



CONSTRUCTION
LAW
INSTITUTE

IS FRAUD ARBITRABLE?

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Background

Fraud is an intentional perversion of truth for the purpose of inducing another in reliance upon it to part with some valuable thing belonging to him or to surrender a legal right. It seems obvious that one cannot arbitrate a dispute involving fraud. The Court will set aside an Arbitral award if it finds that the subject matter of the dispute is not capable of settlement by arbitration or the award is in conflict with the public policy of a Country. Fraud is contrary to public policy and therefore not arbitrable.



Exceptions

In a recent Kenyan case of **Kenneth Maweu Kasinga v Cytonn High Yield Solutions LLP & Capital Markets Authority**, the Court discussed the exceptions to the general rule that fraud is not arbitrable. The Plaintiff entered into an investment agreement with the Cytonn and invested his money into a structured investment fund at a pre-agreed return, payable upon maturity. The parties agreed to refer all disputes that may arise under that agreement to an Arbitrator for final resolution.

Due to the COVID19 pandemic, Cytonn invoked the force majeure clause and communicated to the Plaintiff that he was unable to redeem his investment and interest and thereby extended the investment period for another 12 months. The Plaintiff was dissatisfied with that decision and he filed a suit against Cytonn and Capital Markets Authority (CMA).

In a bid to avoid the arbitration agreement, the Plaintiff pleaded that the Investment Agreement was entered into as a result of fraudulent misrepresentation. That contrary to the law, the number of investors in Cytonn's private offer was more than 100 which made it a public offer and not the promised private offering. The Court was faced with the issue of whether the suit should be stayed and referred to arbitration or whether the subject matter of the suit being fraud, is non-arbitrable and therefore not subject to the Arbitration Agreement between the Plaintiff and Cytonn



The Decision.

The Court was alive to the principle that save for fraud, Courts would ordinarily respect arbitration agreements between the parties. In respect to the pleadings of the parties, three governing principles on fraud have emerged:

1. Where a party pleads fraud and the fraud relates to a right against the whole world (in rem) as opposed to a right against a particular person (in personam), then the matter is non-arbitrable.
2. Where the fraud relates to a dispute against a particular person (in personam) but involves a serious or complex question of fraud, then arbitration is similarly ousted as an appropriate forum for the dispute.
3. The Court does not oust the arbitration jurisdiction merely on the allegation of fraud. A party who seeks to oust the jurisdiction of an Arbitrator must not only plead fraud but must demonstrate the nature of the alleged fraud with full particulars, which on the face of the pleadings raise a serious question of fraud to be tried.

Pleadings and Remedies

The Court is duty bound to scrutinize the remedies sought in the pleadings. Where the reliefs sought are in the nature of remedies for a breach of contract as opposed to its rescission due to the alleged fraud, a Court is more likely to conclude that the allegations of fraud are strategic and insufficient to oust the jurisdiction of the Arbitrator. Conversely, where the pleadings show a close fit between the allegations of fraud made and the remedies which are not in the nature of enforcing the contract but avoiding it, the Court is more likely to oust the jurisdiction of the Arbitrator and hold that the dispute is not arbitrable. The Court observed that the Plaintiff pleaded a case sounding in breach of contract. That the prayers sought in the Plaint revealed that the Plaintiff was interested in enforcing the contract but not to avoid it. The Plaintiff wanted to obtain the benefits of the contract as concluded between himself and the Cytonn through specific performance. Having made this choice, the Plaintiff cannot turn around and make the claim that he is, in fact, suing for fraud and deception. The Court concluded that the dispute was arbitrable and that the parties were bound by their arbitration agreement. The suit was stayed pending arbitration.

Conclusion

It is not enough to plead fraud and hope that it is a magic wand for a Court to oust the jurisdiction of an Arbitrator. The pleadings must be drafted in a consistent style with the allegations of fraud flowing to the remedies that vitiate a contract. A party cannot approbate and reprobate all at the same time



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