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Fraud Claims in London Maritime Arbitration

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1. In the long history of London arbitration, fraud is a relative newcomer. Prior to the Arbitration Act 1996, fraud was not really an issue, save in a peripheral manner. Practitioners would tend to avoid allegations of fraud, as any such allegation could bring an arbitration to a sharp halt as the High Court could simply stop the arbitration proceedings and re-direct the claim to itself.[1]

2. It was then considered that every party had "*the right to clear his name in judicial proceedings where the evidence could be aired fully and in public*", as opposed to being obliged to accept the ruling of an arbitrator that he had been fraudulent[2]. In *Permavox Ltd v Royal Exchange Assurance,*[3] Mr Justice Greaves-Lord stated that a charge of fraud should "*be tried in open court and in the light of day*".

3. Why an alleged fraudster should want to see his dirty laundry on public display seems an oddity today, and indeed by 1996 the movement towards independence of the arbitral process trumped the perceived benefit of such public exoneration. Section 24(2) of the Arbitration Act 1950 was repealed by the Arbitration Act 1996.[4] Henceforth, fraudsters' activities would be shrouded in arbitral confidentiality.

4. This legislation, however, did not of itself necessarily unlock the door for fraud to become arbitrable. There was considerable handwringing as to the wording of arbitration clauses. Certain wordings were held to be wider than others. There was a reluctance to allow certain claims and in particular tortious claims

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ancillary to the contractual claim. This reluctance was swept aside by the Fiona Trust case. In a robust judgment Lord Hoffman examined the matter as to whether the words "*arising under*" and "*arising out of*" meant materially different things in law, and concluded:

> *"In my opinion the distinction which they make reflects no credit upon English commercial law."* [5]

5. He set out a new test as follows:

> "*…The construction of an arbitration clause should start from the assumption that the parties as rational businessmen are likely to have intended any dispute arising out of the relationship into which they have entered or proposed to enter to be decided by the same tribunal. The clause should be constructed in accordance with that presumption unless the language makes it clear that certain question were intended to be excluded from the arbitrator's jurisdiction*."

6. In particular, Lord Hoffman accepted that questions of fraud, bribery and misrepresentation were within the scope of an arbitration clause referring to "*any dispute under this charter…*", and so it is reasonable to suppose that the majority of arbitration clauses in use in shipping contracts will be wide enough to encompass such issues.

7. Lest there was any doubt as to the robustness of the Fiona Trust decision, in *Egiazaryan v OJSC and the City of Moscow* [6], Burton J addressed the arbitrability of torts head-on, and found that even foreign torts could be arbitrated in England even though they might not be closely connected to the contract entered into by the parties. In this regard the Judge had regard to the definition of an "*arbitration agreement*" in the Arbitration Act 1996:

> *"…an arbitration agreement means an agreement to submit to arbitration present or future disputes (whether they are contractual or not)"*[7]

The Meaning of "Fraud"

8. Having seen the tide change, the next question is to explain as far as possible, the meaning of "fraud" in this context. As long ago as 1759, Lord Hardwicke wrote:

> "*Fraud is infinite, and were a court once to define strictly the species of evidences of it, the jurisdiction would be cramped and perpetually eluded by new schemes which the fertility of man's invention would contrive"* [8]

9. The idea of 'fraud' as a self-standing legal concept is illusory, at least in a civil law setting. In a modern text, Paul McGrath QC describes "fraud" as follows:

> *"Fraud is notoriously difficult to define. That is because it is not an activity. X does not do fraud….It is effectively not an activity as such but the way in which an activity is performed … Fraud potentially pervades most commercial activity."*[9]

10. There exists a crime of "fraud" as defined by the Fraud Act 2006 namely: - fraud by representation; fraud by failing to disclose information and finally fraud by abuse of position. There is however no tort of "fraud". So in discussing "fraud", I will be seeking to identify those individual torts which underlie the fraudulent activity. Such torts are generally known as the "economic torts".

11. Before dealing with these torts, it is worth considering why fraud might become an issue in an arbitration. Inevitably, the dispute will have a contractual basis, as without a contract, there would be no arbitration agreement. Why then would a claimant not simply sue in contract? As this paper will seek to show, alleging fraud is complicated and therefore likely to be more expensive. Indeed it may serve a claimant better to abandon the fraud aspects of his claim and choose the simpler option of suing in contract. However, there may be any number of reasons why a claimant might wish to allege "fraud".

12. First of all there are some cases which demand an assertion of fraud, as it would be impossible to characterise the claim in any other realistic way. Ante-dated bills of

lading are one such example. Alternatively a claimant may have sought and obtained a freezing order on the basis of an allegation of fraud and will need to make good on his belief as stated to the court. This might be one of many associated actions (for example in conspiracy), which is forced into arbitration by the existence of an arbitration agreement.

13. Other factors which might also be perceived by a claimant as relevant are to avoid an exclusion or limitation clause, or to obtain a more generous damages regime. Finally, a robust claimant might simply wish to obtain greater leverage for the purposes of settlement negotiations (although fraud should never be alleged unless there is a proper basis for doing so). An allegation of fraud against an individual director of a company will certainly concentrate his mind, even though he is not actually a named respondent. In short, there are any number of reasons why a claimant or indeed a respondent might wish to assert fraud in arbitration.

Identifying the Underlying Tort

14. A lawyer or arbitrator steeped in shipping law approaches the economic torts at a disadvantage. We are used to a world of standard form contracts, and well developed jurisprudence on a narrow range of topics. From time to time, different situations produce surprises, but the train usually runs along familiar tracks.

15. The economic torts, by contrast, run in numerous directions, and the authorities are drawn from diverse sources. By way of illustration of the random nature of those sources, I take three examples:-

    a. A master of a slavery ship warning off his competitors with a cannon[10].
    b. The picketing of businesses by trades unions[11].
    c. The merchandising of exclusive pictures of Catherine Zeta Jones' wedding by "Hello" magazine[12].

16. It is not only contract lawyers who have found the economic torts difficult to grasp. In Lord Hoffman's speech in *OBG v Allen*[13], his Lordship, in dealing with certain of the economic torts, roundly criticised the judgments in a number of venerable cases[14] as having created a 'muddle'. Those judges had apparently erred by adopting what was known as the 'unified theory', namely a general tort of actionable interference with contractual rights, involving various sub-species. Not so – according to Lord Hoffman, there were few if any general principles of tort. Henceforth the tort complained of should be clearly identified, and should fall within the category circumscribed by the law relating to that particular tort[15] .

17. Such reasoning should mean that subsequent judgments identify precisely the tort, so that the asserted tort can be placed within a judicial pigeon-hole. Whether it can truly be said that this direction has been followed by successive court decisions is questionable, but more a matter for academic debate than for this forum. Be that as it may, Lord Hoffmann's dictum holds true for practitioners. We must seek to identify the tort alleged with some precision, and to ensure that the circumstances giving rise to that tort fall within the parameters judicially ascribed to that tort.

18. But why might such diverse and arcane torts be of interest to the maritime community? Although the economic torts have developed primarily in the areas of competition or employment law, they increasingly provide a vehicle by which commercial misconduct can be challenged. Shipping and trading companies are well experienced in using corporate vehicles to ring-fence liabilities. In the great majority of cases such a use is entirely legitimate. However, companies and the individuals controlling them can and do overstep the mark on occasion. Equally, practices which might in former days have been regarded as "tricks of the trade" might well be regarded as unlawful nowadays. The economic torts provide a vehicle to "*curb clearly excessive conduct*"[16] in certain circumstances.

19. I now set out to identify in turn those torts which may come before a maritime arbitrator and to set out, but restrict myself, to the essential elements of those torts.

Deceit

20. The first of the torts which requires identification is the tort of deceit. Paul McGrath comments:

> '*Deceit is the closest the English law of tort comes to fraud'*[17]

And indeed deceit will be familiar to maritime arbitrators, the most obvious examples being the back-dating or other infelicities relating to the issue of bills of lading[18]. Perhaps the case which most comes to mind here is the case of *Brown Jenkinson v Percy Dalton (London) Ltd*[19], relating to the deceitful issue of clean bills of lading.

21. The elements of deceit have recently been reviewed by the Court of Appeal. The elements of the tort are:-

1) The defendant makes a false representation to the claimant.
2) The defendant knows that the representation is false, alternatively is reckless as to whether it is true or false.
3) The defendant intends that the claimant should act on it
4) The claimant does act in reliance on it[20].

22. If the contract was induced by a misrepresentation, a claimant will more usually find it easier to pursue a case for damages or rescission under the Misrepresentation Act 1967 than a claim at common law.

Causing Loss by Unlawful Means

23. It is when we come to this point that we begin to see the complications referred to earlier in this paper. Even the Supreme Court judges have had difficulties with analysing this tort, and there have been significant disagreements between those

judges as to the scope of the tort. Academics are no less interested[21]. In my view, the most accessible judgment on this topic (and on unlawful means conspiracy discussed below) is that of Morgan J in *Digicel v Cable and Wireless*[22]. The judge compares the various views as to the nature of the tort and states a preference for the view that the law seeks to '*curb clearly excessive conduct. The law seeks to provide a remedy for intentional harm caused by unacceptable means"*[23].

24. The 'unacceptable' and therefore 'unlawful' means include tortious activity, crimes and breaches of contract[24].

Inducing a Breach of Contract

25. There is an inducement to breach a contract if a person having knowledge of a contract between two other persons induces one of those persons to breach that contract and causes loss to 'the innocent party'. Although this is on the face of it a similar tort to that of Causing Loss by Unlawful Means, Lord Hoffman's judgment in *OBG v Allan* makes it clear that they are separate. Although the cases have generally involved contracts of employment, it is not difficult to envisage a maritime scenario where one party in a charterparty or sale of goods chain seeks to enhance his own interests by interfering with contractual relationships in other parts of the chain. An example of this type of tort in the maritime sphere is the case of Stocznia Gdanska SA v Latreefers Inc[25] where the parent company was held liable for inducing the breach of contract by its subsidiary (although it is not clear whether the basis for the decision has survived Lord Hoffman's remarks in the subsequent case of OBG v Allan).

Unlawful Means Conspiracy[26]

26. The elements of this tort are as follows:

    1) Two or more persons must 'combine' (i.e. conspire);
    2) The conspirators must use 'unlawful means';

3) The conspirators must intend to cause damage to the claimant, although this need not be the conspirators' predominant intention;

4) The claimant must suffer loss as a result.

27. It has been suggested that conspiracy is not a suitable matter for arbitration, because only one of the alleged conspirators, namely the conspirator who was party to the arbitration agreement, could be a party to the arbitration to the exclusion of the other conspirators. That suggestion was exemplified in the case of in *Egiazaryan v OJSC and the City of Moscow*[27], where a panel of prominent arbitrators took this view.

28. However, on appeal from the award, Burton J was puzzled by that finding and took the opposing view. He stated:

> "*No authority is cited and the suggestion is really that no conspiracy claim can be brought within an arbitration agreement, because a conspiracy always needs more than one party. It is my experience that the fact that there may be outstanding claims against other parties arising out of the same facts is not an objection to the bringing of a claim which falls within the terms of an arbitration clause.*"

Conversion

29. Conversion occurs where a person interferes with the personal property of another, so as to amount to treating the property as his own, and conversely not as the property of the true owner. It is now codified by section 2(2) of the Torts (Interference with Goods) Act 1977.

30. The damages will be the value of the goods at the time of the conversion. The tort of conversion is more likely to appear in Sale of Goods arbitrations than shipping arbitrations. There is statutory protection for a buyer who buys from a seller lacking title, if the buyer purchases in good faith[28].

Bribery

31. The elements of bribery are:

    a. A person makes payment to an agent or representative of another person with whom he is dealing;
    b. he makes the payment knowing that the payee is acting as the agent of the other party;
    c. he fails to disclose to the other person with whom he is dealing that he has made such payment.

32. The tort does not require the money to be paid or received dishonestly, as fraud will be presumed. It is also presumed that the briber paid the bribe in order to obtain a benefit in the context of the transaction with the principal, although it should be said that these presumptions will not apply to small gifts. In relation to shipping arbitration, the best known example of alleged bribery is, of course, the Fiona Trust case itself.

Piercing the Corporate Veil

33. The starting point for any case involving piercing the corporate veil is that the company is an entity distinct from its directors or shareholders[29] and the Courts and by extension arbitrators should view any argument to the contrary with considerable wariness.

34. The present position, according to Lord Sumption in *Prest v Petrodel Resources*, appears to be that the Court will pierce the veil in extremely rare cases:

> "*where a person is under an existing legal obligation or liability or subject to an existing legal obligation whose enforcement he deliberately frustrates by interposing a company under his control. The court may then pierce the corporate veil for the purpose, and only for the purpose of depriving the*

company or its controller of the advantage they would others have obtained by the company's separate legal personality."[30]

35. The remedy is only available if there is no other remedy. It is to be noted that there appears to be some tension as between Lord Sumption's view and Lord Neuberger's view in another previously decided case of *VTB v Nutritek*[31], as the latter judgment indicated that in order for the corporate veil to be pierced, the corporate entity must exist only as *"a façade to conceal the true facts*". Again, this appears to be a developing area of law.

Unjust Enrichment

36. Certain restitutionary claims will be regarded as a claim for "fraud", and therefore I mention here the concept of Unjust Enrichment. My focus, however, in this paper is fraudulent activity via the economic torts. As Unjust Enrichment has been developed from different roots, I therefore put down a marker as to its availability as a remedy but do not elaborate further in this paper.

The Treatment of Fraud in London Maritime Arbitration – Some Suggestions

37. Older practitioners may recall Lord Donaldson's famous quote:-

"*The shipping and commodity trades of the world are unusual in that they do not regard … arbitration with abhorrence. On the contrary, they regard it as a normal incident of commercial life – a civilised way of resolving the many differences of opinion which are bound to arise*." [32]

38. The introduction of fraud into this well-mannered environment is a clunking intrusion. There is little civilised about a fraud case. Heat will be raised. No matter how much the arbitration community might wish to avoid such turmoil, they are there to do justice and must grasp the nettle. This section of the paper endeavours to provide some suggestions as to how fraud claims might be dealt with.

39. The starting point is of course that arbitrators decide their own procedures suitable to the circumstances of the particular case[33]. Arbitrators are right when they refuse, as they often do, to follow slavishly certain aspects of court procedure. However, many of the court rules relating to fraud are based on policy considerations.

40. Lord Millet has set out the policy of the Court:

> *"an allegation of fraud or dishonesty must be sufficiently particularised, and that particulars of facts which are consistent with honesty are not sufficient. This is only partly a matter of pleading. It is also a matter of substance. As I have said, the defendant is entitled to know the case he has to meet. But since dishonesty is usually a matter of inference from primary facts, this involves knowing not only that he is alleged to have acted dishonestly, but also the primary facts which will be relied upon at trial to justify the inference. At trial the court will not normally allow proof of primary facts which have not been pleaded, and will not do so in a case of fraud[34]."* (underlining supplied)

41. The circumstances of a fraud case present different challenges to an ordinary contractual case. I now deal with various aspects of procedure which require sensitive handling.

Pleadings/Submissions

42. As noted, claims in fraud must be pleaded with proper particularity. Both barristers and solicitors are required by their professional bodies to take care in pleading fraud and only to do so if there is a *prima facie* case of fraud. The pleader

> *"should have material of such a character as to lead responsible counsel to conclude that serious allegations could properly be based upon it"[35].*

43. Although legally-qualified arbitrators, and particular barrister-arbitrators will be at home in the midst of the black arts of pleading, commercial arbitrators are understandably unsympathetic to such points – such antipathy being particularly pertinent when one of the parties is not represented by an English or common-law

lawyer. However, in fraud claims, arbitrators must insist on particularity in the submission, as directed by Lord Millett.

44. Balanced against this must be the obstacles faced by the claimant. Fraudsters do not advertise their misdeeds. A claimant will rarely be able to describe each aspect of the fraud precisely, until he has seen the disclosure. Significant parts of the claim submission may therefore be inferences from those facts which are known. As the case progresses, arbitrators might expect to see amendments to the claims submissions when disclosure is given as, if the claimant is right in his assertions, the factual position of the fraud will become clearer, and certain inferences will be replaced by facts.

45. Particularity is also required to allow the parties and the arbitrator to identify the tort alleged and how it properly fits into the judicial pigeon-hole as predicated by Lord Hoffman. A mere comment reciting facts, and concluding 'X thereby acted fraudulently' is to my mind plainly insufficient. If lack of particularity is challenged by the respondent, this should be the subject of an arbitral order that the submission be pleaded properly with each element of the cause of action set out.

Disclosure

46. Disclosure is invariably the battle-ground. The claimant will need it to prove his case. He will be looking not only for the documents which shows what the respondent did, but also the absence of those documents evidencing what he might have been expected to do, had he been behaving properly. The search for such absent documents is of course a search without limits. The advent of electronic disclosure has, counter-intuitively, only served to complicate matters yet further

47. On the other hand the respondent will deeply resent a 'fishing expedition' costing money and disrupting his business. Further, a dishonest respondent may be doing his utmost to conceal or delay the disclosure of incriminating documents. And the

tribunal have to come to decisions on this within the confines of the general duty of the Tribunal to run fair and cost- effective arbitrations[36]. Not an easy task.

Evidence

48. I now turn to the burden of proof. As this is a civil proceeding, the burden which the claimant has to surpass is the balance of probabilities. So far so good.

49. However, it is not as simple of this. Mr Justice Bingham (as he then was) refers to:

> *"the high standard required for proof of fraud in a civil case... a balance of probabilities appropriate to the seriousness of the charge, a standard falling not far short of the rigorous criminal standard"*[37]

50. Lewison J has said in similar vein:-

> "*Although the standard of proof is the same in every civil case, where fraud is alleged cogent evidence is needed to prove it, because the evidence must overcome the inherent improbability that people act dishonestly rather than carelessly. On the other hand inherent improbabilities must be assessed in the light of the actual circumstances of the case…"*[38]

51. Peter Macdonald Eggars QC suggests that in respect of deceit claims, the apparent contradiction can be reconciled:-

> *"This sceptical standard of proof, however, relates only to establishing the defendant's "deceitful state of mind", which one would take to mean the defendant's fraudulent knowledge and fraudulent intention. The other ingredients of the tort, such as the making of the representation, the falsity of the representation, the matter of materiality and inducement, and the question of damage, are all to be established in accordance with the civil standard of proof, without the scepticism, as usually applied to other torts, such as negligence."*[39]

52. Oral evidence in such cases is always going to be interesting. Unless the claimant's claim is fanciful, the parties' witnesses will have some difficult questions to answer. It is inevitable that there will be a conflict of evidence. Obviously falsehoods are not

unique to fraud claims, but they are invariably inherent in such claims, and it is the arbitrators who must resolve any such conflicts.

53. The arbitrators will consider each part of the oral evidence and test it in the context of corroborating or conflicting documentary evidence and the evidence of the other witnesses. Judging the case on the demeanour of the witness is, however, dangerous ground. Scientific studies have shown that the prospects of detecting lies are about 50%[40] - namely the toss of a coin. A quote from the recent obituary of the eminent Supreme Court judge Lord Toulson identified his view of this issue:

> *"Years of doing my particular area of law led me to believe that some of my clients who I thought were absolutely the most honest were the most awkward and shifty in the witness box, whereas others who I thought were total rogues came across with great smoothness and self-assurance"*[41]*.*

However, despite the common reluctance to brand any witness a liar, an arbitrator's function is to administer justice. Justice may require him to overcome his misgivings.

Conclusion

54. The law reports evidence considerable growth in cases involving the economic torts over the last five years. Inventive lawyers are increasingly regarding these as effective weapons in the right cases. As arbitration is based on contract, such growth will presumably not materialise at the same rate in arbitration, but the likelihood exists and presents challenges. In order to dispense justice, arbitrators must rise to such challenges.

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[1] *Under section 24(2) of the Arbitration Act 1950:*
"Where an agreement between any parties provides that disputes which may arise in the public between them will be referred to arbitration, and a dispute which so arises involved the question whether any such party has been guilty of fraud, the High Court shall, so far as may be necessary to enable that question to be determined by the High Court, have the power to order that the agreement shall cease to have effect and power to give leave to revoke the authority of any arbitrator or umpire appointed by or by virtue of the agreement."
[2] *Arbitration Law para 3.23 Robert Merkin (Lloyds Commercial Law Library)*
[3] *(1939) 64 LI L Rep 145, 146*
[4] *s.107(2)*
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[6] *[2015] EWHC 3532 (Comm)*
[7] *Section 6 (1) Arbitration Act 1996*
[8] *Letter to Lord Kames – cited in Holdsworth 'A History of English Law (1972) vol 12 , at 262 (quoted by Ross Fentem and Lucy Walker of Guildhall Chambers – "Civil Fraud – Back to Basics")*
[9] *Commercial Fraud in Civil Practice- Paul McGrath QC 2nd edn para 1.07*
[10] *Tarelton v M'Gawley (1793) Peake 270*
[11] *E.g. Thomas v NUM [1986]1 WLR 20*
[12] *Douglas v Hello! (No 3) [2007 UKHL21*
[13] *OBG v Allan [2007]UKHL 21*
[14] *Quinn v Leatham [1901] AC 495GWK Ltd v Dunlop Co Ltd; DC Thomason & Co v Deakin [1052] Ch 646; Torquay Hotel Ltd v Cousins [196]*
[15] *See OB G v Allan ibid at page 27 para 32, where Professor Cane's text is quoted with approval*
[16] *OBG v Allan ibid per Lord Nicholls at para 153*
[17] *Commercial Fraud in Civil Practice Paul McGrath QC 2nd edition para 2.02 (OUP)*
[18] *See Standard Chartered Bank v Pakistan National Shipping Corporation various judgments 1995-2002*
[19] *[1957] 2 Lloyds Rep 1*
[20] *Eco3 Capital v Ludsin Overseas [2013] EWCA Civ 413*
[21] *See in particularly The Analysis Of Economic Torts 2nd edition by Hazel Carty (OUP)- a thought provoking analysis much quoted by courts in a number of jurisdictions*
[22] *[2010] EWHC 774 Appendix I.*
[23] *Ibid page 521*
[24] *Total Network v HMRC [2008] UKHL civ 39*
[25] *[2002] 2 Lloyd's Rep 436*
[26] *There is also a tort of Lawful Means Conspiracy, which is sufficiently rare not to warrant inclusion here*
[27] *[2015] EWHC 3532 (Comm)*
[28] *s 21, 24, and 25 Sale of Goods act 1979; s 2 Factors Act 1889*
[29] *Saloman v Saloman[1897] AC 22*
[30] *Prest v Petrodel Resources Ltd [2013] UKSC 34 at [35]*
[31] *[2013] UKSC 5*
[32] *Pando Compania Naviera SA v Filmo SAS [1975] Q.B. 742, 745*
[33] *Arbitration Act s 33(b)*
[34] *Three Rivers District Council v Governor & Company of the Bank of England (No. 3) [2003] ZAC-1 paras 183-188*
[35] *Medcalf v Mardell [2003] UKHL 27*
[36] *S 33 Arbitration Act 1966*
[37] *The Zinovia [1984] 2 Lloyds Rep 264, 272*
[38] *Foodco UK LLP v Henry Boot Developments Ltd [2010] EWHC 358 (Ch) at [3]*
[39] *Deceit: The Lie of the Law, Peter Macdonald Eggars QC – at para 1.58 (Informa)*
[40] *The Face by Daniel McNeill (Penguin) 246*
[41] *Obituary , The Times June 30th 2017*

Biography

Charles Williams is a partner at the London law firm of Thomas Cooper LLP. He qualified as a solicitor in 1979, and has specialised in shipping and trade litigation and arbitration cases since then. He is a Supporting Member of the LMAA and a former Chairman of the BMLA Sub-Committee on Arbitration and ADR. He is also a Visiting Professor of City, University of London, where he lectures on Carriage of Goods.