STAY OF COURT PROCEEDINGS UNDER THE INTERNATIONAL ARBITRATION ACT

by PROFESSOR MICHAEL PRYLES

TANNING RESEARCH LABORATORIES INC v O'BRIEN (1990 64 ALJR 211)

Australia is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the 1958 New York Convention). Article II (3) of the Convention requires a court to stay proceedings on account of an arbitration agreement. This provision is implemented in Australia by section 7 of the International Arbitration Act 1974 (Cth.). Recently in *Tanning Research Laboratories Inc. v. O'Brien* (1990) 64 ALJR 211 the High Court considered this provision.

The case raises the issues of whether a liquidator of a company which is party to an arbitration agreement is bound by the arbitration agreement under s.7 (2) (a) and s.7 (4) of the Act and, whether proceedings involve the determination of a matter that, in pursuance of the agreement, is capable of settlement by arbitration within s.7 (2) (b) of the Act. Tanning Research Laboratories Inc. ("Tanning") was a Florida corporation which granted an exclusive licence to a New South Wales corporation—Hawaiian Tropic Pty Ltd ("Hawaiian"). The agreement was dated 24 June 1975 and was expressed to bind the parties to the agreement and their legal representatives, successors, and permitted assigns. It contained an arbitration agreement. In April 1981 Hawaiian was ordered to be wound up in the Supreme Court of New South Wales and a liquidator was appointed. Subsequently Tanning purported unilaterally to revoke the licence agreement. The liquidator then gave instructions to commence proceedings in a Florida court in the name of Hawaiian seeking a declaratory judgment reinstating rights under the agreement and awarding damages. The court ordered that the matter be settled by arbitration and in January 1985 arbitrators made an award which recited, inter alia, that Hawaiian had breached the licence agreement by failing to timely pay amounts due for products it had received in the sum of $US179,000 and by incurring liquidation under Australian law.

In the New South Wales liquidation proceedings Tanning claimed that Hawaiian was indebted to it in the sum of at least $323,132 for goods sold pursuant to the licence agreement. Alternatively, Tanning claimed $US179,000 in reliance upon the arbitrators' award. The liquidator rejected in whole the proof of the debt whereupon Tanning instituted proceedings in the Supreme Court of New South Wales seeking an order reversing the liquidator's decision. Cohen J ordered that the liquidator allow the

proof in the sum of $55,502.63 but the order was set aside by the Court of Appeal which ordered that the amount of the debt should be referred to arbitrators for determination. The High Court held that the liquidator was a person claiming through or under a party to the arbitration agreement within the meaning of s.7 (4) of the *International Arbitration Act* and further that the proceedings involved the determination of a matter that in pursuance of the agreement was capable of settlement by arbitration within s.7 (2) (b) of the Act. In the view of the Court these questions were to some extent inter-related.

The inter-relationship between the two questions was most directly acknowledged by Dean and Gaudron JJ. who observed:

> "To ascertain whether s.7 (2) operates in respect of proceedings pending in a court it is necessary to first identify the subject matter of the controversy which falls for determination in those proceedings. Only when that has been done is it possible to identify whether the proceedings "involve the determination of a matter . . . capable of settlement by arbitration": s.7 (2) (b). That process of identification is also necessary to ascertain whether, if a party to the proceedings is not a party to the arbitration agreement, he or she is a person "claiming through or under a party": s.7 (4)."

In relation to the second matter, Tanning argued that the question was what proof of debt should be admitted in the winding up and they contended that this did not fall within the arbitration agreement. However Deane and Gaudron JJ. observed that s.7 (2) could not be ousted simply because some issues may fall outside the arbitration agreement. They went on to say:

> "In the context of s.7 (2), the expression 'matter . . . capable of settlement by arbitration' may, but does not necessarily, meaning the whole matter in controversy in the court proceedings. So too, it may, but does not necessarily encompass all the claims within the scope of the controversy in the court proceedings. Even so, the expression 'matter . . . capable of settlement by arbitration' indicates something more than a mere issue which might fall for decision in the court proceedings or might fall for decision in arbitral proceedings if they were instituted: see *Flakt*, at 250. It requires that there be some subject matter, some right or liability in controversy which, if not co-extensive with the subject matter in controversy in the court proceedings, is at least susceptible of settlement as a discrete controversy. The words 'capable of settlement by arbitration' indicate that the controversy must be one falling within the scope of the arbitration agreement and, perhaps, one relating to rights which are not required to be determined exclusively by the exercise of judicial power."

They concluded that the substance of the controversy between Tanning and the liquidator was the amount enforceable as a debt for goods sold and delivered to Hawaiian under the licence agreement. This controversy was susceptible of settlement as a discrete controversy.

On the question of whether the liquidator claimed through or under Hawaiian, Deane and Gaudron JJ. observed:

> "Because s.7 (2) has this wider operation, the question whether a person is claiming through or under a party to the arbitration agreement is necessarily to be answered

> by reference to the subject matter in controversy rather than the formal nature of the proceedings or the precise legal character of the person initiating or defending the proceedings."

As the liquidator had not suggested that there were any grounds upon which he was entitled, as a matter of discretion, to refuse to admit the proof of debt if it would have otherwise been enforceable against the company it followed that the liquidator was a person claiming through or under a party to the arbitration agreement, namely, Hawaiian. This aspect was particularly emphasised by Brennan and Dawson JJ. They noted that principles which determined the enforceabililty of a liability in liquidation proceedings were the same as the principles which would be applied in an action brought directly against the company to enforce that liability. But there were some qualifications and in some instances a liquidator could reject a proof of debt, in the interests of the creditors, even though it was enforceable against the company. In the instant case there was no suggestion that the liquidator would challenge the debt on any grounds which would not have been available to Hawaiian. Consequently s.7 (2) of the Act applied and the proceedings had to be stayed.

All judges dealt with the allegations that there were estoppels. One was said to arise from the finding of the arbitrators that Hawaiian was indebted to Tanning in the sum of $US179,000. All the justices agreed that this was an issue which could be referred to the arbitrators as part of the wider question of what was Hawaiian's indebtedness to Tanning. While Deane and Gaudron JJ conceded that the alleged estoppel arose out of the arbitration rather than the licence agreement they were all aspects of the wider controversy as to the amount enforceable as a debt for goods sold and delivered under the licence agreement. Hawaiian had also alleged a broader estoppel based on Tanning's failure to actually counter-claim in the earlier arbitration proceedings for the debt due. A majority of the court (Deane, Gaudron and Toohey JJ.) held that this was also an issue which could be referred to arbitration. Brennan and Dawson JJ dissented on this point.