, it identifies the conditions required for the doctrine to apply. Particular emphasis is placed on the role of ‘consent’. The question here is whether the ‘consent’ of the non-signatory party is required by the tribunals and the courts for the application of the doctrine, or whether alternative non-consensual factors may be used as a substitute for the requirement of ‘consent’. The conclusions of this chapter and the previous one on ‘equitable estoppel’ will provide the basis for discussion in the next chapter, where the thesis presents its overall view on the ‘extension doctrines’ and the contractual approach in general.

5.1 OVERVIEW OF THE DOCTRINE

As was already mentioned, it was the celebrated *Dow Chemical v Isover Saint Gobain* award that first introduced the ‘group of companies’ doctrine into international arbitration. Two subsidiaries of the Dow Chemical Company group entered into two separate distribution contracts with Boussois-Isolation, whose rights and obligations were subsequently assigned to Isover Saint Gobain. Both distribution agreements contained an ICC arbitration clause. When a dispute arose out of the distribution agreements, the two Dow Chemical subsidiaries alongside their parent company and another subsidiary of the same group initiated arbitration proceedings against Isover Saint Gobain. The respondent challenged the jurisdiction of the tribunal on the basis that the parent company and the third subsidiary of the claimants were not parties to either of the two arbitration agreements incorporated in the distributions contracts. The ICC tribunal, comprised of three academics,⁴ accepted jurisdiction to examine the claims brought by the non-signatory parent and subsidiary company.

⁴ Prof. Pieter Sanders (chair), Prof. Goldman and Prof. Vasseur.

The tribunal, by an interim award,⁵ rejected the respondent's objections that the tribunal lacked jurisdiction over the non-signatory parties (*l'exception d'incompétence*), and that the claims brought by those non-signatories were non-admissible (*exception d'irrecevabilité*) of the claims brought by the non-signatories. To establish its jurisdiction, the tribunal made specific references to:

- The factual context of the contractual relationship in question revealing the *active role* of the non-signatories in the conclusion and performance of the contracts
- The common intention of the parties to arbitrate
- The fact that the signatories and the non-signatories were companies belonging to the *same group*
- The *autonomy of the arbitration agreement* from the main contract which allowed the tribunal to determine the scope and effects of the arbitration agreement in accordance with a law different from that applicable to the merits of the dispute. In particular, the tribunal applied *substantive rules of international commerce*, part of which, the tribunal held, was the 'group of company' concept.

The respondent challenged the award before the French courts, but the Paris Cour d'appel upheld the interim award, and confirmed jurisdiction of the tribunal over the non-signatories.⁶

Since the *Dow Chemical* case, the doctrine has been applied by several tribunals and has been accepted by many national courts. The *Dow Chemical* award has become one of the most celebrated arbitration cases and has been the reference point in many cases. It is difficult for 'arbitral precedent' to develop, due to the international character of arbitration and the lack of hierarchy amongst the several arbitral tribunals.⁷ Nevertheless, it can be argued that the 'group of companies' doctrine constitutes the clearest case of 'arbitral precedent', with several arbitral

⁵ Interim award in ICC case no. 4131 of 1982. *Dow Chemical v Isover-Saint-Gobain*, supra n. 3.

⁶ Paris Cour d'appel, 21 October 1983, (1984) *Rev.Arb.*, p. 98 with note Chapelle. Like the arbitral tribunal, the Cour d'appel made also references to the common intention of the parties and to substantive rules of international commerce.

⁷ See G. Kaufmann-Kohler, "Arbitral Precedent: Dream, Necessity or Excuse?", 2006 School of International Arbitration-Freshfields' Lecture, (2007) 23 (3), *Arb. Int'l*, p. 357.

awards making express reference to the *Dow Chemical* case and the ‘group of companies’ doctrine established thereby.⁸

5.2 LEGAL BASIS OF THE DOCTRINE

It is not uncommon for companies with strong financial, business and corporate ties to maintain separate legal personalities. As was explained in Chapter 2, national laws generally provide for the principle of limited liability of the stockholders and the principle of separate liability of the parent company. Therefore the several companies of the same group are largely treated as separate legal personalities. This, in terms of contract law, means that a parent or any other company of the group lacks the capacity to bind contractually another company in the same group, except from itself. Unless acting in accordance with traditional contract law principles, such as agency for example, the company concluding a contract will be the only entity of the group to assume any contractual duties and rights from that contract. This equally applies to arbitration agreements: only the company entering into an arbitration agreement, rather than any other company in the group, will be bound by that agreement.

No national or international law provides for any exception from the traditional contract law rules with regard to group of companies. No national or international contract law provides for the ability of a company to have other companies in the group bound by a contract concluded by the former. Equally, no express *arbitration* rule in national law or international treaty provides for an exception from the traditional contract law rules, with regard to arbitration contracts. Accordingly, the “group of companies doctrine” in arbitration *applies on the basis of arbitral case law and international arbitral practice*.⁹

This explains why tribunals will normally apply the ‘group of companies’ doctrine on the basis of international rules rather than national law. Indeed, the tribunals, in order to assume jurisdiction over the several companies in the same group, will not apply the national substantive law applicable to the merits of the case or, indeed, any national law at all. Based on the doctrine of separability and the principle of ‘autonomy of arbitration agreements’, the tribunals have on many occasions

⁸ By way of example, see case ICC no. 5103 of 1988, 2 (1991) 2 *ICC Bull.*, p.20; ICC case no. 5920 of 1989, 2 (1991) 2 *ICC Bull.*, p.27; ICC case no.10758 of 2000, 16 (2005) 2 *ICC Bull.*, p. 87.

⁹ C. Jarrosson, “Conventions d’arbitrage et groupes de sociétés”, in *Arbitration Agreement – Its Multifold Critical Aspects*: (1999) ASA Special Series No 8, p.212.

determined the boundaries of the arbitration agreement and, therefore, the boundaries of their jurisdiction, on the basis of ‘usages of international trade’, the ‘common intention of the parties’, ‘transnational substantive rules’ and ‘lex mercatoria’.¹⁰

5.3 CONDITIONS FOR THE APPLICATION OF THE DOCTRINE

No distinction should be drawn between the situation where the non-signatory company invokes an arbitration clause, and that where a signatory attempts to enforce an arbitration clause against a non-signatory.¹¹ The group of companies doctrine has been applied equally to the case where the non-signatory company has acted as

¹⁰ See for example, the arbitral awards: ICC case no. 4131 of 1982, *Dow Chemical v Isover-Saint-Gobain*, supra n. 3: “et en tenant également compte [...] des usages conformes aux besoins du commerce international”; ICC case no. 6000 of 1988, 2 (1991) 2 *ICC Bull.*, p.34: “the usages of the international trade [...] would justify and require the extension to this company, party to a group of companies, of the arbitration clauses included in the contracts executed” by the other companies of the group; the same in partial award ICC case no. 5894 of 1989, 2 (1991) 2 *ICC Bull.*, p.25; ICC case no 4131 (Interim Award) of 1982, (1983) 110 *JDI (Clunet)*, p.899, with note Y.Derains; ICC case no 5721 of 1990, (1990) 117 *JDI (Clunet)*, p.1019, with note Y.Derains; ICC award, on 10 March 2003, *C & M Farming Ltd v Peterson Farms Inc* (unpublished).

See also the decisions of Paris Cour d’ appel in *Dow Chemical v Isover-Saint-Gobain*, supra n. 3, upholding the award by reference to the trade usages and art 13.5 of the previous ICC rules (*cf* ICC rules (1998) art 17: “In all cases the Arbitral Tribunal shall take account of the provision of the contract and the relevant trade usages” (*cf* also French NCCP art. 1496(2): “[The arbitrator] in all cases shall take the usages of the trade into consideration”); Paris Cour d’ appel, 21 Oct 1983, (1984) *Rev. Arb.*, p. 98, with note A. Chapelle; Pau Cour d’ appel, *Sponsor A.B. v Lestrade*, 26 November 1986, (1988) *Rev.Arb.*, p.153 with note A. Chapelle.

This is the prevailing view in arbitration literature too: J. Lew, L. Mistelis and S. Kroell, *Comparative International Commercial Arbitration*, (Kluwer London 2003), para 6-73; Fouchard, Gaillard and Goldman, *On International Commercial Arbitration*, E.Gaillard and J.Savage (eds) (Kluwer 1999), para 443 et seq.; see also Derain and Schauf, “Clauses d’ Arbitrages et Groupes de Sociétés”, (1985) *Rev. Dr. Aff. Int.*, p. 231; J-F Poudret “L’ extension de la clause d’ arbitrage: approches française et suisse”, (1995) 122 *JDI (Clunet)*, p. 923; *cf* S. Jarvin in his note on the ICC case no 4504 of 1985-1986, (1986) *JDI (Clunet)*, p. 1130 and M. Blessing, “The law applicable to the Arbitration Clause and Arbitrability”, van den Berg (ed), ICCA Congress series no.9, p. 174. *Contra* O. Sandrock, “Extending the Scope of Arbitration Agreements to Non-Signatories”, in *Arbitration Agreement – Its Multifold Critical Aspects*; (1999) ASA Special Series No 8, p.167 and O. Sandrock, “Arbitration Agreements and Group of Companies” (1993) 27 *International Lawyer*, p. 945, who argues that the contours of *lex mercatoria* are too vague to provide support to the ‘group of companies’ doctrine. Instead, Sandrock argues for the application of national law as determined by the relevant conflict of laws rules.

¹¹ See Interim Award in ICC case 9517 of 2000, 16 (2005) 2 *ICC Bull.*, p.80: “These distinctions are not however conclusive. The principles which govern the extension of the clause to non-signatory respondents may generally be considered applicable, mutatis mutandis, to a case where a party [...] tries to avail itself of an arbitration clause to which it did not formally adhere.” Same in Fouchard, Gaillard and Goldman, *idem*, para 502, note 200; In the US, although the ‘equitable estoppel’ doctrine in principle is applied in both situations also, in the majority of the cases the ‘equitable estoppel’ doctrine has been applied to estop a signatory party from avoiding arbitration.

respondent, resisting the arbitration agreement,¹² and where the non-signatory company has been a claimant attempting to enforce the arbitration agreement.¹³

Likewise, there is no clear evidence that there should be a distinction between the case where the non-signatory party is a parent company and that where the non-signatory party is a subsidiary company of the group.¹⁴ Thus, tribunals have ‘extended’ arbitration agreements to a non-signatory *parent company* of the group,¹⁵ to a non-signatory subsidiary,¹⁶ and even to directors and shareholders of the group.¹⁷

As will be demonstrated in the following sections, analysis of the relevant case law suggests that the key-factor for the application of the doctrine is ‘consent’. Courts and tribunals will extend the arbitration agreement to the non-signatory only when they are satisfied that that latter has actually consented to the arbitration agreement. Therefore, arbitration agreements in the context of ‘group of companies doctrine’ are examined exclusively from a contractual viewpoint as an ordinary contract: they bind those, and only those, parties that have consented thereto. Indeed, with the exception of the argument of the “autonomous validity and effectiveness” of international arbitration agreements discussed below, the prominence of consent has never actually been challenged in the context of the ‘group of companies’ doctrine.¹⁸

¹² Pau Court d’appel, 26 November 1986, *Sponsor A.B. v Lestrade*, (1988) Rev.Arb., p.153 with note A. Chapelle; or ICC no.6000 of 1988, 2 (1991) 2 ICC Bull., p.31.

¹³ See, for example, ICC case no 2375 of 1975, (1985) Rev. Arb., p. 583; or the award ICC award, on 10 March 2003, *C & M Farming Ltd v Peterson Farms Inc* (unpublished).

¹⁴ See in more details, all the possible factual schemes presented by B. Hanotiau, “Groups of Companies in International Arbitration”, in *Pervasive Problems in International Arbitration*, L. Mistelis and J Lew (eds), (Kluwer Law International 2006) para 14-11 and B. Hanotiau, *Complex Arbitrations: Multiparty, Multi-contract, Multi-issue and Class Actions*, (Kluwer Law International 2005), p. 54 et seq. Note however, that Hanotiau argues for the emergence of a rebuttable presumption that a parent company binds its subsidiaries but that on the other hand only companies that have participated in the conclusion and performance of the agreement will be bound by that contact and the arbitration clause” *ibid*, p.98.

¹⁵ For example, see the *Dow Chemical v Isover-Saint-Gobain*, supra n. 3, and the decision of Pau Court d’appel, 26 November 1986, *Sponsor A.B. v Lestrade*, (1988) Rev.Arb., p.153 with note A.Chapelle.

¹⁶ For example see the Paris Cour d’appel, *Kis France and other v Général and other*, (1991) 16 YBCA, p. 145; (1992) Rev. Arb., p.90, and the Partial award in ICC case no.5894 of 1989, 2 (1991) 2 ICC Bull., p. 25.

¹⁷ For example. ICC case no 6519 of 1991. (1991) 118 JDI (*Clunet*). p.1065; see also Hanotiau, *Complex Arbitrations*, supra n. 14 p. 98.

¹⁸ Arbitration discourse agrees almost unanimously that the application of the ‘group of companies’ doctrine depends on ‘consent’ of the non-signatory: see, for example, Fouchard, Gaillard and Goldman. supra n. 10, para 500; Lew, Mistelis and Kroell, supra n. 10, para 7-51; C. Jarrosson, supra n. 9, p. 220; Y. Derains, “L’ Extension de la Clause d’Arbitrage aux Non-Signatories- la Doctrine des Groupes de Sociétés”, in *Arbitration Agreement – Its Multifold Critical Aspects*, (1999) ASA Special Series No 8. p. 242.

In this consensual context, two divergent approaches to the doctrine can be identified. The first view challenges the need for a ‘group of companies doctrine’ to exist at all. Since the key factor in the doctrine is ‘consent’, the well-established principles of contract law will suffice to determine whether a non-signatory party is bound by a specific arbitration agreement.¹⁹ General principles with regard to the formation and interpretation of contracts can be found in every national law. Thus, the tribunals, instead of referring to the group of companies’ doctrine, should refer to:

- Legal principles of representation or agency,²⁰
- Principles governing the ratification of contracts;²¹

¹⁹ This is the approach taken by I. Fadlallah, “Clause d’Arbitrage et Groupes de Sociétés”, *Travaux du Comité Français de Droit International Privé 1984-1985*, (1987), p.105 et seq.; also, O. Sandrock, “Extending the Scope of Arbitration Agreements to Non-Signatories”, in *Arbitration Agreement – Its Multifold Critical Aspects*; (1999) ASA Special Series No 8, p. 165. Cf A. Redfern, M. Hunter, N. Blackaby and N. Partasides, *Law and Practice of International Commercial Arbitration*, (Kluwer Law International 2004), para 3-33: “More established principles of private law—such as assignment, agency and succession—thus remain the surest way in which to bind a third party to an arbitration agreement”.

Cf the US decision in *Sarhank Group v Oracle Corp*, 404 F.3d 657, (2nd Cir. 2005) at 662:

“While this Court has recognized instances in which non-signatories can be bound to the arbitration agreements of others, such cases are limited to instances of incorporation by reference, assumption, veil piercing/alter ego and estoppel and the like. See *Monegasque De Reassurances S.A.M. (Monde Re) v Nak Naftogaz of Ukr.*, 311 F.3d 488, 495 (2d Cir.2002.) In all such situations a court has found an agreement to arbitrate, under general principles of contract law, that is to say that the totality of the evidence supports an objective intention to agree to arbitrate”.

Cf *Thomson-CSF, S.A. v. American Arbitration Ass’n*, 64 F.3d 773, 777 (2d Cir.1995) at 662: “[t]raditional principles of agency law may bind a nonsignatory to an arbitration agreement.” Similar approach has the English High Court taken in the recent *Peterson Farms Inc. v C & M Farming Ltd*, [2004] 1 Lloyd’s Rep. 603.

²⁰ Which can take the form of the ‘apparent or ostensible representation’ or ‘agency’ in English law; the ‘apparent authority’ or ‘authority by estoppel’ or ‘agency’ in US law; the ‘mandat apparent’ in French law or the ‘Duldungsvollmacht und Anscheinsvollmacht’ in German and Swiss Law, see M. Blessing, “Extension of the Arbitration Clause to Non-Signatories” in *Arbitration Agreement – Its Multifold Critical Aspects*; (1999) ASA Special Series No 8., p.161 and O. Sandrock, “Extending the Scope of Arbitration Agreements to Non-Signatories”, in *Arbitration Agreement – Its Multifold Critical Aspects*; (1999) ASA Special Series No 8, p. 170.

The Partial award in ICC case no. 4402 of 1983, (1984) *Y.Com.Arb.*, P. Sanders (ed.), Vol. IX, p. 138 (seat in Geneva), examined whether an arbitration agreement, signed by the chairman of a subsidiary, could be extended to the parent company, on the basis of *representation*. The tribunal finally refused to extend the arbitration agreement on the grounds that the chairman “could not act on behalf of the concern and had no power to sign an arbitration clause on behalf of the mother company”, *Yearbook Commercial Arbitration*, P. Sanders (ed.), Vol. IX (1984), p. 140; the same view on similar facts was taken in Interim award ICC case 4504 of 1985-1986. (seat also in Geneva), (1986) 113 *JDI (Chunet)*, p. 1118.

For a case of “apparent authority” see Swiss Tribunal Fédéral, 29 January 1996, (1996) 14 *ASA Bull.*, p. 496, noting that an arbitration agreement will be extended only in very particular circumstances which justify a *bona fide* reliance of a party to an appearance caused by the non-signatory.

Cf also the US case *Pritzker v Merrill Lynch, Pierce, Fenner & Smith*. 7 F.3d 1110 (3rd Cir.1993), where the extension to the sister company non-signatory was mainly premised on traditional principles of agency law.

- Third party beneficiary theories;²²
- *Alter ego* and corporate veil theories;²³
- General principles of interpretation.²⁴

According to this view, the ‘group of companies’ doctrine is ambiguous and confusing.²⁵

By contrast, the second approach upholds the doctrine as an important theoretical construct in international arbitration. According to this view, the existence of strong corporate relationships between the several companies in a group is a factor that must be taken into account by tribunals in determining whether the non-signatory members of the group have consented to arbitrate or not.²⁶ Thus, the existence of a corporate structure indicates the implied intention of the non-signatory members of the group to arbitrate.²⁷ In other words, the ‘group of ‘companies’ doctrine should be used by the

²¹ See for example, ICC case no 4504 of 1985-1986, (1986) 113 *JDI (Clunet)*, p. 1118; cf also Derains, “L’ Extension de la Clause d’Arbitrage aux Non-Signatories- la Doctrine des Groupes de Sociétés”, in *Arbitration Agreement – Its Multifold Critical Aspects*, (1999) ASA Special Series No 8, p.242.

²² See for example award in ICC case no 2375 of 1975, in ICC arbitral awards 1974-1985 (Y. Derains and S. Jarvin), p.259; or award in ICC case no 6519 of 1991, (1991) 118 *JDI (Clunet)*, p. 1065. It is not clear however whether an arbitration agreement should be considered as a beneficial clause, since arbitration agreements establish not only rights but also duties vis-à-vis the parties.

²³ See for example the ICC case no.6000 (1988) ICC *Bull.* Vol.2 no.2, p. 31; cf the *Orri* case, Paris Cour d’appel, 11 January 1990, *Orri v Lubrifiants Elf Aquitaine*, (1992) *Rev. Arb.*, p.95, with note D. Cohen; (1991) 118 *J.D.I.*, p.141, with note B. Audit and the decision of Cour de cassation Cass. 1e civ., June 11, 1991, *Orri v Lubrifiants Elf Aquitaine*, (1992) *Rev. Arb.*, p.73, with note D. Cohen.

²⁴ For example, ICC case no. 1434 of 1975, ICC Arbitral Awards 1974-1985 (S. Jarvin and Y. Derains eds 1990), p. 264, where the tribunal accepted the extension of the arbitration agreement to a non-signatory company of a group, on the grounds of implied consent, ascertained by reasonable interpretation of the contract.

²⁵ See O. Sandrock, “Group of Companies and Arbitration”, (2005) *Tijdschrift voor Arbitrage*, p.6: “The doctrine must however, be rejected for several reasons... First, the rules developed under this doctrine are not clear-cut and define enough to permit their unambiguous application... Secondly, the basic principle of privity of contract is confusingly blurred... Thirdly, there is no reason whatsoever to deviate from the traditional approach which guarantees a much higher degree of certainty of law and foresee ability....Fourthly, this theory often also runs counter to the clear intention of the parties”.

²⁶ Y Derains and S. Schaf, “Clauses d’Arbitrages et Groupes de Sociétés”, (1985) *Rev. Dr. Aff. Inter’l*, p.231; A Chappelle, “Groupes de Sociétés: Interventions d’Etat” *Rapport Général sur l’arbitrage et les tiers: Le Droit des Personnes Morales*, (1988) *Rev Arb*, p. 475.

²⁷ B. Hanotiau. *Complex Arbitrations. Multiparty, Multi-contract, Multi-issue and Class Actions*, supra n. 14, p. 51: “the issue of consent to arbitration may take a special dimension when one (or more) company(ies) to a complex international transaction is (are) member(s) of a group of companies, given the nature of the relationships which exist between the companies of such group. In particular, *consent to arbitrate may sometimes be implied from the conduct of a company of the group*-although it did not sign the relevant arbitration agreement – by reason of its “implication” in the negotiation and/or the performance and/or the termination of the agreement containing the arbitration clause and to which one or more members of its group are a party” (emphasis added).

tribunals as a kind of “facilitator” to assert the implied consent of the non-signatory parties.

In the context of the second approach, specific criteria have been developed by case law for the ascertainment of the implied consent of the non-signatories. When these conditions are met, tribunals will usually be satisfied that consent of the non-signatory party to arbitrate exists and, thus, they will extend the arbitration agreement to the non-signatory members of the group by reference to *the ‘group of companies’ doctrine*.²⁸ Drawing on the analysis of the relevant case law, the conditions for the application of the doctrine may be summarised as follows:

5.3.1 First, the group corporate structure

Despite their separate legal personalities, the several companies must be structured on a *group corporate* basis. This necessitates that strong group organisational, financial and control systems within the group must be proved.²⁹ It has been held that the group corporate structure of the group can be evidenced when:

- The several companies in the group are structured in a hierarchical order.³⁰ In most cases, there will be a business divisional structure underpinning the group.³¹ This will be the case, for example, when a parent company holds the commanding role in the business strategy of the whole group,³² with several other subsidiaries and sub-subsidiaries, or even dormant companies

²⁸ See, for example, ICC case no.6000 of 1988, 2 (1991) 2 ICC *Bull.*, p. 31, accepted the extension of the arbitration agreement to the non-signatory company, although it did not accept that there was an assignment of the main contract or the arbitration agreement; or ICC case 6519 of 1991, (1991) 118 *JDI (Clunet)*, p. 1065, which also accepted the extension of the arbitration agreement to non-signatory company, although it expressly noted that no representation principle was applicable to the case in hand. However, as is explained in the next chapter, the tribunals might refer to traditional contract law principles, in addition to the ‘group of companies’ doctrine.

²⁹ See some very interesting case studies for the complicated group structure in group of multinational groups in T. Hadden. *supra* n. 1.

³⁰ However, in some cases a ‘heterarchical’ network of cooperative and lateral relationships rather than a vertical hierarchical structure may be adopted by the group. P. Muchlinski, *supra* n. 1, p. 59.

³¹ Although in most of the cases a clear symmetry or rationality will be lacking, due to the large numbers of the subsidiaries and the sheer organizational complexity of the group.

³² See for example the case Paris Cour d’appel, *Kis France and other v Général and other*, (1991) 16 *YBCA*, p. 145; (1992) *Rev. Arb.*, p.90, where the parent company had a dominant role vis-à-vis its subsidiaries.

constituting the executive branches of the group.³³ In some cases subsidiaries can be set up merely to execute a one-off business project.

- The several companies in the group share intellectual property rights, assets, financial or human resources including, for example, ownership titles, corporate name, offices and premises, officers, bank accounts, trademarks.³⁴
- The several companies constitute a ‘single economic unit’ or a ‘single economic reality.’³⁵ For the several companies to constitute a ‘single economic unit’ they need to be part of the same business and commercial strategy. It is not simply a matter of sharing financial assets. There must be an overarching business policy or organizational rationale applying to the several members of the group.³⁶

For the courts and tribunals to ascertain that a group structure among the several companies exists, they need to perform an in-depth, and often complicated economic and commercial analysis. This requires a thorough understanding of commercial

³³ See Partial award in ICC case no.5894 of 1989, 2 (1991) 2 *ICC Bull.*, p.25: “the subsidiaries though they were not sham companies set up solely for the purpose of the said agreements, were operating to carry them out under the close control and following the instructions of the parent companies which made all the important decisions commercial as well as financial either unilaterally or jointly”. In the same vein, ICC case no. 1434 of 1975, (1976) 103 *JDI (Clunet)*, p.978: “The group organises the performance of its task in the most efficient manner, using those entities in the group that are best adapted to carry out the job”.

³⁴ In ICC case no. 6000 of 1988, 2 (1991) 2 *ICC Bull.*, p.31 the tribunal was satisfied that a close business and corporate link between the two defendants existed, as evidenced by the fact that the two companies had the same share holders in the same proportion, the same business place, the same subject matter of the activities, the same representatives. See also ICC case no 4131 of 1982, (1983) 110 *JDI (Clunet)*, p. 899 the several companies in the same group were sharing the use of the same trademarks.

³⁵ “Une réalité économique unique, dont les tribunaux doivent tenir compte” in ICC case no. 4131 of 1982, *Dow Chemical v Isover-Saint-Gobain*, *supra* n. 3; the same in Pau Court d’appel, 26 November 1986, *Sponsor A.B. v Lestrade*, (1988) *Rev.Arb.*, p.153 with note A. Chapelle; cf ICC case no. 6000 of 1988, 2 (1991) 2, *ICC Bull.*, p. 31: “there could not be more clear and obvious admission of the fact that [the companies] are one and the same entity (*in economic terms*)”. In ICC case no. 5103 of 1988, 2 (1991) 2, *ICC Bull.*, p. 20, the tribunal assumed jurisdiction over the several claimants and the several respondents on the basis of the “group of companies” doctrine. The tribunal undertook a detailed analysis of the corporate structure and the business organization of all the companies involved. The tribunal found that both the several claimants and the several defendants formed an economic unit. Claimants, for example, were set up, owned and controlled by the same natural person; a company of the Claimants group would invoice another company of the group for delivery of the goods while the notice of delivery and verification would be in the name of a third company of the group. On the other hand, the several respondents had permanently mixed up their telexes and business papers.

In ICC case no.5891 of 1988, 2 (1991) 2 *ICC Bull.*, p.23, the tribunal underlined the lack of structural connection between the companies (different headquarters, different places of registry) and accordingly refused to accept jurisdiction on the basis of the group of companies doctrine.

³⁶ In ICC case no.5103 of 1988, 2 (1991) 2, *ICC Bull.*, p. 20, the tribunal noted that the payment facilities obtained for a company essentially financed another company of the group, “as the latter was the beneficiary of a group policy aimed at financing its investments”(emphasis added).

reality, where the focus must be on the factual rather than the legal circumstances of the case.

5.3.2 Second, active role of the non-signatory companies in the negotiations, performance or termination of the contract

The non-signatory companies must have an active role in the negotiations, the performance or the termination of the contract in which the arbitration agreement in question is included.³⁷ Thus, for the doctrine to apply, it is not enough that the several companies have a ‘group structure’, in general. This ‘multi-company structure’ must be reflected in the specific contractual relationship out of which the dispute arises: the non-signatory companies must assume a complementary role to the signatory companies of the group in the negotiations, performance or termination of the specific contract.

For example, it is not unusual for the contract to be negotiated or signed by one company, and performed by another company of the group.³⁸ It often occurs also, that the several companies of the group sign different but interrelated contracts regarding the same business project. This may result in a contractual network of indivisible rights and duties,³⁹ assumed by the several companies as a group rather than as

³⁷ “...par le rôle qu’ elle on joué dans la conclusion, l’ exécution ou la résiliation de contrats contenant lesdites clauses”, see *Société Sponsor AB v Lestrade* (Cour d’appel Paris, (1988) Rev. Arb., p.154, with note A. Chapelle). See also the *Dow Chemical* award, *supra* n. 3: “DOW FRANCE, therefore, played in the execution of the contracts an equally *preponderant* role as it did in the establishment of the contractual relations” and “played an essential role in the termination of the contract” at 134.

In ICC case no. 6000 of 1988, 2 (1991) 2 *ICC Bull.*, p. 32, the tribunal noted that “the actual performance of the contracts by all the parties during the whole period until the notice of termination and even after such notice was given [...] brings persuasive evidence of the factual identity” between the several companies.

In ICC case no 6519 of 1991, (1991) 118 *JDI (Clunet)*, p.1065 noted that: “without denying the economic reality of a ‘group of companies’ the scope of an arbitration clause may be extended to non-signatory companies with separate legal significance only if they played an active role in the negotiations leading to the agreement containing the clause or if they are directly implicated in the agreement. “

The same was held in ICC case no. 5103 of 1988, *Three European companies v Four Tunisian companies*, (1988) 115 *JDI (Clunet)*, p. 1206; 2 (1991) 2 *ICC Bull.*, p. 22.

In ICC case no. 7604 and 7610 of 1995, (1998) 125 *JDI (Clunet)*, p.1027, the tribunal examined in detail the role of the parent company in the negotiation, conclusion, execution and termination of the contract signed by its subsidiary, and concluded that on the face of the evidence the arbitration agreement could not be extended to the parent company. The same was held in ICC case no. 7155 of 1993, *Norwegian company v Three French companies*, (1996) 123 *JDI (Clunet)*, p. 1037, with note J.-J. Arnaldez.

³⁸ See for example, ICC case no. 5103 of 1988, 2 (1991) 2, *ICC Bull.*, p. 20, where the tribunal found that one of the companies of the group had the commanding role, whereas, another would be the “technical instrument of the Group for the payment of debts” owed by other companies of the group.

³⁹ See for example ICC award case 8163 of 1996. 16 (2005) 2 *ICC Bull.*, p.77.

separate legal entities,⁴⁰ in which case the several companies of the group can be held jointly and severally liable vis-à-vis the other signatory party.⁴¹ In situations like this, tribunals have found it impossible to isolate the arbitration agreement included in one only of the several interrelated contracts.⁴²

5.3.3 Third, legitimate impression of the co-contracting party that the non-signatory companies are genuine contracting parties

The group structure and the active role of the non-signatories in the negotiation and execution of the particular contract must legitimately lead the co-contracting party to believe that the non-signatory companies are genuine parties to the contract containing the arbitration clause.

There are two requirements for this condition to apply. The first is that the co-contracting party is, indeed, under the impression that the non-signatory company was a genuine party to the contract. Here, tribunals will seek evidence of *actual impression* focusing on behaviour of the co-contracting party. In particular, tribunals will explore whether the co-contracting party showed that it actually wanted to deal, or had an interest in dealing with the whole group rather than just the signatory companies.⁴³

⁴⁰ Pau Court d'appel, 26 November 1986, *Sponsor A.B. v Lestrade*, (1988) Rev. Arb., p.153 with note A.Chapelle: "En effet, un group de sociétés possède, en dépit de la personnalité juridique distincte appartenant à chacune de celles-ci, une réalité économique" (in fact, the group of companies has, despite the separate legal personality of the companies comprising the group, an economic reality) (author's translation).

Also, see Partial award in ICC case no. 5894 of 1989, 2 (1991) 2 *ICC Bull.*, p. 25: "the agreements create a tight network of obligations to be discharged by or for the companies concerned".

In *Kis France and other v Général and other*, (1991) 16 YBCA, p. 145; (1992) Rev. Arb., p.90, the Paris Cour d'appel found that the several companies of the group *had assumed mutual substantive obligations which were inexorably linked*.

⁴¹ See ICC case no.5103 of 1988, 2 (1991) 2, *ICC Bull.*, p. 20.

⁴² "The protocol signed by the parent company was a unit where each of the subsidiaries and the parent companies of the two groups were indissolubly bound. *There was a network of rights and duties which would make the isolation of the arbitration agreement inconceivable*" (emphasis added) in ICC case no. 2375 of 1975, (1985) Rev. Arb., p. 583.

⁴³ In ICC case no. 6000 of 1988, 2 (1991) 2 *ICC Bull.*, p.3: "On their own side the [co-contractor] have shown during the performance of the contracts that they considered [the non-signatory company] as their true partner in that performance".

ICC award, on 10 March 2003, *C & M Farming Ltd v Peterson Farms Inc* (unpublished), para 87, the tribunal pointed out that Peterson knew that it was contracting with the C & M group as a whole and that its product would be used in an integrated operation that involved all members of the C & M Group: "In this respect, the Tribunal considered that Peterson, the seller, *was aware throughout the negotiating period and at the time of contracting that it was dealing with the C&M group and would have obligations to all C&M companies*" and in para 91: "Furthermore, the draft Sales Right Agreement attached to Peterson's Submission in Response to the Claimant's Memorandum on

The second requirement is that co-contracting party *legitimately* had the impression that the non-signatory company was a genuine party to the arbitration agreement. Here, the tribunal will focus on the behaviour of the non-signatory party. For example, the impression of the co-contracting party will be legitimate when the non-signatory company adopts ‘a genuine party behaviour’ leading the co-contractor to confuse the different companies of the group.⁴⁴ In some cases the ‘genuine party behaviour’ of the non-signatory company may well border on fraud, particularly if the non-signatory actively, or even intentionally, encourages an incorrect understanding of the co-contractor.⁴⁵

Jurisdiction dated 28 June 2002, again indicates the parties understanding and intention. The Tribunal finds that this supports C&M's contention that Peterson knew it was contracting with and would have obligations to all C&M Group companies”.

In the *Dow Chemical* award, *supra* n. 3, the tribunal noted that the respondents did not “attach the slightest importance to the choice of the company within the DOW Group that would sign the contracts” and “it was with the aggregate of these entities that the present defendant's predecessors understood themselves to be contracting”.

In ICC case no. 5721 of 1990, (1990) 117 *JDI* (*Clunet*), p.1023, *ICC Arbitral Awards* 1986-1990 (Y. Derains, S. Jarvin and J.J. Arnaldez), p. 400, the tribunal rejected the extension of the arbitration agreement to the person controlling the company (respondent) on the grounds that the claimant did not establish that it “intended to deal with” that person, or indeed that such person “intended personally to be a party to the arbitration agreement”.

⁴⁴ See ICC case no. 4505 in 1985 and 1986, (1986) 113 *JDI* (*Clunet*), p. 1118; *ICC Arbitral Awards* 1986-1990 (Y. Derains, S. Jarvin and J.J. Arnaldez), p. 279, the same person would give the impression that he represented all the several companies of the group the several companies.

See also the ICC Award No. 1434 in 1975, *ICC Arbitral Awards* 1974-1985 (S. Jarvin and Y. Derains 1990), p. 264; (1976) 103 *JDI* (*Clunet*), p. 978, with note Y. Derains: the tribunal held that the person signed the several agreements was representing the whole group, since “throughout the conclusion of the agreements requiems by the transaction behaved in conformity with what he was in essence, the manager in charge the leader of this large industrial group”.

The same in ICC case no. 2375 of 1975, *French company v Two Spanish companies*, (1976) 103 *JDI* (*Clunet*), p. 973.

⁴⁵ In which case moral considerations may come into play in determining whether the arbitration agreement should be extended the non-signatory party, *cf* Fouchard, Galliard and Goldman, *supra* n. 10, para 501. See arbitral award in ICC case 10758 of 2000, 16 (2005) 2 *ICC Bull.*, p.87: “where a corporate structure is used in bad faith as an instrument of deliberate concealment or confusion, or to defeat a possible award against the named party to an arbitration agreement, the the Arbitral Tribunal might be justified in lifting the corporate veil”; in the Partial Award in ICC case No. 5730 of 1989, *Lubrificants Elf Aquitaine v A.R. Orri*, (1990) 117 *JDI* (*Clunet*), p. 1029); (1992) *Rev. Arb.*, p. 125 with note Cohen, the tribunal decided that the arbitration agreement had been extended to the director of the group as the clause had been signed “in his name, on his instructions and in his presence” by his employee “who simply carried out his wishes and had no other involvement”); *cf* the decisions of the Cour d’appel and Cour de Cassation in *Orri* case confirming the award on the ground of fraud: Paris Cour d’appel, 11 January 1990, *Orri v Lubrificants Elf Aquitaine*, (1992) *Rev. Arb.*, p.95, with note D. Cohen: (1991) 118 *J.D.I.*, p.141, with note B.Audit and the decision of Cassation Cass 1e civ., June 11, 1991, *Orri v Lubrificants Elf Aquitaine*, (1992) *Rev. Arb.*, p.73, with note D. Cohen.

However, note in ICC case no. 5721 of 1990, (1990) 117 *JDI* (*Clunet*), p.1023; *ICC Arbitral Awards* 1986-1990 (Y. Derains, S. Jarvin and J.J. Arnaldez), p. 400, the tribunal pointed out that any extension of the arbitration agreement must not take place as a way of punishing the behaviour of a thire party, and that if the behaviour of a non-signatory party raises issues of fraud the ordinary courts should take care of this action, rather than the tribunals.

It should be noted that the ‘genuine party behaviour’ of the non-signatory in the context of the ‘group of companies’ doctrine bears similarities to principle of agency or representation, blurring the boundaries between the group of companies doctrine and traditional principles of contract law.⁴⁶ Thus, ‘real party behaviour’ adopted by the non-signatory company may well be regarded as a case of ‘apparent or ostensible authority’, in which case the non-signatory party may be bound by the contract under the principles of agency. The ‘genuine party behaviour’ may also bring the US principle of ‘equitable estoppel’ into play: if the co-contracting party relied on the ‘genuine party behaviour’ of the non-signatory, the latter may well be estopped from avoiding the duties arising out of the contract.

It follows that it is not always easy to separate the doctrine from traditional contract law principles. However, it would be a mistake to dismiss the doctrine as superfluous and, thus, diminish its contribution to the discussion on ‘arbitration agreements and third parties’. Despite the criticism leveled in the next chapter at the extension doctrines and the ‘group of companies’ doctrine in particular, it should be emphasised that the latter has brought a new dimension to the debate on ‘arbitration and third parties’. The fact that, twenty years after the *Dow Chemical* award, the ‘group of companies doctrine’ is prominently discussed both in case law and legal discourse is a testament to the importance of the doctrine.⁴⁷

⁴⁶ See the Paris Cour d’appel, *Kis France and other v Général and other*, (1991) 16 YBCA, p. 145; (1992) Rev. Arb., p.90, made references to both the principle of representation (the parent company of a group signed the framework-contract on behalf of its subsidiaries) and the ‘group of companies’ doctrine.

⁴⁷ See S. Wilske and L. Shore, “The Rise and Fall of the ‘Group of Companies’ Doctrine”, (2005) 4 *Journal of International Dispute Resolution*, p. 157, arguing that the doctrine after its initial remarkable rise in the last decade has now started to fall.

CHAPTER 6: CRITIQUE ON THE EXTENSION DOCTRINES	98
6.1 <i>Positive contribution of extension doctrines</i>	98
6. 2 <i>Conceptual inefficiencies of the extension doctrines</i>	99
6.2.1 The extension doctrines fail to distinguish between the different types of third parties	99
6.2.2 Limitations of the extension doctrines based on consent (consensual extension doctrines)	100
6.2.2.1 Deduction of implied consent is not always justified.....	102
6.2.2.2 Specific arbitral consent is required for the non-signatory to be bound by the arbitration agreement.....	105
6.2.2.3 Misapplication of traditional principles of contract law in the context of the extension doctrines	110
6.2.2.4 Conclusions on the extension doctrines based on consent	112
6.2.3 Limitations of extension doctrines not based on consent (non-consensual extension doctrines)	113
6.2.4 The extension doctrines and the “writing requirement”	118
6.3 <i>Conclusions on the extension doctrines and the contractual approach</i>	120

CHAPTER 6: CRITIQUE ON THE EXTENSION DOCTRINES

The previous two chapters reviewed the two most significant doctrines on extension of arbitration agreements to third or non-signatory parties: Chapter 4 discussed the doctrine of “equitable estoppel,”¹ while Chapter 5 examined the “group of companies” doctrine. This chapter further examines the “extension doctrines”. At the outset, it provides an account of their positive contribution to the third-party discussion. The main purpose of the chapter, however, is to highlight their conceptual inefficiencies.

6.1 POSITIVE CONTRIBUTION OF EXTENSION DOCTRINES

“Extension doctrines” have been developed to address the intrinsic difficulties arising out of multiparty relationships that are “procedurally fragmented.”² For all their conceptual flaws and practical difficulties, which will be shown in this chapter, extension doctrines constitute a radical and, thus, intriguing attempt to accommodate

¹ As was noted in Chapter 4, the US courts have been employing a *negative* wording (“estopped from avoiding arbitration”) when applying the estoppel doctrine. In essence, however, the application of the doctrine means that the non-signatory party is bound by the arbitration agreement concluded by the original parties.

² See Chapter 1 for more details on procedural fragmentation.

the perplexing issues of multiparty transactions in the context of arbitration. Extension doctrines provoked a fruitful debate on the role of ‘third parties’ in arbitration, showing that a party that has neither signed nor ever consented to an arbitration agreement may not necessarily be a total *stranger* to arbitration proceedings between two other parties. Extension doctrines shifted the focus of the discussion on the contractual interrelatedness between the genuine and the third parties. In other words, extension doctrines highlighted the fact that those third parties that are commercial partners of two genuine parties to an arbitration agreement should not be overlooked in the arbitration proceedings.

In sum, extension doctrines have drawn attention to the relevance of third parties in the context of arbitration, and, thus, their overall contribution to the “third parties” discussion is regarded as positive.

6. 2 CONCEPTUAL INEFFICIENCIES OF THE EXTENSION DOCTRINES

In spite of their positive contribution to the third party discussion, the extension doctrines have significant limitations, demonstrated by the following.

6.2.1 The extension doctrines fail to distinguish between the different types of third parties

Extension doctrines do not distinguish between the various types of ‘third parties.’ As was shown in Part I, not every person not bound by an arbitration agreement is relevant to the discussion on arbitration and third parties. Only those third parties with an interest in the dispute pending before a tribunal would be relevant, i.e. the false third parties. Furthermore, false third parties should be distinguished into different groups, on the basis of the difference in the degree of association between the genuine and the false third parties. As will be shown in Part III, the degree of contractual interrelatedness between the third and the real parties is a key factor for determining whether these parties should be brought before the same arbitral tribunal.

However, courts and tribunals have applied extension doctrines to different types of false third parties indiscriminately. The doctrine of equitable estoppel, for example, has been applied to a wide range of different types of contractual relationships. It has been applied to compel arbitration between a debtor and its surety,³ between a

³ *Choctaw Generation v American Home Assurance*, 271 F.3d 403 (2nd Cir.2001).

licensor and a licensee,⁴ and between a yacht owner and a ship classification society.⁵ Likewise, the “group of companies” doctrine has applied to extend the arbitration agreement to a parent company⁶, to a subsidiary⁷ and to the chairman of a group of companies.⁸

There are, however, fundamental differences between the above multiparty contractual relationships. It is true that whether arbitration agreements should be extended to third parties is a question depending to a large extent on the particular factual circumstances of each case. Nonetheless, a rough identification of the types of false third parties that are, in principle, conducive to the application of extension doctrines, would help the extension doctrines to be applied in a consistently rather than indiscriminatingly. In this regard, it would be helpful to determine *a priori* the minimum degree of contractual interrelatedness between the genuine and the false third parties that would warrant the participation of a third party in the arbitration proceedings between the two genuine parties.

6.2.2 Limitations of the extension doctrines based on consent (consensual extension doctrines)

As already explained in the previous chapters, ‘extension doctrines’ are, in essence, based on the principle of consent.⁹ This applies particularly for the doctrine of “group of companies”: for courts and tribunals to extend an arbitration agreement to a non-signatory member of a group of companies, they need to be satisfied that the signatory and the non-signatory parties have consented to arbitration. As far as the doctrine of “equitable estoppel” is concerned, despite the fact that the ‘intertwined version’ of the doctrine seems to have deviated from its equitable origins, the traditional equitable

⁴ *Sunkist Soft Drinks v Sunkist Growers*, 10 F.3d 753 (11th Cir. 1981).

⁵ *American Bureau of Shipping v Tencara Shipyard*, 170 F.3d 349 (2nd Cir. 1999).

⁶ See, for example, Interim award in ICC case no. 4131 of 1982, *Dow Chemical v Isover-Saint-Gobain*, (1984) Rev. Arb. 137; (1983) 110 Clunet 899, with note Derains; Pau Cour d’appel, *Sponsor v Lestrade*, (1988) Rev.Arb., p.153, with note A. Chapelle.

⁷ See, for example, ICC case no. 2375 of 1975, in ICC arbitral awards 1974-1985 (Y. Derains and S. Jarvin), p.259.

⁸ See, for example, *Marine Drive Complex v Ghana*, (1994) 19 YBCA, p.11.

⁹ Cf J.Hosking “Non-Signatories and International Arbitration in the United States: the Quest for Consent”. 24 (2004) 3, *Arbitration International*, at p. 303: “A review of the theories, principles and procedures employed to bind non-signatories, reveals – perhaps unsurprisingly – that the ‘touchstone’ for this determination is whether or not the relevant entities *consented* to arbitrate with one another”.

version of the doctrine is largely applied on consensual premises, as was shown in Chapter 4.¹⁰

Therefore, it is questionable whether the extension doctrines are even genuine “extension doctrine.” Here, the non-signatory party is not a third party in its real sense, namely a party not bound by the arbitration agreement. It is merely a party that has consented to the arbitration agreement, despite the fact that it has failed to sign it. Therefore, it is not accurate that an arbitration agreement is “extended” to a third party. Rather, it binds the non-signatory party in the same way as the two genuine parties. The discussion in the context of the “group of companies” doctrine, in particular, relates merely to the formal requirement of signature. The main question here is whether there is scope for a party that has not signed the arbitration agreement to be, nevertheless, bound by it? In this regard, the term ‘extension’, used in the context of the ‘group of companies’, is superfluous if not confusing.

Indeed, with a few exceptions,¹¹ the requirement of consent as fundamental to the conclusion of arbitration agreements has never really been challenged by the ‘extension doctrines’. As was shown in the previous chapters, the ‘multi-company group structure’ or the ‘single economic unity’ of the several companies in the same group are used as factors indicating consent to arbitration on the part of the non-signatory party. These factors alone would not be sufficient to provide the conceptual premises for the ‘extension’ of arbitration agreements to the non-signatory companies of the group.¹² The underlined premise for the extension is, as courts and tribunals have consistently, held the “the common intention of all the parties.”¹³

¹⁰ See discussion in Ch.4.3.2 above.

¹¹ See section 4.3.2, on intertwined equitable estoppel above, and section 6.2.3 below.

¹² “L’existence d’un group de société n’est pas une condition suffisante pour retenir dans l’arbitrage l’ensemble des sociétés du group” see ICC no 7155 in 1993, (1996) *JDI (Clunet)*, p.1037, note J-J Arnaldez and ICC cases 7604 and 7610 in 1995, (1998) *JDI (Clunet)*, p 1027; cf D. Vidal, “The Extension of Arbitration Agreements within Groups of Companies: The Alter Ego Doctrine in Arbitral and Court Decisions”, 16 (2005) 2 *ICC Bull.*, p.73: “Case law does offer any significant examples of the extension of an arbitration agreement on the sole basis of the economic unity of a group”.

¹³ The reference to “the common will of all the parties to the proceedings” (“selon la commune volonté de toutes les parties”) was first found in the seminal *Dow Chemical* award in ICC Case No. 4131 (1982), *Dow Chemical v Isover-Saint-Gobain*, (1984) Rev. Arb. 137; (1983) 110 *JDI (Clunet)* 899, with note Derains. Since then it can be found in many other awards or court decisions applying the group of companies doctrine; see for example the more recent arbitral award in ICC case 10758 of 2000, 16 (2005) 2 *ICC Bull.*, p.87; or the Paris Cour d’appel, *Société Sponsor AB v Lestrade*, (1988) Rev. Arb. p.154, with note A. Chapelle; see also the award of the tribunal and the decision of the Paris Cour d’appel in the case *Re Société Kis France v Société Générale* (1992) Rev. Arb. p.90; XVI *YBCA*. 145 (1991).

Thus, the ‘group of companies’ doctrine is employed to ascertain implied consent, rather than to dispense with it. In this consensual context, the true essence of the doctrine is *to facilitate the deduction of consent*: intention of the non-signatory party to arbitrate is more easily inferred when the non-signatory is a member of a group of companies.¹⁴

The fact that the ‘group of companies’ doctrine has, in principle, adhered to the requirement of consent has kept the doctrine in line with the contractual origins of arbitration. At the same time, however, the insistence on ‘consent’ has created a number of theoretical and practical inconsistencies. In fact, it has proved to be one of the main weaknesses of the ‘group of companies’ doctrine, as it obliges courts and tribunals to engage in a complicated quest for consent. This argument is demonstrated by following:

6.2.2.1 Deduction of implied consent is not always justified

In the context of group of companies doctrine, courts and tribunals have on many instances ascertained “common intention of the parties” to arbitrate by reference to the ‘*group structure*’ or the ‘*economic unit*’ of the several companies, or by reference to the ‘*active role*’ of the non-signatories in the negotiations or the performance of the contract.¹⁵ It is questionable, however, whether references to the ‘group structure’ or the ‘active role’ can warrant deduction of intention to arbitrate.

For example, in ICC case 5103 of 1988, in order to prove that the several companies (claimants) belonged to the same group the tribunal set out a list of facts and documents regarding the close corporate relationships between the several companies. In particular, the tribunal had regard to financial statements referring to the several companies as a group; to consolidated balance sheets of the several companies of the group; to the fact that the several companies had the same CEO and common headquarters; to the fact that goods were delivered by one company of the group whereas another company was invoiced. Therefore, the tribunal assumed jurisdiction over all claimants since:

¹⁴ B. Hanotiau, *Complex Arbitrations: Multiparty, Multi-contract, Multi-issue and Class Actions*, (Kluwer Law International 2005), p.51, see also B. Hanotiau, “Groups of Companies in International Arbitration”, in, L. Mistelis- J. Lew (eds.). (Kluwer Law International 2005) *Pervasive Problems in International Arbitration* paras 14-5 and 14-6.

¹⁵ See above n.13.

“The three claimant companies appear to have been at the time of the conclusion, execution, non-execution and re-negotiation of their contractual links with the [defendants] genuine partners to all these contracts, *by the common will of the parties to the proceedings*” (emphasis added)¹⁶

Similarly, in ICC no.6000 of 1988,¹⁷ in order to prove that the several defendants were members of the same group the tribunal made specific references to the fact that the several companies had the same owners and the same representatives. The tribunal was satisfied that the several companies had very close corporate relationships, if they were not substantially identical. In addition to the close corporate relationships between the several defendants, the tribunal made specific references to the fact that the non-signatory defendant had taken part in the negotiations and the performance of the contract. In fact, the active role of the non-signatory in the negotiations of the contract led the tribunal to conclude that the arbitration agreement was extended to the non signatory company of the group, since:

“the common will of the parties was obviously that the [non-signatory defendant] be fully -and indeed, almost exclusively- involved in the conclusion, the performance and the termination of the contracts in dispute.”¹⁸

However, it is difficult to see why the fact that several companies have close corporate relationships should be viewed as such a decisive factor for revealing “common will” of the parties to arbitrate. Or why, in that matter, close corporate relationships should weigh more than the actual fact that the non-signatory and the co-contracting party never signed the contract or the arbitration agreement included therein. At face value, the decision of all the parties involved in the multiparty transaction, not to include the non-signatory company in the contract, incorporating the arbitration agreement, *should be accepted as a conscious decision of the parties not have the non-signatory bound by the specific contract*.¹⁹ Or at least it should be viewed as a strong presumption that the non-signatory and the co-contracting

¹⁶ 2 (1991) 2 ICC Bull., p.20 to 22.

¹⁷ 2 (1991) 2 ICC Bull, p.31.

¹⁸ The references to the active role of the non-signatory are set out under the heading: “common will of the parties”, *ibid*, p.34.

¹⁹ See Derains, “L’extension de la clause d’arbitrage aux non signatories-La doctrine des groupes de sociétés”, in *Arbitration Agreement- its Multifold Critical Aspects*, (1999) ASA Special Series No 8, at p.242).

company did not want to arbitrate. In the ICC case no, 10758 of 2000, the tribunal, rightly, noted that:

“By not signing the Contract, [the non-signatory] intended to respect the legal independence of [its affiliate signatory]’s legal personality and to be in harmony with the privity of contract principle, that is to say precisely not to become a party to the Contract nor to its arbitration clause”²⁰

Moreover, the fact that the non-signatory company had an ‘active role’ in the negotiation or the execution of the specific transaction does not necessarily rebut this presumption.²¹ It does not prove that the non-signatory has consented to the substantive contract. In the context of contemporary business, it is likely that the internal division of labour within the group, and its complex structure require that different companies of the group will be involved in the performance or the termination of the contract. In this regard, a non-signatory company may well take part in the performance of the contract merely as an executing branch of the group or a supervising unit of the group, rather than as a company that assumes legal duties or responsibilities from this contract.

In the ICC case no in case 10818 of 2001 (Partial Award),²² the non-signatory party took over the performance of the exclusive distribution agreement signed by another company of the group of the contract. The non-signatory party was providing the co-contractor (claimant) with technical, marketing and operational support with regard to the exclusive distribution agreement. In fact, the claimant was dealing exclusively with the non-signatory throughout the period until the contract was terminated. Nonetheless the tribunal found that the fact that the non-signatory party contributed to the performance of the agreement did not evidence an intention to assume responsibilities instead of or in addition to the signatory.

²⁰ 16 (2005) 2 *ICC Bull.*, p.92. para 25. The same in Partial Award in ICC case no 10818 of 2001, 16 (2005) 2 *ICC Bull.*, p.94.

²¹ Unless is it considered as ratification (consent at a later stage), in which case this should be expressly noted in the arbitral awards or the court judgments; cf ICC case no. 4504 of 1985-1986 where the active role of a second company in the same group of companies was not considered critical for this company to be bound by the arbitration agreement concluded by another company in the group. The tribunal noted that “one could not deduce there from [the role of the second company in the negotiation and performance of the agreement that the second defendant had ratified the agreement” ICC awards 1986-1990 (Y. Derains, S. Jarvin and J.J. Arnaldez), p.279.

²² 16 (2005) 2 *ICC Bull.*, p.94.

This should be the right approach to the issue. In principle, it is considered legitimate commercial practice for a group to adopt a multi-divisional structure where certain companies are assigned specific duties and a parent company is merely holding a supervisory role. Therefore, the involvement of companies other than the non-signatory may be due to a legitimate divisional structure of the group. This does not, or at least does not necessarily, reveal an unequivocal intention of the non-signatories to be bound by the substantive contract between the two signatories.

6.2.2.2 Specific arbitral consent is required for the non-signatory to be bound by the arbitration agreement

Moreover, even if it were accepted that the ‘active participation’ of the non-signatories to the performance of the contract between the two signatories could reveal intention of the non-signatories to be bound by the substantive contract, this would not necessarily reveal their intention to be bound by the arbitration agreement too (‘arbitral intention’). The ‘active role’ of the non-signatory pertains to the substantive part of the contract, rather than to the arbitration agreement.²³ Therefore, it is questionable whether a specific intention to arbitrate can be ascertained by reference to the participation of the non-signatory in the performance of the substantive part of the contract between the two signatories. The non-signatory might not even be aware of the arbitration agreement in the main contract.

The French courts, in the context of the ‘group of companies’ doctrine, have held that the fact that a non-signatory party has taken part in the negotiation or the performance of the contract raises the presumption that the non-signatory party is aware of the existence and the scope of the arbitration agreement included in this contract.²⁴ It may be queried whether the view taken by the French courts is correct. In fact, it has rightly been criticized, as going too far.²⁵

²³ The tribunal in ICC case no. 2138 of 1974 succinctly observed “it is not at all certain that if the non-signatory had signed itself the contract [...] it would have accepted the arbitration clause”, in ICC awards 1974-1985 (Y. Derains and S. Jarvin), at p.934.

²⁴ “Their respective situations and activities raise the presumption that they were aware of the existence and scope of the arbitration clause, and irrespective of the fact that they did not sign the contract containing the arbitration agreement”, see for example Paris Cour d’appel, Nov. 30, 1988, *Korsnas Marma v Durand-Auzias*, (1989) REV. ARB., p.691, with note Tschanz 208 and Paris Cour d’Appel, 7 Dec. 1994, *V 2000 v Project XJ 220 ITD et autre*, (1996) Rev Arb, p.67, with note C Jarrosson; Paris Cour d’appel, 22 March 1995, *SMABTP et autre soc Statinor*, (1997) Rev.Arb. p.550.

²⁵ Fouchard, Gaillard and Goldman, *On International Commercial Arbitration*, E. Gaillard and J. Savage (eds) (Kluwer 1999), paras 481 and 505.

In any case, even if it were accepted that the non-signatory by its active role is presumably aware of the arbitration agreement, this would not be enough for the non-signatory to *be bound* by the arbitration agreement. *Unambiguous consent* rather than mere awareness is the uncompromised threshold for a person to be bound by an arbitration agreement, as indeed by any other contract.

In fact, not even the unilateral consent of the non-signatory would be enough. *Mutual consent* of both the non-signatory and the signatory must be proved. While the focus is usually on whether the non-signatory party has given its consent, the intention of the signatory parties is not always given proper consideration. In the ICC case 9517 of 2000 (Interim Award),²⁶ the tribunal felt that it should underline this point:

“Although this is self-evident, it is worth emphasising that the intention that the non-signatories be party to the agreement must be common to the latter and the other party(ies) to the arbitration clause”

It follows that an arbitration agreement must be founded upon a meeting of minds of both the signatories and the non-signatories, which must be ascertained by reference to specific facts revealing the mutual intention of the parties to resort to arbitration.²⁷

The well-established principle of autonomy of arbitration agreements²⁸ must apply in its fullest sense in the context of the ‘extension doctrines’: all formal and substantive requirements of validity and, above all, intention of all parties to arbitrate must be met with regard to an arbitration agreement independently. Therefore, the assertion of *specific arbitration consent* is indispensable for a non-signatory to be bound by an arbitration agreement concluded between the signatories.

In the recent case of *Celanese Corporation and Celanese (Nanjing) Chemical Co., v The Boc Group Plc*,²⁹ an agreement regarding the construction of a plant in China was signed between BOC plc and BOC Nanjing (its wholly owned subsidiary) on the one hand and Celanese AG and Celanese Nanjing (its wholly owned subsidiary) on the

²⁶ 16 (2005) 2 *ICC Bull.*, p.80.

²⁷ “An agreement implied in fact is founded upon a meeting of minds, which, although not embodied in an express contract, is inferred, as a fact, from conduct of the parties showing, in the light of the surrounding circumstances, their tacit understanding.” *Hercules, Inc. v United States*, 516 U.S. 417, 424 (1996) (quoting *Baltimore & Ohio R.R. Co. v United States*, 261 U.S. 592, 597 (1923)).

²⁸ See J.Lew, L.Mistelis and S.Kroell, *Comparative International Commercial Arbitration*, (Kluwer Law International 2003) at para 6-7 et seq; Fouchard, Gaillard and Goldman, *supra* n. 25, Part 2 Chapter I; see also Cass. 1e civ., 7 May 1963, *Raymond Gosset v Carapelli*, (1963) JCP, Ed. G., Pt. II, No. 13, 405 (1963), with note B. Goldman; also ICC Case No.2138 of 1974, (1975) *JDI (Clunet)*, p.934 and ICC Case No.1434 of 1976, (1976) *JDI (Clunet)*, p. 974.

²⁹ U.S.D.Court Texas 2006. Slip Copy. (2006 WL 3513633).

other. However, the parent companies (Celanese AG and BOC plc) were not included in the definition of the terms ‘Party’ or ‘Parties’ used in the arbitration clause incorporated in the substantive agreement. The terms expressly referred only to the subsidiaries.

When Celanese Corporation and Celanese Nanjing brought an action against the BOC Group before the US courts, the latter initiated ICC arbitration proceedings against Celanese AG and its subsidiary Celanese Nanjing. At the same time, BOC filed a motion before the US courts to stay proceedings under the FAA s.4, pending final award in the ICC arbitration and compel arbitration. The District court refused to compel arbitration on the grounds that Celanese Corporation and BOC plc were not parties to the arbitration agreement. According to the court, the fact that the parent companies had taken part in the negotiations to the contract and, in addition, had signed the substantive agreement of the contract did not necessarily reveal their intent to arbitrate. The court held:

“[...] both BOC plc and BOC Nanjing were signatories to the Agreement, and yet BOC plc expressly excluded themselves as a party to the arbitration clause. Although the arbitration agreement may evidence clear and unmistakable intent to arbitrate questions of arbitrability between the two parties to that agreement, this hardly evidences a clear intent between BOC plc and Plaintiffs to arbitrate questions of arbitrability when BOC plc and BOC Nanjing acted as separate entities when negotiating the Agreement and BOC plc chose to be a non-party to the arbitration clause”³⁰

“[...] Because BOC plc was aware of the arbitration agreement and seemingly had an opportunity to participate in such agreement, yet, for whatever reason, expressly chose not to do so, the Court cannot now allow BOC plc to force Celanese Nanjing and Celanese Corporation to arbitrate their claims against only BOC plc”³¹

In the ICC case no, 10758 of 2000, the non-signatory parent company became actively involved after the contract was signed, at the stage of the negotiations attempting to resolve the dispute. The active role of the non-signatory in the dispute resolution process leading to arbitration could have been taken as an indication that

³⁰ *Ibid*, at 3.

³¹ *Ibid*, at 7.

the parent company had the intention to be part of the arbitration proceedings too. The tribunal however held that:

“[...] this involvement, beginning eight years after the Contract was signed, does not reveal any intention to accept either responsibility for the Contract or its arbitration clause. A parent company can assist a wholly-owned subsidiary in resolving a dispute regarding a major project that the latter is involved with, especially when it is mandated by law to supervise its subsidiaries as in the instant case, without thereby taking over the project; otherwise, it could retrospectively assume liabilities it did not contract for in the first place or become itself a party to the dispute or the ensuing arbitration”³²

It has been argued that specific arbitration consent is not always required for the existence of arbitration agreements. In particular, Fouchard-Galliard-Goldman express the view -at least in the context of assignment and incorporation of arbitration agreements by reference-³³ that:

“The principle of the autonomy of the arbitration agreement from the main contract raises no obstacle to the validity of an arbitration agreement [...]. The principle of autonomy does not require the arbitration agreement to be contained in a separate document in order to be valid.”³⁴

Their view is based on the premise that:

³² No 10758 of 2000, 16 (2005) 2 *ICC Bull.*, p. 93 para 27.

³³ Fouchard, Gaillard and Goldman, *supra* n. 25, para 426 et seq and para 492 et seq. It should be noted, though, that there is a fundamental difference between the case of assignment and the case of extension of arbitration agreements to third parties. In the former case, the assignee consents to assume all the rights and obligations of the assignor vis-à-vis its co-contractor. In essence, the assignee consents to take the place of the assignor. There is no need to distinguish between consent to assume the substantive obligations and consent to arbitrate. The general consent of the assignee to substitutes the assignor covers every right and obligation vis-à-vis the co-contractor. On the other hand, a ‘third party’ is added to the arbitration agreement. It is as new party in its own right, rather than a party that substitutes one of the original ones. Therefore, all validity requirements, and above all *intention to arbitrate*, must be examined autonomously with regard to the third party. Fouchard, Gaillard and Goldman rightly argue for the automatic assignment of the obligation to arbitrate from the assignor to the assignee. This is correct since “if it was otherwise, the assignee could unilaterally alter the position of the remaining party, who had initially agreed with the assignor to arbitration” (by reference to the judgment of the Supreme Court of Sweden, Oct. 15, 1997, *MS Emja Braack Schiffahrts KG v Wärtsilä Diesel Aktiebolag*, (1998) *Rev. Arb.*, p.431. with note A-C. Hansson Lecoanet and S. Jarvin) However, this argument does not apply to the case of the extension of the arbitration agreement to third parties. As has just been noticed, a third party does not substitute one of the original parties to the arbitration agreement. It does not interfere with the arbitration agreement between the original parties. The third party assumes in its own right vis-à-vis the original parties the obligation to arbitrate. Therefore, the obligation of the original parties to arbitrate cannot be altered by the third party unilaterally.

³⁴ Fouchard, Gaillard and Goldman. *idem*.

“Any other understanding of the principle of autonomy would resuscitate the anachronistic distinction between arbitration clauses and submission agreements, thus creating new obstacles to the validity of the arbitration agreement, despite the fact that the principle of autonomy was precisely intended to promote that validity.”³⁵

It is questionable whether this argument is correct. The principle of “autonomy of the arbitration agreement” or the principle of separability does not promote the validity of arbitration agreements. In fact, the principles pertain to the invalidity rather than the validity of arbitration agreements. According to the true meaning of the principle of “autonomy of the arbitration agreement” and separability, arbitration agreements are not necessarily rendered invalid merely because the main contract is invalid. However, the principles cannot salvage the validity of the arbitration agreement when the main contract is invalid. By the same token, the fact that the main contract is valid is not, by itself, a reason for the arbitration agreement included in the contract to be valid too. Therefore, irrespective of the existence or validity of the main contract, the existence or validity of the arbitration agreement must be determined independently. This necessarily means that for an arbitration agreement to be valid, a general intention of a party to be bound by the main contract is not enough. A specific intention to arbitrate must exist.

A specific intention to arbitrate can be inferred from the conduct of the non-signatory revealing its tacit consent to the arbitration agreement. This will be the case, for example, if the original party to the arbitration agreement initiates court proceedings against the non-signatory, which requests a stay by reference to the arbitration agreement between the signatories.³⁶ Alternatively, it may be that the

³⁵ *Idem*

³⁶ See ICC case no.7453 of 1994, 124 JDI 107 (1997) where the claimant commenced court proceedings in the US against both a signatory and a non-signatory. Both defendants objected to the jurisdiction of the US courts by reference to the ICC arbitration clause included in the contract between the claimant and the defendant signatory. After the claimant commenced arbitral proceedings against both defendants the non-signatory contested the jurisdiction of the tribunal this time, on the grounds that it had never signed the contract and the arbitration clause therein. The sole arbitrator, indeed, refused to assume jurisdiction over the non-signatory. In his view the fact that the non-signatory contested the jurisdiction of the US courts did not amount to an arbitration submission in the meaning of sec.2 of the United States Federal Arbitration Act. In particular, the arbitrator noted at para 12:

“In considering the first such possible mode of consent it is appropriate to quote the second section of the Act (9 U.S.C. 2) ‘A written provision in [...] a contract [...] to settle by arbitration a controversy thereafter arising out of such contract [...] or an agreement in writing to submit to

signatory initiates arbitration proceedings against the whole group of companies, including both signatory and non-signatory parties, which do not object to the jurisdiction of the arbitral tribunal.³⁷

6.2.2.3 *Misapplication of traditional principles of contract law in the context of the extension doctrines*

In some cases, the tribunals in addition to references to the ‘common intention of the parties’ have supported the extension of the arbitration agreement to non-signatories by reference to traditional principles of contract law. In particular, the tribunals have often referred to the principles of representation or agency, which are basically founded upon consent.³⁸

However, reference to traditional principles of contract law in the context of ‘extension doctrines’ is problematic. In fact, it is contradictory to the essence of ‘extension doctrines,’ or at least superfluous: once the intention of the non-signatories to arbitrate has been “asserted” by reference to the doctrine of ‘group of companies’ or ‘equitable estoppel’, any additional reference to traditional principles of contract law has no relevance. Autonomous principles of inferring intention to arbitrate have been developed in the context of ‘extension doctrines’. For example, extension doctrines do not require an examination of whether the non-signatory acted as agent of the signatory. They require an examination of whether there is the “group

arbitration an existing controversy [...] shall be valid, irrevocable, and enforceable, *save upon such grounds as exist in law or in equity for the revocation of any contract.*” (emphasis added).

“Here, Counsel for claimant says that the pleadings and briefs amount to an agreement in writing to submit to arbitration an existing controversy, namely, the claim against second defendant. I have found that those documents were ambiguous as to whether first defendant consented to the joinder of second defendant. [...] The matter therefore falls within the emphasised passage from 9 U.S.C. 2 quoted above. The contract arising from the pleadings in Federal Court to arbitrate the claims against second defendant, if it ever existed, is revocable within the meaning of that passage”.

Arbitrator’s decision not to assume jurisdiction over the non-signatory on the above facts is questionable. The fact that the non-signatory contested the jurisdiction of the national courts invoking the arbitration agreement is conduct that clearly reveals ‘implied arbitral consent’. Rather than relying on the formal requirement of writing provided in the US FAA s.2, the arbitrator should have given effect to the real intention of the non-signatory to arbitrate.

³⁷ See ICC 5730 of 1988 (The *Orri* case), (1990) 117 *JDI (Clunet)* p.1029; (1992) *Rev. Arb.* p.25 with note Cohen. where the claimant initiated arbitration proceedings against two companies (enterprise X and company X SA) of the same group and an individual, who was a manager and a major shareholder of the group. Although a non-signatory, company X SA did not challenge the jurisdiction of the tribunal and, therefore, the tribunal naturally assumed jurisdiction over the non-signatory company X SA.

³⁸ ICC award no.1434 of 1975, (1976) *JDI (Clunet)* 978; ICC award no.5721 of 1990, (1990) 117 *JDI (Clunet)* 1029 or the *Orri* case, ICC 5730 of 1988, (1990) 117 *JDI (Clunet)* p.1029; (1992) *Rev. Arb.* p.25 with note Cohen.

structure” or “an active role” of the non-signatory (group of companies doctrine) or whether the non-signatory has obtained any benefit from or relies on the contract that including the arbitration agreement (equitable estoppel doctrine).

It follows that traditional contract law principles have independent rather than supplementary theoretical premises. Therefore, ‘consent to arbitrate’ is a requirement that must be met in full either by exclusive reference to extension doctrines or by exclusive reference to traditional principles of contract law. It cannot be a combination of the two. If anything, the supplementary reference to traditional principles of contract law principles indicates that tribunals, when referring to traditional principles of contract law in addition to extension doctrines, are in doubt about whether the extension of arbitration agreements to third parties can be justified solely on the basis of ‘extension doctrines’. Arguably, references to traditional principles of contract law are employed more to support the ‘extension doctrines’ than because the application of the traditional principles themselves is warranted under the factual circumstances of the case.

For example, the arbitral award in *C&M Farming Ltd v Peterson Farms Inc*³⁹ made specific reference to the agency theory in addition to the application of a ‘group of companies’ doctrine:

“The Tribunal considers that it was logical to have the name of one member of that group as the contracting partner with Peterson. One company had to take formal legal responsibility for the contract with Peterson. C&M Group, as such, was not a legal entity and therefore could not contract in its own name. There would have been greater uncertainty had it sought to do so. *Nasik* [later changed its name to C&M,] *contracted on behalf of and as the agent for the whole C&M Group*. This was clearly understood by Peterson”⁴⁰ (emphasis added)

The English Court, before which the award was challenged, rightly, commented on the application of the agency theory:

“Far from there being ‘greater uncertainty’ had the Agreement named ‘C&M Group’ as a party, on the tribunal's reasoning that would have been both accurate and well understood. In contrast the nomination of *Nasik* on that

³⁹ ICC award, on 10 March 2003, *C & M Farming Ltd v Peterson Farms Inc* (unpublished).

⁴⁰ *Ibid*, para 92.

reasoning created or at least increased any uncertainty. The last two sentences of par. 92 represent all that the tribunal said about ‘agency’. Not only do those sentences ignore the fact that no case in agency was ever advanced by C&M before the tribunal but had there been an agency relationship between C&M and ‘the whole C&M Group’ there would have been no need for C&M to advance the Group of Companies doctrine as it did nor for ‘one company to take formal legal responsibility for the contract’. That company could indeed have signed as agent as well as for itself⁴¹

6.2.2.4 Conclusions on the extension doctrines based on consent

In the light of the above, it seems clear that the assertion of implied consent requires the application of specific principles and techniques⁴² of interpretation which must reveal the “intention to arbitrate” with a degree of certainty, rather than probability.⁴³ In this interpretation process, the principle of *in favorem validitatis* cannot be applicable.⁴⁴ There can be no presumption in favour of the existence of the arbitration agreement, and therefore, no presumption in favour of the existence of the intention to arbitrate.⁴⁵

However, as this chapter demonstrated, it is doubtful whether such an intention to arbitrate can be ascertained with the necessary degree of certainty by reference to the

⁴¹ *Peterson Farms Inc. v C&M Farming Ltd*, [2004] 1 Lloyd's Rep. 603, Langley J, at 610.

⁴² See Fouchard, Gaillard and Goldman, *supra* n. 25, at para 477 et seq. referring to ‘the principle of interpretation in good faith’, which seeks to establish the actual intention of the parties, ‘the principle of effective interpretation’, giving favouring the interpretation enabling the clause to be effective over the interpretation preventing the clause from being effective, and ‘the principle of interpretation contra proferentem’ establishing the presumption that an agreement should be interpreted against the party that drafted the clause in dispute. Cf also, ICC case no. 1434 of 1975, ICC Arbitral Awards 1974-1985 (S. Jarvin and Y. Derains eds 1990), p. 264, where the tribunal accepted the extension of the arbitration agreement to a non-signatory company of a group, on the grounds of implied consent, ascertained by reasonable interpretation of the contract.

⁴³ Cf Fouchard, Gaillard and Goldman, *supra* n. 25, at para 472 “When determining whether or not the parties actually agreed to submit their disputes to arbitration, arbitrators and the courts apply various principles of interpretation. In the light of these principles, they establish the degree of certainty required for the parties’ consent to be effective as well as the scope of that consent.” and at para 482 “Case law shows that the primary concern shared by both arbitrators and the courts is to give full effect to the parties’ intention to refer their disputes to arbitration. This is true of both the degree of certainty required of the consent given by the parties and its scope”.

⁴⁴ Fouchard, Gaillard and Goldman, *supra* n. 25, at para 480: “It is equally inappropriate to resort to a general principle of interpretation *in favorem validitatis* or *in favorem jurisdictionis*, whereby arbitration agreements are to be interpreted extensively. Although it is true that arbitration is now a normal means of resolving disputes in international trade, and that arbitration agreements should therefore not be interpreted “restrictively” or “strictly,” it remains perfectly legitimate to choose to have one’s international disputes settled by the courts.

⁴⁵ See in more detail S. Brekoulakis, “The Notion of Superiority of Arbitration Agreements over Jurisdiction Agreements: Is it time to Abandon it?” 24 (2007) 4, *J Int’l Arb.*, p. 341 et seq.

‘group structure’ of the group of companies or the ‘active participation’ of the non-signatory company in the negotiation or the performance of the contract concluded by other companies of the same group. The above analysis of the relevant case law has shown that in some cases the ‘group structure’ or the ‘active participation’ are used as presumptions for the existence of the intention of the non-signatory to arbitrate, and thus as a presumption in favour of the existence of the arbitration agreement.⁴⁶ In this way the principle of consent is misapplied.

This is not to argue that the only safe way to ascertain consent is signature. A strict formalistic approach to the issue of consent is increasingly difficult to justify, in the context of contemporary international commerce.⁴⁷ Signature should be disassociated from the assertion of consent, or be used as one of several criteria to evidence consent to arbitrate. On the other hand, when the signature of the third party is missing, the intention to arbitrate must be ascertained by clear evidence rather than presumed by general reference to the “active role” of the third party in the negotiations or the performance of the substantive contract. It is inconsistent for the courts and tribunals on the one hand to accept that the group of companies must be applied on the basis of consent, and on the other hand infer consent on the basis of insufficient evidence

6.2.3 Limitations of extension doctrines not based on consent (non-consensual extension doctrines)

As has already been explained, ‘extension doctrines’ are based on consensual premises: it is necessary that signatories and non-signatories have actually consented to arbitrate. Nevertheless, there have been versions of “extension doctrines” which have deviated from this rule. Here, other factors than ‘consent’ are critical for the determination of whether a third party may be bound by an arbitration agreement. Thus, the term ‘extension’ of the arbitration agreement to third parties finds its literal meaning: it refers to an arbitration agreement binding a person that has never actually

⁴⁶ Cf Hanotiau, *Complex Arbitrations*, *supra* n. 14, p.98 : “The analysis of the arbitral awards also leads to the emergence of a rebuttable presumption that the parent company binds its subsidiaries”; Cf X.Y. Li. *La transmission et l’extension de la clause compromissoire dans l’arbitrage international*, 1993 (Dijon), p.321, who also argues that in the context of international arbitration the consent of the third party company should be presumed.

⁴⁷ See the discussion in Lew-Mistelis-Kroell, *supra* n.28, para 7-7 et seq.

consented to that arbitration agreement.⁴⁸ Two versions of extension doctrines are of particular interest.

The first is the ‘intertwined version’ of the “equitable estoppel” doctrine (intertwined estoppel) developed by the US courts. “Intertwined estoppel” suggests that a third party is bound by an arbitration agreement concluded between the two real parties if *the dispute between the third party and one of the real parties is closely intertwined with the underlying relationship between the real parties*. Here the extension of the arbitration agreement depends on how close the contractual relationships of the several parties are, rather than on whether the third and the real parties have consented to arbitrate their dispute.⁴⁹ Thus, it can be argued that the requirement of “consent” has been diminished -if not dispensed with- in the context of the intertwined version of the estoppel doctrine.

The second is the argument of the autonomous validity and effectiveness of arbitration agreements, advanced by the French courts in the context of the ‘group of companies’ doctrine. In particular, it has been argued that an arbitration agreement included in an international contract has an autonomous validity and effectiveness that calls for the extension of this arbitration agreement to parties that have been involved in the performance of the contract. As in the case of ‘intertwined estoppel’, here the extension of the arbitration agreement to third parties is not based on whether the third parties have actually consented to the arbitration agreement. It was the Cour d’appel of Paris in *Korsnas Marma v Durand-Auzias*, which first noted that:

“[...] la clause compromissoire insérée dans un contrat international a une validité et une efficacité propres qui commandent d’en étendre l’ application aux parties directement impliquées dans l’exécution du contrat et dans les litiges qui peuvent en résulter, dès lors qu’il est établi que leur situation et leurs activités font présumer qu’ elles ont eu connaissance de l’ existence et de la

⁴⁸ Cf ICC case no 5721, ICC Arbitral Awards 1974-1985 (S.Jarvin & Y Derains eds 1990). p. 404, where the term extension of arbitration agreements is wrongly employed to refer to the case where a non-signatory is bound by an arbitration agreement on the basis of an implied consent.

⁴⁹ See in particular *Choctaw Generation v American Home Assurance*, 271 F.3d 403 (2nd Cir.2001) and *McBro Planning & Development Co v Triangle Electronic Construction*, 741 F.2d 342, 343 (11th Cir. 1984).

portée de la clause d'arbitrage, bien qu'elles n'aient pas été signataires du contrat la stipulant.”⁵⁰

Since then, the argument of the autonomous validity and effectiveness of arbitration agreements has been reiterated by the Paris Cour d'appel in a number of cases.⁵¹ Despite the criticism of it,⁵² the theory of the 'autonomous validity and effectiveness' of arbitration agreements carries an intriguing implication, namely that in the context of international transactions mere awareness of the arbitration agreement rather than consent is enough for the valid conclusion of such an agreement. Moreover, the theory suggests that whenever a third party assumes a 'direct role'⁵³ in the performance of the main contract, this party should be presumed to be aware of the existence of the arbitration agreement included in the contract and, therefore, be bound by it. Thus, the key factor for a third party to be bound by an arbitration agreement is whether it has performed a 'direct role' in the performance of the substantive contract rather than whether the third party actually had any intention to arbitrate.

However, the argument of the autonomous validity and effectiveness of arbitration agreements is in direct conflict with the contractual nature of arbitration agreements. This criticism applies equally to the 'intertwined estoppel' adopted by the US courts. In both cases, the existence of arbitration agreements is in essence presumed, irrespective of whether the third party has actually consented to the arbitration agreement. The rationale behind both theories is that once the arbitration agreement is

⁵⁰ "...an arbitration clause included in an international contract has an autonomous validity and effectiveness, which calls for the clause to be extended to parties directly involved in the performance of the contract and in the disputes arising out of the contract, provided that it is established that their [the parties'] activities raise the presumption that they [the parties] were aware of the existence and the scope of the arbitration clause, and irrespective of the fact that they did not sign the contract including the arbitration agreement" (translation of the author); Paris Cour d'appel, 30 Nov. 1988, *Korsnas Marma v Durand-Auzias*, (1989) Rev. Arb., p.691, with note P.-Y. Tschanz.

⁵¹ Paris Cour d'appel, 14 February 1989, *Ofer Bros v Tokyo Marine and Fire Insurance*, (1989) Rev. Arb., p.691, with note P.-Y. Tschanz; Paris Cour d'appel, 11 January 1990, *Orri v Lubrifiants Elf Aquitaine*, (1992) Rev. Arb., p.95, with note D. Cohen; (1991) 118 J.D.I., p.141, with note B. Audit. It should be noted though that the Cour de cassation distanced itself from the argument for the autonomous validity and effectiveness of the arbitration agreement, adopted by the Cour d'appel. Instead, the Cour de cassation referred to "fraud aimed at concealing the identity of the real contractor" (fraude, destiné à dissimuler le véritable contractant) in order to uphold the extension of the arbitration agreement to the non-signatory (Cass 1e civ., June 11, 1991, *Orri v Lubrifiants Elf Aquitaine*, (1992) Rev. Arb., p.73, with note D. Cohen). See also Paris Cour d'Appel, 7 Dec 1994, *V 2000 v Project XJ 220 ITD et autre*, (1996) Rev. Arb., p.67, with note C Jarrosson (but not in the context of the group of companies doctrine); Paris Cour d'appel, 22 March 1995, *SMABTP et autre v Stationor et autre*, (1997) Rev. Arb., p.550.

⁵² See for example, Fouchard, Gaillard and Goldman, *supra* n. 27 paras 481 and 505.

⁵³ "...parties directement impliquées dans l'exécution du contrat".

validly concluded between the two original parties, fewer validity requirements should be needed for this arbitration agreement to bind a third party. Once an arbitration agreement ‘comes into existence’ there is no need for it to be concluded afresh with regard to a third party. This argument, however, although attractive at first sight, finds no support in contract law theory.

Arbitration agreements do not differ in terms of validity requirements from ordinary contracts.⁵⁴ For an arbitration agreement to be validly concluded, the general principles of contract law must apply. There is no provision in any arbitration law or arbitration treaty providing for more lenient validity requirements with regard to arbitration agreements than with regard to any ordinary contract. In fact, arbitration laws and treaties deal only with formal validity,⁵⁵ exactly because the requirements of substantive validity of arbitration agreements are left to general contractual principles.

The same must apply when determining whether an already existing arbitration agreement would bind a third party. The question here is, in effect, whether the minds of the third and the original parties actually met with regard to the arbitration agreements. The validity of the arbitration agreement must be determined independently for the third party. The same principles of contract law, applied for the conclusion of the arbitration agreement between the original parties, must also apply to determine whether the arbitration agreement has been “extended” to the third party.⁵⁶ An arbitration agreement, as is the case with any other contract, cannot bind a third party merely because it exists between two other parties.⁵⁷

The question of whether a third party is bound by an arbitration agreement or not *pertains to the existence or validity, rather than to the scope*, of the arbitration agreement. It is a matter as to whether an arbitration agreement between the third and the

⁵⁴ See Williston, *On Contracts*, (4th ed), ed. R. Lord, (WestGroup 2001) para 57:1; cf the US Supreme Court in *Doctor's Associates v Casarotto*, 116 S.Ct 1652, 517 U.S. 681 (1996) that refused to apply the special limits on the validity of arbitration agreements imposed by Montana statute, which limits were not applicable to ordinary contracts in general.

⁵⁵ See for example, NY art.II(2).

⁵⁶ See D. Cohen, note in Cour de cassation, 5 Jan 1999, and Cour de cassation, 19 Oct 1999, (2000) *Rev. Arb.*, p. 92, rightly noting that the validity of a contract does not entail the extension of this contract, and, thus, arbitration agreements cannot contravene the general principles of contract law in this regard (“la validité d’une convention n’entraîne pas sa transmission et on voit mal comment, de ce point de vue, la clause d’arbitrage pourrait défier à ce point la théorie générale des obligations”).

Cf also *Thomson-CSF v American Arbitration Ass’n*, 64 F.3d 773 (2d Cir. 1995) at 779, at 780: “A non-signatory may not be bound to arbitrate except as dictated by some accepted theory under agency or contract law”.

⁵⁷ “Contrat de fait”.

genuine parties validly exists, rather than whether the scope of an arbitration agreement between two parties covers a third party. General principles favouring arbitration and arbitration agreements apply to issues concerning the scope rather than the conclusion of arbitration agreements.⁵⁸ Therefore, there is no reason why consent of a third party should be dispensed with when an arbitration agreement already exists between two original parties. All the requirements of substantive validity of an arbitration agreement must be fully met with regard to the third party too.

Therefore, it is concluded that intention of the third party to arbitrate is an indispensable requirement for an arbitration agreement to bind this third party. As the US 2nd Circuit characteristically observed in *Thomson-CSF v American Arbitration Ass'n*:

“a non-signatory [cannot] be bound to an arbitration agreement with a less than full showing of some articulable theory under contract or agency law.”⁵⁹

Neither the ‘intertwined’ version of estoppel nor the argument for the ‘autonomous validity and effectiveness’ of arbitration agreements explains why the fundamental requirement of consent of a third party can be dispensed with in the case of arbitration agreements as opposed to ordinary contracts. The above theories fail to explain why an arbitration agreement, even in an international context, should have such autonomous validity and effectiveness deviating from the principle of privity.

Naturally, thus, the argument for the autonomous validity and effectiveness of arbitration agreements has been criticized.⁶⁰ Equally naturally, in recent years,⁶¹ there are signs that the US courts are becoming increasingly cautious in applying the intertwined version of equitable estoppel.⁶² On some occasions lately, the US courts have refused to apply the doctrine of equitable estoppel to bind a third party by an

⁵⁸ See *McCarthy v. Azure*, 22 F.3d 351 (1st Cir. 1994), at 355 noting that the federal policy favoring arbitration applies to issues concerning the scope of an arbitration agreement entered into consensually by contracting parties; it does not serve to extend the reach of an arbitration provision to parties who never agreed to arbitrate in the first place. Thus, requiring that arbitration rest on a consensual foundation is wholly consistent with federal policy.

⁵⁹ *Supra* note, at 780.

⁶⁰ Fouchard, Gaillard and Goldman, *supra* n. 27 paras 481 and 505; see also D. Cohen, note in Cass 1e civ., June 11, 1991, *Orri v Lubrifiants Elf Aquitaine*, (1992) Rev. Arb., p.73.

⁶¹ Especially after 2000, when *International Paper v Schwabedissen Maschinen & Anlagen GmbH* 206 F.3d 411 (4th Cir. 2000) was decided.

⁶² J.M. Townsend, “Non-Signatories in International Arbitration: an American Perspective”, paper in Conference of the International Council for Commercial Arbitration, Montreal 31 May-3 June 2006, p.10.

arbitration agreement. Instead, they have emphasized the importance of the consent of the third party.

For example, the 2nd Circuit in *Merrill Lynch Investment Managers v Optibase*,⁶³ characteristically noted that:

“it matters whether the party resisting arbitration is signatory or not”⁶⁴

In the same vein, the 1st Circuit in *InterGen N.V. v Grina*⁶⁵ observed that:

“the courts should be extremely cautious about forcing arbitration in situations in which the identity of the parties who have agreed to arbitrate is unclear”⁶⁶

6.2.4 The extension doctrines and the “writing requirement”

Before concluding the discussion on the extension of arbitration agreements to non-signatories, a few remarks should be made with regard to the writing requirement for a valid arbitration agreement. As has already been explained, the thesis argues that for an arbitration agreement to bind a ‘third party’, all the validity requirements for the arbitration agreement must be met with regard to this third party. This applies both to the formal and substantive requirements of arbitration agreements. There is no reason why the writing requirement should be relaxed with regard to the third party. As explained above, there are no convincing arguments to support the view that, once the arbitration agreement is formally concluded between two original parties, fewer validity requirements should be needed for this arbitration agreement to bind a third party.⁶⁷ Arbitration provisions providing for the writing form,⁶⁸ do not distinguish

⁶³ 337 F.3d 125 (2nd Cir. 2003).

⁶⁴ *Ibid* at 130.

⁶⁵ 344 F.3d 134 (1st Cir 2003).

⁶⁶ *Ibid* at 143, quoting *McCarthy v Azure*, 22 F.3d 351, 354-55 (1st Cir.1994) Cf also *E.I Dupont de Nemours & Co. v Rhone Poulenc & Resin Intermediaries* (269 F.3d 187, 204 (3d Cir. 2001)) and *Comer v Micor*, 436 F.3d 1098 (9th Cir.2006) confirming that “a non-signatory cannot be bound to arbitrate unless it is bound under traditional principles of contract and agency law to be akin to a signatory of the underlying agreement”.

⁶⁷ This was what the Swiss Federal Supreme Court held recently. In particular, in its decision of 16 October 2003, *X. S.A.L., Y. S.A.L. and A v Z, SARL and ICC Arbitral Tribunal*, CCI, BGE 129 III 727, it held that the writing form is an one off requirement need not to be met with regard to the third party. The Swiss Supreme Court held that if the original parties have agreed in writing in the first place the non-signatory party may be added to this arbitration agreement without its signature: Swiss PILA art. 178(1) does not require that the writing form is met again for the non-signatory. J-F Poudret has criticised the decision in “Note - Tribunal Fédéral, Ire Cour Civile, 16 octobre 2003, (4P.115/2003); Un statut privilégié pour l'arbitrage aux tiers?”, 2 (2004) 2 *ASA Bulletin*, p. 390. In the US of the *Fisser v Intr'l Bank*, 82 F.2d 231 (2nd Cir. 1960), at 233: “Under Federal Arbitration Act a written provision in any maritime transaction to settle by arbitration a controversy thereafter arising out of such transaction is the sine qua non of enforceable arbitration agreement, but it does

between the case where arbitration agreements are concluded for the first time and the case where they are “extended” to a third party once they have already been validly concluded.

A relatively recent ICC award stated:

“We note that when it is alleged, as here, that a non-signatory intended and consented to be a party to the arbitration agreement, then that intention or consent must be evidenced in writing”⁶⁹

After pointing out that the fact that the non-signatory did not sign the contract is evidence of the fact that it did not intend to commit itself either to the substantive or to the arbitration agreement, the tribunal concluded:

“No documents were produced from which it could be established:

- the existence of a written proposal to arbitrate from one party and a written acceptance communicated to the other Party; or
- an express acceptance by Respondent of the arbitration clause contained in Article 17 of the contract or;
- any arbitration agreement signed by [Claimant] and [Respondent] or contained in an exchange of letters or telegrams between [Claimant] and [Respondent] or in other written communications, made in accordance with the formal requirements provided for by Art. 178.1 PILA.

This conclusion is sufficient for this Tribunal to decline its jurisdiction”⁷⁰

This does not mean that the thesis supports that arbitration agreement should be required to be concluded in a writing form. On the contrary, the thesis shares the mounting criticism in the literature and caselaw of the writing requirement.⁷¹ Strict formal requirements for arbitration agreements have become, in the context of

not follow that under the Act an obligation to arbitrate attaches only to one who has personally signed written arbitration provision”.

⁶⁸ See for example, NY Convention art. II(2), Model Law art. 7(2), Swiss PILA art.178(1).

⁶⁹ ICC case no 10758 of 2000, 16 (2005) 2 *ICC Bull.*, p.92 at para 24.

⁷⁰ *Ibid*, para 25. The same in Partial Award in case 10818 of 2001, 16 (2005) 2 *ICC Bull.*, p.94.

⁷¹ See Lew, Mistelis and Kroell, *supra* n. 28, para. 7-7 et seq. *Shpere Drake Insurance v Marine Towing*, 16 F3d 666 (5th Circ 1994), or, Swiss Tribunal Federal, 16 January 1995, *Compagnie de Navigation et Transport v MSC* (1996) XXI YBCA 690.

contemporary international commerce, increasingly difficult to justify.⁷² Therefore, the writing requirement should be liberally construed. This, however, should apply equally when the courts and tribunals examine whether an arbitration agreement exists between the two original parties, and when they examine whether an arbitration agreement binds a 'third party'.⁷³ The debate on the writing requirement is not relevant to discussion on 'arbitration agreements and third parties'.

From a contractual point of view, there is no way to dispense with the writing requirement: an arbitration agreement, as any other contractual agreement, will bind a 'third party' only if both formal and substantive requirements of validity are fully met. That is why tribunals on many occasions have objected to the 'group of companies' doctrine on grounds of formal validity.⁷⁴ As the thesis explains in the next part, the writing requirement can be addressed in a more consistent way under a 'jurisdictional approach' to the issue of arbitration agreements and third parties.

6.3 CONCLUSIONS ON THE EXTENSION DOCTRINES AND THE CONTRACTUAL APPROACH

In the light of the above discussion, it can be concluded that the main weakness of the extension doctrines is the fact that, although they aim to apply to arbitration, they are not underpinned by rationale relating to arbitration in particular.

More specifically, the 'extension doctrines' based on consent fail to explain why consent of non-signatories to arbitrate should be more easily ascertained with regard

⁷² See N. Kaplan, "Is the Need for Writing as Expressed in the New York Convention and the Model Law out of Step with Commercial Practice?", (1996) 12 *Arb. Int.* p.27.

Cf ICC case no. 6769 of 1991, (1992) *JDI (Clunet)*, p. 1019 with note Y. Derains.

⁷³ See J-F Poudret "Note - Tribunal Fédéral, Ire Cour Civile, 16 octobre 2003, (4P.115/2003); Un statut privilégié pour l'arbitrage aux tiers?", 2 (2004) 2 *ASA Bulletin*, p. 390.

⁷⁴ Note, however, that there have been tribunals and national courts that have opposed to the 'group of companies' doctrine on the grounds that the formal requirement was not met with regard to the non-signatory. This would be particularly the case when the *lex arbitri* or the *lex fori* expressly provides for a writing requirement; see Partial Award in the ICC case no. 4402 of 1983, (1984) IX Yearbook Commercial Arbitration, P. Sanders (ed.), p. 138: here, the seat of tribunal was in Geneva (Switzerland); the Canton of Geneva has ratified the Swiss Intercantonal Arbitration Convention; article 6 of this Convention is mandatory and provides for a written document containing an arbitration clause. This written document has to fulfill the requirements of article 13 ss. of the Swiss Code of Obligations. If those are not complied with, a party may not be forced to submit a dispute to an arbitral tribunal.

Cf also the Interim Award in the ICC case no. 4505 in 1985 and 1986, (1986) 113 *JDI (Clunet)*, p. 1118; ICC Arbitral Awards 1986-1990 (Y. Derains, S. Jarvin and J.J. Arnaldez), p. 279.

Mustill and Boyd argue that in case the writing requirement is not satisfied the award resulting out of the arbitration, would not be enforceable, neither under the EAA ss 66 or 100 nor under the NY Convention, see Mustill and Boyd, *Commercial Arbitration, 2001 Companion* (Butterworths, 2001), p. 149.

to *arbitration agreements than with regard to any other contract*. Equally, the versions of ‘extension doctrines’, deviating from the requirement of consent fail to explain why *arbitration agreements, as opposed to ordinary contracts*, may dispense with the requirement of consent or the principle of privity.

Accordingly, all versions of ‘extension doctrines’ fail to explain why they should apply only to arbitration agreements and not to jurisdiction agreements.⁷⁵ What is the difference between an arbitration agreement and any other jurisdiction agreement in this respect?⁷⁶ Why should the well-established rule of legal independence of the several companies in the same group be abandoned *in the context of arbitration in particular*?

The failure of the extension doctrines to provide answers to the above questions can be explained by the fact that they focus only on the contractual characteristics of arbitration agreements. In the context of extension doctrines and the contractual approach in general, the discussion is limited to ‘consent’ or to the law applicable to determine the validity of arbitration agreements. However, from a contractual point of view, arbitration agreements have clear constraints: only those parties that have consented to arbitration may be bound by arbitration agreements. Moreover, consent of the parties has to be deduced in the same way as in any other contract. Any exception to these rules is exclusively provided by general principles of contract law. However, the latter provides for no exception from the principle of privity in relation to arbitration agreements as opposed to any other ordinary contract. No exception is provided either from the general contract interpretation principles applied to deduce or consent, which exception would allow consent to arbitration agreements to be ascertained more easily than in any other agreement. Therefore, the contractual

⁷⁵ See *Dayhoff v H.J. Heinz Co*, 86 F.3d 1287 (3rd Cir.1996), where the Third Circuit, held that an arbitration agreement cannot be extended to a third party on the grounds that the third party has close corporate links with a signatory party to the arbitration agreement, at 1297-98: “We also point out that Heinz Italia and H.J. Heinz Co should not by reason of their corporate relationship with Heinz Dolciaria be able to invoke the arbitration and forum selection clauses, *for there is no more reason to disregard the corporate structure with respect to such claims as there would be to disregard it with respect to other legal matters*” (emphasis added). Heinz Italia was the parent corporation of Heinz Dolciaria and, in turn, was a subsidiary of H.J. Heinz Co. At the end, it was held that the “third party” was bound by the arbitration agreement on contract law principles; in particular, it was held that the “third party” was as successor in interest to one of the original parties to the arbitration agreement in question.

⁷⁶ Cf the Supreme Court in *Scherk v Alberto-Culver Co.*, 417 U.S. 506, 519, 94 S.Ct. 2449, 2457, 41 L.Ed.2d 270 (1974) that classified an agreement to arbitrate before a specified tribunal as “a specialized kind of forum-selection clause”.

approach to the issue of arbitration agreements and third parties is constrained by the limitations of arbitration agreements as ordinary contracts.

A jurisdictional approach is lacking. Arbitration agreements have important jurisdictional effects. Arbitration law is not, and should not be viewed merely as an advanced version of contract law. *Arbitration has significant jurisdictional implications that go beyond the contractual origins of arbitration.* Focusing exclusively on the contractual nature of arbitration agreements obscures the real issue here, which is *whether arbitration agreements may have any jurisdictional implications vis-à-vis 'third parties'*. The focus should be on whether arbitral tribunals may assume *jurisdiction* over third parties and if so, under what circumstances.

In this jurisdictional context, the consensual character of arbitration agreements clearly remains relevant: an arbitration agreement outlines the jurisdictional basis of an arbitral tribunal. However, as the next part will show, in order to determine the full spectrum of jurisdiction of an arbitral tribunal, discussion should not be limited to the scope of an arbitration agreement. There are important jurisdictional considerations that should also be taken into account in the discussion of arbitration and third parties.

PART III: THE SUGGESTION FOR A JURISDICTIONAL APPROACH TO THE ISSUE OF THIRD PARTIES AND ARBITRATION

The thesis in Part II offered a detailed account of the contractual approach and extension doctrines in particular. Chapter 6 demonstrated the conceptual and practical limitations of extension doctrines and concluded that the contractual approach cannot deal satisfactorily with the problems relating to the issue of third parties in arbitration. From a strict contractual viewpoint, arbitration agreements as any other ordinary contract have inherent constraints: they bind only those persons that have clearly consented thereto. In this contractual context, consent is the indispensable requirement for a person to be bound by an agreement, and it can neither be substituted nor presumed. Otherwise, fundamental principles of contract law and contract interpretation would be violated.

Part III puts forward the main suggestion of the thesis. It argues for the substitution of the contractual with a jurisdictional approach to the issue of arbitration and third parties. In particular, the main argument, here, is that the issue of third parties in arbitration can be better addressed, if the focus is shifted from the contractual nature of arbitration agreements to their *jurisdictional effects*. Arbitration agreements differ from any other substantive contract in that they have significant jurisdictional effects. It is suggested that the discussion should be focused on the *dispute pending before the tribunal* and on *any implications the dispute may have for third parties*, rather than on the requirement of consent to arbitration agreements, as is the case with the prevailing contractual approach.

More specifically, Chapter 7 presents in detail the conceptual premises of the suggested *jurisdictional approach*. Necessary corollary of the jurisdictional approach is the concept of *effective arbitral jurisdiction*, according to which a tribunal should be able to assume as much jurisdiction as is necessary for the tribunal to achieve its main goal, namely the resolution of the pending dispute. Therefore, the pending dispute should play a key role for the determination of the jurisdiction of a tribunal. As is argued here, a tribunal in order to assert its jurisdiction should not only examine the scope of an arbitration agreement but it should also take into account the full implications of the dispute pending before it. This is particularly necessary when third parties to an arbitration agreement are integral part of the dispute pending before the

tribunal. Indeed, as will be demonstrated, when the pending dispute necessary implicates third parties, arbitration agreements may produce jurisdictional effects *that stretch beyond their contractual boundaries and the genuine parties thereto*. In fact, it is argued here, arbitration agreements may have *collateral jurisdictional effects on persons never consented thereto, i.e. third parties*.

Since tribunals should be able to assume as much jurisdiction as is necessary for them to resolve the pending dispute and since arbitration agreements may stretch beyond their contractual origins, the thesis argues that it is possible for a tribunal to assume *extra-contractual jurisdiction*. As will be particularly emphasised, it is only in *extremely exceptional circumstances and with particular caution* that a tribunal should assume extra-contractual jurisdiction. However, the aim of Chapter 7 is to demonstrate that *as a matter of principle* extra-contractual jurisdiction is not incompatible with arbitration.

The argument for extra-contractual jurisdiction and the jurisdictional approach, in general, is exemplified first, by reference to the extra-contractual *lis pendens* effect of arbitration agreements which has been repeatedly accepted by case-law (section 7.1.1). Secondly, by a cautious analogy to the extra-territorial jurisdiction assumed under certain circumstances by national courts (section 7.1.2).

As is explained in this chapter, tribunals may assume extra-contractual jurisdiction over third parties by applying third party-mechanisms, such as joinder, interpleading, intervention or consolidation.

While Chapter 7 establishes that as a matter of principle and under exceptional circumstances, a tribunal *may* assume extra-contractual jurisdiction over third parties and apply third-party mechanisms, Chapter 8 addresses some equally important issues: first, it examines whether a tribunal *should* assume extra-contractual jurisdiction and apply third-party mechanisms. Here, the thesis embarks on a policy-oriented analysis, which will show that third-party mechanisms are necessary in the context of international arbitration. There are important policy reasons suggesting that arbitration despite its contractual basis should not remain a closed system, reserved only for the parties that have agreed to an arbitration agreement. Instead arbitration should be a dispute resolution system, which -under particular circumstances- should be open to relevant third parties. A procedural system of communication between genuine and third parties should be established in arbitration.

Secondly, it explores *the rationale behind third-party mechanisms in general*: what purposes do they serve and how do they operate. The exploration of this question takes place against a comparative background of several national and regional procedural systems. It is suggested that the key-element for third-party mechanisms is the pending dispute and the implications of this dispute for third parties in terms of substantive liability and interests.

In particular, it will be shown that the extent to which a third party may participate in the proceedings between two original parties is directly relevant to the *degree of association between the third party and one of the original parties, in terms of substantive liability and interests*. Here, the rule is, *the closer the substantive association between the original and the third party, the more effective are the third-party mechanisms provided by procedural systems*. More specifically, third-party mechanisms of *compulsory character* are provided when the third party and the original parties are *strongly associated in substantive terms*, whereas third-party mechanisms of *permissive character* are provided when the third party and the original parties are *contractually interrelated but not strongly associated* in substantive terms.

The above analysis puts the discussion on arbitration and third parties in a wider comparative context. More importantly though, the outcome of this analysis will be used in Chapters 9 and 10 as policy guidelines in order for the thesis to determine the general conditions required for a tribunal to assume extra-contractual jurisdiction and apply third-party mechanisms. Thus, the findings on the rationale behind third-party mechanisms in general will be applied to arbitration against the backdrop of the particular principles prevailing in arbitration and, in particular, the principle of procedural party autonomy. More specifically, Chapter 9 and 10 examine whether third-party mechanisms are compatible or not with the widely accepted freedom of the parties to determine the forum and the procedures for the resolution of their disputes in the way it best serves their commercial interests. It should be noted that the analysis here is also taken from a jurisdictional viewpoint. Thus, third-party mechanisms are tested against the principle of procedural party autonomy in terms of “jurisdictional intensity”.

In particular, Chapter 9 demonstrates that in the majority of the cases the principle of procedural party autonomy should prevail, rendering third-party mechanisms inapplicable to arbitration. It is argued here that the right of the parties to arrange for a

scheme of several bi-lateral procedures rather than providing for third-party mechanisms should be upheld by courts and tribunals, even if this scheme would result to the jurisdictional fragmentation of the multiparty contractual relationship. Jurisdictional fragmentation, despite its unfavourable consequences, should be accepted as a legitimate repercussion of procedural party autonomy.

However, Chapter 10 argues that there are exceptional circumstances where third-party mechanisms should take precedence over procedural party autonomy. It is suggested that this should happen whenever third parties are strongly interrelated with the genuine parties to the arbitration agreement, so that third and genuine parties are *co-liable or co-holders of rights and duties*. This will typically be the case regarding false third parties of the first group, as defined in Chapter 2. As will be demonstrated, in such a case the several parties (third and genuine) constitute *an inseparable unit in terms of jurisdiction*. This jurisdictional unit, due to the strong substantive interrelations of the several parties, should not be separated and, therefore, it should prevail over the scheme of several bilateral dispute resolution agreements between the several parties. Accordingly, a tribunal should be able to assume jurisdiction over the whole jurisdictional unit, of the several genuine and third parties.

Chapter 11 makes the final remarks on the jurisdictional approach and discusses its practical relevance and advantages over the contractual approach.

The discussion on arbitration and third parties would have been incomplete without looking into the effect that arbitral awards may produce on third parties. Thus, in Chapter 12, the attention is shifted from arbitration agreements to arbitral awards. Here, it is argued that arbitral awards should produce a third-party effect, affecting a wider circle of third parties than just the parties to the proceedings and their privies. The suggestion lying behind this argument is that the problems arising out of multiparty situations may be addressed more effectively by a arbitral award than by an arbitration agreement.

CHAPTER 7: THE CONCEPTUAL PREMISES OF THE JURISDICTIONAL APPROACH:
EFFECTIVE ARBITRAL JURISDICTION AND EXTRA-CONTRACTUAL JURISDICTION127

7.1 <i>The extra-contractual lis pendens effect of arbitration agreements in the context of multiparty relationships</i>	129
7.2 <i>National courts and extraterritorial jurisdiction: the case for application by analogy in the context of arbitration</i>	134

**CHAPTER 7: THE CONCEPTUAL PREMISES OF THE JURISDICTIONAL
APPROACH: EFFECTIVE ARBITRAL JURISDICTION AND EXTRA-
CONTRACTUAL JURISDICTION**

Extension doctrines largely view arbitration agreements as ordinary contracts. Undisputedly, arbitration agreements have contractual origins. Contract law provides for the same requirements for their valid conclusion as for any other substantive contract. However, arbitration agreements may extend beyond their contractual origins. They have important jurisdictional effects. *Arbitration law is not, and should not be viewed merely as an advanced version of contract law.* It is predominately related to jurisdictional issues. Accordingly, arbitration agreements differ from ordinary contracts in that they provide tribunals with significant jurisdictional powers. These jurisdictional powers are necessary for a tribunal to achieve its primary goal: the resolution of the dispute at hand.¹ Therefore, in order to achieve its primary goal, a tribunal should be able to assume as much jurisdiction as necessary to resolve the dispute effectively (the *effective arbitral jurisdiction*).

Therefore, as soon as a dispute, which falls under the scope of an arbitration agreement, arises the jurisdictional effects of that arbitration agreement take effect. An arbitration agreement provides a tribunal with the necessary power to determine the pending dispute. However, nonetheless, the jurisdiction assumed by a tribunal has repercussions that stretch beyond the contractual constraints of an arbitration agreement and the parties that originally concluded this agreement. This can be exemplified by the following:

¹ Cf EAA s. 1(a): “*the object of the arbitration is to obtain the fair resolution of disputes...*” (emphasis added).

First, once a tribunal is constituted, its judicial powers are determined by a network of national and international provisions in wider terms than is provided in the arbitration agreement.² These national and international provisions provide tribunals with jurisdiction that is to a great extent *similar* to the jurisdiction assumed by national courts. For example, US Federal Arbitration Act s.7 provides that:

“the arbitrators [...] may summon in writing any person to attend before them or any of them as a witness and in a proper case to bring with him or them any book, record, document, or paper which may be deemed material as evidence in the case.[...]. Said summons shall issue in the name of the arbitrator or arbitrators, or a majority of them and shall be signed by the arbitrators, or a majority of them, and shall be directed to the said person and shall be served in the same manner as subpoenas to appear and testify before the court”.³

A tribunal may also appoint experts or legal advisers.⁴ These powers come as a corollary of the judicial role assumed by an arbitral tribunal, and are necessary for the latter to resolve the dispute.

Secondly, an arbitral award is enforced as a national judgment rather than as a contract. This fact reflects the public character of the judicial mandate assumed by a tribunal. In other words, an arbitral award comes as a corollary of the jurisdictional power that a tribunal has to determine a dispute in an authoritative way. Hence, an arbitral award is vested with the power of *res judicata*.⁵

Thirdly, and most importantly, the *lis pendens* effect of a dispute covered by an arbitration agreement goes beyond the circle of the parties that have concluded the arbitration agreement. This can be demonstrated from the following.

² See for example EAA s.33 et seq. and in particular ss.34, 37, 38, 39, 41; *cf* also Model Law art. 19 et seq.

³ *Cf* also EAA s.38.

⁴ See for example EAA s.37.

⁵ See Restatement (Second) Judgements. (1982), para.84; in England see *Fidelitas Shipping Ltd v V/O Exportchleb*, [1965] 1 Lloyd's Rep 13; Merkin, *Arbitration Law*, (LLP London) para.16.116. In France see NCPC art.1476 (for domestic arbitration) and art.1500 (for international), see also Cass. Soc. 19 March 1981, (1982) *Rev Arb.*, 44; in the Netherlands Arbitration Act 1986, art.1059; in the Belgian Judicial Code art.1703(1); in the new Austrian CCP s. 607; *cf* also the Hong-Kong Arbitration Ordinance, ss. 2GG (applicable to both domestic and international arbitration), 40B.2 (domestic only) and 42 (international only).

7.1 THE EXTRA-CONTRACTUAL *LIS PENDENS* EFFECT OF ARBITRATION AGREEMENTS IN THE CONTEXT OF MULTIPARTY RELATIONSHIPS

Enforcement of arbitration agreements is secured by a coherent framework of international and national provisions. Thus, by reference to provisions such as the New York Convention art.II(3), the English Arbitration Act 1996 s.9 or the Model Law art.8, national courts will normally safeguard the exclusive jurisdiction of a tribunal, by preventing a party to an arbitration agreement from bringing an action in respect of a matter falling under the jurisdiction of a tribunal.⁶ However, as their wording indicates, the above provisions apply only to genuine parties to an arbitration agreement, i.e. persons that are contractually bound by an arbitration agreement.⁷ The scope of their application does not cover third parties.⁸

Nonetheless, as will be shown, national courts have on several occasions stayed proceedings between a party to an arbitration agreement and a third party, on the ground that the action was inextricably involved with the subject matter of the arbitration agreement in question. Normally, national courts would have jurisdiction over a party not bound by an arbitration agreement. However, national courts have shown considerable reluctance to examine a dispute involving a third party to an arbitration agreement, when this dispute is intertwined with the subject matter of that arbitration agreement. National courts would not risk pre-empting the dispute between the two genuine parties to an arbitration agreement. In other words, they would not risk frustrating the exclusive jurisdiction of a tribunal over this particular dispute. In a case like the above, it is the jurisdiction rather than the contractual effect of an arbitration agreement that prevents the national courts from examining a dispute involving a third party. Ordinary contracts between two parties cannot prevent third

⁶ Unless the arbitration agreement is null and void, inoperative or incapable of being performed.

⁷ See British Columbia Court of Appeal, Canada, 10 March 2002, published in CLOUT case No. 31; British Columbia Supreme Court, Canada, 31 January 1996, published in CLOUT case No. 178; *Nanhai West Shipping Co. v Hong Kong United Dockyards Ltd*, 11 December 1996, (unpublished) available at <http://www.lexis.com>. The same M. Mustill and S. Boyd, *Commercial Arbitration*, (2nd ed., Butterworths London-Edinburgh 1989 and 2001 Companion) p.471; cf also the wording of the provisions: NY, art II(3) "...in a matter in respect of which *the parties* have made an agreement ..."; EAA s.9(1) "*A party* to an arbitration agreement..."; Swiss PILA art.7 "if *the parties* have concluded an arbitration agreement..." (emphasis added).

⁸ Although EAA s.82 provides that "a party to an arbitration agreement includes any *person claiming under or through a party to the agreement*", the phrase "person claiming under or through a party" is generally construed quite narrowly, applying for examples to assignees, but excluding persons such as guarantors from being treated as parties to the arbitration agreement, see R.Merkin, *Arbitration Law*, (Lloyd's London 1991), para. 1.37.

parties from exercising their own rights and claims. It is reasonable to argue that, *once the dispute arises, an arbitration agreement may have jurisdictional effects that stretch beyond the parties to that arbitration agreement*. In fact, it may have a *collateral effect on third parties*. This will apply particularly to false third parties, i.e. third parties with an interest in the dispute between the two genuine parties to the arbitration agreement.

For example, in *Morrie Mages v Thrifty Corporation*,⁹ a creditor filed a suit against a guarantor to recover on the guarantee agreement. The guarantor moved for a stay of the court proceedings pending the outcome of the arbitration between the creditor and the debtor, although the guarantor was not a party to the arbitration agreement binding the creditor and the debtor. While the district court denied the motion and proceeded with the merits of the dispute, the seventh Circuit overturned the decision of the district court decision and granted the stay. The seventh Circuit made clear that the guarantor was not bound by the arbitration agreement including in the main contract between the creditor and the debtor. The stay was not granted because the guarantor was a *party* to the arbitration agreement:

“Thrifty's [the guarantor] alternative claim that it is entitled to a stay because it is a party to the arbitration agreement is belied by the record. The Guaranty does not contain an arbitration clause and does not incorporate the arbitration provision of the Agreement between the Mages [creditor] and MC [debtor]”¹⁰

Nevertheless, the court noted that it had a *discretionary power* to grant the stay, because a decision of the court on whether the guarantor was liable against the creditor, would pre-empt the decision of the tribunal on whether the debtor was liable or not. In other words, it would frustrate the exclusive jurisdiction of the tribunal.

The court explained that:

“Under the plain language *of the contract as a whole*, Thrifty's [the guarantor] indisputable absolute liability does not arise until an arbitrator resolves the issues of whether MC [debtor] defaulted”.¹¹ [...]

“The claim in this case requires a showing of liability against MC, an undisputed party to the arbitration agreement, as a predicate to recovery

⁹ 916 F.2d 402 (7th Cir. 1990).

¹⁰ *Ibid*, at 406 note 1.

¹¹ *Ibid*, at 407.

against Thrifty, a disputed party to the arbitration agreement. [...] The amount of Thrifty's liability under the Guaranty (if indeed Thrifty is liable) is coterminous with the amount of MC's liability under the Note and Agreement [...] The resolution of the issue of whether Thrifty is liable under the Guaranty and the extent of such liability is, thus, completely dependent upon the arbitrable issues of the fact and extent of MC's liability”¹²

The Court cited *McCowan v Sears, Roebuck and Co.*¹³:

“Although fashioned as two separate lawsuits, there is in reality a single "controversy" at issue[...].”

the court concluded that the surety is entitled to a stay of the litigation

“regardless of its status as a party to the arbitration agreement.”

Otherwise, according to the Court, there would be:

“a potential for impairment of the issues before the arbitrator due to the collateral estoppel effect of the Mages -Thrifty litigation.”

In *Hill, Grimes and Canatxx Energy Ventures v G E Power Systems et al.*,¹⁴ an energy company and a project developer entered into a contract, containing an arbitration agreement. Pending arbitration between the two of them, the former filed a suit before the US courts against the latter and another company (the lender) that had secured the finance of the project. Both defendants applied for a stay of the court proceedings on the basis of the pending arbitration, although the lender was neither a party to the arbitration agreement nor the arbitration proceedings.

The Second Circuit held that the claim against the lender was inherently inseparable from the claim against the project developer in the main agreement, which contained arbitration clause, and, consequently, the court proceedings should be stayed even though the lender was not a party to the arbitration agreement.¹⁵

The court was reluctant to determine part of the dispute that was pending in arbitration and noted that the stay must be granted whenever

¹² *Idem*

¹³ 908 F.2d 1099, 1106 (2d Cir. 1990), *cert. denied*, 498 U.S. 897, 111 S. Ct. 250, 112 L. Ed. 2d 209 (1990), at 1106.

¹⁴ 282 F.3d 343 (5th Cir. 2002).

¹⁵ The same was held in *Subway Equipment Leasing Corp. v Forte*, 169 F.3d 324 (5th Cir.1999) and in *Harvey v Joyce* 199 F.3d 790 (5th Cir.2000).

“the determination of factual and legal issues related to the claims brought against the non-signatories [...] would be the subject of an arbitration proceeding between signatories to the arbitration agreement”.¹⁶

US courts held similarly in two cases in the context of group of companies.

First, in *Dale Metals v KIWA*,¹⁷ a US company and a Japanese manufacturer entered into a sales agreement, containing an arbitration agreement. Pending arbitration proceedings between the US and the Japanese party, the former alongside with its parent company filed a lawsuit before the US courts against the Japanese manufacturer and its two US distributors. The defendants applied for a stay on the basis of the pending arbitration between the US subsidiary and the Japanese manufacturer. Although not all parties in litigation were parties to the arbitration agreement or to the arbitral proceedings, the District Court of New York granted the stay. The court observed:

“In short, it is fair to say that in an arbitration proceeding between [the parties to the arbitration agreement], every issue that is raised here [under the court proceedings] will be vigorously pressed. In such circumstances a stay is appropriate *even though it affects parties who are not bound to arbitrate*”¹⁸ (emphasis added).

Secondly, in *Lawson v Akzona*,¹⁹ a dispute arose out of a sale agreement, containing an arbitration agreement. Pending arbitration proceedings between the parties (Lawson and Blanchard) to the sale agreement over whether the goods sold were of the contractual standards, the claimant filed a suit before courts against the respondent in the arbitration proceedings and its parent company, on the basis of fraud and misrepresentation. The second defendant (parent company) was not a party to the sales agreement or the arbitration agreement included therein. Nonetheless, the court stayed its proceedings with regard to both defendants by reference to the arbitration agreement and the dispute pending before the tribunal.

The court noticed:

¹⁶ *Supra* n. 12. at 347.

¹⁷ 442 F.Supp.78 (SDNY 1977).

¹⁸ *Ibid*, at 81.

¹⁹ 355 F. Supp. 1146 (S.D.N.Y.), *aff'd* 486 F.2d 1394 (2d Cir. 1973).

“The claims against Akzona [the parent company of the respondent to the arbitration] basically involve the allegation that it conspired with and encouraged Blanchard to deliver improper, mislabelled goods in order to defraud Lawson. The decision of the arbitration as to whether, in fact, Lawson has been defrauded will inevitably decide whether non-conforming and mislabelled goods were delivered, and, thus, will at least partially determine the issues which form the basis of the claim against Akzona. If the arbitration finds no mislabelling or misrepresentation, then the claims of plaintiffs against Akzona will also be repudiated.”²⁰

The court made clear that it intended to preserve the exclusive jurisdiction of the arbitral tribunal to resolve the dispute by extending the stay to persons that were not parties to the arbitration agreement.

“Lastly, we agree with the statement made by Judge Coffin of the First Circuit in *Hilti, Inc. v Oldach*, 392 F.2d 368 (1968), where he said: ‘If arbitration . . . could be foreclosed simply by adding as a defendant a person not a party to an arbitration agreement, the utility of such agreements would be seriously compromised.’ If this Court were to allow Lawson to prevent the arbitration of these issues by the naming of Akzona as a party to this action, the Federal policy in favour of arbitration would be thwarted”²¹

Similar decisions of US courts can be found in the context of construction disputes, where proceedings between a sub-contractor and the surety of the main contractor on its payment bond have been stayed, pending arbitration between the contractor and the sub-contractor.²²

In the same vein, courts in other jurisdictions have stayed court proceedings initiated by or against third parties to arbitration agreements. In England, in *Reichhold Norway A.S.A. and another v. Goldman Sachs International*,²³ the defendants had been engaged as agents by a Norwegian company to advise in and negotiate the sale of one of its subsidiaries to the claimants. The sale was concluded between the

²⁰ *Ibid*, at 1151.

²¹ *Idem*.

²² See *United States v Continental Casualty*, 214 F. Supp. 947 (U.S. Dist. 1963) and in *J & S Construction v Travellers Indemnity Company*, 520 F.2d 809 (U.S. App. 1975), *Warren Bros. v Cardi Corp.*, 471 F.2d 1304 (1st Cir.1973).

²³ [2000] 1 W.L.R. 173.

claimants and the Norwegian company. It contained an arbitration agreement providing for arbitration in Norway. The claimants began an action in England against the defendants, claiming damages for negligent misstatement, and then commenced arbitration proceedings in Norway against the seller Norwegian company. The defendants, although not bound by the arbitration agreement, asked for a stay of the court proceedings, pending arbitration between the claimants and the sellers. The Court of Appeal upheld the decision of the High court to grant the stay exercising *its inherent jurisdiction*.²⁴ This sort of inherent jurisdiction of the court to stay proceedings between a genuine and a false third party has been recognised in other cases too.²⁵

In Singapore, the High Court, granted a stay of the court proceedings between a project developer and an architect, pending arbitration between the architect and a contractor with regard to disputes concerning the same construction project, although the project developer was not a party to the arbitration agreement.²⁶

7.2 NATIONAL COURTS AND EXTRATERRITORIAL JURISDICTION: THE CASE FOR APPLICATION BY ANALOGY IN THE CONTEXT OF ARBITRATION

By analogy, the jurisdictional approach and the extra-contractual jurisdiction of arbitral tribunals, suggested here, find further support in the “extra-territorial jurisdiction” assumed, under certain circumstances, by national courts. As a general rule, jurisdiction in the context of national litigation is determined on a territorial basis. More specifically, national courts of a particular state will assume jurisdiction over a defendant that is resident, domiciled or present within the geographical

²⁴ Preserved by section 49(3) of the Supreme Court Act 1981.

²⁵ See for example *McAlpine Construction v Unex*, [1994] 38 Con LR 63 (CA); *Mabey and Johnson Ltd v Jonathan Laszlo Danos, Barry Joyce, Deryck A Gibson Ltd, Deryck Gibson* [2007] EWHC 1094 (Ch), although in these cases, on the basis of the specific facts the stay was not granted at the end.

²⁶ 31 August 2005, *Yee Hong Pte Ltd v Tan Chye Hee, Andrew and Ho Bee Development Pte Ltd*, published in Lawnet - Singapore Court Judgments, reproduced in www.Kluwerarbitration.com (last visited 16 June 2007). It should be noted however, that the court held that a project developer should be understood as a *person claiming through or under an architect who was a party to the arbitration agreement with the contractor*, provided in s. 6 (5) of the Arbitration Act of Singapore. This is an unusually wide meaning to the term “person claiming through or under a party to an arbitration agreement”; cf the very narrow construction generally accepted with regard to the same term in EAA, see *supra* n. 8.

boundaries of that state.²⁷ Whenever a dispute involves several persons, national courts may assume jurisdiction over all these persons by virtue of multiparty mechanisms provided in their national laws. When all the several persons domicile in the territory of a single state, national courts of that state will have no difficulty to assume jurisdiction over them on the basis of the rule of *territorial jurisdiction*.

However, there might be that some of the persons, considered necessary for the resolution of the pending dispute, are not linked in territorial terms with the state of the national courts exclusively seised of that dispute. In such cases, it is accepted that national courts may exercise *extra-territorial jurisdiction* over those persons, whose presence in the proceedings is considered necessary, even though they have no domicile, residence or presence in the state of these national courts.

For example, in England courts have assumed overseas jurisdiction on many occasions.²⁸ In particular, extra-territorial jurisdiction may be assumed by virtue of CPR 6.20, entitled “Service out of the jurisdiction where the permission of the court is required”. Rule 6.20(3) and (3A) read:

“[...] a claim form may be served out of the jurisdiction with the permission of the court if-

[...] (3) a claim is made against someone on whom the claim form has been or will be served (otherwise than in reliance on this paragraph) and-

(a) there is between the claimant and that person a real issue which it is reasonable for the court to try; and

²⁷ See for example French NCPC art. 42, or European Regulation 44/2001 art.2, under which the *domicile* of the defendant will be the relevant criterion for the courts to determine their jurisdiction. In England, under the Civil Jurisdiction and Judgments Act 1982 Part II section I art. 2 jurisdiction will also be determined in accordance with the domicile of the defendant, whereas under common law *presence* can also be used as a factor to establish jurisdiction, see *John Russell and Co Ltd v Cayzer, Irvine and Co* [1916] 2 AC 298, HL; *cf* also Restatement of Judgments (second): para 4 “The relevance of territorial boundaries to the exercise of jurisdiction by states within the federal union, and by courts of this country within the international community, arises from the fact that the states and nations are defined as political and legal entities in terms of their geographical boundaries. Since these entities are legally defined in terms of geographical place, the geographical location of a transaction is significant in determining whether a court of such an entity may properly exercise jurisdiction in a particular controversy”.

²⁸ *United Film Distribution Ltd v Chhabria* [2001] EWCA Civ 416 [2001] 2 All E.R. (Comm) 865 (CA); *Barings Plc (in Administration) v Coopers & Lybrand*, [1997] I.L.Pr. 12; *Petroleo Brasileiro SA v Mellitus Shipping Inc (The Baltic Flame)*, [2001] EWCA Civ 418; [2001] 1 All E.R. (Comm) 993 (CA). See also Ian Brownlie, *Principles of Public International Law*, (5th ed Oxford 1998) p.301, calling for extra-territorial jurisdiction of national courts for companies that belong to the same group of companies.

(b) the claimant wishes to serve the claim form on another person *who is a necessary or proper party to that claim*;

(3A) a claim is a Part 20 claim and the person to be served is a *necessary or proper party to the claim* against the Part 20 claimant” (emphasis added)²⁹

Similarly, courts in the US³⁰ and other common law jurisdictions have also asserted extra-territorial jurisdiction over foreign companies.³¹

Thus, for example, in *Frummer v Hilton Hotels International, Inc.*,³² where New York Courts assumed jurisdiction over Hilton Inc., a company incorporated in England.³³ The court noted:

“We are not unmindful that litigation in a foreign jurisdiction is a burdensome inconvenience for any company. However, it is part of the price which may

²⁹ CPR 6.20(3) replaced the similar Ord. 11 r. 1(1)(c) of the 1965 Rules.

³⁰ See for example cases where courts in the US have assumed jurisdiction over foreign companies: *Bryant v Finnish Nat. Airline*, 15 N.Y.2d 426, 260 N.Y.S.2d 625, 208 N.E.2d 439 (1965); *Taca Intern. Airlines v Rolls-Royce of England*, 15 N.Y.2d 97, 256 N.Y.S.2d 129, 204 N.E.2d 329 (1965); *Wells Fargo & Co. v Wells Fargo Exp. Co.* 556 F.2d 406 (9th Cir. 1977).

Cf rules Restatement (Second) Conflict of Laws, para 42:

“Principles Underlying Judicial Jurisdiction Over Foreign Corporations:

(1) A state has power to exercise judicial jurisdiction over a foreign corporation if the relationship of the corporation to the state is such as to make the exercise of such jurisdiction reasonable.
(2) The relationships which are sufficient to support an exercise of judicial jurisdiction over a foreign corporation are stated in paras 43-52”

See also Fed.Rules Civ.Proc. rule 4(d)(3, 7), (e), (e)(1), (f), (i)(1), 28 U.S.C.A. See

³¹ Extraterritorial jurisdiction is also accepted in Canada, see Castel, *Canadian Conflict of laws* (4th Ed, 1997) para 126; and in New Zealand see NZ High Court Rule 219.

³² 19 N.Y.2d 533, 227 N.E.2d 851, 281 N.Y.S.2d 41 ((1967).

³³ *Cf* in general the New York Civil Practice Law Rules para 302, *Personal Jurisdiction By Acts Of Non-Domiciliaries*:

(a) Acts which are the basis of jurisdiction. As to a cause of action arising from any of the acts enumerated in this section, a court may exercise personal jurisdiction over any non-domiciliary, or his executor or administrator, who in person or through an agent:

1. transacts any business within the state or contracts anywhere to supply goods or services in the state; or
2. commits a tortious act within the state, except as to a cause of action for defamation of character arising from the act; or
3. commits a tortious act without the state causing injury to person or property within the state, except as to a cause of action for defamation of character arising from the act, if he
 - (i) regularly does or solicits business, or engages in any other persistent course of conduct, or derives substantial revenue from goods used or consumed or services rendered, in the state, or
 - (ii) expects or should reasonably expect the act to have consequences in the state and derives substantial revenue from interstate or international commerce; or
4. owns, uses or possesses any real property situated within the state.

properly be demanded of those who extensively engage in international trade.”³⁴

Unlike the case in litigation where the jurisdiction of national courts is determined on a territorial basis, the jurisdiction of arbitral tribunals is determined on the basis of a contract, namely an arbitration agreement. Nonetheless, both arbitral tribunals and national courts assume the same type of adjudicatory power, namely the power to determine the pending dispute, and the power to issue an award or a judgment with the force of *res judicata*.

Despite the fact that it stems from an *arbitration agreement* rather than from *national rules*, jurisdiction of an arbitral tribunal is by no means inferior to that of a national court. This becomes clear from the following:

- First, jurisdiction of national courts may also stem from an agreement, namely a jurisdiction agreement or choice of court agreement. The rules for extra-territorial jurisdiction apply, even when the national courts have initially assumed jurisdiction on the basis of a jurisdictional agreement.³⁵
- Second, jurisdiction derived from procedural agreements (either jurisdiction or arbitration ones) is ultimately based on national or international procedural rules. This is exactly the case with jurisdiction assumed on a territorial basis. Thus, procedural rules are the original source of jurisdiction in all cases, be that jurisdiction based on territorial or jurisdiction based on contractual basis.³⁶

Therefore, despite the fact that they are established in different ways, jurisdiction of an arbitral tribunal is of the same quality as that of a national court. There is no difference between jurisdiction established on a territorial basis and jurisdiction established on the basis of an arbitration agreement. Once their power to examine the case is confirmed by reference either to a valid arbitration agreement or to the applicable procedural rules, arbitral tribunals and national courts assume the same

³⁴ *Ibid.*, at 45.

³⁵ This was the case in *Sinochem International Oil (London) Co Ltd v Mobil Sales and Supply Corp.* [2000] 1 Lloyd's Rep. 670 where English courts assumed jurisdiction over overseas parties on the basis of a jurisdiction agreement.

³⁶ With regard to arbitration agreements see for example: New York art. II(3), EAA 1996 s.9(1), French CNPC art. 1458, German Code of Civil Proceedings s.1032, Swiss PILA art.7. With regard to jurisdiction agreement see for example Council Regulation 44/2001 on “Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters” art. 23. In Germany, see ZPO ss.38-40 or England Civil Jurisdiction and Judgments Act 1982 Part II section 6 art.17.

kind of jurisdiction: jurisdiction to determine the dispute at hand in the most effective way.

Therefore, since national courts are allowed to assume jurisdiction beyond their territorial boundaries, arbitral tribunals should also be allowed to assume jurisdiction beyond the boundaries of the arbitration agreement as an ordinary contract (extra-contractual jurisdiction), whenever this is necessary for them to resolve the dispute effectively. More generally, it can be argued that when it is necessary for the determination of the dispute an adjudicatory forum, be that a national court or an arbitral tribunal, may extend its jurisdiction beyond its original boundaries, be that geographical territory or an arbitration contract

This is not to argue that extra-contractual jurisdiction should be the norm. It must be emphasised that jurisdiction beyond the territorial or contractual boundaries should be allowed only as a rare exception and under strict conditions.³⁷ Extra-territorial or extra-contractual jurisdiction should only be allowed in case the extra-territorial or extra-contractual parties and the original parties constitute a necessary procedural unit. As already indicated, this requirement applies usually in case all the several claimants or several defendants are inextricably tied up with the dispute. Co-liability or community of rights and obligations will be the threshold. Mere avoidance of multiplicity of the litigation of the dispute should not be accepted as a valid basis for the courts and tribunals to assume extra-territorial or extra-contractual jurisdiction.

However, once the above condition is satisfied, extra territorial or extra-contractual jurisdiction as a matter of principle should be equally accepted for both national courts and arbitral tribunals.

³⁷ Cf Cheshire and North's, *Private International Law*, by PM North and JJ Fawcett (13th ed Butterworths 1999) p. 301, who note with regard to extraterritorial jurisdiction: "There has, for many years, been a particular reluctance to exercise the discretion to allow service out of the jurisdiction under this head [ie when the party out of the jurisdiction is a necessary or proper party]".

Chapter 8: The underlying principles and rationale of third-party mechanisms ...	139
8.1 The importance of third-party mechanisms in international arbitration	140
8.1.1 Third-party mechanisms and functional equilibrium between substance and procedure in multiparty relationships.....	140
8.1.2 Efficiency in arbitration: regulating overlapping parallel proceedings	142
8.1.3 Third-party mechanisms and the interests of the several parties to arbitration	144
8.2 Comparative analysis of third-party mechanisms in the context of national and international litigation: underpinning rationale and general principles	148
8.2.1 Overview and different groups of third-party mechanisms	148
8.2.2 Policy analysis of the third-party mechanisms: distinctions and underpinning rationale	153
8.3 Conclusions of Chapter 8	164

CHAPTER 8: THE UNDERLYING PRINCIPLES AND RATIONALE OF THIRD-PARTY MECHANISMS

The previous chapter demonstrated that as a matter of principle an arbitral tribunal *can* assume extra-contractual jurisdiction and apply third-party mechanisms as a corollary of the concept of effective arbitral jurisdiction and the jurisdictional approach in general. This chapter addresses some equally important issues: first, it examines whether the tribunal *should* assume extra-contractual jurisdiction and apply third-party mechanisms. Here, the thesis embarks on a policy-oriented analysis, which will show that third-party mechanisms are necessary in the context of international arbitration (section 8.1)

Secondly, it explores *the rationale behind third-party mechanisms in general*: what purposes they serve and how do they operate (section 8.2). The exploration of these questions takes place against a comparative background of several national litigation and regional procedural systems. It is suggested that the key-element for the operation of third-party mechanisms is the pending dispute and the implications this dispute has for the third parties in terms of substantive liability and interests.

Such kind of analysis puts the discussion on arbitration and third parties in a wider comparative context. More importantly though, the findings on the underpinning rationale of third-party mechanisms will be used in Chapters 9 and 10 as policy guidelines in order for the thesis to determine the general conditions required for a tribunal to assume extra-contractual jurisdiction and apply third-party mechanisms.

8.1 THE IMPORTANCE OF THIRD-PARTY MECHANISMS IN INTERNATIONAL ARBITRATION

The question that invariably arises in the context of the discussion on arbitration and third parties is why there should be any provision for third parties at all. The prevailing contractual approach argues that, since it is a private dispute resolution mechanism, arbitration should be available only to those parties that have agreed thereto. There should not exist mechanisms for the participation of third parties even when the latter have a financial or legal interest in the dispute between the genuine parties to the arbitration agreement and proceedings.

However, in policy terms third-party mechanisms are necessary in the context of international arbitration. Although it is a private dispute resolute system, arbitration should not remain a closed system, exclusively reserved for those parties that are contractually bound by an arbitration agreement. Instead, arbitration should be a dispute resolution system, which -under particular circumstances- has to be flexible and able to communicate with third parties that have legal and financial interests in the dispute before the tribunal. A procedural mechanism of communication between the genuine and third parties should be established in arbitration. General legal principles, as well as practical considerations, militate for the application of third party mechanisms in international arbitration.

8.1.1 Third-party mechanisms and functional equilibrium between substance and procedure in multiparty relationships

The principle of “contractual freedom” permits commercial parties to structure their contractual relationships in the way that best accommodates their commercial interests. In cases where several parties are involved in the same commercial project, these parties have the right to enter into several bilateral contracts between them rather than enter into a single multiparty agreement. These contracts, although bilateral, are in most cases inextricably intertwined in terms of substance. The performance or non-performance of one of these contracts will necessarily affect the others.

As was illustrated in Chapter one, the contract between an owner and a contractor, has in many cases express references to the duties or rights of a sub-contractor. Likewise, in several instances a contract between a creditor and a debtor expressly provides for a guarantee. In an opposing manner, a subcontract is concluded in view

of a work whose specifications are set out in the main contract; or a guarantee agreement will secure the specific debt or performance undertaken in the main contract. Thus, should a dispute arise between two of the several intertwined parties the others would not be strangers in this dispute. This strong contractual interrelation amongst the several parties cannot be ignored at the dispute resolution proceedings.

It is for this reason that national litigation systems provide for extensive third-party mechanisms. In this way, the related third parties may be brought in the proceedings between two other parties, as they are relevant to the dispute between the original parties, and therefore their involvement in the dispute resolution process is considered necessary or at least desirable. Thus, the contractual interrelation between the several parties at a substantive level is reflected at a procedural level. Generally, it can be argued that *the procedural status of the parties reflects their substantive status so that a functional equilibrium between substance and procedure is established*. As the next section will show, this is an overarching principle common to all procedural systems.

Arbitration, like litigation, constitutes a dispute resolution system. It is true that unlike litigation, arbitration borders on contractual law due to its contractual origins. However, once the jurisdiction of an arbitral tribunal is established contractually, arbitration assumes a jurisdictional, that is procedural, role. As the previous chapter demonstrated, the jurisdictional aspect of arbitration has a predominant role, particularly after the dispute arises. Accordingly, this functional equilibrium between substance and procedure should, as a matter of general principle, apply to arbitration too. Parties that are not bound by an arbitration agreement, but that are nevertheless strongly associated with the parties to that arbitration agreement are not strangers and should not be altogether excluded from the arbitration process. Such a pure contractual approach would create an *artificial discrepancy* between *the substantive and procedural side* of intertwined multiparty relationships. The substantive interrelation between the several parties should be *proportionally reflected* on the arbitration process. The arbitration should, to some extent, be able to interact with third parties that are an integral part of the pending dispute.

It is accepted that the principle of procedural party autonomy in arbitration gives the parties the freedom to choose the party with whom they want to arbitrate. However, it should be under question whether and to what extent procedural party autonomy can altogether overturn the contractual background of the intertwined relationships, set out by the parties themselves by virtue of another equally important

principle, namely the principle of contractual freedom. The latter gives commercial parties the freedom to enter into several bilateral but at the same time interrelated contracts in relation to a single commercial project. This interrelation at a substantive level should be reflected at a procedural level. In other words, the principle of procedural autonomy in arbitration should operate in line with the principle of contractual freedom. The freedom of the parties to choose their party in arbitration should be preserved, while at the same time, it should operate within the intertwining contractual context. In this way *the important functional equilibrium between substance and procedure will be preserved*.

8.1.2 Efficiency in arbitration: regulating overlapping parallel proceedings

Third-party mechanisms prevent the commencement of several bilateral proceedings with overlapping subject matters between multiple parties. Parallel overlapping proceedings create the risk that the determinations of an arbitral award between the two genuine parties to an arbitration agreement might be irreconcilable, not to say conflicting,¹ with those of a subsequent award or judgment between the third party and one of the genuine parties.²

Whenever several parties are contractually intertwined in a multi-party commercial project, it is very likely that the same issues will come up before the several proceedings.³ As was explained in Part One, in the context of string construction

¹ The term irreconcilable is preferred to the term conflicting which is more often used in this context, because, technically speaking, the terms are slightly different: the former is stricter, referring to decisions with *mutually exclusive legal consequences* between the same two parties, whereas the latter is wider referring to merely contradictory decisions in the case of multiparty relationships; however, both “conflicting” and “irreconcilable” decisions result in problematic, and thus unacceptable situations; in the context of the Brussels Convention and the art.22 (now Reg.44/2001 art.28), the test of irreconcilability for Advocate General Tesauro, accepted by the ECJ, in the *Tatry* case (*The Owners of the Cargo Lately Laden on Board the ship ‘Tatry’ v The Owners of the ship ‘Maciej Rataj’*, C-406/92 [1994] ECR I-5439) was *essentially common issues of fact and law risking conflict of decisions or reasoning*: “The rationale of art 22 is to encourage harmonious judgments and to avoid conflicts at the recognition stage even only as to the reasoning of different judgments (para.28)”; cf the European Regulation 44/2001 art.34.4 which precludes the recognition of “irreconcilable” rather than merely “conflicting” judgments, although this term was given a narrow meaning in *Hoffmann v Krieg*, Case 145/86.

² Cf *McAlpine Construction v Unex*, [1994] 38 Con LR 63 (CA) “It is clear that to a considerable extent the issues in the arbitration and in the action, if it is fought, will overlap. Clearly this is undesirable, and there is a strong case for preventing duplication of proceedings. The parties have chosen arbitration to decide the issues which do overlap, and there is thus a presumption that the same issues should not be decided in an action also, with the possible risk that the judge in the action will arrive at a different decision from the arbitrator on some of those issues.” (Glidewell LJ, at 77).

³ Consolidation of arbitration proceedings was appropriate where both disputes centered on same construction project, principal issue in both proceedings was a question of who was responsible for

contracts the issue of causation or liability will probably arise both in the proceedings between an owner and a contractor, and in the proceedings between the contractor and a subcontractor. Similarly, defects or delay in the work of a subcontractor will affect the liability of the contractor vis-à-vis the employer, and the amount of damages owed by him against the employer.⁴ The same applies to web-type construction contracts or secured transactions.

It is, fortunately, the case that inconsistent awards are rare.⁵ However, when they do occur, not only do they raise doubts about the reliability of international arbitration but they also defeat the expectations of the parties. An arbitral award as a national judgment is presumed to be an authoritative determination of the pending dispute. The authority of a judgment or an award is established by the doctrine of *res judicata* applicable both to judgments and awards. This does not mean that national judgments or arbitral awards cannot be wrong. They are indeed fallible.⁶ It is precisely because national legal systems accept the inherent fallibility of a decision, be that a judgment or an award, that they safeguard this decision with the authority of *res judicata*. *Res judicata* renders an award or a judgment final, albeit fallible. In other words, a decision, which is merely fallible, i.e. only *possibly wrong*, is tolerated by legal systems, as long as this decision *is never exposed as clearly wrong*. However, the issuance of two irreconcilable decisions with inconsistent determinations on the same factual or legal issues *renders fallible decisions into clearly wrong decisions*. Whenever two conflicting decisions are rendered, one of them must clearly be wrong. Therefore, irreconcilable decisions negate the purpose of *res judicata* and expose the whole legal system as defective. In fact, irreconcilable decisions constitute a legal sore.⁷

extra costs incurred in completion of the project, and resolution of disputes in separate proceedings could lead to inconsistent findings; see *Cable Belt Conveyors, Inc. v Alumina Partners of Jamaica*, S.D.N.Y.1987, 669 F.Supp. 577, affirmed 857 F.2d 1461.

⁴ See Chapter 2.3.

⁵ For a recent example of irreconcilable awards see UNCITRAL Arbitration Tribunal, final award, September 3, 2001, *R.S.Lauder v Czech Republic*, (2002) 14 World Trade and Arbitration Material 35 (Final Award); UNCITRAL Arbitral Tribunal, partial award, September 13, 2001, *CME Czech Republic v The Czech Republic*, (2002) 14 World Trade and Arbitration Materials 109; and Svea Court of Appeals (Sweden), May 15, 2003, *CME Czech Republic v The Czech Republic*, (2003) 15 World Trade and Arbitration Materials 171.

⁶ Decisions “. . . are not final because [they] are infallible but [they] are infallible only because [they] are final.” *Brown v Allen*, 344 U.S. 443, 540 (1953) (Jackson, J. concurring).

⁷ Cf *Abu Dhabi Gas Liquefaction [ADGAS] v Eastern Bechtel*, [1982] 2 Lloyd's Rep. 425, 427 “As we have often pointed out, there is a danger in having two separate arbitrations in a case like this. You might get inconsistent findings if there were two separate arbitrators. This has been said in many cases [...] it is most undesirable that there should be inconsistent findings by two separate arbitrators

Moreover, irreconcilable awards frustrate the expectations that commercial parties have from international arbitration. Parties trust international arbitration as a worldwide authoritative mechanism and they resort to it in order to obtain a final and binding determination of their disputes. In a case where this dispute happens to involve other parties as well, the parties to an arbitration agreement want the award to have the authority to determine dispute once and for all. It is reasonable to assume that the parties would not want the award to leave room for third parties to challenge before a different forum the determinations of the arbitral award. The parties would want an arbitral award with as much clout as possible. Their expectations would be defeated and the enforceability of their award would become doubtful if this award was in conflict with another award or judgment. When parties opt for bilateral arbitration against a background of multiparty contractual relationships, they do not necessarily waive their expectations for an award that will not be conflicting with another award or judgment. For the above reasons, it is concluded that irreconcilable awards and decisions challenge the authority of international arbitration, undermine its effectiveness and should clearly be prevented.

8.1.3 Third-party mechanisms and the interests of the several parties to arbitration

Third-party mechanisms should be also examined in view of the various parties involved in typical multiparty relationships.

It is true that some of the parties to the arbitration proceedings would have less interest in involving a third party in the bilateral arbitration. This is particularly the case for an owner, in the context of vertical construction contracts, or an architect, in the context of horizontal construction contracts. Their interests would be better served if the dispute against a contractor, in the former case, or an owner in the latter were resolved as quickly as possible. The involvement of a third party, be that a subcontractor or a contractor, in the pending dispute would complicate the proceedings and increase the money and the time needed for the dispute to be finally determined.

However, there are other parties that would benefit from third-party mechanisms in arbitration. Thus, in the context of several string contracts, third-party mechanisms

on virtually the self-same question, such as causation. It is very desirable that everything should be done to avoid such a circumstance" (Lord Denning).

would benefit the contractor, who stands as the middle party between the two successive contracts. For example, in arbitral proceedings between an owner and a contractor, the latter will want the subcontractor to be bound by the determinations of the arbitral award, particularly in the case the tribunal finds that the delivered work is defective and the contractor is liable against the owner. Otherwise, the contractor would face the risk that a second tribunal or a court, in subsequent proceedings between the contractor and the subcontractor, might find the same work not defective, in which case the contractor would be held responsible for work actually done by the subcontractor.

Likewise, in the context of web-type construction contracts an owner would want the contractor to be bound by the determinations of the arbitral award issued in proceedings between the architect and the owner.⁸ This would particularly be the case, if the tribunal found the work defective but the architect not liable. Otherwise, the owner would run the risk that the second court or tribunal, in proceedings between the owner and the contractor, would find the work not defective or, in any event, the contractor not liable, in which case the owner would have no one to recover the damage from the defective work.

The same applies to secured transactions. In a case of a guarantee, for example, a debtor would have an interest in the guarantor being bound by the determinations of an award in arbitral proceedings between the creditor and the debtor. Otherwise, the creditor might obtain a judgment or an award in its favour in second proceedings against the guarantor, which would give the latter a claim to recourse against the debtor. In this way, the debtor would face the possibility of paying the guarantor for a debt for which he has already been found not liable.

Third-party mechanisms would also serve the interests of some types of third parties. As will be explained in Chapter 12, an arbitral award may have collateral effects on third parties. In such a case, a third party would have a strong interest to intervene into the pending arbitral proceedings in order to prevent any adversary effect against its legal position.⁹ Depending on the specific factual circumstances a guarantor or a subcontractor, for example, might have an interest to intervene in the

⁸ Cf T. Stipanowich, "Arbitration and the Multiparty Dispute: The Search for Workable Solutions", (1987) 72 *Iowa L. Rev.* p.478.

⁹ Compare the very interesting analysis of the third parties' interests in Alexis Mourre, "L'Intervention des Tiers à l'Arbitrage", Recueil Vol.I (2000-2002) *Les Cahiers de l'Arbitrage*, p. 100 arguing for the analogous application of national intervention mechanisms in arbitration.

pending proceedings between the debtor and the creditor, and the owner and the contractor respectively, if they believe that their legal position will be affected by the determination of the issues pending before the tribunal.

Of course, the main question here is whether the interests of third parties should bear any relevance in the context of arbitration. While the interests of third parties are generally taken into account in the context of litigation, where third parties are granted extensive rights to intervene in pending proceedings,¹⁰ it is arguable whether the same should apply to arbitration. Third parties have taken a considered decision not to conclude an arbitration agreement, and, therefore it could be argued that they have excluded themselves from the arbitration process altogether.

There is a view arguing that the interests of third parties should be taken into account in arbitration, and that participatory rights should be accorded to third parties on the basis of equity and due process or public policy considerations.¹¹ Equity

¹⁰ See in detail Section 8.2 below.

¹¹ See S. Strong, "Intervention And Joinder As Of Right In International Arbitration: An infringement Of Individual Contract Rights Or A Proper Equitable Measure?" (1998) 31 *Vand.J.Transnat'l L.*, p. 915 arguing, at 981, that the third parties' interests should be taken into account on the basis of the principle of 'equality of the parties', which should "be read to include all parties to the contract, not just those who are participating in the arbitration." This interpretation of the term equality of the parties would include parties that have signed the substantive contract but are not involved in the arbitration. Could this broad interpretation be taken a step further and be read to refer to "equality of the parties to the dispute", which would include parties that have not signed the main contract but are still involved in the dispute? See also T. Stipanowich, "Arbitration and the Multiparty Dispute: The Search for Workable Solutions", (1987) 72 *Iowa L. Rev.*, p 473, also arguing for the application of participatory mechanism in arbitration; cf the very interesting analysis of the third parties' interests in A. Mourre, "L'intervention des Tiers à l'Arbitrage", (2000-2002) *Les cahiers de l'arbitrage*, Recueil, Vol. I, p. 100 arguing for the analogous application of national intervention mechanisms in arbitration.

There is also case-law that has by analogy applied national participatory provisions to arbitration. See for example, *Association of Contracting Plumbers v United Ass. of Journeymen*, 841 F.2d 461, 466 (2nd Cir. 1988); *Woolworth v Miscellaneous Warehousemen's Union*, 629 F.2d 1204, 1213 (7th Cir. 1980); *Holborn Oil Trading v Interpetrol Bermuda*, 658 F. Supp. 1205, 1206-09 (S.D.N.Y. 1987), applied US Fed.Proc.R.24 intervention as of right; *Litton Bionetics v Glen*, 292 Md.34, 437 A.2d 208 (1981); *Plaza Development Services v Joe Harden Builder*, 294 S.C.430, 365 S.E.2d 231 (1988).

Specific mention should be made of the particularly well-know *Compania Espanola de Petroleos v Nereus Shipping*, 527 F.2d, 966 (2nd Cir.1975), ordering the consolidation of arbitration proceedings between a ship-owner and its charterer, on one hand and the ship-owner and the guarantor of the charterer on the other hand. In this case, the 2nd Circuit applied US Fed.R.Civ.P. s.42(a) to arbitration proceedings by virtue of s.81(a)(3), which provides that "in proceedings under title 9.USC relating to arbitration [...] these rules apply only to the extent that matters of procedure are not provided for in those statutes". *Nereus* case triggered an extensive debate on the issue of compulsory consolidation in arbitration: see for example Dore, *Theory and Practice of Multiparty Commercial Arbitration*, (Graham & Trotman/Marinus Nijhoff London/Dordrecht/Boston 1990); T. Stipanowich, "Arbitration and the Multiparty Dispute: The Search for Workable Solutions", (1987) 72 *Iowa L. Rev.* p.478; J.Lew, L.Mistelis and S.Kroell, *Comparative International Commercial Arbitration*, (Kluwer Law International 2003) at para 16.77. *Nereus* was recognized as authority in *Marine Trading Ltd. v Ore International Corp.*, 432 F. Supp. 683 (SDNY 1977); *Sociedad Anonima de Navegacion Petrolera v Cia de Petroleos de Chile*, 634 F.Supp.805 (SDNY 1986); *Cable Belt*

principles are not easy to define, due to their abstract nature. Thus, it is not clear whether and to what extent they should bear any relevance in the context of international arbitration.¹² Due process and public policy are, indeed, accepted as legitimate limitations of party autonomy in international arbitration.¹³ However, both due process and public policy have an exceptional character, and as result a limited application. It is therefore difficult to accept that these principles will be violated if third parties are not given participatory rights, unless the interests of the third parties in the pending dispute are particularly strong.

It becomes clear that what should constitute the yardstick for the tribunal to determine whether third-mechanisms should apply to arbitration or not is the interests of all the parties involved in the dispute, rather than general principles of equity or public policy.

As will be explained in the next section, this will largely depend on the specific factual circumstances and, in particular, on the degree of association between third and genuine parties in terms of contractual rights and liability. Only when third and genuine parties to an arbitration agreement are strongly associated in substantive terms, might their interrelated interests be served better by multiparty proceedings, and third-party mechanisms.¹⁴

Conveyors v Alumina Partners of Jamaica, 669 F.Supp.577 (SDNY 1987); *North River v Philadelphia Reinsurance*, 856 F.Supp.850 (SDNY 1994) (refused to order consolidation on other grounds) and *Specialty Bakeries v Robhal*, 1997 WL 379184 (ED pa. 1997) (also refused to order consolidation). However, more recent authority suggests that it is at least doubtful whether *Nereus* is still good law. In particular see the following decisions that refused to follow *Nereus*: *Philadelphia Reinsurance v Employers of Wausau*, 61 Fed. Appx. 816 (3rd Cir. 2003); *Cavalier Mfg. v Clarke*, 862 So. 2d 634 (Ala. 2003); *Hartford Accident and Indem. v Swiss Reinsurance America*, 87 F. Supp. 2d 300 (S.D. N.Y. 2000); cf *Weyebaeuser v Western Seas Shipping*, 743 F.2d 635 (9th Cir. 1994); *United Kingdom of Great Britain v Boeing*, 998 F.2d 68 (2nd Cir. 1993) and *Ore & Chemical v Stinnes Interoil*, 606 F.Supp.1510 (S.D.N.Y. 1985).

¹² Unless the parties have expressly provided for the arbitrators to act as amiable compositeurs or *ex aequo et bono*.

¹³ See J.Lew, L.Mistelis and S.Kroell, *Comparative International Commercial Arbitration*, (Kluwer Law International 2003), para 21-16 et seq, 26-80 and 26-111 et seq.

¹⁴ "Persons having interest in subject matter of litigation which may conveniently be settled therein are 'proper parties,' whereas those whose presence is essential to determination of entire controversy are 'necessary parties.'" See *Texas & P. Ry. Co. v Brotherhood of R. Trainmen*, W.D.La.1945, 60 F.Supp. 263.

8.2 COMPARATIVE ANALYSIS OF THIRD-PARTY MECHANISMS IN THE CONTEXT OF NATIONAL AND INTERNATIONAL LITIGATION: UNDERPINNING RATIONALE AND GENERAL PRINCIPLES

8.2.1 Overview and different groups of third-party mechanisms

National litigation systems have over the course of many decades, developed procedural mechanisms ensuring that third parties with a legitimate interest in the dispute between two other parties are not excluded from court proceedings dealing with the determination of this dispute. Highly technical, if not complicated, third-party procedural mechanisms provide many ways in which third parties may participate in the proceedings either as co-claimants or co-defendants. Not every third party is accorded the right, or is subject to the duty, to participate to proceedings between the two original parties. Third-party mechanisms are reserved to third parties with an interest, deemed worthy of protection. As the following analysis will show, whether a third party may participate in the proceedings, and also the nature of its participation is directly relevant to the *degree of association between a third party and one of the original parties, in terms of substantive liability and interests*. Here, the general rule is: *the closer the substantive association between an original and a third party, the more effective are the third-party mechanisms provided by the litigation systems*.¹⁵ More specifically, third-party mechanisms become relevant at three different stages:

- At the beginning of proceedings
- During the proceedings
- After the judgment is issued

1. At the beginning of proceedings. At this stage, third parties may come into play on the basis of provisions, allowing for

- Common jurisdictional bases; or
- Joinder¹⁶ of the several parties from the outset of the proceedings.¹⁷

¹⁵ In terms of methodology it should be noted that the national procedural systems examined in the next sections come from different legal traditions. Finding general principles common to all these systems necessarily requires a degree of generalisation. Thus, the analysis emphasises the general features rather than the technical procedural details of the different national systems. Otherwise, the goal of revealing the rationale behind the third party mechanism and applying it in the context of arbitration would be clearly defeated.

¹⁶ The term joinder, except in England, is used to refer to cases where parties can bring several and thus third parties before the same forum, from the outset of the proceedings. In this regard joinder proceedings differ from intervention or interpleading or consolidation, proceedings which are used

Examples of common jurisdictional bases can be found in the French New Code of Civil Procedure art.42(2), providing that when several defendants domicile in different places, the claimant may sue all the several defendants before the court of the place where one of them domiciles.¹⁸ Similar provisions can be found in the US,¹⁹ the Code of Civil Procedure of Germany (s.36(1)(3)),²⁰ the Code of Civil Procedure of Greece (art.31(1))²¹ and the Council Regulation (EC) No.44/2001, on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters for the 44/2001, art.6.²² Thus, when several persons who are relevant for the resolution of the dispute are subject to the jurisdiction of different courts, national procedural laws provide that all of them can be brought before the jurisdiction of a single court (common jurisdictional basis). That court will usually be either the court of the place where one of the several parties resides or domiciles, or the court of the place where an event relevant to the dispute happened (for example, the court of the

to bring third parties before the same forum only during the proceedings. In England, however, joinder has a wider meaning encompassing all cases where a third party and original parties are brought before the same court: this either happens at the beginning of the proceedings or at a later stage. Thus, in England there is no technical distinction between joinder and intervention or interpleading.

¹⁷ These third-party participatory mechanisms should be distinguished from collective actions provided, mainly, in common law systems: class actions in the US (Fed.Rul.23), Group Litigation in England (CPR 19.10 *et seq*) and the representative actions under the old rule in the Chancery Division (see *Duke of Bedford v Ellis*, [1901] A.C.1). In civil law systems, there have been some attempts to enact class-action legislation, but in most cases there have been either withdrawn (France) or still pending (Italy). Collective actions, as opposed to third party mechanisms discussed in the thesis, will usually apply in the context of accidents where numerous parties are involved. It is, thus, not the quality/type of the relationship between the several parties that requires the application of representative actions, although a degree of common interest among the several parties must exist. Rather it is the fact that “the parties [are] so numerous that you never could ‘come at justice’ ... if everybody interested was made a party”, *Duke of Bedford*, at 8; *cf* US Red Rul. 23(a)1: “the class is so numerous that joinder of all members is impracticable”. There are, thus, different sorts of considerations underpinning collective actions, which the thesis will not examine.

¹⁸ New Code Civil Procedure (NCPC) Art. 42 (2). This would be applicable, for example, in a case of more co-creditors, see Civ 2nd, 27 Feb.1985, Gaz. Pal. 1985.2. Somm.262.

¹⁹ Federal courts assume jurisdiction over several parties from different states See Title 28 U.S.C. § 1367(a) (Supplemental jurisdiction); see further on US federal jurisdiction in D. Siegel, “Changes In Federal Jurisdiction And Practice Under The New (Dec. 1, 1990) Judicial Improvements Act”, 133 F.R.D. 61, Wright & Miller, 647 Fed. Prac. & Proc. Civ.3d § 1659. On the other hand long arm statutes provide state courts with jurisdiction over several parties from the same state. See, for example, Pennsylvania long-arm statute, 42 Pa CS § 5322(b), or South Dakota SDCL § 15-7-2.

²⁰ Code of Civil Procedure (ZPO) s.36(1)(3). establishes jurisdiction of special venue for several co-defendants.

²¹ Code of Civil Procedure, art 31(1) provides common jurisdiction for one court to hear all cases with regard to several relevant claims of several parties. This expressly includes the claims against the guarantor and the debtor. and the claims of the parties that have a right to intervene

²² Art.6 establishes common jurisdiction the court of one Member State for several defendants in claims “closely connected” (6(2)) and for the case of a third party warrantor or guarantor (6(3)).

place of the accident, in case of a tort claim; or the place of the court where the contract was concluded, in case of a contractual claim).

Examples of joinder from the outset of the proceedings can be found in the US Federal Rules of Civil Procedure r.19, providing that a person will be joined in a claim brought by another party if:

- A. “In that person’s absence, the court cannot accord complete relief among existing parties; or
- B. That person claims an interest relating to the subject of the action and is so situated that disposing of the action in the person’s absence may: (i) as a practical matter impair or impede the person’s ability to protect the interest; or (ii) leave an existing party subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations because of the interest”

Also, US Fed. Rules r. 20 provides that several persons may be joined as co-claimants where

- A. “They assert any right to relief jointly, severally, or in the alternative with respect to or arising out of the same transaction, occurrence, or series of transactions or occurrences; and
- B. Any question of law or fact common to all plaintiffs will arise in the action”

Similarly, English Civil Procedural Rules (CPR) r.6.20(3)b provides that a person domiciled outside the English jurisdiction may be joined as a co-defendant with a person domiciled in England, if the former is “a necessary or proper party to the claim”.²³ Analogous provisions for joinder can be found in Germany²⁴, Greece²⁵ and the UNIDROIT Principles of Transnational Civil Procedure.²⁶

2. During the proceedings. Here, two types of mechanisms regulate the role of third parties in relation to pending proceedings:

First, third-party mechanisms bringing third-parties in before the court examining the dispute between the original parties: these are mechanisms by which, after the proceedings between the original parties have commenced, third parties may be

²³ The provision will, usually, apply when the several defendants are liable jointly, or jointly and severally, or in the alternative, Morris, *The Conflict of Laws*, D. McClean-K. Beevers (eds), (6th ed.) (2005) (London Sweet & Maxwell) at 5-017.

²⁴ German Code of Civil Procedure. s.59-61.

²⁵ Greek Code of Civil Procedure art.37(1) and arts.74-76.

²⁶ Rule 12.1:” A party may assert any claim substantially connected to the subject matter of the proceedings against another party or against a third person who is subject of the jurisdiction of the court”.

brought in before the court hearing the case between the original parties. This can be achieved in different ways.

To begin with, third parties may *intervene* in the pending proceedings on their own initiative. For example, the US Fed Rules Civ. Proc. R. 24(a) provides that the

“court must permit anyone to intervene who: (1) is given an unconditional right to intervene by a federal statute; or (2) claims an interest relating to the property or transaction that is the subject of the action, and is so situated that disposing of the action may as a practical matter impair or impede the movant’s ability to protect its interest, unless existing parties adequately represent that interest.”

Similar provisions may be found in England,²⁷ France,²⁸ Germany,²⁹ Greece,³⁰ and the UNIDROIT Principles of Trans-national Civil Procedure.³¹

Moreover, it is the original parties that may bring third parties in the proceedings (interpleader). Thus, the claimant may request a third part to join the proceedings, as provided for example in the US Rules of Civ. Proc. R. 22(1):

“Persons with claims that may expose a plaintiff to double or multiple liability may be joined as defendants and required to interplead”.

Equally, the defendant may take the initiative and request a third party to take part in the pending proceedings between the original parties, as provided for example in the US Rules of Civ. Proc R.22(2):

“A defendant exposed to similar liability may seek interpleader through a crossclaim or counterclaim.”

Similar provisions are included in the Codes of Civil Procedure in Germany,³² France,³³ Greece³⁴, and the UNIDROIT Principles of Trans-national Civil Procedure.³⁵

²⁷ England CPR r.19(2)-19(3).

²⁸ France, Civil Code of Procedure (CCP) art. 325 et seq.

²⁹ Germany, Civil Code of Procedure (CCP) s. 66.

³⁰ Greece, Civil Code of Procedure (CCP) art.80 et seq.

³¹ R.12.2 first line: “ A person having an interest substantially connected with the subject matter of the proceedings may apply to intervene”.

³² German CCP s.72.

³³ French CCP art.331 (mis en cause or intervention forcée).

³⁴ Greek CCP art.86-88.

Finally, when proceedings between a third party and one of the original parties commence in parallel to the proceedings between the original parties, the two or several parallel proceedings may be *consolidated* so that all the relevant parties are brought before the same court.³⁶ National provisions for consolidation include the US FRCP r.42(a), the German ZPO art.147, the French NCCP art.367, the Greek CCP art.246 and UNIDROIT r.12.5.

Secondly, third-party mechanisms that avert the commencement of parallel proceedings between the several parties: third-party mechanisms of this type are used to avert the commencement or the continuation of two parallel proceedings on the same or related subject matter. Here for example the rule established by *lis alibi pendens* is that when proceedings have been initiated on a particular subject matter, a second set of proceedings on the same or related matter should be stayed, at least until the first decision is rendered.³⁷ *Lis pendens* is normally applicable when the parties in the two parallel trials are the same, as for example in the case in the EC Reg. 44/2201 art.27. However, there are cases where *lis pendens* applies even when the several parties in the two parallel proceedings are not different, in other words where third parties are involved.³⁸ This is for example the case in the EC Reg. 44/2001 art.28, providing that “where related actions are pending in the courts of different Member States any court other than the court first seised may stay its proceeding.” Here, even different parties in the second set of proceedings will be subject to the *litispendens* effect of the first set. Therefore, *lis pendens* prevents third parties from commencing proceedings regarding an already pending subject matter and, thus it eliminates the risk of conflicting decisions.

³⁵ R.12.2 second line “The court itself or on motion of a party, may require notice to the person having such an interest, inviting intervention”.

³⁶ It should be noted that consolidation is not an exclusive third-party mechanism. It may be used to consolidate two parallel related actions that may involve either several different parties or the same two parties; *cf Attala Hydratane Gas v Lowry Tims.*, N.D.Miss.1966, 41 F.R.D. 164: “Consolidation of actions is not limited to actions involving identical parties, but is available to different parties in actions having common questions of fact and law”. To the extent that it is used to bring original and third parties together, consolidation is considered to be an important third party mechanism, for the purposes of the thesis.

³⁷ In the US and England *lis pendens* is provided as a common law rule see *McHenry v Lewis* (1882) 22 Ch.D.397; whereas in international litigation *lis pendens* is examined in the general context of *forum non convenience*, see Morris *supra* n.23, para 5-047, Halsbury’s, *Laws of England*, 4th ed. (Lexis Nexis 2003), para. 355.

For civil law jurisdictions see France CCP art.100 et seq, German CCP s.261(3), Greek CCP art.222.

³⁸ The extent to which a third party may be affected by *lis pendens* or other similar national mechanisms is addressed in detail in Chapter 12.

3. At a stage after the decision is rendered. A national judgment that is final obtains an authoritative status, which prevents the re-litigation of the same subject matter of the dispute (the *res judicata* effect).³⁹ As in the case of *lis pendens*, the rule here is that a judgment binds only parties that have taken part in the proceedings. However, there are exceptions to this rule, so that third parties may be affected by a judgment rendered between the original parties. In other words, a decision may, under specific circumstances, produce a *third-party effect*. Both the third-party effect of a national judgment, and most importantly, that of an *arbitral award* are examined in detail in Chapter 12 of the thesis. At this point it suffices to mention that a third-party effect of a national judgment, to some extent, may *prevent* a third party from re-litigating issues that have been determined in previous proceedings between the original parties. Thus, the third-party effect of a decision operates as a third-party mechanism regulating overlapping proceedings between several parties, and reducing thus, the risk of conflicting decisions or conflicting determinations on the same issues.

8.2.2 Policy analysis of the third-party mechanisms: distinctions and underpinning rationale

In policy terms, third-party mechanisms provided by national litigation systems have been designed to accommodate the interests of administration of justice in general, but also the interests of both the third and original parties in litigation proceedings. Their objectives are:⁴⁰

- First, to achieve consistency in the determination of several related disputes and

³⁹ P. Barnett, *Res Judicata, Estoppel and Foreign Judgments*, (OUP 2001) para.1.12: “The doctrine encapsulates the principle inherent in all judicial systems which provides that an earlier adjudication is conclusive in a second suit involving the same subject matter and the same legal bases”. See *ibid* for the legislative history of the principle that goes back to the Ancient Greek and Roman times. It was even recognized in the Hindu text of Katyayana.

⁴⁰ See, for example, *Linder Steel Erection, v Wedemeyer*, D.C.Md.1984, 585 F.Supp. 1530: Bifurcation of trials is intended to further convenience, avoid delay and prejudice, and to serve ends of justice; it is appropriate only when the court believes that separation will achieve one of these purposes; *Barcelo v Brown*, D.C.Puerto Rico 1978, 78 F.R.D. 531:

“to accomplish greater convenience and economy in the administration of justice and to avoid overlapping duplication in motion practice, pre-trial and trial procedures occasioned by competing counsel representing different plaintiffs”

See, also *Tetra Moletric Limited v Japan Imports Limited* (CA) pointing at “requirements of justice and of the efficient conduct of the hearing”: In France see an in-depth analysis of all the interests served by the involvement of a third party in pending proceedings between the original parties: P-D Saint-Hilaire, *Le Tiers à l’acte Juridique*, L.G.D.J, 2000.

- Second, to permit disposition of the entire subject matter in an economic and expeditious way.

Thus, third-party mechanisms aim to prevent multiplicity of several related claims before different courts that would not waste procedural resources and also increase the risk of conflicting judgments.

In order to achieve these objectives most efficiently national procedural laws, as was shown above, provide for a variety of third-party mechanisms. This type of third-party mechanism applicable to a particular case depends on dispute pending between the original parties, and the implications that this dispute has for third parties; these implications are in turn directly relevant to the contractual interrelation between third and original parties. As the following analysis demonstrates, the rule here is: *the stronger the association between original and third parties in terms of substantive rights and liability, the more effective third-party mechanisms are provided by national litigation systems.*

This conclusion is in line with the distinction of false third parties into two groups, as suggested in Chapter 2. As will be recalled, the distinction depends on the degree of association between the original and the false third parties, in terms of substantive liability and interests.⁴¹ In particular:

First group: As was explained in Chapter 2, third parties in this group are *strongly associated* with one of the original parties to the proceedings, in terms of contractual interests and liability. Original and false third parties have *concurrent interests* in the pending dispute and the commercial project in general, and are typically *co-liable* or *co-holders of rights and duties* (community of rights and liability).

This strong substantive association between an original and a false third party makes the presence of the latter in the pending proceedings *indispensable* for the disposition of the claims between the *original parties*. The final determination of the pending dispute will not be possible, unless the final decision binds all the several parties, including the false third party involved in the dispute. Justice will be hollow if the third party is left out of this process, and the interests of at least one of the original

⁴¹ As regards terminology, it should be mentioned that the term “false third parties” used in Chapter 2 to describe third parties with an interest in the dispute between two genuine parties to arbitral proceedings, is also used here in the context of litigation to describe third parties with an interest in the dispute between the two parties originally taking part in court proceedings.

parties would be jeopardised.⁴² Therefore, due to their strong association in substantive terms, original and false third parties of this group constitute *an inseparable unit in terms of jurisdiction*.

Take, for example, the case of two co-holders of rights in immovable property. If a dispute arises in connection with rights *in rem* in this property- say for example that another person challenges the ownership of the two co-owners in the property- both co-owners must be present in the proceedings. The dispute can be finally resolved only if all the relevant parties, including of course both co-owners, participate in a single set of proceedings, which would result in a single judgment.⁴³ Here, the final judgment must bind both co-owners, otherwise it would not dispose of the overall ownership dispute.⁴⁴ In case the claimant obtains a judgment in his favour, he would need a judgment enforceable against both co-owners.

Therefore, a third party that is so closely associated, in substantive terms, with a genuine party, must be present in the determination of the dispute. Moreover, it must be present in autonomously. It cannot be represented by the original party to which it is related despite their strong association in terms of interests. This is because the interests of the original and the false third party in the dispute *concur but they do not coincide altogether*. For example, the interests of two partners in the same legal entity or two co-owners in the same property are in principle very similar, but can nevertheless be slightly divergent. This slight asymmetry in their interests means that each co-party must participate in the proceedings in its own right in order to protect its own interests.⁴⁵

⁴² Cf US Fed.R.C.P. 19.(a)(2)(ii) “leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of the claimed interest”.

⁴³ Rule.19: Joinder of Persons Needed for Just Adjudication (a)(1) “in the person's absence complete relief cannot be accorded among those already parties...”; see *Lowe v Loftus* (1970, DC Ga) 314 F Supp 620, for an application of r.19 in the context of a real property dispute.

⁴⁴ See *Amon v Raphael Tuck & Sons*, [1956] 1 QB 357, per J. Devlin J. at 380: “The only reason which makes it necessary to make a person a party to an action is so that he should be bound by the result of the action, and the question to be settled therefore must be a question in the action which cannot be effectually and completely settled unless he is a party”; cf *Fire Auto & Marine v Greene*, [1964] 2 Q.B. 687, where John Stephenson J. took a wider view of a “necessary party”, as a party that is “at least [...] able to show that some legal right enforceable by him against one of the parties to the action or some legal duty enforceable against him by one of the parties to the action will be affected by the result of the action” at 697. For the US see J. Rydstrom, “Who must be joined in action as person ‘needed for just adjudication’ under Rule 19(a), Federal Rules of Civil Procedures”, (1975) 22 A.L.R. Fed 765.

⁴⁵ Cf US Fed.R.C.P. r.24(a)(2) providing for intervention as a matter of right “when the applicant claims an interest relating to the property or transaction which is the subject of the action and the applicant is so situated that the disposition of the action may as a practical matter impair or impede

Thus, it is concluded that the presence of the false third parties of this group is normally considered *indispensable* for two reasons: first, because this type of false third party is strongly interrelated with one of the original parties to the proceedings; second, because despite their strong interrelation, the third party cannot be represented by one of the original parties.

Accordingly, with regard to false third parties of this group, national provisions procedural systems normally provide for *third party mechanisms of mandatory character*.

For example, the US Federal Rules of Civil Proceedings provide for intervention *as a matter of right*;⁴⁶ or they provide for the *mandatory* joinder of persons *needed* for adjudication.⁴⁷ The English Civil Procedure Rules require that where the third party is jointly entitled with one of the original parties, the third party must be joined in the proceedings *as a matter of necessity*.⁴⁸ The French New Code of Civil Procedure provides that a third party will be *forced* to join proceedings in case the decision must commonly bind the third party and the original parties.⁴⁹

Moreover, once it is joined in the pending proceedings, the false third party assumes a procedural position very close to that of the original party, with whom it is closely associated. Thus, the two co-parties in the proceedings constitute a procedural

the applicant's ability to protect that interest..."; the interest of the potential intervenor, although it is less than standing to sue; and r.19(a)(2) providing for joinder of a party needed when it "claims an interest relating to the subject of the action and is so situated that the disposition of the action in the person's absence may as a practical matter impair or impede the person's ability to protect that interest..."; similarly in France 331(1): "Un tiers peut être mis en cause aux fins de condamnation par toute partie qui est en droit d'agir contre lui à titre principal".

See more on this, J. P. Ludington, "When is representation of applicant's interest by existing parties inadequate and applicant bound by judgment so as to be entitled to intervention as of right under Federal Rule 24(a)(2) and similar state statutes or rules" (Originally published in 1962) 84 A.L.R.2d, p. 1412.

⁴⁶ US Fed.R.C.P. r.24(a); see *United States v Georgia*, 19 F.3d 1388, 1393 (11th Cir.1994): "Once a party establishes all the prerequisites to intervention, the *district court has no discretion to deny the motion*".

⁴⁷ US Fed.R.C.P. r.19.

⁴⁸ R.19.3(1): "where a claimant claims a remedy to which some other person is jointly entitled with him, all persons jointly entitled to the remedy *must* be parties unless the court orders otherwise". Cf Halsbury's, *Laws of England*, (Lexis Nexis Butterworths 2007), para 1080: "Since a joint promise creates only one obligation, all the promisors must generally be joined as defendants to the action." [...] "Indeed, the general rule is that *prima facie* a joint promisor has the right to insist upon the other joint promisors being joined as co-defendants; and that he may apply for a stay of proceedings until they are so joined".

⁴⁹ Art.331(2). See also art 332(1): « le juge peut inviter les parties a mettre en cause tous les intéressés dont la présence lui paraît nécessaire a la solution du litige ».

unit.⁵⁰ In fact, the strong procedural ties between these two parties reflect the intensity of their substantive links.

In this way, national procedural rules ensure that a third party that is closely interrelated to the dispute between the original parties, will take part in the proceedings and, more importantly, it will be bound by the final determination. Only in exceptional circumstances will the trial proceed without the participation of a “necessary” false third party.⁵¹

Second group: This group includes persons that are *contractually linked but not strongly associated* with one of the original parties to the proceedings, in terms of contractual interests and liability. Here, original and false third parties will typically have interrelated but not *concurrent interests*. Original and false third parties of this group will not normally share liability. They will either be *liable in the alternative* or *only one of them will be liable* vis-à-vis the other original party.

Therefore, the main dispute between two original parties can be determined in bilateral rather than multiparty proceedings. It is not imperative that a false third party of this group is bound by the final judgment. Indeed, neither the original nor the false third party will be running the risk to suffer an *irreparable harm*, should the false third party be left outside the proceedings between the two original parties. It is not *necessary* for the interests of parties, or indeed the interests of the administration of justice, that all related claims be tried together and all related parties be bound by the final decision.⁵²

⁵⁰ German CCP s. 62: “In the event that a disputed legal relationship can only be determined altogether vis-à-vis all joined or in the event that the joinder of parties is necessary for another reason, then in the event that a hearing or term is attended by some joined parties, the defaulting joined parties shall be deemed to be represented by the non-defaulting joined parties”; similarly, Greek CCP art.76.

⁵¹ See US r. 19(d) providing that when the joinder of a person needed is not feasible the “court shall determine whether in equity and good conscience the action should proceed among the parties before it, or should be dismissed, the absent person being thus regarded as indispensable. The factors to be considered by the court include:

- first, to what extent a judgment rendered in the person's absence might be prejudicial to the person or those already parties;
- second, the extent to which, by protective provisions in the judgment, by the shaping of relief, or other measures, the prejudice can be lessened or avoided;
- third, whether a judgment rendered in the person's absence will be adequate;
- fourth, whether the plaintiff will have an adequate remedy if the action is dismissed for nonjoinder”.

⁵² Cf Halsbury's, Laws of England, (Lexis Nexis Butterworths 2007), para 1081, on Joint promisees:

“Where, by a simple contract or a contract made by deed entered into before 1926, a promise was made to a number of persons jointly, they were entitled collectively to performance of it. Proceedings to enforce the performance of such a promise could be taken only in the names of all the joint promisees; one of them could not sue alone, because the promise was made to all of them jointly, and not to any of them separately; Where a joint promisee refused to be joined

For example, the claim of an owner against a contractor may, normally, be determined without the presence of the subcontractor. A possible judgment against the contractor may be enforced even if the subcontractor is not bound by this judgment. In principle, the dispute between the original parties may be disposed of bilaterally without the participation of the false third party in the proceedings.

However, third-party mechanisms even in this case are highly advisable for policy reasons, since they reduce the risk of irreconcilable decisions, they preserve procedural resources, and of course, they accommodate the interests of the parties. For example, a false third party would have an interest in preventing a judgment against an original party with which it is contractually intertwined. A judgment against a contractor would make the subcontractor's position weaker, in the sense that it would trigger a claim by the contractor against the sub-contractor himself.

Thus, in general, a false third party would have an interest in joining the proceedings supporting the original party with whom they are substantively associated. A decision against the latter would undermine the legal position of the former too, and thus a false third party has an interest to join the proceedings and try to prevent such decision.⁵³ This is an interest complementary to that of original

as a plaintiff in the proceedings, he might, after tender of an indemnity against costs, be made a defendant. The effect was that at common law where a promise was made to two or more persons jointly, it could be enforced by any of the promisees. This is certainly the case with regard to a promisee who has supplied any part of the consideration, and it was probably also the case where he had provided no part of the consideration; but there should be distinguished the situation of joint and several promisees”.

⁵³ Cf art 330 NCCP : « ... si son auteur a intérêt pour la conservation de ses droits, a soutenir cette partie ... » and see TGI Paris, 21 Sept 1983, Gaz. Pal. 1984.51: “the interest of the third party consists in preserving its rights that may be compromised by the judgment, to prevent a contingent damage on his legal position”; ZPO art.66: “a person with an interest in the success of one party in the action pending between other persons may join such party for the purpose of supporting him; Greek CCP art 80 “in case where a third party has legal interest for one of the original parties in pending proceedings to win, the third party has a right [...] to intervene for this original party”. The interest-threshold for permissive intervention is lower than that for compulsory intervention. Thus, permissive intervention does not require a direct pecuniary interest in litigation (*Textile Workers Union of America v Allendale*, C.A.D.C.1955, 226 F.2d 765, 96 U.S.App.D.C. 401). In Greece, the interest required for intervention, in accordance with CCP art.86, is construed liberally: Κεραμεύς-Νίκας-Καλαβρός, ΕρμΚΠολΔ, αρθρ.80 and ΕφΠειρ. 470/1994, ΕλλΔικ 1995.704; however, a mere economic right is not enough: ΑΠ 1184/1984, ΝοΒ 1985, 797: no right for shareholders to intervene in proceedings in which the company takes part. For a compulsory intervention the intervenor must possess “a direct, significant legally protectable” interest, see *Reich v ABC/York-Estes Corp.*, 64 F.3d 316, 321 (7th Cir.1995), regarding the application of US Fed Rul. 24(a); *Security Ins. Co. of Hartford v Schipporeit, Inc.*, 69 F.3d 1377, 1380-81 (7th Cir.1995). But still the intervenor as a matter of right need not have standing to sue one of the original parties: *U. S. v Board of School Com'rs of City of Indianapolis*, Ind., C.A.7 (Ind.) 1972, 466 F.2d 573: requirements for intervention in a pending proceedings should generally be more liberal than those for standing to bring suit. *Day v Sebelius*, D.Kan. 2005, 376 F.Supp.2d 1022: intervenors need not show standing; see also, Carl Tobias, “Standing To Intervene” (1991) *Wis. L. Rev.*, p. 415.

parties, rather than a direct one.⁵⁴ Nevertheless, it is an interest sufficient for a third party to become involved in the proceedings between two original parties in proceedings and, therefore, it is an interest worthy of protection.⁵⁵

Thus, with regard to false third parties of this group, third-party mechanisms are *advisable* but not *necessary*. Accordingly, national procedural laws provide for third-party mechanisms, which are, however, of *permissive or ancillary character*. In particular, national laws usually provide for:

- Common jurisdictional basis of optional character.⁵⁶
- Permissive intervention⁵⁷ as opposed to intervention as of right.
- Joinder⁵⁸ of a proper party drafted in permissive terms,⁵⁹ as opposed to joinder of party necessary for the adjudication.
- Consolidation⁶⁰ in permissive terms.⁶¹

⁵⁴ Vincent-Guinchard, *Procédure Civile*, (27th ed. 2003), para 1157.

⁵⁵ Cf French CCP art.325: L'intervention n'est recevable que si elle se rattache aux prétentions des parties par *un lien suffisant*.

⁵⁶ EC Reg. 44/2001 art. 6, French CCP art. 42, Greek CCP art. 37.

⁵⁷ US Fed R.C.P. r.24(b)(2).

England CPR r.19.2, particularly para (b).

French CCP art 330 (intervention accessoire).

German CCP s. 66.

Greek CCP art. 80.

Cf UNIDROIT r.12.2.

Different national provisions use different terms for this type of intervention: voluntary ancillary (France), simple ancillary (Greece), intervention of desirable party (England), permissive intervention (US). They are all of permissive character, though, In England there was a distinction between intervention as an absolute right and intervention in discretionary right, even before the new CPR; for the former see *In re Metropolitan Amalgamated Estates, Ltd.*, (1912) 2 Ch. 497 (receivership); for the latter see *Re Fowler*, 142 L.T.Jo. 94 (Ch.1916).

⁵⁸ US Fed R.C.P. r.20(a).

England CPR r.19.2.

Germany CCP s.60.

Greek CCP art. 74.

Cf UNIDROIT r.12.1.

Again different terms are found in different national provisions: for example permissive (US), joinder of desirable party (England), simple joinder (Greece).

⁵⁹ The court has a *discretionary right rather than a duty* to order a permissive joinder, even when all the formal requirements are met (AII 343/1971, EEN 1971.521), whereas once a party establishes all the prerequisites to intervention of a right, the *district court has no discretion to deny the motion*; see *United States v Georgia*, 19 F.3d 1388, 1393 (11th Cir.1994)).

⁶⁰ US Fed R.C.P. r.42.

French CCP art. 367.

German CCP, s.147.

Greek CCP 246.

Cf UNIDROIT r.12.5.

⁶¹ See the wording of all the above provisions ("the court *may* order"); cf *Kelly v Kelly*, N.D.N.Y.1996, 911 F.Supp. 66 "Where there is common question of fact or law, cases may be joined in interests of efficiency, but consolidation is by no means a necessity"; to the same effect *Lloyd v Industrial Bio-Test Laboratories, Inc.*, D.C.N.Y.1978, 454 F.Supp. 807; and *Williams v National Sur.*, C.A.5 (Ala.) 1958, 257 F.2d 77 1: consolidation of several actions in the context of vertical construction contracts

- Interpleading in permissive terms.⁶²

Permissive third-party mechanisms are accorded to the relevant parties as a matter of discretion rather than duty. In addition, unlike the case in compulsory third-party mechanisms, national courts may not permit the application of permissive third-party mechanisms, if they decide that multiparty proceedings would not be beneficial in view of the circumstances of the particular case.⁶³ In this instance, bilateral proceedings between the two original parties would go on and, therefore, the judgment would bind only the original parties in the proceedings. Multiparty proceedings are not compulsory with regard to third parties that have loose substantive links with an original party to the proceedings.⁶⁴

Also, even if the third party is brought in the proceedings between the original parties, the several co-claimants or co-defendants will retain a degree of procedural autonomy during the proceedings.⁶⁵ They will not merge into a procedural unit as would be the case when a third party is brought in the proceedings by reference to compulsory third-party mechanisms. The weak substantive links between original and false third parties of this group are echoed in their procedural relationship.

is just a matter of *discretion*; similarly, *International Paving Systems v Van-Tulco*, E.D.N.Y.1992, 806 F.Supp. 17.

⁶² US Fed. R.C.P.: art 14 (a), which even allows for cross claims between the third party and the original party, and (b).

England CPR r.19(2).

French CCP art.331(1).

German CCP s.72. Greek CCP art. 88.

⁶³ See for example US Fed.R.C.P. r.24 (2): "On timely motion, the court may permit anyone to intervene", as opposed to r.24 (1): "On timely motion, the court must permit anyone to intervene"

⁶⁴ *Dunham v Robertson*, C.A.10 (Wyo.) 1952, 198 F.2d 316: proper parties are those who have an interest in the subject-matter which may be conveniently settled in the suit, but whose presence is not essential to the determination of the controversy between the immediate litigants; and see too *Jones Knitting v Pullen*, S.D.N.Y.1970, 50 F.R.D. 311: parties who are jointly and severally liable are not indispensable parties but are proper parties who may be joined but who have no substantive right to compel joinder.

⁶⁵ Thus, it is possible that separate judgments are rendered against each joined defendant *National Sur v City of Allentown*, 27 F. Supp. 515 (E.D. Pa. 1939). Or, as is accepted in France, the consolidation of several proceedings by virtue of NCCP art.367 does not merge the several parties or claims; see Civ.2nd, 9 May 1985, *Bull.civ.II*, 93 and Vincent para 1166; cf also French NCCP art.324: "les acts accomplis par ou contre l'un des cointéressés ne profitent ni ne nuisent aux autres...". In the US, it is also accepted that consolidated proceedings are not merged: see *Zdanok v Glidden*, C.A.2 (N.Y.) 1964, 327 F.2d 944, holding that consolidation does not merge actions into a single cause, or change the rights of the parties, or make those who are parties in one suit parties in another; see also G. Virden, "Consolidation Under Rule 42 Of The Federal Rules Of Civil Procedure", 141 *F.R.D.*, p.169.

In the same vein, German CCP s.61 provides for loose procedural relationships between the several co-parties after the joinder: "unless otherwise provided by the Civil Code or this Act, the joined have the status of individual parties vis-à-vis the opposing party such that the actions of one of the joined parties shall not affect the others to their benefit or detriment"; it is indeed provided otherwise in art 62 with regard to the *joinder of necessary parties*. see above. The same provisions can be found in Greek CCP arts. 75-76.

Furthermore, the application of *permissive* third-party mechanisms, as opposed to *compulsory* ones, is subject to less stringent conditions. For permissive third-party mechanisms to apply, national procedural laws normally require that third party has either

- *Some interest*⁶⁶ in the dispute between the original parties; or
- That the several claims arise out of the *same transaction*;⁶⁷ or
- That the several claims arise out of a *substantially similar factual and legal basis*;⁶⁸ or
- That there is *a common question of law or fact* or there is an issue involving the new party and an existing party, which is connected to the matters in dispute in the proceedings⁶⁹

As national courts have repeatedly found, the above condition for the application of permissive third party mechanisms are normally met without difficulty in the context of false third parties of the second group. Indeed, national courts will normally apply third-party mechanisms of permissive character to multiparty relationships where the several parties are contractually interrelated but not strongly associated in terms of rights and liability, i.e. co-liaible or co-holder of rights and duties.

Thus, for example, the US national courts have accepted the application of permissive intervention in the context of insurance contracts, holding that an insurer should be permitted to intervene in pending proceedings between a co-insurant and the insured pursuant to r.24(b), but not as a matter of right 24(a).⁷⁰ It has also been held that an indemnitor may intervene in action against a principal debtor. Permissive intervention has also been accepted in the context of secured transactions,⁷¹ construction disputes⁷² and product liability.⁷³ Permissive joinder has also been accepted in the context of web-type construction contracts where an owner has direct

⁶⁶ For example French CCP art.330 or Greek CCP art.80, which is usually construed liberally, see above note (12 notes above) on the meaning of this interest.

⁶⁷ For example, US Fed R.C.CP. r.20.

⁶⁸ For example, German CCP s.60.

⁶⁹ For example English CPR 19(2).

⁷⁰ In *United States Fire Insurance v Freedom Village Of Sun City Center*, 2006 WL 1046946 (M.D.Fla.) Insurer's intervention as a matter of right was rejected also in *Continental Cas v ZHA*.M.D.Fla.1994, 154 F.R.D. 281.

⁷¹ See *Knapp v Hankins*, E.D.Ill.1952, 106 F.Supp.43.

⁷² *Use of Automatic Sprinkler Corp. of America v Fidelity & Deposit*, Md., M.D.Pa.1958, 22 F.R.D. 248.

⁷³ See *Sackman v Liggett Group, Inc.*, E.D.N.Y.1996, 167 F.R.D.6.

claims against both an engineer and an architect, at least in the alternative;⁷⁴ or in the context of secured transaction where a creditor has direct claims against both a surety and a debtor.⁷⁵

Finally, consolidation has been accepted in the context of secured transactions,⁷⁶ whereas interpleading has been accepted in the context of secured transactions⁷⁷ and string construction contracts.⁷⁸

⁷⁴ In some jurisdictions joinder, even in the permissive form, will not be applicable in the context of string contracts or vertical construction contracts. This is because some national civil procedures require in order for two persons to be joined as co-defendants the claimant must have a *direct claim* (joint, several or, at least, in the alternative) against both of the co-parties (for example, in the US where r.20 requires that co-parties are liable jointly, or severally or in the alternative, and in Greece where CCP art 74 requires a joint or a joint and several, in the least, liability, see Κεραμεύς-Νίκας-Καλαβρός, ΕρμΚΠολΔ, αρθρ. 74). So, the joinder of the contractor and the subcontractor (or the joinder of the seller and the manufacturer) will require that the owner (or the buyer) has a direct claim against both the contractor and the subcontractor. In that case the joinder will be possible only in the event of tortious or pass-through claims by the owner against the subcontractor or in the event of warranty (expressed or implied) liability of the manufacturer vis-à-vis the buyer.

See for example, *Tyler v Dowell, Inc.*, C.A.10 (N.M.) 1960, 274 F.2d 890, where the second-tier subcontractor had a “hold-harmless agreement” with the contractor. The same will apply when there is a direct claim based on a bond: *U. S. to Use of Par-Lock Appliers of New Jersey v J. A. J. Const.*, E.D.Pa.1943, 49 F.Supp. 85, affirmed 137 F.2d 584: subcontractor was a ‘proper party’ defendant to suit on general contractor's payment bond to recover balance due from the subcontractor's subcontractor for labor and materials furnished for construction of a public work.

But see *Mississippi Valley Structural Steel v Huber, Hunt & Nichols*, D.C.Ill.1969, 295 F.Supp. 139, where a second-tier subcontractor, who had no cause of action directly against the general contractor, was permitted to join, by virtue of US FRCP r.20, with a first-tier subcontractor as plaintiff when it was alleged that the general contractor's breach of the contract with the first-tier subcontractor caused the latter's breach of his contract with the second-tier subcontractor and that the general contractor would ultimately be liable. This decision is criticized as erroneous by Wright and Miller§ 1656, “because the text of Rule 20 permits joinder only of plaintiffs asserting a right to relief against the defendant”.

⁷⁵ *Minneapolis Brewing v Merritt*, D.C.N.D.1956, 143 F.Supp. 146: joinder of principal obligor and guarantor as defendants in the same action was permissible; the same *Decatur Coca-Cola Bottling v Variety Vending*, N.D.Ga.1967, 277 F.Supp. 393; *Delia Plastering v D.H. Dave*, N.D.Ohio 1951, 11 F.R.D. 304: where the surety company was liable jointly and severally with subcontractor on contract, surety company was a proper party to the action for breach of subcontract action within this rule; cf also *Pierce Consulting Engineering v City of Burlington*, Vt., D.C.Vt.1953, 15 F.R.D. 23.

⁷⁶ See *Williams v National Sur. Corp.*, C.A.5 (Ala.) 1958, 257 F.2d 771: actions by a subcontractor against a contractor for the unpaid balance of the contract price and claimed extras and by contractor against subcontractor's surety, which impleaded subcontractor, involved common issues of fact and law, and consolidation of such actions for trial was matter within trial court's discretion; *International Paving Systems v Van-Tulco.*, E.D.N.Y.1992, 806 F.Supp. 17: action brought by a subcontractor's concrete supplier seeking payment from general contractor and sureties on public construction project would be consolidated with related action in which subcontractor's trustee was suing general contractor; both actions involved question of who was responsible for concrete's cracking; cf *Cruickshank v Clean Seas*, D.Mass.2005, 402 F.Supp.2d 328: separate actions arising from damages caused by allegedly defective anti-fouling bottom paint for boats would be consolidated, since they involved common parties, all within the manufacture and sales chain, and nearly identical facts and some overlapping legal claims, and consolidation would substantially reduce judicial time and resources required to manage and try the two cases.

⁷⁷ See *Commercial Credit Development Corp. v Scottish Inns of America, Inc.*, 69 F.R.D. 110 (E.D. Tenn. 1975) and *Atlantic Coast Line R. Co. v U.S. Fidelity & Guaranty Co.*, 52 F. Supp. 177 (M.D. Ga. 1943): both held that interpleading by virtue of r.14 is proper in a case where a surety or

In England joinder of a third party insurer's bureau as co-defendant was accepted in the proceedings between the person injured and the person responsible for the injury.⁷⁹ It was held that the bureau, which had an obligation under an agreement to pay all unsatisfied judgments against motorists was "plainly not 'a person who *ought* to have been joined as a party'".⁸⁰ The bureau was, nevertheless, a party that *should* be joined in the proceedings so that "all matters in dispute in the cause or matter may be effectually and completely determined and adjudicated upon."⁸¹

In France, courts have accepted permissive intervention for a guarantor to participate in disputes between a debtor and a creditor.⁸²

In Greece interpleading has been accepted in the context of a guarantee,⁸³ an insurance company,⁸⁴ and in the context of vertical construction contracts.⁸⁵

To sum up, when several parties are contractually interrelated but not strongly associated in terms of rights and liability, national procedural laws provide for an extensive legal framework of *permissive* third-party mechanisms. This permissive legal framework reflects the intensity of the substantive nexus between original and false third parties of this type: the latter are not strangers to the dispute between the original parties but they are not indispensable for the determination of the dispute either.

guarantor seeks to enforce the liability of a principal who has agreed to indemnify him or her; *Federal Deposit Ins. Corp. v National Sur. Corp.*, 434 F. Supp. 61 (E.D.N.Y. 1977) held the same based on the theory of subrogation; see also *State ex rel. Neal v Johnson*, 33 F. Supp. 850 (W.D. Okla. 1940): If the original action is brought against the surety and the principal, the principal may implead another surety who has also furnished a bond guaranteeing faithful performance of the same duties.

⁷⁸ See *Jeub v B/G Foods*, 2 F.R.D. 238 (D.Minn. 1942); *Tevington v International Milling*, 71 F. Supp. 621 (W.D.N.Y. 1945) and *Altec v FWD*, 399 F.2d 860 (5th Cir. 1968), holding that the seller may seek indemnity up the chain of privity, by virtue of art 14 and impleading, through theories of warranty either implied or express. See also L. Warden "Right of retailer sued by consumer for breach of implied warranty of wholesomeness or fitness of food or drink, to bring in as a party defendant the wholesaler or manufacturer from whom article was procured" 24 A.L.R.2d 913 (Originally published in 1952), arguing that in the context of string contracts "the trend established [...] is, clearly, that under modern practice statutes such an impleader is proper" at 913. Interpleading is liberally permitted in construction disputes in which a court wishes to determine in one action whether a material supplier, a subcontractor, or someone else on the site is responsible for the defects, see for example *LASA Per L'Industria Del Marmo Societa Per Azioni of Lasa v Alexander*, 414 F.2d 143 (6th Cir. 1969) and *Westinghouse Elec. Supply v Nicholas*, 28 F.R.D. 8 (D. Minn. 1961).

⁷⁹ See *Gurtner v Circuit*, [1968] 2 Q.B. 587 (CA).

⁸⁰ Under the Rules of Supreme Court Order 15, r.6(2).

⁸¹ Per Diplock L.J. at 601.

⁸² Civ.2e, 9 Octo. 1975, *JCP* 1977.II18580, note Martin Vincent-Guinchard, *Procédure Civile*, (27th ed. 2003) para 991.

⁸³ See ΑΠ 689/1964, *NoB* 1965, 399.

⁸⁴ See ΑΠ 88/1984, *ΑρχΝομ* 1984, 744.

⁸⁵ See ΕφΑθ 11789/1987 *ΑρχΝομ* 1989, 40.

8.3 CONCLUSIONS OF CHAPTER 8

In the light of the above analysis it is concluded that: the procedural relationships between false third parties and original parties reflect their association in terms of substantive interests and liability. More specifically, the following scheme is established:

- In the first group of false third parties, where original and false third parties are strongly associated in substantive terms (typically co-liaible or co-holders of rights and duties) → *compulsory* third-party mechanisms and *close* procedural relationships between the several co-parties will be provided by national litigation systems.
- In the second group of false third parties, where original and false third parties are contractually interrelated but not *strongly associated* (normally liable in the alternative rather than co-liaible) → *permissive* third-party mechanisms and looser procedural relationships between the several co-parties will be provided by national litigation systems.

The above general conclusion is subject to the considerable divergence of the various national laws.⁸⁶ Nevertheless, it is reasonable to argue that, in principle, the above conclusion qualifies as a general guideline on third-party mechanisms. Therefore, it will be used in the following chapters as the yardstick to examine whether third-party mechanisms *can* and *should* be applicable to international arbitration and, if yes, in which particular circumstances.

⁸⁶ In the US, the 1966 Amendments liberalised the procedural system with regard to the third-party participation into proceedings between original parties. For example the terms “indispensable” and “necessary” in the original r.19 were substituted with the wider term “party needed”; or the condition of intervention found in the original r.24(a)(2) that the third party “is or may be bound by a judgment in the action” was omitted (in general, see Advisory Committee Notes on art.19 and 24). The 1966 Amendments have facilitated and expanded the application of third party mechanisms to a wider circle of persons. However, they have not overturned the basic distinction between third party mechanisms of permissive character and those that are applicable as a matter of right.

Chapter 9: Third-party mechanisms in the context of arbitration and the principle of procedural party autonomy	165
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9.1 Relevance of the principle of procedural party autonomy	165
9.2 Procedural party autonomy, as a rule, will prevail over third-party mechanisms	167
9.3 Third-party mechanisms in the context of multiparty projects where parties are contractually interrelated but not strongly associated in substantive terms.	170

CHAPTER 9: THIRD-PARTY MECHANISMS IN THE CONTEXT OF ARBITRATION AND THE PRINCIPLE OF PROCEDURAL PARTY AUTONOMY

9.1 RELEVANCE OF THE PRINCIPLE OF PROCEDURAL PARTY AUTONOMY

The focus of the discussion in this Chapter shifts from litigation to arbitration. The aim here is to determine whether third-party mechanisms should be applied to arbitration and, if yes, in which circumstances. The findings of the previous Chapter on the underlying principles and rationale of third-party mechanisms in general are tested here against the backdrop of the prevailing principles in arbitration specifically. Particular attention is focused on the principle of *procedural party autonomy*, according to which the parties have the freedom to choose the forum where they will have their disputes resolved and to determine the procedure applicable to the resolution of their disputes. Thus, procedural party autonomy gives the parties the right to regulate their procedural relationships in a way that best serves their commercial interests.

The choice of procedural party autonomy as the most relevant principle for the discussion here was made for three main reasons: First, arguably, party autonomy is the most distinctive feature of arbitration, particularly in an international context where national considerations and, therefore, national mandatory rules are of less importance.¹

Secondly, other key arbitration principles bear less relevance to the particular discussion of arbitration and third parties. As was demonstrated in Part II, the

¹ J. Lew, L. Mistelis and S. Kroell, *Comparative International Commercial Arbitration*, (Kluwer Arbitration Law 2003), para. 2-44: “party autonomy is the primary source of arbitration and the procedure. See also Fouchard, Gaillard and Goldman, *On International Commercial Arbitration*, E. Gaillard and J. Savage (eds) (Kluwer 1999), para 44 et seq.

principle of contractual origins of arbitration, for example, while important in other areas of arbitration, cannot deal satisfactorily with the problems relating to third parties. In fact, the discussion on third parties and arbitration pertains more to jurisdiction rather than contract law, and accordingly the principle of contractual nature of arbitration has limited relevance here.

The same applies to the principle of confidential character of arbitration. The latter has a conspicuous role in arbitration, and references thereto are frequent even in the context of the discussion on third parties.² However, it is arguable whether confidentiality is an *inherent conceptual feature of arbitration*.³ Confidentiality is not *ipso facto* applicable to arbitration. Rather, it must be expressly provided by an arbitration agreement or the applicable arbitration rules.⁴ It can be argued, therefore, that confidentiality does not have an institutional role in arbitration. This is not to suggest that confidentiality, particularly when the parties have expressly provided for it, has no bearing whatsoever on the discussion arbitration and third parties. On the contrary, whenever applicable, confidentiality will have a role to play, militating against the application of third-party mechanisms and the participation of third parties in bilateral proceedings which the original parties wanted confidential. However, compared to procedural party autonomy, confidentiality would only be one factor of relative importance, which tribunals should take into account among other factors in determining whether third-party mechanisms should apply to a particular case.

Third, procedural party autonomy not only is an intrinsic characteristic of arbitration, but it is also directly relevant to the jurisdictional viewpoint taken by the thesis. As was explained in detail above, the thesis adopts a jurisdictional approach focusing on the jurisdictional implications of an arbitration agreement and the dispute pending before a tribunal for third parties. In this context, procedural party autonomy has a significant pertinence to the discussion here. This is because, procedural party autonomy, in effect, regulates the freedom of parties to allocate jurisdiction to the forum they think best for their commercial needs. In other words, procedural party autonomy is a *jurisdictional tool*, by which parties make jurisdictional arrangements for the resolution of their disputes. Therefore, procedural party autonomy more than

² Leboulanger, "Multi-contract arbitration" (1996) 13(4) *J'Int'l Arb.* 43, p. 65, Nichlish, "Multiparty Arbitration and Dispute Resolution in Major Industrial Projects" (1994) *J' Int'l Arb* 57, p. p.69.

³ See Lew-Mistelis-Kroell: "Without an explicit agreement between the parties there will be no binding obligation of confidentiality under most arbitration laws", *supra* n.1, para. 8-45 and the judgment of the Swedish Supreme Court, 27 Oct 2000, 51(11) *Mealey's IAR*, B 1, cited therein.

⁴ *Idem*.

any other arbitration principle constitutes the touchstone to determine whether third-party mechanisms, by nature jurisdictional, should apply to arbitration.

9.2 PROCEDURAL PARTY AUTONOMY, AS A RULE, WILL PREVAILS OVER THIRD-PARTY MECHANISMS

The key argument in this Chapter is that, as a rule, procedural party autonomy will prevail over third-party mechanisms. The right of the parties to opt for several bilateral arrangements rather than a single multilateral agreement for the resolution of their disputes should be observed. The scheme of several bilateral dispute resolution agreements should be uphold even against the background of a multiparty commercial project. Of course, this might result in jurisdictional fragmentation of the multiparty project with the several parties involved therein being subject to the jurisdiction of different adjudicatory fora. However, jurisdictional fragmentation should be accepted as a legitimate side effect of procedural party autonomy, which as a rule should prevail over third-party mechanisms. This is demonstrated by the following.

Jurisdiction, in general is determined on the basis of personal connecting factors, usually by reference to the defendant's presence, domicile or residency.⁵ In other words, jurisdiction is determined on the basis of the *unique* link between a particular court and a particular party. Thus, the rule is that every person will be tried on its "personal forum", that is a forum individually identified by reference to the personal characteristics of that party. It follows that *jurisdiction, as a general rule, is determined on individual and party-oriented basis*.

However, third-party mechanisms contravene this rule. Third-party mechanisms confer jurisdiction on a single court over several parties, which otherwise would be subject to the jurisdiction of another court.⁶

For example, French New Code of Civil Procedure art. 42 provides that, when the claimant has a claim against several defendants which are subject to the jurisdiction of different courts, the claimant may bring a single claim against all the defendants

⁵ In Germany, see ZPO s.13 (residence); in France, see NCCP art.42 (domicile); in England see s.41 of the Civil Jurisdiction and Judgments Act 1982 providing for domicile; however, English traditional rules on jurisdiction provide for presence, see Morris, *The Conflict of Laws*, (6th ed) (London Sweet & Maxwell 2005), para. 5-0001 et seq; in Greece see Greek CCP art.22 (domicile); in the Context of European Regulation 44/2001 see art.2 (domicile); *cf* also the NY CPLR s.301 (Presence, or domicile).

⁶ European Regulation 44/2001 art. 6. or French NCCP art.42(2), German ZPO s.36(1)(3), Greek CCP art 31(1).

before a single court, namely the court of the domicile of one of the several defendants. Thus, many of the several co-defendants will be brought before a court different from the court of their own domicile, i.e. their “personal forum”. Jurisdiction for those defendants will not be determined on the basis of their personal connecting factors (personal domicile or residence or presence). In order for one court to resolve all the matters in dispute, the several defendants will have to be subject to the jurisdiction of a court other than their “personal forum”. *The principle of effective resolution of the dispute, here, takes precedence over the rule requiring that jurisdiction should be determined on a personal basis.*

Similarly, English Civil Procedural Rules (CPR) r.19.2(2) provides that:

“The court may order a person to be added as a new party if (a) it is desirable to add the new party so that the court can resolve all the matters in dispute in the proceedings; or (b) there is an issue involving the new party and an existing party which is connected to the matters in the dispute in the proceedings, and it is desirable to add the new party so that the court can resolve that issue”.

Here again, a person that is “connected to the matters in the dispute in the proceedings” will be added as a new party to proceedings before a court that most likely is not his “personal forum”, namely the court that would have been sued at, were this party the only defendant.

Likewise, English CPR r. 6.20(3) provides that service out of the English jurisdiction is permitted when:

“A claim is made against someone on whom the claim form has been or will be served (otherwise than in reliance on this paragraph) and (a) there is between the claimant and that person a real issue which is reasonable for the court to try; and (b) the claimant wishes to serve the claim form on another person who is a necessary or proper party to that claim”.

Here, service out of the English jurisdiction will be permitted for a person considered necessary for the resolution of the dispute pending between two other parties. Thus, this “necessary person” will be subject to the jurisdiction of a court determined by reference to residence, presence or any other personal connecting factor of the *original defendant*, rather than by reference to his own residence, domicile or any other personal connecting factor.

The same applies for third-party mechanisms provided in other jurisdictions, such as the US Federal Rules of Civil Procedure r. 14 or r.19, the EC Regulation 44/2001 art.6 or the German Civil Code of Civil Procedure s.36(1)(3). In all the above cases, third-party mechanisms establish jurisdiction of a single court over several parties in a way that deviates from the rule according to which jurisdiction has to be determined on an individual basis, by reference to the personal connecting factors of the parties in the claim. Thus, in the context of third-party mechanisms jurisdiction is established on a *multiparty basis*, by reference to the *pending dispute* and its *implications for third parties*. Therefore, *in third-party mechanisms jurisdiction is determined on multilateral and dispute-oriented basis*.

Provided that certain conditions are met, this is, indeed, a legitimate deviation. However, it still remains a deviation, which allows the reasonable conclusion that third-party mechanisms establish the jurisdiction of a particular court *on an exceptional basis*. Third-party mechanisms, therefore, are *exceptional in nature*.

Accordingly, *the presumption* should be for the determination of jurisdiction on a *personal basis rather than on a multiparty basis*. The presumption should be that jurisdiction would be determined *on the basis of the personal connecting factors of the parties, rather than the pending dispute*. Therefore, as a matter of general rule, *third-party mechanisms should apply only if exceptional circumstances exist*.

The same applies to arbitration. Here, *an arbitration agreement* constitutes the *personal connecting link* between the parties, which have entered into an arbitration agreement, and the specific arbitral tribunal determined therein. Jurisdiction, as a rule, should be determined on the basis of this *personal jurisdictional factor*, namely the arbitration agreement alone. The arbitral tribunal becomes, thus, the “personal forum” for the parties to an arbitration agreement. The same, of course, will apply when two parties enter into a jurisdictional agreement, which confers exclusive jurisdiction to the courts of a particular country, which, therefore, becomes the personal forum for the parties to the jurisdiction agreement.

Consequently, whenever two parties enter into a valid dispute resolution agreement, jurisdiction will have to be determined on the basis of this agreement alone. Therefore, here again -as in the context of litigation- jurisdiction is determined *on a individual and party-oriented basis*. Therefore, in arbitration the way jurisdiction is established follows the general rule.

Thus, whenever several parties in the context of a multiparty commercial project conclude several bilateral dispute resolution agreements, jurisdiction will have to follow the general rule: it should be determined on an individual and party-oriented basis, namely on the basis of the several bilateral dispute resolution agreements alone. The scheme of several dispute resolution agreements of the parties is in accord with the general rule for the determination of the jurisdiction, and therefore this scheme should be presumed to have priority over any other mechanism providing otherwise. In particular, the scheme of the several bilateral agreements on jurisdiction should be presumed to have priority over the third-party mechanisms, in the context of which, jurisdiction is determined on a multilateral and dispute-oriented basis. For third-party mechanisms to overturn this scheme and bring all the parties before the same forum, *exceptional circumstances must exist*.

Therefore, in principle, jurisdictional fragmentation of a multiparty commercial project, which may result from several bilateral jurisdiction arrangements, must be considered *perfectly legitimate*. The principle of procedural party autonomy, allowing the parties to make jurisdictional arrangements in a way that best serves their commercial interests, constitutes the rule and, therefore, it should take precedence over the third-party mechanisms that constitute the exception.

This conclusion will apply *a fortiori* when, as in the majority of the cases, the scheme of several bilateral dispute resolution arrangements provide for *exclusive* arbitration or jurisdiction agreements, conferring exclusive power to a specific arbitral tribunal or the courts of a particular country. Consequently, it will be even more difficult for third-party mechanisms to apply here. In fact, only in rare exceptional circumstances will third-party mechanisms overturn procedural party autonomy in the context of arbitration.

9.3 THIRD-PARTY MECHANISMS IN THE CONTEXT OF MULTIPARTY PROJECTS WHERE PARTIES ARE CONTRACTUALLY INTERRELATED BUT NOT STRONGLY ASSOCIATED IN SUBSTANTIVE TERMS

The rule, that procedural party autonomy will prevail over third-party mechanisms, will particularly apply when, as in the majority of the cases, the parties in a multiparty project are contractually interrelated but not strongly associated in terms of interests and liability (the second group of false third-parties as defined in Chapter 2). As the following analysis will show, when several parties do not share rights or liability no

exceptional circumstances will exist in order to overturn the general rule, even if these parties are contractually intertwined.

Here, the analysis is based on the findings of the previous chapter: as was shown there, third-party mechanisms of permissive character should be provided whenever the several parties are contractually interrelated but not strongly associated in terms of interests and liability. However, in terms of jurisdiction, third-party mechanisms of *permissive character* rank below in the hierarchy compared to procedural party autonomy. Therefore, they cannot overturn the scheme of several bilateral arrangements on jurisdiction of the several parties.

This is accepted in many jurisdictions. For example, in England it is accepted that where there is an effective exclusive jurisdiction clause between two only of several interrelated parties the possibility of a multiplicity of proceedings will not necessarily prevent it being given effect.⁷

In *Credit Suisse First Boston (Europe) Ltd v MLC (Bermuda) Ltd*,⁸ the defendant, MLC, concluded two bond purchase agreements with Credit Swiss Europe, which provided for exclusive jurisdiction of English courts. The defendant had a separate customer agreement with a US affiliate of Credit Swiss Europe, Credit Swiss US, which agreement contained no jurisdiction clause. Thus, the parties here had opted for bilateral jurisdictional agreements: MLC and Credit Swiss Europe were subject to exclusive jurisdiction of English courts, whereas MLC and Credit US were subject to the jurisdiction of the national courts of either Bermuda (the place of domicile of MLC) or the US (place of domicile of Credit Swiss US).

When a dispute arose out of the sales agreement, Credit Swiss Europe commenced proceedings against the MLC before the English courts in accordance with the exclusive jurisdiction agreement. MLC responded by commencing legal proceedings against the Credit Swiss US and Credit Swiss Europe before the US courts.

Credit Swiss Europe applied to the English courts for an anti-suit injunction to restrain MLC from going on with the US proceedings against the Credit Swiss Europe and the Credit Swiss US on the basis of the English jurisdiction clause contained in the purchase agreement. In addition, Credit Swiss Europe requested the English courts to join Credit Swiss US as a party to the action against MLC. The latter applied for a stay of the English proceedings in favour of New York.

⁷ Civil Procedure, (The White Book). Brook (ed) (Sweet & Maxwell 2005) at 6.21.29.

⁸ [1999] 1 Lloyd's Rep. 767.

The English court seised of the dispute had to look, among other issues, into two different options: the court could opt for multiparty proceedings, issuing an anti-suit injunction against MLC and joining Credit Swiss US to the English proceedings; alternatively the court could give effect to the exclusive bilateral agreement between Credit Swiss Europe and MLC and allow two parallel set of proceedings to go on before two different fora. The English Court, rightly, opted for the latter option. Rix J, held that:

“On the other hand, where different agreements are entered into for different aspects of an overall relationship, and those different agreements contain different terms as to jurisdiction, it would seem to be applying too broad and indiscriminate a brush simply to ignore the parties’ careful selection of palette [...] [the dispute resolution clause] is part of a bilateral agreement between a seller and a buyer, and the disputes to which such an agreement may give rise are prima facie bilateral disputes.”⁹

Similarly, in the US it has been held that “the mere fact of a possibility of piecemeal litigation will not be enough to accept participatory proceedings.”¹⁰ In particular, in *Snap-on Tools v Mason*,¹¹ claimant and defendant had entered into a dealer agreement that included an arbitration agreement. After a dispute arose, the defendant filled court proceedings against the claimant and four other of employees of the claimant. The claimant filed for a motion to stay proceedings on the basis of the exclusive arbitration agreement. The defendant maintained that the dispute involved more persons than the defendant and the claimant, and, therefore, the exclusive arbitration agreement should surrender before the risk of multiplicity of proceedings. The Fifth Circuit, referring to decision of the Supreme Court in *Moses H. Cone*,¹² noticed that the “desirability of avoiding piecemeal litigation” was indeed one valid consideration that could be taken into account so that the arbitration agreement was not given effect and all the several parties were brought before the same court. However, this consideration was only one of exceptional character and would apply only in view of exceptional factual circumstances. These exceptional factual circumstances did not apply in the case at hand, and therefore the bilateral arbitration

⁹ *Ibid.*, at 777.

¹⁰ See *Snap-on Tools v Mason*, 18 F.3d 1261, 1267 (5th Cir. 1994); see also *Dean Witter Reynolds v Byrd*, 105 S.Ct. 1238, 1242 (1985).

¹¹ 18 F.3d 1261, 1267 (5th Cir. 1994).

¹² 460 U.S. 1, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983).

arrangement should prevail over multiparty proceedings. Accordingly, the Court making also reference to the federal policy favouring arbitration, gave effect to the arbitration agreement pointing out that

“However, even if some piecemeal litigation does result, that sometimes is the inevitable result of a congressional policy strongly favoring arbitration”¹³

In similar facts, the Supreme Court in *Dean Witter Reynolds v Byrd*,¹⁴ gave effect to a bilateral arbitration agreement over third-party mechanisms, noting that

“The Arbitration Act requires district courts to compel arbitration of pendent arbitrable claims when one of the parties files a motion to compel, even when the result would be the possibly inefficient maintenance of separate proceedings in different forums. By its terms, the Act leaves no room for the exercise of discretion by a district court, but instead mandates that district courts shall direct the parties to proceed to arbitration on issues as to which an arbitration agreement has been signed. The Act's legislative history establishes that its principal purpose was to ensure judicial enforcement of privately made arbitration agreements, and not to promote the expeditious resolution of claims”¹⁵

The Court, here, recognised the legitimacy and, indeed, supremacy of contractual bilateral dispute resolution arrangements and gave effect to the arbitration agreement.

In all the above examples, the interrelation of the several parties in terms of interests and liability was not strong enough to warrant the application of third-party mechanisms of compulsory character. Most probably, in the context of litigation, the contractual interrelation of the several parties would only warrant the application of permissive third-party mechanisms, which could not overturn procedural party autonomy.

Equally, in France permissive consolidation of two cases involving several parties is not possible when one of the two disputes falls under the exclusive jurisdiction of one court.¹⁶ Also, in the same jurisdiction a party to court proceedings may interplead a third party and bring it before the court where dispute is pending between the two original parties, even if the third party would not be subject to the jurisdiction of this

¹³ *Ibid* at 1266.

¹⁴ 105 S.Ct. 1238, 1242 (1985).

¹⁵ 1240-1244.

¹⁶ Vincent-Guinchard, *Procédure Civile*, (27th ed. 2003), para 464.

court. However, when an effective arbitration agreement exists between the third party and one of the original parties the permissive third-party mechanism of interpleading will not be applicable.¹⁷

The same applies in other civil law jurisdictions, such as Greece for example. Permissive joinder cannot be effected when two of the several parties are bound by a valid jurisdiction agreement. The parties' right to establish an exclusive bilateral forum overrides permissive third-party mechanisms.¹⁸

Similarly in the context of the Brussels Convention:¹⁹ in *Hough v P&O Containers*,²⁰ the claimant brought an action in England against his employers, an English shipowning company, alleging that he was injured while working for them in a drydock in Germany. The defendants asked the court to join the German repairers as third parties to the action on the basis that the injuries of the claimant were the result of the negligence of the German repairers. The defendants relied on Art. 6(2) of the Brussels Convention providing that

“A person domiciled in a contracting state *may* also be sued . . . (2) As a third party in an action on a warranty or guarantee or in any other third party proceedings, in the court seised of the original proceedings”

In view of the above provision, the defendants argued that the German repairers must be brought before the English courts, as a third party against which the defendants would have a claim in case the court decided for the claimant.

However, the German repairers resisted the joinder relying on an exclusive jurisdiction agreement between them and the English shipowning company, which provided for exclusive jurisdiction of the German courts.

The court held that third-party proceedings provided by Brussels Convention 6(2) were not applicable in this case, because of the existence of the exclusive jurisdiction agreement between the third party and the defendants. The exclusive jurisdiction had a mandatory character and it had to take priority over the permissive third-party mechanism provided by Brussels Convention art.6(2).

¹⁷ See French NCPC art. 333 and Com. 8 Nov. 1982, Gaz Pal. 1983. Pan.99, note Guinchard. Art 333 provides: « le tiers mis en cause est tenu de procéder devant la juridiction saisie de la demande originaire, sans qu'il puisse décliner la compétence territoriale de cette juridiction, même en invoquant une clause attributive de compétence ».

¹⁸ EφΑθ 5065/1987, (1988) ΝοΒ 356; ΕφΑθ 10033/1995, (1996) ΕΛΛ 1386.

¹⁹ Superseded now by the Reg 44/2001.

²⁰ [1999] QB 834.

In the light of the above analysis two conclusions may be drawn:

First, as a rule procedural party autonomy will prevail over third-party mechanisms. Therefore, a scheme of several bilateral arbitration agreements between several parties, which constitute an expression of procedural party autonomy, should be upheld even against the backdrop of multiparty relationships. The jurisdiction of a tribunal should be limited to those parties that have concluded an arbitration agreement, rather than extend to third parties. In jurisdictional terms, procedural party autonomy prevails over third-party mechanisms.²¹

Secondly, this rule will apply in the majority of the multiparty projects, and particularly when the several parties in a multiparty project are contractually interrelated rather than strongly associated in terms of interests and liability (the second group of false third-parties as defined in Chapter 2). In other words, where the substantive links between the several parties would only warrant the application of permissive rather than compulsory third-party mechanisms. Thus, in principle, false third parties of the second group, such as a guarantor or a subcontractor or a parent company would not be able to take part in the arbitral proceedings between a creditor and a debtor, or an employer and a subcontractor, or a subsidiary and its co-contractor. The association between a false third party of this type and a genuine party, in terms of substantive liability and interests, is not strong enough to warrant the participation of the false third party in the bilateral arbitration proceedings. Here, third party-mechanisms cannot apply and, therefore, the tribunal should not assume extra-contractual jurisdiction over false-third parties of this group.

²¹ In fact, the application of permissive participatory mechanisms should be excluded *a fortiori* in the context of international arbitration. This is because of the clear pro-arbitration policy found in many jurisdictions. Parties are encouraged to conclude arbitration agreements, even if this would necessarily entail, in some cases, the jurisdictional fragmentation of interrelated relationships. Naturally, thus, in cases where an arbitration agreement is involved the courts will be even more reluctant to recognise participatory rights, at least of permissive character; instead, they will uphold the exclusive jurisdiction of the arbitral tribunal as established by a valid arbitration agreement, even if this would entail the jurisdictional fragmentation of an intertwined multiparty contractual relationship

Chapter 10: The exceptional circumstances where third-party mechanisms should apply in arbitration	176
10.1 The fundamental role of the pending dispute for the determination of the jurisdiction of a tribunal.....	177
10.2 Co-liability or community of rights between the several parties as a threshold for extra-contractual jurisdiction and third-party mechanisms	179
10.2.1 First: co-liability resulting from the contractual arrangements of the several parties.....	181
10.2.2 Second: co-liability resulting from the applicable substantive law	187
10.2.3 No lower threshold than co-liability or community of rights and duties warrants extra-contractual jurisdiction and third-party mechanisms.....	193

CHAPTER 10: THE EXCEPTIONAL CIRCUMSTANCES WHERE THIRD-PARTY MECHANISMS SHOULD APPLY IN ARBITRATION

The previous chapter established the rule that procedural party autonomy should prevail over third-party mechanisms. As was noted, *for third-party mechanisms to overturn the scheme of several bilateral jurisdiction arrangements, bringing all the parties before the same forum, exceptional circumstances must exist.*

The aim of this Chapter is to determine those exceptional circumstances. It is suggested that third-party mechanisms should apply to arbitration whenever third parties are strongly interrelated with the parties to the arbitration, i.e. whenever third and genuine parties are *co-liable or co-holders of rights and duties* (as is typically the case in the first group of false third parties, defined in Chapter 2). In such a case the several parties (third and genuine) will constitute *an inseparable unit in terms of jurisdiction*. A tribunal should apply third-party mechanisms and assume extra-contractual jurisdiction over the whole jurisdictional unit of the several genuine and third parties.

The Chapter first examines the fundamental role of the dispute in the determination of the jurisdiction of the tribunal when third parties are relevant to the resolution of the dispute (Section 10.1). It then sets out the conditions required for a tribunal to apply third-party mechanisms and assume extra-contractual jurisdiction (Section 10.2)

10.1 THE FUNDAMENTAL ROLE OF THE PENDING DISPUTE FOR THE DETERMINATION OF THE JURISDICTION OF A TRIBUNAL

Chapter 7 showed that once a dispute arises, arbitration agreements cease to be ordinary contracts affecting only those persons that have agreed thereto. Rather, arbitration agreements have *jurisdictional repercussions that may affect* a circle of persons wider than that of the parties originally set out in the arbitration contract. Arbitration agreements provide tribunals with jurisdictional power similar to that of national courts. Therefore, it was argued that a tribunal should be able to assume as much jurisdiction as necessary to resolve the pending dispute effectively (the notion of effective arbitral jurisdiction).

Once a dispute arises, there is a clear shift from the contractual to the jurisdictional characteristics of arbitration agreements. The dispute is the catalyst that “transforms” an arbitration agreement from an ordinary contract to an instrument with significant jurisdictional effects. Indeed, at the time of their conclusion, arbitration agreements are ordinary contracts. This is why their validity is determined in accordance with principles of contract law. However, once a dispute arises the jurisdictional effects of arbitration agreements start to take effect: jurisdiction of a tribunal is established over the specific dispute, excluding the jurisdiction of national courts. It follows that the jurisdictional effects of an arbitration agreement *can only be produced in relation to and in the context of a specific dispute*. Unless a specific dispute arises, it is impossible for a court or a tribunal to determine which forum would have jurisdiction over two parties bound by an otherwise valid arbitration agreement. Therefore, *the jurisdiction of an arbitral tribunal should always be determined in the light of the specific dispute at hand*.

This is not to argue that arbitration agreements have only jurisdictional characteristics. Their contractual origins remain present after a dispute arises. It is the original arbitration contract that sets out the contractual relationship out of which a dispute might arise at a later stage. It is the original arbitration contract that determines the principal goal of the tribunal that will be constituted at a later stage, namely the resolution of the dispute.¹ Accordingly, the jurisdiction of a tribunal is founded upon the original arbitration contract: *if it is found that an arbitration*

¹ Cf EAA s. 1(a): “*the object of the arbitration is to obtain the fair resolution of disputes...*” (emphasis added).

agreement as an ordinary contract was never validly concluded, the jurisdiction of a tribunal will be automatically revoked. The award will be hollow.² This is the fundamental difference between jurisdiction of national courts and jurisdiction of arbitral tribunals. The contractual origins of the jurisdiction of a tribunal remain always present, albeit latent.

However, once a dispute arises and a tribunal is established in accordance with the arbitration contract, the tribunal obtains its own jurisdictional dynamic. The jurisdictional character of the arbitration agreement becomes preponderant and vests the tribunal with jurisdiction to resolve the dispute in the most efficient way. The resolution of the dispute becomes the ultimate goal of the tribunal, and, accordingly, the latter should be able to assume as much jurisdiction as is necessary to get effectively disposed of the dispute.

It becomes clear from the above that *the jurisdiction of a tribunal should be co-determined by both the arbitration agreement and the pending dispute.* Otherwise, the jurisdiction of the tribunal will be truncated. Therefore, in terms of jurisdiction, it matters whether the dispute pending before a tribunal is inextricably tied up with a third party. In such a case, the arbitral tribunal should be able to assert its jurisdiction over the third party. Otherwise it would not be able to attain its primary goal: the effective resolution of the pending dispute.

Therefore, whether a dispute between two parties to an arbitration agreement has any implications for any third party bears significant relevance to the discussion of arbitration and third parties. This conclusion is in line with the findings of the previous chapter on the way jurisdiction is determined, in general. As was shown in Section 9.2 jurisdiction as a general rule is determined on individual and party-oriented basis. The jurisdiction of an adjudicatory forum is established by reference to personal connecting factors relating to the parties in action. However, it was noted that when third parties are so inextricably involved in the dispute that their presence in the proceedings is considered necessary for the resolution of the dispute, jurisdiction will be determined by reference to the pending dispute and its implications for the third parties. In this case the jurisdiction of the adjudicatory forum will be determined on multilateral and dispute-oriented basis. Therefore, eventually *whether jurisdiction will be determined on party-oriented basis or on*

² Cf NY art.V(1)(a).

dispute-oriented basis depends on the dispute and its implications. It depends on the extent to which third parties are involved in the pending dispute.

The same applies to arbitration. As a rule, the jurisdiction of a tribunal will be determined by reference to the arbitration agreements. Here the arbitration agreement between two parties will be the connecting factor relevant for the determination of the jurisdiction. However, when third parties to this arbitration agreement are inextricably involved in the resolution of the pending dispute, jurisdiction of the tribunal should be determined by reference to the pending dispute and its implications for the several parties. In this case too, the jurisdiction of the tribunals should be determined on multilateral and dispute-oriented basis.

Therefore, the role of the dispute in the discussion relating to jurisdiction and third parties is fundamental. In order to determine the scope of its jurisdiction, a tribunal should not only focus on the arbitration agreement. It should also examine the pending dispute and its implications for any third party.

10.2 CO-LIABILITY OR COMMUNITY OF RIGHTS BETWEEN THE SEVERAL PARTIES AS A THRESHOLD FOR EXTRA-CONTRACTUAL JURISDICTION AND THIRD-PARTY MECHANISMS

The next step is to determine the circumstances under which a dispute pending between two parties will have implications for a third party, which will require the tribunal to assume jurisdiction over the third party. In other words, the next step is to determine the conditions for extra-contractual arbitral jurisdiction.

It is submitted that a tribunal should assume extra-contractual jurisdiction by reference to the dispute only in case a third party is strongly associated with a genuine party to an arbitration agreement in terms of substantive rights and obligations. In particular, *it is necessary that a third party is co-liable or co-holder of rights and obligations with one of the genuine parties to an arbitration agreement.* Co-liability or community of rights and obligations between genuine and third parties will be the standards required for the tribunal to apply third-party mechanisms. As will be recalled, co-liability and community of rights and duties is the typical characteristic of the false third parties of the *first group* (described in Chapter 2). It should be noted that the typical examples of this group, examined in Chapter 2, do not constitute an exhaustive list of contractual relationships where third-party mechanisms will apply.

Eventually, it will be for an arbitral tribunal to determine whether the *specific* pending dispute has implications for a third party, which would warrant the application of third-party mechanisms. The aim of this study is to set out the *principles* for the application of third-party mechanisms, rather than to suggest a complete list of cases where third-party mechanisms must apply.

Thus, in general the tribunal should assume extra-contractual jurisdiction in the exceptional circumstances where the presence of a third party in the pending dispute between two other parties is considered *necessary, rather than merely desirable*. As national courts have held, this will be accepted in rare cases, where, the multiplicity of proceedings would not merely cause inconvenience but it would, for example,

- Cause the risk that “the interests of justice” are harmed;³ or
- Entail a “potential disaster from a legal point of view”;⁴ or
- Make the claims “virtually untriable”⁵

This suggestion is in line with the findings of Chapter 8 on the underpinning principles of third-party mechanisms: whenever a third and a genuine party are strongly associated in terms of substantive interests and liability they will constitute a *necessary jurisdictional unit*, upon which third-party mechanisms of compulsory character should apply. In such a case, the third party is an integral part of the pending dispute between the two genuine parties, so that third-party mechanisms should apply, even at the expense of procedural party autonomy.

³ *Sinochem International Oil v Mobil*, [2000] 1 Lloyd’s Rep. 670, J. Rix refused to stay the English proceedings commenced on the basis of a jurisdictional agreement even if that had the risk of multiplicity of proceedings: see at 680 “I do not see in the mere possibility of the multiplicity of proceedings, should Sinochem Beijing choose to commence new proceedings in Hong Kong, a strong reason why in the interests of justice Sinochem London should be relieved [of a jurisdictional agreement establishing jurisdiction of the English courts]”. Cf also *Reichhold Norway ASA v Goldman Sachs International* [1999] 2 All E.R. 174.

However, see *The Electric Furnace v Selas Corporation of America*, [1987] R.P.C. 23, where the Court of Appeal adopted a liberal approach to the term “interest of justice”, allowing a third party to be served out of jurisdiction despite the fact that it was not a necessary party to the action but merely a proper one; cf, however, the CPR r.19.5 providing for the addition or the substitution of a party only when it is *necessary*.

⁴ See *Aratra Potato v Egyptian Navigation (The El Amria)*, [1981] 2 Lloyd’s Rep. 119 (CA), LJ Brandon, at p. 128: “I do not regard it merely as convenient that the two actions, in which many of the same issues fall to be determined, should be tried together; rather I regard it as a *potential disaster from a legal point of view if they were not*, because of the risk inherent in separate trials, one in Egypt and the other in England, that the same issues might be determined differently in the two countries”.

⁵ *Mahavir Minerals v Cho Yang Shipping (The M C Pearl)*, [1997] 1 Lloyd’s Rep. 566, J Rix at 569: “It seems to me that so far the plaintiffs have shown strong cause why the jurisdiction clause should not be enforced. This is indeed a paradigm case for the concentration of all the relevant parties’ disputes in a single jurisdiction. If in such a case a host of different jurisdiction clauses were to be observed, the casualty at the root of the action would become *virtually untriable*”.

This close association in substantive terms between a third and genuine party to an arbitration agreement may result from

- First, the particular contractual arrangements between the several parties; or
- Second, the substantive law applicable to dispute

10.2.1 First: co-liability resulting from the contractual arrangements of the several parties

Based on the principles of party autonomy and contractual freedom, several parties are free to conclude several bilateral contracts with interrelated contractual terms, resulting in common rights or co-liability between the several parties. This is particularly the case, when the several contracts contain cross-references, setting out *cross-contract rights and duties*, namely rights and duties owned by parties to one contract vis-à-vis parties to another contract.

Cross-contract rights and duties may well jurisdictional repercussions: the several parties to different, albeit intersected contracts, might constitute a *necessary jurisdictional unit*. The *Sinochem International Oil (London) Co Ltd v Mobil Sales and Supply Corp.*⁶ case in the context of jurisdiction agreements exemplifies how contractual arrangements between several interrelated parties might have jurisdictional repercussions. Sinochem London sold crude oil to Mobil Delaware. Their contract provided for jurisdiction of the English courts and the application of English law (the English contract). The buyer, Mobil Delaware, admitted the sum due under the English contract but it claimed to set off sums allegedly due under a different contract between Mobil Oil Hong Kong (an affiliate of Mobil Delaware) as sellers and Sinochem Beijing (an affiliation of Sinochem London) as buyers. The contract between the two affiliates provided for jurisdiction of the Hong Kong courts and the application of Hong Kong Law (the Hong Kong contract).

Clause 18 in the English contract between the two parent companies expressly provided:

“Non-Performance

All payments under this agreement shall be made without set-off or counterclaim and will not be subject to any conditions except as provided in the following:

⁶ [2000] 1 Lloyd's Rep. 670.

Notwithstanding any other provisions of this or any other contract between the parties or their affiliates, in the event any party ('the non-performance party') shall default in the payment the other party ('the performing party') shall have the right to set-off, counterclaim or withhold payment in respect of any default by the non-performing party or any affiliate of the non-performing party under this agreement or any other agreement between the parties or their affiliates ...”

When Sinochem London filed a lawsuit against Mobil Delaware for the outstanding price before the English courts, which had exclusive jurisdiction on the basis of the jurisdiction agreement contained in the English contract, Mobil Delaware applied for permission to serve out of the jurisdiction Sinochem Beijing as a necessary or proper party to the existing proceedings. Sinochem Beijing and Sinochem London challenged the jurisdiction of the English courts with regard to the former: Sinochem Beijing was neither a party to the English contract nor a party to the jurisdiction agreement concluded exclusively between Sinochem London and Mobil Delaware.

Thus, the English Commercial Court seized of the dispute was faced with a rather complicated situation of conflicting jurisdictions: the several parties (the two parent and the two affiliate companies) had contractually established two separate adjudicatory fora with exclusive jurisdiction. In particular, they had established one forum in England with jurisdiction to resolve disputes between the two parent companies and another forum in Hong Kong with jurisdiction to resolve disputes between the two affiliates. However, because of the substantive interaction of the two contracts, the dispute between the two parent companies, falling under the exclusive jurisdiction of the English courts, was inextricably involving the affiliates. The question before Rix J was, thus, *whether the jurisdiction of the English courts, before which proceedings had been commenced between the two parent companies, should be extended to the affiliates.*

In order to determine the boundaries of the jurisdiction of the English courts, Rix J. focused on the pending dispute between the two parent companies. Clause 18 of the English contract expressly provided for cross-contract duties and rights between the two parent companies parties to the English contract and the two affiliates parties to the Honk Kong contract. Thus, the two affiliates, although not parties to the English jurisdiction agreement, were directly involved in the contractual arrangements set out

in the English contract. Therefore, they were integral parts of the dispute that arose out of the English contract. By reference to clause 18 in the English contract, the sum due by Mobil Delaware to Sinochem English could be set off against the sum due by Sinochem HK against Mobil HK. Consequently, Mobil Delaware and its affiliate Mobil H.K. were potentially co-holders of the claim against Sinochem HK under the HK contract, while Sinochem England and its affiliate Sinochem HK were potentially co-liaible for the price due by the latter against the Mobil H.K under the HK contract.

Thus, there was a *discrepancy between the scope of the dispute pending before the English courts and the scope of the English jurisdiction agreement*: due to the specific contractual arrangements the dispute necessarily involved parties falling outside the scope of the English courts, which was the forum with the exclusive jurisdiction to resolve the dispute. More generally, there was a *discrepancy between the substantive terms and the jurisdictional terms of the contractual arrangements of the several parties*.

Rix J rightly accepted that the jurisdiction of English courts should be determined not only by reference to *the English jurisdiction agreement* but also *by reference to the specific dispute at hand*. Since the affiliates were inextricably involved in the dispute at hand, the jurisdiction of the English courts, stemming from the English jurisdiction agreement, should be also asserted over the affiliates, despite the fact that the latter were not a party thereto. In essence, it was accepted that whenever several parties are strongly interrelated in contractual terms, they should be treated as a *jurisdictional unit*.

Rix J, noted:

“I come to that conclusion the more readily when I bear in mind that *Sinochem Beijing is only nominally a different party from Sinochem London*, and that the latter is of course not only already a party to these proceedings but is the claimant in them. I am naturally conscious that Sinochem Beijing has a separate legal persona from Sinochem London, and is incorporated in a different and foreign jurisdiction. Nevertheless, not only are Sinochem London and Sinochem Beijing associated companies, all part of the Sinochem group of companies, but *the special set-off clause contained in the English contract emphasizes just how closely the contracts of such affiliate companies are to be regarded for present purposes*. In other words, I think that I am entitled to

consider the two Sinochem companies as being in a very real sense, *for the purposes of the dispute which arises out of the English contract, one entity*" (emphasis added).⁷

In that way, one forum will have jurisdiction over the whole dispute and, thus, the discrepancy between the substantive and procedural arrangements of the several parties will be rectified. The jurisdictional arrangements should in effect follow the substantive arrangements of the parties, since the latter constitute the primary contractual goal of the parties. In this way a functional equilibrium between the substantive and procedural aspects of the same multiparty relationship will be re-established. In the words of Rix J:

"it seems to me that I am at least entitled to regard the parties as acting with at any rate assumed knowledge of their inter-group contractual relationship and as having intended the consequences of their agreement. It follows, therefore, that I must regard the English contract as having been agreed in its form, containing as it does both its special set-off clause and its exclusive English jurisdiction clause, *against the general background that a contract between affiliates such as would trigger off a right of set-off under the set-off clause might well contain its own jurisdiction clause*, as well as against the specific background that at the time the English contract was entered into the potential dispute arising out of the non-payment under the Hong Kong contract had already arisen. In such circumstances, to stay an action under the English contract on the basis that it involved a dispute under an affiliates' contract which could or even should more appropriately be litigated in another forum *would be to disregard the carefully balanced agreement which the parties to the English contract had seen fit to make.*"⁸

A similar approach was taken by the ICC tribunal in the case 5894 of 1989,⁹ in the context of arbitration agreements. A bank signed a finance agreement with a French company (the parents' agreement). The agreement set out a financing scheme through leasing in several countries and it contained an ICC arbitration clause. The framework finance agreement was followed by a separate agreement between a US subsidiary of

⁷ *Ibid.*, at 680.

⁸ *Ibid.*, at 679.

⁹ Partial award, 2 (1991) 2 *ICC Bull.*, p.25.

the bank and a US subsidiary of the French company (the subsidiaries' agreement). The bank and two of its subsidiaries commenced arbitration proceedings against the French company and its French subsidiary for sums payable by a US subsidiary of the French company to the claimant bank. The respondents, the French company and its French subsidiary, alleged that the claim could only be brought by the US subsidiary of the claimants against the US subsidiary of the French company, respondent.

The tribunal noted that the framework agreement between the two parent companies provided for rights and obligations not only for parent companies but also for their subsidiaries (cross-contract rights and obligations):

“the framework agreement... provides in its Article VII that all local agreements will proceed from it; [...] Article VIII of the [second] agreement applicable to US operations, of which it has already been said that it made express references to the [framework] agreement, provides that it will terminate immediately if notice of termination of the latter is given.”

Because of the close interrelatedness between the two agreements, the dispute before the tribunal was inextricably involving third parties to the arbitration agreement, which provided the foundations of the tribunal's jurisdiction. Thus, the tribunal held that it could assume jurisdiction over those third parties that were inextricably involved to the dispute. Here as in the *Sinochem* case, the several intersected contractual arrangements were cross-contract rights and obligations between the several parties. The several parties were co-liaible or co-holders of the same rights. Hence, the several parties from the separate contracts constituted a jurisdictional unit, over which the tribunal could assume jurisdiction in order to resolve the dispute inextricably involving all of them.

In ICC case no 8817 of 1997,¹⁰ the tribunal took a different approach. Here, two Danish companies entered into a distribution agreement with a Spanish company. The contract contained an ICC arbitration clause. The two Danish companies were subsequently bought by X, which terminated the distribution agreement with the Spanish company. The latter commenced ICC arbitration proceedings against X, claiming damages for unjustified termination of contract. In addition, the Spanish company claimed from X certain sums allegedly owed to the claimant by a US subsidiary company of X, XX. The Spanish company alleged that although XX was

¹⁰ (2000) 25 *YBCA* 355.

not a party to the distribution agreement, and, therefore, to the arbitration agreement, the claim for the outstanding sum owed to the claimant by XX was coming out of the distribution agreement. The claimant explained that the policy of X was to lower its credit towards the Spanish company, and to establish a credit of Spanish company vis-à-vis XX.

The arbitrator, however, took a strict contractual approach to the jurisdictional issue at hand and applied principles of the ‘group of companies’ doctrine. In particular, the tribunal examined whether XX was a party to the distribution and, thus, to the arbitration agreement by reference *to the intention of the parties*:

“The sole arbitrator notes that the effect of an international arbitration agreement may extend to other legal entities belonging to the same economic group even if they have not signed the agreement at issue. This possibility exists where the interests of the various companies of the group are closely linked and these companies intend to act jointly. Further, the arbitration agreement must *show the intention of the parties to apply it to all companies of the group, which participate in the execution of the contract*. X did not object to the application of the arbitration agreement signed by other legal entities. However, *we cannot infer from the fact that XX was a customer of [the Spanish company] that it was also a party to the execution of the exclusive distributorship contract which contains the arbitration agreement.*”¹¹
(emphasis added)

Therefore the arbitrator refused to assume jurisdiction over XX. It is questionable the tribunal took the right approach. Instead, it should have looked, at least *prima facie*, into whether the contractual arrangements between the several parties had established a scheme through which X and XX, were co-liaible vis-à-vis the claimant. Due to the specific contractual arrangements between the several parties the claimant had a claim against a third party (XX) arising out of the distribution agreement, containing the arbitration agreement. Thus, the tribunal should have focused on whether this claim was an integral part of the pending dispute, rather than whether XX, in accordance with the intention of the parties, was to be a party to the arbitration agreement. If the dispute between the claimant and the respondent had significant implications for the third party, subsidiary of the respondent, the tribunal

¹¹ *Ibid*, para 44.

should have assumed jurisdiction over the third party in order to be able to resolve the pending dispute effectively.

In ICC 5103 of 1988,¹² the tribunal examined both the potential liability of the several claimants and respondents, and the intentions of the parties in order to determine whether it had jurisdiction over third parties.

On the one hand, the tribunal found that the pending dispute was inextricably related to all the several claimants and the several respondents, and, therefore, genuine and third parties were, at least potentially, jointly and severally liable vis-à-vis the other party:

“...the reliability of international commercial relations demands that this economic reality be taken into account and that all the companies in the group be held jointly and severally liable for the debts from which they have directly or indirectly profited”

On the other hand, however, the tribunal took a contractual approach reference to the ‘group of companies’ doctrine, noting that:

“[all] claimants appear to have been at the time of the conclusion, execution, non-execution and re-negotiation of their contractual links with the [defendants], *genuine partners to all these contracts, by the common will of all the parties to the proceedings*”.(emphasis added)

Based on the above, the tribunal assumed jurisdiction over all the several claimants and respondents, although not all them were parties to the arbitration agreement.

10.2.2 Second: co-liability resulting from the applicable substantive law

Two or more persons can be co-labile or co-holders of rights and obligations by virtue of express legal provisions rather than several interrelated contracts. For example, national laws generally provide that partners in the same legal entity will be co-labile on contracts entered into by the firm;¹³ or that the maker, the acceptor or

¹² 2 (1991) 2 ICC Bull., p.20.

¹³ See Chapter 2.1 above for more details. For example, in the US, section 15 of the Uniform Partnership Act provides that partners are liable jointly and severally for tort or breach of trust, but jointly on partnership contracts; see also *Bullis v Bear, Stearns & Co Inc*, 553 N.W.2d 599 (Iowa 1996).

indorser of the same negotiable instrument will be co-liaible vis-à-vis the holder of the instrument.¹⁴

As was explained in detail in Chapter 2, co-liability is the main characteristic of the false third parties of the first group. The rule for the several parties belonging to the second group is that they are contractually interrelated but not co-liaible. It was demonstrated, for example, that in the context of string construction contracts, a contractor and a subcontractor will not be co-liaible vis-à-vis an employer. Equally, an employer and a contractor will not be co-liaible vis-à-vis a subcontractor. The same applies to web-type construction contracts: an architect and a contractor will usually be liable in the alternative, rather than co-liaible vis-à-vis an employer. Similarly a guarantor and a debtor will not usually be co-liaible vis-à-vis a creditor. Finally, the principle of separate legal liability is the prevailing rule in the context of group of companies, so that liability from a contract concluded by one company will not be shared with other companies in the same group.

However, exceptionally, even the above parties might be co-liaible, by reference to some national laws. For example, French law¹⁵ and the law of some countries¹⁶ influenced by French law provide that, under certain conditions, a sub-contractor may have a direct action not only against a contractor but also against an employer. The same is argued in Swiss law, although not expressly provided by law.¹⁷ In such a case, employer and contractor would be co-liaible vis-à-vis the sub-contractor by reference to the relevant provisions of the applicable national law. Therefore, the employer

In England see the Partnership Act 1890 s 9; The liability of the partners of a firm on contracts entered into by the firm is joint, not joint and several *cf* also Halsbury's, *Laws of England*, (Lexis Nexis Butterworths 2007), para 1083.

¹⁴ E.g. promissory notes, bills of exchange, bonds etc.

In the US, see section 3-118(e) of the Uniform Commercial Code that provides that "unless the instrument otherwise specifies" two or more persons who sign commercial paper as maker, acceptor or drawer or indorser and as part of the same transaction are jointly and severally liable.

In England, the makers of a promissory note may be liable on it either jointly, or jointly and severally, according to the tenor of the note; but the acceptors of a bill of exchange can only be liable jointly: see the Bills of Exchange Act 1882 ss 6(2), 85; *cf* Halsbury's, *ibid*, para 327.

¹⁵ Law No. 75-1334 of December 31, 1975. See further on this, C. Seppala, "French Law on Subcontracting" [1991] *ICLR*, p. 78.

¹⁶ See for example, Algerian Code art. 565, Egyptian Code art.662, Libyan Code art. 661.

¹⁷ See F. Chaix and S. Marchand, "The right of Recourse of an Employer against a Subcontractor", (1998) 15 *ICLR*, p. 21: they argue that the Code of Obligations art. 339(3) ("if the agent has assigned the obligation to a third person (...) the Principal may bring any claims which he has against his agent directly against the third person") regulating the relationships between agent-principal and the third party should be applied by analogy to the contractors for work and materials. Swiss law, however, expressly provides for a direct action of the owner against the subtenant art. Swiss Code of Obligations 262 (3), *cf* also Swiss Supreme Court ATF 120 II 112).

would be inextricably involved in the dispute between the contractor and the subcontractor, which in turn means that employer and contractor would constitute a necessary unit in jurisdictional terms. Even if there is an arbitration agreement between the contractor and the subcontractor, the tribunal should in this case be able to assume jurisdiction over both the contractor and the employer in order to dispose of the claim of the sub-contractor.

International tribunals have assumed jurisdiction over parties not bound by an arbitration agreement on the basis of common rights or co-liability between a third and a genuine party, provided directly by the applicable substantive law.

The most characteristic example is the preliminary ICC award in *Westland Helicopters*.¹⁸ Westland, a UK company, entered into a 'Shareholders Agreement' with the Arab Organisation for Industrialisation (AOI) comprised by four Arab States. The shareholders agreement provided for a 'joint stock company' (The Arab British Helicopters Company - ABH). The agreement contained an ICC arbitration clause. Westland commenced ICC proceedings against the four Arab States and the AOI. The four Arab States contested the jurisdiction of the tribunal on the grounds that none of them was a party to the arbitration agreement. The tribunal held that it had jurisdiction not only over the AOI but also over its members, based on principles of general partnership:

"A partner is bound by the arbitration clause entered into by a general partnership (*Société en nom collectif*) of which he is a partner, and the co-contracting party may rely upon the arbitration clause if he brings his action against the partner instead of bringing it against the partnership"¹⁹

The tribunal put emphasis on the common obligations arising out of the partnership between the several respondents, provided by the applicable substantive law:

"The question whether the four States are bound by the arbitration clause concluded by the AOI in its own name (Shareholders Agreement contracted with Westland, clause 12.1) is exactly the same as the substantive law question whether the four States are bound in general by the obligations contracted by the AOI. If the obligations under substantive law flowing from the Shareholders Agreement are obligations not only of the AOI, but also of the

¹⁸ Preliminary award in ICC case no 3879, (1986) 11 *YBCA* 127.

¹⁹ *Ibid*, para 5.

four States, if the *locus standi* to conduct the defence in relation to those obligations can be attributed not only to the AOI, but also to the four States, then the latter are therefore bound by the arbitration clause, just as they might, had they been summoned before an ordinary Court, have availed themselves of this clause as a ground in their defence.”²⁰

In effect, the tribunal noted that an arbitration agreement is not the sole factor to be taken into account by a tribunal, when determining its tribunal. Attention should also be focused on the nexus of *the substantive contractual commitments of all the parties involved in the pending dispute*, as this nexus is determined by reference to the applicable substantive law:

“The mandatory force of the arbitration clause cannot be dissociated from that of the substantive contractual commitments; the reply to the question as to whether the four States are bound by the acts of the AOI must always be the same, whether the procedural aspect of the arbitration clause is involved or that of the substantive law concerning the financial obligations of the four States.”²¹

The award was set aside by the Swiss Federal Court,²² which took the view that AOI was a public international law entity and, therefore, Swiss principles of general partnership regarding private law entities could not apply to the public law Organisation. In effect, the disagreement between the Swiss Federal Court and the arbitral tribunal was on which law was applicable to the shareholders agreement. The Swiss Federal Court held that international law should be applicable, while the tribunal held that private law principles would apply to the dispute, even though the context arose in the context of public international law. However, there is nothing to indicate that the Swiss Federal Court would not have accepted that the tribunal would have had jurisdiction over the third parties, should AOI and the Arabian States were private law entities, in which case Swiss principles of general partnership would apply.

²⁰ *Ibid* para 7.

²¹ *Idem*.

²² (1989) *Rev. Arb.* p. 525; (1991) 16 *Y.B. Com. Arb.* p. 180.

In ICC case no 9762 of 2001,²³ a contractor commenced arbitration against, among others, the Ministry of Agriculture and Food of state Z that had signed an agreement contained the arbitration agreement, and State Z that was not a party to that arbitration agreement. The tribunal assumed jurisdiction over both respondents, making reference to the fact that both respondents were responsible and liable vis-à-vis the claimant. The tribunal noted that:

“The right of a claimant to act against all possible responsible subjects cannot be denied.”²⁴

and that

“no distinction can be made between the liability of first respondent [the Ministry] and third respondent [State Z] (if any).”²⁵

As far as arbitration rules are concerned, only Vienna Arbitration Rules of the Austrian Federal Economic Chamber²⁶ make express reference to the substantive law applicable to the merits as a factor that the tribunal should take into account in asserting jurisdiction over parties not bound by the arbitration agreement as an ordinary contract. More specifically, Vienna Rules Art 10(1)(a) reads:

“Multiparty Proceedings

²³ (2004) 29 *Y.B. Com. Arb.*, p. 26.

²⁴ *Ibid*, para 55.

²⁵ *Ibid*, para 58. It should be noted, however, that it is not clear whether the shared liability of the Ministry and the State, was the main basis for the tribunal to assume jurisdiction over the latter. At some point the tribunal seems to take a traditional contractual approach to the issue of the jurisdiction, implying that the Ministry was acting also an agent, on behalf of the State, so that the latter was bound by the arbitration agreement, as a contract, on the basis of representation. The tribunal mentioned that:

“The binding effect of the arbitration agreement against parties who did not sign it is a question widely discussed both in doctrine and in jurisprudence. It is generally accepted that if a third party is bound by the same obligations stipulated by a party to a contract and this contract contains an arbitration clause or, in relation to it, an arbitration agreement exists, such a third party is also bound by the arbitration clause, or arbitration agreement, even if it did not sign it. In other words, the mandatory force of the arbitration clause (or arbitration agreement) cannot be dissociated from that of the substantive contractual commitments. This may be the case of companies belonging to the same ‘group of companies’, whenever there is a sufficient evidence of the global liability of the ‘group’. This may be the case of an individual partner being bound by an arbitration clause signed by a general partnership. This may also be the case of States when engaging in transactions of an economic nature through one of their administrative bodies, or even through a separate legal entity provided, in this last case, that the State has full control over it and is bound by the acts of it” *ibid*, para 49- 55.

²⁶ With effect from 1 January 2001.

1. A claim against two or more Defendants shall be admissible only if the Centre has jurisdiction for all the Defendants and in case of proceedings before an arbitral tribunal if all Claimants have nominated the same arbitrator, and:

a. If the applicable law positively provides that the claim is to be directed against several persons”

Vienna Rules art. 10(1)(b)-(e) list four more cases where a tribunal may proceed with multiparty proceedings, all of which are based on the express or implied consent for multiparty arbitration of all the relevant parties. For example, in accordance with art. 10(1)(b), multiparty proceedings may be held “if all parties are bound by the same arbitration agreement”; or in accordance with art. 10(1)(c) “if the admissibility of multiparty proceedings has been agreed upon”. By contrast, under art.10(1)(a), multiparty proceedings are based on *the fact that the law applicable to the merits expressly implicates several parties to the dispute*, rather than on unanimous consent of all parties to an arbitration agreement. Accordingly, by virtue of Vienna Rules art.10(1)(a), the tribunal may assert jurisdiction over all persons co-liable even if some of them are not bound by the arbitration agreement.

Art. 10(1)(a) will only apply whenever several co-respondents are co-liable (“...the claim is to be directed against several persons”). It does not seem to cover the case where several co-claimants are co-holders of the same rights against the same respondent or against several co-respondents. Nonetheless, it takes the right approach to the issue of multiparty proceedings: on the one hand, it provides for multiparty proceedings on the basis of multiparty consent; on the other hand, it recognises the *jurisdictional dimension of arbitral tribunals* and puts emphasis on the dispute and the law applicable to the merits.

It is suggested that the adoption of analogous provisions by other popular arbitration rules would offer an effective solution to the complicated issue of multiparty proceedings in arbitration.

In the light of the above, the parties’ choice on the substantive applicable law becomes crucial not only with regard to the determination of their contractual rights and duties, but also *with regard to the jurisdiction of the tribunal*.

10.2.3 No lower threshold than co-liability or community of rights and duties warrants extra-contractual jurisdiction and third-party mechanisms

As showed above the threshold for a tribunal to assume extra-contractual jurisdiction is community of rights or co-liability between a party to an arbitration agreement and a third party thereto. Only then, third and genuine party will constitute an inseparable unit in terms of jurisdiction. Therefore, community of rights and co-liability between a genuine and a third party constitutes a limitation for the tribunal to assume extra-contractual jurisdiction through the application of third-party mechanisms.

Accordingly, other sort of considerations, such as a general policy to avoid multiplicity of proceedings over the same factual and legal issues, will not warrant extra-contractual jurisdiction. As was shown in Chapter 8, procedural systems in the context of litigation provide for third-party mechanisms when several actions, pending before several courts between several parties, involve *a common question of law or fact*.²⁷ However, as was explained, in such a case third-party mechanisms of permissive character will usually be provided. Third-party mechanisms may apply for reasons of procedural convenience, rather than because the several actions cannot be tried separately. The several parties in this case will not constitute a necessary jurisdictional unit, and therefore it will not be mandatory for all them to be brought before the same forum.

Similarly, in the context of arbitration, whenever several actions pending before different tribunal between several parties involve a common question of law or facts, it will not be necessary for all of the parties to be brought before the same tribunal. The disputes pending before the several tribunals will be tried and determined separately. Therefore, there will be no sufficient ground for one tribunal to assume extra-contractual jurisdiction over third parties. The several bilateral proceedings should proceed in accordance with the several bilateral arbitration agreements.

In *Credit Suisse First Boston (Europe) Ltd v MLC (Bermuda) Ltd*,²⁸ the defendant, MLC, concluded two bond purchase agreements with Credit Swiss Europe. The purchase agreements provided for exclusive jurisdiction of English courts. The defendant had a separate customer agreement with a US affiliate of Credit Swiss

²⁷ See for example Federal Rules of Civil Procedure Rule 42 (consolidation), and in more detail, Chapter 8.

²⁸ [1999] 1 Lloyd's Rep. 767.

Europe, Credit Swiss US, which agreement contained no jurisdiction clause. A dispute arose out of the purchase agreement and Credit Swiss Europe commenced proceedings against MLC before the English courts in accordance with the exclusive jurisdiction agreement. At the same time MLC commenced legal proceedings before the US courts against both Credit Swiss US and Credit Swiss Europe.

Credit Swiss Europe applied to the English courts for an anti-suit injunction to restrain MLC from going on with the US proceedings on the basis of the English jurisdiction clause contained in the purchase agreement. In addition, Credit Swiss Europe asked the English courts to join Credit Swiss US as a party to the action against MLC. The latter applied for a stay of the English proceedings in favour of the New York proceedings.

The English court seised of the dispute had to examine, among other issues, whether the jurisdiction of the English courts, stemming from a jurisdiction clause in the purchase agreement between Credit Swiss Europe and MLC, should be asserted over Credit Swiss US too.

Rix J, held that, in this case, English jurisdiction could not be exercised over the third party, Credit Swiss US, because the claims between Credit Swiss US and MLC were *separate* from the claims between Credit Swiss Europe and MLC. Credit Swiss Europe and Credit Swiss US were not co-liable in the dispute before the English courts. Indeed, there was an express provision in the Purchase agreement that:

“[Credit Swiss US] shall otherwise have no liability in respect of this Agreement or such Transaction except for its gross negligence or wilful misconduct, or its failure to comply with applicable U.S. securities laws and regulations, in performing its duties as facilitating agent hereunder.”

Therefore Credit Swiss Europe and Credit Swiss US did not constitute a necessary unit in terms of jurisdiction. Here, there was no reason supporting the extra-contractual jurisdiction of the English courts over the third party, Credit Swiss US. The English proceedings between the two parties to the jurisdiction agreement should proceed in parallel to the US proceedings between Credit Swiss US and MLC, even though it was high likely that the two proceedings would turn to the same legal and factual issues.

Here, the English courts rightly refused to apply extra-contractual jurisdiction. There was not sufficient ground not to let the sets of proceedings (one in New York

and another in London) to go ahead separately, in accordance with the jurisdictional arrangements of the parties. The association of the several parties in terms of substantive rights and liability was not so strong as to warrant multiparty proceedings. Therefore, the procedural arrangements made by the parties in their different contracts, leaving room for different set of proceedings, should be upheld:

“On the other hand, where different agreements are entered into for different aspects of an overall relationship, and those different agreements contain different terms as to jurisdiction, it would seem to be applying too broad and indiscriminate a brush simply to ignore the parties’ careful selection of palette [...] [the dispute resolution clause] is part of a bilateral agreement between a seller and a buyer, and the disputes to which such an agreement may give rise are *prima facie* bilateral disputes. Indeed, it is I would have thought axiomatic that, at any rate in the absence of plain language to the contrary, a contract seeks neither to benefit nor to prejudice non-parties: even where such plain language is used, it is black-letter law that the non-party can himself neither take the benefit nor suffer the burden of the contract.”²⁹

In view of the specific facts, Credit Swiss US and Credit Swiss Europe did not constitute a necessary unit in terms of jurisdiction. The unwelcome risk of multiplicity of proceedings over the same factual and legal issues could not alone overturn the procedural arrangements of the several parties:

“Claims against Credit Swiss US [...] would not be enjoined because however undesirable it was in principle to have parallel litigation in two jurisdictions, it seemed that the duplication of litigation did not in itself make it in the interests of justice to enjoin the New York proceedings in so far as the claims against Credit Swiss US [...] were concerned; the claims against CS US were made either under Federal statute law or New York common law or under the Customer Agreement; to the extent that such claims were free-standing of any contract between MLC and CS US no jurisdiction clause applied”.³⁰

²⁹ *Ibid.*, at 777.

³⁰ *Ibid.*, at 769.

Similar approach was taken by Lord Denning in the well known ADGAS case,³¹ regarding the construction of huge tanks for the purposes of liquefying gas from oil. When cracks appeared in one of the tanks, the employers claimed against the main contractors, which in turn claimed against the sub-contractors. The main contract provided for arbitration in London. The contractor concluded two subcontracts, one for the installation and erection of the tanks, which provided for arbitration in London, and another for the supply of the materials, which provided for arbitration in Japan. Lord Denning examined, *inter alia*, whether two separate sets of arbitration proceedings should be allowed to go on or the two proceedings should be consolidated.

It was held that the mere fact that the two parallel arbitration proceedings could turn to the same legal and factual issues would not warrant multiparty proceedings. The risk of inconsistent findings, however undesirable it was, could not support the decision of the court to thwart the scheme of several bilateral procedural agreements of the parties.

As is well known, Lord Denning M.R, came up with the solution of appointing the same arbitrator for the two separate proceedings. However, he felt that he could not order all the parties in the dispute to appear before a single tribunal despite the fact that:

“There is a danger in having two separate arbitrations in a case like this. You might get inconsistent findings if there were two separate arbitrators.”³²

Also that:

“It is most undesirable that there should be inconsistent findings by two separate arbitrators on virtually the self-same question, such as causation.”³³

Only when the parties have expressly provided so in their dispute resolution agreements, can the risk of inconsistent findings on the same factual and legal issues in different proceedings provide the basis for multiparty proceedings. Indeed, there are cases where the parties expressly provide for multiparty proceedings on the condition that disputes between different parties will raise the same and legal issues.

³¹ *Abu Dhabi Gas Liquefaction Co. Ltd. v Eastern Bechtel Corporation and Chiyoda Chemical Engineering & Construction Co. Ltd. v Ishikawajima-Harima Heavy Industries Co. Ltd.* [1982] 2 Lloyd's Rep. 425 (CA).

³² At 427 per.

³³ *Idem*.

For example, in *City & General (Holborn) Limited v AYH Plc*,³⁴ a contractor entered into a contract with an employer and agreed to carry out works of refurbishment and rebuilding at a construction project. The contract incorporated the JCT Standard Form of Building Contract 1998 Edition with amendments. The employer entered into a contract (deed of appointment) with a project manager who agreed to administer and supervise the construction works. The two agreements, contractor-employer and employer-project manager, were linked in terms of jurisdiction and arbitration proceedings. In particular, clause 17 of the deed of appointment between the employer and the project manager provided that:

“17.2. If the dispute to be referred to arbitration under this Deed raises issues which are substantially the same as or are connected with issues raised in related disputes between either party to this Deed and any other person, and if the related dispute has already been referred to determination to an Arbitrator, the parties to this Deed agree that:

17.2.1 The dispute under this Deed shall be referred to the Arbitrator appointed to determine the related dispute, [...] and

17.2.2 The Arbitrator shall have power to make such directions and all necessary Awards in the same way as if the procedure of the High Court as to joining 1 or more Defendants or co-joining Defendants or 3rd parties was available to the parties and to him.”

Here, the parties had made express arrangements for a single forum and a single set of arbitration proceedings, in case the dispute arising out of one contract raised issues that were “substantially the same as or are connected with issues raised in related disputes”. In other words, the parties here had provided for different but interlinked dispute resolution procedures. They had, in fact, established a scheme where the separate contracts were *convergent in jurisdictional terms*. In such a case, the lower threshold of “common questions of law or fact” between the two disputes may warrant multiparty arbitration proceedings.

The English High Court even noted that:

³⁴ [2005] EWHC 2494 (TCC).

“It is not necessary [...] for every single issue in dispute B to be substantially the same or connected with an issue in dispute A.”³⁵

A mere convergence of the legal or factual issues in both disputes would be enough for a single tribunal to assume jurisdiction over all the several parties. In this context, the avoidance of multiplicity of proceedings would certainly be relevant:

“It is to avoid multiplicity of proceedings, which (as is well known) generate excessive costs and carry the risk of inconsistent findings. Bearing in mind the commercial objective, I do not think that the threshold of clause 17.2 should be set too high. It is not necessary that the majority of issues in dispute B should be the same as or connected with issues in dispute A. In my judgment, it is sufficient if a material portion of the issues in dispute B have that characteristic. Once a material portion of the issues in dispute B are the same as, or are connected with, issues in dispute A, then it makes obvious commercial sense for both disputes to be dealt with by the same tribunal.”³⁶

The same approach was taken in *Trafalgar House Construction (Regions) Limited v Railtrack plc*.³⁷ Here, R employed T as the main contractor for the construction of certain works whereas T entered into two nominated subcontracts with TA and BW. Both the main contract and the two subcontracts contained a dispute resolution provision quite similar to the clause 17.2 in the *City & General (Holborn)* case. Different disputes arose between the several parties to the above contracts. Lloyd J held that the dispute in the subcontracts should:³⁸

“Be referred to the arbitrator appointed under the main contract provided of course that the sub-contract dispute raises issues which *are substantially the same as or connected with the main contract dispute* and provided that this is done before an arbitrator has been agreed or appointed to determine the sub-contract dispute.”

Otherwise:

³⁵ *Ibid.*, para 43.

³⁶ *Ibid.*, para 47.

³⁷ [1995] 75 BLR 55.

³⁸ *Ibid.*, para 86.

“Multiplicity of proceedings is likely to lead to different tribunals reaching different conclusions on the same facts and, thus, substantial injustice may result”

In *Lafarge Redland Aggregates Ltd. v Shephard Hill Civil Engineering Ltd.*³⁹, the parties had expressly provided for joint proceedings on the condition that the dispute in the main contract “touched or concerned the subcontract works”. More specifically, the subcontract was in a F.C.E.C. Standard Form of Subcontract, which under clause 18(2) provided that:

“If any dispute arises in connection with the main contract and the contractor is of the opinion that such dispute touches or concerns the subcontract works, then, provided that an arbitrator has not already been agreed or appointed in pursuance of the preceding sub-clause, the contractor may by notice in writing to the subcontractor require that any such dispute under this subcontract shall be dealt with jointly with the dispute under the main contract in accordance with the provisions of clause 66 thereof. In connection with such joint dispute the subcontractor shall be bound in like manner as the contractor by any decision of the engineer or any award by an arbitrator.”

The majority of the House of Lords⁴⁰ agreed with the view taken by the Court of Appeal that such a dispute resolution clause would allow for a tripartite arbitration between employer, contractor and subcontractor.⁴¹ Here, the parties in their contracts had expressly provided for certain dispute resolution mechanisms, which, although formally separate, were to become interlinked if the dispute in the main contract “touched or concerned the subcontract works”.

Whenever this condition was qualified, in the opinion of the contractor, the disputes would be tried jointly. Thus, because of the specific dispute resolution arrangements between the several parties, multiparty proceedings were possible whenever “the disputes in the main contract touch[ed] or concern[ed] the subcontract works”

³⁹ [2000] HL.

⁴⁰ Two members of the House of Lords disagreed.

⁴¹ Although at the particular case such a tripartite arbitration was held not be possible because the contractor, had not initiated the procedure against the main employer within a reasonable time, as he was obliged under the main contract.

In more general terms, the parties in the above cases, had expressly conditioned multiparty proceedings upon the threshold of “common questions of law or fact” or “avoidance of multiplicity of proceedings” or “disputes in one contract that touch upon the subject matter of the other contract”. In all these cases the threshold is lower than “co-liability or community of rights and obligations”. However, the scheme of “jurisdictional convergence” of the several contracts established by the parties allowed a single tribunal to assume jurisdiction over all the several parties, despite the fact that the parties were not co-labile.

Conversely, when the dispute resolution clauses in the several contracts are not interlinked or contain no cross-references, the threshold for multiparty proceedings between all the several parties necessarily involved in the pending dispute will be the higher threshold of co- liability between the several parties. Thus, for example, in the *City & General (Holborn)*,⁴² had the parties not provided for the specific clause 17(2), the constitution of a single forum for the whole dispute would not have been possible. As was explained in detail in Chapter 2, contractor and project manager are normally liable *in the alternative* rather than *co-labile* vis-à-vis the employer. Thus, the presence of a project manager in the proceedings between an employer and a contractor will not be warranted.

⁴² *Supra* n. 70.

Chapter 11: Final remarks on the jurisdictional approach	201
11.1 Applying third-party mechanisms in arbitration: The third party will remain a party not bound by the arbitration agreement	201
11.2 Examining the dispute at the stage of determination of the jurisdiction does not lead to prejudgment of the merits of the dispute	203
11.3 Practical relevance of the jurisdictional approach	205
11.3.1 The law applicable to the validity and the interpretation of the arbitration agreement	205
11.3.2 Jurisdiction in accordance with the jurisdictional approach is determined on a basis closer to commercial reality	210

CHAPTER 11: FINAL REMARKS ON THE JURISDICTIONAL APPROACH

This chapter concludes the discussion on the jurisdictional approach looking into three issues. Firstly, how a tribunal should apply third-party mechanisms to arbitration proceedings (Section 11.1). Second, whether the examination of the dispute for jurisdictional purposes might lead to the merits of the case being prejudged (Section 11.2). Third, what is the practical relevance of the jurisdictional approach and which are its practical advantages over the contractual approach (Section 11.3).

11.1 APPLYING THIRD-PARTY MECHANISMS IN ARBITRATION: THE THIRD PARTY WILL REMAIN A PARTY NOT BOUND BY THE ARBITRATION AGREEMENT

The tribunal, under the jurisdictional approach, may assume jurisdiction over a third party whenever the latter is strongly associated with a genuine party in terms of substantive rights, interests and liability. In such a case, jurisdiction of the tribunal will not be based on contractual grounds: the third party will remain a third party as far as the arbitration agreement is concerned. In other words, extra-contractual jurisdiction of a tribunal over the third party will be *circumstantial*. The tribunal will assume jurisdiction over a third party, because the latter is an integral part of the pending dispute, rather than because the third party has *a contractual right in its own* to participate in the proceedings. It is not suggested here that the several interrelated contracts between the several parties constitute a contractual unit in legal or and even economic terms. Thus, the several parties will constitute a jurisdictional not a

contractual unit. This constitutes a fundamental difference between the jurisdictional approach suggested here and the prevailing contractual approach.¹

This in practice means that *the arbitration agreement cannot actually be enforced by or against the third party*. Therefore, a third party can only be *joined* to the proceedings as co-claimant or co-respondent to the genuine parties; or *intervene* thereto; or be *interpleaded* by one of the original parties to the proceedings. Accordingly, if one of the genuine parties to a bilateral arbitration agreement brings a claim against a third party alone rather than join a third party in a claim against the other genuine party, the tribunal should reject this claim as inadmissible to the proceedings. The same should apply if the third party alone rather than as a co-claimant to a genuine party to an arbitration agreement, brings a claim against the other genuine party.

It follows, for example, that a parent company will not have a right to file claims alone against the co-contractor of its subsidiary in order to recover damages occurred to the subsidiary, even if the parent company was found by the tribunal strongly associated with the subsidiary in terms of substantive rights. Since the parent company is not contractually bound by an arbitration agreement, it will not have the right to enforce it. The parent company will need to bring the claim as a co-claimant alongside its subsidiary, and request the tribunal to assume jurisdiction over it on the ground that parent and subsidiary constitute a necessary unit in terms of jurisdiction on the basis of the specific factual circumstances.

For example, in *General Electric Company v Deutz AG*,² Deutz guaranteed the performance assumed by its subsidiary in a contract with General Electric. When General Electric filed a claim before the US courts against Deutz, the latter challenged the jurisdiction of the US courts on the basis of an arbitration agreement

¹ Cf in France contractual approach suggests that arbitration agreements should extend as a contractual terms to all the interrelated contracts ("*ensemble contractuel*") with the same economic and operational purpose, irrespective of whether the arbitration agreement has actually been inserted into one or some of the several contracts. See F-X Train, *Les contrats liés devant l'arbitre du commerce international*, (L.G.D.J 2003), para 42 *et seq*, for the several variations of the theory of interrelated contracts having close economic links ("*liés économiques étroit*"), or having the same economic operation aiming at the same object "*une opération économique unique qui concourt au même objet*". See also P. Leboulanger, "Multi-Contract Arbitration" 13 (4) *J Int'l Arb*, (1996), p. 43; P. Delebecque, "La notion de groupe de contrats: quels critères?", 4 *Cah. Dr. Entr.* (1989) p.25; and P. Fouchard, E. Galliard and B. Goldman, *On International Commercial Arbitration*, E. Gaillard and J. Savage (eds.) (Kluwer Law International 1999), para., par 518 *et seq.*; and B Hanotiau, *Complex Arbitrations, Multiparty, Multi-contract, Multi-issue and Class Actions* (Kluwer Law International 2005) p. 101 *et seq.*

² 270 F.3d 144 (3rd Cir. 2001).

included in the main contract between its subsidiary and General Electric. At the same time Deutz commenced ICC arbitration proceedings in London against General Electric alone. The US courts rejected the argument of Deutz and assumed jurisdiction over it. In the same vein the tribunal rejected the right of Deutz to enforce the arbitration agreement.

Both the US courts and the tribunal took the right approach. Deutz, as a parent company or a guarantor, was never a party to the arbitration agreement concluded by its subsidiary. Therefore, it had no right to enforce the arbitration agreement. The tribunal could have assumed jurisdiction over the parent company, only if the subsidiary, which was the genuine party to the arbitration agreement, had joined the parent company as co-claimant against General Electric. It would then have been for the tribunal to decide whether, in the light of the factual circumstances of the particular case, parent company and subsidiary were strongly associated in substantive terms, and, therefore, they should be viewed as a jurisdictional unit.

11.2 EXAMINING THE DISPUTE AT THE STAGE OF DETERMINATION OF THE JURISDICTION DOES NOT LEAD TO PREJUDGMENT OF THE MERITS OF THE DISPUTE

As was explained already, the jurisdictional approach suggests that a tribunal in order to determine its jurisdiction should examine both the arbitration agreement and the dispute at hand. However, this does not necessarily mean that the tribunal will have to determine the merits of the case before determining its jurisdiction. The ordinary course of action in the arbitral proceedings will not be reversed. Determination of the jurisdiction will not pre-empt the final decision on the rights, duties or liability of the parties. This is evidenced by the following.

As is suggested here, co-liability or community of rights and obligations between a third and a genuine party is necessary for the tribunal to assume jurisdiction over the third party. Accordingly, the tribunal in order to determine its jurisdiction will have to look into the substantive links between the several parties involved in the dispute. However, the standards of proof of co-liability required for the determination of the jurisdiction are much lower than the standards required for the final determination of the dispute. In the latter case, the proof-threshold will be that of *reasonable degree of*

probability or even higher,³ whereas in the former case the proof-threshold will be that of *mere possibility*. A tribunal, in order to assume extra-contractual jurisdiction over a third party, needs to be satisfied *prima facie* that the several parties are *possibly* co-liaible. Therefore, a tribunal will not have to go beyond a *prima facie examination of the merits*: parties that are *potentially* co-liaible or co-holders of rights and duties may constitute a jurisdictional unit.

In *Sinochem International Oil (London) Co Ltd v Mobil Sales and Supply Corp*, for example, the English courts assumed extra-contractual jurisdiction over third parties, on the basis that the third parties seemed to be closely interwoven with the dispute at hand. The court was satisfied *prima facie* that Mobilil England had a debt to Sinochem London and that this debt could *in principle* be set off against the debt *prima facie* owed by Mobil Oil Hong Kong against Sinochem Beijing. The court did not decide whether either debt was finally valid or whether the debts were *actually* set off. This decision was left for the stage of the merits. The question at the stage where jurisdiction was determined was whether the English courts could have jurisdiction over the claim against Sinochem Beijing, as a third party to a jurisdiction agreement. For that purpose it was enough for the court to examine that the debt of Mobil England to Sinochem London *could be* set off against the debt of Sinochem Beijing to Mobil Oil Hong Kong.

Even under the contractual approach, where the examination will focus on whether an arbitration agreement as an ordinary contract is valid, arbitrators will have to touch upon issues relating to the substance of the dispute, in order to determine their jurisdiction. Very often, the question of which persons are bound by an arbitration agreement necessarily involves the examination of issues closely related to the main contract and, therefore, to the dispute at hand. For example, the tribunal, at the stage of jurisdiction, will have to examine whether the substantive contract including the arbitration agreement was ever concluded; or whether the substantive contract, and, therefore, the arbitration agreement, was validly assigned to a third party;⁴ or whether a person was acting as an agent of another person when concluding the substantive contract and, therefore, the arbitration agreement.⁵

³ A. Redfern, "The Standards and Burden of Proof in International Arbitration", 3 (1994) 10 *Arb. Int'l*, p. 317.

⁴ SCC case 17 of 1997, in SCC Arbitral Awards 1999-2003 (edited by S. Jarvin and A. Magnusson), p.1.

⁵ ICC case 5721 of 1990, (1990) 117 *JDI (Chunet)*, p. 1019.

The same applies to litigation. National courts in order to assume jurisdiction over a claimant and a defendant, they have to examine whether a *prima facie* contractual relationship between these two parties exists. Similarly, whenever a claim is brought by several claimants or against several defendants, courts will have to examine whether the several co-claimants or co-defendants are *prima facie* joint co-contractors, in order to decide whether all parties should be joined at the same claim.⁶ A *prima facie* determination of co-liability will suffice for the parties to be joined.⁷ In all the above cases, the standards of proof required for the courts to determine their jurisdiction are, thus, lower than the standards required for the final determination of the dispute.⁸

Therefore, the fact that according to the jurisdictional approach the courts or tribunals have to take a *prima facie* look into the merits of a dispute in order to determine their jurisdiction should not create any theoretical or practical difficulties.

11.3 PRACTICAL RELEVANCE OF THE JURISDICTIONAL APPROACH

The suggestion for a jurisdictional approach to the matter of arbitration and third parties has not only theoretical but also practical relevance. In fact, it exhibits two important practical advantages over the contractual approach.

11.3.1 The law applicable to the validity and the interpretation of the arbitration agreement

First, it diminishes the relevance of the discussion on the law applicable to the validity and interpretation of the arbitration agreement, which has often caused conceptual and practical problems. Under the jurisdictional approach, the focus is shifted from the contractual boundaries of an arbitration agreement to the implications that the pending dispute may have for third parties. Therefore, the issue of which law would be applicable to the validity and interpretation of an arbitration agreement becomes less relevant, at least in terms of jurisdiction.

⁶*Fardell Traction Haulage Co Ltd v Basset* (1899) 15 TLR 204, CA; *Norbury Natzio & Co Ltd v Griffiths* [1918] 2 KB 369 (CA): “it is sufficient that the defendant makes out a reasonable and probable case of a joint contract”.

⁷ Halsbury’s, *Laws of England*, (Lexis Nexis Butterworths 2007), para. 108.

⁸ *Hargrave v Fireboard*, 710 F. 2nd 1154 at 1161 (5th Cir. 1983).

More specifically, as was explained in Part II, the discussion in the context of extension doctrines and the “group of companies” doctrine in particular focuses on the boundaries of arbitration agreements as substantive contracts. Consequently, the question of which rules apply to determine the boundaries of the arbitration contract has been at the centre of this discussion. The question becomes even more important given the fact that no national law recognises a “group of companies” doctrine in relation to arbitration agreements in particular. Accordingly, the presumption that a parent company is bound by an arbitration agreement signed by its subsidiary would not be accepted by any national law, as no national law would accept such presumption with regard to any other substantive agreement. Similarly, no national law accepts that consent of a parent company can be deduced more easily with regard to an arbitration agreement than with regard to any other substantive agreement.⁹ Naturally thus, in order to avoid the constraints of national laws, international tribunals have held that the “group of companies” doctrine would apply by reference to ‘usages of international trade’, or ‘transnational substantive rules’ and ‘lex mercatoria’, rather than by reference to national law.¹⁰

⁹ See above Part II.

¹⁰ See for example, the arbitral awards: interim award in ICC case no. 4131 of 1982, *Dow Chemical v Isover-Saint-Gobain*, (1984) Rev. Arb. 137; (1983) 110 Clunet 899, with note Derains: “et en tenant également compte [...] des usages conformes aux besoins du commerce international”; ICC case no. 6000 of 1988, 2 (1991) 2 ICC Bull., p.34: “the usages of the international trade [...] would justify and require the extension to this company, party to a group of companies, of the arbitration clauses included in the contracts executed” by the other companies of the group; the same in partial award ICC case no. 5894 of 1989, 2 (1991) 2 ICC Bull., p.25; in ICC case no 5721 of 1990, (1990) 117 JDI (Clunet), p.1023; ICC case no 4131 of 1982, (1983) 110 JDI (Clunet), p.899, with note Y.Derains; ICC case no 5721 of 1990, (1990) 117 JDI (Clunet), p.1019, with note Y.Derains; the award in *C & M Farming Ltd v Peterson Farms Inc.* (unpublished).

See also the decisions of the French national courts: Paris Cour d’appel in *Dow Chemical v Isover-Saint-Gobain*, Paris Cour d’appel, 21 October 1983, (1984) Rev.Arb., p. 98 with note Chapelle upholding the award by reference to the trade usages and art 13.5 of the previous ICC rules (*cf* ICC rules (1998) art 17: “In all cases the Arbitral Tribunal shall take account of the provision of the contract and the relevant trade usages”; *cf* also French NCCP art. 1496(2): “[The arbitrator] in all cases shall take the usages of the trade into consideration”; Paris Cour d’appel, 21 Oct 1983, (1986) Rev. Arb., p. 98, with note A. Chapelle; Pau Cour d’appel, *Sponsor A.B. v Lestrade*, 26 November 1986, (1988) Rev.Arb., p.153 with note A.Chapelle.

This is the prevailing view in arbitration literature too: J Lew, L. Mistelis and S. Kroell, *Comparative International Commercial Arbitration*, (Kluwer London 2003), para 6-73; Fouchard, Gaillard and Goldman, *On International Commercial Arbitration*, E.Gaillard and J.Savage (eds) (Kluwer 1999), para 443 et seq.; see also Derain and Schauf, “Clauses d Arbitrages et Groupes de Sociétés”, (1985) Rev. Dr. Aff. Int., p. 231; J-F Poudret “L’ extension de la clause d’ arbitrage: approches française et suisse, (1995) 122 JDI (Clunet), p. 923; *cf* S. Jarvin in his note on the ICC case no 4504 of 1985-1986, (1986) JDI (Clunet), p. 1130 and M. Blessing, “The law applicable to the Arbitration Clause and Arbitrability”, van den Berg (ed), ICCA Congress series no.9, p. 174. *Contra* O. Sandrock, “Extending the Scope of Arbitration Agreements to Non-Signatories”, in *Arbitration Agreement – Its Multifold Critical Aspects*; (1999) ASA Special Series No 8, p.167 and O. Sandrock, “Arbitration Agreements and Group of Companies” (1993) 27 International Lawyer, p.

This approach taken by tribunals is questionable. First, it is rather doubtful whether there is actually such an “international trade usage” or a “transnational substantive rule” ready to recognise the “group of companies” doctrine.¹¹ More importantly though, when the parties have expressly subjected their contract to a particular national law, references to “lex mercatoria” or “transnational substantive rules” will in effect negate this choice made by parties themselves. To overcome this, tribunals have held that, by reference to the doctrine of separability and the principle of “autonomy of the arbitration agreement”, different sets of rules should be applicable to the arbitration agreement and the substantive contract.¹² Therefore, according to several arbitral awards, the validity of an arbitration agreement should be determined on the basis of “the common intent of the parties” or “a-national or transnational substantive rules”, despite the express reference of the parties in their contract to the national law of a particular country.

However, national courts have not always been keen to accept the above practice of international tribunals. For example, in the well known *Peterson Farms Inc. v C & M Farming Ltd* case,¹³ the parties in their contract had made express reference to Arkansas law as the law governing their contract. The tribunal applied the “group of companies” doctrine and held that the parent company of the C & M group was bound by the arbitration agreement, concluded by a subsidiary of the same group. The tribunal applied the doctrine by reference to “the common intent of the parties” and the principles of separability and “autonomy of the arbitration agreement.”¹⁴

945, who argues that the contours of *lex mercatoria* are too vague to provide support to the ‘group of companies’ doctrine. Instead, Sadrock argues for the application of national law as determined by the relevant conflict of laws rules.

¹¹ In general, a commercial practice will qualify as a trade usage, only under very strict requirements. These requirements would include a practice adopted by individuals or groups in business and mercantile transactions for a considerable amount of time. It would also require that the persons adopt this practice being aware of the fact that it constitutes the general commercial practice.

¹² See case law and literature as in footnote 81 *supra*.

¹³ *Peterson Farms Inc. v C & M Farming Ltd*, [2004] 1 Lloyd’s Rep. 603, at 612: “The evidence on Arkansas law showed that Arkansas law was the same as English law. English law treated the issue of agency as one subject to the chosen proper law of the Agreement, and that excluded the ‘group of companies’ doctrine”; see also M. Mustill and S. Boyd, *The Law and Practice of Commercial Arbitration in England*, (2nd ed) (London Butterworths 1989), p.149, where they argue that an award based on the ‘group of companies’ theory will not be enforceable in England; on the same issue see also J. Leadley and L. Williams, “Peterson Farms: There Is No Group Of Companies Doctrine In English Law”, 7 (2004) 4, *Int. A.L.R.*, p.112.

¹⁴ Para 86 of the award (unpublished):

“The tribunal does not accept Peterson’s arguments. Under the doctrine of separability, an arbitration agreement is separable and autonomous from the underlying contract in which it appears. The autonomy of arbitration agreements has become a universal principle in the realm

English court rejected that the “group of companies” doctrine could be applicable in this case, and set part of the arbitral award aside, by virtue of EAA s.67. In essence, the court did not accept that the issue of jurisdiction should be determined not by the law expressly agreed on by the parties. The court noted that:

“The autonomy of the arbitration agreement is not in point.”

As indicated, under the jurisdictional approach the dilemma on whether national or a-national rules would apply to the validity and interpretation of the arbitration agreement is irrelevant to the issue of the jurisdiction of a tribunal over third parties. Under the jurisdictional approach, the focus is shifted from the boundaries of an arbitration agreement to the implications that the dispute may have for third parties. The pending dispute rather than the arbitration agreement as a substantive contract is at the heart of the examination: tribunals should examine whether a third party, in the light of the dispute, is strongly associated with one of the genuine parties. Accordingly, this examination will be done by reference to the law applicable to the merits of the dispute. Naturally, thus, if the parties have expressly agreed on that law, the question of whether the dispute has any implications for any third party will have to be determined exactly by the law agreed by the parties.

If the tribunal in *Peterson Farms* had taken the jurisdictional approach suggested here, the question of whether the tribunal had jurisdiction over the parent company of the C & M group, would effectively be a question of *whether the parent company was entitled to claim damages for losses suffered by its subsidiary*. This is a question relevant to the dispute, and, accordingly, it should have been determined by reference to the law applicable to the substance, in this case Arkansas law. In other words, the tribunal should have looked into the Arkansas law, the express choice of the parties, in order to determine whether, in accordance with that law, the damage suffered by a subsidiary may have any implications for the parent company. In other words, the tribunal should have examined whether, in accordance with Arkansas law, the parent company was entitled to pursue damages suffered by its subsidiary. If the answer to

of international commercial arbitration. A corollary to the separability doctrine is that the law applicable to the arbitration agreement may differ from the law applicable both to the substance of the contract underlying the dispute and to the arbitral proceedings themselves. The right of C&M to make claims for the C&M Group is a question of interpretation of the arbitration agreement contained in the Agreement, including the intention of the parties. In the absence of any choice of law made by the parties with regard to the arbitration agreement itself, this tribunal will determine this question in accordance with the common intent of the parties”.

the above question were in the affirmative, the tribunal would have been entitled to assume jurisdiction over the claims of the parent company, despite the fact that the parent company was not a party to the arbitration agreement. It is likely that English courts would have upheld this approach.¹⁵

Furthermore, this approach is consistent with the principle of ‘party autonomy’. The parties by reference to the principle of party autonomy are free to subject their contractual relationship to a specific substantive law. In fact, whenever the parties refer to a substantive law in their contract, they expressly *annex their relationship to this particular law*. This is the law to which the parties entrust the fate of their relationship as a whole. The expectations of the parties are that arbitrators in order to resolve the dispute will seek guidance from this particular law. Accordingly, whenever the parties have made an express reference to a national law, this law should be the primary source that arbitrators should turn to. In such a case, given the indisputable prevalence of party autonomy in arbitration, it seems difficult to reconcile the parties’ express reference to a particular national law with the application of a-national rules by arbitrators.

It is contrary to the expectations of the parties, if arbitrators apply the “group of companies” doctrine by reference to transnational rules, while the parties have expressly agreed to submit their contract to a national law that does not recognise the “group of companies” doctrine. It is reasonable to argue, that whether a third party parent company will have the right to recover damages from a genuine party is an issue that should be determined by reference to the substantive law expressed to which the parties have subjected their relationship, rather than by reference a-national rules which the parties presumably never envisaged.

The contractual approach by reference to the principle of “autonomy of the arbitration agreement” completely separates jurisdiction from the substance of the dispute. According to the contractual approach, on the one hand the dispute is to be resolved in accordance with the rules agreed by the parties, while on the other hand jurisdiction of the tribunal over this dispute is to be determined exclusively by contractual a-national rules. The strict dichotomy between procedure (determination of the jurisdiction of tribunal) and substance (resolution of the dispute) seems

¹⁵ In this case, the court asked from the parties to furnish evidence on whether Arkansas law recognised the doctrine of group of companies. The evidence showed that Arkansas law was adherent to the principle of ‘separate legal entity’ and did not recognise the “group of companies doctrine”.

artificial, incompatible with the expectations of the parties, and certainly parochial.¹⁶ By contrast, the jurisdictional approach *recognises that jurisdiction and substance are interrelated. Jurisdiction cannot be separated from the dispute.* The law applicable to the dispute should be relevant to determine whether the tribunal would assert jurisdiction over a third party, which brings the issue closer to the expectations of the parties.

11.3.2 Jurisdiction in accordance with the jurisdictional approach is determined on a basis closer to commercial reality

Second, the jurisdiction of the tribunal is determined on a basis closer to commercial reality. Here, the focus is on the dispute rather than on the arbitration agreement and its contractual boundaries. The commercial implications of the dispute for third parties become relevant for the determination of the jurisdiction. The allocation of liability between genuine and third parties will be under scrutiny. Accordingly, *business and economic standards* may well come into play, when a tribunal will assess the actual business relationships between third and genuine parties. This is particularly true for disputes involving multinational group of companies.

Nowadays multinational groups adopt new corporate structures, more sophisticated than the linear parent-subsidary type of organisation. Groups often reorganise their structures along the process of ‘divisionalisation’,¹⁷ which may result to a “shift of emphasis away from a hierarchical, vertical control structure to a ‘heterarchical’ network of cooperative and lateral relationships”.¹⁸ This, in effect, means that new models of corporate organisation, that have been followed in recent years by several

¹⁶ See K. Kerameus, “Procedural unification: the need and the limitations”, I. R. Scott (ed.), *International Perspectives on Civil Justice*, Essays in honour of Sir Jack I. H. Jacob Q.C. (London 1990), at 53-55. The court in *Peterson Farms*, alluded to that, albeit not clearly, by noting that “The identification of the parties to an agreement is a question of substantive not procedural law”, *supra* n. 13 at para 43.

¹⁷ “Divisionalization is defined as the process by which the structure of a group of companies is changed from the traditional relationship of parent and subsidiary company to one where all the operation functions of several, or possibly all of the wholly-owned subsidiaries, are performed within one corporate entity, and the discreet functions are organised within separate divisions of that company. The previous structure in which each function had a separate formal and legal corporate existence is dispensed with” see Deloitte, Haskins and Sells, *Corporate structure- subsidiaries or divisions?* (August 1983) cited in P. Muchlinski, *Multinational Enterprises and the Law*, (Blackwell London 1999), p.59.

¹⁸ Muchlinski, *ibid*, p.59 et seq.; J. H. Dunning, *Multinational Enterprises and the Global Economy*, (Addison Wesley, 1992), chapter 8.

multinational groups, do not fit anymore into the legal types provided in the traditional company law. Therefore, the legal forms of the several companies belonging in the same group do not always reflect the real allocation of the decision-making power in the group. Consequently, it is difficult for a tribunal to assess *the actual relevance that each company in the group has to a contractual relationship and the dispute*, on the basis of the already known legal types of companies. Tribunals in order to allocate liability within a group of companies might need to apply new liability theories developed in the context of company law.

While the principle of “separate legal personality” is still prevailing,¹⁹ new theories, such as the “managerial control” theories, have been developed relatively recently in the context of company and economic law.²⁰ These new theories take into account the significant changes in the conventional notion of the group of companies as linear corporate structures. They are, thus, better equipped to allocate liability within the group in the context of contemporary business. Analysis on the basis of managerial control theories is not limited to equity-based groups, where the several companies of the group are linked by shares held by the parent and its intermediate holding companies. Analysis extends to any group, in which one entity can exercise a significant influence over another company through contractual rather than equity means, such as international consortia or franchising agreements.²¹ Therefore, this type of analysis goes beyond the traditional examination of the stereotypical linear forms of parent-subsidiary relationships, in the context of the theory of ‘piercing the corporate veil’.

¹⁹ See Chapter 2 above.

²⁰ See, for example, the “managerial control” theories and in particular the “enterprise entity” theory. The “enterprise entity” theory differs from the existing concepts of group liability as it attempts to assert parent liability from the degree of the economic rather than the corporate integration between the companies of the group. The theory recognises the corporate group as a distinct form of business association, see P. Muchlinski, *supra* n.17, p. 328 et seq.

See also the “network liability” approach put forward by Prof Teubner regarding the lift of the contractual veil in transnational contractual network enterprises, see G. Teubner “The many-headed Hydra: networks as higher order collective actors”, in S. McCahery, S. Picciotto., C. Scott, (Eds), *Corporate Control and Accountability: Changing Structures and Dynamics*, (1991 Authority F University Press), p. 59.

²¹ Muchlinski, *supra* n. 17, p. 63 et seq. and p. 327 et seq. In such cases, the question that arises is whether the contractual rather than corporate veil between the contractually associated parties can be lifted, so that the controlling party could be held liable along with the controlled party for acts causing loss to third parties in which both contracting parties have participated by reason of the economic and business relationship underlying the contract between them where the managerial control is. *Cf* also Teubner, *idem*.

When determining their jurisdiction in cases involving groups of companies, the tribunals should benefit from the latest theoretical developments on economic and company law. The jurisdictional approach suggested here, focuses on the dispute, the rights and liabilities of the genuine and third parties. Therefore, the jurisdictional approach allows the theories to come into play so that they provide a better understanding of the boundaries of the dispute, the rights and liabilities of all the parties involved. A detailed assessment of the business organisation and operation of the group, on the basis of managerial theories, may reveal the true degree of integration of the several companies in the group. The more integrated the several corporations are in the group, the more likely it is for them to *constitute a necessary procedural unit*. Therefore the jurisdictional approach may assist the tribunal to determine the jurisdiction on a basis closer to contemporary business reality.

By contrast, the analysis in the context of the contractual approach examines an arbitration agreement as a substantive contract and, therefore, it is limited to the interpretation of the scope and the contractual boundaries of this agreement. Naturally, the discussion in the context under the contractual approach is usually confined to the requirement of “consent” and traditional principles of contract law. Here, the examination is focused on whether the parent company is contractually bound by the arbitration agreement signed by the subsidiary rather than on whether liability can potentially be allocated within the group so that the group may constitute a jurisdictional unit.

It follows from the above, that the tribunal may assert jurisdiction over more companies in the same group whenever more companies are potentially co-liable, i.e. whenever liability can be allocated along the group. Having said that, it is only when co-liability between a parent and a subsidiary is determined by reference to the applicable substantive law, that parent and subsidiary will constitute a jurisdictional unit. This would make it very difficult for the a parent and a subsidiary to be held co-liable. As explained in Chapter 2, the principle of separate liability between a parent and a subsidiary still prevails in the majority of national jurisdiction. Group liability is provided only as a rare exception in the area of tax law or insolvency law.²² Consequently, when the parties have made provisions in their contract for a national law to apply, there would be no room for the group liability theories to apply.

²² See Chapter 2.5 for more details.

Accordingly, under the jurisdictional approach, the tribunal could not assert jurisdiction over more companies in a group.

When, however, the parties have expressly provided for a-national or transnational rules to apply or, when the parties have failed to provide for any rules or law and the tribunal decides that a-national or transnational rules should apply, there would be room for a tribunal to look into group liability theories and assume jurisdiction over the whole group. In such cases, a tribunal would be allowed to take a non-national approach and take into account new developments on liability within multinational groups.

Of course, one has to ask whether the above developments in literature would constitute sufficient evidence that a new rule providing for allocation of liability within group of companies has emerged in the context of international corporate law. The thesis does not suggest that liberal managerial theories should necessarily be adopted in order to impute liability to parent companies. If anything it should always be born in mind that the principle of separate legal personality, despite its limitations, has, in general, enhanced efficiency of business and has proved beneficial for international commerce.²³

Nevertheless, it can be argued that there are signs in legal discourse²⁴ and case law²⁵ indicating that the principle of “separate liability” although still prevailing

²³ This is also admitted by Muchlinski, *supra* n. 17, p.329.

²⁴ See the discussion in Blumberg, “American Law of Corporate Groups”; McCahery, Picciotto and Scott (eds.) *Corporate Control and Accountability* (OUP 1993) and in particular T. Hadden “Regulating Corporate Groups” therein; T. Hadden, *The Control of Corporate Groups*, (Institute Advanced Legal Studies- University of London 1983); Muchlinski, *supra* n.17; K. Hofstetter, “Parent Responsibility for Subsidiary Corporations: Evaluating European Trends”, 39 (1990) *Int’l Comp. L.Q.* 578 et seq.

²⁵ See in the US indicative case law suggesting that corporate liability may be asserted on the basis of equitable considerations *International Financial Services Corp. v Chromas Technologies Canada, Inc.*, 356 F.3d 731, 2004 WL 103311 (7th Cir. 2004); *Cosgrove Distributors, Inc. v Haff*, 343 Ill. App. 3d 426, 278 Ill. Dec. 292, 798 N.E.2d 139 (3d Dist. 2003); *Smith v Grand Canyon Expeditions Co.*, 2003 UT 57 (Utah 2003).

In France, see Com 4 March 1997, *Bull Civ IV*, n. 65: D. Affaires 1997, p. 449, holding that the several companies of Econom group were co-liaible for the breach of a contract concluded by another company of the same group. The French commercial court allocated group liability for breach of contract, on the basis that the several companies in the group were strongly interrelated, *rather than because the non-signatory companies of the group were bound by the contract*. The strong interrelation among the companies resulting to the lack of autonomy in business terms was the decisive factor for the group liability: « que c’est par une “décision du groupe” qu’il a été décidé de mettre fin aux activités de la société Econom software avant l’achèvement de l’exécution du contrat ; qu’ayant ainsi caractérisé l’absence d’autonomie de cette société et l’immixtion des autres sociétés du groupe dans sa gestion, la cour d’appel a ainsi pu, par une décision légalement justifiée, les condamner à supporter les conséquences de l’inexécution du contrat ».

should have to be revisited, so that liability is allocated within groups on a basis of actual decision making.

In any case, this question relates more to company and economic law, and certainly goes beyond the scope of this work. The aim of this section was:

- First, to show that there is a ongoing discussion in international company law on the issue of liability within multinationals. This discussion on liability may have relevance to the issue of jurisdiction in the context of arbitration.
- Second, to show that the focus with regard to jurisdiction of tribunals over group of companies should be shifted from the contractual characteristics of an arbitration agreement to the pending dispute; from “consent” to “liability”; from traditional rules of contract law to commercial reality and the new corporate structures of modern multinational groups.
- Third, to argue that the jurisdictional approach allows the new developments in company and economic law to come into play and affect the decision on the jurisdiction.

In Germany, see the *ITT* case, Bundesgerichtshof. 65 BGHZ 15, where the German Federal Court noting that a parent company with a controlling influence over a subsidiary has fiduciary duties to the subsidiary, held that liability can be allocated between parent and subsidiary on the basis of the degree of involvement of the parent company in the subsidiary’s affairs. See also the *Autokran* decision, 95 BGHZ 330 (1985), holding a parent company, involved in the management of the bankrupt subsidiary, was liable directly to the subsidiary creditors; both cases cited in Hofstetter, *ibid*, p. 583.

CHAPTER 12: THE EFFECT OF AN ARBITRAL AWARD AND THIRD PARTIES IN INTERNATIONAL ARBITRATION..... 215

<i>12.1 THE ARBITRAL EFFECT</i>	217
12.1.1 Legal Framework Regarding Arbitral Effect.....	218
12.1.2 National Regimes on Res Judicata: Differences and Constituent Elements....	220
12.1.2.1 Differences	220
12.1.2.2 Constituent Elements of Res Judicata	222
<i>12.2 RES JUDICATA AND THIRD PARTIES</i>	224
12.2.1 The “Same Parties” Requirement: Rule and Exceptions	224
12.2.2 False Third Parties: The Problem	227
12.2.2.1: Solutions in the context of litigation: unification and harmonisation mechanisms	228
12.2.2.2 Solutions in the context of Arbitration.....	232
<i>12.3 THE SUGGESTED THIRD-PARTY ARBITRAL EFFECT</i>	234
12.3.1. Examination of the Suggested Effect.....	234
12.3.2 Characteristics of the Third-Party Arbitral Effect- Distinction from <i>Res Judicata</i>	238
12.3.3 Requirements of the Arbitral Effect.....	240
12.3.4 The Parties Affected	242
<i>12.4. THE LEGAL BASIS OF THE EFFECT OF AN INTERNATIONAL AWARD</i>	245
<i>12.5. CONCLUSION</i>	248

CHAPTER 12: THE EFFECT OF AN ARBITRAL AWARD AND THIRD PARTIES IN INTERNATIONAL ARBITRATION

Until now, the thesis has been focusing on the effect of arbitration agreements upon third parties. In this chapter, the attention is shifted to the effect that arbitral awards may produce on third parties. Accordingly, the focus will be on persons who have not taken part into the arbitration proceedings resulting in an arbitral award: third parties to an arbitral award. The main question here is whether third parties with a significant interest in the dispute determined by an arbitral award can and should be affected by the determinations of this award.

The discussion on the effects of arbitral awards is inescapably related to the doctrine of *res judicata*. *Res judicata* has been the main, if not the only, effect recognised in relation to arbitral awards.¹ Hence, it was considered necessary to look

¹ See the relative discussion in literature: Interim Report of the International Law Association (ILA), Committee on *Res judicata and Arbitration* (Berlin Conference 2004), available at <http://www.ila->

first into the existing international framework relating to the *res judicata* effect of arbitral awards. In particular, Section 12.1 undertakes a comparative analysis of several arbitral rules and national laws, showing that the current national and international framework relating to the effect of an arbitral award is, where it exists at all, divergent and incomplete; in any event, it fails to meet the particular needs of international arbitration. Section 12.1.2 in particular explores those features of *res judicata* that constitute a common denominator in different legal systems. The results of this examination provide the conceptual basis for defining the appropriate effect of an arbitral award on third parties in Section 12.3.

Section 12.2 outlines the problems and limitations of the application of the doctrine of *res judicata* vis-à-vis third parties, namely persons that have not taken part in the arbitral proceedings. Here the thesis challenges the practice according to which an international award, once it is recognized by a national jurisdiction, is equated to a national judgment in terms of its effect. It is argued that this practice overlooks the international character of an international award, which character should survive even after an award is incorporated into the national legal system. Most importantly, though, this practice fails to accommodate the systemic problems arising in international arbitration with regard to intertwined multiparty relationships.

Section 12.3 puts forward the principal suggestion of this chapter. In particular, it is argued that arbitral awards should be able to affect a wider circle of third parties than the one affected by national judgments in order to compensate for the lack of third-party mechanisms at an earlier stage analogous to the mechanisms provided in the context of litigation. Thus, it is suggested that arbitral awards should somehow affect parties with an interest in the dispute (those have been named in the thesis false third parties) rather than just the parties to the proceedings and their privies. In other words, the case for a *third-party effect* of arbitral awards is made. However, as is

http://www.ila-hq.org/html/layout_committee.htm (last visited on 20 Dec 2007); Resolution No. 1/2006 issued by the International Arbitration Committee of the International Law Association, at the Conference held in Toronto June 4-8, 2006, available at http://www.ila-hq.org/html/layout_committee.htm (last visited on 20 Dec 2007); final Report Report of the International Law Association (ILA), Committee on *Res judicata and Arbitration* (Toronto Conference 2006), available at http://www.ila-hq.org/html/layout_committee.htm (last visited on 20 Dec 2007); N. Gallagher, "Parallel Proceedings, *Res Judicata* and *Lis Pendens*: Problems and Possible Solutions" in L. Mistelis and J. Lew (eds), *Pervasive Problems in International Arbitration*, (Kluwer Law International 2006), Ch.17; Dossiers ICC Institute Of World Business Law (No. 692), Bernardo M. Cremades & Julian D. M. Lew (eds), *Parallel State And Arbitral Procedures In International Arbitration* (2005); Bernard Hanotiau, "The Res Judicata Effect of Arbitral Awards" in *Complex Arbitrations*, ICC Arb Bull. Special Supplement, 43 (2003).

explained, an arbitral award should affect only some specific groups of third parties, and in a different, and certainly less drastic, way than privies. Sections 12.3.2-4 set out the content, the boundaries and the qualifications of this third-party effect of arbitral awards

Finally, Section 12.4 completes the discussion on the suggested third-party arbitral effect by exploring the legal basis of the effect of an arbitral award at an international level. Here, the focus is on the need for a harmonized regulation of the arbitral effect, instead of the current fragmented and, on many occasions, conflicting national regimes.

It is essential at the outset to clarify the sense in which *res judicata* will be used in the thesis. The term *res judicata* is often used to describe the effect produced both by a judgment and an arbitral award.² However, as will be shown, *res judicata* is a term of art developed in the context of national civil procedures, where it refers to a particularly technical and sophisticated procedural mechanism. It is thus debatable whether the term should be used to describe the effect of an award in the fundamentally different context of international arbitration. Accordingly, the descriptive term “arbitral effect” is used in the thesis with regard to the arbitration award, while the term *res judicata* is confined to national judgments.

12.1 THE ARBITRAL EFFECT

Despite the great divergence in national jurisdictions, the principle that a valid determination, either judgment or award, produces a conclusive effect with regard to the subject matter and the parties of the dispute constitutes a fundamental legal principle embedded in every legal system.³

In the context of international arbitration, in particular, the arbitral effect comes as a legal and logical corollary of the jurisdictional nature of an arbitral award. It is true that arbitration begins as a contractual phenomenon, with an arbitration agreement binding only those parties that have manifestly submitted to its jurisdiction. However, as was already explained in detail in the previous chapters, as the arbitral procedure

² See, e.g., the ILA Interim and Final Reports, *supra* n. 1.

³ P. Barnett, *Res Judicata, Estoppel And Foreign Judgments*, (OUP 2001) para.1.12: “The doctrine encapsulates the principle inherent in all judicial systems which provides that an earlier adjudication is conclusive in a second suit involving the same subject matter and the same legal bases.” See *id.* for the legislative history of the principle that goes back to Roman and ancient Greek times. It was even recognized in the Hindu text of *Katyavana*.

unfolds, the initial contractual agreement is transformed into a phenomenon with jurisdictional dimensions.⁴ The result of the arbitral proceedings is an award, which is enforceable worldwide. It has authoritative clout and it demands recognition against any natural, legal or state entity. This is why an award is not enforced as a simple contract, but is enforced with the aid of a state's coercive mechanism as would any other judicial judgment. Irrespective of any theoretical debate on the nature of the arbitral award, there are important practical implications relating to the arbitral effect. It is generally suggested that the conclusive effect of a decision, in general, serves both public and private interests.⁵ While public concerns, such as the preservation of legal resources, are less relevant in the context of international arbitration than they are in national litigation, private considerations such as the need for commercial security resulting from the finality and repose of the dispute are critical for the interests and the expectations of the parties in international arbitration. Parties resort to arbitration to have their disputes finally resolved by the award. If the issues determined in the first award were open to a fresh determination, possibly leading to conflicting awards, parties' expectations of finality and repose of their dispute would be thwarted and the effectiveness of arbitration would be compromised.⁶

12.1.1 Legal Framework Regarding Arbitral Effect

The current arbitration rules and laws constitute a suggested rather than a clear and comprehensive legal framework regarding the conclusive effect of an arbitral award. In particular, most arbitral rules merely state that "the award shall be binding on the parties."⁷ Similarly unsatisfactory is the way in which national arbitration laws address the issue, lacking, as they do, any regulation regarding an arbitral effect

⁴ See the discussion in Chapter 7 et seq. Cf. also Julian D. M. Lew, *The Law Applicable to the Form and Substance of the Arbitration Clause*, in ICCA Congress Series No. 9, Improving The Efficiency Of Arbitration And Awards: 40 Years Of Application Of The New York Convention 114 (Albert Jan van den Berg ed., 1999) ("arbitration agreement has both jurisdictional and contractual nature. It is contractual by virtue of the required agreement of the parties. It is jurisdictional by virtue of conferring jurisdiction upon the arbitration tribunal").

⁵ Cf. Barnett, *supra* note 3, para. 1.13 and R. Shell, "Res Judicata and Collateral Estoppel Effects on Commercial Arbitration", 35 (1988) *UCLA* p. 623, 640-641, for an analysis on the importance of *res judicata* on both public and private grounds.

⁶ See UNCITRAL Arbitration Tribunal, final award, September 3, 2001, *R.S.Lauder v Czech Republic*, (2002) 14 World Trade and Arbitration Material p.35 (Final Award); UNCITRAL Arbitral Tribunal, partial award, September 13, 2001, *CME Czech Republic v The Czech Republic*, (2002) 14 World Trade and Arbitration Materials, p.109; and Svea Court of Appeals (Sweden), May 15, 2003, *CME Czech Republic v The Czech Republic*, (2003) 15 World Trade and Arbitration Materials, p.171.

⁷ UNCITRAL Arbitration Rules art.32(2), American Arbitration Association Rules art. 27(1), CIETAC Arbitration Rules art.60, ICC Arbitration Rules art.28(6), LCIA Rules art.29(6), WIPO Arbitration Rules art.64(b).

specifically designed for international arbitration. Instead, it is accepted in both civil⁸ and common-law⁹ jurisdictions that international arbitral awards, after their recognition by the national domestic jurisdiction, have the same effect as domestic judgments: that is, they have the national *res judicata* effect. Nor can adequate regulation regarding the effect of an international award be found in the New York Convention, which deals with the enforcement rather than the conclusiveness of arbitral awards. This explains the lack of any detailed provision in the New York Convention with respect to the arbitral effect of an international award, apart from the brief statement in Article III that:

“[e]ach Contracting State shall recognize arbitral awards as binding...”

Laconic, almost cryptic, the above national and international laws and rules fail to address a series of important issues with regard to the effect of an arbitral award. Thus, a series of questions remains unanswered:

- To what extent, if at all, does the arbitral award prevent the relitigation of the issues that have been determined therein? Does it merely cover the legal claims or does it extend to the facts?
- Does the arbitral effect apply only to the dispositive part of the award or does it extend to the reasoning as well?

⁸ This is expressly stated in the French NCPC art.1476 (for domestic arbitration) and art.1500 (for international), see also Cass. Soc. 19 March 1981, (1982) *Rev Arb.*, 44; in the Netherlands Arbitration Act 1986, art.1059; in the Belgian Judicial Code art.1703(1); in the new Austrian CCP s. 607; in Greece, art 35(2) of the 2735/1999 Act reads in tandem with art.896 Code of Civil Procedure, see also AΠ 448/1969, (1970) NoB 36. Cf UNCITRAL Model Law art.35(1) and German ZPO art.1055: “the award is binding”. These provisions practically refer to national provisions regarding *res judicata*; cf H. Koch and F. Dierich, *Civil Procedure in Germany*, (Kluwer Law International 1998), para 92. In Swiss Law, it is accepted that a final award produces the effects of *res judicata*. Swiss law also recognises *res judicata* to a foreign arbitral award to the same extent that the law of the country in which the award was made would recognise that award. On the other hand, these effects cannot go beyond those which the award would have if it was a Swiss award made in Switzerland, see art.190 of the Private International Law Statute (1990) and S. Berti (ed.), *International arbitration in Switzerland*, (Kluwer Law International 2000), art 190 para.6 and art 194 para.134 et seq.

⁹ In the US, despite the fact that the FAA lacks any specific reference to the effect of an arbitral award, it is good law that the award has the same effects as a national judgment under the rules of *res judicata*, subject to the same exceptions and qualifications, see Restatement (Second) Judgments, (1982), para.84; Shell, *supra* n.5, p. 641 and the relevant case-law therein: “The American courts have long held that *res judicata* applies to arbitration awards.” The same is accepted in England, although the English Arbitration Act 1996 (EAA), s.58(1) merely refers to a “final and binding” award: see *Fidelitas Shipping Ltd v V/O Exportchleb*, [1965] 1 Lloyd’s Rep 13; Merkin, *Arbitration Law*, (LLP London 1996 loose-leaf) para.16.116; see also EAA s.101(3): “Where leave [on enforcement] is so given, judgment may be entered in terms of the award”, ie judgment and award are equated after the recognition of the award in the domestic jurisdiction. Cf also the Hong-Kong Arbitration Ordinance, ss. 2GG (applicable to both domestic and international arbitration), 40B.2 (domestic only) and 42 (international only).

- To what extent is a subsequent arbitration tribunal or a national court bound by the findings of an award previously rendered?
- Does the arbitral effect cover any issue that was not raised in the arbitral proceedings, but which ought to have been raised?

More importantly, though, for the purposes of the thesis, the existing legal framework regarding the effect of an international award fails to address the question of

- Which persons are bound by the arbitral effect, or
- Whether an arbitral award can extend to, or in any other way, affect any third party¹⁰

No answer can be given to any of the above questions, since the current arbitral framework falls short of providing a sufficient and autonomous regulation of the effect of international arbitral awards. Instead, the issue is referred, either expressly or impliedly, to the domestic provisions on *res judicata* that apply to national judgments. However, as the following two sections show, the national *res judicata* regimes are not only divergent, but also designed for domestic litigation and national judgments. They are thus unsuitable in practical terms for application to international arbitration and arbitral awards.

12.1.2 National Regimes on Res Judicata: Differences and Constituent Elements

The doctrine of *res judicata* has developed as one of the most sophisticated, technical and overregulated doctrines in national civil procedures. A detailed consideration of the different national regimes on *res judicata* goes far beyond the scope of the thesis. The aim of this brief comparative overview is first to highlight the divergent approaches taken by legal systems with regard to *res judicata*, and second to ascertain the constituent elements of the meaning of *res judicata*.

12.1.2.1 Differences

There is a great divergence among national legal regimes with regard to *res judicata*. The difference is particularly marked between common and civil law jurisdictions. The basic difference in their approach may be summarised as follows.

¹⁰ It must be underlined that with regard to this question, even the ILA Final Report on Res Judicata, *supra* n.1, expressly avoided to give any guidance to the “because of the complexity of those issues and in order not to preempt any such development”.

- In common-law countries, case law has developed a broader notion of *res judicata* which prevents the re-litigation not only of the claims¹¹ but also that of the issues,¹² factual and legal, adjudicated in the judgment. From this it appears that common-law countries consider that a judgment represents a judicial record of what actually happened with regard to the dispute. *Res judicata* in this sense has a fact-determination purpose. It is considered as a means of evidence, as an authoritative assertion of the whole “story” of the dispute. The term *estoppel per rem judicata* comes from the term *estoppel by record* in common law and reflects exactly this common-law approach to *res judicata*,¹³ which is closer to the Roman rule that “*res judicata pro veritate accipitur*”.¹⁴
- In contrast, in modern civil procedural systems, the codified *res judicata*¹⁵ is normally confined to the claims rather than the issues determined in a judgment.¹⁶ The prevailing view here is that the *res judicata* effect does not apply to the factual findings in a judgment. Civil-law countries seem to subscribe to the view that a judicial determination is fallible by nature and, in that sense, can only determine the *legal consequences* of what seems to have happened rather than determine *what actually happened*, that is, the facts. Parties are thus free to re-litigate facts determined in a judgment simply because *res judicata* does not bear any evidentiary significance for them.

¹¹ In England, the term used is “Cause of action estoppel”; see Barnett, *supra* n. 5, para. 1-38 *et seq*, Halsbury’s, *Laws Of England*, (4th ed. 2003) para 179-180. In the U.S., the term used is “Claim preclusion”; see *Parklane Hosiery v Shore*, 439 U.S. 322 (1979), Restatement, *supra* n. 9, para. 18-20, and Shell, *supra* n. 5 at 639.

¹² In England, the term used is “issue estoppel”; see *Carl-Zeiss Stiftung v Rayner & Keeler Ltd*, [1967] 1 AC 853, and *New Brunswick Ry v British and French Trust Corp* [1939] AC 1, HL (Lord Maugham LC), at 20, referring to issue estoppel (“it is unjust and unreasonable to permit the same issue to be litigated afresh”), and Halsbury’s, *supra* n. 11, para 434 (“issue estoppel applies whether the point involved in the earlier decision is one of fact or one of law or one of mixed fact and law”). In the U.S., the term used is “collateral estoppel”; see Restatement, *supra* n.9, para. 27, and Shell, *supra* n.5, p.647.

¹³ See Halsbury’s, *supra* n. 11, para. 964

¹⁴ Note, however, that the French notion of *res judicata* seems close to this concept, since *res judicata* is promulgated by Code Civil, art. 1351 under Section III, which deals with evidentiary presumptions, of Chapter VI, which deals with issues of proof. It follows that they too give *res judicata* an evidentiary power: *cf. also* Vincent-Guinchard, *Procédure Civile*, para.179 (27th ed. 2003).

¹⁵ France, NCPC, art. 480, Belgian Code of Civil Procedure, art. 23, German ZPO art. 322, Greece Code of Civil Procedure, art. 321 *et seq*. The doctrine is not codified in Switzerland.

¹⁶ ILA Interim Report, *supra* note 1 at 16. See also in France. Dalloz, NCPC, 97th ed. (2005), art. 480 and Vincent-Guinchard, *supra* note 14 (for France); in Switzerland, Berti, *supra* note 8, art. 187 para. 41 and Fabienne Hohl, *Procédure Civile*, Tom I, (Staempfi Berne 2001), para. 1292 (for Switzerland); in Greece, Κεραμεύς Κονδύλης Νίκας, *ΕρμΚΠολΔ*, (Σάκκουλας Αθήνα Θεσσαλονίκη 2000), art.321-334.

12.1.2.2 Constituent Elements of *Res Judicata*

Having briefly outlined the differences in the approach of the national legal regimes to *res judicata*, it is now necessary to explore conceptual features of *res judicata* which are common to different legal jurisdictions. This common denominator will effectively provide the constituent elements of the concept of *res judicata* which, in turn, is essential to determining, in Section 12.3, which is the right effect of an international arbitral award.

The *raison d'être* of *res judicata* is the preservation of a decision's authority. While a decision determines the legal status of the dispute in question, *res judicata* ensures that this determination is not circumvented or overturned by subsequent conflicting determinations.¹⁷ To achieve this objective, *res judicata* produces different kinds of effects:

1. *Prohibits reassertion*: this kind of effect comes into play in a case where the subject matter and the parties to the second set of proceedings coincide with those of the first set. In these cases *res judicata* precludes the reassertion of the cause of action adjudicated in the first judgment, prohibiting a party to the first set of proceedings from even filing an action based on the cause already determined. This type of effect reflects the fundamental principle of the *ne bis in idem* in accordance with which a party cannot be granted relief twice on the same cause of action.¹⁸

2. *Preclusive effect*: this kind of effect comes into play in relation to pleas rather than the cause of action of the first set of proceedings. In particular, it prevents the re-litigation of any plea which was determined in the judgment and which plea arises in the second set of proceedings not as the main subject matter (cause of action) but as an issue necessary to determine the main subject matter.¹⁹ The preclusive effect

¹⁷ As used here, "*res judicata*" encompasses the doctrine of "collateral estoppel" too.

¹⁸ In the common law, the previous cause of action is considered to be merged, and thus extinguished, with the first judgment. See Barnett, *supra* note 3 para. 1.41; cf. *Thoday v Thoday*, [1964] P 181 CA (Diplock LJ) at 197: "...it is a plea that prevents a party in subsequent litigation from asserting or denying the existence of a particular cause of action, the non existence or existence of which has been determined by a court of competent jurisdiction in previous litigation between the same parties or their privies." In civil-law countries the prohibition on reassertion is considered more like a procedural impediment to exercise the same cause of action twice.

¹⁹ Restatement, *supra* n. 9, ch. 1, *Introduction*: "'Preclusive effects' refers to limitations on the opportunity in a second action to litigate claims or issues which have been or could have been litigated in a prior action. In general terms, these limitations include the rules of claim preclusion and issue preclusion."

follows from the *ne bis in idem* principle, but applies only in a case where the subject matter in the two sets of proceedings to some extent overlap, rather than coincide.^{20 21}

3. *Conclusive effect*: *Res judicata* does not simply prohibit relitigation of an issue or a claim that have been litigated in a prior action (negative effect). It ensures that the determinations in the first decision will be followed by the second one, whenever the same issues arise in the second set of proceedings as issues necessary to determine the main subject matter of the second action (positive effect). Thus, in a case where a previously determined issue is raised in the second set of proceedings, the second forum should accept the determination of the first judgment on these issues as conclusive and thus accept this determination as a logical and legal basis of the second decision. In other words the determinations of the first decision are binding on the second forum. In this sense, *res judicata* has a harmonising effect, ensuring that the two overlapping decisions. Only the combination of preclusive and conclusive effects can effectively preserve the authoritative status of the first decision.

4. *Enforcement*: The *res judicata* effect is interrelated with the enforcement of a judgment. *Res judicata* and enforcement are two sides of the same coin and their boundaries, in terms of *ratione personae*, necessarily coincide.²² Thus, in principle, a judgment is enforceable against those parties and only those parties that are bound by *res judicata*. Thus, the enforcement is a legal and logical corollary of the

²⁰ This preclusive effect under particular circumstances may be extended not only to the issues that were actually raised in the proceedings but also to those that, by due diligence, could have been raised but eventually were not (the extended form of *res judicata*). This is clearly the case in England, where this type of effect is understood as part of the principle of abuse of process. See *Henderson v Henderson*, [1844] 6 QB 288 and the more recent *Johnson v Gore Wood & Co.*, [2000] 2 AC 1; cf. also EAA s.73(1)d. The extended preclusive effect also operates slightly differently in the U.S., see Restatement, *supra* n. 9 para. 27. In addition, it is found in some civil-law countries, but not as part of the abuse of process principle, which is unknown to these jurisdictions. See e.g., the Greek Civil Procedure Code, art. 330: “*Res judicata* covers those pleas that have been raised, as well as those that could have been raised but were not.”

²¹ Although there is a fundamental difference between the common and the civil law regarding the extent of this effect (it is extended to both claims and issues (factual and legal) in common law but only to claims in civil, *supra*), the preclusive effect constitutes a basic common denominator of the *res judicata* concept in both legal systems. See Vincent-Guinchard, *supra* n.14, para. 179.b.

²² See Vincent-Guinchard, *supra* n. 14, para. 178: « l'autorité de la chose jugée s'identifie alors avec la force obligatoire de la sentence ». In Switzerland see F. Hohl, *supra* n.16, para. 4-1. In England cf. s.58 EAA: “ unless otherwise agreed by the parties, an award made by the tribunal pursuant to an arbitration agreement is final and binding, both on parties and on any persons claiming through or under them” (subjective boundaries of an arbitral award) with s.82(2): “...a party to an arbitration agreement include any person claiming under or through a party to the agreement” (subjective boundaries of an arbitration agreement) (emphasis added). See also Koch & Diedrich, *supra* n. 8, para. 133.

conclusiveness of the decision. The converse is also the case: *res judicata* is a condition precedent for enforcement.²³

12.2 RES JUDICATA AND THIRD PARTIES

12.2.1 The “Same Parties” Requirement: Rule and Exceptions

The above four different kinds of effect explain *how* the *res judicata* effect should apply. It is also important, however, to determine *the parties* that should be affected by *res judicata*. Hence, this subsection examines the “same parties” requirement, the analysis of which will define who is bound by *res judicata*, including the extent to which third parties may be affected.

The “same parties” requirement means that, as a rule, a decision affects only those persons who took part in the proceedings that resulted in the decision, namely the parties in action (genuine parties) as opposed to any third party. This requirement serves the fundamental principle of due process, that is, the right of the party to be heard. This rule, however, is by no means without exceptions. Almost every legal system under certain circumstances provides for exceptions to the “same parties” requirement, so that even persons not taking part in the proceedings are bound or somehow affected by the decision.

This is true in common, civil and even Shari’a law.²⁴ The extent of these exceptions, of course, differs among jurisdictions, but the extension of the effect of a judgment to a “circle” of parties other than the real parties constitutes a general principle common to almost every legal system. In civil-law countries this circle of third parties, to which *res judicata* is extended, is limited and is normally determined *a priori*, by civil and procedural codes.²⁵ In contrast, in common-law countries the

²³ This is not to say that *res judicata* and enforceability have the same effect. In order to be enforced a judgment normally requires an order which is granted by the national courts (*exequatur*). All that is suggested here is that the *res judicata* is, as a rule, a condition precedent for the enforcement of a judgment, as both effects implement the authoritative determination of the decision.

²⁴ For example, the judgment is extended to the heirs of the deceased when it has been issued against the deceased and against the debtor if issued against the guarantor. See ‘Ali Hay Dar Durar Al-Hukkam, “Commentaries Of Majalla”, Art. 1842, found in Samir Saleh, *Commercial Arbitration The Arab Middle East*, (2nd ed. 2006), p.70.

²⁵ Thus, in Germany, the German Code of Civil Procedure (ZPO) ss.326-327 provides for the extension of *res judicata* to the successors, assignors and executors. In France, as an exception to the general rule stipulated in the French Civil Code Art. 1351, it is accepted that *res judicata* is extended to those third parties that are deemed to be represented by the parties to the proceedings. The exception is applied in the case of universal successors, assignors, and jointly and severally liable debtors of a party. See, in general, Dalloz, Code Civil, Art. 1351, Vincent-Guinchard, *supra* n. 14, para. 179b.1 and Boyer, “Les effets des jugements a l’egard des tiers”, 49 (1951) *Rev. Trim.*

circle consists of the so-called privies, i.e. persons that are in privity with one of the parties in an action.²⁶ Defining the concept of privity is difficult, not least because it has a different meaning in the U.S.²⁷ from that which it has in England.²⁸

In general, the test of whether the *res judicata* will be extended to a third party is the “community of interest” test between this third party and one of the parties to the action. More specifically it is required that the third party and one of the parties to the action are so closely associated in terms of interests that the third party’s interests “are represented by a party to the action.”²⁹ ³⁰ In fact, for the *res judicata* effect to be

Dr. Civ., p. 163. In Greece, *res judicata* extends, *inter alia*, to the assignor and successor in right, the trustee, the executor, and the guarantor (but only in a case where the judgment is for the debtor against the creditor). See Greek Code Civil Procedure, Arts. 325-329 AΠ 936/1986, NoB 1987, p.1219; Κεραμεύς Κονδύλης Νίκας, *supra* n. 16, art. 325.

²⁶ Restatement (First) Judgments, (1942), para. 83: “A person who is not a party but who is in privity with the parties in an action terminating in a valid judgment is bound by and entitled to the benefits of the rules of *res judicata*.” ²⁷ The Restatement (Second), notes, characteristically, “It may be less misleading if not much more meaningful to use the term ‘relationship’ between parties instead of ‘privity.’” Restatement (Second), *supra* note 9, para. 1 (*Introduction*); and again: “The term ‘privity,’ unless it refers to some definite legal relationship such as bailment or assignment, is so amorphous that it often operates as a conclusion rather than an explanation,” Restatement (Second), para. 62.

²⁷ In general, the U.S. law takes a broad view privies, encompassing all persons that have a title or a substantive right of their own but do not take part in the litigation with the real parties, either because they choose not to or because they are not allowed to. This includes, for example, the executor, administrator, guardian, cases of principal and agent, the assignor-assignee, bailor-bailee, and certain cases of partnership; see Shell, *supra* n. 5, at 640: “The notion of privity in the law of *res judicata* has also been flexible and it simply signifies that parties are in such relationship to one another that a judgment involving one may justly be conclusive upon the other”; see, *in general*, Restatement, *supra* n 9, paras. 34-62 *et seq*, for a detailed presentation of the different types of third parties affected by *res judicata* and Herbert Semmel, “Collateral Estoppel, Mutuality and Joinder of Parties”, 68 (1968) *Colum. L. Rev.*, p. 1460: “some cases have stretched the concept of privity to the constitutional limit and perhaps beyond,” referring to the example of *Makariw v Rinard*, 222 F. Supp. 336 (E.D. Pa 1963).

²⁸ English law takes a much narrower view of privity, limiting the “circle” to parties that claim a title or a right under, through or on behalf of another party. This group includes the case of the ancestors and heirs (privies in blood) or the case of a successor to rights or liability (privies in title) or the case of a trustee-beneficiary (privies in interest). See Halsbury’s, *supra* n. 11, at 452 *et seq*; Barnett, *supra* n. 3, paras. 3-20 *et seq*; cf. also Carl Zeiss, *supra* n. 12; cf. EAA ss. 58 & 82(2) and *House of Spring Gardens v Waite*, [1991] 1 QB 241(CA).

²⁹ Gary Cunningham, “Collateral Estoppel: The Changing Role of The Rule of Mutuality”, 41 (1976) *Mo. L. Rev.*, p. 522; cf. *Shiels v Blakeley*, (1986) 2 NZLR 262,268 (NZCA): “ there must be shown such union or nexus, such a community or mutuality of interest, such an identity between a party to the first proceeding and the person claimed to be estopped in the subsequent proceeding that to estop the latter will produce a fair and just result.”

³⁰ This identification is basically substantive: co-owners in property, for example. However, it may also be procedural, as is the relationship between the trustee and the beneficiary. It is usually contractual but may be tortious. Thus, tortfeasors are considered in privity. See *House of Spring Gardens v Waite*, [1991] 1 QB 241 (CA) and in the U.S., Restatement, *supra* n. 9, para. 48; different in Barnett, *supra* n. 3, paras. 3-17, who puts tortfeasors under the category of “deemed parties” as well.

extended to a third-party, the latter and the party to the action must have identical interests.³¹

Two conclusions may be drawn from above analysis: First, the exception to the “same parties” rule is so well-established in almost every legal system that it may be argued that the fact the exception is also a constituent element of *res judicata*. It follows that the “same parties” rule in *res judicata* should read: *res judicata* applies mainly to the parties to the action but also, in exceptional circumstances, to third parties.

Second, the circle of the third parties bound by *res judicata* is extremely narrow, since the extension of *res judicata* to a third party requires a substantial degree of identification, in terms of interests, between the third party and one of the parties to action. As the “identification test” is so strict, it is only in very limited circumstances that the *res judicata* effect is extended to a third party.

This strict test thus leaves all other third parties beyond the reach of any judgment effect. This rule, in principle, applies to arbitration as well, since awards and judgments are equated in terms of effect.³² Thus, the effect of an arbitral award may not bind or even affect any person other than one substantially identified with the parties to the arbitration proceedings. In effect, only privies to the parties to the arbitral proceedings will be bound by the *res judicata* effect of an arbitral award. By contrast, false third parties, who are neither genuine parties to the arbitral proceedings nor privies to the parties thereto, will not be bound by the *res judicata* effect of an arbitral award. This applies to both groups of false third parties identified in the thesis in Chapter 2. False third parties may be contractually interrelated to, or even co-liaible with, the parties to the action, however, their interests are not identical to those of the parties in the proceedings, and therefore they fall short of privity.

The following sections show in detail why the *res judicata* effect recognised for arbitral awards is not sufficient to address the problems related to multiparty

³¹ Cf. *Drouot Assurances S.A. v Consolidated Metallurgical Industries, Protea Assurance and GIE*, ECJ Case C-351/96, [1998] E.C.R I-3317 which employs the criterion of “identical and indissociable interests”; see also para. 19: “there had to be such a degree of identity between the interests of the insurer and the insured that a judgment in relation to one would be *res judicata* for the other”; cf. Peter Kaye, *Law Of The European Judgments Convention*, (Chichester: Barry Rose Law Publishers 1999), p. 2780: “the fundamental underlying criterion for assessment of whether insurer and insured are to be treated as same parties ... is whether they have such identical and indissociable interests as to satisfy the requirements of the efficient administration of justice and avoidance of irreconcilable judgments balanced against fairness to parties without denial of justice through trial.”

³² See Section 12.1 above.

contractual relationships in arbitration. As it will be argue the circle of third parties that may be affected by an international arbitral award should be wider than that affected by *res judicata* resulting from a judgment. By the same token, however, the *kind* of third-party effect produced by an international award should be different from the *res judicata* effect produced by a judgment.

12.2.2 False Third Parties: The Problem

As was already mentioned, false third parties fall short of privity with the genuine parties. The interests of false third parties in the multiparty project, although interlinked, are not identical to those of the parties to the arbitral proceedings. This applies to both groups of false third parties, namely false third parties that are co-liaible or simply contractual interrelated to the genuine parties. Nevertheless, there is a strong substantive nexus between false third parties and genuine parties. They might not be privies, but their contractual rights are inextricably intertwined with the rights of at least one of the parties to the arbitral proceedings.³³ This most likely means that many of the legal and factual issues arising in the bilateral arbitral proceedings will also arise in subsequent proceedings between false third parties and one of the parties to the first set of proceedings. There is thus the risk of inconsistent, if not conflicting, decisions³⁴ arising out of the several sets of proceedings in relation to the same multiparty commercial project.

As has repeatedly been argued in the thesis, there is a clear need for the communication between parallel overlapping proceedings, so that ensuing the decisions are to the extent possible harmonised.

³³ Compare the very interesting analysis of the third parties' interests in Alexis Mourre, "L'Intervention des Tiers à l'Arbitrage", Recueil Vol.I (2000-2002) *Les Cahiers de l'Arbitrage*, p. 100 arguing for the analogous application of national intervention mechanisms in arbitration.

³⁴ There is a slight difference between the terms "conflicting" and "irreconcilable" decisions: the former is stricter, referring to decisions between the same two parties but with *mutually exclusive legal consequences*, whereas the latter is wider referring to contradictory decisions in the case of multiparty relationships. However, problematic situations may arise not only from "conflicting" but also from "irreconcilable decisions." Cf Council Regulation (EC) no.44/2001, on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters, art.34.4 which provides for resistance to the recognition of "irreconcilable" rather than "conflicting" judgments.

12.2.2.1: Solutions in the context of litigation: unification and harmonisation mechanisms

In the context of litigation, there are two ways in which two or more parallel proceedings involving the same legal and factual issues are regulated so that conflicting decisions are avoided:

First, by third-party mechanisms that bring all the relevant parties before a single forum. This type of third-party mechanisms can be named *unification mechanisms*. Examples of unification mechanisms are: common jurisdictional bases, class actions, intervention and joinder, interpleading and consolidation.³⁵ In this way parallel proceedings are avoided altogether, and regulation of multiparty relationships is achieved in an early stage, namely in a pre-judgment stage. Unification mechanisms bring all the relevant parties in the same set of proceedings in a rather intrusive and drastic way. Parties are not allowed to litigate their disputes bilaterally. Instead, through unification mechanisms, third parties are brought in the proceedings between two other parties, at some times even against the will of the original parties or even against the will of the third parties themselves.³⁶

Secondly, by mechanisms that merely *harmonise* the outcomes of the parallel proceedings, rather than bring all the several parties before a single forum. Typical examples of *harmonisation mechanisms* are *lis pendens* and *res judicata*. Here, the several set of proceeding remain parallel, instead of being consolidated. However, *lis pendens* and *res judicata* regulate the parallel proceedings, so that conflicting findings and decisions are avoided. In particular, *lis pendens* prevents the continuation of the second set of proceedings until a decision in the first set of proceedings is granted. *Res judicata*, either prevents the second set of proceedings to commence at all or ensures that the second forum is bound by the determinations of the first decision.

Both *lis pendens* and *res judicata* ensure that the second proceedings do not continue without taking the determinations of the first decision into account. In this way, the results of the first proceedings are communicated with the second trial so

³⁵ See in detail Section 8.2 above.

³⁶ In many instances third party provisions are drafted as compulsory mechanisms: see, for example, art.331 NCPC (intervention forcéé) or US Fed.R. r.24.(a)(intervention as a matter of right). See below for more details; *cf. Vaccaro v Moore-McCormack Lines*, S.D.N.Y.1974, 64 F.R.D. 395: consent of the parties is not required for a consolidation of actions; rather, it is the trial court's decision whether common questions of law and fact indicate that sufficient judicial economy would be achieved by consolidation, when balanced against any inconvenience, delay, or expense caused to the parties by attending trial of some issues not shared by all.

that conflicting judgments are avoided. Thus, harmonisation mechanisms are designed to prevent conflicting decisions in a different way than bringing all the relevant parties before the same court. Harmonisation mechanisms bring the several decisions *into accord*, rather than they consolidate the several proceedings.

As a matter of general policy, national civil procedures give precedence to the application of unification over harmonisation mechanisms. The former, as explained above, are more drastic, achieving the maximum results in terms of preservation of procedural recourses and consistency in the determination of the multiparty dispute.

Thus, in general, third-party unification mechanisms are more broadly applicable than harmonisation mechanisms. Indeed, the right of intervention or joinder is accorded to a wide circle of third parties, whereas the application of *lis pendens* or *res judicata* to third parties usually hinges on more stringent conditions, namely the “same parties” requirement and the strict test of identification of interests explained above.

Thus, for example, in proceedings between an employer and a contractor, a subcontractor may either intervene on its own³⁷ or be interpleaded by one of the real parties.³⁸ However, a subcontractor will typically not be bound by the *res judicata* effect of the decision between a contractor and an employer, since contractor and subcontractor have interrelated but certainly not identical interests in the dispute, and therefore they can never be taken as the “same parties”. It, therefore, seems clear that, whereas unification mechanisms are designed to apply to third parties, harmonisation mechanisms are applicable to third parties only as a limited exception.

The precedence of unification over harmonization mechanism is based on sound reasons.

- First, as a matter of general policy, procedural harmonisation of multiparty relationships is welcome at as early a stage as possible. It is difficult to resolve any inconsistency after conflicting judgments have been given, since at that stage both judgments enjoy the status of authority and are presumed to be enforceable.³⁹

Thus, it is preferable to apply unification mechanisms, which are available even

³⁷ For example, French NCPC art 330 or US Fed R.r.24(b).

³⁸ For example, French NCPC 331 or US Fed R. r. 14.

³⁹ Cf P. Kaye, *Law of the European Judgments Convention*, *supra* n.31, p.2631: “it is better to prevent the situation from arising in the recognition context in the first place by tackling the problem at the adjudicatory stage”.

from the beginning of the proceedings, rather than harmonisation mechanisms that are available at a later stage or even after one decision is issued.

- Secondly, issues of violation of due process may arise with regard to harmonisation mechanisms, and *res judicata* in particular. The extension of the drastic effect of *res judicata* to third parties raises the question of violation of the constitutional right of the third party to be heard.⁴⁰ On the other hand, participation of a third party in the proceedings, via unification mechanisms, ensures that the third party is, at least, given the opportunity to present its case.

However, efficient as unification mechanisms may be, their application is not always possible. In many cases *impediments of jurisdictional nature* preclude a court from assuming jurisdiction over all the relevant parties or claims. Therefore, multiparty proceedings are not possible. In these cases, unification mechanisms fail to work and the duty to prevent conflicting judgments passes down to the harmonisation mechanisms.

For example, in the US, the US Federal Rules providing for joinder or intervention are not applicable where joinder or intervention of third parties would deprive court of jurisdiction by destroying diversity of citizenship. For the third party to be joined or intervene all the several parties must be submitted to the jurisdiction of different states.⁴¹ Here, the lack of diversity of citizenship constitutes a “jurisdictional impediment”, precluding the application of unification mechanisms.

Similarly in the context of the European Regulation 44/2001, a creditor by virtue of art.6(1) of the Regulation can bring a joint action against a debtor and its guarantor as co-defendants before a single national court, even if the debtor and the guarantor domicile in different Member States. However, as is generally accepted, the joinder of a guarantor and a debtor in a single action is not possible where a bilateral jurisdiction agreement between the creditor and the debtor exists.⁴² In such a case, the creditor will have to file two different actions before two different courts in different

⁴⁰ See Restatement (Second) Judgments, (1982) para.29b and Reporters Note: “The proposition that a non-party cannot be bound by a judgment, unless he is represented by a party or has interests that are derivative from a party, is a rule of Constitutional Law: see also *Bernhard v Bank of America*, (1942) 19 Cal.2d, 122 P.2d, at 894: *res judicata* must “conform to the mandate of due process of law that no person be deprived of personal or property rights by a judgment without notice and an opportunity to be heard”.

⁴¹ See *Chesapeake Bay Village v Costle* (1980, DC Md) 502 F Supp 213 and *Bakia v County of Los Angeles* (1982 Cal) 687 F2d 299, 34 FR Serv 2d 1527.

⁴² See *Hough v P & O Containers Ltd* [1999] Q.B. 834; Cf Morris, *The Conflict of Laws*, (6th ed) (London Thomson Sweet & Maxwell 2005), para 4-038, n. 7.

Member States: one against the debtor in accordance with the jurisdiction agreement, and another against the guarantor in accordance with the general rules on jurisdiction (Chapter II of the Reg. 44/2001). Here, the joinder of a debtor and a guarantor in a single action before a single court will not be possible. The exclusive jurisdiction agreement between the creditor and the debtor will constitute a “jurisdictional impediment”, precluding the application of the unification mechanism of Reg. 44/2001 art.6(1) .

However, when the regulation of the several proceedings by reference to unifications mechanisms is not possible, harmonisation mechanisms may come into play to avoid conflicting decisions.

Indeed, even if the application of Reg. 44/2001 art. 6(1) fails to apply and a creditor has to bring two separate actions against a debtor and a guarantor, the two sets of proceedings will not necessarily result into conflicting decisions. The harmonisation mechanism of *lis pendens*, provided by Reg.44/2001 arts. 27 and 28 will come into play, in order to harmonise the two parallel proceedings so that conflicting judgments are avoided. Thus, the second proceedings, say between a creditor and a guarantor, will most likely be stayed until the first proceedings between the creditor and the debtor are completed and a decision is finally given.⁴³

The conclusion that can be drawn from the above is that unification third-party mechanisms are, indeed, given precedence over harmonisation mechanisms. However, when unification is not possible due to an overriding jurisdictional impediment, such as the existence of an exclusive jurisdiction agreement between two only of the several parties, harmonisation mechanisms may take over and regulate the parallel proceedings.

⁴³ Art.28, rather than art.27, is more likely to apply in this example. In *Drouot Assurances v CMI et alia*, *supra* n.31, the European Court of Justice (ECJ) held that art.21 of the Brussels Convention 1968 (ie art.27 in the Reg. 44/2004) is not applicable with regard to two parallel proceedings between a barge insurer against the cargo owner and the cargo insurer on the one hand, and the barge owner/insured against the same parties on the other hand. However, as Advocate General Fennelly mentioned in his opinion (European Court Reports 1998, page I-03075, at para.30) article 22 (ie art.28 now in the Reg.44/2001) has a broader scope and, thus, could apply in this context instead of art.21. It should be noted that, according to the most persuasive view, art.28 is not subject to art.23 and, thus, it would apply notwithstanding the existence of an exclusive jurisdiction agreement, see P. Kaye, *Law of the European Judgments Conventions*, *supra* n. 31, p.2784; *cf also*, *The Linda* [1988] 1 Lloyd's Rep.175, where insurers were involved in the first proceedings but not in the second. Sheen J. noted, at 179: “If, as I assume, the insurers have a right of subrogation, then adding their names as plaintiffs may be a necessary procedure in the Netherlands, but it adds nothing of substance. In my judgment, art.21 applies and the Court must give effect to it by declining jurisdiction. If I am wrong in that decision, then art.22 must apply”.

12.2.2.2 Solutions in the context of Arbitration

As has been shown in detail in the previous chapters, third parties cannot in general be brought before arbitral proceedings between two genuine parties thereto.⁴⁴ The principle of party autonomy expressed in the form of an arbitration agreement will, as a matter of rule, prevail over the desirability to bring the several parties before a single arbitral tribunal. The existence of an arbitration agreement between two of the several parties involved in a multiparty commercial project constitutes a overriding “jurisdictional impediment”, which precludes the application of unification mechanisms to international arbitration. Therefore, the policy of an early regulation of the parallel proceedings applicable in litigation will normally not apply to arbitration.

In this way, arbitration is left without any means of regulation for multiparty disputes at all. False third parties, namely third parties with a significant interest in the outcome of the arbitration between two other parties, are left totally outside the arbitration both during the proceedings and after the award is given

- At the pre-award stage, intervention or joinder or consolidation is generally not allowed, due to the principle of party autonomy.
- At the stage after the award has been made, the arbitral award obtains the status of a judgment and thus has limited third-party effects, or at least third-party effects that do not extend to false third parties.

Hence a subcontractor, a surety, a partner, an affiliated company and many other cases of false third parties remain, as a rule, unaffected, both by the arbitral proceedings and the award, between the genuine parties.

It can be argued thus that the regulation of multiparty disputes should be passed down to harmonisation mechanisms: *lis pendens* and *res judicata* or another type of arbitral effect. In the context of multiparty disputes, the arbitral proceedings and the arbitral award should affect a wider circle of persons than those who are parties to the arbitration agreement. In this way, arbitration can accommodate the intrinsic problems arising out of multiparty relationships and disputes and compensate for the lack of third-party mechanisms at an earlier stage analogous to the mechanisms provided in the context of litigation

⁴⁴ Unless, the jurisdictional approach suggested here is taken with regard to the false third parties of the first group.

As regards the arbitral proceedings and *lis pendens*, courts have accepted in many cases that the *lis pendens* effect of arbitral proceedings has been extended to false third parties. This has been demonstrated in detail in Chapter 7.1 and needs not to be repeated here. It suffices to say, that pending arbitration proceedings between the two parties to an arbitration agreement, national courts may stay proceedings between a party to an arbitration agreement and a false third party, on the ground that the second action is inextricably involved with the subject matter of the pending dispute before the tribunal.⁴⁵ Thus, the parallel interrelated proceedings are attuned.

The same should be accepted with regard to arbitral awards. Arbitral awards should have an effect extending the genuine parties to arbitration proceedings in order to harmonise the parallel proceedings. However, as explained, any third-party effect of arbitral awards is not possible, because arbitral awards obtain the status of a national judgment, whose *res judicata* effect is limited only to the parties in action and their privies.

It follows that an arbitral award should obtain a different status from that of a national judgment, which would allow an arbitral award to produce a different kind of effect on false third parties, than the *res judicata* effect. This arbitral effect on false third parties should be analogous to the degree of association between false third parties and parties to the arbitral proceedings, in terms of interests.

As was explained, a party in an action and its privy are considered to have identical interests and therefore the *res judicata* effect is extended to the privy.⁴⁶ False third parties, however, have interlinked, but certainly not identical interests with the parties to arbitral proceedings. If the *res judicata* effect extended to false third parties, issues related to due process and their right to be heard would arise.

⁴⁵ For example, in the US see *Lawson v Akzona*, 355 F. Supp. 1146 (S.D.N.Y.), *aff'd* 486 F.2d 1394 (2d Cir. 1973); *Dale Metals v KIWA*, 442 F.Supp.78 (SDNY 1977); *Morrie Mages v Thrifty Corporation*, 916 F.2d 402 (7th Cir. 1990); *Subway Equipment Leasing Corp. v Forte*, 169 F.3d 324 (5th Cir.1999) and in *Harvey v Joyce* 199 F.3d 790 (5th Cir.2000); *Hill, Grimes and Canatxx Energy Ventures v G E Power Systems et al.*, 282 F.3d 343 (5th Circuit 2002). In England, see for example, *Reichhold Norway A.S.A. and another v Goldman Sachs International*, [2000] 1 W.L.R. 173.

⁴⁶ Cf. *ECJ Drouot Assurances S.A. v Consolidated Metallurgical Industries, Protea Assurance and GIE*, *supra* n.30, which employs the criterion of “identical and indissociable interests”; see also para. 19: “there had to be such a degree of identity between the interests of the insurer and the insured that a judgment in relation to one would be *res judicata* for the other”; cf. P. Kaye, *Law Of The European Judgments Convention*, *supra* n.31, p. 2780: “the fundamental underlying criterion for assessment of whether insurer and insured are to be treated as same parties ... is whether they have such identical and indissociable interests as to satisfy the requirements of the efficient administration of justice and avoidance of irreconcilable judgments balanced against fairness to parties without denial of justice through trial”.

Consequently, a full *res judicata* effect of an award to false third parties should be rejected as excessive and thus inappropriate for arbitration. Therefore, an arbitral award should affect the false third parties, in a way that reflects the degree of their association in terms of interests with the parties to the proceedings.

The next section argues for a suitable and thus proportional third-party effect of arbitral awards, which would simultaneously keep intact the principle of due process and accommodate the desirability to regulate the outcomes of the several proceedings arising out of multiparty relationships.

12.3 THE SUGGESTED THIRD-PARTY ARBITRAL EFFECT

The solution suggested here is:

- First, to recognize a third-party effect of an arbitral award, which would be analogous to the association between false third parties and parties to the arbitral proceedings, in terms of interests. This is outlined in this section.
- Second, to recognize this effect as an autonomous, inherent element of international arbitral awards, rather than an effect recognised by national legal systems depending on divergent conditions. This legal basis of the third-party arbitral effect is considered in Section 12.5.

12.3.1. Examination of the Suggested Effect

Chapter 8 established the principle that the procedural relationships between the false third parties and the original parties reflect their association, in terms of substantive interests and liability. Applied to judgments this principle suggests *that the degree of substantive interrelation between a third party and the parties in the proceedings will determine the impact of the ensuing judgment upon the third party*. Indeed, there are examples in the context of litigation showing that while the *res judicata* effect will be only extended to privies, a judgment may produce a different sort of effect upon third parties who, although fall short of privity, are interrelated to the parties in the proceedings.

For example, in the US the *collateral estoppel* effect rather than the *res judicata* one may apply to a wider circle of third parties, not just privies to the parties in the

action.⁴⁷ It should be noted that *collateral estoppel* relates only to the preclusive effect of a judgment, and it has thus narrower effect than *res judicata*, which, as explained above, also relates to prohibition of reassertion, the conclusive effect and the enforcement of a judgment. Thus, a kind of more limited effect of a national judgment (*collateral estoppel*), than the drastic *res judicata*, is extended to a wider circle of third parties that are simply interrelated rather than identified with the parties in action. Indeed, it seems that the U.S. courts, due to the abandonment of the requirement of mutuality with regard to *collateral estoppel*, have greatly expanded the applicability of *collateral estoppel* to third parties in civil cases.⁴⁸ They have also extended the right of third parties to a prior litigation to assert both offensive and defensive *collateral estoppel* in a subsequent action against a person who was a party in the prior case.⁴⁹ Thus, a third party, either as a claimant or as a defendant in subsequent proceedings may rely on an issue determined in a first judgment against one of the real parties (third-party preclusive effect).⁵⁰

Similarly, civil law jurisdictions recognise a kind of third-party effect that is different from that of *res judicata*. Indeed, in principle, a judgment may have an impact which is weaker than that of *res judicata* upon third parties whose interests are interrelated but not identical to those of the parties in the proceedings.⁵¹ This effect is

⁴⁷ *Blonder-Tongue Laboratories, Inc. v University of Illinois Foundation*, 402 U.S. 313, 329 (1971), *on remand*, 334 F.Supp. 2d 47 (N.D.Ill.1971), *aff'd*, 465 F.2d 380 (7th Cir. 1972), *cert. den.*, 409 U.S. 1061, (1972); *Parklane Hosiery v Shore*, 439 U.S. 322 (1979). In contrast, English law remains firm on the doctrine of mutuality. Hence, any preclusive effect requires that both parties have taken part in both proceedings in the same right. See, however, Lord Denning's attempt to change this view in *McIlkenny v Chief Constable of the West Midlands*, [1980] QB283, 317 (CA): "If a decision has been given *against* a man on the identical issue arising in previous proceedings - and he had full and fair opportunity of defending himself in it - then he is estopped from contesting it again in subsequent proceedings" (*contra* Goff L.J. and Sir George Baker). The mutuality principle was confirmed by the House of Lords in *Hunter v Chief Constable of the West Midlands*, [1982] AC 529 (HL); in *Carl Zeiss*, *supra* note 12, and the recent *Sun Life Insurance Company of Canada v The Lincoln National Life Insurance Company*, [2004] 1 Lloyd's Rep.606.

⁴⁸ See Restatement, *supra* n. 9, Reporter's note, para. 29; Semmel, *supra* n.27, p.1457.

⁴⁹ Restatement, *supra* n.9, Reporter's note, para. 29.

⁵⁰ However, the converse does not apply, so that the real party may not use against a third party a judgment issued in proceedings where the former did take part but the latter did not. See *DeWitt v Hall*, 225 N.E.2d 195 (1967); *Bernhard v Bank of America Nat'l Sav. & Trust Ass'n*, 122 P.2d 892 (1942); *Blonder-Tongue Laboratories v University of Illinois Foundation* 402 U.S. 313 (1971).

⁵¹ See, e.g., the French NCPC, art. 581 and *cf.* art.1481 for arbitration: they provide for "tierce opposition," a means by which a third party may attack a judgment, that just affects the third party rather than binding it with a *res judicata* effect. The effect may prejudice the interests of the third party. See Dalloz, Art. 583, para.7 for those parties that may use the "tierce opposition": only those that are neither parties to the proceedings not represented by the real parties. *Cf.* Civ.2e, 16 May 1973, *Bull. Civ. II*, No. 165. However, it should be noted that the "tierce opposition" is not applicable in the context of international arbitration: see NCPC art.1507. See also A. Mourre, *supra* n. 32, p.104. A similar means of recourse available to third parties against a judgment made

more like an adverse effect or a prejudice *vis-à-vis* third parties rather than a full extension of *res judicata*. It usually requires previous notice of the proceedings to the third party, which, if it does not intervene in the ongoing proceedings between the real parties, loses the right of recourse against the judgment. Also, the final judgment will be enforced by or against the third party. Nevertheless, again the same pattern applies: a kind of more limited effect of a national judgment, than the drastic *res judicata*, is extended to a wider circle of third parties that are simply interrelated rather than identified with the parties in action.

Thus this conclusion is in line with the general principle that *the degree of a substantive interrelation between a third party and the parties in the proceedings determines the impact of the judgment upon the third party*. This conclusion can be verified by way of cautious analogy to *lis pendens* too.⁵²

For example, the European Regulation 44/2001 sets out the following *litispendens* mechanism:

- Article 27 provides that when two different courts are seized of the same subject matter, the court seized of the second case must stay and, after the jurisdiction of the first court is established, decline jurisdiction on its own motion. In other words, it provides for the *litispendens* effect of the first set of proceedings upon the second one. In order to operate, Article 27 requires that the parties in the parallel proceedings be the same or that they be third parties that share a substantial degree of identification with them, and that the two claims in question almost coincide.
- Article 28, on the other hand, provides for the situation where the two parallel proceedings are not identical but merely similar⁵³ both in terms of the subject matter and in terms of the parties. Thus, there is no need for the parties in the second set of proceedings to be substantially identified, in terms of interest, with the parties in the first. Even substantially different third parties in the second set may be subject to the *litispendens* effect of the first set. It is enough that the third party in the second set and one of the parties in the first set are contractually

between two other persons is also provided in the Greek Code of Civil Procedure, art.92 and art. 583 *et seq* (where again a third party may attack a judgment by which it is not bound by *res judicata*).

⁵² Here, the focus is on the impact of a set of proceedings (*lis pendens*) rather than that of a judgment (*res judicata*) vis-à-vis third parties.

⁵³ *I.e.*, “closely connected.”

intertwined and have, thus, interrelated interests. However, the consequences in Article 28 are different: the court, on the application of one of the parties, has mere discretion, rather than an *ex officio* obligation, to stay⁵⁴ the proceedings.⁵⁵

It follows that for Article 27 to apply the threshold requirement of a substantive degree of identity is high and the resulting *litispendens* effect is accordingly drastic: an *ex officio* duty to decline jurisdiction. However, for Article 28 to apply the threshold requirement of similar, rather than identical proceedings, is lower and the *litispendens* effect is accordingly less drastic: the mere discretion to stay the proceedings on application of one of the parties. In this way, the Regulation provides for a different kind of *litispendens* effect depending on the degree of substantive identification of the two cases and the parties.

In the light of the above analysis, it is submitted that the following third-party effect mechanism can be considered in respect of either a set of proceedings (judicial or arbitral) or a decision (judicial or arbitral):

- Looser conditions (looser identity / contractually intertwined parties) → less drastic effect
- Strict identity of parties + claim → more drastic effect

This system may also apply to arbitration: the degree of substantive association between a genuine and a party to an arbitration should determine the intensity of the arbitral effect upon the third party, that is, the extent of procedural repercussions for the third party. Thus, where third parties share a great degree of substantive identification with genuine parties an arbitral award should produce a full *res judicata* effect vis-à-vis the third parties. This is the case with privies where their interests are almost identical to those of the parties in action, and therefore a full extension of the arbitral effect to the privies is justified. However, where the parties in the proceedings and the third parties are interrelated rather than identified in terms of interests, as in the case of false third parties, an arbitral award should still have an impact upon the “false third party,” but, this time, a lesser one.

⁵⁴ Or decline only in case the stricter conditions of Reg. art. 28(2) apply.

⁵⁵ Substantive interrelation has procedural repercussions also in the case of the common-law rules of *Forum Non Conveniens*: the courts in exercising their discretion to decline jurisdiction should take into account the existence of proceedings abroad that are substantively connected to the proceedings. In England, see P. Kaye, *Civil Jurisdiction And Enforcement Of Foreign Judgments*, (1987), p. 1233-1234.

12.3.2 Characteristics of the Third-Party Arbitral Effect- Distinction from *Res Judicata*

The suggested third-party effect of an arbitral award should be clearly distinguished from the *res judicata* effect, which is particularly drastic and linked to the enforceability of the award. In particular, the third-party arbitral effect should not include:

1. *A prohibition against reassertion*: The first arbitral proceedings between the genuine parties have a different subject matter from that of the proceedings between a false third party and one of the genuine parties. Thus, the false third party will not be prohibited from bringing his claim against a genuine party, and vice versa, before a different tribunal or national court. The first arbitral award will not extinguish the claim of the false third party. It falls outside the jurisdiction of the first tribunal to decide on a false third party's claim that it is not the subject matter of the arbitration.

2. *The enforceability effect*: The first award cannot be enforced by or against the false third party. A second trial is indispensable for the false third party's claim to be determined. Any claim or objection with regard to the false third party should be the subject matter of a new trial and a new decision, which, in turn, would be enforceable by or against the false third party. Otherwise, the extension of the enforceable effect of the award against a third party would clearly violate the due process principle. The parties bound by an arbitration agreement should coincide with those bound by the ensuing arbitral award. Since an arbitration agreement cannot and should not be enforced by or against any third party,⁵⁶ neither should the ensuing arbitral award be enforced by or against this false third party.

However, an arbitral award should produce both a conclusive and preclusive effect vis-à-vis the false third party.⁵⁷ This kind of double effect is a necessary corollary of the strong contractual interrelation typically found between genuine and false third parties. Due to this substantive proximity, it is most likely that the second proceedings would have to examine factual and legal issues already examined and determined by the first award. Thus, the preclusive effect of the first award should prevent any re-litigation of these issues, while the conclusive effect would provide the logical and legal basis for the second forum to reach a decision in accordance with the determination of the first arbitral award. Applied in this way, the combined arbitral

⁵⁶ See discussion in Chapter 6 and 7 above.

⁵⁷ In the sense in which they have been explained above in Section 12.1.2.2

effect will harmonise the legal and factual ground of the multiparty relationship and will ensure that any contradictory result is avoided.

More particularly the arbitral third-party effect should cover:

- *Both legal and factual issues determined in the first arbitral proceedings:* As has already been mentioned, most civil-law jurisdictions do not extend the *res judicata* effect to facts on the ground that a judgment or an award is inherently fallible and thus can never completely determine the truth. However, the conclusiveness of a decision stems precisely from the concession that courts and tribunals are not infallible. Decisions “. . . are not final because [they] are infallible but [they] are infallible only because [they] are final.”⁵⁸ Decisions are agents of justice rather than the truth. The law of *res judicata* is a “convention designed to compensate for man’s incomplete knowledge and strong tendency to quarrel.”⁵⁹ Thus, any conclusive effect of a determination in a decision effectively constitutes a convention: although the decision may, by nature, be fallible, all issues, factual as well as legal, must, at some point, be finally determined, infallibly or not, so that the dispute is eventually laid to rest.⁶⁰ For this reason, the suggested effect of an arbitral award should include legal issues as well as facts.⁶¹ Moreover, distinguishing between factual legal issues would be wrong in practical terms, since it is, on many occasions, too difficult to separate facts from law.⁶²
- *All issues that are common in both proceedings:* As explained, it is likely that issues examined and finally determined in the first award will arise in the second proceedings. This legal and factual ground, common to both proceedings, should be subject to the preclusive and conclusive effect of the first award. All determinations that can be clearly inferred from the first award, regarding issues that have been examined, proved and authoritatively

⁵⁸ *Brown v Allen*, 344 U.S. 443, 540 (1953) (Jackson, J. concurring).

⁵⁹ Restatement (Second) Judgments, *supra* n.9, Ch.1, Introduction.

⁶⁰ *Idem*, “The law of *res judicata* cumulatively reinforces the authoritativeness of the law itself” and “compels repose.” *See also id.*, “The rules of *res judicata* in modern procedure . . . may fairly be characterized as illiberal toward the opportunity for relitigation” and this applies to the re-litigation of either claims or a facts.

⁶¹ Cf the ILA Final Report and Res.1/2006, *supra* n.1, suggesting that “a more extensive notion of *res judicata* than is known in civil law jurisdictions in relation to issue estoppel, as in Recommendation 4.2” should be adopted in arbitration.

⁶² There are cases where factual and legal issues are inextricably tied up. *See idem* para. 28, referring to “genuinely mixed issues of fact and law”.

determined, should not be re-litigated. It should be noted, however, that preclusion of re-litigation should be hinged on the condition that the issue in question before the second forum must have been *essential* for the first award, in the sense that the relevant issue directly supports the operative part of the award.⁶³

12.3.3 Requirements of the Arbitral Effect

The following conditions are required for the effect to apply:

- *A contractually intertwined multiparty relationship*, with closely interwoven rights and duties, arising out of common factual circumstances. These multiparty cases cannot be exhaustively determined *a priori*. There is a need for an *ad hoc* investigation, depending on the specific facts at hand. However, in general the third party effect should apply to the two groups of false third parties determined in Chapter 2.
- *Jurisdictional fragmentation of this relationship*, where some of the several parties to the multiparty relationship have agreed on arbitration whereas others have agreed on litigation or a different arbitration.
- *A valid arbitral award*, resulting from proceedings between two of the several parties involved in the multiparty relationship.⁶⁴
- *Previous invitation to the false third party to join the first arbitral proceedings*. As argued above the tribunal only in exceptional circumstances should be able to assume jurisdiction over a false third party,⁶⁵ without the general consent of all the parties involved in the proceedings and the false third party. In any case, though, an arbitrator faced with an intertwined multiparty relationship should assume the initiative and suggest to the parties the joinder of a false third party. If all the parties agree that the false third party should be joined to the proceedings, then the proceedings should go on as multiparty. If however, one of the parties to the proceedings or the false third party rejects the joinder then

⁶³ Cf. Hanotiau, *supra* note 1 paras. 34-35. This is also required in litigation. See, e.g., the English case *Carl Zeiss*, *supra* note 12; in the U.S. cf. Restatement, *supra* note 9, para. 27 and *Bahler v Fletcher*, 474 P.2d 329,338 (Ore. 1970), holding that collateral estoppel applies only to those issues that have “necessarily been decided in the prior action and [are] decisive of the present action.” This principle is applied in civil law as well, where *obiter dicta* are not covered by *res judicata*. See, for example in Greece, AΠ 1366/1996, (1997) *ΕΛΛΑΔΗ*, 1785.

⁶⁴ All arbitral awards, in principle, are presumed valid and enforceable in accordance with the N.Y. Convention unless they are proved otherwise.

⁶⁵ See Ch. 11 above, exceptional circumstances will be when false third party and a genuine party to an arbitration agreement are co-liable.

multiparty proceedings will not be possible. In this case, the third-party effect of the arbitral award will arise and will apply, particularly, to the party that rejected the joinder.

- *A second set of arbitral or judicial proceedings*, between one of the genuine parties to the first arbitration and a false third party. Here the role of the second tribunal or court becomes crucial. The latter should make an in-depth analysis of the contractual relationship in question and determine whether, and to what extent, it is intertwined with the subject matter of the first award. In a case where the subject matter of the award and that of the pending proceedings are, indeed, closely interwoven, the second forum should refuse to re-examine issues determined in the award (preclusive effect) and accept the determination therein of these issues as conclusive (conclusive effect). This is of particular importance where the first award has undergone a fact-finding procedure, the result of which can be deduced from the award.⁶⁶ The use of different standards of proof or different evidentiary procedures by the tribunal should not be taken as an argument against the third-party effect of the award, as long as the arbitral proceedings met the standards of due process.⁶⁷
- *Discretionary application by the courts or tribunals*: the decision on the third-party effect rests in the discretion of the second tribunal or court, which should exercise this discretion taking into account all the relevant factors and the competing interests.
- *Relief from the effect*: A false third party should be given the opportunity to obtain relief from the conclusive effect of an arbitral award in case of fraud or collusion between the original parties.⁶⁸ In such a case the award cannot be determinative. Therefore, the second forum should ignore it and make a fresh examination of common ground between the two proceedings.⁶⁹

⁶⁶ It is true, however, that awards are not always particularly detailed, making any inference difficult. See Shell, *supra* n.5 at 660.

⁶⁷ Under the N.Y. Convention scheme, once the award is issued, it is presumed to meet due process standards. The due process requirement, in the context of international arbitration, is determined by international standards rather than by procedural technicalities of national laws. See J. Lew, L. Mistelis and S. Kroell, *Comparative International Commercial Arbitration*, (Kluwer Law International 2003), para. 28-80 *et seq*; cf. Semmel, *supra* n.27, p. 1469.

⁶⁸ Cf. also Restatement, *supra* n. 9, Ch.5.

⁶⁹ The burden of proving the fraud or collusion would lie upon the third party according to the fundamental procedural rule that each party should prove the facts upon which it relies. See Lew-Mistelis- Kroell, *supra* n.67, para. 22-25.

12.3.4 The Parties Affected

While *res judicata* regulates the relations between the original parties to proceedings, the third-party effect refers to the relations of the genuine parties with a false third party. There are two occasions on which the relevance of the third-party effect could arise:

1) The effect can be relied upon by a false third party in a second set of proceedings against one of the genuine parties acting either as claimant or as a defendant. Take, for example, the case of a secured transaction where a surety has guaranteed the performance of a seller. In the first arbitration between the seller and the buyer, the seller is awarded the full price of goods sold and delivered. This award necessarily includes an implied decision that the goods involved were of the quality specified in the sales contract. This determination of the award should be conclusive on the buyer in the event of a second trial against the surety. This is a straightforward application of the third-party effect and should not create any theoretical difficulties. The genuine party had a full day in court, where he had the opportunity to present his arguments and defend his legal position.⁷⁰ Any inconvenience caused to the genuine party should yield before the need for an effective arbitral award that would harmonise the jurisdictionally fragmented multiparty relationship and prevent conflicting decisions.⁷¹ This is accepted in some national procedural systems with regard to the binding effect of national judgments,⁷² while it has also been accepted and applied in some arbitral cases.⁷³

2) The converse situation, however, calls for a more careful analysis of the competing interests. The question that arises here is whether the genuine party should rely on issues determined by the arbitral award against a false third party. What is

⁷⁰ Cf. Lord Denning in *McIlkenny v Chief Constable of the West Midlands*, [1980] QB 283, 317 (CA): "If a decision has been given against a man on the identical issue arising in previous proceedings - and he had full and fair opportunity of defending himself in it - then he is estopped from contesting it again in subsequent proceedings"

⁷¹ There is authority suggesting that we should distinguish between the case where the party in the first set of proceedings is claimant in the second set and the case where it is defendant. According to this view we should accept the preclusive effect of the first decision against the claimant in the former case, but we should reject it in the latter, on the ground that it would be unfair to establish liability for the defendant in this way. See Cunningham, *supra* n. 28 at 530 and case law therein. However, the fact that the party in the first proceedings has been given a fair and full opportunity to litigate should be enough, whether it acts as claimant or as defendant in the second proceedings. See *Parklane Hosiery v Shore*, 439 U.S.322 (1979), *Popp v Eberlein*, 409 F.2d 309 (7th Cir. 1969), *cert denied*, 396 U.S. 909 (1969).

⁷² This is the case particularly in the U.S., where the mutuality requirement has been abandoned.

⁷³ See *Blumberg v Berland*, 678 F.2d 1068 (11th Cir. 1982); *Sports Factory v Chanoff*, 586 F.Supp. 342 (E.D. Pa 1984); cf. Shell, *supra* n. 5, p. 667-668.

really at stake in this case is the fundamental⁷⁴ due process right of the third party to present his case. The general rule is that only parties that have taken part in the proceedings should be bound by the ensuing award. However, even if the suggested third-party effect is applied against the genuine party due process is duly observed, since:

- First, as mentioned above, an arbitrator faced with an intertwined multiparty relationship should assume the initiative and suggest to the parties the joinder of the false third party. Thus, on the condition that the latter was invited and refused to join the arbitral proceedings between the genuine parties thereto, the false third party should not be able to challenge the factual and legal issues determined in the first award, and which will then arise in the second set of proceedings. An opportunity for a party to be heard in the proceedings is enough to meet the due process standards.⁷⁵ A party that wastes this opportunity, standing by and choosing the wait-and-see tactic, should have to accept any adverse consequence arising from such tactic. This is a principle that can be found in different legal systems.⁷⁶
- Second, after the award is rendered, the false third party is given the means to obtain relief from the conclusive effect of the award in the case of fraud or collusion by the original parties.⁷⁷

The false third party thus is not left without recourse against a third-party arbitral effect. On the contrary, it is given a twofold “protection” which safeguards its right to be heard: the pre-award invitation to join and the post-award possibility of obtaining relief.

In any case, there is a fundamental difference between the case where a third party *is bound* by an award and the case where he is merely *affected* by an award. In the former case the full effect of an award -in the sense of *res judicata*- is extended to the third party. In contrast, in the case of the suggested third-party arbitral effect, the third party is merely *affected* rather than bound by the award. The effect does not pre-empt any of the false third party’s rights or duties. In fact, the award has not authority to

⁷⁴ See in the U.S., *Blonder-Tongue Laboratories v University of Illinois Foundation*, 402 U.S. 313, 329, (1971) and Restatement, *supra* n. 9, para. 34.

⁷⁵ Cf. Lew- Mistelis- Kroell, *supra* n. 67, para 26-86.

⁷⁶ See, e.g., the *Henderson v Henderson* principle of abuse of process, *supra* n.20, or Semmel, *supra* n. 27, p.1474-77 and Cunningham, *supra* n. 29, p.526.

⁷⁷ Cf. also Restatement, *supra* n. 9, para.75.

refer to the false third party at all: if it does so, it will exceed its jurisdiction. The award may only refer to factual and legal issues which relate to the genuine parties. However, since all parties, genuine and false third, are involved in the same contractual multiparty relationship, it is very likely that the false third party's legal position is, to some extent, affected by the determination of the award between the two genuine parties. The factual and legal issues common in both sets of proceedings should be determined only once, binding all the relevant parties. This comes as a logical corollary of the inextricable interrelation between the several parties rather than an argument against the third-party effect.

It should also be noted that a false third party is not a contingent stranger to the genuine parties. It becomes contractually involved in a multiparty situation, which it necessarily accepts in the first place. A surety, for example, accepts the risk that a debtor may fail to perform and activate its own liability. Parties are aware of the commercial and thus legal implications of a multiparty business relationship.

Finally, the burden of proving that the issue in question in the second action is identical to the issue which has been determined in the first will lie with the real party. This can prove a difficult burden to discharge, especially in those not infrequent arbitration cases where the awards are written in a concise form, avoiding disclosure of detail on the matters determined.⁷⁸ This burden may, thus, to some extent mitigate any inconvenience caused to the false third party.⁷⁹

The above sets out an adequate protective framework for a false third party that would justify the use of the effect even against it. Thus, extending the secured transaction example, if an award finds that the quality of the goods was not as agreed, this determination should also be opposed by the buyer against the surety in subsequent proceedings. A second example is that of a construction dispute between an employer and a contractor, where the award, based on a meticulous fact-finding process involving several experts, witnesses, onsite inspections etc, finds that the work actually carried out is defective. There should be no valid reason for this authoritative determination not to constitute the basis of subsequent proceedings between the contractor and the subcontractor.

It is not suggested here that the first award should be conclusive of the subcontractor's liability. This would not, in any event, be possible since the

⁷⁸ See *supra* n. 66.

⁷⁹ See Cunningham, *supra* n. 29, n. 55; *contra* Semmel, *supra* n. 27, p. 665.

subcontractor's liability would fall outside the subject matter of the first arbitration. Only factual and legal issues common to both proceedings should be covered by the third-party effect. The subcontractor's liability could not arise, let alone determined, in the proceedings between the employer and the contractor. This is an issue that falls exclusively under the jurisdiction of a second set of proceedings between the contractor and the subcontractor, during which the latter will have the opportunity to make use of any personal defense vis-à-vis the contractor and, possibly, escape liability in accordance with the terms of the subcontract. The first tribunal, however, has the exclusive jurisdiction to determine whether the contractor was liable or not, a determination which, as a legal and logical necessity, presupposes the determination of whether the work actually performed by the subcontractor was defective.

12.4. THE LEGAL BASIS OF THE EFFECT OF AN INTERNATIONAL AWARD

This section makes a tentative rather than an exhaustive suggestion as to the legal basis of the effect of an arbitral award, which suggestion is not necessarily limited to the third-party arbitral effect. In fact, it extends beyond this to the legal basis of the effect of international arbitral awards in general.

As has been mentioned above, the international arbitration framework lacks a harmonised regulation of the effect of an international award. Instead, different national regimes result in a confusing divergence in this respect. This falls short of the unparalleled uniformity that the New York Convention has established with regard to the enforcement of international arbitral awards.

The New York Convention abolished national technicalities and created a self-regulated international arena where arbitral awards have achieved independence from national regimes. The validity and enforceability of an international award are generally examined in accordance with uniform and international standards established by the Convention, rather than national standards set out in domestic legislation. This policy has promoted equality and predictability in international business, and has enhanced the effectiveness of the arbitral award as a means of international dispute resolution.

This unrivalled success of the New York Convention has strengthened the argument in favor of de-nationalisation of international arbitration. Thus, harmonised

a-national procedural⁸⁰ and substantive⁸¹ standards develop and become more relevant in international arbitration than ever before. In fact, one of the few aspects of international arbitration that remains in the exclusive domain of national jurisdictions is the regulation of the effect of an arbitral award. The practice whereby an arbitral award is equated to a national judgment in terms of its effect causes unpredictability and undermines the effectiveness of the international award. Thus, the effects of an international arbitral award depend on the different, and, in many cases conflicting, regulations of the different national jurisdictions. For example, an international award between a creditor and a debtor, depending on which jurisdiction will be enforced:

- May have no effect vis-à-vis a surety;⁸² or
- May be *res judicata* vis-à-vis a surety, in a case where it is favorable to the debtor, but not in a case in which it is favorable to the creditor;⁸³ or
- May be used as *prima facie* evidence vis-à-vis a surety.⁸⁴

Because of the lack of international regulation on the effects of arbitration awards, the international status of an arbitration award disappears after it is recognised and enters the national jurisdiction. Thus, the harmonised effects of the New York Convention do not extend further than the conditions for the recognition of an international arbitral award. This, however, is in conflict with the spirit of the Convention, which has created an international arena where the enforcement and, thus, the free movement of awards is facilitated.⁸⁵ It follows that enforceable awards

⁸⁰ The fundamental principles of “due process” and “fair hearing” constitute basically the unified procedural principles in international arbitration. See Lew-Mistelis-Kroell, *supra* n. 67, para. 5-68 *et seq.* See also Alex Baum, “International Arbitration: the Path toward Uniform Procedures”, in *Global Reflections On International Law, Commerce And Dispute Resolution, Liber Amicorum In Honor Of Robert Briner* (Gerald Aksen et al. eds., ICC pub. No. 693, 2005), p.51.

⁸¹ E.g. the application of *lex mercatoria* or international sets of rules such as the INCOTERMS, UCP, UNIDROIT principles etc. See in general Lew-Mistelis-Kroell, *supra* n. 67, para.18-41 *et seq.*

⁸² This will be the case in England for example, See *Re Kitchin, exp Young*, (1881) 19 ChD 668 and *Bruns v Colocotronis* (The “Vasso”), [1979] 2 Lloyd’s Rep 412, (Commercial Court).

⁸³ This will be the case, for example, in Greece: see Greek Code of Civil Procedure, arts. 896 and 328.

⁸⁴ This will be the case, for example, in the US: *Norris v Mersereau*, 74 Mich 687, 690; 42 NW 153 (1889); *Sauer v Detroit Fidelity & Surety Co*, 237 Mich 697, 702; 213 NW 98; 51 ALR 1485 (1927); *Kent Probate Judge v American Employers Insurance Co*, 283 Mich 328, 334-335; 278 NW 85 (1938); *PR Post Corporation v Maryland Casualty Company*, 68 Mich. App. 182; 242 N.W.2d 62 (Mich. App.1976) where it was held that the award will have be used as “prima facie” evidence against a third party (surety). See also the cases *Fidelity and Deposit v Parsons & Whittemore Contractors*, 48 N.Y.2d 127 (N.Y. 1979) and *Madawick Contracting v Travelers Insurance Company*, 307 N.Y. 111; 120 N.E.2d 520 (N.Y.1954) where it was held that the award between the contractor and the subcontractor is binding upon the surety with regard to the issue of the subcontractor’s liability, which should not be re-litigated in a later suit of the contractor against the surety.

⁸⁵ Cf. Lew-Mistelis-Kroell, *supra* n. 67, para. 26-36.

should obtain the maximum degree of effectiveness within the international arena. Allowing divergent regulation of the arbitral effect by national systems reduces the effectiveness of the international award and hampers the free movement of international awards.

National states are reluctant to relinquish their right to control and regulate the effects of a judgment or an award, the consequences of which are “felt” within their own jurisdiction. This may be a reasonable argument as far as national judgments are concerned, where enforcement is effected by divergent domestic standards rather than by reference to uniform standards determined by an international convention such as the New York Convention. Allowing foreign judgments, from several different jurisdictions to carry their own national status and effect into the country of enforcement, would cause chaotic divergence and uncertainty. It is necessary, therefore, that the enforcing country should regulate and determine the effects of foreign judgments, assimilating their effects with those of domestic judgments.⁸⁶

The argument, however, is less persuasive in the context of international arbitration. An international arbitration, by definition, has no national forum. Thus, the arbitral award is not the product of a particular national legal system, and, in any case, the seat of arbitration bears no relation to the effect of an arbitral award. An international arbitral award does not carry any national *res judicata* status. It is “given” the status of *res judicata* only after it enters national jurisdictions. It seems contradictory that an international award rendered and recognised exclusively according to international standards should be given a national status with regard to its conclusiveness and effect. Instead, international awards should have an international harmonised effect, designed for the particular needs of international arbitration, an effect which an arbitral award should carry into national jurisdictions. There should be a shift from a national to an international viewpoint as regards the effects of arbitral awards. National jurisdictions should retain, as a safety net, the right to reject the effect only if this violates the international public policy of the

⁸⁶ See Restatement, *supra* n. 9, para. 98. See also *Panama Processes v Cities Service*, 796 P.2d 276 (Okla. 1990): in enforcing a Brazilian judgment, the U.S. courts decided to apply their domestic law of *res judicata* as opposed to Brazilian law. Cf. *McCord v Jet Spray*, 847 F.Supp. 436 (D.Mas.1994), assuming that the Belgian concept of *res judicata* was comparable to the American concept the U.S. court concluded that it would recognize the judgment with the conclusive power that it would have under Belgian law. See also Berti, *supra* n. 8, Art. 194, para 134 *et seq*: Swiss law also applies *res judicata* to a foreign arbitral award to the extent that the law of the country in which the award was made, would recognize that award. On the other hand, these effects could not go beyond those who the award would have if it were a Swiss award made in Switzerland.

country in question. This, in fact, is the real scope of the N.Y. Convention, Article V(2)(b). Enforcement is the judicial process that gives effect to the mandate of the award.⁸⁷ In other words, enforcement is the vehicle by which the effects of the award are transplanted to the enforcement country. In cases where the courts of the enforcement country consider that the effects of the award to be enforced manifestly violate its public policy, they will not allow the enforcement process to proceed. Thus, the New York Convention, in Article V(2) (b), determines the boundaries of the legitimate authority of the national state over an international award regarding the effects of the award. The national state has, indeed, a legitimate interest in reviewing, rather than determining as a whole, the effects of an international award. The legitimacy of this interest, however, is strictly related to public policy considerations and cannot be extended beyond public policy boundaries.

12.5. CONCLUSION

The purpose of this Chapter has been to show that the technical mechanism of *res judicata* recognised in relation to national judgments is not always suitable for international awards. The principal argument outlined here has been that the arbitral award should produce a third-party effect, which differs from the *res judicata* effect, and is designed for the needs of international arbitration. The content and boundaries of this third-party effect, as well as the conditions of its application have also been considered here. Finally, a tentative suggestion as to the legal basis of the arbitral effect, in general, has been made. The suggested third-party effect of an international arbitral award strikes a satisfactory compromise between the several conflicting interests:

- It accommodates the problems arising out of multiparty contractual relationships in the context of international arbitration.
- It reduces the chances of conflicting awards.
- It is consistent with the principle of party autonomy.
- It is flexible, giving the courts and tribunals the discretion to recognise a third-party effect, on a case by a case basis.
- It promotes the efficiency of international commercial arbitration.

⁸⁷ See Lew, Mistelis and Kroell, *supra* n. 67, para 26-12.

This is not to suggest that the proposal is ideal. The problems arising out of the relationship between arbitration and third parties are arguably the most complicated and delicate problems in the area of international arbitration. On many occasions the scholar or the practitioner finds himself in a “catch-22” situation. On the one hand, bringing all the parties in a multiparty situation before a common arbitral forum may violate the fundamental principle of procedural party autonomy. On the other hand, allowing the several parties to bring overlapping claims before different fora leaves the door open for conflicting decisions.

This may undermine the effectiveness of international arbitration and frustrate parties’ expectations. The suggestion lying behind this Chapter is that the problems of a multiparty situation may be addressed more effectively by the arbitral award than by an arbitration agreement. In other words, in international arbitration, unlike litigation, the necessary harmonisation of parallel proceedings may be achieved more effectively at the stage after the first award is issued rather than at the stage of the hearings.

CONCLUSIONS

The purpose of this study was to examine the role of third parties in relation to arbitration. The result produced from this work was twofold: first, existing views on the topic were challenged; secondly, some new suggestions were made.

REMARKS ON EXISTING VIEWS ON ARBITRATION AND THIRD PARTIES

Arbitration and third parties is one of the most frequently discussed subjects in arbitration literature and practice. However, as the thesis showed, in spite of the extensive literature the discussion on the topic has been incomplete and it has not yielded general solutions.

To begin with, attention has been focused exclusively on the effect of arbitration agreements upon third parties, whereas the effect of arbitral awards upon third parties has been largely understudied. Moreover, even with regard to the effect of arbitration agreements, the discussion remained limited to a contractual approach, focusing merely on issues of “signature” and “evidence of consent”.

Within this contractual approach two different views have been adopted. According to the first, arbitration agreements cannot have any impact whatsoever on any person, who has not clearly consented to arbitration, as this consent is evidenced by his signature. According to the second, taken by what is known as “extension doctrines”, it is possible under certain conditions for non-signatories to enter into an arbitration agreement, notwithstanding their failure to sign it. However, as the thesis demonstrated, neither of the above views succeeds in giving satisfactory answers to the problem of arbitration agreements and third parties.

The first view, by treating all persons who have not signed an arbitration agreement as total strangers to the arbitration process, contravenes commercial reality. Very often, modern international transactions require the participation of several persons for the delivery of large-scale projects. All persons participating in a multiparty project will naturally have invested financial interests therein. Therefore, any dispute arising in the context of this project will most likely affect their legal position, even when the dispute arises between two other persons which take part in the same project and which are exclusively bound by a bilateral arbitration agreement.

As the thesis illustrated in Chapter 8, even persons who have not agreed to an arbitration agreement might have a legitimate interest in participating in the arbitration proceedings. Likewise, it was showed that the interests of parties to an arbitration agreement might be better protected if third parties with an interest in the dispute could somehow participate in the arbitration process.

Consequently, it was argued that in order to achieve its maximum effectiveness as a dispute resolution mechanism arbitration must find ways to communicate with third parties that sustain strong interests in the dispute pending before an arbitral tribunal. The complexity of contemporary commerce can be better served by flexible rather than exclusive dispute resolution systems. In the context of multiparty relationships this would require that when a dispute between two parties to an arbitration agreement has implications for third parties, the latter should be take into account in the arbitration between the two original parties, rather than be treated as total strangers.

By contrast, the second view acknowledges this last point. What the thesis has named “extension doctrines”, such as the ‘equitable estoppel’ and the ‘group of companies’ doctrine, argue for the ‘extension’ of arbitration agreements to non-signatories. The thesis demonstrated in Part II the theoretical and practical limitations of the extension doctrines. As was explained there, the theoretical premise of the extension doctrines is that consent to arbitrate is not necessarily evidenced by signature. Therefore, in the context of multiparty projects arbitration agreements may bind persons involved in the project, even if they have failed to sign this arbitration agreement.

In essence, the extension doctrines have been developed and employed to facilitate deduction of implied consent to arbitrate. Thus, intention of the non-signatory party to arbitrate can be more easily inferred in the context of the ‘equitable estoppel’ or the ‘group of companies’ doctrines. In some cases, the ‘group of companies’ doctrine has even gone as far as setting presumptions for the existence of consent: it is enough for a party to prove that several companies constitute an ‘economic unit’ or that the non-signatory company has taken an ‘active role in the negotiation or the performance of the contract containing the arbitration agreement’ to presume consent of the non-signatory party to arbitrate.

However, while it may be correct to argue that consent to arbitrate cannot only be proved by signature or an agreement in writing, it is wrong to suggest that consent to

arbitration agreements should be presumed or ascertained more easily than consent to any other procedural or substantive agreement. As the thesis demonstrated, the question of whether a third party is bound by an arbitration agreement or not *pertains to the validity rather than the scope* of the arbitration agreement. Therefore, the assertion of implied consent requires the application of specific principles and techniques of interpretation which must reveal the “intention to arbitrate” with a degree of certainty rather than probability. In this interpretation process, the principle of *in favorem validitatis* cannot apply. There can be no presumption in favour of the validity of an arbitration agreement, and therefore, no presumption in favour of the existence of an intention to arbitrate. Analysis of the relevant case law showed that, in many cases, courts and tribunals *have misapplied the principle of consent* by wrongfully accepting presumptions for the existence of an intention to arbitrate on the part of a non-signatory, and, therefore, accepting presumptions in favour of the validity of arbitration agreements.

In fact, there is an inherent contradiction in all extension doctrines: while they principally adhere to the requirement of consent, they argue at the same time that consent to arbitrate should be more easily inferred or even presumed. This is exactly where the main weakness of these doctrines lies: they focus exclusively on the contractual characteristics of arbitration agreements, and thus necessarily adhere to the requirement of consent. In the context of extension doctrines, the discussion is limited to issues relating ‘consent’ or the law applicable to validity of an arbitration agreement. A strict contractual approach to arbitration agreements is adopted, and thus the latter are examined only as ordinary contracts.

However, under this strict contractual viewpoint, it is difficult to explain why consent of the non-signatories should be more easily ascertained with regard to *arbitration agreements*, as opposed to any other substantive or, indeed, jurisdiction agreement. If attention is focused on the contractual nature of the arbitration agreements, there is nothing that would justify any kind of concession with regard to the requirement of consent for arbitration agreements in particular.

From a contractual point of view, arbitration agreements have clear constraints as any other substantive contract: only those parties that have consented to an arbitration agreement will be bound by this contract. Moreover, consent of the parties has to be deduced in the same way as in any other contract, in accordance with general

principles of contract law and interpretation. The latter provide for no exception to the principle of privity in relation to arbitration agreements. Nor do they provide that consent for arbitration agreements can be ascertained more easily than in the case of other agreement. Thus, the contractual approach to the issue of arbitration agreements and third parties is naturally constrained by the general principles of contract law applicable to any ordinary contract.

Generally, the discussion on arbitration agreements and third parties has failed to pay sufficient attention to the specific characteristics of arbitration agreements, as opposed to ordinary contracts. The theory behind the existing views on arbitration agreements and third parties is related to contract rather than arbitration law.

As regards the effect of an arbitral award upon third parties, the sole viewpoint here equates arbitral awards to national decisions. Consequently, the question of whether an arbitration award may have any sort of impact upon third parties depends on the national provisions regarding *res judicata*, which, as the thesis explained in Chapter 12, largely provide that the *res judicata* effect is strictly limited to the parties in action and their privies. Therefore, as far as an arbitral award is concerned, any person other than the parties in the proceedings or their privies is regarded as a complete stranger.

The thesis challenged this view, showing that equating awards to national judgment overlooks the differences in nature and function between international awards and national decisions. While national procedural systems provide for ways in which third parties can be brought in the proceedings between the original parties, arbitration in general lacks any kind of third-party mechanism.

In this way, arbitration is left without any means of communication with third parties at all: on the one hand, arbitration agreements have no effect upon any third party unless the latter has consented to the arbitration agreement; on the other, arbitral awards obtain the status of national judgments and thus have no effect upon any party that has not taken part in the proceedings.

In sum, the main problem appearing in the existing views on the effect of arbitration agreements and arbitral awards on third parties is that they all adopt an “all or nothing” approach to the topic: “third parties” with a legal or financial interest in a dispute between two genuine arbitration parties are regarded

- Either as *total strangers* to the arbitration between two genuine parties; or

- As “*contractual parties*” to an arbitration agreement between the two original parties, in which case the arbitration agreement and the ensuing arbitral award will be enforceable by and against the third party.

This approach, however, fails to distinguish between the various types of third parties, which exist in the context of modern business practice. It becomes obvious therefore, that a more flexible than the “all or nothing” approach is required in order to accommodate the nuances of commercial reality.

SUGGESTIONS OF THE THESIS ON “ARBITRATION AND THIRD PARTIES”

To address the above problem, the thesis suggested, in Chapter one, that different groups of ‘third parties’ should be identified. More specifically, the notion of “false third parties” was introduced as a group of third parties with a significant legal or financial interest in the dispute between the two genuine parties to an arbitration agreement or to arbitration proceedings.

To begin with, the group of “false third parties” was distinguished from persons such as a principal, an assignee, a consignee and a successor in a contract containing an arbitration agreement. The thesis showed that, although they are some times taken as third parties, the above persons should be considered *genuine parties* to arbitration agreements rather than third parties, since they will be contractually bound by an arbitration agreement by reference to rules of contract law.

Then, the thesis focused on the notion of “false third parties”, in particular, and distinguished between two different groups thereof. The distinction was based on the difference in the degree of association between genuine and false third parties, in terms of contractual interests and liability.

Thus, persons in the first group *are third parties strongly associated* with one of the genuine parties to an arbitration agreement or the arbitration proceedings, in terms of contractual interests and liability. Here, genuine and false third party will typically be *co-liable or co-holders of rights or duties*.

Persons in the second group *are third parties contractually linked but not strongly associated* with one of the genuine parties to an arbitration agreement or the arbitration proceedings, in terms of contractual interests and liability. Here, genuine and false third party will be contractually linked but they will not be sharing the same rights, duties or liability. Either they will be *liable in the alternative or only one of*

them will be liable vis-à-vis the other genuine party. False third parties of this group, as was shown in detail in Chapter 2, will typically include a subcontractor or an architect in the context of several construction contracts; a guarantor in the context of security agreements; a parent or another affiliated company in the context of transactions with a multinational group.

The distinction between these two groups of third parties constituted the basis for the principal suggestions of the thesis on the effect of arbitration agreements and arbitral awards on third parties.

Then the thesis contemplated the effect of arbitration agreements on third parties: as opposed to the contractual approach taken by the extension doctrines, the thesis suggested that a jurisdictional approach should be adopted. It was underlined that arbitration agreements are not like any other substantive contract; they have important jurisdictional effects. As was emphasised throughout the thesis, arbitration law is not, and should not be viewed merely as an advanced version of contract law. Accordingly, as was shown in Chapter Seven, *arbitration has significant jurisdictional implications that go beyond the contractual origins of arbitration and may affect parties other than those consented to an arbitration agreement*. This was illustrated, in Section 7.2 by reference to case law showing that national courts have on several occasions stayed proceedings between a person that is party to an arbitration agreement (genuine party) and a person that is not (third party), on the ground that the action was inextricably involved with the subject matter of that arbitration agreement. This demonstrates that arbitration agreements may, in certain circumstances, have collateral jurisdictional effects to third parties, namely extra-contractual effects. Therefore, it was argued that *arbitral tribunals should, in principle, be able to assume extra-contractual jurisdiction over third parties*.

Here, the important role of the dispute was underlined: arbitral tribunals will assume jurisdiction over third parties, only when this is necessary for them to resolve the dispute effectively. Necessary corollary of the jurisdictional approach adopted by the thesis is the concept of *effective arbitral jurisdiction*, according to which a tribunal should be able to assume as much jurisdiction as is necessary for the tribunal to achieve its main goal, namely the resolution of the pending dispute. Therefore, the jurisdiction of an arbitral tribunal should always be determined in the light of the specific dispute at hand.

The suggestion that arbitral tribunals should in principle be able to assume extra-contractual jurisdiction if this is necessary for the effective resolution of the dispute finds further support, by analogy, in the “extra-territorial jurisdiction” assumed by national courts. Section 7.3 illustrated that despite the fact that their jurisdiction stems from a different source, national courts and arbitral tribunals assume jurisdiction of the same quality. There is no difference between jurisdiction established on a territorial basis (as in the case of national courts) and jurisdiction established on the basis of an agreement (as in the case of arbitral tribunals). Once their power to examine the pending dispute is confirmed by reference to either a valid arbitration agreement or the applicable procedural rules, arbitral tribunals and national courts assume the same jurisdictional duty: to resolve the dispute at hand in the most effective way. Therefore, it was submitted that, since national courts are allowed to assume jurisdiction beyond their territorial boundaries, arbitral tribunals should also be allowed to assume jurisdiction beyond the boundaries of the arbitration agreement as an ordinary contract (extra-contractual jurisdiction). More generally, it was argued that when it is necessary for the determination of the dispute, an adjudicatory forum, be that a national court or an arbitral tribunal, may extend its jurisdiction beyond its original boundaries, be that a state territory or an arbitration contract.

It was accordingly concluded that, in principle, third parties could be brought into play in arbitral proceedings between two genuine parties to an arbitration agreement.

This conclusion is supported by a policy analysis undertaken in Section 8.1, showing that third-party mechanisms allowing the participation of third parties in the arbitral proceedings are important for international arbitration. As was explained there, third-party mechanisms are not incompatible with arbitration. On the contrary, they are necessary for a number of reasons:

- First, to sustain a functional equilibrium between substance and procedure in the context of multiparty commercial relationships;
- Second, to promote efficiency in arbitration by minimizing the risk of irreconcilable awards and judgments, which will frustrate the expectations of the parties in arbitration;
- Third, to serve the interests of, at least, some of the parties to the arbitration.

In sum, the above demonstrated that

- First, as a matter of principle, arbitration agreements may have jurisdictional effects on third parties, which would allow the tribunal to assume extra-contractual jurisdiction over third parties
- Second, that the participation of third parties in arbitration is not necessarily incompatible, in policy terms, with arbitration. On the contrary, in some cases, it may enhance efficiency in arbitration and promote the interests of the parties.

Although it was demonstrated that third-party mechanisms might in principle apply to arbitration, this was not to suggest that the participation of third parties in arbitration should be the norm. On the contrary, it was stressed that, as in the case of extra-territorial jurisdiction in litigation, extra-contractual jurisdiction in arbitration should be accepted only in exceptional circumstances. It was illustrated that the rule in litigation is that jurisdiction is determined on an individual basis, in view of a personal link between a particular defendant and a particular forum (the rule of individually determined jurisdiction). Third-party mechanisms, enabling several parties to come before a single forum, constitute derogation from the rule of individually determined jurisdiction, and therefore they should apply only in exceptional circumstances.

The next step of the thesis aimed at when *should* arbitral tribunals assume extra-contractual jurisdiction and bring third parties in arbitral proceedings. In order to achieve this goal, the thesis sought guidance from national and regional litigation systems regarding the participation of third parties in court proceedings. This comparative study provided useful insight on third-party mechanisms in general. More specifically, it was found that the extent to which a third party may participate in the proceedings between two original parties is directly relevant to the *degree of association between the third party and one of the original parties, in terms of substantive liability and interests*. Here, the rule is, *the closer the substantive association between the original and the third party, the more effective are the third party mechanisms provided by the litigation systems*.

In particular, the following scheme was established:

- When one of the original parties in the proceedings and a third party are strongly associated in substantive terms (they are typically co-liable or co-

holders of rights and duties),¹ the original parties and the third party are considered a *necessary unit in terms of jurisdiction*, and, therefore, *compulsory third-party mechanisms* will be normally provided.

- When one of the original parties in the proceedings and a third party are contractually interrelated but not *strongly associated* (they are typically liable in the alternative rather than co-liaible),² the original parties and the third party are not considered a necessary unit in terms of jurisdiction and, therefore, *permissive third party mechanisms* will be normally provided.

As was demonstrated in Chapter 8, the above scheme applies to the majority if not all national and regional procedural systems and, therefore, it would be safe to argue that it constitutes a general principle on the role of third parties in the context of litigation.

The thesis, then, sought to apply this principle to arbitration, taking into account the particular principles and unique characteristics of international arbitration. Here, as was explained in Section 9.1, the most relevant principle to take into account was the principle of procedural party autonomy, according to which commercial parties have the right to regulate their procedural relationships in a way that best serves their commercial interests.

By contrast other arbitration principles, such as the principle of contractual origins of arbitration or confidentiality, although important in other areas of arbitration bear less relevance to the purposes of the thesis. With regard to former it was demonstrated that the discussion on third parties and arbitration does not pertain to the principle of contractual nature. Rather, it pertains to the jurisdictional aspect of arbitration. Whether third parties may participate in arbitration is a matter related to jurisdiction rather than contract law, and therefore, the principle of contractual nature of arbitration agreements should not be directly relevant here. Similarly, confidentiality is not an inherent conceptual feature of arbitration, and would apply only if the parties provide for it, either in their arbitration agreement or by reference to the applicable arbitration rules. Thus, confidentiality does not have an institutional role in arbitration, and therefore, compared to the principle of procedural party autonomy has less relevance for the purposes of the thesis. Accordingly, the principle of party

¹ Persons that the thesis has identified as false third parties of the first group.

² Persons that the thesis has identified as false third parties of the second group.

autonomy rather than the principle of the contractual nature of arbitration or confidentiality will provide the benchmark for the determination of the circumstances under which third parties should be brought before bilateral arbitration proceedings.

Procedural party autonomy includes the right of the parties to choose the arbitration tribunal where they will have their disputes decided, but also their right to choose their opponent in arbitration. Procedural party autonomy is materialised through arbitration agreements where the parties set out their arrangements on jurisdiction. Thus, it is perfectly legitimate and consistent with procedural party autonomy for the parties to agree on several bilateral arbitration proceedings rather than a single set of multiparty proceedings. Accordingly, it was argued in Section 9.2, that the scheme of several bilateral dispute resolution agreements should be upheld even against the background of a multiparty commercial project. Since third-party mechanisms are of exceptional character and party autonomy is the overarching principle prevailing in arbitration any conflict between the two should be in principle lifted in favour of procedural party autonomy. The presumption should be for procedural party autonomy to prevail over third-party mechanisms, even if this would result in procedural fragmentation of a multiparty relationship.

This rule will particularly apply when, as in the majority of the cases, the parties in a multiparty project are contractually interrelated but not strongly associated in terms of interests and liability (the second group of false third-parties as defined in Chapter 2). As was demonstrated in Section 9.3, when the several parties are contractually intertwined but they do not share rights or liability, no exceptional circumstances would exist in order to overturn the general rule. The scheme of several bilateral agreements on jurisdiction should be given precedence. This conclusion is consistent with the general rule established in Chapter 8 on third-party mechanisms: mechanisms of permissive only character would be provided whenever the several parties are contractually interrelated but not strongly associated in terms of interests and liability. However, as was showed by reference to various national jurisdictions, third-party mechanisms of *permissive character*, in terms of jurisdiction, rank below in the hierarchy compared to procedural party autonomy. Therefore, it was concluded that they could not overturn the scheme of several bilateral arrangements on jurisdiction of the several parties, and thus they should not apply to arbitration. In this case the loose links between the several parties, in terms of interests and substantive liability would

not warrant the participation of third parties in bilateral arbitration proceedings. This would mean, for example, that in the context of a multiparty security relationship a guarantor could not take part in the arbitration proceedings between a creditor and a debtor. The scheme of two separate bilateral agreements -for example, an arbitration agreement between a creditor and a debtor, and another arbitration or jurisdiction agreement between a creditor and a guarantor- should be upheld. In such a case, no third-party mechanism should be accepted to allow the participation of the guarantor in the bilateral arbitration proceedings between the two other parties. The same would apply to the scheme of separate bilateral agreements between an employer, a contractor and a subcontractor, or to any other multiparty relationship of this type.

Therefore, as a matter of rule, third-party mechanisms should not apply to arbitration. For third-party mechanisms to overturn the scheme of several bilateral personal jurisdictions, and bring all the parties before the same forum, *exceptional circumstances* must exist.

Chapter 10 ventured to determine those exceptional circumstances. It was suggested there that third-party mechanisms should apply in arbitration whenever the third parties are strongly interrelated with the parties to the arbitration, so that third and genuine parties are *co-liable or co-holders of rights and duties*, as is typically the case in the first group of false third parties, defined in Chapter 2. In such a case the several parties (third and genuine) would constitute *an inseparable unit in terms of jurisdiction*. This jurisdictional unit, due to the strong substantive interrelations of the several parties, should not be separated. Thus, third-party mechanisms should apply to give jurisdiction to a tribunal over the inseparable unit of several parties. In fact, third-party mechanisms in such circumstances should apply despite the existence of a scheme of several bilateral dispute resolution agreements between the several parties. Therefore, a tribunal should be able to assume extra-contractual jurisdiction over the whole jurisdictional unit, including all the genuine and third parties.

This conclusion is also consistent with the general rule established in Chapter 8 on third-party mechanisms: co-liability or community of parties between several parties normally warrants the application of third-party mechanisms of compulsory character. As was demonstrated in Chapter 10, in terms of jurisdiction, third-party mechanisms of compulsory character are strong enough to overturn the scheme of bilateral arrangements between several parties. Therefore, it was suggested that the threshold

required for a tribunal to assume extra-contractual jurisdiction and allow a third party in the proceedings is co-liability or community of rights and obligations. In particular, it will be required that a third party will be co-liable or co-holder of right and obligations with one of the genuine parties to an arbitration agreement. As was illustrated, co-liability or community of rights and obligations between several parties may result from

- Either the contractual arrangements between several parties
- Or the applicable substantive law

In the last chapter the thesis turned to the effect of arbitral awards upon third parties. It was argued that arbitral awards should not be equated to national judgments in terms of their effect. Rather, the effect of arbitral awards should be determined in view of the unique needs and characteristics of arbitration. Accordingly, it was suggested that arbitral awards should affect a wider circle of third parties than in the case of national judgements.

The suggestion was based on the following grounds. In the context of litigation, there are two ways in which two or more parallel proceedings involving the same legal and factual issues are regulated in order for conflicting decisions to be avoided: First, by third-party mechanisms that bring all the relevant parties before a single forum, named by the thesis *unification mechanisms*. In this way parallel proceedings are avoided altogether and regulation of multiparty relationships is achieved in an early stage, namely in a pre-judgment stage. Examples of this type of third-party mechanisms are common jurisdictional bases, class actions, intervention and joinder, interpleading and consolidation. Secondly, by mechanisms *harmonising* the outcomes of the several parallel proceedings, rather than bringing all the several parties before a single forum. Typical examples of *harmonisation mechanisms* are *lis pendens* and *res judicata*. Here the several sets of proceeding remain parallel, instead of being consolidated. However, *lis pendens* and *res judicata* regulate the parallel proceedings, so that conflicting findings and decisions are avoided. In particular, *lis pendens* prevents the continuation of the second set of proceedings until a decision in the first set of proceedings is granted. *Res judicata*, either prevents the second set of proceedings to commence or ensures that the second forum is bound by the determinations of the first decision. Thus, the regulation of multiparty relationships is achieved after the first decision has been issued: it is the decisions of the parallel

proceedings that are brought into accord (“harmonised”). The multiple parties will not be brought before the same forum, as in the case of unification third-party mechanisms.

The thesis showed that as a matter of general policy the procedural regulation of multiparty relationships is welcome at as early a stage as possible. Thus, in the context of national civil procedures, unification third-party mechanisms are given priority over harmonisation mechanisms. Therefore, national procedural systems provide extensive possibilities for a wider circle of third parties to intervene or be joined by the original parties, whereas the application of *lis pendens* or *res judicata* is limited to a narrow circle of third parties and usually hinges on more stringent conditions.

However, as was noted, the policy of an early regulation of the multiparty proceedings cannot apply to arbitration. According to the prevailing contractual approach, at least, third parties cannot be brought before the arbitral proceedings between two parties bound by a bilateral arbitration agreement. Thus, arbitration is left without any means of procedural regulation of multiparty relationships at all: at the pre-award stage third party cannot be brought into the proceedings, while at the post-award stage arbitral awards obtain the status of national judgments and thus have an effect which is limited to privies only. False third parties, such as a subcontractor or a surety, remain unaffected both by the arbitration proceedings and the award between two genuine parties to a bilateral arbitration.

Accordingly, it was argued that arbitral awards should be able to affect a wider circle of third parties than the one affected by national judgments. A wider arbitral effect would compensate for the lack of unification mechanisms at an earlier stage in arbitration analogous to the mechanism provided in the context of litigation. It was suggested, in particular, that arbitral awards should somehow affect the false third parties rather than just the privies to the parties in action.

However, this effect should be different than the effect upon privies. The legal position of a party in action is almost identical to that of its privy, in terms of substantive rights and interests. Naturally thus, it is accepted a privy is bound by the *res judicata* effect of the award issued between its privy and another person. In other words the award can be enforced by and against a privy, although the latter has not taken part in the arbitral proceedings.

The legal position of false third parties, on the other hand, is contractually interrelated but not identical to that of the parties to the proceedings. They could not be bound by *res judicata*. Otherwise issues of due process would be raised. Therefore, it was argued that an arbitral award should affect false third parties, albeit in a different, and certainly less drastic, way than privies are.

This suggestion accords to the general principle underpinning the whole work here: that the procedural relationships between several parties must correlate to their relationships in substantive terms.

Accordingly, Section 12.4 determined the content and boundaries of the effect that an arbitral award should produce on false third parties. More specifically, it was argued that arbitral awards should have both conclusive and preclusive effects on false third parties. Thus, the preclusive effect of an award between two parties will prevent re-litigation of any factual and legal issue that might arise again in the second set of proceedings between a false third party and one of the parties in the first set of proceedings. In addition, the conclusive effect of the award between two parties will provide the logical and legal basis for the second forum (court or tribunal) to reach a decision in accordance with the determination of the first award. Applied in this way, the combined arbitral effect will harmonise the several sets of proceedings, in the context of a multiparty relationship, and it will ensure that any conflicting awards are avoided.

As was explained, this type of arbitral effect will be less effective than the *res judicata* effect. The award will merely affect rather than bind a false third party. The award given in proceedings between the two genuine parties will not be able to be enforced by or against the false third parties. This third-party effect will not pre-empt any of the third party's rights or duties. A second trial will be required for the third party's claim to be determined.

It was argued that this type of arbitral effect can be particularly used by the third party in the second set of proceedings against one of the genuine parties acting either as claimant or as defendant. It was also suggested that one of the parties in the first set of arbitral proceedings should be able to use the arbitral effect against the false third party. This however will require, as a condition precedent, that the former will have invited the latter to join the first arbitral proceedings, and the latter will have refused to do so.

This kind of arbitral effect will basically apply to any third party that has a significant interest in the dispute between two other parties bound exclusively by an arbitration agreement. It will thus apply to guarantors, or subcontractors and any other third party covered by the term false third parties of the second group, as this was determined in the thesis. *A fortiori*, this kind of arbitral effect will also apply to false third parties of the first group (co-liaible or co-holders of rights or duties with one of the two parties in the arbitral proceedings), on the condition that the latter have not taken part in the arbitral proceedings on the basis of the suggested jurisdictional approach. In case they have take part in the proceedings, false third parties of the first group will, of course, be bound by the *res judicata* effect of an award, as genuine parties to arbitral proceedings.

Finally, and with regard to the legal basis of the effect of arbitral awards, it was argued that the effects of arbitral awards should be determined at an international level rather than by national provisions. It was suggested that international awards should acquire an international status, which they should carry into national jurisdictions after their recognition and enforcement. Allowing divergent regulation of the effects of arbitral awards by national systems reduces the effectiveness of international awards and hampers their free circulation.

Overall, the suggestions on the effect that arbitral awards and arbitration agreements may have upon third parties can be summarised in the following scheme (see also Table 1, below):

- First, persons (and their privies) who are contractually bound by an arbitration agreement and who take part to the arbitration proceedings, i.e. genuine parties to arbitration agreement and proceedings, and their privies →
 - They will be bound by the arbitration agreement as an ordinary contract, thus the arbitration agreement will be enforceable by and against them
 - They will be bound by the *res judicata* effect of the arbitral award, thus the award will be enforceable by and against them
- Second, persons who are not contractually bound by an arbitration agreement, but who are strongly associated with one of the genuine parties to the arbitration agreement or the proceedings, in terms of contractual interests and

liability (false third parties of the first group). These persons will typically be co-liable with the genuine parties →

- They will not be bound by the arbitration agreement as an ordinary contract. However, the tribunal may assume jurisdiction over them, so that they may take part in the arbitration proceedings as joined claimants or joined respondents
- If they do take part in the arbitration proceedings, they will be bound by the *res judicata* effect of the arbitral award, thus the award will be enforceable by and against them. If they do not take part in the arbitration proceedings, they will be affected by the third-party effect of the arbitral award as suggested by the thesis
- Third, persons who are not contractually bound by an arbitration agreement, and are contractually interrelated but not strongly associated with one of the genuine parties to the arbitration agreement or the proceedings, in terms of contractual interests and liability (false third parties of the second group)
 - They will not be bound by the arbitration agreement as an ordinary contract. Moreover, the tribunal may not assume jurisdiction over them and, therefore, they cannot be brought into the arbitral proceedings between the two genuine parties, unless all the parties (genuine and third) agree to this effect.
 - They will not be bound by the *res judicata* effect of the arbitral award between the two genuine parties, and therefore the award will not be enforceable by or against them. However, they will be bound by the third-party effect of this award, as suggested by the thesis

The role of third parties in arbitration remains still an enigma. This is largely because the discussion on third parties is multifaceted. Indeed, the discussion has a policy background. The main question here is whether arbitration should remain a closed dispute resolution system, reserved only for those parties that are contractually bound by an arbitration agreement; alternatively, whether arbitration should be a flexible dispute resolution system, able to communicate with third parties that have legal and financial interests in the dispute pending before the tribunal.

However, the discussion on arbitration and third parties is not, and should not be, exhausted in a policy debate. There is great amount of theory related to the discussion. Since third-party mechanisms are jurisdictional in nature, the most effective way to assess the role of third parties in arbitration is to focus on whether arbitration may have any jurisdictional implications for third parties. Therefore, the thesis focused on procedural theory in order to examine and reveal the rationale and the principles behind third-party mechanisms.

It would appear that there is a growing scepticism in arbitration against procedural theory. It is feared that study based on procedural doctrine will bring arbitration closer to litigation. This view is understandable to some extent. “Proceduralisation” of arbitration has to be avoided. Arbitration has to retain a degree of flexibility, staying away from unnecessarily complicated dogmatism prevalent in almost all litigation systems.

However, it would be equally wrong to shun any attempt to examine arbitration by reference to procedural theory, which was developed to address real commercial problems in the first place. It is vitally essential to keep looking into fundamental principles underpinning procedural theory, and applying those principles against the unique backdrop of arbitration. In this regard, scholar analysis of arbitration has to be moderately rehabilitated.

In this context the discussion on arbitration and third parties is directly pertinent to the very nature of arbitration. The outcome of this discussion will depend on the way which arbitration will eventually follow. Indiscriminately importing litigation mechanisms to arbitration would render arbitration ineffective and eventually alienate it from the business community. Avoiding procedural theory altogether will deprive arbitration from the academic depth necessary to address real problems in practice.

It is truly hoped that the delicate balance between theory and substance was attained in this study.

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decisions from civil law countries are listed chronologically*

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