IN THE COURT OF APPEAL

AT NAIROBI

(Coram: Law, Miller & Potter JJA)

CIVIL APPEALS NOS. 14 & 15 OF 1980

BETWEEN

RIFT VALLEY TEXTILES LTD.....APPELLANT

AND

COTTON DISTRIBUTORS INCORPORATED.....RESPONDENT

JUDGMENT

Law JA These two appeals have been consolidated. The facts out of which they arise are as follows. The appellant in both appeals is a limited liability company which carries on the business of spinning cotton and manufacturing cotton material at Eldoret. The respondent is a Corporation carrying on the business of cotton brokers and dealers in cotton in Switzerland.

In early 1977, negotiations took place between the appellant and the respondent for the sale by the respondent to the appellant of certain quantities of Sudan Acala Raw Cotton. The cotton was to be shipped from Port Sudan at an agreed CIF Mombasa price.

Four printed contract forms were sent by the respondent to the appellant for signature by the appellant in Kenya.

These contracts were:

a) No 10377018 dated March 4, 1977 and signed by the appellant on March 31, 1977. (Contract 18).

b) No 10377037 dated March 23, 1977 and signed by the appellant on April 12, 1977. (Contract 37)

c) No 10377047 dated May 9, 1977. (Contract 47)

d) No 10377048 dated May 11, 1977. (Contract 48)

Before the first shipment of cotton arrived at Mombasa, the appellant received information that the cotton might be infested with honeydew. Cotton infested with honeydew would not be suitable for use in the appellant's factory as it might cause damage to the appellant's machinery.

The appellant says that it therefore asked the respondent to confirm that the cotton to be supplied under these four contracts would not be infested with honeydew, and the respondent confirmed by telex on May 26, 1977 and over the telephone at about the same time that the cotton to be supplied by the respondent

would not be infested with honeydew.

The representations that the cotton would be honeydew free were allegedly made after the dates on the contracts 18 and 37.

The cotton for contracts 18 and 37 came in 3 shipments. When the first shipment arrived, the appellant proceeded to process the cotton. The appellant claims that the cotton was then found to be infested with honeydew and that it caused considerable damage to the appellants' machinery.

The appellant then refused to sign contracts 47 and 48 and informed the respondent that it would not accept delivery of any cotton thereunder.

The respondent commenced arbitration proceedings in Liverpool in respect of contracts 47 and 48, under clauses in those contracts providing for the settlement of disputes by arbitration under the Liverpool Cotton Association Rules. Awards were made in favour of the respondent. The appellant appealed to the Technical Appeal Committee. The awards were upheld with minor amendments on March 19, 1979.

On July 12, 1979, the appellant filed suit against the respondent in the High Court Civil Case No 2273 of 1979 claiming damages in respect of the allegedly contaminated cotton in contracts 18 and 37. I will refer to this suit as "the first suit."

The appellant claimed Kshs 12,375,296 as loss and damage suffered by the appellant as a result of the respondent's negligent misrepresentation that the cotton would not be infested with honeydew.

The respondent entered an appearance and applied under Section 6 of the Arbitration Act (Cap 49) for a stay. An order of stay was made by Wilkinson-Guillemard, J on November 29, 1979. It is against this Order that Civil Appeal No 14 of 1980 has been lodged (hereinafter referred to as CA 14/80).

On December 5, 1979, the respondent filed suit against the appellant in High Court Civil Case No 3936 of 1979 to enforce the arbitration awards in respect of contracts 47 and 48. I will refer to this suit as "the second suit." The appellant filed a defence. Paragraphs 2 and 3 of the defence relate solely to the arbitration awards and are not relevant to these consolidated appeals. The rest of the defence consists of what is described as a set-off. The set-off arises out of contracts 18 and 37 and is in substantially the same form as the plaint in CA 14/80 in that the set-off is based solely on the tort of negligent misrepresentation and makes no reliance on any breach of contract.

The respondent applied for the set-off to be stayed. An order to stay was made by Scriven J on April 25, 1980. It is against this order that Civil Appeal No 15 of 1980 has been lodged (hereinafter referred to as CA 15/ 80).

In the first suit, the learned judge in his ruling set out in detail the submissions made by the advocates for both parties but made no findings on these submissions. He merely held that it was not for him to decide whether or not the claim for damages came within the scope of the arbitration clause, but that this was a matter which should be dealt with by the arbitrators. Inferentially, he must have decided that there was a valid arbitration clause contained in the contracts, as he ordered the proceedings to be stayed. In the second suit, Scriven J made a clear finding that the contracts were the subject of an Agreement to arbitrate, and made findings on all the other issues.

The first ground of appeal, argued by Mr Fraser, is common to both appeals and is that there was no valid arbitration Agreement –

a) as the clause in the contracts was not within Rule 200(2) of the Liverpool Cotton Association rules, and

b) as the contracts did not have affixed to them the official stamp of the Liverpool Cotton Association as required By-Law 126 of the Association.

As regards (b), Scriven J, noted that By-Law 126 only requires stamp duty to be paid on cotton imported into the United Kingdom. Mr Fraser submits that although no stamp duty is payable, a contract to be valid must be presented to the Association for its stamp to be affixed. Paragraph (1) of By-Law 126 provides that no contract will be recognized as subject to the Rules of the Association "unless the official stamp of the Association for the Stamp Duty due has been duly affixed." As I read that provision, it is only when stamp duty is due that the official stamp has to be affixed. As regards (a), the contracts contain, against the sub-head "Rules, Arbitration and other Conditions", the words "Liverpool Cotton Association - such rules contain amongst other things provision as to the closure of contracts and provide for the settlement of disputes by Arbitration."

Overleaf appear the words:

> "1. This contract shall not be cancelled on any ground and is subject to the Rules of the Cotton Association mentioned overleaf and any dispute shall be settled according to these rules."

Sub-rule 2 of Rule 200 provides that

> "Whenever any difference touches or arises out of any transaction or contract that is subject to the By-Laws and Rules of the Association, or subject to Liverpool Arbitration, or contain words to similar effect, such difference shall be referred to Arbitration in accordance with the By-laws and Rules".

Mr Fraser submitted that as the contracts make no reference to the By- Laws, or to "Liverpool Arbitration", there is no valid arbitration clause. The learned judge in the first suit made no finding on it; Scriven J, in the second suit held that the omission of a reference to By-Laws was unimportant as definition No 102 in the By-Laws is to the effect that "Rules means and includes By-Laws." But if the By-Laws do not apply, the definition does not avail. There is no corresponding definition in the Rules. The answer to this highly technical point is, I think, that the contracts refer to "Liverpool Cotton Association" and to "settlement of disputes by arbitration" which in my view are "words to a similar effect" to "Liverpool Arbitration" so as to make sub-rule (2) of Rule 200 applicable, with the result that there is a valid arbitration clause. In my view, ground 1 fails, ground 2, which is that Switzerland was not shown to have been a party to the protocol set out in the First Schedule to the Act, is now not relied on by Mr Fraser in view of this court having allowed the fact of Switzerland being a party to be proved at the hearing of these consolidated appeals by additional evidence in the form of a "Certificat de Costume". In any event I agree with Mr Deverell, for the respondent, that this fact, in the absence of evidence to the contrary, was sufficiently proved, as held by Scriven J, on the authority of Halsbury's Laws of England (4th Ed Paragraph 556 in Vol. 2) where both Switzerland and Kenya are listed among the contracting states which have adopted the protocol.

The third ground of appeal is common to both appeals, and is that Section 6(2) of the Act did not apply as there had been no reference to arbitration. The importance of this ground is that if Section 6(2) does apply, it is mandatory for the court to stay the proceedings. If Section 6(2) does not apply, then Section 6(1) applies, and the court has a discretion whether or not to order a stay. Mr Fraser's submission in this regard is that Section 6(1) applies where a party to "an arbitration Agreement" commences legal proceedings, whereas Section 6(2) only applies where a party to "a reference to arbitration" made pursuant to an Agreement to which the protocol applies commences legal proceedings. Mr Fraser went on to submit that comparison of the phrases "arbitration Agreement" as defined in Section 2 of the Act and the phrase "reference to arbitration" makes it clear that the two phrases are not synonymous. The definition of an "arbitration Agreement" makes clear that a reference is a stage further along the line. It is the actual presentation of an existing dispute to arbitration.

To accede to this argument would mean equating the words "a reference to arbitration" in Section 6(2) with an actual submission. The term "arbitration Agreement" is defined in Section 2 of the Act as being a written agreement to refer present or future differences to arbitration.

Mr Deverell's submission on this point is that the words "party to a reference to arbitration" in Section

6(2) do not refer to an existing dispute only, but also cover a future dispute, and he relies on the judgment of Scarman J, (as he then was) in *The Merak* [1965] 1 All ER 230 at p 233. Scriven J, dealt most fully with this point in the second suit. He concluded, with some hesitation, that where in a contract there is an agreement that disputes shall be arbitrated, that is in itself a submission, or a reference, to arbitration without any further step being required. I am of the same view. In my opinion "a reference to arbitration" in Section 6 (2) means both an actual reference of an existing dispute and an Agreement to refer future disputes. That interpretation accords with clause 1 of the Protocol to which Section 6(2) relates and is intended to implement. I therefore do not find it necessary to deal with ground 5, which would only arise if it were held that Section 6(2) did not apply, in which case the court would have a discretion whether or not to order a stay.

Ground 4 is common to both appeals, and relates to the claim for damages contained in the plaint in the first suit to the related set-off pleaded as a defence in the second suit.

The plaint in the first suit claims damages of over Kshs 12,000,000 suffered "as a result of the defendant's breach of contract and/or alternatively as a result of the defendant's negligent misrepresentation that the cotton would not be infested with honeydew". Although laid in contract as well in tort, Mr Fraser is prepared to drop the claim in contract and to rely solely on the claim in tort, and to amend the plaint accordingly, as the alleged misrepresentation was made some time after the first two contracts were signed. The learned judge in the first suit held that it was for the arbitrators to decide whether or not the claim was to recover sums awarded to the respondent in arbitration proceedings arising out of contracts 47 and 48, the appellant as defendant substantially repeated the contents of the plaint in the first suit, but confined the cause of action to negligent misrepresentation. By paragraphs 21 and 22 of the defence:

> "21. The defendant therefore claims from the plaintiff Kshs 12,375,296 as loss and damage suffered by the defendant as a result of the plaintiff's negligent misrepresentation that the cotton would not be infested with honeydew.
> 22. The defendant sets-off the sum of Kshs 12,375,296 against any sum found due to the plaintiff."

Scriven J, in the second suit, when dealing with the question whether the court had power to order stay of a set-off, correctly in my view said that it depended on the true nature of the set-off. What is described as a set-off in this case is in the nature of a counter-claim because, to be effective, the "claim" pleaded in paragraph 22 of the defence will have to be adjudicated. If the appellant is unable to establish a negligent misrepresentation, or to prove damage resulting from it, the so-called set-off will fall away. I find myself in full agreement with Scriven J, that in these circumstances, the set-off, by reason of Order VIII rule 2 of the Civil Procedure Rules, has the same effect as a cross-suit, and the pleading of it is therefore a commencement of proceedings within the meaning of Section 6 of the Arbitration Act. This disposes of ground 6 in CA 15/80.

To revert to ground 4, Wilkinson-Guillemard J in the first suit made no specific finding that the claim for damages for negligent misrepresentation touched or arose out of the contracts, so as to come within the arbitration clause, beyond saying that it was a matter for the arbitrators to decide, but he must inferentially have made such a finding or he would not have stayed the suit. Scriven J held that even though laid in tort, the facts pleaded in the set-off show a difference touching or arising out of the contract and accordingly falling within the arbitration clause. Mr Fraser referred us to a number of cases in which causes of action not directly arising out of a contract were held not to fall within the arbitration clause contained in the contract.

In *Turnock v Sartoris* (1890) 43 Ch D 150, a lease provided "that if any dispute, question, difference, or controversy shall arise … touching these presents or any clause, matter, or thing herein contained, or the construction hereof, or any matter in any way connected with these presents, or the operation hereof, or the rights, duties or liabilities of either party in connection with the premises" then the dispute should be referred to arbitration. In the lease, provision was made for the supply of water. Disputes arose relating to the supply of water and an agreement was entered into settling those disputes. The plaintiff commenced

proceedings for damages for breach of the agreement. On an application to stay the proceedings Cotton LJ, after setting out the arbitration clause, said:

> "that to my mind simply refers to questions arising under the lease alone and does not extend to all questions arising as to property included in the lease, and I therefore hold that the clause of reference to arbitration does not include all the matters that may arise under the subsequent Agreement."

In *Printing Machinery Company Ltd v Linotype and Machinery Ltd* [1912] 1 Ch 566, Warrington J held that an action for rectification on an agreement did not come within the arbitration clause covering "any dispute, difference or question which may at any time arise … touching the construction, meaning or effect of these presents … or the rights or liabilities of the parties … under these presents or otherwise however in relation to these presents."

In *Union of India v EB Aaby's Rederi A/S* [1975] AC 797, there was a charter party containing an arbitration clause. A general average claim arose during the course of the charter. To avoid a lien being exercised over the cargo, the chatterer gave an undertaking to the owner to pay any general average contribution, which might be due. It was held that the undertaking was a fresh agreement and was not covered by the arbitration clause.

These cases, as I understand them, all relate to disputes arising from fresh agreements entered into subsequent to an original agreement, but connected with the original agreement. Such disputes were held not to be subject to the arbitration clause in the original agreement. I do not, with respect, consider those cases relevant to the questions for decision in these consolidated appeals. The claims for damages for the results of alleged negligent misrepresentation do not arise from a fresh agreement subsequent to the original contract containing the arbitration clause. Mr Fraser submits that these claims arise from "a separate and independent relationship". Scriven J, held that, although the alleged misrepresentation was made subsequently to the contract, the remedy claimed by the plaint in the first suit and the set-off in the second suit arose out of the contracts, by reason of the contractual relationship of the parties. It was, in his view, the type of dispute that the parties to the arbitration clause intended to refer to the Association. I see no reason to differ, having regard to the very wide scope of the arbitration by the Association any difference touching or arising out of any transaction or contract that is subject to the Rules of the Association. Surely the question as to whether cotton was infested with honeydew, and if so whether it was misrepresented as being free from honeydew, is a question which touches or arises from the contracts under which the cotton was supplied, and is a question within the scope of the arbitration clause. That, at any rate, is my opinion.

To summarize, although we have not had the benefit of the learned judge's findings on the issues before him, I agree with his conclusion in the first suit, and would hold, for the reasons I have attempted to set out, that appeal CA 14/80 fails because:

a. the contacts were subject to an Agreement to refer disputes to arbitration by the Liverpool Cotton Association;
b. the contracts were valid without the need for the Association's stamp;
c. the appellant's suit touched and arose out of the contracts;
d. that Switzerland and Kenya are parties to the Protocol;
e. that Section 6(2) of the Act applies.

For the same reasons, I am also of the opinion that the appeal CA 15/80 fails and in that appeal I hold that the so-called set-off was properly regarded by Scriven J, as being in the nature of and having the same effect as a cross-suit or counter-claim, thus being a "commencement of proceedings" within Section 6 of the Act.

I would accordingly dismiss both these appeals, with costs, except that I would not allow the respondent any costs it may have incurred by its application to adduce additional evidence. As Miller and Potter JJ A agree, it is so ordered.

Miller JA. I have had the privilege of reading the judgment of Law JA in draft and I agree with it and with the orders proposed.

Potter JA. I have had the advantage of reading the judgment of Law JA in draft; I agree with it and with the orders proposed, and I have nothing useful to add.

Dated and delivered at Nairobi this 1st day of December, 1980.

E.J.E LAW

…….....

JUDGE OF APPEAL

C.H.E MILLER

…….....

JUDGE OF APPEAL

K.D POTTER

…….....

JUDGE OF APPEAL

I certify that this is a true copy of the original

DEPUTY REGISTRAR