

GERMANY



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Party agreement versus procedural order – where to draw the line?

1. Introduction

During the half-year conference of the German Institution of Arbitration (“DIS”¹) in October 2012, an order dated 17 February 2011 (“Order”) of the higher regional court of Frankfurt (“Court”)² was intensively discussed. By this Order, the Court set aside a final award in accordance with section 1059, para. 2, no 1(d) of the German code of civil procedure (“ZPO”)³, on the grounds that the arbitral procedure was not in accordance with the procedural agreement of the parties.⁴ The Order relates to the highly important distinction between procedural rules agreed upon between the parties (section 1042, para. 3 of the ZPO⁵) and such rules issued by an arbitral tribunal (section 1042, para. 4, sentence 1 of the ZPO⁶).⁷ While the former can only be changed with the consent of the parties to the arbitration, the latter, in principle, is subject to the discretion of the arbitral tribunal.

2. Facts

The dispute in question arose in connection with a sale and purchase agreement (“SPA”). Under the SPA one party (“Seller”) was obliged to sell and transfer all of its shares in the company X (“Target”) to the other party (“Buyer”). The Buyer was obliged to pay a purchase price, the amount of which depended, *inter alia*, on the net financial liabilities of the Target towards the Seller and its affiliated companies at the date of closing of the SPA.⁸ Prior to the closing of the SPA, the Buyer argued that the Seller had increased the net

¹ Deutsche Institution für Schiedsgerichtsbarkeit (DIS)

² Beschluss dated 17 February 2013 of the Oberlandesgericht Frankfurt/Main, Az.: 26 Sch 13/10 (published in *SchiedsVZ_German Arbitration Journal_January/February 2013*, 49-62)

³ Section 1059 – Application for Setting Aside

“(1) Recourse to a court against an arbitral award may be made only by an application for setting aside in accordance with sub-sections 2 and 3 of this section.

(2) An arbitral award may be set aside only if:

1. the applicant shows sufficient cause that:

a) [...]

d) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with a provision of this Book [the 10th Book of the ZPO codifies the German arbitration law] or with an admissible agreement of the parties and this presumably affected the award; [...].”

⁴ Beschluss OLG Frankfurt/Main, para. 51.

⁵ Section 1042, para. 3 of the ZPO: “Otherwise, subject to the mandatory provisions of this Book, the parties are free to determine the procedure themselves or by reference to a set of arbitration rules.”

⁶ Section 1042 para. 4 of the ZPO: “Failing an agreement by the parties, and in the absence of provisions in this Book, the arbitral tribunal shall conduct the arbitration in such manner as it considers appropriate.”

⁷ The arbitral tribunal’s power to issue procedural orders stems from section 1042 para.4 of the ZPO (compare Joachim Münch_ MünchenerKommentar_Zivilprozessordnung, Sections 1025 – 1109, 4th ed., Munich, 2013, section 1042, paras. 91-92).

⁸ Beschluss OLG Frankfurt/Main, paras. 2 and 3.

financial liabilities of the Target in breach of the “Ordinary Course of Business” clause.⁹ The Buyer refused to fulfil its payment obligation under the SPA. According to the arbitration clause contained in the SPA disputes arising out of or in connection with the SPA are to be settled in accordance with the arbitration rules of the DIS (“DIS Arbitration Rules”).¹⁰ The Seller initiated arbitration proceedings requesting the arbitral tribunal to order the Buyer to pay damages for the non-fulfilment of the payment obligation contained in the SPA.¹¹

3. Procedural History

The arbitral tribunal bifurcated the arbitration proceedings in a liability and a quantum phase and by partial award, dated 15 September 2006, declared that the Buyer was liable for the breach of the SPA. A procedural conference call was scheduled for 11 October 2006 to discuss the conduct of the arbitration proceedings during the quantum phase. During this procedural conference call, the chairman advised the parties that the taking of evidence would strictly follow the DIS Arbitration Rules and the ZPO, unless the parties agreed otherwise. In the event the parties wanted to enter into any such agreements, the arbitral tribunal would document those.¹² Following the procedural conference call, the arbitral tribunal circulated a draft procedural order no 10 (“Draft PO”) and asked for the parties’ approval or suggestions to be made for changes to the Draft PO.¹³ In accordance with the parties’ submitted requests for changes, the arbitral tribunal amended the relevant section III of the Draft PO, circulated the amended Draft PO to the parties and requested their approval of the amended wording. Upon receiving the parties’ approval, the arbitral tribunal issued procedural order no 10 on 8 November 2006 (“PO 10”).¹⁴

The introduction of section III of PO 10 reads: “Furthermore, the arbitral tribunal documents the parties’ agreement as to the content of the written submissions”.¹⁵ According to section III of PO 10 the parties, *inter alia*, have to submit any expert reports together with their submissions in support of disputed facts. Further, section III of PO 10 provides that any documents which a party-appointed expert has reviewed and taken into consideration have to be attached to the expert report.¹⁶ The Seller failed to completely submit the documents which its party-appointed expert had reviewed. The Buyer requested the arbitral tribunal to order the Seller to disclose any documents which were necessary to analyse the amount of damages claimed by the Seller and which must have been available to the Seller’s party-appointed expert. The Arbitral Tribunal advised the parties that according to section III of PO 10 the Seller was only obliged to disclose already existing documents, but not “new” documents¹⁷. The arbitral tribunal dismissed the Buyer’s request and based its decision on its discretion with respect to document disclosure.¹⁸ In its final award (“Award”), the arbitral tribunal ordered the Buyer to pay an amount of approximately EUR 210 million in damages to the Seller.¹⁹

4. Setting aside proceedings

The Court set aside the Award upon application of the Buyer.²⁰ The Court held that section III of PO 10 constituted an admissible procedural agreement for the purposes of Section 1059, para. 2 no 1(d) of

⁹ Ibid, para. 5.

¹⁰ Ibid, para. 4.

¹¹ Ibid, para. 6.

¹² Ibid, para. 11.

¹³ Ibid, para. 12.

¹⁴ Beschluss OLG Frankfurt/Main, paras. 12 et seq.

¹⁵ Ibid, para. 17: “Das Schiedsgericht hält des Weiteren die Vereinbarung der Parteien zum Inhalt der weiteren Schriftsätze fest.”

¹⁶ Ibid, paras. 14-15

¹⁷ Ibid, para. 18.

¹⁸ Ibid, para. 18.

¹⁹ Ibid, para. 22.

²⁰ Ibid, paras. 49 and 51.

the ZPO.²¹ This procedural agreement was binding upon the arbitral tribunal. The arbitral tribunal failed to comply with the parties' agreement by dismissing the Buyer's request to have all documents disclosed.²² Unlike procedural rules issued by an arbitral tribunal in accordance with section 1042, para. 4, sentence 1 of the ZPO²³, the arbitral tribunal does not have any discretion to change the parties' procedural agreements. Further, such agreements supersede procedural rules issued by an arbitral tribunal according to section 1042, para. 4 of the ZPO.²⁴

The Court also held that a procedural agreement does not lose its legal character as an agreement merely because it is contained in a procedural order. The negotiation history of section III of PO 10 - in particular the content of the conference call dated 11 October 2006 and the subsequent correspondence with respect to the Draft PO - and the wording of the introductory sentence of section III of PO 10 confirms that this section can only be understood as an agreement between the parties on procedural rules.²⁵

²¹ In deviation from article 34 (2)(c) UNCITRAL Model Law, section 1059, para. 2, no 1(d) of the ZPO furthermore requires that the procedural defect presumably affected the award (compare Stefan Kröll, Karl Heinz Böckstiegel and Patricia Nacimiento *Arbitration in Germany, The Model Law in Practice*, The Netherlands, 2007, section 1059, para. 69); In addition to the breach of an admissible agreement, the Court in the Order also held that the requirement of this necessary causality of the breach was fulfilled (section 1059, para. 2, no 1(d) of the ZPO: "[...] this presumably affected the award"). The Court held that if the arbitral procedure had been conducted in accordance with the agreement of the parties, it cannot be excluded that a different Award would have been issued.

²² Beschluss OLG Frankfurt/Main, paras. 51 and 64.

²³ Joachim Münch *MünchenerKommentar*, section 1042, para. 92.

²⁴ Beschluss OLG Frankfurt/Main, paras. 53 and 54; also compare Joachim Münch *MünchenerKommentar*, section 1042, para. 76.

²⁵ Beschluss OLG Frankfurt/Main, paras. 57-59.