Separability and arbitral tribunals being 'open for business'?

In *DHL Project & Chartering Ltd v Gemini Ocean Shipping Co. Ltd* [2022] EWCA Civ 1555 (DHL v Gemini), the Court of Appeal of England and Wales dealt with the separability principle. The principle deals with the existence of an arbitration agreement in an invalid or rescinded contract.

By Richard Pidgeon

The separability principle explained

As the Court of Appeal in *DHL v Gemini* noted, the separability principle is *an important concept for arbitration lawyers, although it may be questioned how many business people who include an arbitration clause in their contracts are aware that it exists*.[1] The separability principle is provided for in statute, in Art 16 of Schedule One of the Arbitration Act 1996 (NZ) and section 7 of the UK Act.

The separability principle means that the invalidity or rescission of the main contract does not necessarily entail the invalidity or rescission of the arbitration agreement. The arbitration agreement is a *distinct agreement* and can be void or voidable only on grounds which relate directly to the arbitration agreement.[2] This means the arbitral tribunal might be 'open for business' even if the principal contract is not concluded.

Section 7 of the Arbitration Act 1996 (UK) was the mainstay of Gemini's argument in both Courts. It holds:

> **Separability of arbitration agreement**
>
> Unless otherwise agreed by the parties, an arbitration agreement which forms or was intended to form part of another agreement (whether or not in writing) shall not be regarded as invalid, nonexistent or ineffective because that other agreement is invalid, or did not come into existence or has become ineffective, and it shall for that purpose be treated as a distinct agreement.

The background facts: DHL v Gemini

The background to the case is straightforward. DHL and Gemini were charterparties who reached a simple agreement *subject shipper/ receiver's approval*,[3] (a condition precedent involving the approval of two third parties), for a putative journey from Australia to China in September 2020.

The agreement had an arbitration clause in it, for an arbitration to be heard in London with English law to apply. The arbitration agreement conferred jurisdiction on a sole arbitrator to determine whether a charterparty existed.[4] The 'subject' was never lifted and neither a contract nor an arbitration agreement were ever concluded. Gemini referred the matter to an arbitral tribunal

1 *DHL Project & Chartering Ltd v Gemini Ocean Shipping Co. Ltd* [2022] EWCA Civ 1555 at [43].

2 *Fiona Trust & Holding Corp v Privalov* [2007] UKHL 40, [2007] 4 All ER 951 at [17] per Hoffmann LJ. This passage was cited with approval in *Carr v Gallaway Cook Allan* [2014] NZSC 75, [2014] 1 NZLR 792 at [43]. See further Sir D Willams & A Kawharu Williams and Kawharu on Arbitration (2nd ed LexisNexis, Wellington 2017) at 4.11.

3 At [1].

4 At [1].

which met in the absence of DHL (as it so happened).[5] The arbitrator awarded Gemini damages of USD 283,416.21 for repudiatory breach by DHL and made orders for payment of costs.

DHL applied to the High Court under section 67 of the Arbitration Act 1996 (UK) on the basis the arbitrator lacked substantive jurisdiction, seeking to set aside the award. In the alternative, DHL appealed under section 69 on a point of law, submitting the subject clause was not qualified by other contract terms.

The High Court: condition precedent not lifted, neither contract nor arbitration agreement were concluded

Justice Jacobs decided the High Court matter in March 2022 (*DHL Project & Chartering Ltd v Gemini Ocean Shipping Co. Ltd* [2022] EWHC 181 (Comm)) on the basis (as a rehearing under section 67):

- The principal contract was subject to shipper/receiver's approval: which was found at the start of the agreement and affected the *full* bundle of rights and obligations under the agreement.
- Importantly, the 'subject' clause was unqualified by other terms in the same contract.[6]
- The 'subject' created a precondition to the contract,[7] which was never lifted.
- The section 67 argument turned on whether a binding arbitration agreement was reached, not whether a binding charterparty contract was concluded.
- No contract (and *here* no arbitration agreement on the facts) had been formed.
- The arbitrator who awarded damages to Gemini did not have substantive jurisdiction.
- The arbitrator's award was set aside: Gemini could not rely on the doctrine of separability of arbitration clauses.

Gemini had argued the 'subject' clause was a condition subsequent and that permission for its fulfillment could not be unreasonably withheld. The section 69 issue was not dealt with, as the section 67 issue carried the day. The arbitration agreement was *here* not a *mini agreement which is in some way divorced from the "main" agreement*.[8]

Gemini sought to appeal the High Court decision and Justice Jacobs granted leave to appeal, as the consideration of section 67 of the UK Act was a matter of public importance.

The Court of Appeal: the separability principle was not persuasive in DHL v Gemini

In the Court of Appeal, DHL supported the reasoning of Justice Jacobs in the High Court.[9]

On 24 November 2022, the Court of Appeal issued its decision, which effectively confirmed the lower court decision. For the unanimous Court of Appeal, Lord Justice Males wrote regarding the 'subject' term that:[10]

> …Commercial parties would reasonably expect such a "subject" to apply to

5 At [24].

6 This followed *Nautica Marine Ltd v Trafigura Trading LLC (The "Leonidas")* [2020] EWHC 1986 (Comm) as to the nature and effect of a 'subject' of this type.

7 At [65]; this followed *Hyundai Merchant Marine Company Limited v Americas Bulk Transport Limited (The "Pacific Champ")* [2013] EWHC 470 (Comm), [2013] 2 Lloyd's Rep 320, in holding that a "subject" of this type created a precondition to the conclusion of a binding arbitration.

8 *DHL Project & Chartering Ltd v Gemini Ocean Shipping Co. Ltd* [2022] EWHC Civ 181 at [93]; and unlike in *Heli-Flight New Zealand Ltd v Massey University* HC Auckland Civ-2005-404-4855 per Harrison J, where he held an agreement to arbitrate survived termination of contract.

9 At [33].

10 At [80].

> the whole proposed contract and not to everything apart from the proposed arbitration clause.

The Court clarified that an arbitration agreement is *a contract like any other*,[11] and the primary issue is whether a contract has been formed *in the first place*;[12] that is, it was a contract formation case,[13] not a contractual validity case. The Court agreed with DHL's submission that if there is no binding arbitration agreement, there is nothing to which the separability principle can apply.[14]

The separability principle gave no comfort here to Gemini, as the principal contract was never formed and *on the facts* of the case no valid arbitration clause existed:[15]

> One-stop shopping is all very well, but if the parties have not entered into an arbitration agreement, the shop is not open for business in the first place.

This result would not affect the general ability to hold ad hoc arbitrations as to whether a binding contract had been formed, without prejudice to other rights.

Conclusion

The arbitration agreement is the foundation of the arbitrator's authority to decide anything. *DHL v Gemini* was a case on the formation of the contract: it was never formed. That is distinct from the validity of the contract where an arbitration clause is present and effective and is not directly impeached.

The arbitration agreement and proposed charterparty stood or fell together *in this case*.[16]

The facts of the case and the terms of the contract are crucial, as ever. Specific drafting is a must,[17] as is the factual matrix of the negotiations as to whether the condition precedent (if unfulfilled) will prevent an arbitration agreement from being effective and prevent the arbitral tribunal from being *open for business*.

11 At [75].

12 At [57], [75] and [80].

13 At [66]–[67] and [72], citing *BCY v BCZ* [2016] SGHC 249, [2016] 2 Lloyd's Rep 583; the *BCY* case is what Males LJ described in *DHL v Gemini* as the "clearest" non-application of the separability principle.

14 At [57].

15 At [75].

16 At [28] and [29]; and *DHL Project & Chartering Ltd v Gemini Ocean Shipping Co. Ltd* [2022] EWHC Civ 181 at [126].

17 Such as using New Zealand Dispute Resolution Centre's model clauses.

About the author

Richard works as a Knowledge Manager in The ADR Centre's Knowledge Management Team, working with both NZDRC and NZIAC.

He is a Doctor of Law and previously practiced as a civil litigation barrister in Auckland.