SPARE WHEEL ARBITRATORS

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Introduction

Arbitrator-umpire clauses are widespread but troublesome. Were umpires killed off by the Arbitration Act 1990? Does the appointment of an umpire leave an arbitrator free to retain a special connection with his or her appointing party? What is the umpires role during the substantive hearing? Must the parties put up with the cost and delay of three arbitrators rather than one? Are umpires unnecessary spare wheels?

This paper considers those questions en route to two conclusions. One is that umpires are legally alive and well. The other is that the parties would often be better off adopting some other approach.

What is an umpire?

Under a typical arbitrator-umpire clause, each party chooses its own first-tier arbitrator, the first-tier arbitrators choose a second-tier arbitrator, and the second-tier arbitrator steps in if the first two are unable to agree. In this configuration the second-tier arbitrator is traditionally known as an umpire. The umpire is essentially a spare wheel to be used if and when there is a puncture: he or she is wheeled in only if needed to fix an impasse.

An arbitrator-umpire clause may be as simple as the following:

> The arbitration shall be by reference to two arbitrators one to be appointed by each party and then (if the arbitrators cannot agree) to the decision of an umpire to be appointed by the two arbitrators.[1]

More elaborate clauses are often found in leases, a typical one being:

a. [provision for renewal of lease at a rent to be determined on expiration by effluxion of time]

b. Within six calendar months previous to the expiry by effluxion of time of the lease hereby granted or so soon thereafter as may be a valuation shall be made of the fair annual rent of the land hereby demised so that the rent so valued shall be uniform throughout the first five year period of the renewed lease.

c. The said valuations shall be made by two indifferent persons as arbitrators one of whom shall be appointed by the Lessor and the other by the Lessee.

d. The arbitrators before commencing to make the said valuations shall together appoint a third person who shall be an umpire as between them.

e. The decision of the two arbitrators if they agree or in such respects as they agree or of the umpire if the arbitrators do not agree or in such respects as they do not agree shall be binding on all parties.

f. The duty of the umpire on reference to him of any questions shall be to consider the respective valuations of the two arbitrators in the matters in which their valuations do not agree and then to make an independent and substantive valuation and the last-mentioned valuation shall be the decision of the umpire but in giving his decision on any question so referred to him the umpire shall in every case be bound to make a valuation not exceeding the higher and not less than the lower of the valuations made by the arbitrators respectively.[2]

However phrased, and whether imposed by contract or statute, arbitrator/umpire clauses have always been a central feature of the New Zealand arbitration landscape.

What impact did the Arbitration Act 1996 have on umpires?

Whether umpires survived the Arbitration Act 1996 has been a matter of much uncertainty in the arbitration world. Of the two local leading texts on the subject, one considered that the 1996 Act effectively ended the historical reign of the umpire[3] while the other considered that umpires are something which the parties may continue to stipulate for if they wish.[4] The Law Commission appears to have thought that the 1996 Act did away with them[5] but in at least one case since the Act was passed, a Court has appointed a new one.[6]

The cause of the uncertainty is the lack of express reference to umpires in the 1996 Act. Whereas the Arbitration Act 1908 expressly provided for their appointment, the 1996 Act ignores the whole subject. In its place, the new Act has the following features:

Arbitral tribunal and arbitrator are the expressions used at many points to define the powers and duties of arbitrators. Arbitrator is not defined but arbitral tribunal is defined in s 2(1) as a sole arbitrator or a panel of arbitrators.

If the arbitration clause in the contract is silent as to the number of arbitrators, the default is three arbitrators for an international arbitration and one for a domestic one.[7] There is no suggestion that one of the three arbitrators is there only to break any impasse between the other two.

The transitional provision for appointment of umpires under old agreements is theoretical only, being limited to cases in which (i) thearbitration agreement was made before 1 July 1997 (ii) the agreement provided for appointment of two

> arbitrators but made no contractual provision for appointment of an umpire and (iii) arbitral proceedings were commenced between 1 July 1997 and 18 October 2007..[8]
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> Failing agreement on the process of appointment for a three arbitrator panel with two parties, each party appoints one arbitrator, the two arbitrators appoint a third arbitrator[9] and in the absence of agreement on the third arbitrator, the Court appoints an arbitrator.[10]
>
> The default position over decision-making is that any decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members.[11] That may be compared with the more limited role of an umpire who steps in only if the two arbitrators cannot agree.

At no point in the 1996 Act does the word umpire figure. Nor is there express provision for an impasse-breaking arbitrator by any other name. At least in the absence of any express contractual term to the contrary, an arbitral tribunal of three arbitrators confers equal status and functions on all three.

It may not be surprising, therefore, that many thought that the 1996 Act abolished umpires. But is that really the case?

The starting point is the absence of anything in the Act precluding umpires. The fact that the Act provides default positions[12] does not impliedly exclude other approaches if the parties so prefer. In particular, the provisions for the appointment of three arbitrators, and decisions by a majority, are expressly stated to apply only in the absence of agreement to the contrary. So there is nothing expressly there to prevent the parties from providing in their agreement that one arbitrator is to be appointed by the other two, and that instead of decision by a majority, there is to be a decision by two with the third kept in reserve unless the others are unable to agree.

The second point is that the words arbitrator and umpire are not mutually exclusive. Arbitrators come in different forms. What matters is not the terminology but the substance.[13] The substance is gleaned from Parliamentary intention (in the case of those specialist statutes which impose arbitrator-umpire clauses on the parties) or the intention of the parties (for those contracts that choose to adopt such clauses voluntarily). Umpires are subsumed within the broader expression arbitrator.[14] As Elias CJ pointed out:

> In my view, it makes no difference that under the 1996 Act the term "umpire" is not used. Arbitration under the 1996 Act results from the submission of disputes by agreement to the determination of an "arbitral tribunal". The Act defines an "arbitral tribunal" as either a "sole arbitrator" or "a panel of arbitrators". The term "arbitrator" is not defined. It is not a term of art. It refers to a person appointed under an agreement to decide disputes between the parties. It includes an umpire.[15]

There is no reason in principle why a particular sub-species of arbitrator traditionally known as umpires should not be subject to a regime providing for their appointment in a particular way and giving them a particular role in the decision-making process.

The third point is that to prevent the parties from adopting an arbitrator-umpire formula would be contrary to the party autonomy philosophy underlying the 1996 Act. Both before[16] and after[17] the Act the courts have gone to considerable lengths to uphold the right of the parties to choose the form of arbitration they want. If the parties want an umpire, it is difficult to see why they should be denied one.

Party autonomy assumes particular significance when consideration is given to the volume and history of arbitrator-umpire clauses in New Zealand.[18] They are enshrined in over 100 statutes imposing an arbitrator-umpire formula upon, or requiring the inclusion of such a clause in, the rules or contracts of parties to specified types of contract.[19] A simple example is s 109 of the Building Societies Act 1965 which provides:

> **109. Determination of disputes by arbitration**
> (1) This section shall have effect where a society's rules direct that disputes shall be referred to arbitration.
> (2) Every such reference to arbitration shall be
> (a) To a sole arbitrator agreed on by the parties to the dispute; or
> (b) If the parties do not agree on a sole arbitrator, to 2 arbitrators, one to be appointed by each party to the dispute, with power to the 2 arbitrators to appoint an umpire.

The First Schedule to the Public Bodies Leases Act 1969 alone is a prolific source of leases containing arbitrator-umpire clauses. Nor are such clauses confined to those generated by statute. For years parties to leases, construction contracts, and other types of contract, have voluntarily chosen that formula. Whether they were wise to do so is another matter. But it would be surprising if the 1996 Act were intended to repudiate the expectations of Parliament in so many statutes, and that of the parties in so many contracts, over so many years. The fact is that what Parliament and contracting parties have asked for in those cases is two first-tier arbitrators who appoint an impasse-breaking second-tier arbitrator, not three first-tier arbitrators. To give them something else would be to overrule what they asked for.

It seems safe to conclude that the Arbitration Act 1996 did not abolish umpires. All it did was to include them in the generic word arbitrator for the purposes of that statute. This does not appear to have changed anything of substance. The effect of the typical arbitrator-umpire clause will continue to be that the umpire is appointed by party-appointed arbitrators and that the umpire will continue to step in only if and when the party-appointed arbitrators are unable to agree.

Does the appointment of an umpire leave the arbitrators free to retain a special connection with their appointing parties?

Another major uncertainty in the arbitration world has concerned the effect of an arbitrator-umpire clause on the nature of the relationship between arbitrators and their appointing parties.

Sketching in the factual background to a recent arbitration case in New Zealand, the Judge noted in passing that:

> The Board and Mr Brown have respectively appointed Messrs [A] and [B] as arbitrators. Both are highly qualified and experienced real estate valuers. But, *acting on instruction of their appointers*, the arbitrators have been unable to agree informally on appointment of an umpire. Mr [A] has nominated [C], also a highly qualified and respected real estate valuer. Mr B has nominated [D], a distinguished retired Judge of this Court who has considerable experience in conducting rental arbitrations. (emphasis added).

What is disturbing about that case is not the inability of the arbitrators to agree but the fact that, even after their appointment, these very experienced arbitrators saw themselves as still subject to riding instructions from their appointers.

Nor would the arbitrators in that case seem to be alone in that view. For a long time there was a perception that the provision for an umpire left the arbitrators free to retain a special relationship with, and sympathy for, the particular party that appointed them.[20] On that perception, natural justice and its requirements of independence and impartiality could be safely left to the umpire.

Clearly the law has moved on since then. If the process wanted by the parties is arbitration, they can not contract out of the natural justice requirements of Arts 12, 18 and 34(2)(b)(ii) of Schedule 1.[21] Arbitrators remain arbitrators whether or not there is an umpire.[22] All members of an arbitral tribunal are subject to the natural justice requirements of independence and impartiality. So in a recent rent review case based on an arbitrator-umpire clause, the lessor was held entitled to object to the arbitrator nominated by the lessees on the ground that she was neither independent nor impartial. The fact that there would be an umpire was no answer to her lack of independence. [23]

This has clear implications for valuers, engineers, lawyers, and other professionals who may be approached in the first instance to undertake professional work for a client. Once that relationship has been formed, it will normally be too late for them to then accept appointment as an arbitrator in relation to the same subject matter, with or without provision for the appointment of an umpire.

Rent reviews illustrate the point. They typically make provision for valuers to prepare a valuation for each side before there is perceived to be a dispute, and therefore before the necessity for an arbitration is anticipated. It is difficult to see how a valuer who has already provided a valuation to a party could be free to accept appointment as an arbitrator.

Even more clear is the ban on unilateral communications between an arbitrator and one of the parties without the participation of the other. There can be an exception for communications of a purely administrative nature but even this is better avoided. It generates suspicion and the possibility that a breach of natural justice will be alleged. If the unilateral communication

happens to be between the arbitrator and the party which appointed that arbitrator, the suspicion will be all the greater.

What is an umpires role during the substantive hearing?

A third area of uncertainty has been the role of an umpire during the substantive hearing.

Strictly interpreted, arbitrator-umpire clauses normally deny an umpire any active role prior to a first-tier disagreement. For a clause of the *Bowport*type quoted earlier, the umpire is not even appointed unless and until the disagreement arises. For a clause of the *Cornwall Park Trust Board* type quoted earlier, the umpire is appointed at the outset but is given no formal role unless there is a disagreement. At that point the duty of the umpire on reference to him of any questions shall be to consider the respective valuations of the two arbitrators . There is no suggestion that the umpire has any active role unless and until that occurs.

The result is that there is no formal basis for umpires to participate in any of the interlocutory processes that precede the substantive hearing nor any formal basis for them to attend the substantive hearing itself. If they do attend the substantive hearing, they can be an embarrassment in the absence of agreement as to their status and role can they chair the proceedings, question witnesses, participate in discussion of submissions with counsel, and/or participate in discussion with the first instance arbitrators? Are they entitled to be paid for such attendances if the arbitration clause expressly limits their role to the resolution of an impasse if and when one arises? These matters are at least open to serious doubt.

Fortunately this embarrassment is almost invariably resolved by agreement. The basis on which it should be resolved will be the subject of the next section. It is worth noting, however, that in those rare cases in which the parties are unable to agree on any earlier role for the umpire, it is doubtful whether the umpire can and should do anything at all before there is a disagreement between the first-tier arbitrators.

Choosing the best tribunal structure for the job.

Whatever the wording of the original arbitration clause, it will usually be in the interests of the parties to review the constitution of the arbitral tribunal after a dispute has arisen. Only then will they know the sum at stake, the kind of dispute, the nature and level of expertise required, and the form of tribunal that will best suit their needs.

Consenting parties are not bound to adhere to the terms of their original arbitration clause. In this situation they have broadly four choices.

The first is to have the umpire attend all hearings while retaining the status as umpire. The traditional reasons for doing so were to avoid the risk of a rehearing if the first-tier arbitrators disagreed and to give the umpire a flying start if called upon later.

The second possibility is to confine all hearings to the first-tier arbitrators, leaving the impasse-breaker in the wings unless and until any disagreement actually occurs. So long as the first-tier arbitrators are professional and independent, irreconcilable disagreements will be rare. A three-member panel is more expensive and organizationally demanding. Rehearings can usually be avoided by digitally recording the initial hearing. If the second-tier arbitrator does need to step in later, a transcript can be prepared from the digital recording. The second-tier arbitrator can then resolve the disagreement on the papers, with or without supplementary submissions from the parties.

The third is to elevate the umpire from a mere impasse-breaker to full membership of the arbitral panel. This avoids uncertainty over the extent to which umpires can and should engage with witnesses, counsel, and other arbitrators. If it is agreed that the second-tier arbitrator is to actively participate at hearings, it will usually be preferable to have three full members and appoint one as presiding arbitrator.

The fourth possibility is to substitute a sole arbitrator for the three-member panel. Arbitrations run by sole arbitrators are simpler, quicker and cheaper. If simplicity, speed and/or economy are the dominant concerns, and the parties have not interfered in the process by which the first-tier arbitrators had appointed the second-tier arbitrator, the neutrality of the process will often encourage the parties to agree on the second-tier arbitrator as the sole arbitrator.

Switching to a sole arbitrator will be particularly appropriate if the first-tier arbitrators have already disagreed by the time the second-tier arbitrator is appointed. This is common in valuation disputes. If the first-tier arbitrators are valuers who have already disagreed, it will usually be safer and more efficient for them to withdraw from the arbitral tribunal and continue as expert witnesses.

A practical detail is that where there is more than one active arbitrator, it will be more efficient and economical to appoint one of their number as presiding arbitrator with power to determine procedural matters unilaterally (Art 29). The presiding arbitrator can be relied upon to consult with the other arbitrator or arbitrators on anything significant but can act quickly and economically on minor matters.

Conclusions

The Arbitration Act 1996 did not abolish umpires. For the purposes of the Act they are subsumed within the broader expression arbitrator. Whether the agreement giving rise to their appointment came before or after the Act, umpires continue to be appointed by first-tier arbitrators and continue to be confined to an impasse-breaking role.

Whether contracting parties would be wise to adhere to the traditional arbitrator-umpire framework is another matter. The fact that they are faced with an arbitrator-umpire clause does not mean that they must adhere to it. So long as they can agree, the parties are free to adopt

whatever structure best suits their needs. The chief considerations guiding their choice have been outlined. It is the job of arbitrators to help the parties in their choice.

Whatever choice is made, it is clear that the existence of an umpire or third arbitrator can never leave a first-tier arbitrator free to retain a special connection with his or her appointing party. A prior connection with a party, at least in relation to the subject matter of the dispute, disqualifies a candidate from appointment. Once appointed, arbitrators must break off all private communication with individual parties and treat all parties in precisely the same way.

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[1] As in *Bowport Ltd v Yachts International Ltd* [2004] 1 NZLR 361 at 372.

[2] As in *Cornwall Park Trust Board (Inc) v Brown (*22/4/08 Rhys Harrison J, HC Auckland CIV-2007-404-7934)

[3] *Green and Hunt on Arbitration Law & Practice* ARSch1.10.03; and the view expressed atARSch1.29.02; and DA4.1.10 that the 1996 Act makes no provision for umpires but DA4.1.12 does recognise that an award made by an umpire is an award under the 1996 Act citing *TH Barnes & Co v Minster of Inland Revenue* [1998] 2 NZLR 463 (CA)

[4] AAP Willy *Arbitration in New Zealand* 2nd ed pp 52 and 78

[5] NZ Law Commission, *Improving the Arbitration Act 1996,* Report Paper No. 83 (February 2003) at paras 131 and 132.

[6] *Cornwall Park Trust Board Inc v Brown* 22/4/08 Rhys Harrison J, HC Auckland CIV-2007-404-7934.

[7] Art 10 of Sched 1 to the Arbitration Act 1996.

[8] S 19(3) and (3A); *Bowport Ltd v Yachts International Ltd* (supra)

[9] Art 11(3)(a).

[10] Art 11(3)(a) and (4)

[11] Art 29

[12] See in particular Arts 10, 11 and 29

[13] *Street v Mountford* [1985] AC 809 (HL); [1985] 2 All ER 289 at p 819 (... The manufacture of a five-pronged implement for manual digging results in a fork even if the manufacturer, unfamiliar with the English language, insists that he intended to make and has made a spade);*Fatac Ltd (In Liquidation) v Commissioner of Inland Revenue* [2002] 3 NZLR 648 (CA) at 661 (the only intention that matters is intention as to substantive rights, not intention as to legal classification)

[14] *Con Dev Construction Ltd v Financial Shelves No 49 Ltd* 22 December 1997, Master Venning, High Court Christchurch, CP 179/97; *Bowport Ltd v Yachts International Ltd* (supra);*Grey District Council v Banks* [2003] NZAR 487 (HC) at 493; contra *Grandilla Ltd v Berben*(1998) 12 PRNZ 371 (HC).

[15] Ibid n 2, para 30.

[16] *CBI NZ Ltd v Badger Chiyoda* [1989] 2 NZLR 669 (CA) at 675 party autonomy a strong trend; *McLaren v Waikato Regional Council* [1993] 1 NZLR 710, at 717 the tide has been flowing away from judicial intervention in arbitrations and towards respect for party autonomy.

[17] *General Distributors Ltd v Cassata Ltd* [2006] 2 NZLR 721 (SC) at para 116 (party autonomy a theme of the Arbitration Act 1996) *Methanex Motunui Ltd v Spellman* [2004] 1 NZLR 95, at para 46 need to respect the parties' free and deliberate choice of [an arbitral] process; *Gold and Resource Developments (NZ) Ltd v Doug Hood Ltd* [2000] 3 NZLR 318 (CA) at para 52 (presumption of party autonomy so strong as to curtail availability of judicial review); *Weatherhead v Deka New Zealand Ltd* [1999] 1 NZLR 492 (observation that Law Commission's preliminary paper ARBITRATION A discussion paper" (NZLC PP7) (1988) and concept of party autonomy required that arbitration (properly so called) [be] founded on the agreement of the parties

[18]In *Bowport Ltd v Yachts International Ltd (supra)* Elias CJ referred to the prevalence of such clauses.

[19] New Zealand Law Commission, *Improving the Arbitration Act 1996,* Report Paper No. 83 (February 2003) at para 140.

[20] *Russell on Arbitration* (22d ed) at para 4-008 cited in *Banks v Grey District Council*[2004] 2 NZLR 19 (CA) at para 27 but apparently written before the Arbitration Act 1996 (UK).
[21] *Methanex Motunui Ltd v Spellman* [2004] 1 NZLR 95 (HC) at para 46; [2004] 3 NZLR 454 (CA), at para 116; *Parts and Services Ltd v Brooks* [2006] BCL 114, at para 60; *Banks v Grey District Council* [2003] NZAR 487 (HC) CA40/03 19 December 2003 (CA)
[22] *S N Funnell Ltd v Payn* 18/4/85, Thorp J, HC Auckland A128/83; A266/83 (one party to an arbitrator-umpire clause not entitled to appoint as arbitrator an engineer who had held the position of supervisor to the contract works, it being impossible for the engineer to bring to his task that openness of mind required for arbitration) ; The requirement for arbitrators to be completely impartial and unbiased applies equally to two arbitrators, even when the arbitrators have been appointed by one of the parties to the dispute: *Hawkes Bay Electric Power Board v Napier Borough Council* [1930] NZLR 162, affirmed in *Tolmarsh Developments Ltd v Stobbs* 10/9/90, Tompkins J, HC Auckland M809/90.
[23] *Banks v Grey District Council* supra fn 21