

## Supreme Court Ruling in the First Case of Enforcement of Foreign Arbitral Award

This Client Briefing summarizes a Supreme Court decision dated 2075/9/11 (December 26, 2017), rendered by the Division Bench consisting of Honorable Justices Harikrishna Karki and Tanka Bahadur Moktan in Case No. 067-WO-0419 on a Writ Petition seeking an Order of Mandamus and Certiorari filed by Hanil Engineering & Construction Co., Ltd. through its authorized representative, Advocate Devendra Pradhan against KONECO Pvt. Ltd. *et. al.* The full text of the judgment was recently released by the Supreme Court.

### Background

Hanil Engineering & Construction Co., Ltd. (“**Hanil**”), a South Korean company, entered into an agreement with Melamchi Water Supply Development Board (“**Melamchi Board**”) to construct access roads for the Melamchi Water Supply Project. Hanil subcontracted the construction work to KONECO Pvt. Ltd. (“**Koneco**”), a Nepali company, under the condition that the entire construction be completed by the deadline. Despite repeated warnings, Koneco failed to fulfill its obligations. As a result, Hanil was in breach of its main agreement with Melamchi Board, which forfeited Hanil’s bank guarantee, and Hanil suffered financial loss totaling USD 1,758,578 plus interest.

The agreement between Hanil and Koneco included an arbitration clause and Korean law as the choice of law for settlement of disputes. The arbitration clause also stipulated that any dispute between the parties shall be settled amicably and in good faith before resorting to arbitration. The parties didn’t adopt institutional arbitration in the agreement. Nonetheless, Hanil applied to the Korean Commercial Arbitration Board (“**Arbitration Board**”) to adjudicate its dispute with Koneco. In July 2009, the Arbitration Board awarded Hanil damages against Koneco in the amount of USD 1,758,578 plus interest. To enforce the award in Nepal, Hanil submitted an application before the then-Appellate Court Patan requesting that the Arbitration Board’s decision be enforced as required under Nepal’s Arbitration Act 2055 (1999) (“**Arbitration Act**”). The Appellate Court Patan declined to enforce the award. Hanil then filed a Writ Petition at the Supreme Court of Nepal seeking to quash the decision of the Appellate Court Patan and to enforce the Arbitration Board’s award under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (“**New York Convention**”) and the Arbitration Act.

### Decision

The Supreme Court ruled that in the instant case the Arbitration Board’s foreign arbitral award was unenforceable in Nepal. In its decision, the Supreme Court laid down the following principles regarding enforcement of a foreign arbitral award in Nepal:

1. **Governing Law:** Under the “Doctrine of Separability,” the arbitration clause is separable from the contract. Unless the parties specifically agree otherwise, the governing law of the contract will not necessarily apply to the appointment of arbitrator(s) and arbitration proceedings. In

other words, the governing law of the contract cannot be automatically deemed to be the governing law of the arbitration clause as well.

2. **Dispute Resolution:** The Supreme Court interpreted that the arbitration clause required Hanil and Koneco to settle their dispute amicably and in good faith before resorting to arbitration. In the instant case, the Supreme Court ruled that the parties initiated the arbitration prematurely without first attempting to resolve their disputes amicably, resulting in non-compliance of the agreement between the parties. The Supreme Court found that Koneco was thus deprived of its right to amicably resolve the dispute as stipulated by the agreement.
3. **Appointing Authority:** If the parties failed to authorize an organization or individual to appoint the arbitrator(s), the procedural law selected by the parties for the arbitration proceedings will apply for appointment of arbitrator(s).
4. **Appointment of Arbitrator(s):** The Supreme Court cited Article V.1.d of the New York Convention and § 34(2)(a) of the Arbitration Act, which require that arbitrator(s) must be appointed as agreed to by the parties. The parties must agree, either in the main agreement or in a separate agreement, on the appointment of arbitrator(s). In other words, the appointment of the arbitrator(s) must be done and the arbitrator(s)' decision must be made under the laws and procedures specified by the agreement. Only if the parties fail to appoint arbitrator(s) by mutual agreement and request a court to appoint arbitrator(s), the court may do so under applicable national laws. This principle is also adopted by Article 12(2) of the Korean Arbitration Act 1999 (“KA Act”) and under § 7 of the Arbitration Act, both of which, according to the Supreme Court, were not followed in the instant case.

The Supreme Court found that the parties in the instant case had not agreed on the appointment of arbitrator(s) or the appointment procedure. Nonetheless, the Arbitration Board appointed arbitrator(s) based on Hanil's *ex parte* request. As the arbitrators were not appointed under either the laws of Korea or Nepal, the arbitral award did not satisfy § 34(2)(a) of the Arbitration Act requiring that the arbitrator(s) be appointed as per the laws and procedures specified by the parties. The Supreme Court concluded that the appointment of the arbitrator(s) and arbitration proceedings were not done as per the agreement between the parties as well as the laws selected by the parties and that the arbitrators were not appointed based on the principle of fair and impartial hearing.

5. **Service of Notice:** The Supreme Court ruled that under § 34(2)(c) of the Arbitration Act, which requires that for a foreign arbitral award to be recognized and enforced in Nepal, the parties must be timely notified of the arbitration proceedings so that they may be able to present evidence in their defense. Emphasizing the need for timely notice, separate notice must be issued during each step of arbitration proceedings in accordance with the law in order for the foreign arbitral award to be recognized and enforceable in Nepal. A decision that is issued when a party does not have a fair notice and opportunity to be heard is against the principles of natural justice.

In the instant case, a notice for appointment of arbitrator(s) was served to Mr. Hyunil Chung, Managing Director of Koneco in Korea after the notice could not be delivered at Koneco's address in Nepal. The Supreme Court stated that Koneco had not authorized Mr. Chung to participate in the arbitration proceedings on behalf of Koneco. Thus, Mr. Chung's receipt of the notice failed to meet the requirement for notice to Koneco. Further, the Supreme Court noted, the notice served on Mr. Chung was solely for the purpose of appointment of arbitrator(s), and no other notice was issued to Koneco to participate in the arbitration

proceedings. A notice must be served timely and properly to ensure the parties' right to a fair hearing. The Supreme Court concluded that Koneco did not get a fair opportunity to be heard.

## Analysis

Nepal is party to the New York Convention, the major international instrument for enforcement of foreign arbitral awards. An arbitral award rendered in a foreign jurisdiction is enforceable in Nepal provided that it meets the requirements specified in § 34 of the Arbitration Act, which is based on the New York Convention. After twenty years of enforcement of the Arbitration Act, the Supreme Court has rendered its judgment on enforceability of a foreign arbitral award for the first time in this case. The judgment affirms that a foreign arbitral award, which is intended to be recognized and enforced in Nepal, must ensure that the arbitration proceedings fulfill the requirements specified in § 34 of the Arbitration Act and the New York Convention.

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