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Rio Algom Ltd. v. Sammi Steel Co.

Between
Rio Algom Limited, Plaintiff, and
Sammi Steel Co. Ltd. and Sammi Steel Canada Inc., Defendants

Ontario Judgments: [1991] O.J. No. 268
Action No. 43610/89

Ontario Court of Justice - General Division
Toronto, Ontario
Henry J.
Heard: February 14 and 15, 1991
Judgment: March 1, 1991

[Ed. Note: Corrigenda, released March 7, 1991, appended and correction made to judgment.]

John T. Morin, Q.C. and David C. Rosenbaum, for the Plaintiff.
Robert Rueter, for the Defendants.

HENRY J.:-- Although counsel fully and ably argued the motion for leave to appeal the order of Kane J. over a period of one and a half days, I intend to dispose of the matter more briefly.

The issue of fundamental importance is whether, once the parties to an international commercial agreement have agreed to adopt the dispute resolution mechanism provided by the International Commercial Arbitration Act, 1988, S.O. 1988, c. 30, issues defining the scope of the arbitration agreement, which raise matters of contract interpretation, ought to be resolved by the courts before arbitration proceeds or by the arbitrator in the first instance before resort to the courts.

The parties agreed that Sammi would purchase Rio's steel manufacturing business in Welland, Ontario, Tracy, Quebec and in New York State. The Canadian purchase was accomplished by the purchase and sale of shares - in Canada by a "Share Purchase Agreement" and in New York by a "Stock Purchase Agreement". Both agreements were dated May 11, 1989. In the Canadian agreement (their terms being substantially similar) the initial price to be paid by Sammi, calculated on the basis of unaudited financial statements as at December 31, 1988, was to be adjusted after closing of the transaction in accordance with a Closing Date Balance Sheet reflecting the difference in the net asset value of the businesses between December 31, 1988 and the final audit as of the date of closing. The seller and purchaser were to prepare a Closing Date Balance Sheet as soon as possible after closing and submit it for audit to Deloitte, Haskins. The Closing Date Balance Sheet was to be prepared in conformity with generally accepted accounting principles (GAAP) and on a basis consistent with the balance sheet forming part of the 1988 financial statements; it was to be prepared subject to certain exceptions (which are the subject of the order of Kane J. referring those matters for decision to the court as issues of contract construction).

Subsection 2.5(e) of the agreement provides that if either party wishes to dispute "any matter in the final draft of the Closing Date Balance Sheet, it may do so by notice in writing given to the other party ...". It is further provided that if the dispute is not resolved within a designated time frame, any unresolved matters will be referred to a Third Party Auditor for final and binding resolution. This is a reference to arbitration.

Sammi's balance sheet as audited by Deloitte, Haskins was referred to both Rio and Sammi. Neither was prepared to accept it. Sammi submitted a Notice of Dispute and referred the matter for resolution to the Third Party Auditor (Price, Waterhouse) pursuant to s. 2.5(e) of the Share Purchase Agreement.

Rio in turn commenced this action (without giving notice of dispute) to challenge before the court the jurisdiction of the Third Party Auditor to arbitrate the issues, and for an order staying the arbitration proceedings. Rio also prepared a balance sheet which it considered was in conformity with the Share Purchase Agreement; while at the same time it expressed disagreement with the Sammi/Deloitte balance sheet.

Before Kane J., Sammi took the position that the dispute mechanism provided by s. 2.5 of the Share Purchase Agreement was governed by the International Commercial Arbitration Act, 1988 (the I.C.A.A.) which adopted as the law of Ontario the United Nations UNCITRAL Model Law on International Commercial Arbitration (the Model Law). The effect of the Model Law is to require the court to stay the action and refer the parties to arbitration in accordance with their agreement.

Rio's position before Kane J. was that the dispute over which balance sheet is the Closing Date Balance Sheet required by the Share Purchase Agreement is a dispute involving a question of contract interpretation going to the arbitrator's jurisdiction which can only be determined by the court. Rio also argued that disputes about four specific accounting entries in the Closing Date Balance Sheet raised further issues of contract interpretation which also could only be determined by the court. In accordance with the case law governing s. 7 of the domestic Arbitration Act, R.S.O. 1980, c. 25, Rio sought to have the arbitration proceeding stayed and the issues resolved by the court or alternatively to have the trial of an issue directed to determine those items in dispute involving contract construction. Kane J. accepted Rio's submissions and directed the trial of issues of contract construction in paras. 1(a) to (d) of his order of November 22, 1990, and otherwise stayed the action. He further ordered that the parties should proceed to arbitration in accordance with s. 2.5(e) of the Share Purchase Agreement but not until final determination of the issues to be tried by the court as directed. In so holding Kane J. applied the I.C.A.A. rather than the Arbitration Act, but withdrew from the arbitrator (the Third Party Auditor) the issues that he directed to be tried by the court.

On the motion for leave to appeal before me there is no dispute that the I.C.A.A. applies, as does the Model Law that it adopts. It is common ground that the Share Purchase Agreement contains in s. 2.5 an arbitration agreement within the meaning of the Model Law.

On behalf of Sammi it is submitted that the arbitration clause is clear when it says:

> If either Seller or Purchaser wishes to dispute any matter in the final draft of the Closing Date Balance Sheet, it may do so by notice in writing given to the other party....

This permits submission to the arbitrator under the Model Law of any matter disputed in the final balance sheet. This is particularly so in light of Article 16 of the Model Law which expressly provides as follows:

> (1) The arbitral tribunal may rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement. For that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail ipso jure the invalidity of the arbitration clause.
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> (2) A plea that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence. A party is not precluded from raising such a plea by the fact that he has appointed, or participated in the appointment of, an arbitrator. A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings. The arbitral tribunal may, in either case, admit a later plea if it considers the delay justified.
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> (3) The arbitral tribunal may rule on a plea referred to in paragraph (2) of this article either as a preliminary question or in an award on the merits. If the arbitral tribunal rules as a preliminary question that it has jurisdiction, any party may request, within thirty days after having received notice of that ruling, the court specified in article 6 to decide the matter, which decision shall be subject to no appeal; while such a request is pending, the arbitral tribunal may continue the arbitral proceedings and make an award.

The contrary position argued on behalf of Rio is that first, the Closing Date Balance Sheet is not the statement required by the Share Purchase Agreement because it does not meet the conditions specified in the agreement so that there is at present no such statement to go to the arbitrator; and second, that by the Share Purchase Agreement the parties have expressly withdrawn the disputed items from inclusion in the balance sheet and price adjustment and so those issues are not arbitrable, and must be left to the court to determine.

As I have said, Kane J., while finding that the dispute of any matters in the final draft of the Closing Date Balance Sheet shall be determined by a third party auditor pursuant to the ICAA and the Model Law, held that, "the interpretation of s. 2.5(a) of the Share Purchase Agreement is a threshold issue to be determined by the court prior to resort to the arbitration process". He therefore segregated for trial by the court before arbitration the issues of which balance sheet is the true Closing Date Balance Sheet, and whether on a true construction of the Share Purchase Agreement there can be adjustments to the purchase price with respect to the sales tax expense, stores write-down and reserve, and environmental liabilities. The principle upon which he so decided is that only the court can determine what the parties have agreed to submit to arbitration and other issues of law; that, as I understand it, is the principle underlying the domestic Arbitration Act. See M. Loeb Ltd. v. Harzena Holdings Ltd. (1980), 18 (P.C. 245 (Ont. H.C.). In the case of international agreements however, the Model Law as I see it, leaves that determination to the arbitrator in the first instance, who is authorized to determine its own jurisdiction and the scope of its authority (Article 16, supra). Not only that, but it may also rule on any objections with respect to the validity or existence of the arbitration agreement or clause.

By Article 8 of the Model Law it is provided:

> (1) A court before which an action is brought in a matter which is the subject of an arbitration agreement shall, ... refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.

That appears to me to be arguably the only role for the court prior to arbitration; if the arbitration is already in progress that question may be decided by the arbitrator under Article 16.

It is important to note that where the arbitrator decides a question of jurisdiction or scope of authority raised in the arbitration proceedings, the jurisdiction of the courts is not ousted; once the arbitrator has made a preliminary ruling or a final decision on the merits a party may move the court to set it aside (Article 16(3) and Article 34).

Apart from this, Article 5 of the Model Law provides that:

> In matters governed by this Law, no court shall intervene except where so provided in this Law.

What appears to me of significance is that the Model Law reflects an emphasis in favour of arbitration in the first instance in international commercial arbitrations to which it applies (of which it is common ground this is one). The courts in matters of contract interpretation as such are limited in that they do not appear to have a role in determining matters of law or construction; jurisdiction and scope of authority are for the arbitrator to determine in the first instance, subject to later recourse to set aside the ruling or award. The role of the court before arbitration appears to be confined to determining whether the arbitration clause is null and void, inoperative or incapable of being performed (Article 8) - if not it is mandatory to send the parties to arbitration. Kane J. did not follow this course - he referred questions of the construction of the agreement to trial without apparent reference to the condition specified in Article 8; these issues to be tried relate to matters

of law, including jurisdiction and scope of the arbitrator's authority, but not, so far as I can see, to the issues for the court to determine under Article 8. It seems to me to be at least arguable that the matters referred to trial are not matters that permit the intervention of the court in the light of Article 5, supra.

Grounds for granting leave to appeal are governed by rule 62.02(5):

> (5) Leave to appeal shall not be granted unless,
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> (a) there is a conflicting decision by another judge or court in Ontario or elsewhere on the matter involved in the proposed appeal and it is, in the opinion of the judge hearing the motion, desirable that leave to appeal be granted; or
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> (b) there appears to the judge hearing the motion good reason to doubt the correctness of the order in question and the proposed appeal involves matters of such importance that, in his or her opinion, leave to appeal should be granted.

It is my opinion that the circumstances fall readily into para. (b). There appears to me to be good reason to doubt the correctness of the order of Kane J. as I have already indicated. There can be no doubt that the proposed appeal involves matters of considerable importance to the development of consistency in the application of the Model Law throughout the nations that have adopted it. As I understand it, the purpose and spirit of the I.C.A.A. in adopting the Model Law, was to make Ontario commercial arbitration law consistent with the law of other international trading countries so as to enhance and encourage international commerce in Ontario and the resolution of disputes by rules of international commercial arbitration; for this it is important that appellate courts address the issues emerging in this case.

HENRY J.

Corrigenda

Released: March 7, 1991

Page 1, correction of counsel's name from "David C. Rosenberg" to " David C. Rosenbaum".