Angels Dancing on the Head of a Pin

The Alberta Court's Take on an Arbitration with a Strong Dissent

***SMART Technologies ULC v Electroboard Solutions Pty Ltd*, 2017 ABQB 559 (CanLII)**

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SMART Technologies ("**SMART**") develops interactive whiteboards and group collaboration tools for classrooms and meeting rooms. In the mid-1990's, Electroboard Solutions Pty Ltd. and Electroboard Solutions (NZ) Ltd. ("**Electroboard**") started distributing SMART products in Australia and New Zealand. Until 2014, Electroboard was SMART's only distributor in those countries and had entered into several distribution agreements (collectively, the "**Distribution Agreement**").

Electroboard failed to pay a number of SMART invoices totalling approximately $3.6M. On July 3, 2014, SMART issued its claim for payment of the invoices. On July 31, 2014 SMART terminated the Distribution Agreement. Electroboard defended and issued a counterclaim which raised problems with SMART's products' functionality, breach of contract, and passing off. Later, Electroboard amended its counterclaim to add an allegation that SMART breached a duty to negotiate in good faith and relied on *Bhasin v Hrynew*, 2014 SCC 71 (CanLII). Electroboard sought to set-off SMART's claim by returning $3.6 million in SMART products and claimed approximately $18M for other damages. SMART's position on the counterclaim was that Distribution Agreement precluded SMART's liability and contained a "no set-off" clause.

The Distribution Agreement required that:

- any disputes be resolved through arbitration;
- the arbitration would be administered by the American Arbitration Association, in accordance with the International Centre for Dispute Resolution's International Arbitration Rules (the "**ICDR Rules**");
- secondary to the ICDR Rules, the arbitration and agreements would be governed by the laws of the Province of Alberta and the federal laws of Canada;
- an arbitral award could be appealed to a panel of three arbitrators and, pursuant to clause 10.1.6 of the Distribution Agreement, the appeal tribunal could replace or modify the initial arbitral award only if it found clear errors of law or clear and convincing factual errors:

> 10.1.6 All arbitration awards shall be final and binding, and enforcement of the award shall not be subject to appeal except as expressly provided in this agreement. If the award exceeds $750,000 US. a party may notify the AAA of an intention to appeal to a second arbitral tribunal of three arbitrators, constituted in the same manner as the initial tribunal. The appeal tribunal shall not modify or replace the initial award except for clear errors of law or clear and convincing factual errors. The award of the appeal tribunal shall be final and binding, and enforcement of the tribunal's award shall not be subject to appeal or further review.

- the applicable law is the International Commercial Arbitration Act, RSA 2000, c I-5, and in particular Schedule 2 to the Act, the UNCITRAL Model Law on International Commercial Arbitration (the "**Model Law**").

The parties submitted their dispute to a single arbitrator: Daniel J. McDonald, QC, FCIArb. On the application of SMART, the arbitrator issued a summary judgment award in favour of SMART on the outstanding invoices and a later award in favour of SMART on the remaining issues, including dismissing Electroboard's amended counterclaim focusing on the breach of the duty and good faith and honesty in contractual performance.

The initial arbitral award was appealed to an appeal arbitral tribunal (the "**Appeal Tribunal**"):

- John Lorn McDougall, QC, of Arbitration Place in Toronto (Chair) (majority);
- Ret. Judge Billie Colombaro, a former appellate court judge of the United States' Third Circuit Court of Appeal (majority); and
- Ret. Judge Carl Anderson, a former presiding justice of the California Court of Appeal (dissent).

The majority of the Appeal Tribunal reversed the initial arbitral award, dismissed SMART's claim and ordered SMART to take back all of Electroboard's remaining stock of SMART products for credit and reimburse Electroboard for shipping and related expenses. Solicitor-client costs followed.

One of the arbitrators on the Appeal Tribunal issued a strong and stinging defence which is described in paragraphs 63 to 65:

> [63] A strong dissent was issued by one of the members of the Appeal Tribunal. The dissenting arbitrator raised the issue of the role of an appellate arbitrator. He stated that the proper role is to review the interpretation and application of the law of the initial arbitrator for "clear error" and to review the initial arbitrator's findings of fact for "clear and convincing factual errors". He noted that instead of doing this, the Majority took a "holistic" approach to appellate review and believed their role was "to do justice between the parties above all else" and reach a "just result relatively *unhindered* by the findings below."
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> [64] The Dissent took issue with the Majority's decision 1) to reverse the Summary Judgment Award on an issue that was first raised on appeal, and 2) to reverse the Partial Final Award by failing to give due deference to the findings of fact made by the Arbitrator.
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> [65] The Dissent was especially concerned with the Majority's approach to the facts because the Arbitrator heard live evidence from witnesses whereas the Appeal Tribunal only had a written record to review. He noted that the credibility of witnesses is best judged by those who see and observe how a witness gives evidence and responds to questions, noting it is a tenet of appellate judicial review to give deference to the trier of fact. He condemned the Majority's reweighing of the impact of the evidence and found the Majority "totally disregard[ed] every finding of fact the Arbitrator found below to be true."

SMART applied to the Alberta Court of Queen's Bench to set aside the Appeal Tribunal's award and restore the initial award. Electroboard applied for enforcement of the Appeal Tribunal's award. On the application the Court acknowledged that it was bound by Article 34 of the Model Law.

The Model Law contains only 6 grounds on which an arbitral award can be overturned. As the Court noted, it is clear that only true jurisdictional errors permit judicial intervention. Pursuant to Article 34(2)(a)(iii), SMART argued that the majority of the Appeal Tribunal exceeded its jurisdiction by deciding the case on the basis of *ex aequo et bono* (what is equitable and good):

> Article 34. Application for setting aside as exclusive recourse against arbitral award ...
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> (2) An arbitral award may be set aside by the court specified in article 6 only if:
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> (a) the party making the application furnishes proof that: ...
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> (iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration ...

The Court summarized the arguments of SMART and Electroboard at paragraphs 20 to 23:

> [20] In support of its argument, SMART provided a detailed review of the procedural steps and awards made from the early stages in front of the Arbitrator to the Final Award issued by the Appeal Tribunal. SMART points to a number of instances which it argues demonstrate the Majority's disregard for the law and pursuit of justice on its own terms.
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> [21] Those instances include:
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> 1) The Chair of the Appeal Panel (a member of the Majority) commenting at the appeal that submissions on the standard of review were "angels dancing on the head of a pin."
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> 2) The Majority exceeding the scope of the submission to arbitration by considering the Arbitrator's decision to grant the Summary Award. The Majority challenged the evidentiary record and the legal test relied upon (*Hryniak v Mauldin*…), despite the fact the parties had agreed on both of those matters. The Majority also raised the issue of the Arbitrator's jurisdiction on its own volition as it was not in Electroboard's Notices of Appeal.
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> 3) The Majority deciding to set aside the entirety of the Summary Awards instead of modifying the awards to allow set-off as requested by ELB.
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> 4) The Majority failing to show any deference to the Arbitrator's findings of fact.
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> 5) The Majority deciding impermissible questions of mixed fact and law, whereas appeals are only allowed on clear errors of law and clear and convincing errors of fact.

6) The Majority based its costs decision on an improper ground of appeal, as the Majority found Electroboard should be awarded full indemnity because it was deprived of its right to be heard at the initial stage of the arbitration. SMART submits that the Arbitrator did not have the opportunity to grant or deny Electroboard the right to be heard on any issue that was relevant to the Appeal, so this was an improper basis for awarding indemnity costs.

[22] In the alternative, SMART argues the Majority ignored the Appellant Rules on costs that applied to the Appeal. It submits this was an error of jurisdiction on its own.

[23] Electroboard disagrees with SMART's characterization of the Majority's decision. It argues that the Majority decided the Appeal within the terms and scope of the submission to arbitration by concluding that the Arbitrator made clear errors of law and fact. Electroboard submits that SMART is attempting to re-litigate the merits underlying the Appeal, which is specifically prohibited under Article 34.

The Court noted some of the difficulties with the decision of the Appeal Tribunal, expressed its sympathy for SMART, but ruled against it for the reasons set out in paragraphs 85 and 89 to 91 and 94 to 96:

[85] I have some sympathy for SMART's position, as it appears the Majority of the Appeal Tribunal did not follow the typical approach in appellate review, at least in courts, of focusing their discussion on a review of the findings of fact and the application of the law to those facts in the court below. In particular, the Majority gave little deference to some of the Arbitrator's findings of fact, stating that deference was not owed on the Summary Judgment Award because the Arbitrator decided the matter on the Record and did not observe witnesses or decide credibility on the basis of in-person observations. However, the Majority did not acknowledge that deference should apply to some findings of fact and the credibility assessments considering that the Arbitrator heard a 5-day oral hearing for the Partial Final Award. Instead, the Majority declared no deference arose for the Partial Final Award because there were clear and convincing factual errors. This is not convincing on its own.

. . .

[89] There are some gaps and problems in the approach of the Majority to its review, and its comments about "angels dancing on the head of a pin" are unfortunate, however the focus of this Court's inquiry is on whether the Majority decided a matter within its jurisdiction.

[90] Therefore, despite some hesitation regarding the Majority's approach to appellate review, I reject SMART's allegation that the Majority decided the matter *ex aequo et bono* and completely ignored the applicable standard of review.

[91] In particular, I note that even if the Appeal Tribunal's standard of review was improperly applied, a failure to apply the appropriate standard of review is an error of law, not an error of jurisdiction … A jurisdictional error would only have occurred if the Majority's

> decision ignored the standards of review completely and was based solely on what the Majority saw as “equitable and good” (*ex aequo et bono*) …
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> . . .
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> [94] The comments of the Dissent, which evidence obvious frustration with the “holistic” approach to appellate review of the Majority, does not go so far as to suggest that the Majority did not apply the law in coming to its decision. In fact the Dissent notes that the Arbitrator and the Majority interpret *Bhasin’s* new contractual obligations differently. The Arbitrator’s interpretation was reasonable and did not rise to the level of a ‘clear error of law’ for the Dissenting Arbitrator. The Majority came to the opposite conclusion. However, there was not a failure to apply the law.
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> [95] At most, SMART and the Dissent’s view on the Majority’s problematic appellate approach could support a finding that the standard of review was applied improperly. However as noted previously, that would be an error of law, not jurisdiction.
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> [96] I find that the Majority of the Appeal Tribunal applied the law and did not decide the appeal *ex aequo et bono*.

This case is a cautionary tale for those who think that errors of law are not just "angels dancing on the head of a pin".