Stay Pending Arbitration : Incorporation Of Arbitration Agreement By Reference In Recitals?

GISE KAM KWAN INTERNATIONAL TRADE LTD V ANTARA STEEL MILLS SDN BHD [W-02(IM)(NCvC)-2329-12/2022]

30th September 2024

ISSUES

Section 9(5) of the Arbitration Act 2005 ("**AA 2005**") provides that, where a contract refers to a document containing an arbitration clause, such reference would constitute an arbitration agreement so long as it is in writing and the reference is "*such to make that clause part of the agreement*".

What if the reference to the earlier agreement containing the arbitration agreement, is only made at the recital of the later agreement? Would such reference constitutes a reference to make the arbitration clause part of the latter agreement?

Would the situation be different if the latter agreement is an agreement to terminate the earlier agreement that contains the arbitration clause? Would the latter agreement terminate the earlier agreement together with the arbitration clause therein?

These questions were answered in the recent Court of Appeal case of **Gise Kam Kwan International Trade Ltd v Antara Steel Mills Sdn Bhd [W-02(IM)-2329-12/2022]**.

BRIEF FACTS

The brief facts of the case are as follows:-

(a) There were 2 main agreements between the Appellant and Respondent (**"Main Agreements**"). Both the Main Agreements contained an arbitration agreement.

(b) Parties thereafter executed a Termination and Settlement Agreement ("**TSA**"). Whilst the recitals made a general reference to the Main Agreements, there was no reference to the arbitration agreement in the body of the TSA.

(c) However, clause 6 of the TSA provides that the Appellant "*is entitled to take legal action to claim outstanding payment and all direct and indirect loss including… court fee*" if the Respondent breaches the TSA [emphasis added].

(d) Following the above, the Appellant commenced a court action to recover the amount outstanding under the TSA.

(e) On the other hand, the Respondent filed an application for stay of the Court proceedings and for a reference of the dispute to arbitration pursuant to section 10 of the Arbitration Act 2005 ("**AA 2005**").

(f) The High Court was conscious that there was no express arbitration agreement in the TSA but found, amongst other, that the arbitration agreement under the Main Agreements had been incorporated into the TSA as the TSA contained a reference to the Main Agreement.

(g) Consequently, the High Court granted a stay of the Court proceedings pending reference to arbitration pursuant to section 10 of AA 2005.

(h) Dissatisfied with the outcome, the Appellant appealed to the Court of Appeal.

PROCEEDINGS BEFORE THE COURT OF APPEAL

The issues before the Court of Appeal are as follows:-

> *"(i) Whether the arbitration agreement in the Main Agreements had been incorporated by reference such as to make that arbitration clause part of the TSA;*
>
> *(ii) Whether the TSA is a stand-alone entire agreement independent of the Main Agreements and superseding the Main Agreements;*
>
> *(iii) Whether the references to "take legal action to claim the amount" and "court fee" indicate a clear intention of the parties to resolve all disputes arising from the TSA via Court proceedings;*
>
> *(iv) Whether the doctrine of separability and kompetenze-kompetenze apply such that matter is to be referred to arbitration."*

Incorporation by reference

The Court of Appeal noted that the Main Agreements contain an arbitration agreement and that an arbitration agreement can be incorporated by reference pursuant to section 9(5) of AA 2005. However, the Court of Appeal held that such reference must be for the purpose of incorporating the arbitration clause thereunder into the new agreement (TSA):-

> *"[13] Further s 9(5) of the AA 2005 deals with the incorporation of an arbitration clause by reference to it in an agreement and the reference is such as to make that clause part of the agreement as follows:*
>
> > *"(5) A reference in an agreement to a document containing an arbitration clause shall constitute an arbitration agreement, provided that the agreement is in writing* ***and the reference is such as to make that clause part of the agreement****." (emphasis added)*
>
> *[14] Thus, it is not every reference in an agreement to a document containing an arbitration clause that would automatically incorporate that arbitration clause as part of the agreement. The reference must be for the purpose of making that arbitration clause part of the agreement which in this case is the TSA."*

The Court of Appeal accepted that there need not be an explicit reference to the arbitration clause itself in the latter agreement, if parties' intention to incorporate the arbitration clause is clear. However, the Main Agreements were only referred to in the Recitals of the TSA and such reference is generally for context and is "*not typically considered to be legally binding*":-

> *"[18]* ***Generally, the Recital to an agreement preceded by the word "Whereas" would set out the chronology of key events for context*** *and the terms and conditions of the agreement would be found in the main body of the agreement or its Operative part.* ***A Recital in an agreement serves as an introduction to the background and purpose of the agreement. A clause in the Recital is not typically considered to be legally binding as opposed to the Operative clauses of an agreement****. Nevertheless, a Recital plays an important role in helping one to discern the intentions of the parties.*
>
> *[19]* ***Recitals do not generally contain specific obligations, rights and duties of the parties and therefore are not enforceable****. They provide the factual matrix in interpreting the Operative clauses but by themselves they do not create binding agreement. They set the stage for the substantive clauses and sound forth its scope."*
>
> [Emphasis added]

Considering the above, the Court of Appeal found that the reference in the Recital is for context and chronology only and as such, there is no effective incorporation of the arbitration agreement by reference:-

> *"[24] We are of the considered view that as the reference here is in the Recital and for context and chronology and nothing coming close to the terms and conditions agreed by the parties,* ***there has not been an effective incorporation***

by reference as the reference is not such as to make that arbitration clause part of the TSA.

[25] It is the operative part of the TSA that is binding on the parties and there is clearly no reference to the Main Agreements there. ***A reference to it in the Recital for context is ineffective in incorporating the arbitration agreement found in the Main Agreements into the TSA****."*

[Emphasis added]

TSA is a stand-alone agreement : "Take Legal Action" / "Court Fee"

Further, the Court of Appeal also found that the latter TSA is a stand-alone agreement to resolve the disputes between parties as well as to terminate the earlier Main Agreements. Consequently, there is no outstanding obligations remaining in the earlier Main Agreements:-

"[27] All the outstanding and unresolved matters have crystallised into the TSA and in that sense it is a stand-alone entire agreement. ***There is nothing on the Main Agreements of 2009 and 2013 that needs referencing or resurrecting****. The TSA is self-contained…*

*[29] However, what is settled in the TSA is also severable from the Main Agreements both in its implementation and enforcement****. There is nothing left of the obligations of the parties in the Main Agreements save for the obligation of Antara Steel to pay Gise International the agreed amount.*** *There is no allegation of misrepresentation, fraud, forgery or lack of authority or capacity to enter into the TSA…*

[31] ***Here is a case where both the parties had reached a consensus on the termination and settlement of all outstanding obligations arising from the termination which the parties had reached as spelt out in the terms and conditions of the TSA****."*

[Emphasis added]

The Court of Appeal also found that there is a separate dispute resolution clause in the TSA and the different language used in the dispute resolution clause is a strong indication that parties no longer desire to be bound by the earlier arbitration clause:-

"[32] The remaining question then is whether there is an arbitration agreement in the TSA with respect to any dispute in the interpretation or construction of the TSA and reading the TSA as a whole, both parties did not contemplate anymore issues that could arise following the mutual termination and settlement

agreement. Little wonder that instead of an arbitration agreement, the parties crafted a markedly different dispute resolution clause in Clause 6 of the TSA that reads:

> *"If Party A [Antara Steel] fails to pay any payment stated herein, Party B [Gise International] is entitled to* ***take legal action to claim outstanding payment*** *and all the direct and indirect loss including without limitation to liquidated damages, late fee, attorney fee and* ***court fee*** *from Party A [Antara Steel]." (emphasis added)*

[34] By drafting a different dispute resolution clause, the parties' clear intention was no longer to submit any further disputes to arbitration and so the parties have taken the arbitration agreement out from the TSA and substituted it with a clause on "to take legal action to claim outstanding payment."

[35] The drafting of a new dispute resolution clause by the same parties must be a strong indication of the parties desiring not to be bound by the previous arbitration clause but instead to have the new dispute resolution clause applied to them. ***There is a strong presumption that when different words are used, the parties intend to express a different meaning and intention****."*

[Emphasis added]

Doctrine of Kompetenze-kompetenze and Separability

On the doctrine of Kompetenze-kompetenze, the Court of Appeal held that both the Courts and Arbitral Tribunal has jurisdiction to determine the existence of an arbitration agreement, depending on whether the jurisdiction issue is raised before the Tribunal or raised before the Court.

Where it is already before the Court under a section 10 AA 2005 Stay Application, the Court will have to first determine the existence of an arbitration agreement before deciding on the stay. The doctrine does not preclude the Courts to determine the existence of an arbitration clause where the issue is before the Court:-

> *"[70] In a matter that is already before the Court under a s 10 AA stay application, it is for the Court to decide whether there is an arbitration agreement to begin with, before deciding if the arbitration agreement is null and void, inoperative or incapable of performance…*
>
> *[78] The Court when confronted by a s 10 AA 2005 application for a stay of the Court proceedings and an applicant seeking to refer the matter to arbitration, need not have to abdicate its responsibility to decide on whether there was an*

arbitration agreement between the parties to begin with. ***The doctrine of kompetenze-kompetenze conferring the power on the Arbitral Tribunal to decide on its own jurisdiction does not mean that the Court must invariably cede to the Arbitral Tribunal to decide on jurisdiction when the issue is raised in a s 10 AA 2005 application****."*

[Emphasis added]

As for the doctrine of separability, the Court of Appeal determined that the TSA is a new agreement superseding the earlier Main Agreements. The arbitration clause in the Main Agreements would not survive the termination vide the TSA, notwithstanding the doctrine of separability. The TSA is a new agreement that supersedes the Main Agreements whereafter the Main Agreements and the arbitration clause thereunder ceases to operate.

"[75] If by the application of the doctrine of separability is meant here that the arbitration clause found in the Main Agreements survives the termination of the Main Agreements and by virtue of that, is applicable upon termination to resolving the dispute that has arisen, then regard must be had to the fact that the termination agreement is also a settlement agreement…

[76] It is also a new agreement that has superseded the previous Main Agreements such that ***it can be confidently said that the Main Agreements including the arbitration clause therein have ceased to operate by reason of some further agreement between the parties in the TSA****. It may be said for argument sake that even if there had been an arbitration agreement, that has been rendered inoperative by the TSA that has its own dispute resolution clause."*

[Emphasis added]

In the upshot, the Court of Appeal allowed the Appeal and remitted the matter back to the High Court for hearing.

KEY TAKEAWAY

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

(a) Whilst section 9(5) of AA 2005 recognises that an arbitration agreement can be incorporated by reference to a document containing an arbitration clause, such reference must be for the purpose of incorporating the arbitration clause thereunder into the new agreement.

(b) Where the agreement's recitals refer to earlier agreement containing an arbitration clause, such references in the recitals would not be an effective incorporation of the arbitration clause as references in the recitals are generally for context only and "*not typically considered to be legally binding as opposed to the Operative clauses of an agreement*".

(c) Where the latter agreement is a settlement and termination agreement that supersedes the earlier agreement, the earlier agreement together with its arbitration clause would cease to operate. The doctrine of Kompetenze-kompetenze or separability would not assist the survival of the arbitration clause in such circumstances.

If you have any questions or comments on this article, please contact:-

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