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This article examines the Osaka High Court decision in 2016 that set aside an arbitral award because of an arbitrator's failure to disclose a potential conflict of interest and introduces recent initiatives to promote arbitration in Japan.

Recent court decision involving arbitration – advance waiver and consequence of failure to disclose a potential conflict of interest

In the 2017 edition of the *Asia-Pacific Arbitration Review*, we introduced an Osaka District Court case[1] in which a failed party challenged an arbitral award on the basis of the presiding arbitrator's failure to disclose a potential conflict of interest in a Japan Commercial Arbitration Association (JCAA) arbitration seated in Osaka. The Osaka District Court dismissed the challenge. The Osaka High Court,[2] however, reversed the district court decision and upheld the challenge. The case is now pending before the Supreme Court. This court decision, together with its lower court decision, is of particular importance as, for the first time, the court dealt with the issue of the consequences of advance waiver and a breach of the duty to disclose on an arbitral award in Japan.

Facts

The arbitration case involved a dispute between a Japanese party and its affiliate in Singapore (the claimants) and certain US parties (the respondents) over the validity of termination of a sale-and-purchase agreement between one of the respondents and the claimants, and one of the claimants' alleged breach of a development agreement with the other respondent. An arbitral award was rendered on 11 August 2014, upholding virtually all of the claimants' claims and defences. The respondents challenged the award on 13 November 2014 in the Osaka District Court. One of the grounds of the challenge was that the presiding arbitrator failed to disclose a potential conflict of interest and, accordingly, the composition of the tribunal and arbitration proceedings violated Japanese law[3] and procedural public policy.[4] The potential conflict of interest that the presiding arbitrator from Singapore failed to disclose was that his colleague, who joined the arbitrator's firm in his San Francisco office 20 months after the commencement of the arbitration, had been representing the claimants' ultimate Japanese parent company and its affiliate in the US in the Cathode Ray Tube antitrust class action in California (the Class Action) while the arbitration was pending (the Potential Conflict).

Before he was appointed, the presiding arbitrator submitted an advance waiver to the JCAA and the parties disclosing potential future conflicts to the effect that:

- he was not aware of any present or past circumstances that were likely to give rise to justifiable doubts as to his impartiality and independence;
- lawyers of his firm could advise or represent in the future a client in a matter unrelated to the arbitration but having a conflict of interest with any of the parties to the arbitration or their affiliates;
- lawyers of his firm could advise or represent in the future any of the parties to the arbitration or their affiliates in a matter unrelated to the arbitration; and
- he would not be involved in any of these matters or receive any information on any of these matters during the arbitration proceedings and he considered that such matters would not affect his independence and impartiality as an arbitrator in this arbitration.

Neither the parties nor the JCAA appeared to have commented on or questioned such qualification. The presiding arbitrator was then jointly appointed by the co-arbitrators, one of whom was appointed by the JCAA as the respondents chose not to appoint a co-arbitrator because they contested the jurisdiction of the tribunal.

Ruling

The High Court examined the issues of (i) whether the Potential Conflict was subject to the arbitrator's disclosure obligation, (ii) whether the arbitrator was released from his disclosure obligation because the arbitrator was not allegedly informed of the Class Action, (iii) whether the arbitrator was deemed to have disclosed the Potential Conflict by way of the advance waiver, and (iv) whether a breach of a disclosure obligation amounts to grounds to set aside an arbitral award.

First, the High Court found the Potential Conflict was subject to the arbitrator's disclosure obligation reasoning that the scope of the disclosure obligation was broader than that of the challenges against the arbitrators, and from the respondents' perspective, the circumstances under which the arbitrator's colleague was representing the claimants' affiliates was likely to give rise to justifiable doubts as to his independence and impartiality, which could be also a basis on which to challenge the arbitrators.

Second, the High Court found that an arbitrator has an ongoing obligation to investigate potential conflicts that are relatively easy to identify and an arbitrator is not released from his ongoing disclosure obligation simply because he was not aware of a potential conflict. In this case, the arbitrator's law firm should have identified potential conflicts by carrying out a process of conflict checks, and the arbitrator violated his disclosure obligation irrespective of whether or not the firm conducted a conflict check.

Third, the High Court found that the disclosure of potential future conflicts in the advance waiver did not constitute the fulfilment of his disclosure obligation because the information to be disclosed should be facts that have occurred or would occur, and the disclosure should be specific and concrete enough to enable a party to decide whether to challenge an arbitrator, as opposed to abstract information on potential conflicts in an abstract sense that might occur in the future.

Fourth, the High Court dismissed the claimants' allegation that a breach of a disclosure obligation, if any, was not serious enough to sustain a challenge against the arbitration award and that, even if a breach of disclosure obligation amounts to grounds to set aside an arbitral award, the court should use the discretion afforded by the Arbitration Act not to set aside the award because (i) the breach was cured as a result of the respondents' failure to challenge the presiding arbitrator during the arbitration as well as their comments that the proceedings were fair; and (ii) there was no causation between a breach of a disclosure obligation and the outcome of the case. The High Court strongly denounced the arbitrator's breach of his disclosure obligation by holding that an arbitrator's disclosure obligation is pivotal to ensuring the integrity of arbitration proceedings and arbitrators; and, given that the Potential Conflict could justify a challenge of the arbitrator, a breach of such obligation is, in itself, serious enough to result in the composition of the tribunal and arbitration proceedings violating Japanese law. The respondents' failure to challenge the arbitrator and their comment on the fairness of the proceedings did not cure the breach as they were not informed of the Potential Conflict. The High Court concluded that the arbitral award could not be sustained while also ensuring the integrity of arbitration proceedings and arbitral awards, and securing public trust in the arbitration system.

Analysis

Differences between the District Court decision and High Court decision

While both the District Court and the High Court found a breach of the duty to disclose and that such a breach could amount to grounds to set aside the award, the two courts differed on the level of seriousness of the breach of law and implication for the advance waiver that led to an opposite conclusion. First, the District Court did not find that the circumstances justified challenges to the arbitrator because the Potential Conflict involved lawyers in different offices, unrelated matters and different parties. The presiding arbitrator was also not informed of the Potential Conflict, and, therefore, a breach of the duty to disclose could not have affected the outcome of the case. In contrast, the High Court did find that the circumstances could, in fact, amount to justify challenges to the arbitrator and whether the circumstances could have affected the outcome was irrelevant in the context of the challenge.

Second, the District Court found that the respondents could have anticipated the arbitrator's colleague representing the parties' affiliates based on the advance waiver disclosing potential future conflicts, and the fact that the respondents did not object to the advance waiver suggests that the respondents did not care much about such potential conflict. In contrast, the High Court held that the advance waiver did not release the arbitrator from his ongoing obligation to investigate and disclose circumstances that were likely to give rise to justifiable doubts as to his independence and impartiality, and, in order to give effect to the disclosure of future conflicts, specific and concrete facts that enable the parties to decide whether to challenge the arbitrator should be disclosed. The High Court was particularly critical about the arbitrator and his firm as the firm could have easily identified the Potential Conflict but elected either not to conduct a conflict check or not to disclose the identified Potential Conflict.

Differences between the Osaka High Court decision and the English High Court decision in W Limited v M SND BHD[5]

The English High Court rendered a decision on 2 March 2016 dismissing a challenge of awards based on an arbitrator's failure to disclose a potential conflict. This case became widely known partly because it challenged the 2014 International Bar Association (IBA) Conflict of Interest Guidelines, namely on the lack of a case-specific approach in relation to its 'non-waivable red list'. In *W Limited v M SND BHD*, an arbitrator was a partner in a law firm that earned substantial remuneration from providing legal services to a client that happened to become a sister company of a party to the arbitration after the arbitrator submitted a statement of independence to the parties. Although the M&A transaction that created the conflict of interest was widely publicised, the conflict-check system of the arbitrator's law firm failed to detect the conflict of interest and the arbitrator consequently failed to disclose such conflict to the parties. The arbitrator regretted what happened and stated that he would have made the appropriate disclosure had he known about the conflict. The English High Court found that a fair-minded and informed observer would not conclude that there was a real possibility that the tribunal was biased or lacked independence or impartiality, and dismissed the challenge. Both the Osaka High Court and English High Court dealt with cases where an arbitrator failed to disclose a potential or actual conflict of interest, yet the two courts came to different conclusions. The question of why is particularly interesting because the English High Court dealt with an actual and serious conflict, and the Osaka High Court dealt with only a potential conflict. Two elements can be considered to have contributed to such starkly different outcomes between the two cases: first, the test applied by each court; and second, the circumstances that led to the relevant arbitrator's failure to disclose.

First, the English High Court applied a test of whether the arbitrator had apparent bias as a result of the conflict of interest, while the Osaka High Court applied a test of whether there was a serious breach of law in the arbitration proceedings. Consequently, the Osaka High Court's approach was less flexible because the question focused narrowly on how serious the breach of law by the arbitrator was.

Second, in the Osaka High Court case, the court appears to have presumed that the arbitrator and his firm elected either not to investigate potential conflicts or not to disclose the Potential Conflict because of the advance waiver. Conversely, in the English High Court case the firm engaged in an ongoing investigation. Unfortunately, however, such investigation did not detect any conflicts, which meant that the arbitrator was not aware of the actual conflict. While in both cases the arbitrator was not aware of the particular conflict there was a fundamental difference between the two in terms of their commitment to transparency. Clearly the arbitrator in the English High Court case was eager to disclose any potential conflicts, whereas the arbitrator and firm in the Osaka High Court were not. It is likely that these factors, together with other differences, resulted in a different conclusion between the two courts, which again reinforces the importance of an arbitrator's and his or her firm's diligent performance of the duty to disclose.

Setting aside procedure in Japan

Japanese courts have a long tradition of advocating a pro-arbitration approach and, with very limited exceptions such as the Osaka High Court decision, consistently dismiss challenges against arbitral awards. Procedures for setting aside arbitral awards were simplified to expedite the challenge proceedings when the Arbitration Act, consistent with the 1985 UNCITRAL Model Law, was introduced in 2004. In the Osaka High Court decision,

the respondents challenged the award on 13 November 2015, and the Osaka District Court rendered its decision on 17 March 2016, within only four months from the date of the challenge. In fact, one of the parties' counsel to this case wrote that the judges appeared to have already formed their impression based on the submissions even before the one (and only) hearing was held on 20 February 2016 and when granting the respondents' leave for supplemental submission the court commented that they believed such supplemental submission was unnecessary but would consider it if they submit it before 13 March 2016.[6] This demonstrates the Japanese court's strong presumption that arbitration awards are to be sustained, which gives comfort to parties who choose Japan as the seat of arbitration.

Institutional practice – advance waiver

As practitioners may realise, arbitral institutions take different approaches towards advance waivers or qualified statements of independence.[7] For instance, the International Chamber of Commerce (ICC) has adopted a policy to the effect that the ICC Court will not be bound by the arbitrator's statement relating to future conflicts of interest, and the ICC secretariat will inform, in writing, both the arbitrator concerned and the parties of such ICC policy.[8] The latest ICC Note to Parties and Arbitral Tribunals on the Conduct of the Arbitration[9] provides that, although an advance declaration or waiver in relation to possible conflicts of interest arising from facts and circumstances that may arise in the future may or may not in certain circumstances be taken into account by the ICC Court, an arbitrator is not discharged from his or her ongoing duty to disclose. On the other hand, the Singapore International Arbitration Centre (SIAC) takes a different approach depending on whether an arbitrator is appointed by SIAC or nominated by a party. While SIAC will unlikely appoint an arbitrator who requires an advance waiver, SIAC will usually accept a nomination of an arbitrator who requires an advance waiver so long as all the parties agree to the advance waiver.

In the Osaka High Court case, the JCAA did not appear to have reminded the arbitrator of his ongoing disclosure obligations under the Arbitration Act (article 18(3)) or the JCAA Rules (Rule 28(4)) in response to the advance waiver. Given the Osaka High Court decision, the JCAA, going forward, will most likely remind the arbitrators concerned and the parties of the applicable ongoing disclosure obligations, and will not appoint an arbitrator who requires an advance waiver when acting as an appointing authority.

Takeaway from the Osaka High Court decision

The independence and impartiality of arbitrators is a paramount principle to ensure the integrity of and trust in arbitration. In fact, scepticism towards arbitrators' independence and impartiality partly contributed to the establishment of a permanent investment court under the Comprehensive and Economic Trade Agreement between the EU and Canada, which restricts party autonomy in its investor-state dispute settlement mechanism in contrast to conventional arbitration.

On the other hand, because the IBA Guidelines and jurisprudence in many jurisdictions require a high standard of integrity of arbitrators' independence and impartiality, arbitration practitioners at large law firms may feel hesitant to accept an appointment as his or her appointment would restrict his or her colleagues' ability to take instructions from any of the parties to the arbitration and their affiliates during the pendency of arbitration, particularly when any of the parties is a large conglomerate. While the courts, arbitral institutions and institutions such as the IBA try to strike a balance between party autonomy and conflicts of interest, the decisions tend to be fact specific and general guidelines are difficult to craft. In this connection, the Osaka High Court set a clear rule to the effect that an arbitrator is not to be released from his or her ongoing duty to investigate and disclose potential conflicts by way of advance waiver. Those who practice arbitration in Japan, irrespective of institutional rules and practices, should be aware of this rule set forth by the Osaka High Court.

Initiatives to promote international arbitration and mediation in Japan

Two initiatives have been recently launched to promote international arbitration and mediation in Japan. The Japan Federation of Bar Associations and the Japan Association of Arbitrators put together proposals to promote international arbitration and mediation in Japan, and in so doing have involved major Japanese economic organisations, such as Keidanren.[10] Those behind this initiative are now trying to influence both the legislative branch and the executive branch so that cross-sectional policies and plans that are necessary to achieve the goals of this initiative will be adopted with collaboration among different institutions.

While those behind this initiative are in the process of compiling detailed action plans, some examples of the specific agenda items addressed in the initiatives are as follows:

- establishment of a state-of-the-art hearing facility dedicated to international arbitration and mediation in Japan;
- amendment of the Arbitration Act to reflect developments in international arbitration practices;
- implementing steps to facilitate a pro-arbitration judiciary and aid the arbitration process;
- enhancement of local arbitration institutions; and
- educating current and prospective arbitration practitioners.

The competition among potential seats and arbitration institutions is intensifying, particularly in the Asia-Pacific region, and institutions such as SIAC, the Hong Kong International Arbitration Centre, the Korean Commercial Arbitration Board and the Kuala Lumpur Regional Centre for Arbitration are regularly announcing new rules and practices, and recording high arbitration caseloads each year. Conversely, the JCAA has been suffering a consistently low caseload of around 20 cases per year and Japan's position as a seat of arbitration has relatively deteriorated. The arbitration caseload involving Japanese parties and Japanese arbitrators of the JCAA and other arbitration institutions is disproportionately low compared to the size of the Japanese economy. The above-mentioned initiative has identified issues related to, for example, disadvantages to Japanese parties and disincentives to foreign investment in Japan, and the objectives of neighbouring countries investing in the promotion of international arbitration in their own countries, and the economic, political and diplomatic benefits to promoting arbitration within their own countries. It seems the messages contained in the initiative have reached certain MPs and ministries, and it is hoped that the initiative will eventually develop into a joint collaboration among the different ministries and institutions with the aim of achieving a unified goal of promoting international arbitration in Japan.

Notes

1 Osaka District Court, 17 March 2015, 2014 (arb) No. 3, 2270 Hanrei Jiho 74.

2 Osaka High Court, 28 June 2016, 2015 (ra) No. 547, 1431 Hanrei Times 108.

3 Article 44(1)(6)of the Arbitration Act. Unofficial English translation is available at www.japaneselawtranslation.go.jp/law/detail/?id=2784&vm=04&re=01&new=1.
4 Article 44(1)(8)of the Arbitration Act.
5 *W Ltd v M Sdn Bhd* [2016] EWHC 422 (Comm) (2 March 2016).
6 Yukihiro Terasawa, 'Challenge of Arbitral Award', Jurist, March 2017, No. 1503, p. 69.
7 'Advance Waivers of Arbitrator Conflicts of Interest in International Commercial Arbitrations Seated in New York', A report of the International Commercial Disputes Committee of the New York City Bar Association (2016); www.nycbar.org/member-and-career-services/committees/reports-listing/reports/detail/advance-waivers-of-arbitrator-conflicts-of-interest-in-international-commercial-arbitrations-seated-in-new-york.
8 Jason Fry, et al, *The Secretariat's Guide To ICC Arbitration*, ICC (2012).
9 Paragraph 22 of 'Note to Parties and Arbitral Tribunals on the Conduct of the Arbitration under the ICC Rules of Arbitration'. https://cdn.iccwbo.org/content/uploads/sites/3/2017/03/ICC-Note-to-Parties-and-Arbitral-Tribunals-on-the-Conduct.
10 www.keidanren.or.jp/en/.

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Ms Ohara is currently serving as a vice president of the ICC and a board member of the Swiss Arbitration Association and Japan Association of Arbitrators. Before then she served as a court member of LCIA (2010-2015) and a vice president of LCIA (2013-2015). She is a frequent speaker and author on the subject of international arbitration. She teaches at the LLM programme of Keio University Law School. She has contributed to shaping soft law in international arbitration as a member of the IBA Task Force on Professional Conduct of Counsel in International Arbitration and the IBA Conflicts of Interest Subcommittee (2013-2014).

She received her LLB from the University of Tokyo and her LLM from Harvard Law School. She is admitted to practise law in Japan and New York.

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