INTRODUCTION OF COUNTERCLAIM OR SET-OFF IN PROCEEDINGS FOR THE ENFORCEMENT OF AN ARBITRAL AWARD UNDER THE NEW YORK CONVENTION, 1958.

- *Mohit Pandey*
India qualified lawyer presently pursuing LLM at MIDS, Geneva.

Introduction

Although arbitration as a method of resolving a dispute is ancient, it can easily be assumed that it received true universal recognition only in the nineteenth century. The emergence of the New York Convention, 1958 [hereinafter "**the Convention**"],[1] brought various jurisdictions on one stage with the essence of accepting and enforcing awards passed in foreign states. The idea is based on reciprocity and mutual recognition of legal proceedings. The Convention provides for international legislative standards for the recognition of arbitration agreements and the recognition and enforcement of arbitral awards in almost all parts of the world.

The Convention also prescribes specific grounds to refuse recognition or enforcement.[2] Parties have also attempted to resist or equalise the award through a counterclaim or setoff. A *counterclaim* is a claim filed by a defendant arising out of the same or related agreement under which disputes have arisen. In contrast, *setoff* is a process of reducing or discharging a debt of one claim against another.

The Convention does not manifestly refer to counterclaims or set-offs, but they might be derived from Article III of the Convention. In enforcement proceedings, a court may grant the enforcement of a counterclaim when it is proper, equitable and not inconsistent with the Convention.[3] In practice, a set-off may come in the arbitral process in the form of a counterclaim when the amount of a set-off claim exceeds that of the original claim. A set-off claim is rarely accepted in enforcement proceedings as a ground for refusing to enforce an arbitral award under the Convention in courts of both common and civil law countries.

[1] United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (Date of Adoption 10 June 1958, entered into force on 06 June 1959) ('New York Convention')
[2] Ibid. Art V.
[3] Review of a Foreign Arbitral Award by National Courts: A comparative Ihab Amro*

For reasons of procedural economy, it has been argued that, in addition to the requirement of a close connection between the relevant contracts, counterclaims should only be admitted if the counterclaims themselves are closely connected to the main claim.[4] By imposing the additional requirement of a close connection between claim and counterclaim, the respondent is supposed to be prevented from raising only vaguely related counterclaims in an attempt to delay the arbitral proceedings. Notwithstanding, except if the parties settle on procedural rules imposing such an extra requirement, the better contentions militate for admitting the counterclaims to the extent that they are covered by the arbitration agreement.

To this specific question, whether counterclaims or setoff can be urged during an enforcement proceeding, the Courts of the Contracting States are divided and have taken distinct routes,[5] depending on the jurisdiction and jurisprudence. This paper analyses the position of Courts in the following jurisdictions:

a. *The United Kingdom*
b. *The United States of America*
c. *Germany*

Analysis of Various Jurisdictions

The United Kingdom

Even though the Courts in the UK have generally discarded counterclaims in enforcement proceedings, it seems like they continuously attempt to explore some connection between the claim and counterclaim to consider the merits of enforcement beyond the limitations of the Convention.

In a recent judgment of *Selevision Saudi v. BMG,*[6] the English High Court considered whether the court's procedure allowed it to adjudicate a counterclaim in an application for enforcement under the Convention.[7] The parties entered into a 'Distributor Agreement' wherein BMG retained Selevision as a non-exclusive distributor of set-top boxes. However, certain disputes arose, which were referred to arbitration under DIFC-LCIA Rules with the seat at DIFC, Dubai. On 5 June 2018, the Arbitral Tribunal rendered its award holding BMG in breach of the contract and awarded

[4] New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 10 June 1958 Article-by-Article Commentary edited by Dr. Reinmar Wolff Second Edition 2019
[5] 304 Procedure for Enforcement - Sett-Off/Counterclaim, in Albert Jan van den Berg (ed), *Yearbook Commercial Arbitration* Vol. XXI (Kluwer Law International; ICCA & Kluwer Law International 1996) 467.
[6] *Selevision Saudi Company v. BEIN Media Group LLC* [2021] EWHC 2802 (Comm) .
[7] Ibid 1.

US$ 8 million to Selevision. BMG's application before the DIFC Court to set aside the award was also rejected.

Selevision filed for enforcement of the award before the present court as a foreign award.[8] The Court, dismissing BMG's application for counterclaim, held that: Firstly, the balance is against permitting any such counterclaim because the counterclaim is proposed in a 'claim' for enforcement of Convention Award and allowing it could result in a practical impediment to enforcement of such awards;[9] secondly, there needs to be a degree of connection between the proposed counterclaim and the existing claim, which was not the case here.[10]

In *Tonguan (USA) v. Uni-Clan Ltd.,*[11] a dispute arose between the parties regarding the performance of machines sold by the Respondent. Tonguan initiated arbitration; however, Uni-Clan chose not to participate. On 6 April 1999, the Tribunal rendered its award holding that the machines were defective, and the seller ought to refund the amount along with interest.
The question before the English High Court was whether it should set aside the order of *Master Miller* granting leave to enforce the award on the grounds that the award is a nullity because the proceedings took place at a different place than the one agreed to, and secondly, whether a summary enforcement of the award would deprive the opportunity for consideration of any 'cross-claim'.

Rejecting the application, the Court held that removing the proceedings from one place to another did not affect the curial law.[12] Finally, regarding the counterclaim, the Court observed that it is not aware of any case in which Courts have agreed that it would be inappropriate to allow a Convention Award only because the judgment debtor has an arguable cross-claim.

The United States of America

The US Courts do not act beyond their role as a court of recognition prescribed under the Convention. In such a strict interpretation, the scope to urge counterclaim/setoff is nil. This approach can be construed as a positive one in upholding the essence of the Convention.

[8] Ibid Arbitration Claim Form filed by the Claimant 9.
[9] Ibid 42 (1).
[10] Ibid 42 (2).
[11] *Tonguan (USA) International Trading Group v. Uni-Clan Limited* UK 58 Yearbook Commercial Arbitration, A.J. van den Berg (ed.), Vol. XXVI (Kluwer Law International; ICCA & Kluwer Law International 2001).
[12] Ibid 8.

In *Mangistaumunaigaz Oil Production v. United World Trade*,[13] disputes arose between parties regarding an agreement to sell crude oil. MOP initiated arbitration, to which UWT declined from participating, stating that it never agreed to arbitrate. Accordingly, the Tribunal rendered its award in favour of MOP, which in turn filed for recognition of the award before the Colorado District Court. In the 'Motion to Confirm', the Respondent asserted four counterclaims. Rejecting the argument, the Court held that the Convention does not provide any basis for counterclaims. The Court further observed that in a confirmation proceeding, the Convention only allows for a limited attack on the validity of a claim, and adjudicating a counterclaim is inappropriate.

In *China Three Gorges v. Rotec Industries*,[14] claims arose on the backdrop of an accident due to the failure of a machine provided by the Respondent. The Claimant invoked arbitration for damage which was awarded in its favour. Subsequently, it filed for partial enforcement in China and the Delaware District Court for the remaining amount. The Respondent resisted confirmation on the ground that the amount can be set off against other dues owed by the Claimant to the Respondent. The Court rejected the contention of Rotec and held that only grounds enumerated in Article V of the Convention are available for setting aside an award, and the existence of outstanding receivables is not a ground for refusal. The Court further observed that its role is limited to reviewing the challenge, and due to the limited nature of the proceeding, setoff is not suitably before the Court.

However, in the case of *Jugometal v. Samincorp, Inc*,[15] the U.S. District Court granted enforcement for the award made in favour of the plaintiff and for those counterclaims made in favour of the defendant, reasoning: "It would be inequitable to permit this plaintiff to recover a judgment here against the defendant on the concededly valid arbitral award in its favour, and at the same time to withhold enforcement of the three counterclaims here, requiring Samincorp to seek their enforcement separately in a foreign tribunal or wherever Jugometal can be found".

Germany

The German Courts have treated the question of setoff/counterclaim in an enforcement proceeding differently than the UK and the US Courts. The German Federal Supreme Court permits parties resisting enforcement to raise the issue of a counterclaim based on circumstances.

[13] *Mangistaumunaigaz Oil Production Association v United World Trade Inc*, 17 June 1997, Civil Action No 96-WY-1290-WD (US District Court, District of Colorado).
[14] *China Three Gorges Project Corporation v. Rotec Industries, Inc*. 2 August 2005, Civil Action No 04-1510- JJF (US District Court, District of Delaware).
[15] Jugometal v. Samincorp, Inc.,1978, D.C.N.Y, no. 78 F.R.D. pp. 504,06,07

The basis of this is found in the German Code of Civil Procedure (ZPO),[16] which provides that a defendant may raise grounds against a judgment of the State Court provided the grounds arose after the judgment was delivered.[17]

In a decision dated 30 September 2010,[18] the Federal Court of Justice considered the implication of ZPO in an arbitration proceeding. In this case, the parties entered into a contract for the delivery of sugar. Disputes arose between parties, and arbitration was invoked under the aegis of the Refined Sugar Association of London. The Tribunal rendered its award and declined from ruling on the counterclaims and setoff, holding that they were based on a separate arbitration agreement. The Court in the confirmation proceeding held that the setoff claim is admissible only if 'it arose either after the conclusion of arbitration proceedings or exceptionally if it arose during the arbitration and the Arbitral Tribunal did not rule on it'. The Court further held that in case the Tribunal abstains from ruling on setoff, the claim can be reiterated before the enforcement court, irrespective of the reason why the Tribunal refused to deal with the setoff.

In *OAO C v. Y GmbH & Co.*,[19] the Higher Regional Court of Hamburg granted recognition of an award passed by ICC Vienna. The case pertained to the sale of production lines between a German seller and a Russian buyer. The buyer invoked arbitration alleging that the lines were defective. The Arbitral Tribunal rendered its award in favour of the buyer. The judgment debtor sought correction in the award, stating that the monies owed by either party should be setoff. The Tribunal rejected the prayer saying this is a new claim and was never contended during the proceedings. The Respondent, in the enforcement proceedings, contended that the award violated public policy as it was not allowed to present an anonymous witness, plus the Tribunal did not consider its setoff request.

The Court rejected both the arguments of the Defendant and held that although in principle a setoff and its effect on discharge must be deliberated in proceedings for enforcement, it does not apply when the setoff falls under the arbitration agreement, and the opposing party relies on that agreement. The Court further observed that the Federal Supreme Court does make an exception when the arbitral tribunal has ruled on the counterclaims as it fulfils the purpose of the arbitration agreement. The Court concluded holding that the Respondent is not barred from raising the setoff, but it will have to do so in a fresh proceeding before an Arbitral Tribunal.

---

[16] Section 767(2) ZPO.
[17] Borris/Hennecke, in: Wolff, *NYC*, (2nd ed. 2019), Art. V page 261.
[18] Docket No. III ZB 57/10.
[19] *OAO C v. Y GmbH & Co. KG, Hanseatic Higher Regional Court of Hamburg*, Case No. 6 Sch 2/11, 3 February 2012, Germany 157 Yearbook Commercial Arbitration, A.J. van den Berg (ed.), Vol. XLI (2016).

It is pertinent here to note this case in the Court of First Instance of Hamburg[20], the respondent opposed the enforcement of an arbitral award made in favour of the Romanian claimant, based on violation of public policy, because setoff claim for damages had not been considered by the arbitral tribunal. In the enforcement proceedings, the respondent led another set-off based on commissions due to it for representation of the Romanian seller. The court denying the respondent's contention held:

> *"According to Article III of the New York Convention, the enforcement takes place in accordance with the rules of procedure of the country where the award is relied upon, this procedure includes the decision concerning a set-off. Under German law, an undisputed set-o# may be brought forward in an enforcement procedure, when it could not have been dealt with in the arbitral proceedings. The latter was the case with the commission on the basis of the representation made by the respondent on behalf of the Romanian Firm C."*

The Court of Appeal affirmed and corrected the lower court's decision, referring to a previous decision made by the Supreme Court.

Conclusion

The approach of civil law countries like Germany borders on inconsistency with the Convention, as allowing any review of merits at the enforcement stage defeats the purpose of the Convention, i.e., to facilitate and expedite exequatur proceedings.[21] Moreover, the standards for those reconsiderations are set quite high. However, courts do accept a setoff claim in Germany when it is not dealt by the arbitral proceedings. Contrary to this, common law countries like the UK and the US approach the enforcement proceedings in their true essence wherein no reconsideration of merits beyond the Convention is entertained. USA, at times does have a diverse view on counter claim defences as seen from the above judgements. These jurisdictions display a pro-enforcement bias. This approach ensures speedy recognition/enforcement proceedings and encourages the use of arbitration as a dispute resolution mechanism.[22]

[20] Firm C (Romania) v. German (F.R) Party, 27 March 1974
[21] *Borris* n(14) 262.
[22] Ibid.