

Newsletter

DUBAI DESK

Case Study

Limits to the Principle of Privity of Contract: Extension of Arbitration Agreement to separate contracts and to non-signatories



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Overview

The principle of Privity of Contract remains intact as a settled and fundamental rule of law. The theory of privity provides that only parties to a contract can enforce or be subject to its benefits or obligations under that contract. A third party, non-signatory, has no such rights or obligations, notwithstanding the fact that the contract was made for the benefit of that party. This has long been considered a settled, fundamental aspect of contract law. It further stipulates that only the parties directly involved in a contract are entitled to enforce the terms and provisions of the contract; For instance, one cannot enforce the benefit of or be liable for any obligation under a contract to which she or he is not a signatory. The underlying premise is that only contract parties may sue or be sued under it. The aforementioned theory has long been deemed as a “Jurisprudence Constante” pursuant which the Supreme Court in Dubai has issued rulings with regards to the arbitration subject.

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Legal Background

It is a central rule of law: Courts are supposed to abide by previous decisions- case precedents- to resolve current disputes. However, it is inevitable sometimes, that precedent has to go, and a court has to overrule another court, or even its own decision from another case. The Supreme Court in Dubai confirmed a long-held the principle of Privity of Contract in Arbitration agreements. The Supreme Court has long ruled in favor of the non-extension of the arbitration clause integrated in one of two contracts to the other contracts, given that each of the two contracts is a separate form of the other and independent of all agreements made between the parties. In a judgement rendered in 2010, the Supreme Court has decided upon a dispute involving two agreements, the first one is a contracting contract with an arbitration clause and the second one related to scaffolding rental. In its judgment, the Court has reasoned that “in the event there are two contracts concluded between the disputed parties, and if each of the contracts constitutes a separate and independent form from the other contract; therefore, the existence of the arbitration clause in one of them does not extend to the other contract that is independent of it and in which the arbitration clause is not included”.

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Through issuance of this judgment, the Supreme Court of Dubai has upheld the precedents of the Courts in the United Arab Emirates in relation to the rule of Privity of Contracts refraining individuals who are non-signatories of an arbitration agreement from complying with its provisions. In other words, aforementioned judgment has adopted the principle of non-extension of arbitration clause to other contracts as long as the two contracts are independent from one another.

Decisions of The Dubai Court of Cassation

Extension of Arbitration Clause to separate contracts

In 2011, the Dubai Court of Cassation has retracted its judgments and overturned the decisions regarding the possibility of extending the arbitration clause contained in a composite contract to other contracts affiliated with it, attached to it, complementary to it, or implementation for its execution, as the Dubai Court of Cassation ruled pursuant to the following: “It is acknowledged that a compound contract is a contract that achieves the purposes and objectives of different contracts which can be analyzed into several contracts in a way that requires applying the provisions of these contracts to them separately. In the event such appliance is not possible, the dominant contract’s provisions shall prevail with regards to its main characteristic...”

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It is also decided that a simple existence of arbitration clause in one of the two contracts is sufficient to refer the dispute arising in the two contracts to arbitration as long as the contract in which the arbitration clause was stipulated is related to the other contract, supplementary to it, or prepared for its execution, i.e., it is not independent”.

Extension of Arbitration Clause to non-signatories

Most notably, in a decision issued in 2004, the Court of Cassation in Egypt had to decide whether its case law on the extension of arbitration clauses contained in a compound contract to other contract related to it, could also apply in relation to third parties non-signatories of the arbitration agreement. The Court has ruled that the presence of one of the parties to the arbitration dispute within a group of companies in which a parent company contributes in its capital is not a proof of the parent company’s commitment to the arbitration clause as long as it did not interfere in the implementation of the contract or cause any confusion to the other contractor.

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Conclusion

In conclusion, notwithstanding the enormous importance and effect of the rule of Privity of Contracts, the jurisprudence in the United Arab Emirates has demonstrated an aim towards a more liberated view allowing the extension of arbitration clause to contracts in which no arbitration clause has been inserted. Such appliance takes place in the presence of composite or compound contracts with contracts related to the main contract or prepared for the purpose of its execution. Such overturn of jurisprudence shall be closely examined with regards to its importance. It enables the spread of arbitration to other contracts in the event that some prerequisites are fulfilled (the simple referral in one of the two contracts on the arbitration clause is sufficient to refer the dispute arising in the two contracts to arbitration as long as the contract in which the arbitration clause was mentioned is affiliated with the other contract, supplementary to it, or prepared to implement it, i.e., it is not independent of it).

Ghenwa Bou Melhem

Paralegal



Mohamed El-Houseny

Partner