



## Supreme Court specifies reasoning standards for awards

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### Introduction

Most arbitration rules require tribunals to state the reasons on which an arbitral award is based.<sup>(1)</sup> The absence of proper reasoning can generally lead to the award being set aside because of a violation of procedural public policy. However, there is little guidance as to what level of reasoning is expected. This problem is further compounded as different national standards are applied in proceedings to set aside an award. For example, under longstanding Austrian Supreme Court case law, defective reasoning did not previously constitute a severe enough violation of procedural public policy to set aside an award.

However, in recent years, the Supreme Court has reversed this trend and repeatedly held that non-adherence to certain reasoning standards in arbitral awards can be a ground to set aside an award. The first decision in this regard was handed down in September 2016 (for further details please see "Supreme Court sets aside arbitral award for defective reasoning"). In its recent decision of 6 March 2020, the Supreme Court has provided further guidance on the required reasoning standards for awards.<sup>(2)</sup>

### Facts

The underlying dispute stemmed from an agreement concluded in 1997 between a mining company and the local municipality. The agreement was a standstill agreement under which the municipality agreed not to raise certain oppositions against the mining approvals in exchange for a yearly lump-sum payment. In 2014 the mining company stopped its payments under the agreement, arguing that it had been terminated. The claimant based this assertion on several grounds, including a clause in the agreement which provided for automatic termination in case of the expiry of its mining permit. As the municipality did not accept this argument, the mining company initiated ad hoc arbitration aimed at declaring the agreement terminated and reclaiming the retrieved security deposit. The arbitral tribunal dismissed the claims.

The mining company initiated proceedings with the Supreme Court in order to have the award set aside, among other things, on the grounds of violation of procedural public policy because of defective reasoning.

## **Arguments**

The claimant argued in the setting-aside proceedings that under the applicable administrative law, the mining permit (and thus the agreement) had ended when the competent administrative authority had approved the plan to close the mine. However, the arbitral tribunal had negated the termination of the agreement on the ground of the mining permit's expiry. In its reasoning, the tribunal had referred to witness statements. The claimant argued that as the witnesses had said nothing on this question, it remained completely unclear on what factual or legal grounds the arbitral tribunal had based its assessment of the continued validity of the agreement.

## **Decision**

The Supreme Court held that the arbitral tribunal had apparently considered the witnesses' testimony. Because the witnesses had not made any relevant statements, the arbitral tribunal had concluded that there was no factual basis for the termination. This reasoning was thus, in the Supreme Court's view, conclusive.

The claimant had also argued that the arbitral award failed to provide any reasoning as to the claimant's legal argument regarding the termination as a consequence of the approval of the plan to partially close the mine, which had led to the mining permit's expiration. The Supreme Court accepted that this could generally amount to a legitimate reason for setting aside the award. However, it held that a two-tier approach must be followed:

- the tribunal must have failed to provide proper reasoning; and
- this issue must concern an essential point in dispute.

While the Supreme Court found that the reasoning in this case was defective, it also noted that the claimant had failed to address this legal issue in the arbitration itself and thus the second prerequisite was not given, as a relevant defective reasoning would exist only if an essential legal issue was not dealt with by the arbitral tribunal.

## **Comment**

The claimant's main argument in the setting aside proceedings was that the arbitral tribunal had failed to consider an essential legal issue: it had held that the mining permit was still valid without considering that the plan to partially close the mine must have – as a legal consequence – led to the mining permit's expiration. The Supreme Court apparently conceded that there had been a deficiency in the arbitral tribunal's reasoning as it had not addressed this legal argument in its award. Consequently, it can be concluded that as a general rule, a tribunal's failure to provide any reasoning for a legal question can amount to a severe enough violation of procedural public policy that the award may be set aside.

However, in the present case, the Supreme Court denied the setting aside as it applied a two-tier test on the basis of its recent case law,<sup>(3)</sup> according to which procedural public policy is violated only if the defective reasoning concerns an essential point in dispute. As the claimant had not asserted in the setting-aside proceedings that the legal issue had been raised in the arbitration proceedings, the Supreme Court saw no justification to address this issue. This is apparently carried by the consideration that a party's failure to raise a legal argument in the course of arbitration does not require the tribunal to deal with this argument on its own initiative. As a consequence, a tribunal's failure to deal with a matter not elevated by a party to an essential point in dispute cannot amount to defective reasoning.

Although the award in this case was ultimately not set aside, this decision can be seen as an important step in the right direction as it calls on arbitral tribunals to further improve and ensure the formal quality of arbitral awards. In this regard, the decision provides valuable guidance on reasoning standards. Further, it contains a reminder for parties that all essential factual and legal arguments must be expressly raised in the course of arbitration proceedings.

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## **Endnotes**

- (1) Article 32(2) of the International Chamber of Commerce Rules, Article 49(3) of the 2015 China International Economic and Trade Arbitration Commission Rules, Article 35(4) of the 2018 Hong Kong International Arbitration Centre Rules, Article 32(4) of the Singapore International Arbitration Centre Rules 2016, Article 34(3) of the United Nations Commission on International Trade Law Rules 2010 and Article 36(1) of the Vienna International Arbitration Centre Rules 2018.
- (2) Supreme Court, 6 March 2020, Docket 18 OCg 11/19w.
- (3) Supreme Court, 8 September 2016, Docket 18 OCg 3/16i; see also "Supreme Court sets aside arbitral award for defective reasoning".