A "I agree with counsel for the defendant that it is no use saying the memorandum incorporates the promissory note if in fact, when one looks at the promissory note, it says something different from what is said in the memorandum. That will not do. One cannot correct the memorandum by looking at the promissory note. One may, I think, incorporate the terms of one document by reference into the memorandum . . ."

B I do not find this passage easy to understand. It appears to have been held that the promissory note was not incorporated in the memorandum as it differed from it but inconsistencies in their terms do not prevent two documents being read as one.

In the present case the memorandum of the agreement and the charge together constitute the note or memorandum for the purposes of section 6 C and as they contained all the terms of the contract, it cannot in my view be held that section 6 was not complied with.

I would therefore allow the appeal.

LORD FRASER OF TULLYBELTON. My Lords, I have had the advantage of reading in draft the speech of my noble and learned friend Lord Wilberforce and I agree with it.

D For the reasons given by him I would allow the appeal and remit the action to the Chancery Division.

LORD KEITH OF KINKEL. My Lords, for the reasons very fully set out by your Lordships, to which I cannot usefully add, I too am of opinion that the appeal should be allowed.

E *Appeal allowed.*

Solicitors: *Herbert Smith & Co.; Adrian James & Co.*, incorporating *Snowman, Gardiner & Co.*

J. A. G.

F [HOUSE OF LORDS]

* NOVA (JERSEY) KNIT LTD. . . . . APPELLANTS

AND

KAMMGARN SPINNEREI G.m.b.H. . . . . RESPONDENTS

G 1976 Dec. 6, 7, 8, 9, 13, 14; 1977 Feb. 16 — Lord Wilberforce, Viscount Dilhorne, Lord Salmon, Lord Fraser of Tullybelton and Lord Russell of Killowen.

Arbitration—Stay of judicial proceedings—Bills of exchange—Payment for machinery sold—Bills dishonoured—Allegation that they were obtained by fraud—Arbitration in Germany—Action in England on bills of exchange — Whether claims on bills H *should be decided by arbitration—"Dispute"—Arbitration Act* 1975 (c. 3), s. 1 (1)

Bill of Exchange — Notice of dishonour — Allegation of fraud — Arbitration in Germany in respect of sale of machinery — Action in England on bills of exchange — Whether claim for unliquidated damages available as defence, set off or counterclaim to action—Whether action to be stayed

By virtue of a partnership agreement made in 1970 and an assignment made in 1973 an English company and a German company became partners; the former was to supply [illegible]

with certain machinery to be used in Germany in partnership operations. It was agreed that all disputes arising from the partnership relationship should be decided by an arbitration tribunal in Germany provided for in a separate agreement. In 1972 the English company sold the machinery to the German company receiving in return 24 bills of exchange payable on different dates between March 1973 and December 1975. After six of them had been honoured, the German company refused further payments, alleging that the bills had been obtained by fraud. The partnership and the German company commenced arbitration proceedings in Germany. In 1974 the English company commenced an action in England claiming payment of the bills. The German company having applied to have this action stayed, Bristow J. refused a stay. The Court of Appeal reversed his decision.

On appeal by the English company:—

Held, allowing the appeal (Lord Salmon dissenting), that the stay of the action should be refused, since, on the evidence relating to German law by which the arbitration agreement was governed, the arbitration agreement did not extend to the claims on the bills of exchange (post, pp. 718B–C, 720B, 722A–B, 729H—730A 732E–G).

Held, further, that there was no "dispute between the parties with regard to the matter agreed to be referred" within section 1 (1) of the Arbitration Act 1975, under which accordingly there was no jurisdiction to stay the court proceedings (post pp. 718C, 720D, 722A–B, 730B–C).

Held, further, that a claim for unliquidated damages under a contract for sale was no defence to a claim under a bill of exchange accepted by the purchaser, nor was it available as set off or counterclaim, and *Russell* v. *Pellegrini* (1856) 6 E. & B. 1020, a case relating to freight, was insufficient authority for departing from that rule (post, pp. 720B–C, 721C–D, 722A–B, 729H—730A, 732G, 733B–D).

Per Lord Russell of Killowen. *Russell* v. *Pellegrini* should not be followed, even in a freight case, since it is contrary to the principle that liability to pay freight is not to be postponed to the assertion of unquantified cross-claims (post, p. 733E–F).

Russell v. *Pellegrini* (1856) 6 E. & B. 1020 considered.

Decision of the Court of Appeal [1976] 2 Lloyd's Rep. 155 reversed.

The following cases are referred to in their Lordships' opinions:

Agra and Masterman's Bank Ltd. v. *Leighton* (1866) L.R. 2 Exch. 56.
Bede Steam Shipping Co. Ltd. v. *Bunge y Born* (1927) 27 Ll.L.Rep. 410.
Brown, Shipley & Co. Ltd. v. *Alicia Hosiery Ltd.* [1966] 1 Lloyd's Rep. 668, C.A.
Dakin v. *Oxley* (1864) 15 C.B.N.S. 646.
Di Sora v. *Phillipps* (1863) 10 H.L.Cas. 624, H.L.(E.).
Henriksens Rederi A/S v. *T.H.Z. Rolimpex (The Brede)* [1974] Q.B. 233; [1973] 3 W.L.R. 556; [1973] 3 All E.R. 589, C.A.
Lamont (James) & Co. Ltd. v. *Hyland Ltd.* [1950] 1 K.B. 585; [1950] 1 All E.R. 341, C.A.
Meyer v. *Dresser* (1864) 16 C.B.N.S. 646.
Russell v. *Pellegrini* (1856) 6 E. & B. 1020; 26 L.J.Q.B. 75.
Seligmann v. *Le Boutillier* (1866) L.R. 1 C.P. 681.
Warwick v. *Nairn* (1855) 10 Exch. 762.

The following additional cases were cited in argument:

Adams v. *National Bank of Greece S.A.* [1961] A.C. 255; [1960] 3 W.L.R. 8; [1960] 2 All E.R. 421; H.L.(E.).

A *Annefield, The* [1971] P. 168; [1971] 2 W.L.R. 320; [1971] 1 All E.R. 394, C.A.
Arab Bank Ltd. v. *Ross* [1952] 2 Q.B. 216; [1952] 1 All E.R. 709, C.A.
Bank Polski v. *K. J. Mulder and Co.* [1942] 1 K.B. 497; [1942] 1 All E.R. 396, C.A.
Bankers & Shippers Insurance Co. of New York v. *Liverpool Marine & General Insurance Co. Ltd.* (1925) 21 Ll.L.Rep. 86, C.A.; 24 Ll.L.Rep. 85, H.L.(E.).
B *Beattie* v. *E. & F. Beattie Ltd.* [1938] Ch. 708; [1938] 3 All E.R. 214, C.A.
Black-Clawson International Ltd. v. *Papierwerke Waldhof-Aschaffenburg A.G.* [1975] A.C. 591; [1975] 2 W.L.R. 513; [1975] 1 All E.R. 81, H.L.(E.).
Chapman v. *Cottrell* (1865) 3 H. & C. 865.
Cottage Club Estates Ltd. v. *Woodside Estates Co. (Amersham) Ltd.* [1928] 2 K.B. 463.
C *Daunt* v. *Lazard* (1858) 27 L.J.Ex. 399.
Dawes, Ex parte, In re Moon (1886) 17 Q.B.D. 275, C.A.
Dawes v. *Tredwell* (1881) 18 Ch.D. 354, C.A.
De Tchihatchef v. *Salerni Coupling Ltd.* [1932] 1 Ch. 330.
Evans Marshall & Co. Ltd. v. *Bertola S.A.* [1975] 2 Lloyd's Rep. 373, C.A.
Graham v. *Seagoe* [1964] 2 Lloyd's Rep. 564, C.A.
D *London and North Western Railway Co.* v. *Jones* [1915] 2 K.B. 35.
London Sack and Bag Co. Ltd. v. *Dixon & Lugton Ltd.* (1943) 170 L.T. 70; [1943] 2 All E.R. 763, C.A.
Moore v. *Povey* [1940] W.N. 121; 56 T.L.R. 564.
Parana Plantations Ltd., In re [1946] 2 All E.R. 214, C.A.
Piercy v. *Young* (1879) 14 Ch.D. 200, C.A.
Rouyer Guillet et Cie v. *Rouyer Guillet & Co. Ltd. (Note)* [1949] 1 All E.R. 244, C.A.
E *Saga of Bond Street Ltd.* v. *Avalon Promotions Ltd. (Note)* [1972] 2 Q.B. 325; [1972] 2 W.L.R. 1250; [1972] 2 All E.R. 545, C.A.
Seven Seas Transportation Ltd. v. *Atlantic Shipping Co. S.A.* [1975] 2 Lloyd's Rep. 188.
Sheels v. *Davis* (1814) 4 Camp. 119.
Thomas (T. W.) & Co. Ltd. v. *Portsea Steamship Co. Ltd.* [1912] A.C. 1, H.L.(E.).
Trickey v. *Larne* (1840) 6 M. & W. 278.
Wilde v. *Sheridan* (1852) 21 L.J.Q.B. 260.

APPEAL from the Court of Appeal.

This was an appeal by the plaintiffs, Nova (Jersey) Knit Ltd., with G leave of the House of Lords, from a decision of the Court of Appeal (Lord Denning M.R., Stephenson and Bridge L.JJ.) allowing unanimously the appeal of the defendants Kammgarn Spinnerei G.m.b.H., the present respondents, from the order of Bristow J. in chambers, whereby he had dismissed the defendants' appeal from the order of Master Ritchie, dismissing the defendants' application for a stay under section 4 of the H Arbitration Act 1950 of all further proceedings herein in respect of the claims under paragraphs 1 and 2 of the statement of claim.

These paragraphs were as follows:

"(1) The plaintiffs are the holders of six bills of exchange drawn by the plaintiffs on the defendants payable to the plaintiffs or order. Each of the said bills was duly accepted by the defendants payable at Barclays Bank International Ltd., 168 Fenchurch Street, London E.C.3 . . .

"(2) Each of the said bills was duly presented for payment but was dishonoured by non-payment and noted for protest." A

The facts are stated in their Lordships' opinions.

Sir John Foster Q.C. and *David Donaldson* for the appellants.
John Wilmers Q.C. and *Jonathan Mance* for the respondents. B

Their Lordships took time for consideration.

February 16, 1977. LORD WILBERFORCE. My Lords, the appellants/plaintiffs are suing the respondents/defendants in an English court upon six bills of exchange drawn by the appellants on and accepted by the respondents. The respondents wish to have the proceeding stayed, under section 1 (1) of the Arbitration Act 1975, in order that the claim may be referred to arbitration in Germany. The Court of Appeal, reversing a judgment of Bristow J., gave effect to the respondents' application for a stay, and the appellants are appealing against that order. No question arises as regards any future steps which may or may not be taken if the action is allowed to proceed. C

The bills were given in part payment for the price of 12 textile machines sold by the appellants to the respondents. The bills themselves of course contained no arbitration clause (they would not be valid bills if they did) and there was no arbitration clause in the (oral) contract for the sale of the machines. To find the agreement for arbitration on which the respondents rely it is necessary to look further into dealings between the parties. D

In 1969 the appellants, an English company, and the respondents, a German company, agreed to a joint venture for the manufacture of jersey material in Bietigheim, Germany, where the respondents carried on business. This venture was organised through a German limited partnership (Kommanditgesellschaft) which was formed on January 20, 1970, by a partnership agreement in writing. The parties to this agreement were, as limited partners, the appellants and a trustee company ("R.T.G."), and (in accordance with a requirement of German law) an unlimited partner, a newly formed company called Nova-Knit Jerseystoffe GmbH. The respondents were not parties to the agreement, or partners (Lord Denning M.R. appears to be under a misapprehension as to this) but, as the appellants were certainly aware, they were one of several "beneficiaries" for whom R.T.G.'s interest in the partnership was held. The respondents later, but not until February 1973, became partners by assignments from R.T.G. The agreement established the new limited partnership under the name Nova Knit Jerseystoffe GmbH, Fabrik textiler Stoffe K.G. ("the K.G.") and provided for the contributions in capital and know-how to be contributed by the partners. It contained an arbitration clause in the following terms (in translation): E F

"18. *Arbitration agreement*

"All disputes arising from the partnership relationship or occasioned by (or 'in connection with') the partnership relationship between the partnership and the partners shall be decided by the arbitration tribunal provided for in a separate document."

The "separate document" was not executed until March 20, 1972. It opened with a recital in the following terms (in translation):

A "A limited partnership agreement was made between the undersigned on 20.1.1970. Under clause 18 of that agreement all disputes arising out of this partnership relationship between the partnership and the partners, or among the partners shall be decided by an arbitration tribunal. Accordingly the parties make the following agreement":

B There followed the usual type of clauses for the constitution and working of the tribunal. This document was signed by the three partners. It was not signed by the respondents.

It is on clause 18 of the partnership agreement as implemented by the 1972 document that the respondents found their argument for a stay.

Before coming to the argument in law, it is necessary to outline briefly the origin and nature of the disputes which have arisen. The C 12 machines already referred to were sold by the appellants to the respondents in October–December 1972: they were then leased by the respondents to the K.G. in accordance with a previously executed leasing agreement (dated August 11, 1970). The machines were invoiced at £16,000 each, and in part payment for them the defendants in January 1973 accepted 24 bills of exchange payable in pairs at monthly intervals D from March 31, 1973, to December 31, 1975, which totalled £173,568 inclusive of interest. Thus, both the agreement for sale and the acceptance of the bills took place before the date (February 1973) when the respondents were partners.

The first six of the bills were paid on maturity, but on December 21, 1973, the respondents, through their lawyer, informed the appellants E that the remaining bills would not be met. The appellants issued the writ in these proceedings on November 13, 1974, claiming the money due on six bills totalling £44,544 plus interest. Later they issued further writs relating to the remaining bills which depend for their result on the present action. The claims which the respondents wish to assert against the appellants by way of defence, set off or counterclaim fall under two heads: (1) They claim damages in respect of the alleged mismanage- F ment of the business of the K.G. which has in fact collapsed for which they say the appellants are responsible. (2) They claim that some of the machines supplied by the appellants were not new machines but second-hand.

These claims are undeniably unliquidated claims for damages. They are being pursued in Germany in arbitration proceedings, brought G initially (April 1974) by the K.G. against the appellants to which, it appears, the respondents have been joined as co-claimants (November 1975 which, in fact, is subsequent to their application for a stay). The substance of the respondents' claim is that the whole of their dispute with the appellants ought to be dealt with by the arbitrators in Germany and that they ought not to be ordered by an English court to pay money due on the bills of exchange until their cross-claims have been H dealt with. It was this argument that was accepted by the Court of Appeal.

The appellants, on the other hand, contend that whatever is the nature and merit of any cross-claims the respondents may have, these cannot be set up against a claim on bills of exchange and that the latter claim is not submissible to arbitration.

The application for a stay is based on section 1 (1) of the Arbitration Act 1975. (There is an alternative contention based on section 4 (2) of

the Arbitration Act 1950, repealed by the Act of 1975, but there is no material difference between the provisions and it is not necessary to decide which applies.)

There is no doubt that the relevant arbitration agreement is not a domestic arbitration agreement so that, prima facie, section 1 (1) applies and a stay is mandatory. It remains however open to the appellants to show, the onus being upon them, that "there is not in fact any dispute between the parties with regard to the matter agreed to be referred." If they succeed in this, the stay will be refused. Either way, no discretion enters in the matter and the, unknown, merits of the respondents or demerits of the appellants are irrelevant.

The appellants take, inter alia, two points. (1) That the agreement for arbitration does not extend to the claim now before the English court, viz., the appellants' claim on the bills. (2) That there is no dispute as to the claim on the bills. In my opinion they are right on both.

As a preliminary it is necessary to ascertain the applicable law. First, there is no dispute that the partnership agreement of 1970 and the separate document of 1972 are both governed by German law. It is common ground—so accepted in the respondents' printed case—that questions as to the legal effect of these documents including in particular the scope of the arbitration agreement, depend entirely upon German law and so are to be decided upon evidence of experts in German law. Each side has adduced evidence of this kind, in affidavit form, from distinguished lawyers who, though in agreement on many points, differ on others and indeed on the crucial issues. As to matters where they differ, the court has to decide which to prefer: this it must do after the best consideration it can give to the authorities quoted, the reasoning used, and, residually, to general and accepted principles of law. There is no certain formula which enables judges in English courts to reach a certain result where experts genuinely differ, and in this case, there are differences between the conclusions of the Court of Appeal and those of the judge (Bristow J.). I shall have to differ from some of those of the Court of Appeal.

Secondly, as to the bills of exchange, I have no doubt that they are governed, as to all matters affecting their substantial effect, by English law. In this, English law agrees with the uncontradicted opinion of the appellants' expert in German law. Under section 72 (2) of the Bills of Exchange Act 1882, the interpretation of the acceptance is determined by the law of the place where the acceptance is made. The word "interpretation" in this context appears to bear a wide meaning (see *Chalmers on Bills of Exchange*, 13th ed. (1964), p. 241 and notes), but even if it does not extend to matters of substance, these would be governed by the proper law, which, in the present case would be the same. "Acceptance" by definition (section 2) means acceptance completed by delivery or notification and (section 21) the contract is not complete until delivery of the instrument or, if acceptance is written on the bill, when the drawee gives notice that he has accepted it.

In the present case, as I read the communications between the respondents (as acceptors) and the appellants (as drawers), the contract was intended to be and was completed by delivery, which undoubtedly took place in London, the communication being, not a notification in the statutory sense, but merely a statement of intention to deliver. If this is not right, and the communication was a "notification," this still took

A place in London as the place where the communication reached the drawer. On any view of the matter therefore all questions as to the effect or discharge of the bills are governed by English law.

In the light of this I revert to the first question, which is to be restated as follows: whether as a matter of German law the arbitration clause (sc. clause 18 in the partnership agreement and the separate agreement) applies to a bill of exchange given in part payment of the B purchase price for goods sold by the appellants to the respondents. For this purpose I assume, contrary to the appellants' contentions and, incidentally, to some formidable arguments, that the arbitration clause applies to disputes between partners (and is not limited to disputes between the partnership and the partners) and that the respondents, though not partners at the date of the arbitration agreement or of the C contract of sale, or of the acceptance of the bills, are entitled to take advantage of the arbitration clause.

The evidence on this point from the expert witnesses is full and helpful. Both experts refer to, cite from and analyse two decisions of the Imperial Supreme Court in Germany, the Reichsgericht, one of 1909 (R.G.Z. 71, 14), the other of 1924 (Hans. R.Z., 787). If these were D the only authorities and there were nothing to do but to decide between them, it would, in my opinion be necessary to prefer the later case. The former was one concerned with a partnership which, in agreement with the appellants' witness, I would understand to have related essentially not to a direct claim on a bill of exchange, but to the obligations of the partners inter se to contribute towards the liability on the bill which one partner had discharged. The later case, on the contrary, E was a commercial case between merchants in Hamburg, in which the court treated the earlier (1909) decision as not establishing a principle: it (the 1924 decision) was said to turn upon "custom" but I accept the opinion that it reflected the general view of market men. But the matter does not rest with these decisions. There are subsequent statements in text books of undoubted authority, quoted verbatim in the evidence which, with varying degrees of emphasis, make it clear that the accepted law now is that if an arbitration clause is to require submission to arbitration of claims under bills given by merchants in payment of a price, there must be a clear indication of intention. Thus *Stranz, Wechselgesetz Kommentar* [*Commentary on the Bills of Exchange Ordinance*], 13th ed., referring specifically to the case of bills of exchange says that "in dubio" it is not to be taken to be the intention to submit claims under the bills G to arbitration. *Thomas* in *Das privatrechtliche Schiedsgerichtsverfahren* [*Arbitration Proceedings*], 2nd ed. (1957), says that the plea of an agreement to submit to arbitration will not succeed if such agreement only relates to the transaction underlying the issue of the bill of exchange. A manifest intention is required. The word "manifest" is also used by *Baumbach-Schwab Schiedsgerichtsbarkeit* [*Arbitration*], 2nd ed. (1960), H described as a work "of great authority." *Grimm-Rochlitz* in *Das Schiedsgericht in der Praxis* [*Arbitration in Practice*] (1959) requires express reservation to an arbitral tribunal. *Schönke* in *Das Schiedsgerichtsverfahren nach dem heutigen deutschen Recht* [*Arbitration Procedure in Modern German Law*], 2nd ed. (1954), after referring to the two Reichsgericht decisions, in a comment on that of 1924 says at pp. 97, 98: "There will be few, if any, arbitration agreements, which hereafter will be held to be applicable to claims under bills of exchange." The respondents' witness

does not refute or deal with these impressive citations but merely asser that there is a difference where the agreement to arbitrate is contained i a partnership agreement. But this is taken account of by the comments tors since they have the 1909 decision clearly in mind. I have, on th balance of evidence no doubt that his opponent's argument is fully mad good. His evidence is disregarded by the Court of Appeal which on th point preferred the respondents' evidence. But the overwhelming weigh of the authority on the appellants' side make it necessary to disagree. I my opinion the conclusion must be reached that the arbitration clause- even on the assumptions I have stated above—does not extend to cov the appellants' claims on the bills. This is sufficient to enable th appellants to succeed.

I shall deal however with the second point. I take it to be clear la that unliquidated cross-claims cannot be relied upon by way of extin guishing set-off against a claim on a bill of exchange: *Warwick* v. *Nai* (1855) 10 Exch. 762; *James Lamont & Co. Ltd.* v. *Hyland Ltd.* [195(1 K.B. 585. As between the immediate parties, a partial failure of co sideration may be relied upon as a pro tanto defence, but only when th amount involved is ascertained and liquidated: *Warwick* v. *Nairn*, Exch. 762; *Agra and Masterman's Bank Ltd.* v. *Leighton* (1866) L.I 2 Exch. 56; *James Lamont & Co.* v. *Hyland* [1950] 1 K.B. 585, *Brow Shipley & Co. Ltd.* v. *Alicia Hosiery Ltd.* [1966] 1 Lloyd's Rep. 66 The amount claimed here in respect of the machines is certainly neith ascertained nor liquidated, and the claim in respect of mismanageme is one for a wholly unrelated tort, so that there would seem to be basis for denying the appellants' claim that, as regards the bills, the is no dispute.

The Court of Appeal, however, in support of their opinion that, view of these cross-claims, the respondents were entitled to have t whole matter referred to arbitration, relied upon a decision of 1856 *Russell* v. *Pellegrini*, 6 E. & B. 1020; 26 L.J.Q.B. 75. This is a case some obscurity—not noticed in *Scrutton on Charterparties*, *Carv Carriage of Goods by Sea*, *Russell on Arbitration*, but maintaining precarious hold on life through a footnote in *Halsbury's Statutes*, vol. p. 438, and mentions in two lesser works, *Hogg, The Law of Arbitrati* (1936), pp. 59, 61, and *Palmer on Arbitration* (1932), p. 16. There are t things I would say about that case.

1. Both the plaintiff's claim (for hire or freight) and the defendan claim (for damages on account of seaworthiness) arose out of one and t same contract—the charterparty—which contained a very wide arbitrati clause (" any difference of opinion between the parties to this contra either in principle or detail "). There is a wide—and surely unbridgeal —gap between that and such a case as this, where the contract su on (the acceptance of the bills) is a separate contract from that of t sale of the machines, and from that contained in the partnership agr ment and itself contains no arbitration clause. To get to an arbitrati clause it is necessary to remove two steps, one to the contract of s and another to a partnership agreement which may have had so connection with the contract of sale. The passage of the judgment Lord Denning M.R. where he says that none of the cases considers position when the contract of sale contains an arbitration clause see with respect, to take its stand on the opposite side of the gap.

2. It is far from clear whether *Russell* v. *Pellegrini* vouches

A proposition that, in such a case as was there involved, there is a "dispute" as to the claim on the bills. Lord Campbell C.J. says, 26 L.J.Q.B. 75, 77:

> "... although ... there is no dispute as to the ... freight claimed, yet as there is a bonâ fide dispute as to the implied warranty of seaworthiness, it must have been in the contemplation of the parties to this agreement that a cross demand of that nature should be a matter to be referred, so that it might be seen on which side the balance was."

If this is saying that, in the end, the cross-claim may be set off against the claim, it is quite inconsistent with later well-known authorities (*Bede Steam Shipping Co. Ltd. v. Bunge y Born* (1927) 27 Ll.L.Rep. 410 and *Henriksens Rederi A/S v. T.H.Z. Rolimpex* (*The Brede*) [1974] Q.B. 233) and must be regarded as wrong.

If, on the other hand, the effect of the decision was that, although both claim and cross-claim were to go to arbitration, the claim, for freight, would even in the arbitration not be capable of dispute (as in effect was held in *The Brede*), then the case is no authority in support of the proposition (the relevant one for present purposes) that there is a dispute about the bills. As Lord Denning M.R. pointed out in *The Brede*, (at p. 249) the case of a bill of exchange is similar to (but a fortiori) a claim for freight, in that unliquidated cross-claims cannot be set up against it.

I am therefore of opinion that *Russell* v. *Pellegrini*, 6 E. & B. 1020, even if right as a decision on the particular clause there involved, is insufficient as authority to set against the established rule that unliquidated claims must be the subject of a cross-action and cannot be used to create a "dispute" in a bill of exchange.

My Lords, I must emphasise, since it seems to be suggested that all the merits require the whole dispute to go to arbitration in Germany, that it is not mere technicality that supports the appellants' claim. When one person buys goods from another, it is often, one would think generally, important for the seller to be sure of his price: he may (as indeed the appellants here) have bought the goods from someone else whom he has to pay. He may demand payment in cash; but if the buyer cannot provide this at once, he may agree to take bills of exchange payable at future dates. These are taken as equivalent to deferred instalments of cash. Unless they are to be treated as unconditionally payable instruments (as in the Act, section 3, says "an unconditional order in writing"), which the seller can negotiate for cash, the seller might just as well give credit. And it is for this reason that English law (and German law appears to be no different) does not allow cross-claims, or defences, except such limited defences as those based on fraud, invalidity, or failure of consideration, to be made. I fear that the Court of Appeal's decision, if it had been allowed to stand, would have made a very substantial inroad upon the commercial principle on which bills of exchange have always rested. In my opinion, this is a straightforward case of an action on bills, to which no admissible defence has been put forward. I would hold that the judge was right, in result, in refusing a stay and I would restore his order and allow the appeal. As I have said, we are not concerned in this appeal with the future course of this action, but I must demur to the view that a result similar to granting a

stay under the Arbitration Act can be obtained by any procedural stay of another character. So to hold would seem quite counter to long accepted principles regarding claims on bills of exchange and would represent an undesirable change in the law.

VISCOUNT DILHORNE. My Lords, I have had the advantage of reading the speech of my noble and learned friend, Lord Wilberforce, and I agree with it entirely. In my opinion the respondents are not entitled to have the proceedings brought against them on the six bills of exchange stayed under section 1 (1) of the Arbitration Act 1975. That was their claim and we were not called upon to express any view on the question whether, if the appellants had obtained judgment on the bills, the making of an order that execution of that judgment should be stayed pending the determination of the cross-claims would have been right or proper. Bearing in mind the intrinsic nature of a bill of exchange, "an unconditional order" which the appellants were entitled to regard as a deferred instalment of cash, and the fact that cross-claims, unless based on fraud, invalidity or failure of consideration are not allowed, it appears to me that seldom, if ever, can it be right while denying the right to bring a cross-claim, to allow a cross-claim to operate as a bar to execution and to prevent the holder of a bill of exchange receiving the deferred instalment of cash which the parties agreed he should get.

In my opinion this appeal should be allowed.

LORD SALMON. My Lords, in 1969 the appellants entered into an oral arrangement with the respondents to embark on a joint venture to manufacture jersey knit material in Germany. The respondents were well known as German manufacturers of worsted yarn but had never manufactured jersey knitwear. The appellants were well known as English manufacturers of jersey knitware. The respondents were to supply the bulk of the capital and the factory premises necessary for carrying out the joint venture whilst the appellants were to supply the managerial marketing and technical expertise, and select and procure the necessary machinery for operating the joint venture. For the purpose of carrying out this arrangement, a partnership with a name to which I shall refer as K.G. was created in Germany by a partnership agreement in writing dated January 20, 1970, and made between the appellants, a trust company (R.T.G.) representing both the respondents' interests and various minor interests in the partnership, and a company wholly owned by the appellants and the respondents. The first two partners were limited partners and the third an unlimited partner. According to German law the respondents were not partners because their very substantial interests in the partnership were held in trust for them by R.T.G. which alone was recognised as a partner representing these interests.

German law differs from English law in that a partnership is an entirely different entity from the partners which comprise it. Clause 18 of the partnership agreement reads as follows:

> "All disputes arising from the partnership relationship or occasioned by (or in connection with) the partnership relationship between the partnership and the partners shall be decided by the arbitration tribunal provided for in a separate document."

In my view clause 18 is obscurely worded. On March 20, 1972, a separate document headed "Arbitration Agreement" was signed on

behalf of all three partners in K.G. and constituted the "separate document" referred to in the partnership agreement of January 20, 1970. It opens with the following words:

> "A limited partnership agreement was entered into between the undersigned on 20.1.70. Under clause 18 of that agreement all disputes arising out of this partnership relationship between the partnership and the partners, or among the partners shall be decided by an arbitration tribunal."

These words seem to me to have clarified or rectified or extended clause 18 of the partnership agreement by making it plain that the parties intended that all disputes arising out of the partnership relationship between the partnership and the partners, or among the partners themselves, should be decided by an arbitration tribunal. It would be odd indeed if the partners had intended that any disputes arising from or occasioned by the partnership relationship should be settled by arbitration if they arose between the partnership and the partners, but not if they arose between the partners themselves. The learned judge, however, took the view that what he describes as the apparent extension of clause 18 contained in the opening words of the arbitration agreement was due to a draftsman's error. This is the only finding in his judgment with which I am unable to agree. I think it would be necessary to have extrinsic evidence of such an error and of the failure of the signatories to notice it—I see that there were five of them—before concluding that any such error was made. An omission of or mistake in a word is one thing and a draftsman's error might well be inferred from it, but the adding of four words is quite a different matter.

On February 28, 1973, the respondents' share in the partnership capital, amounting to DM 1,786,000, was assigned to them by R.T.G. and from that moment they became partners and entitled amongst other things to take advantage of the arbitration clause. It might be said that prior to that moment they were de facto but not de jure partners. After that moment they became partners de jure as well as de facto.

K.G. originally commenced operations with 40 machines leased to them by the respondents. Between October and December 1972, it was decided to replace 12 of these machines which were somewhat out of date by 12 completely new ones. The respondents were prepared to finance this replacement and agreed to buy the new machines from the appellants and lease them back to K.G. at a rent which would over a period of years cover the purchase price. Twelve supposedly new machines were invoiced to the respondents by the appellants at £16,000 each and in part payment the respondents accepted 24 bills of exchange totalling £173,568, payable in pairs at three monthly intervals at Barclays Bank, Fenchurch Street in London between March 31, 1973 and December 31, 1975. The oral agreement for the sale of these machines contained no arbitration clause.

The first six of the 24 bills were honoured on maturity, but on December 21, 1973, the respondents informed the appellants that none of the remaining bills would be met. K.G.'s business was by then collapsing and indeed K.G. became hopelessly insolvent in March of 1973. Mr. Paul Burg, the son of one of the directors and co-owners of the appellants, was dismissed from his position as a director; he had been responsible for the day-to-day management of [illegible] was alleged by the respondents to be due to the manipulation of the business

by Mr. Paul Burg in connivance with the appellants so that large quantities of the goods manufactured by K.G. were sold to the appellants at considerably less than half their market value and yarn was bought from the appellants at about one-third more than its market price in Germany to the great benefit of the appellants but to the ruin of K.G. In addition it was alleged by the respondents that six of the supposedly new machines sold to them by the appellants as new were in fact second-hand, in generally poor condition and worth substantially less than half the price at which they were charged to the respondents.

In April 1974, arbitration proceedings were launched in Germany by K.G. claiming DM. 2 million as damages against the appellants for the loss it had suffered on account of the malpractices of the appellants and Mr. Paul Burg to which I have just referred. The respondents owned by far the largest share in K.G.'s capital which had formerely been held in trust for them by R.G.T. This arbitration, to which the respondents were joined as co-claimants, in May 1975, has, I understand, reached an advanced stage and should be concluded reasonably soon. If K.G. and the respondents are successful and are awarded the amount claimed in the arbitration, this sum would far exceed the total of the amount due under the bills of exchange which the respondents have refused to meet.

When the arbitration proceedings were commenced against the appellants, four of the bills of exchange accepted by the respondents and totalling just on £30,000 had matured and the respondents had refused to meet them. The appellants, however, waited for over six months after the launching of the arbitration proceedings before issuing the writ in the present action. Later they commenced further actions in respect of the remaining bills which will follow the result of the present action.

The appellants' application for a stay is made under section 1 of the Arbitration Act 1975. This section makes it plain that since the arbitration agreement upon which the respondents rely is obviously not a domestic arbitration agreement, then, if the action is "in respect of any matter agreed to be referred" the court is obliged to stay the action "unless [the court is] satisfied that . . . there is not in fact any dispute between the parties with regard to the matter agreed to be referred. . ."

My Lords, it is conceded that the agreements of 1970 and 1972 respectively are both governed by German law nor is there any doubt that the bills of exchange are governed by English law. This last point is, however, of little importance since according to the evidence of the two experts in German law, English and German law are substantially the same so far as bills of exchange are concerned.

As I have indicated earlier, under the arbitration agreement the matters agreed to be referred are all disputes between the partnership and the partners and among the partners arising from or occasioned by the partnership relationship. In my opinion these matters include claims on the bills of exchange. The language of the arbitration agreement is very wide. The appellants however contend in effect that the arbitration agreement should be read as referring to "all disputes excepting those relating to claims on bills of exchange."

In construing a contract governed by foreign law our courts must obtain

> "evidence of any foreign law applicable to the case; and . . . evidence of any peculiar rules of construction if any such rules exist, by the foreign law. With this assistance, the court must interpret

A the contract itself on ordinary principles of construction." (*Di Sora* v. *Phillipps* (1863) 10 H.L.Cas. 624, 633, *per* Lord Cranworth.)

Two exceptionally learned and experienced German lawyers gave the required evidence about German law, unfortunately only on affidavit. I say unfortunately because it is extremely difficult merely from reading documents without any opportunity of asking questions, to decide which B of the two versions (when they conflict) is to be preferred. The Court of Appeal preferred the evidence of the respondents' witness, Professor Heldrich. The learned judge preferred the evidence of the ellants' witness, Dr. Jacques. Nevertheless both the Court of ..peal and the learned judge came to the firm conclusion that this arbitration clause did not exclude disputes relating to claims on bills of exchange. I agree with that view, especially as the C contrary view involves writing into the arbitration agreement words which are not there and which have the effect of forcing the partners into court if there is any dispute between them arising from or occasioned by the partnership relationship involving a claim on a bill of exchange. I do not suppose that partners in Germany are, as a rule, any keener than partners in England to have any dispute of any kind between them forced into open D court. That no doubt is why the arbitration agreement is formulated in such wide terms.

There are apparently only two German decisions which bear directly on the question whether an arbitration clause covers a dispute arising from a claim on a bill of exchange—and these were both cited and analysed by the expert witnesses. The first was a decision of the Imperial Supreme E Court in 1909 (R.G.Z. 71, 14) which upheld the defendants' plea that the plaintiffs' claim under a bill of exchange fell within the arbitration clause in the partnership agreement. In that case the three parties to the agreement, in order to raise money for the partnership, drew a bill on themselves and accepted it and then negotiated it at a bank. The plaintiff paid the bill on aturity and the bank endorsed it to him. He then sued one of the other partners on the bill but the court held that he was prevented by the F arbitration clause in the partnership agreement from suing on the bill and that the dispute should go to arbitration. The second case was decided by the Federal Supreme Court in 1924 (Hans. R.Z. 787). This concerned the scope of an arbitration clause in a contract of sale between Hamburg merchants and raised the question whether a claim on a bill accepted by a buyer in payment for goods bought by him fell within the arbitration clause in the contract of sale. The court held that it did not and that this clause G related only to such questions as the quality of the goods, their delivery and the like. It is not altogether plain whether or not the court, apart from the construction of the arbitration clause, relied on the custom of Hamburg merchants or mercantile custom in general. Nor does it matter. I do not believe that these cases conflict nor that there is any need to choose between them. Much must have depended on the actual wording of the clauses of H which we know little if anything. The first decision concerned an arbitration agreement between partners which for the reasons I have already indicated would be likely to be construed liberally so as to cover all claims including claims on bills of exchange. The second decision concerned an arbitration clause in a commercial contract to which different considerations may well apply.

For myself, I do not think that there is much, if any, real difference between the relevant evidence given by one expert w...

The relevant evidence is confined to German law applicable to the case and any peculiar rules of construction laid down by that law. It must be remembered that it is for our courts and not for the experts to interpret the relevant arbitration agreement on ordinary principles of construction (*Di Sora* v. *Phillipps*, 10 H.L.Cas. 624). I am afraid that a great deal of each witness's evidence (as often happens in similar cases) is concerned with expounding his own interpretation of the agreement.

I agree that Dr. Jaques has set out in his evidence, verbatim, citations from text books of undoubted authority which I have read and re-read as I am sure the Court of Appeal and the learned judge did. I confess that these citations have failed to convince me just as they failed to convince the Court of Appeal and the learned judge that the arbitration agreement in the present case does not cover claims on bills of exchange. I would point out that the citations all relate to arbitration agreements in general or between merchants. None of them touches upon arbitration agreements between partners. *Stranz, Wechselgesetz Kommentar* [*Commentary on the Bills of Exchange Ordinance*], 13th ed., states the general principle: "Whether an arbitration clause . . . extends to obligations under bills of exchange . . . is a question of interpretation in each case." He then goes on to say that in the case of an arbitration clause in a commercial contract for the sale of goods between merchants "it cannot, if there is any doubt, be assumed that (the) clause . . . applies to claims under bills accepted in payment for the goods sold." *Baumbach-Schwab Schiedsgerichtsbarkeit* [*Arbitration*], 2nd. ed. (1960), says much the same at p. 79: "The intention to submit the claim under the bill of exchange to arbitration . . . must, particularly in the case of merchants, be manifest in order to justify the defence." *Schönke* in *Das Schiedsgerichtsverfahren nach dem heutigen deutschen Recht* [*Arbitration Procedure in Modern German Law*], 2nd. ed. (1954), in connection with the 1924 decision writes at pp. 97, 98: "There will be few, if any, arbitration agreements, which hereafter will be held to be applicable to claims under bills of exchange." In my opinion, amongst the few, there will be arbitration agreements between partners.

Since there was no evidence to the contrary, I must assume that German law is the same as English law in requiring the utmost good faith in the relations between partners inter se.

My Lords, it has been argued on behalf of the appellants that (a) there is no dispute in relation to the bills because the respondents have no defence arising from or occasioned by the claim made in respect of them and (b) that even if there is a dispute, it did not arise from nor was it occasioned by the partnership relationship.

I agree that there is no defence to the bills, since the only possible defence (which is not relied on by the respondents) could be that their acceptance had been procured by fraud, duress or for a consideration which had failed and because the damages claimed in the arbitration are unliquidated damages and such damages cannot be set off against a claim on the bills of exchange: *James Lamont & Co. Ltd.* v. *Hyland Ltd.* [1950] 1 K.B. 585.

The courts however certainly have a discretion to stay the execution of a judgment: see R.S.C., Ord. XIV, r. 3 (2). This discretion is rarely exercised in the case of a claim on a bill of exchange save in exceptional cases. The appellants dispute that there is any power to stay execution of a judgment on a bill of exchange although they took no steps to apply for summary judgment which they could have done at any time after the service of the

writ in early 1975 until the judgment of the Court of Appeal given on April 8, 1976.

Although, in my view, there is no defence to the bills, there is, in my view, a very real dispute in relation to them. The appellants were saying that they should obtain payment of the bills at once. The respondents' contention was that it would be a great injustice if they were forced to pay up when they had a strong prima facie case that the appellants, by the grossest breach of good faith, have cheated them out of a considerably larger sum than the total amount of the bills; moreover this issue is about to be decided by the final award of the arbitration tribunal in Germany which has already made its interim award.

The respondents were saying in effect that if the circumstances of this case were not exceptional, it is difficult to imagine any that could be and that accordingly if the appellants obtained judgment in this country, that judgment would be stayed (possibly on terms as to payment into court) until after their cross-claim against the appellants had been decided; and that it is inconceivable that our courts would allow the judgment to be executed against foreign respondents who it might well turn out had been cheated out of vast sums of money by their partners the English appellants. The appellants dispute this.

It seems clear to me that whichever party is right or wrong, this is a dispute within the meaning of that word in the arbitration agreement subject to it arising out of or being occasioned by the partnership relationship between the respondents and the appellants.

I would add that I naturally recognise that bills are generally regarded as the equivalent of money and the courts do not, save in special circumstances, stay a judgment on a bill even if the direct parties to it are the sole parties to the action; and certainly there could be no question of a stay if the bills had been discounted and the holders in due course were the plaintiffs in the action. In the special circumstances alleged in this case, however, I hardly think that if this action was allowed to proceed, there would be any alarm or surprise in the City of London if the judgment which the appellants might obtain on the bills were stayed pending the trial of the counterclaim which would have to be delivered were the order of the master and the trial judge to be restored. For the counterclaim to be fought in London would be a great waste of time and money since the issues in this counterclaim would be the same as those which over a long period have been investigated by the German arbitration tribunal whose final award is now being awaited.

It is obvious that the only reason why the respondents bought the machinery from the appellants was for the purpose of the joint venture which they had arranged. At the time of the purchase, the K.G. partnership was in existence for the purpose of operating the joint venture of the respondents and the appellants. The appellants were partners in K.G. and the respondents had contributed by far the largest share of the partnership capital (held in trust for them by R.G.T. who were partners in K.G.). Moreover, the respondents had leased the machinery to K.G. which obviously they had bought and the appellants had sold for the benefit of that partnership. At the time the dispute arose, the respondents had become partners in K.G. Looking at the realities of the situation, I find it impossible to hold that the dispute arose out of and was occasioned by anything other than the partnership relationship between the respondents and the appellants. Accordingly, in my opinion, quite apart from authority, this case falls

fairly and squarely within the arbitration agreement and the action should be stayed. This conclusion however is also strongly supported by authority. I refer to *Russell* v. *Pellegrini*, 6 E. & B. 1020. That case did not concern a claim on a bill of exchange but a claim by a shipowner for freight due under a charter and a cross-claim by the charterers for damages caused to them by the vessel's unseaworthiness. The charter contained the following clause:

> "Should any difference of opinion arise between parties to this contract, either in principle or detail the same shall be referred for arbitration . . ."

In my opinion there is no real distinction between the words "difference of opinion" in that case and the word "dispute" in the present case. If A who is sued by B says, "I agree that I may have no defence to your claim in law, but I know that you have no defence to mine and I do not think it right that I should pay you before you pay me; and I will not do it," does this not constitute equally "a dispute" and "a difference of opinion (between A and B) either in principle or detail"?

A claim for freight has the following characteristic (vital to this case) which is the same as that of a claim on a bill of exchange: a cross-claim for unliquidated damages cannot be set off or set up against the claim or in any way operate as a defence to it. *Dakin* v. *Oxley* (1864) 15 C.B.N.S. 646; *Meyer* v. *Dresser* (1864) 16 C.B.N.S. 646. There are, of course, numerous differences between bills and freight, but none relevant to this appeal, e.g. a bill is a negotiable instrument but this is irrelevant to a claim by one of the immediate parties to the bill against the other. In *Russell* v. *Pellegrini*, 6 E. & B. 1020, the charterers obtained a stay of the action brought by the owners and an order for the owner's claim and the charterers' cross-claim to be referred to arbitration. I will not repeat the passage in Lord Campbell's judgment, with which I entirely agree, since it is recited in the judgment of Lord Denning M.R. I think the whole case was also put very aptly by Erle J. when he said, at pp. 1029–1030:

> "The shipowner says, pay me my monthly freight. The other says, first pay me my damages. 'On no', says the shipowner . . . 'these are unliquidated damages, and cannot be set off'. The charterer says in reply, 'I am clearly of the opinion that under this contract I ought not to pay you till you pay me; and, if you are of a different opinion, I claim to have that matter referred'. He is summoned into the Bankruptcy Court; and there he says, 'That is my defence'. The commissioner says, most properly, 'That is no defence in a court of law'. 'Well', says the merchant, 'that is the precise reason why I want a reference instead of an action at law. Is it not an honest difference of opinion within the meaning of our agreement?' Now, in my opinion it is, and the case is within the letter and spirit of the Act: . . ."

It was pointed out in the Court of Appeal that the Common Law Procedure Act 1854, section 11, does not differ materially from the Arbitration Act of 1975, section 1 (1) save that in the Act of 1854 the court had a discretion as to whether it should refer whereas under the Act of 1975 there is no such discretion in relation to a non-domestic arbitration agreement. I agree with Stephenson L.J. [1976] 2 Lloyd's Rep. 155, 161:

A "The more I study the different reports of *Russell's* case the harder I find it to resist the common sense behind them, and to resist applying what is said by the judges in that case to this one."

I also agree with Bridge L.J. when he says, at p. 164:

B "If it was . . . right to give the statute of 1854 a large and liberal construction, in my judgment it is, a fortiori, right to do so when construing section 1 (1) of the Act of 1975, bearing in mind that this is an Act to give effect in our domestic law to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards."

If, as I think, *Russell* v. *Pellegrini*, 6 E. & B. 1020 was rightly decided in 1856, nothing has happened in the meantime to make the decision any C less valid now than it was then. That case was followed in *Seligmann* v. *Le Boutillier* (1866) L.R. 1 C.P. 681 by a court consisting of Erle C.J., Willes, Byles and Montague Smith JJ. Authorities of such impeccable lineage cannot lightly be swept aside.

I am afraid that I cannot agree that they should be regarded as inanimate because they have not been referred to in *Scrutton on Charterparties* or *Carver, Carriage of Goods by Sea*, or *Russell on Arbitration*, D nor in any modern reported case. A case which in essence turns upon whether a judgment should be stayed pending the trial of a cross-claim turns on discretion and rarely gets beyond the judge in chambers and, if it does, is quite properly seldom if ever, reported.

I do not attach any importance to the fact that in *Russell* v. *Pellegrini*, 6 E. & B. 1020, the plaintiffs' claim for hire and the defendants' claim for E damages arose out of the same contract which contained the arbitration clause (with which I have already dealt) whereas in the present case the bill naturally contained no arbitration clause, nor, as I have pointed out, did the contract of sale. The arbitration clause in the present case is to be found in the arbitration agreement and partnership agreement which for the reasons I have ventured to explain, is, in my view, vitally connected F with the sale and the dispute between the parties.

The dispute of course concerns the bills, but in this respect only, for no question of set-off arises: it is a dispute as to whether a judgment on the bills would be stayed until after the cross-claim by the respondents for damages has been decided viz. should the respondents be obliged to pay up on the bills now. The respondents contend that the court would in its discretion stay execution of the judgment on the claim. The appellants G dispute this.

For the reasons I have already indicated, I am satisfied that this dispute comes within the arbitration agreement. In those circumstances the Court of Appeal was, in my view, right in concluding that it was obliged to stay the action. In any event it is probably in the interests of both parties that the whole matter should be referred to the arbitration tribunal which is now H dealing with the cross-claim. It would be a waste of time and money if the claim as at present before the tribunal in Germany should have to be relitigated as a counter-claim in the proceedings in this country.

My Lords, I would dismiss this appeal.

LORD FRASER OF TULLYBELTON. My Lords, I have had the advantage of reading in draft the speech of my noble and learned friend, Lord Wilberforce, and I entirely agree with it. I wish to add a brief

comment to emphasise one of the reasons why I consider that, notwithstanding the obvious convenience of having all claims between the parties dealt with together in the German arbitration, the stay of English proceedings should be refused.

The respondents claim that the legal proceedings begun by the appellants in the English court should be stayed because they are "in respect of [a] matter agreed to be referred" to arbitration by an agreement to which section 1 (1) of the Arbitration Act 1975 applies. There is no doubt that the arbitration agreement relied upon by the respondents is not a "domestic arbitration agreement" in the sense of section 1 (2) of the Act. It is therefore one to which section 1 may apply and the question is whether the English proceedings are in respect of a matter agreed to be referred. In my opinion they are not. They are in respect of a claim on bills of exchange and I do not think that the arbitration agreement applies to such a claim.

The arbitration agreement is contained in clause 18 of the partnership agreement dated January 20, 1970, read together with the separate document dated March 20, 1972. It has to be construed according to German law and we have had the benefit of evidence on affidavit from two eminent German lawyers. They were in agreement that bills of exchange occupy a special place in German procedural law but they disagreed on the question of whether the fact that the appellants are suing on bills of exchange accepted by the respondents is of significance for the applicability of the arbitration agreement. Dr. Jaques, whose evidence was produced by the appellants, thought that it was, and Professor Heldrich for the respondents thought not.

Professor Heldrich's opinion on this matter started from the proposition that there is no general presumption either that an arbitration clause is applicable to claims on bills of exchange or that it is excluded, and that the clause itself, the intention of the parties as expressed elsewhere and the other surrounding circumstances are decisive. Professor Heldrich referred to certain German textbooks as authorities in support of that proposition. Dr. Jaques in reply expressed the view that some of these textbooks although compendious and convenient works, did not consider the matter in depth (and his view on that point was not controverted by Professor Heldrich). Dr. Jaques quoted passages from two works which he regarded as the most authoritative on this subject, namely, *Baumbach-Schwab Schiedsgerichtsbarkeit* [*Arbitration*], 2nd ed. (1960), and *Stranz, Wechselgesetz Kommentar* [*Commentary on the Bills of Exchange Ordinance*], 13th ed. The quotation from the latter work includes this sentence:

> "In the case of bills given by merchants in payment of the price of goods it cannot, if there is any doubt, be assumed that a clause providing for submission of disputes to arbitration applies to claims under the bills."

The bills relied upon by the appellants here were given as part of the price of machines bought by them from the appellants. The quotation from the former work includes this sentence:

> "... the intention to submit the claim under the bill of exchange to the arbitration proceedings must, particularly in the case of merchants, be manifest in order to justify the defence."

Other authorities to the same effect are mentioned in the speech of my noble and learned friend, Lord Wilberforce. The result is that in my opinion Dr. Jaques has made good his view, in disagreement with that of Professor Heldrich, to the effect that

A "a very plain manifestation of intention to extend an arbitration clause to claims under bills of exchange is needed to *rebut the presumption* that businessmen neither wish nor expect bills of exchange to be taken into arbitration."

In the present case it is quite clear that the arbitration clause does not contain a plain manifestation to that effect. Accordingly, unless there is B some special reason, arising from the intention of the parties or the circumstances of this case, to make the arbitration clause applicable to claims on the bills it will not do so.

Professor Heldrich's view is that a special reason is to be found in the fact that this arbitration agreement was part of a partnership agreement. I shall assume in favour of the respondents that the clause is to be construed as applying to disputes between partners, as well as to those between the C partnership and one or more partners. Professor Heldrich expresses the opinion that "greater importance is attached to an arbitration clause agreed by a partnership contract than to an arbitration agreement concluded merely on the occasion of an exchange relationship, as for example a sale." He does not cite any authority for that proposition but he relies upon it to explain and reconcile two decisions of the Reichsgericht in 1909 D and 1924 respectively—RG of 2.4.1909, RGZ 71, 14, and RG of 18.8.1925, Seufferts Archiv 79, No. 57. The question in both cases was whether an arbitration clause was applicable to a dispute upon bills of exchange; in the former case the dispute arose between partners, in the latter between a vendor and purchaser. Having considered the explanations of these two cases by Professor Heldrich and Dr. Jaques as carefully as I can, together with a translation of the report in the former case, I come to the opinion E with the greatest respect to Professor Heldrich that it is far from clear that the distinction between them depends upon the fact of the former dispute having arisen between partners. He does not refer to any passage in the textbooks suggesting that as the ground of distinction, and it appears to me that the explanation suggested by Dr. Jaques is more satisfactory; that is that in the 1909 case the bill of exchange had already served its purpose F and the dispute was only concerned with the right of one partner to have a contribution from his co-partner. The result is that, in my opinion, there is nothing special about the intention of the parties or the surrounding circumstances in the present case to lead to an unusually wide construction of the arbitration agreement, and it is not applicable to the present claims on these bills.

G I have the greatest doubt whether the appellants' claim on the bills, assuming in favour of the respondents that there is a "dispute," is a "dispute arising from the partnership relationship or occasioned by [or in connection with] the partnership relationship." At the time when the bills were accepted by the respondents and when the underlying contract of sale of the machines was made (December 1972—January 1973) the respondents were not partners in the partnership referred to in clause 18 H of the partnership agreement. They were "beneficiaries"—see clauses 4 (5) and 14 (4). They subsequently became partners on February 28, 1973, by assignment from the R.T.G., but the R.T.G. had nothing to do with the sale of machines or the acceptance of the bills of exchange and the assignment from them did not carry or include any right or claim in relation to those matters. But it is not necessary to express a concluded opinion upon this point.

I cannot usefully add anything to what my noble [illegible] and on

the Woolsack has said as to the inadmissibility under English law of the respondents' unascertained and unliquidated cross-claim against the appellants' claim on the bills.

I would allow the appeal.

LORD RUSSELL OF KILLOWEN. My Lords, the question in this appeal under the Arbitration Act 1975 appears to me to be whether the condition precedent to an application for a stay is satisfied: and that is whether the plaintiff by its writs on the bills of exchange commenced legal proceedings against the defendant "in respect of any matter agreed to be referred" to arbitration. This must be shown by the defendant in order to establish his standing to apply for a stay: and unless it is established the rest of the section does not arise for consideration.

Was there therefore in this case an agreement taking effect between the plaintiff and the defendant to refer to arbitration the matter of liability of the defendant to the plaintiff under the bills of exchange?

I am prepared to assume that the effect of the 1972 documents was to make clause 18 of the partnership agreement read as though it referred (as in my opinion taken by itself it did not) to disputes between partner and partner: though whether, short of our notions of rectification based upon the 1972 recital, that is right I venture to doubt. I am prepared to assume (without deciding) that the defendant succeeded in 1973 from the trustee company to the latter's complaint as trustee for the defendant (and others) asserted against the plaintiff partner: though I find it difficult to hold that this process of succession has any relevance to a question or matter—the defendant's liability under the bills of exchange—which was no concern at all of the trustee partner.

Be that as it may, and making every assumption in favour of the defendant, the question remains whether on the evidence of German law, the arbitration clause 18 embraces the question (the "matter" within the Arbitration Act) of liability under the bills of exchange. I am in entire agreement with my noble and learned friend, Lord Wilberforce, in his analysis of the evidence of German law on this point. The fact that illness of the plaintiff's expert witness prevented his cross-examination does not detract from the fact that his potent extracts from German works of authority were in no wise challenged as such by the defendant's expert witness in his subsequent affidavit. I conclude therefore that on the evidence of German law there is no ground established for any attitude other than that of English law to the question of the applicability of an arbitration clause to claims under bills of exchange accepted by a purchaser.

This, my Lords, brings me to a consideration of English law in relation to such bills of exchange. It is in my opinion well established that a claim for unliquidated damages under a contract for sale is no defence to a claim under a bill of exchange accepted by the purchaser: nor is it available as set-off or counterclaim. This is a deep rooted concept of English commercial law. A vendor and purchaser who agree upon payment by acceptance of bills of exchange do so not simply upon the basis that credit is given to the purchaser so that the vendor must in due course sue for the price under the contract of sale. The bill is itself a contract separate from the contract of sale. Its purpose is not merely to serve as a negotiable instrument, it is also to avoid postponement of the purchaser's liability to the vendor himself pending agreement grounded upon some allegation of failure in some respect by the vendor under the underlying contract, unless it be total or quantified partial failure of

A consideration. It is conceivable in theory that an arbitration clause in an underlying contract of sale should sufficiently clearly embrace liability under a bill of exchange, though it is not easy to envisage a clause so inconsistent with the nature and function of such a bill. But there is no ground whatever in English law for attributing to clause 18 of the partnership agreement—nor itself even an underlying contract of sale—such potency.

B I conclude therefore that in English law (which would be applicable unless the German law were shown to be different) the defendant has not established that the plaintiff's actions on the bills of exchange are "in respect of a matter agreed to be referred."

It was argued that the case of *Russell* v. *Pellegrini*, 6 E & B. 1020 was persuasive authority at least by analogy, that the claims under the bills C of exchange should be referred to arbitration together with the cross-claims of the defendant. That case concerned freight. It was contended that since in that case the freight claim was stayed for arbitration together with unliquidated cross-claims for damage to cargo, and since a claim to freight shared at least in some measure the sanctity of a claim under a bill of exchange, the same decision should be reached in the instant case. But it is first to be observed that in that case it D was necessary in suing for freight due to assert and rely upon the very contract—the charterparty—that contained the arbitration clause: where as here the bill of exchange operates as a contract in its own right and it was not necessary for the plaintiff to assert the underlying contract for sale of the machines, let alone the partnership agreement containing the arbitration clause.

E But, my Lords, I do not merely rely upon that distinction, because I do not consider that *Russell* v. *Pellegrini* should be followed even in a freight case: the stay of proceedings in order that arbitration might proceed in order to find "where lay the balance" between the freight due and the amount of the unquantified cross-claim for damage to cargo is self-evidently contrary to the well estabished principle of our commercial law that liability to produce freight due is not to be postponed by the F assertion of such cross-claims.

There were in this appeal other points argued of which I need only mention two.

The first was whether the defendant was from the outset of the partnership agreement what was labelled in evidence of German law an "internal partner": but whatever the rights and wrongs of that ques- G tion it is quite impossible to interpret clause 18 as embracing the defendant as a partner from the outset: the agreement distinguished quite clearly a "partner" from a "beneficiary" such as the defendant. The second such point was the argument that the law of the bills of exchange was, under the Bills of Exchange Act, German law because their acceptance was notified in Germany: the shortest answer to that H argument is that it was not: there was no notification until receipt of the letter relied upon in London.

Accordingly, I agree that the appeal must be allowed.

Appeal allowed.

Solicitors: *Herbert Smith & Co.; Herbert Oppenheimer, Nathan & Vandyk.*