Case Study

The Benefits of Arbitration
Larkden Pty Ltd v Lloyd Energy Systems Pty Ltd[1]

Michael DG Heaton QC[2]

Abstract

The *Larkden v Lloyd Energy Systems* cases provide an illustration of the benefits of arbitration under the new *Commercial Arbitration Acts* as well as the Courts' support for arbitration. The arbitration concerned a patent licensing agreement, challenges to jurisdiction, expertise of the arbitral tribunal, speed, efficiency, control, an award involving constructive trusts and specific performance effectively involving third but related parties, enforcement proceedings and party conduct endeavouring to avoid an unfavourable award.

Licencing Agreement and Appointment of Arbitrator

Larkden licensed Lloyd by a worldwide licence in respect of certain patents to inventions and corresponding rights in relation to renewable energy. Lloyd was a research and development company. Larkden claimed that Lloyd and a third party sought to file US and Australian patent applications based on modifications and improvements to Larkden's technology. The applications lodged in the USA were by a US corporation and a subsidiary of Lloyd. Larkden and Lloyd were in dispute as to pending patents and royalty implications under the licencing agreement. The licencing agreement required all disputes arising in connection with the licence to be settled by arbitration in accordance with the *Commercial Arbitration Act 2010* (NSW). Lloyd instituted arbitration proceedings. Mr Steve White, a solicitor,[3] was appointed as arbitrator by the President of the New South Wales Law Society and accepted the appointment on 19 October 2010. Mr White held degrees in intellectual property and specialises as a solicitor in that field. He was also a graded arbitrator with the Institute of Arbitrators and Mediators Australia.

Challenges to Jurisdiction

Larkden first challenged Mr White's jurisdiction on the grounds that the disputes were not arbitrable because they concerned matters exclusively within the province of the Commissioner of Patents or the

1 [2011] NSWSC 268; [2011] NSWSC 1305; [2011] NSWSC 1331 and [2011] NSWSC 1567.

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3 White SW Computer Law – www.computerlaw.com.au.

Federal Court. Larkden also challenged the arbitrator's jurisdiction in respect of certain matters on the basis that they were hypothetical only and did not give rise to a dispute within the meaning of the arbitration clause.

The arbitral tribunal heard the objection on 11 November 2010. On 25 November 2010 Lloyd served a statement of claim in the arbitration. On 26 November 2010 the arbitrator ruled in accordance with section 16(8) of the CAA (NSW) as a preliminary question, that he had jurisdiction.

On 10 December 2010 Larkden pursuant to section 16(9) issued proceedings in the New South Wales Supreme Court requesting the Court to decide the matter of jurisdiction determined by the arbitrator in his preliminary ruling. The hearing took place on 17, 23 and 24 February 2011 at which stage the arbitration was scheduled to resume on 9 May 2011.

On 1 April 2011 Hammerschlag J ruled that the arbitrator stayed within jurisdiction in relation to the issues the subject of the challenge by Larkden and had jurisdiction to grant the relief claimed in the Lloyd claim.

The Arbitration

The arbitration proceeded between 25 July and 3 August 2011 before Mr White. Lloyd was claimant and cross defendant, Larkden was respondent and cross claimant.

On 7 September 2011 Mr White published 'draft reasons' dealing with the various claims and cross claims determining that '*the parties should have the relief that they sought in their respective claims in which they were successful including specific performance*'. Larkden was very substantially the successful party.

In the 'draft reasons' the arbitrator stated:

> *40.1 The parties should have the relief that they sought in their respective claims in which they were successful including specific performance.*
>
> *40.2 However, whilst the Respondent [Larkden] is entitled to, amongst other things, a suitably moulded constructive trust the Tribunal's view is that a declaration against a third party to the arbitration, namely Solfast, or a declaration in rem is not appropriate or available.*
>
> *40.3 That said having regard to the admissions made in paragraph 22 of the Reply the Tribunal is prepared if requested to make orders that the Claimant [Lloyd] holds its shares in Solfast on trust for the Respondent or such other suitably moulded relief.*
>
> *40.4 Further, the Tribunal is only prepared to find that the Respondent's submissions in relation to the constructive trust and fiduciary duties only extend as would arise ordinarily by reason of one holding the legal title of another as bare trustee and no further.*
>
> *40.5 The tribunal's view is that parties should now agree on appropriate orders and if necessary the Tribunal will hear further submissions on this issue.*

On 13 September 2011 Lloyd appointed the voluntary administrators under section 439A of the *Corporations Act 2001* (Cth).

Interim Award

Then on 20 September 2011 the arbitrator published further reasons and made orders constituting the award as follows:

> *(1) The Tribunal determines and declares that, pursuant to clause 5.4(a) of the Licencing Agreement dated 16 November 2001 between the Claimant and the Respondent ("the Head Licence"), the Respondent is entitled to be made owner of, and have assigned to it, all the rights, title and interest in the inventions embodied in:*
>
> > *the Solfast Patent Application (being PCT/AU2009/001278) ("the Solfast Patent Application"); and*
> >
> > *the patent applications ("the Assigned Patent Applications") set out in Exhibit C to the Patent Assignment and Settlement Agreement dated 4 March 2010 between Ausra Inc and the Claimant ("the Ausra Settlement Agreement") as may be amended from time to time in accordance with the Ausra Settlement Agreement.*
>
> *(2) The Tribunal determines and declares that the Claimant holds on constructive trust for the Respondent all its rights, title and interest in Solfast Pty Ltd (including its Solfast Pty Ltd shares) on behalf of the Respondent.*
>
> *(3) The Tribunal determines and declares that the Claimant holds on constructive trust for the Respondent all its rights, title and interest in the inventions embodied in the Assigned Patent Applications.*
>
> *(4) The Tribunal orders, pursuant to section 33A of the Commercial Arbitration Act 2010 (NSW), that the Claimant specifically perform clause 5.4(a) of the Head Licence by:*
>
> > *immediately procuring Solfast Pty Ltd to execute a deed of assignment in the form of the Annexure A to these orders;*
> >
> > *taking all necessary steps to file and prosecute the Solfast Patent Application in the name of the Respondent;*
> >
> > *irrevocably nominating the Respondent as the Nominated Assignee of the Assigned Patent Applications and forthwith notifying Areva Inc in writing of the irrevocable nomination; and*
> >
> > *taking all necessary steps to ensure that the Respondent's interests in the prosecution of the Assigned Patent Applications are protected and secured.*

(5) The Tribunal orders that the Claimant perfect the Respondent's interest in the Assigned Patent Applications by:

irrevocably nominating the Respondent as the Nominated Assignee of the Assigned Patent Applications and forthwith notifying Areva Inc in writing of the irrevocable nomination;

taking all necessary steps to ensure that the Respondent's interests in the prosecution of the pending Ausra Patent Applications are protected and secured.

(6) The Tribunal orders that the Claimant furnish the Respondent with all necessary assistance as requested by the Respondent from time to time, in relation to any proceedings the Respondent may take against Solfast and/or Areva including, without limitation, any proceedings under sections 32 and 36 of the Patents Act 1990 (Cth), such assistance to include (without limitation) providing the Respondent with all documents in the possession, custody or control of the Claimant necessary for the Respondent to prosecute any claims against Solfast and/or Ausra under sections 32 and 36 of the Patents Act 1990 (Cth).

(7) Costs Reserved.

(8) Liberty to Apply.

Enforcement Proceedings and Invalidity Of Charges

On 26 September 2011 Larkden issued proceedings in the New South Wales Supreme Court seeking first leave to commence and prosecute the proceeding pursuant to section 440D(1) of the *Corporations Act 2001* and second an order pursuant to section 35(1) of the CAA (NSW) recognising and enforcing the interim award of 20 September 2011 by Mr White (the interim award) against Lloyd by making declarations and orders in the form set out in the interim award. Hammerschlag J on 5 October 2011 granted leave pursuant to section 440D to proceed to bring recognition and enforcement proceedings under section 35 of CAA (NSW).

On 3 November 2011 Hammerschlag J made orders for recognition and enforcement of the arbitral award. It appears that during the course of the arbitration, on 17 May 2011, Lloyd executed a charge over the Solfast shares in favour of Graphite Energy Pty Ltd. On 3 June 2011 Graphite Energy assigned its interest in the charge to Graphite Energy NV. On 8 September 2011 Graphite Energy NV gave notice of an event of default under the charge and effected transfer of Lloyd's shares in Solfast to Graphite Energy NV. In a First Circular to Creditors dated 15 September 2011 the administrators stated that Graphite Energy and Graphite Energy NV were related parties of Lloyd. Larkden foreshadowed a challenge to the validity of the charge on the basis that it was void under section 267(1) of the Corporations Act 2001 which provides:

(1) where:

a company creates a charge on property of the company in favour of a person who is or

> *in favour of persons at least one of who is, a relevant person in relation to the charge; and*
>
> *within 6 months after the creation of the charge, the chargee purports to take a step in the enforcement of the charge without the court having, under subsection (3), given leave for the charge to be enforced;*
>
> *the charge, and any powers purported to be conferred by an instrument creating or evidencing the charge, are, and are taken always to have been, void.*

Hammerschlag J stated the notice of default was served on Lloyd and Solfast by Graphite Energy NV within 6 months of the creation of the charge and Larkden maintains that both companies are controlled by Mr Geoffrey Kinghorn and Mr Nick Bain who were, at material times, directors of Lloyd. Further Larkden asserted the purported transfer of the Solfast shares to Graphite Energy NV was void and those shares remained held by Lloyd on a constructive trust for Larkden.

Hammerschlag J rejected defences raised by Lloyd under section 36(1)(a)(iii) and section 36(1)(b)(ii) of the CAA. He stated:

> *(21) Under cl.5.4(a) of the licencing agreement, if Lloyd develops any improvements or modifications to the Technologies, it must allow Larkden to own such improvements and modifications. In simple terms, Larkden's assertion, which was accepted by the arbitrator and reflected in the terms of the Award, is that Lloyd had done this through the vehicle of Solfast. This is clearly resolution of a dispute in connection with the Licencing Agreement.*

Costs Award, Enforcement and Challenges

The arbitrator made a costs award on 12 October 2011. The arbitrator ordered that Lloyd pay Larkden's costs of and incidental to the issues included in the award pursuant to section 33B(4)(c) of the CAA The arbitrator settled Larkden's costs on a party and party basis pursuant to section 33B(1) and section 33B(4)(b) of the CAA at $943,849.07. He also ordered that Larkden's costs of and incidental to a second arbitration which was not pursued by Lloyd were payable by Lloyd on a legal practitioner and client basis in accordance with section 33B(4)(c) of the CAA and settled those costs at $38,419.75. He ordered that Lloyd pay Larkden's costs of the costs of award in accordance with section 33B(1) in the sum of $8,000 and finally ordered that all costs were immediately due and payable.

An issue arose between the administrators and Larkden as to whether those costs came within the purview of a deed of company arrangement which had been entered into which would entitle Larkden to participate only to the extent of other unsecured creditors or whether the costs where outside the purview of the deed of company arrangement which would mean Larkden was entitled to enforce them to their full amount.

Hammerschlag J found that the arbitrator's costs award of 12 October 2011 was not a claim arising on or before 13 September 2011 within the meaning of section 444D(1) of the *Corporations Act 2001*. This

judgment was given on 16 December 2011. Hammerschlag J stood over to 20 February 2012 the issue as to whether the costs were covered by the definition of 'Claim' in the deed of company arrangement. His Honour indicated that Larkden was entitled to the orders which it sought irrespective of whether it would succeed on what he termed 'this second issue'. Accordingly he made orders for leave under section 444E(3) of the *Corporations Act 2001* to proceed against Lloyd and for orders against Lloyd for payment of costs as awarded by the arbitrator.

Conclusion

Larkden follows the internationally recognised position in respect of patent disputes, namely that a contractual dispute involving patents which does not impinge on exclusive statutory powers remains prima facie arbitrable. The decision reflects Australia's pro-arbitration policy and reinforces the fact that Australian courts will hold parties to their agreement to arbitrate. Larkden demonstrates the benefits of expertise in the arbitral tribunal, efficiency, speed and control. Further the award involved a constructive trust and specific performance and was effectively enforceable against third parties through the claimant. But for Court applications the arbitration would have been completed in a few months. Even with the Court applications it was completed within about 12 months. How much longer would it have taken in Court?