Malaysia: High Court refuses indemnity costs on successful application for referral to arbitration and determines the effect of time bars on a tribunal's jurisdiction

By Peter Godwin, Daniel Chua and Michele Yee

In _Lineclear Motion Pictures Sdn Bhd v Measat Broadcast Network Systems Sdn Bhd_ (High Court Civil Appeal No.: WA-12ANCC-45-04/2021), the High Court refused to award indemnity costs to a party who successfully obtained a stay of court proceedings under section 10 of the Arbitration Act 2005 (**Act**), on the basis of the conduct of the successful party and the party acting in breach of the arbitration agreement. Following this decision, a party seeking indemnity costs upon successfully obtaining a stay bears the burden to demonstrate unreasonable conduct by the breaching party, and reasonable conduct on its own part, to obtain indemnity costs.

Background

Measat Broadcast Network Systems Sdn Bhd ("**Measat**") commenced proceedings against Lineclear Motion Pictures Sdn Bhd ("**Lineclear**") in the Sessions Court for breach of contract. Prior to the commencement of the proceedings, Measat issued a pre-action letter to Lineclear but was met with no response. As Lineclear did not formally enter its appearance under the rules of the court, nor respond to the claim, Measat obtained a default judgment against Lineclear. Subsequently, Lineclear applied to set aside the default judgment and to stay the proceedings in the Sessions Court pursuant to section 10 of the Act in light of a valid arbitration agreement between the parties.

Measat did not object to the application, instead offering to record a consent order to stay the court proceedings pending arbitration. Lineclear rejected this offer and insisted Measat discontinue its claim. The Sessions Court judge refused to stay the proceedings and refused to grant indemnity costs to Lineclear.

On appeal to the High Court, the key issues were:

- in the event a stay is allowed, whether Measat is entitled to seek an order to preclude Lineclear from pleading the defence of limitation at arbitration; and

- whether Measat is liable to pay indemnity costs to Lineclear given that (a) the proceedings were in breach of the arbitration agreement and (b) Measat unreasonably declined Lineclear's offer to discontinue the claim.

First, the High Court judge granted a stay on the condition that Lineclear be precluded from raising the defence of limitation at arbitration, in accordance with established precedent for imposing similar conditions. The judge reasoned that the stay would be rendered futile without the condition, as Measat's claim – while within the limitation period when first commenced in the Sessions Court – would be time-barred when referred to arbitration.

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Second, the High Court judge refused to award Lineclear's costs on an indemnity basis. The established test requires "*some conduct or some circumstance which takes the case out of the norm.*" In particular, a judge is required to review the unreasonableness of the unsuccessful party's conduct during the proceedings, including: (i) whether it was reasonable for the party to raise and pursue particular allegations and the manner in which the party pursued its case and allegations; and (ii) whether a claim was speculative, weak, opportunistic or thin. Examples of such unreasonable conduct are where a case was brought with an ulterior motive or an improper agenda, or where a party had conducted its case in "*bad faith, or as a personal vendetta, or in an improper or oppressive manner, or who caused costs to be incurred irrationally or out of all proportion as to what is at stake.*" However, these examples are not meant to be exhaustive. In this regard, the High Court found that Lineclear's conduct throughout the proceedings, including its indifference to the pre-action letter and the proceedings leading to the default judgment, as well as its refusal to accept Measat's offer to record a consent order, was unreasonable and did not justify an award of indemnity costs. The High Court judge also found it unreasonable for Lineclear to insist that Measat discontinue the proceedings, given that a successful application under section 10 of the Act would only stay – and not discontinue – an action.

Lineclear relied on the Western Australian Supreme Court's decision in *Pipeline Services WA Pty Ltd v ATCO Gas Australia Pty Ltd* [2014] WASC 10 (see our blog post here) and the English court's decision in *A v B and others (No. 2)* [2007] EWHC 54 (Comm) for the proposition that as a general rule, costs should be recoverable on an indemnity basis upon a successful application for a stay as a remedy for breach of an arbitration clause. The High Court did not appear to accept this proposition, and distinguished these cases on the basis that Measat had acted reasonably throughout the proceedings, whereas Lineclear's conduct justified it being deprived of an order for indemnity costs.

Comment

In practice, Malaysian courts have on rare occasions awarded costs on an indemnity basis upon a successful application to stay court proceedings in favour of arbitration. However, this is the first known written judgment from the Malaysian courts which addressed the principles of awarding costs on an indemnity basis in the context of a breach of an arbitration agreement.

An award of indemnity costs is attractive to parties seeking to uphold an arbitration agreement which has been breached by its counterparty. The advantages include a presumption of reasonableness on the part of the receiving party, and a shift in burden to the paying party to establish that the costs were not reasonably incurred. This achieves indirect compensation for most – if not all – of the legal costs incurred by the innocent party following a breach of an arbitration agreement.
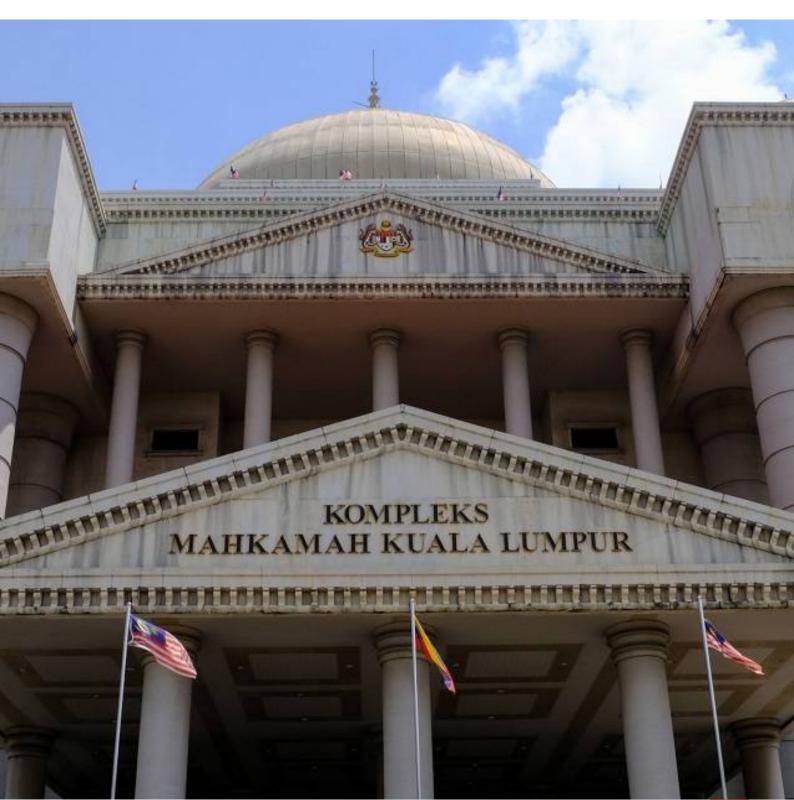
Jurisdictions such as England, Hong Kong (see our blog post here), Singapore and Western Australia take the position that as a general rule, a party who unsuccessfully challenges an arbitration agreement before the court should expect to pay costs on an indemnity basis, unless there was unreasonable conduct by the successful party or special circumstances. By contrast, the current Malaysian position is that a party seeking indemnity costs upon successfully obtaining a stay bears the burden to demonstrate unreasonable conduct by the breaching party, and reasonable conduct on its own part, to obtain indemnity costs. The fact of a breach of an arbitration agreement alone is not necessarily sufficient to justify indemnity costs. Where indemnity costs are not awarded, parties should consider seeking damages for breach of an arbitration agreement which, though untested in Malaysia, is an accepted cause of action in various common law jurisdictions.

Further, in precluding Lineclear from raising the defence of limitation in the arbitration, the court did not appear to give any consideration as to whether limitation was an issue of admissibility or jurisdiction. The distinction holds practical importance: an issue of admissibility is a matter for the arbitral tribunal to decide, and not a question of jurisdiction to be reviewed by the courts. As described by the English courts, "[i]*ssues of jurisdiction go to the existence or otherwise of a tribunal's power to judge the merits of a dispute; issues of admissibility go to whether the tribunal will exercise that power in relation to the claims submitted to it.*" (see our blog posts here and here). It should also be noted that the Singapore Court of Appeal in *BBA v BAZ* [2020] 2 SLR 453, recognising the distinction between jurisdiction and admissibility, held that whether a claim was time barred was a question of admissibility, not a question of jurisdiction.

Although the Malaysian court did not characterise the limitation defence as an issue of admissibility or jurisdiction, its upholding of the arbitration agreement may imply that limitation is a question of admissibility as it does not affect the Tribunal's jurisdiction. The net result of the decision provides some measure of welcome certainty that arbitration agreements will be upheld by the Malaysian courts, even where there are questions regarding the limitation period for commencing claims. However, this approach appears to remove a tribunal's ability to determine issues of admissibility for itself where a Malaysian court is first seised of the matter.

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