

English Commercial Court confirms fraud does not always “unravel all”

Introduction

In *Sinocore International Co Ltd v RBRG Trading (UK) Ltd*¹, the English Commercial Court granted permission for the enforcement of a foreign arbitral award despite allegations that the transaction in question had been “tainted” by fraud. The fraudulent action of one of the parties did not prevent it from pursuing a claim for a separate breach of a lawful contract which had caused its loss.

Background

The case involved a contract between Sinocore International Co Ltd (the “**Seller**”) and RBRG Trading (UK) Ltd (the “**Buyer**”), pursuant to which the Seller agreed to sell and ship steel coils from China to the Buyer in Mexico. It was a condition of the contract that the Buyer needed to obtain a letter of credit from its bank to guarantee payment of the contract price provided the steel coils were shipped “by 31 July 2010”. The Buyer duly obtained such letter of credit, but later wrongfully instructed its bank to change the shipment period to “20-30 July 2010”. The Seller did not consent to this amendment.

The Seller shipped the steel coils on 5-6 July 2010, and the ship issued bills of lading (documents acknowledging receipt of cargo) showing those dates. The Seller sent these to the Buyer. However, on 22 July 2010, the Seller’s bank presented to the Buyer’s bank bills of lading dated 20-21 July 2010, which had been forged to comply with the shipment period on the letter of credit in order to secure payment.

The dispute

The Buyer obtained an injunction from a Dutch court preventing its bank from paying the Seller under the letter of credit. The Seller terminated the contract as it could not recover payment, and had to sell the cargo to another buyer for a greatly reduced price. The Seller claimed that the Buyer was in breach of contract for failing to provide a letter of credit that complied with the contract, and wished to recover the losses it had suffered.

The Seller secured an arbitration award from a CIETAC² tribunal for the difference between the original contract price and the reduced resale price, plus its costs. The Seller sought permission to enforce the award in the English Commercial Court under the New York Convention and the Arbitration Act 1996, pursuant to which Chinese arbitration awards are recognisable and enforceable in the United Kingdom.

The English Commercial Court’s application of the “fraud unravels all” principle

The question before the English Commercial Court was whether enforcement of the award should be permitted, or whether the transaction had been “tainted” by fraud, rendering enforcement contrary to public policy.

In this case, the arbitral tribunal had concluded, as a matter of Chinese law, that:

- Whilst the Seller had attempted to deceive the Buyer’s bank, there had been no deception of the Buyer as the Seller had disclosed the real shipment dates;

¹ [2017] EWHC 251 (Comm)

² China International Economic and Trade Arbitration Commission

- The operative breach of contract was the Buyer’s earlier instruction to its bank to amend the dates on the letter of credit; and
- This had caused the Seller not to receive payment, which was the real reason the contract was terminated and losses followed, not the Seller’s presentation of fraudulent documents to the Buyer’s bank.

In Phillips J’s judgment dated 17 February 2017, he acknowledged that although an English court may not have reached the same conclusion, the arbitral tribunal in this case had found that the contract and its intended performance were entirely lawful. The Judge confirmed that the English courts will not refuse to enforce a lawful claim under a lawful transaction just because fraud is alleged to have “tainted” the transaction. The judgment clarifies that the English courts will, however, consider refusing to enforce arbitral awards that give effect to:

- Contracts which are unlawful in the place of performance;
- Contracts which are contrary to English public policy (e.g. a contract to pay a bribe), even if not illegal under the relevant foreign law; or
- Corrupt practices (e.g. to enforce payment or recovery of a bribe).

Hypothetically (as such a scenario did not arise in this case), had the Seller been seeking to enforce an award for the Buyer’s bank to pay out under the letter of credit against the forged documents, the English court would almost certainly have refused on the basis that banks do not have to fulfil a contractual obligation to pay under a letter of credit when fraudulent documents are presented. This is due to the legal principle that “fraud unravels all” (*ex turpi causa non oritur actio*: out of a disgraceful cause an action cannot arise).

Conclusions

The current position under English case law is that a claimant who presents fraudulent documents is not necessarily prevented from bringing other lawful claims in relation to a lawful transaction generally, just because the opposing party alleges that the transaction is “tainted” by fraud. The Judge in this case stated that to permit such an argument to succeed would introduce uncertainty and undermine party autonomy.

In any event, the Judge determined that it was not appropriate or permissible for the English court to decide whether the arbitral tribunal was wrong as a matter of Chinese law, and that the public interest in the finality of valid arbitration awards “clearly and distinctly outweighs” any allegation that the otherwise lawful transaction had been “tainted”. Concluding that it would not be contrary to English public policy to do so, the Judge granted permission for the award to be enforced. This decision illustrates that fraud does not necessarily “unravel all”, and maintains the position of the English courts that there is a strong presumption in favour of enforcing New York Convention arbitral awards, which will only be set aside on the grounds of public policy in very limited and exceptional circumstances.

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