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COFOLA INTERNATIONAL 2015

Current Challenges to Resolution of International (Cross-border) Disputes

Conference Proceedings

Klára Drličková (ed.)

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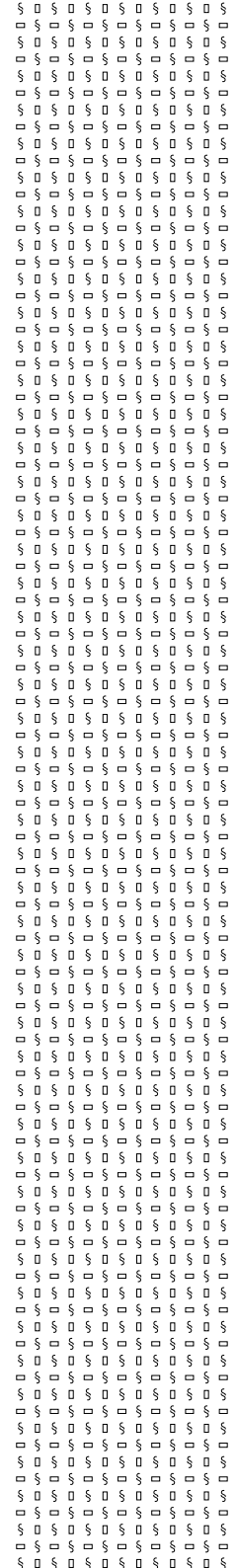

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PREFACE

The conference "COFOLA = Conference for Young Lawyers" is annualy organized by the Masaryk University, Faculty of Law from 2007. The main aim of this conference is to give floor to the doctoral students and young scientists at their early stage of career and enable them to present the results of their scientific activities.

Since 2013 COFOLA has been enriched by special part called "COFOLA INTERNATIONAL". COFOLA INTERNATIONAL focuses primarily on issues of international law and the regulation of cross-border relations and is also oriented to doctoral students and young scientists from foreign countries. COFOLA INTERNATIONAL contributes to the development of international cooperation between students and young scientists from different countries. It constitutes the platform for acadmic discussion and develops scientific and presentation skills of young scientists. Such a platform for scientific debate beyond the boundaries of one country contributes to the global view on the law, which is so important in current days.

COFOLA INTERNATIONAL 2015 dealt with the issue of resolution of international (cross-border) disputes. Disputes are inevitable part of international (cross-border) relationships. There are many sources of possible disagreement between the parties. If the disputes cannot be resolved by the negotiation between the parties, they will need to be resolved in a legal process. International commercial arbitration has become the preferred way of dispute resolution in the area of international commercial contracts. Arbitration is also often used in disputes between states and foreign investors, i.e. investment arbitration. Dispute resolution is an issue in relation to consumer contracts. Last but not least, the use of modern technology in dispute resolution is currently a topic.

All of these areas of dispute resolution have been already discussed in various sources. However, they still raise lot of questions. And that was exactly the reason why COFOLA INTERNATIONAL 2015 focused

on the resolution of international (cross-border) disputes. The participants have chosen some of these questions and tried to elaborate on them. The doctoral students and other young scientists thus spent two days of fruitful discussion which has been reflected in the following papers.

Klára Drličková

(scientific and organizational guarantor of COFOLA INTERNATIONAL)

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INTERNATIONAL COMMERCIAL ARBITRATION

EXTENSION OF ARBITRATION CLAUSES OVER NON-SIGNATORIES

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Abstract

Consent, the final frontier. International commercial arbitration is deemed to be a dispute resolution mechanism embedded in consent of the parties involved. Presentation of such a mutual understanding is done through an arbitration agreement. Therefore, it is often quoted that the arbitration is a creature of such a contract. However, the aim of this paper is to analyse whether its contractual, indeed consensual, nature is the only element which the courts use to identify the subjects who may compel or must be compelled to arbitrate disputes, or whether they employ other considerations as well. The paper will focus mainly on extension doctrines less known even to a professional audience – assignment, piercing of the corporate veil, estoppel & group of companies. A review of a selected case law and expert opinions leads to a conclusion that consent-finding analysis is definitely a starting point of any analysis. However, at the same time courts and arbitrators do indeed use tools of contract interpretation and the ones based on equity or good faith considerations to establish, and exceptionally force, the implication of consent far beyond what is obvious.

Keywords

Arbitration Agreement; Assignment; Consent; Estoppel; Extension; Group of Companies; Piercing of the Corporate Veil.

1 Introduction

Arbitration proceedings is without doubt one of common instruments which helps both domestic and international merchants to settle their disputes in a more effective way. It is a well-established rule that commercial

arbitration's proceedings arise from the consent of the parties.[1] Therefore, if anyone were to analyse arbitration in its very basics, the answer would necessarily include the view, the arbitration is the proceedings of the settlement of disputes by an agreement of the parties, alternating competence of national jurisdictions.[2] This mutual intention and expressed will leads the parties from their respective national courts of law to a private body, which is however vested with similar authority to decide a presented dispute. Grounds for such deviation – the existence of an arbitration agreement – should be of course well established as the arbitration does not necessarily provide all the safeguards and common features which national procedural rules do. As the consequence, task of any national judge or arbitrator should primarily be to determine whether the arbitration agreement was concluded and who the parties to such agreements are.

This starting point seems to be a straightforward one. Whether a person can participate in an arbitration proceedings depends on whether it has previously entered into a valid arbitration agreement. Contrary to a state litigation, legal or financial interests should play no role in determining who the parties of the arbitration are. *Brekoulakis* summarizes this notion clearly: "*Even if a party is strongly implicated in a dispute before a tribunal and has a great interest in its outcome, he simply cannot participate.*"[3]

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1 See e.g. BORN, Gary B. *International Commercial Arbitration.* First edition. Alphen aan den Rijn: Kluwer Law International, 2009. p. 1; FOUCHARD, Philippe; GAILLARD, Emmanuel; GOLDMAN, Berthold; SAVAGE, John. *Fouchard, Gaillard, Goldman on International Commercial Arbitration.* The Hague: Kluwer Law International, 1999. p. 193; LEW, Julian; MISTELIS, Loukas; KRÖLL, Stefan. *Comparative International Commercial Arbitration.* The Hague: Kluwer Law International, 2003. p. 99; DELVOLVÉ Jean-Luis; ROUCHE, Jean; POINTON, Gerald et al. (eds.). *French Arbitration Law and Practice: A Dynamic Civil Law Approach to International Arbitration.* Second edition. Alphen aan den Rijn: Kluwer Law International, 2009. p. 37; RUBINO-SAMMARTANO, Mauro. *International Arbitration Law.* Second edition. The Hague: Kluwer Law International, 2001. p. 195; BLACKABY, Nigel; PARTASIDES, Constantine; REDFERN, Alan; HUNTER, Martin. *Redfern and Hunter on International Arbitration.* Fifth edition. Oxford, New York: Oxford University Press, 2009. p. 85; BREKOULAKIS, Stavros. *Third Parties in International Commercial Arbitration.* Oxford University Press, 2010. p. 10 - 11.

2 LEW, Julian; MISTELIS, Loukas; KRÖLL, Stefan. *Comparative International Commercial Arbitration.* The Hague: Kluwer Law International, 2003. p. 83.

3 BREKULAKIS, Stavros. Parties in International Arbitration: Consent v. Commercial Reality. In SCHOOL OF INTERNATIONAL ARBITRATION (ed.). *The Evolution and Future of International Arbitration: The Next 30 Years.* London: Queen Mary University of London, 2015, p. 1.

However, such an opinion stems from a classical view on commercial transactions as bilateral ones, with clearly designated parties. Though it may be still true for a significant part of trade, especially sales transactions, contemporary projects are often more complex and sophisticated.[4] In addition, current players in the international commerce are often comprised of multinational enterprises, with a broad net of true subsidiaries or just mere SPV companies.

From the point of substantial law, many legal system do indeed provide a possibility how to distribute substantial responsibilities arising out of contracts (e.g. piercing of corporate veil doctrine) or to bound entities which prima facie did not become parties if good faith and/or justice requires to do so (e.g. various estoppel doctrines in common law, or a notion of venire contra factum proprium in many civil law jurisdictions).

However, could an arbitrator or a national court judge use these instruments when considering who is bound by the arbitration agreement? Undoubtedly, arbitration agreement is a contract, but most probably of a hybrid nature, including both substantive and procedural elements. Notwithstanding which doctrine is employed, is he required to always establish an existence of consent, even if merely by implication? Or is he allowed to deem consent as only a traditional element, which may be set aside in specific situations in which more general legal principles should be used?

2 Consent: The One and Only (?)

The answer to the abovementioned questions has two major consequences which arise from the cornerstone of the modern international commercial arbitration – the New York Convention.[5]

The New York Convention provides a clear cut rule in Art. II for each Member States' court to recognize a valid arbitration agreement. This means the Member State's legislation in question must allow for the arbitration proceedings to be held in its territory (positive effect), and prevent

4 One may think especially of construction contracts alongside with financing and insurance transactions.

5 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL).* Available from: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention.html ("New York Convention").

its courts to seize action, once the existence of the arbitration agreement is established (negative effect, unless a subsequent will of the parties would be to the contrary).[6]

More importantly, from the perspective of this paper, Art. V New York Convention provides restrictive set of conditions under which the national court could or should decide on the non-recognition of the presented arbitral award. Amongst the conditions, the non-existence or invalidity of the arbitration agreement takes one of the prominent places.[7]

National legal orders based on the UNCITRAL Model Law[8] follow the same approach. As a result, it is internationally recognized "the arbitration is the creature of the contract".[9] This is the basic methodological point of departure for any further analysis.

The relationship which arises out of the arbitration agreements has, in its essence, a quality of an accessory to a main commercial relationship. A common practice of inserting arbitration agreements into the body of the main contract itself might explain why ordinarily the parties would consider the changes to the main contract would automatically apply to the arbitration clause as well. However, it is a well-established view that the arbitration agreement, though accessory, it is still an autonomous agreement relatively autonomous of the main commercial contract.[10]

This autonomy translates back to the analysis who concluded the arbitration agreement. The main commercial contracts are hardly static ones, especially in the area of international trade and commerce. Quite to the contrary, it may be subject to various changes, either regarding its content or the parties which are performing part or the whole of the obligations. However,

6 VAN DEN BERG, Albert J. *The New York Arbitration Convention of 1958: Towards a Uniform Judicial Interpretation*. Deventer, Boston: Kluwer Law and Taxation, 1981. p. 128.

7 See Art. V(1)(a) New York Convention.

8 UNCITRAL Model Law on International Commercial Arbitration 1985 with amendments as adopted in 2006 [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf

9 LEW, Julian; MISTELIS, Loukas; KRÖLL, Stefan. *Comparative International Commercial Arbitration*. The Hague: Kluwer Law International, 2003. p. 461.

10 HOSKING, James. The Third Party Non-Signatory's Ability to Compel International Commercial Arbitration: Doing Justice without Destroying Consent. *Pepperdine Dispute Resolution Law Journal*. 2012, No. 4, p. 476.

such changes done in the main agreement should not be automatically transferred on the arbitration contract because of its relative autonomy. However, the changes in the content of the main commercial relation do not usually represent a major issue, as the arbitration clauses are typically linked to the subject matter of the main relationship in a general, broad way.

Therefore, the broad scope can in most instances cover even major change executed in the scope of the main obligations. However, any change of the parties to the main relationship or involvement of other subjects in performance of such relationship raise a complex questions of formal and material requirements for the change the accessory arbitration agreement.

3 Written Form: A Condition of Validity or a Mere Proof of Existence

As to the formal validity, the arbitrator should not stop its analysis on the face of the main contract, and narrow it only to the arbitration agreement which was executed in writing – binding only the parties which signed such agreement. Although it is true, that Art. II New York Convention presumes a written form of the arbitration agreement, Art. VII enables parties to avail themselves to any lesser requirement which is stipulated by the legal order of the place where the enforcement of the award is sought.

As an example from an arbitration friendly jurisdiction, one can analyse the Swiss legal order, which is highly regarded in the world of international commercial arbitration.[11] Section 178 Swiss Federal Code on Private International Law ("Swiss Code")[12] requires all arbitration agreements to be in a written form. In this regard, the Swiss Code is considered to be a conservative one. However, in 2003 a major liberal breach was brought by the judgment of the Swiss Federal Supreme Court, which ruled the written form requirement is applicable only to the "original" arbitration

11 In White & Case 2010 International Arbitration Survey: Choices In International Arbitration, Swiss law placed as 4th most commonly governing international contracts, and Geneva scoring 2nd place for the seat of arbitration. See 2010 International Arbitration Survey: Choices In International Arbitration [online]. *Queen Mary University of London. School of International Arbitration* [cit. 2015-09-21].

12 SWITZERLAND. Federal Code from 18 December 1987 on Private International Law. Available from: http://www.admin.ch/opc/de/classified-compilation/19870312/index.html.

agreement, not necessarily to its amendments.[13] Therefore, if there was a written arbitration agreement, the form requirement is met, and the subsequent changes to the agreement may be executed even in other forms.[14]

The liberal trend of non-formalism is not peculiar only to the Swiss legal order. To the contrary, the 2006 amendment of the UNCITRAL Model Law brought some major changes in this field. Art. 7 which deals with the form issues was adopted in two versions: while the first preserved the agreement in writing requirement, but significantly enlarged the meaning of the term "in writing", the second one abandoned any formal requirements at all. Thus, jurisdictions which follow or are inspired by UNCITRAL Model Law provisions do slowly transform their national arbitration acts and drop many of once requested formal elements. As 2009 survey showed,[15] this would be the case of e.g. Denmark, the Netherlands, Norway and Sweden.

The liberal trend was subsequently followed and finally approved by another major arbitration friendly jurisdiction. In 2011, the new French regulation of arbitration was enacted. Though for domestic disputes and arbitration agreements, the formal requirements remained, Art. 1507 Code of Civil Procedure stated explicitly that with regard to any international arbitration agreements, no form requirement exists.[16]

From the formal point of view, the extension / change in the obliged subjects seems to be a possibility. The formal validity of such a change does not seem to be challenged. However, the material validity of such a change seems

13 Decision of Bundesgericht, Switzerland of 16 October 2003, No. 4P.115/2003 [online]. In *www.bger.ch*. Eurospider Information Technology [cit. 2015-07-10]. For comment see HABEGGER, Phillip. Case Note on DFT 129 III 727: Extension of Arbitration Agreements to Non-signatories and Requirements of Form. *ASA Bulletin*. 2004, No. 22, p. 390 et seq.

14 A very similar conclusion was reached in US decision in the Fisser case, where the court examined the doctrine of piercing of the corporate veil, and reached the conclusion that an arbitration agreement may not necessarily bound only the subjects which signed the agreement in person. The written requirement was set more for its evidentiary value, than for the requirement of its validity. Therefore, the written agreement does not necessarily provide an enclosed enumeration of all who are bound by it. See Decision of United States Court of Appeals, Second Circuit, the United State of America of 1. August 1960, No. 25914 [online]. In *Westlaw*. Thomson Reuters [cit. 2015-05-01].

15 WEGEN, Gerhard; WILSKE, Stephan (eds.). *Getting the Deal Through: Arbitration 2009* - Arbitration in 47 jurisdictions. London: Law Business Research, 2010.

16 FRANCE. Code of Civil Procedure. Book IV. Arbitration. In *Legifrance*. Available from: file:///C:/Users/61143/Downloads/Code_39.pdf

unclear – again the consensual nature of the arbitration agreement brings several questions. If the liberal tendencies do not require a strict formal scrutiny, the more important the analysis of parties' true intentions will become.[17]

4 Examples of Extension

The theory and practice of international commercial arbitration recognizes basically two key groups of factual scenarios and legal doctrines which lead to the extension of arbitration agreement.

4.1 Extension as an Exercise in Contract Law

The first group is closely linked with the arbitral contracts deemed as an accessory to the main commercial relationship.[18] The most common examples include the assignment of rights/claims, assumptions of obligations/debts, or change of the contractual party as such. The main interest in these scenarios lies in the analysis how the law applicable treats singular succession cases, especially if it extends its impacts even to the arbitration clauses.

If that is the situation, subjects of the arbitration clause will most probably change automatically with the change of the parties of the main commercial contract. Here, the arbitration clause is a true accessory of the assigned right/assumed obligation/transferred position and share "legal life" of the main subject.[19] The analysis of the true will of the parties is restricted only to the assignment/assumption/transfer agreement. If it is a valid agreement, no further analysis regarding the arbitration clause is necessary.

17 As Sinclair states: "*Article II of the NYC provides a sufficient grounds to refuse the enforceability of the award, if extended over the non-signatory improperly.*" See SINCLAIR, Anthony. The Assignment of Arbitration Agreements. In GAILLARD, Emmanuel; DI PIETRO, Domenico (eds.). *Enforcement of Arbitration Agreements and International Arbitral Awards: The New York Convention 1958 in Practice*. London: Cameron May. 2007, para. 2. 1.

18 YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract and Non-contract Arbitration* [online]. Minneapolis: West, 2009. [cit. 2015-01-30]. § 1. 4.

19 YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract and Non-contract Arbitration* [online]. Minneapolis: West, 2009. [cit. 2015-01-30]. § 1. 5. Additionally see FOUCHARD, Philippe; GAILLARD, Emmanuel; GOLDMAN, Berthold; SAVAGE, John. *Fouchard, Gaillard, Goldman on International Commercial Arbitration*. The Hague: Kluwer Law International, 1999. p. 498; MAYER, Pierré. Extension of the Arbitration Clause to Non-signatories under French Law. In PERMANENT COURT OF ARBITRATION (ed.). *Multiple Party Actions in International Arbitration*. Oxford, New York: Oxford University Press, 2009, p. 194.

However, if the analysis shows the main change is invalid, the change/extension of the parties to the arbitration agreement is still in place, and must be analysed separately. The same is true for jurisdictions which do not consider the arbitration agreement to be an accessory, but indeed a separate, though closely connected, relation. Here, again a separate contractual analysis must be made.

The first approach seems to be dominant in the continental legal orders. The complex of rights and duties which stem from the arbitration agreement moves with the rights and obligation which undergo the change. Arbitration "complex" is deemed as a modality of these rights and obligations, a mode how they could be protected or enforced.[20]

To name some examples. French decisions state the arbitration clauses are conventional, if not indivisible, elements of international commercial contracts,[21] and therefore go sometimes as far as to declare the arbitration agreement as part of the economic value of the contract.[22] Similarly, German decisions stress that a respective arbitration agreement creates a specific *de iure* attribute of the assigned right, and it is therefore transferred automatically alongside such right.[23] Swiss courts reach same conclusion, naming rights and obligations arising out of the arbitration agreement as accessories to the main commercial agreement which are transferred almost automatically; only situation to the contrary may arise out of clear agreement of all parties involved.[24]

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20 See YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract and Non-contract Arbitration* [online]. Minneapolis: West, 2009. [cit. 2015-01-30]. § 1. 5. See also GIRSBERGER, Daniel; HAUSMANINGER, Christian. Assignment of Rights and Agreement to Arbitrate. *Arbitration International*. 1992, No. 8, p. 126 - 130.

21 Courts generally rely on the provision of Art. 1692 French Civil Code which stipulates that the assigned right transfers with all its accessories, including any security. See e.g. Decision of Cour de Cassation, France of 19 October 1999, No. N/A [online]. In *KluwerArbitration* [cit. 2015-05-11].

22 See e.g. Decision of Cour d'Appel de Paris, France of 28 January 1988, No. N/A. In FOUCHARD, Philippe; GAILLARD, Emmanuel; GOLDMAN, Berthold; SAVAGE, John. *Fouchard, Gaillard, Goldman on International Commercial Arbitration*. The Hague: Kluwer Law International, 1999. p. 43.

23 In this regard, German courts employ Art. 401 German Commercial Code, provision quite similar to the abovementioned French one. See e.g. Decision of Bundesgerichtshof, Germany of 2 October 1978, No. III ZR 99/76 [online]. In *JURION* [cit. 2015-05-01].

24 Decision of Bundesgericht, Switzerland of 7 August 2001. No. N/A [online]. In *KluwerArbitration* [cit. 2015-05-01].

English courts reach similar results, however their argumentation is grounded in a different legal basis. Arbitration agreement creates *de iure* procedural remedy, on a contractual basis, for rights claimed out of the contract. The assignment itself may not unbalance the scales of such remedial framework. In other words, the assignee steps into the shoes of the assignor with an acceptance of this remedial framework. Any rights the assignee gained may be claimed and enforce only within such framework.[25]

On the other hand, especially US courts are more reserved and treat the arbitration clauses as any other contract.[26] This tendency may be closely connected to a historic view on the arbitration agreements as personal covenants, which may not easily change the obliged parties.[27] However, the current decisions follow a more flexible approach. The courts concentrate more on the will of the parties, especially a negative one e.g. a non-assignment clauses.[28] Unless a court finds a specific proof of parties' will banning

25 See e.g. Decision of Court of Appeal of England and Wales (Civil Division), Great Britain of 16 April 1997, No. [1997] EWCA CIV 1420 [online]. In *www.bailii.org*. British and Irish Legal Information Institute [cit. 2015-04-15]; Decision of High Court of Justice (Queen's Bench), Great Britain of 21 March 2005, No. [2005] EWHC 455 (COMM) [online]. In *www.bailii.org*. British and Irish Legal Information Institute [cit. 2015-04-15].

26 See YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract, and Non-contract Arbitration* [online]. Minneapolis: West, 2009 [cit. 2015-04-15]. § 5.12; GIRSBERGER, Daniel; HAUSMANINGER, Christian. Assignment of Rights and Agreement to Arbitrate. *Arbitration International.* 1992, No. 8, p. 123.

27 See YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract, and Non-contract Arbitration* [online]. Minneapolis: West, 2009 [cit. 2015-04-15]. § 5. 12.

28 See BORN, Gary B. *International Commercial Arbitration*. First edition. Alphen aan den Rijn: Kluwer Law International, 2009. p. 1187 - 1188. To that regard reference may be made to Lachmar decision where US court specifically pointed to the clause stating the assignee did not take over any obligations arising from the respective commercial agreement. Consequently, it implied it did not take over obligations arising out of arbitration agreement. See Decision of Unites States Court of Appeals, Second Circuit, the United States of America of 14 January 1985, No. 84-7391 [online]. In *Westlaw*. Thomson Reuters [cit. 2015-05-01]. This approach was analysed in GMAC decision where court restricted Lachmar ruling only to those situations when the assignee is respondent of claim, i.e. the party being sued. In other words, the arbitration cannot be compelled against assignee. However, it is possible that assignee may sue under the arbitration agreement as it represent contracted for "remedial system". In other words, the assignee may compel the original debtor to arbitrate the assigned claim. See Decision of United States District Court, Southern District for New York, the United States of America of 25 April 2001, No. 00 CIV. 2893(NRB) [online]. In *Westlaw*. Thomson Reuters [cit. 2015-03-15]; Decision of United States District Court, Southern District for New York, the United States of America of 27 August 2013, No.13 CIV. 2597 (PAE) [online]. In *Westlaw*. Thomson Reuters [cit. 2015-05-01].

the change affecting arbitration agreement, it is most probable it would allow it. In the result, the common law and civil law approach tend to reach similar end results.

Guarantee, contracts for the benefit of thirds, bills of lading and carriage represent another example of the contractual scenario issues.[29] All of them represent a possibility that a third party, which is otherwise not a party to the main commercial relationship, may become a party to the arbitration agreement. However, in these scenarios, the tendency is to prove a specific consent to comply with the arbitration agreement.[30]

4.2 Extension as a Tool for Administration of Justice

The second large group of scenarios stem from the contract law again, however, this time it is interconnected with the doctrines of protection of justice, good faith and the effective resolution of commercial disputes. As the result, the analysis of the parties' will is sometimes overshadowed by these principles.

4.2.1 Estoppel

Common law estoppel doctrine is a classic example. This equity based institute deals with unjust results of unfair, or inconsistent behaviour. As for the specific arbitral estoppel, one can provide a following scenario. A third party commences a court proceedings against any of the parties to contract it draws benefits from.

The argument may be made, that once the benefit is drawn such third party accepts provisions of the contracts, including the arbitration agreement. However, the above mentioned autonomy of the arbitration clause and pure contract analysis may lead to conclusion that the opposite is true. Third party beneficiary might have accepted the performance/benefit, without willing to accede to the arbitration clause, which creates a separate contract, especially if such beneficiary started court proceedings – a clear negation of the arbitration agreement.

29 STEINGRUBER, Andrea. *Consent in International Arbitration.* Oxford: Oxford University Press, 2012. p. 147 - 51.

30 *Ibid.*, p. 42 - 44.

In such situation, depending on all circumstances of the case, the arbitral estoppel may be used by courts, because as decided in e.g. Tepper Realty vs. Mosaic Tile „*In short, [plaintiff] cannot have it both ways. It cannot rely on the contract when it works to its advantage and ignore it when it works to its disadvantage*".[31] Therefore, even though the court would reach the result the third party beneficiary did not consent to the contract, the justice or good faith still require it would be bound by it, as it drew benefits.

The doctrine, used especially by US courts, requires the non-signatory to draw a direct benefit from the main contract. This may either be a situation when a third party willingly accepts the benefit, and when main contracting parties did intent to confer such a benefit on a third party.[32] Decisions indicate that though equitable considerations play a considerable role here, they do not contravene a fundamental consensual basis of arbitration.

On the other hand, another variation of estoppel – so called intertwined estoppel – may lead us clearly outside the realm of consent. This doctrine is often used by US court to deal with claims which arise out of various separate agreements which are however substantially and factually interconnected. But, these various contracts are often concluded between various entities, and may or may not include arbitration clauses.[33] In these cases, the courts seems to favour protection of bona fide expectations and an efficient service of justice within a single type of procedure to a more detailed consent analyses.[34]

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31 BORN, Gary B. *International Commercial Arbitration*. First edition. Alphen aan den Rijn: Kluwer Law International, 2009. p. 1193.

32 Decision of United States District Court, Southern District for New York, the United States of America of 11 August 2011, No. 11 CIV. 00325 (RJH) [online]. In *Westlaw*. Thomson Reuters [cit. 2015-08-20].

33 As a classic example, a construction contract between the client and a construction company, which includes an arbitration provision, connected to various other contract between the company and its suppliers, or subsequent sub-suppliers, or between the client and the general manager of construction. The claims arising out of any of these relationships may be based on evaluation of these other contracts and performance of parties thereto.

34 See e.g. Decision of Unites States Court of Appeals, Eleventh Circuit, the United States of America of 30 December 1993, No. 91-9153 [online]. In *Westlaw*. Thomson Reuters [cit. 2015-08-20]; Decision of Unites States Court of Appeals, Second Circuit, the United States of America of 24 August 1995, No. 94-9118 [online]. In *Westlaw*. Thomson Reuters [cit. 2015-01-14]; Decision of Unites States Court of Appeals, Second Circuit, the United States of America of 18 September 2008, No. 07-2871-CV [online]. In *Westlaw*. Thomson Reuters [cit. 2015-08-20].

4.2.2 Piercing of the Corporate Veil

Another scenario may take us from contract background and lead us to corporate law, where doctrines such as "piercing of the corporate veil" or "alter ego" have place. Though primarily a common law concept, its use in a restricted form could be found even in several civil law countries, e.g. France, Germany and Switzerland.[35] As a globally recognized principle - a basic corporate concept dictates the identity of the corporation is distinctive and separate from the one of its employees, directors and shareholders.[36] Such limitation allows for efficient liability and risk limitation.

However, there may be situation when such independent treatment goes against fairness and justice, especially if it is intentionally misused. As stated by US court itself: "*If any general rule can be laid down, in the present state of authority, it is that a corporation will be looked upon as a legal entity as a general rule, and until sufficient reason to the contrary appears; but, when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime, the law will regard the corporation as an association of persons*."[37]

A classic example - a mother company creating a net of daughter companies as a shield from liability, though the benefits of contracts are directly or indirectly shifted towards the mother. The intensity of immorality varies in the case law, some courts require the malice intent, others analyse only the end results of actions against good faith, morals and justice principles.[38] However, once the analysis of the case allows piercing of the "separability" veil, it is possible to disregard the distinction between the company and its shareholders. Therefore, the use of the doctrine can lead to liability of multiple intertwined companies.

35 See YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract, and Non-contract Arbitration* [online]. Minneapolis: West, 2009 [cit. 2015-01-30]. § 6.01 and 6.15.

36 BLUMBERG, Phillip; STRASSER, Kurt; GOUVIN, Eric; GEORGAKOPOULOS, Nicholas. *Blumberg on Corporate Groups*. Second edition. New York: Aspen Publishers, 2004. Chapter 13. 02. See also BORN, Gary B. *International Commercial Arbitration*. First edition. Alphen aan den Rijn: Kluwer Law International, 2009. p. 1158.

37 BLUMBERG, Phillip; STRASSER, Kurt; GOUVIN, Eric; GEORGAKOPOULOS, Nicholas. *Blumberg on Corporate Groups*. Second edition. New York: Aspen Publishers, 2004. Chapter 13. 02.

38 See See YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract, and Non-contract Arbitration* [online]. Minneapolis: West, 2009 [cit. 2015-01-30]. § 6. 01.

From the perspective of the arbitration analysis, this may lead to a result where not only a signatory to an arbitration agreement, but also its mother company, is bound. One can make an argument, that such a result is not contrary to the consensual nature of the arbitration, as the daughter company never showed will of its own, but of its disguised mother. The legal distinction between puppet daughter and governing mother provided merely a veil to hide the "threads".

4.2.3 Group of Companies

Last, but not least, the French[39] group of companies doctrine concludes the representative list in this category. In a way, it partly resembles estoppel and alter ego doctrines on one hand, and classical contractual approaches on the other hand.[40]

The doctrine is essentially based upon the decision in Dow Chemicals case,[41] and stands on the group of companies settings (not necessarily a holding), and a behaviour of the individual members of such a group. In short, French courts have accepted the extension of the arbitration agreement over such third party subject, which are part of one party's group of companies, and at the same time do actively participate in the conclusion, performance or termination of the commercial relationship. French courts argue, that thought the members to the group are a distinct legal persons, the group as a whole represent a single economic reality. In the original Dow Chemicals decision, this did not automatically imply the members of the group are bound by the arbitration agreement, merely that there may be a (rebuttable) presumption, such members might have conceded to arbitration if they were involved in the course of the contract.[42]

39 Notions of the doctrine, and similar attempts, may be traced even in Swiss case law e.g. Decision of Bundesgericht, Switzerland of 16 October 2003, No. 4P.115/2003 [online]. In *www.bger.ch*. Eurospider Information Technology [cit. 2015-07-10]. On the other hand, it is resolutely denied application in front of UK courts as stated and quite regularly cited Peterson farms decision. See Decision of High Court of Justice (Queen's Bench), United Kingdom of 4 February 2004, No. [2004] EWHC 121 (COMM) [online]. In *www.bailii.org*. British and Irish Legal Information Institute [cit. 2015-01-02].

40 See YOUSSEF, Karim. *Consent in Context: Fulfilling the Promise of International Arbitration: Multiparty, Multi-contract, and Non-contract Arbitration* [online]. Minneapolis: West, 2009 [cit. 2015-01-30]. § 6. 15.

41 Interim Award of ICC International Court of Arbitration of 23 September 1982, No. 4131 [online]. In *KluwerArbitration*. Wolters Kluwer [cit.2015-05-17].

42 MAYER, Pierré. Extension of the Arbitration Clause to Non-signatories under French Law. In PERMANENT COURT OF ARBITRATION (ed.). *Multiple Party Actions in International Arbitration*. Oxford, New York: Oxford University Press, 2009, p. 190 - 191.

However, the subsequent case law shifted the doctrine to a quite extreme position. French courts basically set the single economic reality aside, and based the validity of the arbitration clauses on another presumption. It was argued the arbitration clauses are common feature of international commercial contracts, they represent a usage regarding dispute settlement in international trade.[43] As such, any third party (not necessarily a group member) which is involved in life of the main contract might presume there is an arbitration clause inserted, and by being involved they impliedly agreed to it.[44] This is of course a severe shift from the consensual nature of arbitration, as the proceedings stands not on the presumed consent, but a presumed knowledge, which in turn implies consent.

As the result, though the original group of companies doctrine might have offered an interesting way to analyse a more complex setting, with indeed consent analyses as a prime factor in mind, subsequent (d)evolution of case law shifted this prime factor to background, favouring what seems to be a more mechanical, often consent-less, approach.

5 Conclusion

This article presented several challenges international arbitrators may face once presented with the shifting nature of international commercial contracts. Though the formal validity of such changes is indeed an important one to analyse, it seems the modern liberal trends allow for various modifications of the arbitration clause. The material validity of such changes represents a challenge, as there are various doctrines recognized globally, but whose applicability may be severely limited by the applicable lex arbitri.

Undisputedly, in the core of all the theories, there is a valid arbitration agreement, and the arbitration is consensual in its very essence. However, the application of the theories may lead us to a conclusion, that though consensual in the beginning, in the end it may not be quite so. Principles requiring justice and effective resolution of the economic dispute may bound even the parties which manifestly did not sign the arbitration agreement.

43 Decision of Cour d'Appel de Paris, France of 7 December 1994, No. N/A [online]. In *KluwerArbitration*. Wolters Kluwer [cit. 2015-05-31].

44 *Ibid.*

To summarise, it may be still held that the consent is the cornerstone of the arbitration. However, it means nothing more that consent acts as a mere "triggering mechanism". Case law reveals that once such trigger exists, the analysis of respective courts and arbitral practice quite often ventures outside its presupposed consensual boundaries, contemplating and employing principles of fairness and justice.

As the result, even those who have clearly presented the will not to be bound by such an extension mechanism, may be compelled to subordinate to it. Consent of some is therefore just the beginning, definitely not the final frontier.

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THE INTERPRETATION OF CONTRACTS IN ICC ARBITRATION

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Abstract

In international commercial disputes it could be more difficult to determine the real and common will of both parties by reference to a single applicable national law (especially if there was no choice of law). In arbitration there is a larger space for the approach different from the approach of the state courts, because arbitrator's position is different from that of state courts, which are bound to apply the conflict of laws rules. Opposite to that the international arbitrator often does not have lex fori and he can apply a system of rules different from the national law which would be applied according to the conflict of laws rules. Thus, in arbitration another approach (than application the conflict of laws rules of lex fori) can be provided by the UNIDROIT Principles of International Commercial Contracts. In some cases the ICC tribunals referred to the Chapter 4 of the UNIDROIT Principles, which focuses on the interpretation of legal conduct. The aim of this paper is to analyse the ICC approach to the interpretation of contracts between parties (or we can say the interpretation of the intentions of the parties) and the way in which the Chapter 4 of the UNIDROIT Principles is used for that. As anational rule of law, the UNIDROIT Principles are applied in some cases, especially to supplement the governing law or to fill gaps in applied law.

Keywords

ICC Arbitration; the Interpretation; the UNIDROIT Principles.

1 Introduction

The interpretation of contracts is one of the issues, which frequently arises in international arbitration. Indeed, the contract is the basis for all international commercial arbitration; thus, its interpretation is necessary. This

article focuses only on the interpretation of the principal contracts (of the contractual provisions). It does not consider the interpretation of arbitration clauses, which is different.[1]

The term "interpretation of the contract" can also mean the common will of the parties or the intentions of the parties or also the statements or other conduct of the parties.

In international commercial disputes it may seem unfair to subordinate the interpretation to a single applicable national law (there are differences in national laws of states and one of the parties may not know the applicable national law of the other party and it is therefore disadvantaged compared to the other party). Because of this, it is sometimes preferable to apply some instruments of international contract law. The most often applied are the United Nations Convention on Contracts for the International Sale of Goods ("CISG")[2] and non-state instruments – the UNIDROIT Principles on International Commercial Contracts ("UNIDROIT Principles"),[3] which reception has generally been positive,[4] and Principles of European Contract Law ("PECL").[5] All of these instruments contain provisions that regulate the process of the interpretation.[6]

The aim of this paper is to analyse the practice of cases decided under the Rules of Arbitration of the International Chamber of Commerce ("ICC") in using the Chapter 4 of the UNIDROIT Principles for interpretation of contracts. In this field there is a difference between arbitrators and judges. State courts are bound to apply conflict of laws rules which means

1 KARTON, Joshua D. H. International Commercial Arbitrators' Approaches to Contractual Interpretation. *International Business Law Journal / Revue de Droit des Affaires Internationales* [online]. 2012 [cit. 2015-02-15], p. 2.

2 United Nation Convention on Contracts for the International Sale of Goods (Vienna, 1980) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG.html ("CISG")

3 UNIDROIT Principles on International Commercial Contracts 2010 [online]. *International Institute for the Unification of Private Law (UNIDROIT)*. Available from: http://www.unidroit.org/instruments/commercial-contracts/unidroit-principles-2010 ("UNIDROIT Principles").

4 BONELL, Michael Joachim. The UNOIDROIT Principles in Practice – The Experience of The First Two Years. *Uniform Law Review* [online]. 1997 [cit. 2015-03-15], p. 36.

5 Principles of European Contract Law [online]. *Commission on European Contract Law*. Available from: http://www.trans-lex.org/400200/ ("PECL").

6 Art. 8 CISG, Arts. 4.1 – 4.8 UNIDROIT Principles, Arts. 5:101 – 5:107 PECL.

that they have to determine the applicable national law which governs the relationship between contractual parties (the most common method for determining the applicable law is to use conflict of laws rules of *lex fori*). International arbitrators do not have to apply the conflict of laws rules and national law, so they have more possible ways to assess the case. For example the UNIDROIT Principles may serve the purpose.[7] Moreover, the arbitrators are quite free to interpret contracts.[8] Thus, the use of the UNIDROIT Principles could mean a considerable challenge in resolving international disputes, because they contain rules of the interpretation of the contracts which can be applied by arbitrators.

2 Possibilities Regarding the Application of the UNIDROIT Principles in Arbitration

The purpose of the UNIDROIT Principles is to provide general rules for international commercial contracts.[9] It is a non-state system of law which was devised[10] by independent experts and scholars from all over the world and tries to achieve harmonization of the law regarding international commercial contracts.[11]

The UNIDROIT Principles are not binding for states, but they are significant for arbitration, because they reflect the general consensus (similarly to the CISG but with a wider scope).

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7 DERAINS, Yves. The Role of the UNIDROIT Principles in International Commercial Arbitration (1): A European Perspective. *Special Supplement 2002: UNIDROIT Principles of International Commercial Contracts: Reflections on their Use in International Arbitration* [online]. In *Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-02-15], p. 12 – 13; MAYER, Pierre. The Role of the UNIDROIT Principles in ICC Arbitration Practice. *Special Supplement 2002: UNIDROIT Principles of International Commercial Contracts: Reflections on their Use in International Arbitration* [online]. In *Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-02-15], p. 115.

8 CORDERO-MOSS, Giuditta. Interpretation of Contracts in International Commercial Arbitration: Diversity on More Than One Level. *European Review of Private Law*. 2014, Vol. 22, No. 1, p. 18 – 19.

9 UNIDROIT Principles, Preamble.

10 UNIDROIT Principles were first published in 1994.

11 BONELL, Michael Joachim. Towards a Legislative Codification of the UNIDROIT Principles? In ANDERSEN, Camilla B; SCHROETER, Ulrich G. (eds.). *Sharing International Commercial Law across National Boundaries: Festschrift for Albert H. Kritzer on the Occasion of his Eightieth Birthday* [online]. Wildy, Simmonds & Hill Publishing, 2008 [cit. 2015-02-15], p. 62.

The Preamble of the UNIDROIT Principles supposes their application:

1. When the parties have agreed that their contract be governed by them;
2. When the parties have agreed that their contract be governed by general principles of law, the lex mercatoria or the like;
3. When the parties have not chosen any law to govern their contract;
4. To interpret or supplement international uniform law instruments;
5. To interpret or supplement domestic law;
6. May serve as a model for national and international legislators.

Under Art. 21 Rules of Arbitration of the ICC in force as from 1 January 2012 ("2012 ICC Rules"),[12] the UNIDROIT Principles can be applied on the ground of the express or implied choice of the parties as the proper law of the contract (*lex contractus*). For example, when parties referred to "international law" in their contract, the sole arbitrator decided that it should be understood as international rules applicable to international contracts. The arbitrator also deduced that the parties implicitly referred to *lex mercatoria* and the general principles of law and that the UNIDROIT Principles reflect these general principles.[13] On the other hand, the UNIDROIT Principles are not always accepted. In case No. 9419, the ICC tribunal refused the application of the UNIDROIT Principles because there was no connection between them and *lex mercatoria*, they could not constitute applicable supranational law (they could only be used for reference by the parties) because they were not a binding instrument, but rather private codification.[14]

In addition the arbitral tribunal should take account of the provisions of the contract and the relevant trade usages.[15] Thus, even though the parties expressly choose some national law or international convention, arbitrators

12 Rules of Arbitration of the International Chamber of Commerce, in force as from 1 January 2012 [online]. International Chamber of Commerce. Available from: http://www.iccwbo.org/products-and-services/arbitration-and-adr/arbitration/icc-rules-of-arbitration/ ("2012 ICC Rules").

13 Partial award of ICC International Court of Arbitration of January 2003, No. 12111 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

14 Award of ICC International Court of Arbitration of September 1998, No. 9419 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of March 1998, No. 9029 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

15 Art. 21(2) 2012 ICC Rules.

should, apart from this applicable law, also consider trade usages, and as these usages it is possible to use the UNIDROIT Principles (there is no need for previous agreement among parties, but the use of the UNIDROIT Principles cannot be contrary to the default rules incorporated within applicable law).[16] We can find the award according to that not just the UNIDROIT Principles, but also PECL represent the latest codification of international commercial trade usages.[17]

The UNIDROIT Principles are also useful for filling in gaps and supporting the governing law.[18]

In cases where there is no choice of law, arbitrators have to choose which national law or relevant non-state rules to apply. In these cases neutral non-state rules are sometimes preferred where they are deemed appropriate (Art. 21 2012 ICC Rules). When parties did not choose the applicable law to the merits of the dispute, the arbitral tribunal referred to the UNIDROIT Principles (which it recognized as a representation of international trade usages) in order to supplement the provisions of the agreement between parties.[19]

Finally, the UNIDROIT Principles play a considerable role in the interpretation.

3 Interpretation Rules in the UNIDROIT Principles

The interpretation of the contract is regulated in the Chapter 4 of the UNIDROIT Principles. It covers the intentions of the parties,

16 Procedural Order of ICC International Court of Arbitration of 7 October 2004, No. 12949 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of December 1998, No. 9593 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

17 Partial award of ICC International Court of Arbitration of October 2000, No. 10022 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

18 Award of ICC International Court of Arbitration of January 1999, No. 8547 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Interim award of ICC International Court of Arbitration of December 2001, No. 11295 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

19 Award of ICC International Court of Arbitration of December 1998, No. 9887 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of February 1999, No. 9479 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

the interpretation of statements or other conduct of the parties, relevant circumstances which should be taken account, and auxiliary criteria of interpretation.

Adjustment in the UNIDROIT Principles is wider in scope than adjustment in the CISG, which provides only basic rules of interpretation. The UNIDROIT Principles contain provisions serving directly to interpret contracts.[20] Fundamental to the interpretation of the contract is the common intention of the parties. A common will takes precedence over linguistic interpretation, even over the meaning that reasonable persons would give to it. Only when it is not possible to determine the common will, perspective of reasonable person of the same kind as the parties and in the same circumstances will be used.

Art. 4.2 UNIDROIT Principles is essentially the same as the corresponding Article in the CISG. For the interpretation of unilateral acts, a combination of subjective and objective perspectives is used. The subjective intention of a party prevails if the other party knew, or could not have been unaware of that intention. If it is not possible to determine the subjective intent of the party, interpreter accedes to an objective method – the perspective of a reasonable person.

Concurrent regard should be given to all relevant circumstances (Art. 4.3 provides a demonstrative list of these circumstances).

3.1 Auxiliary Criteria of Interpretation

These rules are regulated by Arts. 4.4 – 4.8 UNIDROIT Principles. The first provides that terms used by the parties should be interpreted in the light of the whole contract and according to context, not individually and in the isolation.

One of the most often used rules in ICC arbitration proceedings states that if possible, the contract should be interpreted in such a way that all provisions are effective.[21] There is the presumption that parties would avoid using words to no purpose and that they have an interest in the effect of the contract as whole.

20 Art. 4.1 UNIDROIT Principles.
21 Art. 4.5 UNIDROIT Principles.

Another one is the *contra proferentem* rule (Art. 4.6). According to it, unclear or ambiguous terms will be interpreted to the disadvantage of the party which supplied them. The purpose of this provision is the protection of fair business dealings in international trade. The initiator of an unclear statement or other ambiguous conduct is to be held responsible for it. A party which makes mistakes in its contractual conduct should not profit from them.[22]

Art. 4.7 resolves situations in which a contract was drawn up in two or more language versions that are equally authoritative but diverse in some points, and in which the parties have not determined which version should prevail. In these cases, there is a preference for the interpretation according to the version in which the contract was originally drawn up.

The last interpretation rule is used to fill gaps in a contract in which some questions remain unresolved by the contracting parties. Supplementary terms must be appropriate to the circumstances of the case. The main factors determining what is appropriate are – the intentions of the parties, the nature and purpose of the contract, good faith and fair dealing and reasonableness.[23]

4 Use of the Chapter 4 of the UNIDROIT Principles in ICC Cases

As already mentioned, the first version of the UNIDROIT Principles was published in 1994. Since then, the UNIDROIT Principles have become quite popular in arbitration. According to ICC statistical reports,[24] when parties chose anational rules of law, they had chosen the CISG, the UNIDROIT Principles or INCOTERMS Rules in most cases. And also, in the process of the interpretation the arbitral tribunals use national laws, CISG and the UNIDROIT Principles (especially, when interpreting contracts arbitrators are most inclined to apply general principles of law).[25] The advantage

22 Decision of the Nejvyšší soud, Czech Republic of 3 March 2009, No. 32 Cdo 661/2008 [online]. *Nejvyšší soud* [cit. 2015-10-01].

23 Art. 4.8 UNIDROIT Principles. *Unidroit Principles of International Commercial Contracts 2010* [online]. Rome: UNIDROIT, 2010 [cit. 2015-02-18], p. 146 – 147.

24 ICC statistical reports from 1997 to 2013 (1997 Statistical Report, 1998 Statistical Report, 1999 Statistical Report, 2000 Statistical Report, 2001 Statistical Report, 2002 Statistical Report, 2003 Statistical Report, 2004 Statistical Report, 2005 Statistical Report, 2006 Statistical Report, 2007 Statistical Report, 2008 Statistical Report, 2009 Statistical Report, 2010 Statistical Report, 2011 Statistical Report, 2012 Statistical Report, 2013 Statistical Report) [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

25 KARTON, Joshua D. H. International Commercial Arbitrators' Approaches to Contractual Interpretation. *International Business Law Journal / Revue de Droit des Affaires Internationales* [online]. 2012 [cit. 2015-03-12], p. 3, 15.

of the UNIDROIT Principles, unlike national laws, is that they are neutral system of rules, which enjoys general acceptance. The UNIDROIT Principles are among others inspired by the CISG. They contain similar rules for the interpretation of statements or other conduct of the parties.[26] Moreover they also expressly regulate the interpretation of the contract[27] (not just the interpretation of the individual intent) and incorporate auxiliary criteria of the interpretation.[28] And the UNIDROIT Principles can serve for interpretation of any sort of commercial contract (not just for interpretation of contracts for the international sale of goods)[29]. Thus, their scope is wider.

In ICC arbitration, the UNIDROIT Principles are not applied more often than national laws, but the aim of this article is to analyze the ways they are applied in cases in which they were used. But, not all ICC awards are available. Twelve[30] of the available awards range from 1996 to 2004 (recent ICC awards are not available) consider or refer to the rules of interpretation contained in the Chapter 4 of the UNIDROIT Principles.

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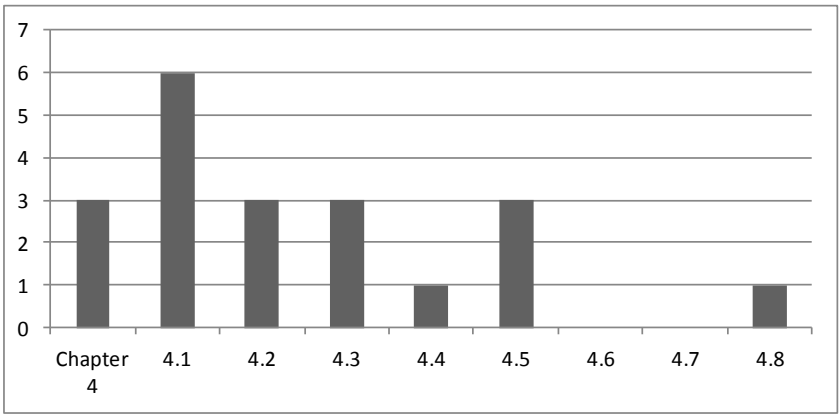
26 Art. 8 CISG, Art. 4.2 and 4.3 UNIDROIT Principles.

27 Art. 4.1 UNIDROIT Principles.

28 Art. 4.4 – 4.8 UNIDROIT Principles.

29 Art. 1(1) CISG; UNIDROIT Principles, Preamble.

30 Award of ICC International Court of Arbitration of December 1996, No. 8331 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of September 1998, No. 8908 [online]. In *Dispute Resolution Library;* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of March 1998, No. 9117 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Partial award of ICC International Court of Arbitration of February 1999, No. 7110 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of January 1999, No. 8547 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Preliminary award of ICC International Court of Arbitration of August 1999, No. 9759 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of August 2000, No. 9651 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of July 2000, No. 9797 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of March 2000, No. 9875 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of October 2000, No. 10335 [online]. In *Dispute Resolution Library,* ICC International Chamber of Commerce [cit. 2015-10-01]; Interim award of ICC International Court of Arbitration of December 2001, No. 11295 [online]. In *Dispute Resolution Library;* International Chamber of Commerce [cit. 2015-10-01]; Procedural Order of ICC International Court of Arbitration of 7 October 2004, No. 12949 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].



The graph illustrates how often the arbitral tribunals applied particular rules of the interpretation. In three of the analyzed cases arbitrators referred to the Chapter 4 generally. The most frequent reference was to Art. 4.1 – common intention of the parties in the process of the interpretation of the contract. This demonstrates that the explicit rule for the interpretation of the contract is useful.

Auxiliary criteria of interpretation (Arts. 4.4 – 4.8) were not used so often (except for the Art. 4.5, which provides that unclear contract terms should be interpreted so as to give effect to all the terms).

Until 1998 only in one published case the Chapter 4 was applied. The UNIDROIT Principles were used by the arbitral tribunal, because the parties agreed that if the tribunal found it necessary and appropriate the UNIDROIT Principles should be applied.[31]

A major change occurred issuing the new ICC Rules in January 1, 1998. The rule for determination of the applicable law changed. Art. 17 (Art. 21 2012 ICC Rules) provided: *"In the absence of any agreement between parties, the Arbitral Tribunal shall apply the rules of law which it determines to be appropriate."* This change meant the termination of using of the conflict of laws method and instead of that referred to appropriate rules of law.

31 Award of ICC International Court of Arbitration of December 1996, No. 8331 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

Thus, in absence of the express choice of law the tribunal applied the UNIDROIT Principles in a few cases. When the parties inserted the term natural justice into their contract the tribunal refused national laws and applied neutral general legal rules and principles which enjoyed wide international consensus. And according to the tribunal these principles and rules were reflected by the UNIDROIT Principles. So the contract between the parties was interpreted in accordance with the Chapter 4.[32] Similarly, in case No. 9875 (the interpretation was the main problem of this case) the arbitral tribunal found *lex mercatoria* as the most appropriate rules of law and as *lex mercatoria* the tribunal considered inter alia the UNIDROIT Principles.[33]

The interpretation rules of the UNIDROIT Principles were also applied to support established national law or CISG, because *"the rules relating to interpretation and good faith contained in the UNIDROIT Principles (in particular, articles 1.7 and from 4.1 to 4.8), which are in all events a useful reference framework for applying and judging a contract of an international nature, also confirm what has been said"*.[34]

Moreover, even though the applicable law was chosen by the parties the tribunals also applied the Chapter 4 of the UNIDROIT Principles in some cases to fill the gaps[35] in the governing law or to support it. For example, when the applicable law referred to the common intent of the parties the arbitral tribunal pointed out that the Art. 4.1 UNIDROIT Principles also contained this rule.[36] Through the UNIDROIT Principles arbitrators demonstrate that the applicable national law is evolving in the same direction

32 Partial award of ICC International Court of Arbitration of February 1999, No. 7110 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

33 Award of ICC International Court of Arbitration of March 2000, No. 9875 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

34 Award of ICC International Court of Arbitration of September 1998, No. 8908 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

35 Award of ICC International Court of Arbitration of January 1999, No. 8547 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Interim award of ICC International Court of Arbitration of December 2001, No. 11295 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

36 Award of ICC International Court of Arbitration of August 2000, No. 9651 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01]; Award of ICC International Court of Arbitration of October 2000, No. 10335 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

as the international commercial law and is in accordance with generally accepted standards.[37] It is supporting to refer to the UNIDROIT Principles, because *"they are said to reflect a world-wide consensus in most of the basic matters of contract law"* [38].

The role of the UNIDROIT Principles was confirmed by the ICC procedural order in 2004.[39] This decision should serve as guidance on the applicability of the CISG and the UNIDROIT Principles. According to that the UNIDROIT Principles can be taken into consideration also without prior agreement of the parties (it just cannot be contrary to the default rules incorporated within applicable national law). And in the same case it was stressed that the UNIDROIT Principles are useful for the interpretation of commercial contracts.

5 Conclusion

The international commercial arbitration provides quite wide scope for the autonomy of the parties (arbitration is based on the will of the parties) and arbitrators (they are quite free to interpret contracts). For the interpretation of the contract or the statements or other conduct of the parties it is possible to apply the UNIDROIT Principles which reception has generally been positive. The UNIDROIT Principles represent a neutral codification of international contract law. The Chapter 4 is one of the most applied in ICC awards in which the UNIDROIT Principles were used. It serves as a means of interpretation of the international contracts.

This paper focused on the application of the Chapter 4 of the UNIDROIT Principles in ICC cases. However, not all ICC awards are available, so it cannot be concluded that the UNIDROIT Principles have become quite popular in international arbitration. They express generally accepted rules and

37 MARRELLA, Fabrizio; GÉLINAS, Fabien. The UNIDROIT Principles of International Commercial Contracts in ICC Arbitration – Introduction and Preliminary Assessment. *ICC International Court of Arbitration Bulletin* [online]. 1999, Vol. 10, No. 2 [cit. 2015-03-15], p. 31 – 32.

38 Award of ICC International Court of Arbitration of March 1998, No. 9117 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

39 Procedural Order of ICC International Court of Arbitration of 7 October 2004, No. 12949 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-10-01].

principles. The change of the ICC Rules in 1998 also contributed to their more frequent use (there is a wider scope for the application of the UNIDROIT Principles because arbitrators are allowed to apply the proper law, not just some national law).

The UNIDROIT Principles are applied not only on the basis of the will of the parties but also as the part of *lex mercatoria* or as the general principles of law, international trade usages and natural justice. And moreover they may be applied also without the agreement of the parties. But still, the contracts with no choice of applicable law are not interpreted as the will of the parties to reject any national law in favour of the UNIDROIT Principles. There is a tendency to resort to them but the silence of the parties does not mean the choice of the UNIDROIT Principles. Thus, their application depends on the particular cases and arbitrators.

In ICC cases the Chapter 4 of the UNIDROIT Principles is the most often applied to support or supplement the governing law.

Still dominate cases in which the UNIDROIT Principles were not used but there is some tendency to use them (although some arbitrators refusing the m) from the year 1998. This conclusion is based on the available ICC awards but unfortunately many other awards are not available (especially more recent ICC awards) and the awards in which the Chapter 4 of the UNIDROIT Principles were used are published only to 2004. Thus, this source is incomplete. However, it can be assumed that the application of the Chapter 4 of the UNIDROIT Principles in unpublished cases is similar as in available awards (until 2004).

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EA ORDER – A POWERFUL TOOL OR JUST A PIECE OF PAPER?

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Abstract

The ICC Rules underwent several changes with their 2012 amendments. One of them are the emergency arbitrator provisions which provide for a whole new type of interim measure – the EA order. As it is a new way of obtaining interim measure, its exact legal status remains unclear, especially with regards to its possible enforcement under the New York Convention or national legislation. Therefore, this paper will firstly address the issue whether the EA order is – as suggested by several authorities – a specific type of contract, or can be considered a judicial decision. Secondly, the paper will deal with enforcement of the EA order and present solutions which have been adopted in order to make it more straightforward.

Keywords

Emergency Arbitrator; 2012 ICC Rules; EA Order; Provisional Measure.

1 Emergency Arbitrator Provisions as a Part of 2012 Amendments

The 2012 amendments of the Rules of Arbitration of the International Chamber of Commerce ("ICC Rules")[1] contain several changes that should reflect challenges for contemporary international arbitration. They mainly show recognition of the need for methods designed to deal with

[1] Rules of Arbitration of the International Chamber of Commerce, in force as from 1 January 2012 [online]. *International Chamber of Commerce*. Available from http://www.iccwbo.org/Products-and-Services/Arbitration-and-ADR/Arbitration/Rules-of-arbitration/ICC-Rules-of-Arbitration/ ("ICC Rules").

the complexity of international arbitration while simultaneously seeking to increase efficiency and decrease the cost of the dispute resolution process.[2] Apart from provisions aimed at improved case management and multiparty situations, the ICC Rules now contain the emergency arbitrator provisions ("EA provisions") which were not embodied in the 1998 version of the rules. It is worth mentioning that similar provisions can be found in case of other arbitral institutions, such as Arbitration Institute of the Stockholm Chamber of Commerce ("SCC"), Swiss Chambers of Commerce Association for Arbitration and Mediation or American Arbitration Association.

The purpose of the EA provisions is to allow a party to seek for interim measure before the Tribunal is constituted. The 1998 version of the ICC Rules did not provide for such a possibility since the only body able to grant interim measure within the ICC arbitration was the tribunal itself. This was considered one of the weakest points of ICC Rules as it left the parties no other option than to request interim measure granted by national courts if they needed interim measure to be granted prior to the constitution of the arbitral tribunal.[3]

The only possibility of obtaining urgent provisional measure within the ICC was the Pre-Arbitral Referee procedure. However, as it was a separate instrument outside the ICC Rules, the parties needed to agree on application of this particular instrument – they needed to opt in the Pre-Arbitral Referee Rules apart from the arbitration agreement itself.[4] This was possibly the most significant reason why only 14 applications were filed with ICC since 1990 when this instrument came into force.[5]

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2 POWER, Richard. Briefing Note on ICC Rule Changes [online]. In *Kluwer Arbitration Blog*. Kluwer Law International [cit. 2015-04-27].

3 VOSER, Nathalie; BOOG Christopher. ICC Emergency Arbitrator Proceedings: An Overview. *ICC International Court of Arbitration Bulletin* [online]. 2011, Vol. 22, No. 2 [cit. 2015-04-29], p. 3.

4 GHAFFARI Amir; WALTERS Emmylou. The Emergency Arbitrator: The Dawn of a New Age? *Arbitration International* [online]. 2014, Vol. 30, No. 1 [cit. 2015-04-29], p. 155.

5 CARLEVARIS Andrea; FERIS José Ricardo. Running in the ICC Emergency Arbitrator Rules: The First Ten Cases. *ICC International Court of Arbitration Bulletin* [online]. 2014, Vol. 25, No. 1. [cit. 2015-04-29], p. 2.

2 Emergency Arbitrator's Order – Contract or a Decision?

Both Art. 29(2) ICC Rules and Art. 6(1) Appendix V state that under the ICC Rules, the emergency arbitrator's decision shall take the form of an order. As explained by *Voser*, the main purpose of this denomination is to distinguish the decision of the emergency arbitrator from an award issued by an arbitral tribunal. It also erases any possible doubts regarding the need for scrutiny by the International Court of Arbitration ("the Court") of any decision rendered by an emergency arbitrator.[6]

This is similar to the aforementioned Pre-Arbitral Referee procedure. Similarly to contemporary ICC Rules, the ICC Pre-Arbitral Referee Rules did not (and still do not) contain any provision which would determine the exact legal nature of the order issued as an outcome of the procedure. Therefore, this issue needed to be determined via case law. Such procedure took place and the nature of the decision was a point of contention before the Court of Appeal in Paris in 2003.

In the Société Nationale des Pétroles du Congo and République du Congo v TotalFinaElf E & P Congo (ICC Pre-Arbitral Referee Procedure No. 11904/DB), the parties entered into the contract where TEP Congo would refinance debts owed by the Republic of Congo in exchange for a certain quantity of crude oil. The agreement contained a specific provision regarding provisional and protective measure, which referred to the ICC Pre-Arbitral Referee procedure. In accordance with this provision, TEP requested protective measure which would, in part, oblige the Republic of Congo to respect its contractual obligations under the agreement.[7] After considering circumstances of the case, prof. Pierre Tercier, who was appointed as a referee in this case, issued the order in favour of TEP. As a response, Republic of Congo initiated the annulment proceeding before the Paris Court of Appeal arguing that the order does amount to an award and is therefore capable of being set aside in accordance with Art. 1504 of the French Code of Civil Procedure.

6 VOSER, Nathalie. Overview of the Most Important Changes in the Revised ICC Arbitration Rules. *ASA Bulletin* [online]. 2011, Vol. 29 [cit. 2015-04-29], p. 818.

7 GAILLARD, Emmanuel. First Court Decision on Pre-Arbitral Referee [online]. *New York Law Journal*. ALM [cit. 2015-05-01], p. 1.

In its decision dated 29 April 2003, the court ruled that such a motion is inadmissible. The court held that it must firstly determine, whether the referee has the power to act as an arbitrator. Here, it pointed out to the foreword to the rules which in the relevant passage state that the "referee" is empowered to order provisional measure needed as a matter of urgency. Taking this into account, the court emphasized that the word "arbitration" or any similar word has been carefully avoided by the drafters. The court also held that the binding nature of the order derived solely from the parties' agreement. On this basis, the court held that the order had no more binding effect than that of a contractual provision and was deprived of the binding effect of a decision being *res iudicata.* [8]

In particular, the court ruled that: "*Considering that the order of 6 February 2002, rendered according to a contractual mechanism founded on the cooperation of the parties, has, despite its designation, a contractual nature in the sense that it derives its authority from the agreement, and that, consequently, an appeal for annulment filed against an award is inadmissible"*[9]

Conclusion that the order rendered within the ICC Pre-Arbitral Referee procedure is of contractual nature was accepted in the scholarly writings.[10] Nevertheless, some concerns were raised by *Gaillard* and *Pinsolle* as they wrote: *"Arbitration is also contractual in nature, but nevertheless undoubtedly leads to a jurisdictional decision. In our view, the referee does render a jurisdictional decision unlike, for example, an expert."*[11] Personally, I hold the second opinion correct. There is no doubt that the "opt-in" of the Pre-Arbitral Rules

8 GAILLARD, Emmanuel; PINSOLLE Philippe. The ICC Pre-Arbitral Referee: First Practical Experience. *Arbitration International* [online]. 2004, Vol. 20, No. 1 [cit. 2015-04-29], p. 22.

9 Judgement of Cour d'Appel Paris, France of 29 April 2003, Case No. 2002/05147. Available as an Appendix 2 to GAILLARD Emmanuel; PINSOLLE, Philippe. The ICC Pre-Arbitral Referee: First Practical Experience. *Arbitration International* [online]. 2004, Vol. 20, No. 1 [cit. 2015-04-29], p. 33 - 37.

10 E.g. BERGER, Klaus Peter. Pre-Arbitral Referees: Arbitrators, Quasi-Arbitrators, Hybrids or Creatures of Contract Law? [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-05-02], p. 6 or VOSER, Nathalie; BOOG Christopher. ICC Emergency Arbitrator Proceedings: An Overview. *ICC International Court of Arbitration Bulletin* [online]. 2011, Vol. 22, No. 2 [cit. 2015-04-29], p. 4 - 5.

11 GAILLARD Emmanuel; PINSOLLE Philippe. The ICC Pre-Arbitral Referee: First Practical Experience. *Arbitration International* [online]. 2004, Vol. 20, No. 1 [cit. 2015-04-29], p. 22.

is a form of a contract. On the other hand, the parties are unable to influence the referee's decision once the request has been transmitted to him. In other words, the parties can contractually agree on the Pre-Arbitral procedure. Nevertheless, they cannot contractually agree on the actual content of the order.

In order to clarify this uncertainty, the Drafting Sub-Committee responsible for drafting of the 2012 amendments wished the emergency arbitrator's decision to be of a judicial nature, i. e. to be as similar as possible to an interim measure granted by an arbitral tribunal.[12] Despite this intent, no provision that would support this result can be found within the ICC Rules. Does that mean that the emergency arbitrator's order ("EA order") is a mere contract as well? Some authors still think so.[13]

Nevertheless, both instruments are not completely identical. Reading carefully, there are several distinctions supporting the view that ICC wanted to avoid problematic parts mentioned in the Paris Court of Appeal's decision and make the EA orders of judicial nature.

The first major distinction is that the order is issued by an "emergency arbitrator", not a "referee". Although the ICC Rules label him as an arbitrator, justification of such a label is questioned in the scholarly writings. For example *Yesilimak* holds the view that emergency arbitrator can be considered an arbitrator, even if he does not finally resolve the dispute.[14] It is because he resolves the request for the interim measure in a judicial manner. To the contrary, *Baigel* argues that even this does not make him an arbitrator since he can take more pragmatic considerations into account which do not necessarily have to be of judicial nature.[15] As to the second distinction, the emergency arbitrator provisions are now part of the ICC Rules.

12 VOSER, Nathalie; BOOG Christopher. ICC Emergency Arbitrator Proceedings: An Overview. *ICC International Court of Arbitration Bulletin* [online]. 2011, Vol. 22, No. 2 [cit. 2015-04-29], p. 5.

13 E.g. BAIGEL, Baruch. The Emergency Arbitrator Procedure under the 2012 ICC Rules: A Juridical Analysis. *Journal of International Arbitration* [online]. 2014, Vol. 31, No. 1 [cit. 2015-04-29], p. 15.

14 YESILIMAK, Ali. *Provisional Measures in International Commercial Arbitration*. Hague: Kluwer Law International, 2005. p. 123.

15 BAIGEL, Baruch. The Emergency Arbitrator Procedure under the 2012 ICC Rules: A Juridical Analysis. *Journal of International Arbitration* [online]. 2014, Vol. 31, No. 1 [cit. 2015-04-29], p. 15.

From the perspective of the whole arbitral proceeding's uniformity, this can be supportive for the result that the emergency arbitrator procedure can be considered a possible "pre-stage" of the arbitration itself. Finally, contrary to the ICC Pre-Arbitral Referee procedure, emergency arbitrator procedure is based on an opt-out principle. Once the parties conclude a valid arbitration agreement in favour of arbitration under ICC Rules,[16] the EA provisions automatically apply, unless otherwise agreed by the parties.

Taking these distinctions into account, conclusions of the Paris Court of Appeal's decision seem rather inapplicable to the emergency arbitrator proceedings. Despite the fact that any clear case-law confirmation is missing, the EA order should be treated as a judicial decision. For example Calvo Gorrel derives judicial nature of emergency measure from the fact that they are provided by the ICC Rules themselves.[17] Furthermore, *Voser* and *Boog* argue that the EA order has the same legal nature as an interim measure ordered by the arbitral tribunal pursuant to Article 28 of the ICC Rules.[18]

This approach can be supported by comparison with another procedural rules providing for emergency measure. As the purpose of the emergency arbitrator procedure is similar in case of other arbitral institutions, the legal nature of emergency arbitrator's decision should be similar as well, regardless of the particular arbitral institution. For example, the emergency arbitrator within the Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce ("SCC Rules")[19] has the same authority to order

16 The agreement must be concluded after 1 January 2012. However, in one of the very first cases where EA provisions were applied, the arbitration agreement concluded before 1 January 2012 referred to the ICC Rules "in force at the time of commencement of the arbitration". The President decided that by virtue of this, the parties can be considered to have accepted the applicability of any future amendments, even if they were unaware of them at the time the arbitration agreement was signed. As a consequence, 2012 amendments including the EA provisions applied and the President allowed the matter to proceed.

17 CALVO GORREL, Karin. The 2012 ICC Rules of Arbitration – An Accelerated Procedure and Substantial Changes. *Journal of International Arbitration* [online]. 2012, Vol. 29, No. 3 [cit. 2015-04-29], p. 323.

18 VOSER, Nathalie; BOOG Christopher. ICC Emergency Arbitrator Proceedings: An Overview. *ICC International Court of Arbitration Bulletin* [online]. 2011, Vol. 22, No. 2 [cit. 2015-04-29], p. 7.

19 Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce [online]. *Arbitration Institute of the Stockholm Chamber of Commerce*. Available from: http://www.sccinstitute.com/media/40120/arbitrationrules_eng_webbversion.pdf ("SCC Rules").

interim measure as an ordinary arbitral tribunal under the SCC Rules.[20] Hence, even the decisions of emergency arbitrator should have the same legal nature, i. e. judicial nature. Similarly like the emergency arbitrator, the arbitral tribunal derives its power to grant provisional measure from parties' agreement. Furthermore, it can derive (and often will) its power from the same arbitration agreement. At this point, considerations that orders granted by arbitral tribunals are of judicial nature whereas the ones granted by emergency arbitrators are not, would lead to an absurd result.

3 Enforcement of an EA Order – A Shark Without Teeth?

Once the applicant reaches his goal and the EA order is issued, an obvious question arises: What if respondent is not willing to comply with it? In case of final awards, enforcement in respondent's seat of business (or any other place where respondent has enough assets) is a typical solution of this situation.[21] However, the EA order does not constitute a final decision and possibilities of its enforcement are therefore limited. These problems also persist if the emergency arbitrator renders the emergency measure in its second basic form – in form of an award.[22]

The choice, which type of the measure will be rendered, lies in the emergency arbitrator's discretion. This discretion is obviously possible only if the arbitral institution's procedural rules permit him to do so. This is the case of e. g. SCC, Singapore International Arbitration Centre ("SIAC") or Hong Kong International Arbitration Centre ("HKIAC") where the rules provide for both types of emergency measure - order or award. However, ICC took (one can say that it needed to take) a different approach since Art. 29(2) ICC Rules states that the emergency arbitrator's decision always takes form

20 Art. 1(2) Appendix II to the SCC Rules; confirmed by OLDENSTAM, Robin et. al. *Concise Guide to Arbitration in Sweden*. Mölnlycke: Elanders Sverige AB, 2014. p. 55.

21 Not only may the applicant enforce the EA order, Art. 29(4) of the ICC Rules also grants the arbitral tribunal power to decide any claims arising out of or in connection with the compliance or non-compliance with the EA order. This will be for example the case, where respondent will have to refrain from disposing with certain commodity, but breaches this obligation, giving rise to potential damage claims. This can also work *vice versa* – if respondent is refrained from disposing with the commodity and the order is later lifted by the arbitral tribunal, respondent may be compensated its lost profit.

22 BORN, Gary. *International Commercial Arbitration*. Hague: Kluwer Law International, 2009. p. 1950.

of an order. Hence, the emergency arbitrator under ICC Rules is not entitled to issue an emergency measure in form of an award. The reason for this limitation is simple. Pursuant to Art. 33 ICC Rules, every award must be scrutinized by the Court. This affects interim measure in form of an award as well as the Court requires them to be subject to its scrutiny for quality-control purposes even if they are not characterized as awards under the law at the place of arbitration.[23]

Such a requirement would be an obstacle for the emergency arbitrator proceeding. It is necessary to emphasise that the purpose of this proceeding is to give the parties opportunity to obtain an interim measure in case their situation is so urgent that it cannot await constitution of the arbitral tribunal. As the scrutiny process normally takes two to three weeks,[24] the idea of scrutiny is mutually incompatible with the emergency arbitration.

It should be noted that even if the emergency arbitrators have the possibility to issue an emergency measure in form of on award, enforcement of such a measure is an uncertain question. As long as there is no international treaty which addresses the issue of the interim measure's enforcement,[25] parties seeking for enforcement of the interim measure will have to choose another way. It may seem that due to its label, such a measure should be enforceable under the New York Convention,[26] the opposite is true. Although the New York Convention itself does not define, what is to be considered an arbitral award, [27] the prevailing view is that such an award must be final and binding in order to be enforceable under the New York Convention.[28] This

23 FRY. Jason; GREENBERG, Simon; MAZZA, Francesca. The Secretariat's Guide to ICC Arbitration [online]. In *Dispute Resolution Library*. International Chamber of Commerce [cit. 2015-05-03], para. 3-1188.

24 FRY. Jason; GREENBERG, Simon; MAZZA, Francesca. The Secretariat's Guide to ICC Arbitration [online]. In *Dispute Resolution Library*. International Chamber of Commerce [cit. 2015-05-03], para. 3-1217.

25 YESILIMAK, Ali. *Provisional Measures in International Commercial Arbitration*. Hague: Kluwer Law International, 2005. p. 259.

26 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf.

27 VAN DEN BERG, Albert Jan. *The New York Arbitration Convention of 1958*. Hague: T. M. C. Asser Institute, 1981. p. 44.

28 LEW, Julian; MISTELIS, Loukas; KRÖLL, Stefan. *Comparative International Commercial Arbitration*. Hague: Kluwer Law International, 2003. p. 635.

approach was confirmed by the Supreme Court of Queensland in 1993 in the Resort Condominiums vs. Ray Bolwell. After being granted interim measure in the United States, claimant sought its enforcement in Australia.

The court, after considering the nature of the measure stated that: "*An interim award determines at least some of the matters in issue between the parties. The award which may be enforced must be an award which is final and binding on the parties. An interlocutory order which may be rescinded, suspended, varied or reopened by the tribunal which pronounced it, is not "final" and binding on the parties.*"[29]

The issue whether an EA order is enforceable – and if yes, how - is one heavily discussed in scholarly writings. The very first step must be clarification of its legal nature. Taking the abovementioned decision into account, it is almost out of the question that such a measure will be enforceable under the New York Convention. Not only does it not resolve a dispute between the parties (in order to be final and binding), it also is not named "award". For these reasons, it is unanimously held that the parties do not have possibility to enforce the EA order under the New York Convention.[30]

Therefore, the only possibility for enforcement is to use legislation providing for enforcement of interim measures granted by the arbitral tribunal itself. Even this way raises some questions. First and foremost, the national legislation must permit enforcement of the interim measures. In general, those jurisdictions which based their legislation on the UNCITRAL Model Law[31] can have a provision arising from Art. 17H which concerns this issue:

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29 Decision of Supreme Court of Queensland, Australia of 29 October 1993, No. 118 ALR 655. Relevant excerpt taken from KRONKE Herbert; NACIMIENTO, Patricia et. al. *Recognition and Enforcement of Foreign Arbitral Awards: A Global Commentary on the New York Convention*. Kluwer Law International, 2010. p. 156 - 157.

30 BAIGLER, Baruch. The Emergency Arbitrator Procedure under the 2012 ICC Rules: A Juridical Analysis. *Journal of International Arbitration* [online]. 2014, Vol. 31, No. 1 [cit. 2015-04-29], p. 17.

31 UNCITRAL Model Law on International Commercial Arbitration 1985 with amendments as adopted in 2006 [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf ("UNCITRAL Model Law"). For jurisdiction adpoted UNCITRAL Model Law see: *Status. UNCITRAL Model Law on International Commercial Arbitration (1985), with amendments as adopted in 2006* [online]. United Nations Commission on International Trade Law (UNCITRAL) [cit. 2015-05-04].

"An interim measure issued by an arbitral tribunal shall be recognized as binding and, unless otherwise provided by the arbitral tribunal, enforced upon application to the competent court, irrespective of the country in which it was issued, subject to the provisions of article 17 I."

A practical example can be found in Sec. 593(3)[32] Austrian Code of Civil Procedure[33] which enables enforcement of interim measures within the territory of Austria whilst its applicability on international arbitration explicitly results from Sec. 577(2) of the same code.

Reading these paragraphs carefully, one could ask whether the said paragraph regards the measures granted by an emergency arbitrator. Obviously, emergency arbitrator is not (and even cannot be[34]) a member of the arbitral tribunal. Nevertheless, it should be kept in mind that the Art. 17H UNICTRAL Model Law was adopted in 2006, i. e. at the time where the emergency arbitrator procedure was rather unknown to the field of international arbitration.[35] Consequently, the UNCITRAL Model Law even could not address this very particular issue. This opens the possibility to interpret Art. 17H and legislation arising from it extensively, i. e. in a way that even emergency measures fall within its scope, even though they are not granted by the arbitral tribunal *stricto sensu*. As suggested by *Voser* and *Boog,* the order should have the same legal nature as an interim measure granted by the arbitral tribunal itself.[36]

32 Upon request of a party the District Court ("Bezirksgericht") in whose district the opponent of the party at risk has its seat, domicile or habitual residence within Austria at the time of the first filing of the request, otherwise the District Court ("Bezirksgericht") in whose district the enforcement of the interim or protective measure shall be carried out, shall enforce such measure. Where the measure provides for a means of protection unknown to Austrian law, the court may, upon request and after hearing the other party, enforce such measure of protection under Austrian law which comes closest to the measure ordered by the arbitral tribunal. In this case the court may also, upon request, reformulate the measure ordered by the arbitral tribunal in order to safeguard the realization of its purpose.

33 AUSTRIA. Act No. 113/1895 RGBl., Code of Civil Procedure. Available from: http://www.viac.eu/images/ZPO_Schiedsrecht_2014_en_im_VIAC_Layout.pdf

34 E.g. Art. 2(6) Appendix V to the 2012 ICC Rules prohibits emergency arbitrator's participation in any arbitration relating to the dispute that gave rise to the Application. Same rule can be found in Art. 4(4) Appendix II to the SCC Rules.

35 UNCITRAL 2012 Digest of Case Law on the Model Law on International Commercial Arbitration [online]. *United Nations Commission on International Trade Law (UNCITRAL)* [cit. 2015-01-09], p. 93.

36 VOSER, Nathalie; BOOG Christopher. ICC Emergency Arbitrator Proceedings: An Overview. *ICC International Court of Arbitration Bulletin* [online]. 2011, Vol. 22, No. 2 [cit. 2015-04-29], p. 7.

In particular, the courts should adopt a "substance over form" approach and not to distinguish between emergency measures granted by emergency arbitrators and interim measures granted by the tribunal itself. What is decisive is that they serve the same purpose.

Possibility of this approach can be illustrated on two examples. In April 2012, the Parliament of Singapore passed amendments to the International Arbitration Act ("IAA")[37] which reacts to the recent developments in international arbitration, including the emergency arbitrator procedure.

In order to prevent ambiguities concerning the emergency arbitrator's status, Sec. 2(1) IAA regulating interpretation of the IAA was amended in so far it states: "*In this Part, unless the context otherwise requires - "arbitral tribunal" means a sole arbitrator or a panel of arbitrators or a permanent arbitral institution, and includes an emergency arbitrator appointed pursuant to the rules of arbitration agreed to or adopted by the parties including the rules of arbitration of an institution or organization."*

A sole inclusion of emergency arbitrator in the definition of the arbitral tribunal would be useless if the same act would prohibit enforcement of interim measures in Singapore. This is not the case since Sec. 12(6) IAA provides: "*All orders or directions made or given by an arbitral tribunal in the course of an arbitration shall, by leave of the High Court or a Judge thereof, be enforceable in the same manner as if they were orders made by a court and, where leave is so given, judgment may be entered in terms of the order or direction."*

Taking this into account, a party wishing to enforce an emergency measure in Singapore will be given such opportunity as the national legislation permits it and the courts will treat the emergency measures as interim measures granted by the arbitral tribunal.

Another way of reaching the same goal was adopted by Hong Kong. In November 2013, the Arbitration Amendment Bill 2013 came into force

37 SINGAPORE. Act 23 of 1994. International Arbitration Act (Chapter 143 A). Available from: http://statutes.agc.gov.sg/aol/download/0/0/pdf/binaryFile/pdfFile.pdf?CompId:dd9f0294-66ec-4d80-ac95-b40c1be85915

and added a provision providing for enforcement of the emergency measures[38] into the Arbitration Ordinance.[39]

Unlike in Singapore, Hong Kong adopted particular provision aimed solely at emergency measures, namely Sec. 22 B which stipulates: "*Any emergency relief granted, whether in or outside Hong Kong, by an emergency arbitrator under the relevant arbitration rules is enforceable in the same manner as an order or direction of the Court that has the same effect, but only with the leave of the Court.*"

At first sight, it seems that both these ways will work in the arbitral practice. However, for the sake of clarity, adopting a particular provision for emergency measures like in Hong Kong seems more appropriate. If both of these ways bring the desirable goal, these cogitations will be more academic than practical.

4 Final Remarks

Bearing the inherent pro-arbitral approach in mind, treating EA orders like interim measures granted by arbitral tribunals seems reasonable. Without the possibility of its enforcement, a mere issuance of an EA order could be a Pyrrhic victory as even the results of non-compliance with it could be still favourable to the party contravening the EA order. Nevertheless, these problematic parts could be easily solved by means of modification of both rules of arbitral institutions and national legislation. Without this, the parties wishing to obtain an EA order are put in peril whether they will be able to enforce it in order to secure their potential claim. Even more so, in the situation where there is no case law which would at least partially clarify this issue.

From my personal perspective, the emergency arbitrator procedure is a good idea which can support the arbitration's position as a primary method of commercial dispute resolution. However, with the persisting questions regarding it, it is necessary to give it a bit more consideration so it is more foreseeable for the parties. Given the fact that request for emergency measure is not

38 D'AGOSTINO, Justin; FREEHILLS, Herbert Smith. Hong Kong tables amendments to arbitration law [online]. In *Kluwer Arbitration Blog*. Kluwer Law International [2015-05-01].

39 HONG KONG. Chapter 609 Arbitration Ordinance. Available from: http://www.legislation.gov.hk/blis_pdf.nsf/6799165D2FEE3FA94825755E0033E532/C05151C760F783AD482577D900541075/$FILE/CAP_609_e_b5.pdf

a cheap business, the parties deserve an instrument which will protect their needs, if necessary. Otherwise, the whole meaning of emergency arbitration would be frustrated. *Cui bono?*

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PRE-CONTRACTUAL LIABILITY AND INTERNATIONAL COMMERCIAL ARBITRATION

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Abstract

Pre-contractual liability (culpa in contrahendo) is a challenging and demanding institute of law by itself. It is not recognized in every legal order in the world and the construction of it can vary across nations. This situation can become even more complicated, when we start to think about pre-contractual liability in connection to international commercial arbitration. Is it even possible to solve the problem of existence of the pre-contractual liability in arbitration? In case of positive answer, what is subsequently the applicable law? The aim of this paper is to find the answers to these questions with the help of ICC awards database and available literature.

Keywords

Applicable Law; International Commercial Arbitration; Pre-contractual Liability.

1 Introduction

Pre-contractual liability (*culpa in contrahendo*) is really a challenging institute of law - especially in the area of Private International Law. One may question why. The reason is that it is possible to find legal orders recognizing this institute as well as others which do not even know what it is.[1] In the situation where a decision on pre-contractual liability needs to be recognized in another state, which does not legally know this institute, that could cause

1 CARDENAS, Jonathan. Deal Jumping in Cross-Border Merger & Acquisition Negotiations: A Comparative Analysis of Pre-Contractual Liability under French, German, United Kingdom and United States Law. *New York University Journal of Law and Business* [online]. 2013, Vol. 9, No. 3 [cit. 2015-03-08], p. 945 - 946.

a problem. It is a tricky situation for everyone who won his or her legal dispute and suddenly realizes that it is worthless, because of non-existence of *culpa in contrahendo* in legislation of a certain country.

However, even if two countries that recognize the concept of pre-contractual liability in their legal orders are found, it does not mean that all problems are solved. In fact, the problems may just begin. The construction of pre-contractual liability can vary across nations. Once it could stem from the contractual basis, in a different case, it exists like a civil tort, for example.[2] It could be difficult to use the institute of *culpa in contrahendo* in legal orders with different concepts of this legal institute.

All problems can become even more complicated when one starts to think about pre-contractual liability in connection with international commercial arbitration. Is it even possible to decide on pre-contractual liability in arbitration? If so, under which conditions? What is then the applicable law?

The aim of this paper is to look deeper into the relationship between *culpa in contrahendo* in Private International Law and international commercial arbitration and to try to search for the answers on the issues mentioned above in the database of awards of the International Court of Arbitration of International Chamber of Commerce ("ICC Court") and in available literature. The ICC Court is one of the most experienced arbitration institutions.[3] Because of this, the opinion of ICC tribunals is very substantive and important and it can serve as guidance for solving particular problems.

2 Pre-contractual Liability

First of all, it is necessary to clarify what it is meant by the pre-contractual liability on the international level. Of course, it is a very hard task since the uniform definition of *culpa in contrahendo* does not exist.[4] However, there are some international attempts to unify the meaning of this institute.

2 The differences between concept of pre-contractual liability in Germany and France can be mentioned.

3 *International Court of Arbitration of the International Chamber of Commerce* [online]. International Chamber of Commerce [cit. 2015-03-08].

4 CARDENAS, Jonathan. Deal Jumping in Cross-Border Merger & Acquisition Negotiations: A Comparative Analysis of Pre-Contractual Liability under French, German, United Kingdom and United States Law. *New York University Journal of Law and Business* [online]. 2013, Vol. 9, No. 3 [cit. 2015-03-08], p. 944 - 948.

To be more specific, these are the UNIDROIT Principles on International Commercial Contracts ("UNIDROIT Principles")[5] and Principles of European Contract Law ("PECL").[6] Both of these international legal documents are trying to define the conditions under which pre-contractual liability can be identified. It is important to note that neither of the definitions is generally legally binding, because both documents were created by a non-state organization.[7]

The definition of pre-contractual liability under UNIDROIT Principles can be found in Arts. 2.1.15 and 2.1.16. These two articles deal with negotiation in bad faith and duty of confidentiality. If we analyze these two articles, we can deduce the basic elements of the concept of pre-contractual liability under UNIDROIT Principles:

1. Existence of pre-contractual negotiation;
2. Termination of pre-contractual negotiation in bad faith;
3. Emergence of damage;
4. Causal nexus between termination of negotiation and emergence of damage;
5. Breach of good faith.[8]

Almost the same definition can be found in Arts. 2.301 and 2.302 PECL. There are these basic elements of the concept of *cupla in contrahendo*:

1. Existence of pre-contractual negotiation;
2. Unjustifiable termination of pre-contractual negotiation;
3. Emergence of damage;

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5 UNIDROIT Principles on International Commercial Contracts 2010 [online]. *International Institute for the Unification of Private Law (UNIDROIT)*. Available from: http://www.unidroit.org/instruments/commercial-contracts/unidroit-principles-2010/ ("UNIDROIT Principles").

6 Principles of European Contract Law [online]. *Commission on European Contract Law*. Available from: http://www.trans-lex.org/400200/ ("PECL").

7 International Institute for Unification of Private Law and Commission on European Contract Law.

8 KOZÁREK, Tomáš. Předsmluvní odpovědnost v novém občanském zákoníku ve srovnání s Vídeňskou úmluvou, Principy UNIDROIT a PECL. In ROZEHNALOVÁ, Naděžda a kol. (ed.). *Nový občanský zákoník pohledem mezinárodních obchodních transakcí*. Brno: Masarykova univerzita, 2014, p. 84.

4. Causal nexus between termination of negotiation and emergence of damage;
5. Breach of good faith.[9]

The elements that have been stated by UNIDROIT Principles and PECL can be labeled as basic elements of the concept of pre-contractual liability on international level. Of course, it is not an official definition, because both documents are not legally binding, unless both contractual parties have chosen them as applicable to their relationship.

3 Possibility to Decide on Pre-contractual Liability in Arbitration

There are two fundamental requirements that must be fulfilled in order to decide on pre-contractual liability in arbitration. First, the dispute has to be arbitrable. Secondly, parties have to conclude the arbitration agreement.

Arbitrability of a dispute means the admissibility of the dispute for resolution by arbitration.[10] According to most of legal orders, there is no doubt that the dispute is arbitrable if it is a property dispute and if parties of the dispute can dispose of the claim freely.[11] These conditions are fulfilled in the case of pre-contractual liability.

Concerning the existence of the arbitration agreement, two situations may be distiguished:

1. The negotiation was terminated and the contract was not concluded.
2. The contract was concluded but one of the parties challenges its validity.

3.1 Contract Was Not Concluded

The first situation when pre-contractual liability can be assessed is if somebody demands her or his claim arising out of failed negotiation; so the contract was not concluded. In this case there exists only one option how

9 KOZÁREK, Tomáš. Předsmluvní odpovědnost v novém občanském zákoníku ve srovnání s Vídeňskou úmluvou, Principy UNIDROIT a PECL. In ROZEHNALOVÁ, Naděžda a kol. (ed.). *Nový občanský zákoník pohledem mezinárodních obchodních transakcí*. Brno: Masarykova univerzita, 2014, p. 85.

10 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. 2nd ed. Praha: ASPI, Wolters Kluwer, 2008. p. 116

11 SVATOŠ, Martin. Arbitrabilita sporu a mezinárodní obchodní arbitráž [online]. In *Repozitář závěrečných prací*, Charles University [cit. 2015-03-08], p. 40 - 44.

pre-contractual liability could be assessed in arbitration. The parties of a dispute must agree with it. In this case, parties of the dispute must conclude the arbitration agreement after the dispute has arisen.

3.2 Contract Was Concluded, but One of the Parties Challenged It

The second situation when pre-contractual liability can be assessed is if parties of negotiation conclude the contract which contains the arbitration clause, but one of the parties challenges the validity of the contract later and it is decided that the contract is invalid. The question is whether somebody can demand the claim arising out of the pre-contractual liability in this situation in arbitration?

First, it must be stated that the invalidity of the main contract automatically does not mean that the arbitration clause contained the rein cannot be used. According to the theory of separation of main contract and the arbitration clause, challenging validity of the main contract does not influence the validity of the arbitration clause.[12] It means that if we dispute validity of the main contract, the arbitration clause as an independent contract still exists and binds contractual parties even if the main contract is voided.[13]

However, the crucial issue is the scope of the arbitration clause. This problem was analysed in one of the ICC cases. Unfortunately, there exists only one ICC case dealing with the question of pre-contractual liability in arbitration. Nonetheless, it is still useful to know the opinion of the ICC Tribunal in this case. Its opinion can be found in Award No. 11789.[14]

In this case the ICC Tribunal had to decide the dispute about the sale of the majority in one EU airline. The dispute arose between consortium of banks, financial institution and non-EU airlines (Respondents) on one side and the Claimants who held the majority in EU airline on the other side. These two subjects concluded the promissory agreement with

12 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. 2nd ed. Praha: ASPI, Wolters Kluwer, 2008. p. 108

13 ROSEN, Janet A. Arbitration under Private International Law: The Doctrines of Separability and Competence de la Competence. *Fordham International Law Journal* [online]. 1994, Vol. 17 [cit. 2015-03-09], p. 606 - 607.

14 Award of ICC International Court of Arbitration of September 2013, No. 11789 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-09-30].

arbitration clause and then they concluded the main sale contract. After the main contract between the parties was concluded, EU Commission did not give permission for sale of the majority in EU airlines. Consequently, the consortium terminated the main contract because of the non-existence of the Commission's authorization, so the sale was not successful. Claimants argued that they were not responsible for the authorization. The responsibility should have laid on Respondents, who had been inadequately industrious. Respondents rejected this accusation.[15]

Claimants saw the possibility to rely on *culpa in contrahendo* based on the existence of promissory agreement and arbitration clause in it. The arbitration clause should cover all disputes arising out of or in connection to the promissory agreement. One of the Respondents' objections was the statement that promissory agreement has already expired.[16]

The ICC Tribunal supported Claimants opinion and decided that Tribunal has jurisdiction in relation to Claimants pre-contractual claim. The pre-contractual claim falls under arbitration clause in promissory agreement because:

1. The wording of the arbitration clause in dispute has a broad scope of applicability covering all disputes arising in connection to the agreement;
2. The fact, that promissory agreement already expired, has no influence on jurisdiction of arbitral tribunal. Generally recognized principle in international arbitration is that an arbitral tribunal shall not cease to have jurisdiction by the fact that the contract is terminated or even null and void.[17]

Based on these statements ICC Tribunal rejected Respondents' objection and constituted its jurisdiction over the pre-contractual liability in this case.[18]

This ICC case cannot be overestimated, but it supports the opinion that for possibility to decide on pre-contractual liability in arbitration the most important is the formulation of arbitration clause. Its formulation must be sufficiently

15 Award of ICC International Court of Arbitration of September 2013, No. 11789 [online]. In *Dispute Resolution Library,* International Chamber of Commerce [cit. 2015-09-30].

16 *Ibid.*

17 *Ibid.*

18 CARLEVARIS, Andrea. The Arbitration of Disputes Relating to Mergers and Acquisitions: A Study of ICC Cases [online]. In *ICC Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-03-09].

broad and must contain disputes arising in connection to the agreement. The wording of the arbitration clause could be e.g. all disputes arising out of or in connection with the agreement will be settled in arbitration. This wording allows deciding on pre-contractual liability in arbitration.

4 Applicable Law

In this part of the paper I would like to answer the question about the law applicable to pre-contractual liability in arbitration.

The first problem to address is whether *culpa in contrahendo* is of contractual or tortious nature. The national courts usually use for this purpose *lex fori*, but arbitrators do not have to do it. They have to find the legal order that could be used for this classification. The most frequent legal order selected for this assessment is the law applicable to the contract.[19]

4.1 Applicable Law - Contract Was Not Concluded

In cases when main contract was not concluded, the situation is a bit complicated. Ideal solution would be if the parties would have chosen applicable law for solution of their dispute in arbitration agreement or settled the mechanism how to choose applicable law. If the parties did not do that, arbitrators must choose applicable law for resolution of dispute. They can choose it based on conflict-of-law rules or as a direct choice of law. Question is what kind of conflict-of-law rules they should use. According to UNCITRAL Model Law on International Commercial Arbitration arbitrators shall use conflict-of-law rules that they consider applicable.[20]

4.2 Applicable Law – Contract Was Concluded, but Its Validity Was Challenged

Arbitrators have several choices while searching for the applicable law. They can use conflict-of-laws procedure or choose applicable law directly.

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19 GONZALES, Florian. The Treatment of Tort in ICC Arbitral Awards [online]. In *Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-03-08], point 8.

20 Art. 28(2) UNCITRAL Model Law on International Commercial Arbitration 1985 with amendments as adopted in 2006 [online]. *United Nations Commission on International Trade Law* (UNCITRAL). Available from: http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf.

In conflict-of-laws procedure several approaches for the determination of the applicable law exist depending on the nature of pre-contractual liability. If pre-contractual liability has a contractual nature, the best possibility is to choose the law that governs the main contract (*lex causae*). The claim based on pre-contractual liability is contractual and it is logical to use the same law as for the main contract.

If pre-contractual liability has tortious nature, the applicable law can be *lex cause,* too. This choice has a substantial benefit – the main contract and all matters connected to it are ruled by the same law – but it is not the only possibility and arbitrator can prefer another way for determining the applicable law.[21]

The usage of the concept *lex loci delicti* or other similar rules as a 'proper law of tort' could be a good alternative to using the applicable law to contract. In this case, the applicable law could be more connected with victim of harm.[22]

Probably the best solution of this whole problem would be the existence of some universal guideline or conflict rules which would give us the precise instruction on how to proceed. There exists the EU Regulation Rome II which has the exact rule for determining the applicable law of the pre-contractual liability (*lex cause*[23]),[24] but this regulation is obligatory only for EU Member States and their institutions.[25] In another situation, the arbitrators should seek the guidance in the conflict of law rules that are applicable.[26]

21 GONZALES, Florian. The Treatment of Tort in ICC Arbitral Awards [online]. In *Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-03-08], point 36.

22 *Ibid.*, point 37.

23 As was said, *lex cause* has advantage with the fact that the main contract and all matters connected to it are ruled by the same law.

24 Article 12 Regulation (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (Rome II). In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32007R0864 & qid=1426498369653 & from=CS

25 ORGONÍK, Martin. Nařízení Řím II. In *Evropské mezinárodní právo soukromé* [online]. Faculty of Law, Masaryk University [cit. 2015-03-10].

26 CAPPER, Phillip; LJUNGSTRÖM, Kristina; DÉPINAY, Paulina. 'Proving' the Contents of the Applicable Substantive Law(s) [online]. In *Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-03-10].

The problem with choice of law procedure is the fact that arbitrators often do not bother with using some conflict of law rules or guidance or methods for searching applicable law and just choose the law they want or think is appropriate.[27] Often, they use the second possibility – direct choice of law. This second possibility for choice of law can make arbitrators' choice of law unpredictable. Without any strict rule for choice of law parties of dispute cannot be sure what will be applicable law for their dispute.

5 Conclusion

The problem of assessment of the pre-contractual liability in international commercial arbitration is very difficult. At the beginning we have asked two questions:

1. Is it even possible to decide on pre-contractual liability in arbitration?
2. In the case of positive answer, what law is applicable?

For the first question there exist two answers. If the contract was not concluded, parties have to agree on assessment of pre-contractual liability in arbitration after dispute arise.

However, in case when contract was concluded, but one of the parties challenged it, the situation is different. Nevertheless, thanks to ICC and legal scholars some clues for determination of pre-contractual liability can be found. The most important factor is the arbitration clause and its scope. If the arbitration clause is sufficiently broadly conceived, also pre-contractual liability may be assessed in arbitration, even if the nature of pre-contractual liability is the tort. The wording of the arbitration clause could be e.g. all disputes arising out of or in connection to the agreement will be settled in arbitration.

For the second question: more possibilities exist while searching for the law applicable in arbitration for assessment of *culpa in contrahendo*. It depends on the nature of the institute of pre-contractual liability (contractual

27 GONZALES, Florian. The Treatment of Tort in ICC Arbitral Awards [online]. In *Dispute Resolution Library*, International Chamber of Commerce [cit. 2015-03-10], point 35.

x tortious), but usually it will be *lex loci delicti, lex cause* (what is probably the best choice, because the main contract and all matters connected to it are ruled by the same law) or the direct choice of the applicable law.

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EFFECTS OF THE OPENING OF INSOLVENCY PROCEEDINGS UNDER THE EU REGULATION No. 1346/2000 ON PENDING ARBITRATION PROCEEDINGS

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Abstract

This paper deals with effects of the opening of insolvency proceedings under the Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings ("Insolvency Regulation"), on pending arbitration concerning asset forming part of the insolvent estate. The present article offers determination of collective character of insolvency proceedings compared to the private character of arbitration brought by an individual creditor and emphasizes the necessity to regulate their mutual interaction. The author analyzes relevant provisions of the Insolvency Regulation and its revised version in order to verify whether its framework establishes rules for determination of the law applicable to effects of the insolvency proceedings on pending arbitration. The Insolvency Regulation establishes the uniform rule in order to determine the law applicable to effects of the opening of insolvency proceedings solely for lawsuits to which a debtor is a party. In spite of the absence of express wording, the author concludes the conflict of laws rule for effects on lawsuits is applicable also with regard to arbitral proceedings.

Keywords

Applicable Law; Arbitration Proceedings; Collective Proceedings; Cross-border Element; Insolvency Proceedings; Insolvency Regulation.

1 Introduction

The commencement of insolvency proceedings implies significant restriction of a debtor to dispose of his assets. The inability of a debtor to pay

debts to his creditors may affect also the proper functioning of the internal market.[1] With regard to increasing cross-border effects of activities of undertakings, the European Union ("EU") has adopted an instrument which coordinates the measures to be taken regarding an asset of the debtor.

The Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings ("Insolvency Regulation") aims to improve an overall effectiveness and efficiency of insolvency proceedings with European cross-border element.[2] The Insolvency Regulation provides the proceedings covered by its scope of application with universal effects constituting the essential condition for effective collective satisfaction of creditor's claims at the supranational level. The universal effects enable to capture debtor's total asset situated in all Member States where the Insolvency Regulation shall apply.[3] Effectiveness of the collective insolvency proceedings may be jeopardized due to conduct of parallel individual proceedings. Most of the national laws tend to provide priority of insolvency proceedings over the pending individual proceedings.[4] The main purpose is to prevent from arbitrary reducing the insolvent estate and to safeguard the orderly satisfaction of creditors. In compliance with the fundamental principle *par conditio creditorum*, the ordinary creditors are to be satisfied *pro rata* in common collective proceedings. In this respect, the ordinary creditors must be precluded from initiating proceedings outside of the insolvency collective proceedings.[5]

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1 Preamble, Recital 3 Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX:32000R1346 ("Insolvency Regulation").

2 Preamble, Recital 2 Insolvency Regulation.

3 Preamble, Recital 12 Insolvency Regulation (for analysis of the model of universality in context of the Insolvency Regulation see VIRGÓS, Miguel; GARCIMARTÍN, Francisco. *The European Insolvency Regulation: Law and Practice*. The Hague: Kluwer Law International, 2004. p. 15 - 19).

4 PFEIFFER, Thomas. Article 15 EIR: Effect of the Insolvency Proceedings on Individual Proceedings in Other member States. In HESS, Burkhard; OBERHAMMER, Paul; PFEIFFER, Thomas. *European Insolvency Law: The Heidelberg-Luxembourg-Vienna Report: On The Application of Regulation No. 1346/2000/EC on Insolvency Proceedings (External Evaluation JUST/2011/JCIV/PR/0049/A4)*. München: C.H. Beck, 2014. p. 217.

5 LAZIĆ, Vesna. Cross-Border Insolvency and Arbitration: Which Consequences of Insolvency Proceedings Should be Given Effect in Arbitration? In KRŐLL, Stefan; MISTELIS, Loukas; PERALES VISCASILLAS, Maria Pilar. *International Arbitration and International Commercial Law: Synergy Convergence and Evolution*. Alphen aan den Rijn: Kluwer Law International, 2011, p. 350.

The Insolvency Regulation provides conflict-of-laws rules determining law applicable to mutual interference between the insolvency opened in one of the Member States and individual proceedings conducted in other Member States.[6] The conflict-of-laws rules make no express reference to pending arbitration concerning assets of the insolvent debtor. Taking into account a frequent use of arbitration to resolve disputes and its potential impact on effectiveness of the insolvency proceedings, it is sufficient to determine law applicable to their mutual interaction. The author sees the challenge in consideration whether the Insolvency Regulation provides any rule determining the governing law. The subject of this paper is whether the scope of the conflict-of-laws rule regarding the effects of insolvency on a pending lawsuit covers the pending arbitration.

The paper deals with interference between two proceedings of very different nature:

Arbitration represents one of the most frequent means of resolving disputes between parties. Arbitration is concerned with will of the parties as a source of the arbitrator's authority to determine his jurisdiction and resolve parties' disputes in a non-judicial forum. Arbitrability of the dispute and valid arbitral agreement of the parties constitute the essential conditions of arbitration proceedings.[7] The will of the parties defines also the extent of the arbitrator's power.[8]

On the other hand, the insolvency is of different nature. The insolvency proceedings are to be conducted under the mandatory procedural as well as substantive law and under a high degree of a state control.[9] The underlying objective is to collect the total asset of the insolvent debtor, convert it into money and satisfy claims of his creditors in compliance with the principle of equal treatment of the creditors. Otherwise the insolvency may lead to restructuring of the debts in order to fulfill them.[10]

6 Art. 15 Insolvency Regulation.

7 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Praha: ASPI, Wolters Kluwer, 2008. p. 42.

8 LAZIĆ, Vesna. *Insolvency Proceedings and Commercial Arbitration*. Austin: Wolters Kluwer, 1998. p. 3.

9 BĚLOHLÁVEK, Alexander. Impact of Insolvency of a Party on Pending Arbitration Proceedings in Czech Republic, England and Switzerland and Other Countries. In ROTH, Marianne; GEISTLINGER, Michael. *Yearbook on International Arbitration* [online]. Vol. I. Antverpen/Berlin/Copenhagen/Wien/Graz: EAP, 2010 [cit. 2015-03-02], p. 146 - 147.

10 GOODE, Royston Miles. *Principles of Corporate Insolvency Law*. 4th ed. London: Sweet & Maxwell, 2011. p. 16.

The aim of this paper is to analyze the relevant provisions of the Insolvency Regulation and to verify following hypothesis: *The Insolvency Regulation lays down conflict-of-laws rules determining the law applicable to effects of the opening of insolvency proceedings on pending arbitration concerning an asset of which the debtor was divested.*

2 Effects of Opening of the Insolvency Proceedings under the National Laws

After opening of the insolvency proceedings, individual creditors may not satisfy their claims by means of proceedings outside the insolvency proceedings. Therefore, the national laws tend to establish special provisions on the effects of declaration of bankruptcy on lawsuits brought by individual creditors in order to satisfy their claims.[11] The main purposes justifying the interference are determined as follows: The aforementioned regulation aims to prevent from dissipation of the insolvent estate, to provide impartial treatment of all debtor's creditors with regard to their rights within the insolvency proceedings as collective proceedings and create the optimal atmosphere for reorganization of the debtor or his liquidation.[12]

Most national laws provide regulation of effects of the insolvency proceedings not only to the ordinary procedures, but also with regard to the arbitration proceedings. For instance, we can mention the French Code of Civil Procedure providing for interruption of arbitration when the insolvency proceedings have been opened. The English and Dutch laws provide the regulation of suspension as a part of their insolvency acts.[13]

On the other hand, the German law includes a special provision on suspension of the proceedings in part of the Code of Civil Procedure which is not applicable to the arbitration proceedings. In German legal theory, there

11 PFEIFFER, Thomas. Article 15 EIR: Effect of the Insolvency Proceedings on Individual Proceedings in Other Member States. In HESS, Burkhard; OBERHAMMER, Paul; PFEIFFER, Thomas. *European Insolvency Law: The Heidelberg-Luxembourg-Vienna Report: On The Application of Regulation No. 1346/2000/EC On Insolvency Proceedings (External Evaluation JUST/2011/JCIV/PR/0049/A4).* München: C.H. Beck, 2014, p. 217; BĚLOHLÁVEK, Alexander J. *Evropské a mezinárodní insolvenční právo: komentář.* 1. ed. Praha: C.H. Beck, 2007. p. 226.

12 MCBRYDE, William; FLESSNER, Axel; KORTMANN, S. *Principles of European Insolvency Law.* Deventer: Kluwer Legal Publishers, 2003. p. 34.

13 LAZIĆ, Vesna. *Insolvency Proceedings and Commercial Arbitration*. Austin: Wolters Kluwer, 1998. p. 290.

is no clear resolution whether the pending arbitration shall be suspended after opening of insolvency proceedings or not. The majority opinion is that the arbitration shall not be interrupted under the aforementioned act. Nevertheless, the interruption may be provided for by the parties in their arbitration agreement.[14]

Until 2014, the Insolvency Act of the Czech Republic did not provide regulation with respect to interference between the insolvency and the arbitration to which the insolvent debtor is a party. The current legislation includes an express provision establishing that the arbitration concerning rights or obligations belonging to the insolvent estate shall be suspended at the time the bankruptcy is declared.[15]

3 Law Applicable to Effects of the Insolvency Proceedings under the Insolvency Regulation

With regard to the impact of insolvency proceedings on lawsuits brought against a person who is the subject of the insolvency, the individual Member States of the EU state mutually different rules. In compliance with the Preamble of the Insolvency Regulation,[16] common framework for insolvency proceedings should guarantee the efficiency and effectiveness of insolvency proceedings within the EU and ensure equal treatment of creditors of the debtor in distribution of insolvent estate among all of them.[17] Therefore, the Insolvency Regulation established uniform rules in order to determine law applicable to such effects.

3.1 Law Applicable to Effects of the Insolvency on "Lawsuits Pending"

Particular provisions of the Insolvency Regulation, such as Art. 4(2)(f) and Art. 15, prevent individual creditors from circumvention the aforementioned

14 LAZIĆ, Vesna. *Insolvency Proceedings and Commercial Arbitration*. Austin: Wolters Kluwer, 1998. p. 292.

15 Sec. 263 CZECH REPUBLIC. Act No. 182/2006 Coll., on insolvency and its resolution ("the Insolvency Act").

16 Preamble, Recitals 2, 3, 4 and 8 Insolvency Regulation.

17 Judgment of the Court of Justice of 17 May 2005. Commission of the European Communities vs. AMI Semiconductor Belgium BVBA and Others. Case C-294/02, point 70.

principles by bringing lawsuits before courts of other Member States.[18] This regulation is followed by Arts. 16 and 17 Insolvency Regulation which safeguard the automatic recognition of judgments concerning opening of the insolvency in any Member State which produces the effect pursuant to the law of state where the insolvency proceeding is opened.[19]

The Insolvency Regulation distinguishes effects of insolvency proceedings on pending lawsuits brought by individual creditors and individual enforcement actions. In accordance with Art. 4(2)(f) Insolvency Regulation,[20] the impact of the insolvency on individual enforcement actions (pending or future),[21] including either suspension or prohibition of proceedings on executions,[22] shall be determined by *lex fori concursus*.[23] The cited provision of the Insolvency Regulation covers also effects on the commencement of individual proceedings. These issues shall be determined in compliance with the law of the state of opening of the insolvency proceedings, except for aspect of international jurisdiction. International jurisdiction to commence a new action shall be determined pursuant to the rules laid down by the Insolvency Regulation itself or the Brussels Ibis Regulation.[24, 25]

18 Opinion of Advocate General Kokott to the judgment of the Court of Justice of 17 May 2005. Commission of the European Communities vs. AMI Semiconductor Belgium BVBA and Others. Case C-294/02, point 84.

19 Judgment of the Court of Justice of 17 May 2005. Commission of the European Communities vs AMI Semiconductor Belgium BVBA and Others. Case C-294/02, point 69.

20 Art. 4(2)(f) Insolvency Regulation states: *„The law of the State of the opening of proceedings shall determine the conditions for the opening of those proceedings, their conduct and their closure. It shall determine in particular: (…) the effects of the insolvency proceedings on proceedings brought by individual creditors, with the exception of lawsuits pending."*

21 VIRGÓS, Miguel; GARCIMARTÍN, Francisco. *The European Insolvency Regulation: Law and Practice*. The Hague: Kluwer Law International, 2004. p. 76.

22 *Ibid*., p. 76.

23 FLETCHER, Ian F. *Insolvency in Private International Law: National and International Approaches*. 2nd ed. Oxford: Oxford University Press, 2005. p. 419 - 420.

24 Regulation (EU) No. 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. In *EUR-lex*. Available from: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0001:0032:en:PDF ("Brussels Ibis Regulation").

25 Rules on the international jurisdiction established by the Insolvency Regulation cover the insolvency-derived actions. In other cases, the international jurisdiction shall be determined pursuant to the Brussels Ibis Regulation. (Compare VIRGÓS, Miguel; GARCIMARTÍN, Francisco. *The European Insolvency Regulation: Law and Practice*. The Hague: Kluwer Law International, 2004. p. 77).

The effects are basically common to all laws of the Member States.[26] *Lex fori concursus* shall govern the effects as such whereas the procedural implementation remains in authority of the state where the proceeding is being conducted. Scope of the national law covers the concrete modification of the effect on procedure in question (either stay, suspension or exclusion of part of the proceedings to a separate procedure in order to secure rights and legitimate interests of other parties to the proceedings).[27]

For completeness, it is necessary to note that the Insolvency Regulation determines the time of the opening of the proceedings as the moment at which the decision to open the proceedings becomes effective, regardless whether the decision is final or not.[28] The time of the opening is to be considered independently of the national concepts established in laws of the Member States.[29]

There is an important exception from application of Art. 4(2)(f) Insolvency Regulation established in relation to lawsuits pending at the moment of commencement of insolvency proceedings in other Member State of the European Union. Art. 15 Insolvency Regulation covers only the pending proceedings to which the debtor is a party. The continuation of such lawsuit at the time of commencement of insolvency proceedings shall be governed by the law of the state where the proceeding is pending.[30]

3.2 Law Applicable to Effects of the Insolvency on "Arbitration Pending"

The current wording of Art. 15 Insolvency Regulation covers effects of insolvency proceedings on lawsuits pending. It does not provide

26 VIRGÓS, Miguel; GARCIMARTÍN, Francisco. *The European Insolvency Regulation: Law and Practice*. The Hague: Kluwer Law International, 2004. p. 76.

27 BĚLOHLÁVEK, Alexander J. *Evropské a mezinárodní insolvenční právo: komentář*. 1. ed. Praha: C.H. Beck, 2007. p. 228.

28 Art. 2(f) Insolvency Regulation in connection with Art. 2(e) Insolvency Regulation defining the term judgment.

29 The regulations of the opening of the insolvency in particular Member States differ one from another (BĚLOHLÁVEK, Alexander J. *Evropské a mezinárodní insolvenční právo: komentář*. 1. ed. Praha: C.H. Beck, 2007. p. 101).

30 Art. 15 Insolvency Regulation states: *"The effects of insolvency proceedings on a lawsuit pending concerning an asset or a right of which the debtor has been divested shall be governed solely by the law of the Member State in which that lawsuit is pending."*

an explicit regulation of law applicable to effects of insolvency proceedings on arbitration, nor any interpretation guidelines in order to consider whether the formulation lawsuits covers the arbitral proceedings or not.

Many authors inclined to follow broad interpretation of Art. 15 Insolvency Regulation.[31] The purpose is to protect the main function of collective insolvency proceedings – orderly examination of the debtor's asset to all his creditors without any competition. Another justification is to achieve the fundamental aim of the Insolvency Regulation - to improve effectiveness and efficiency of the insolvency proceedings in cross-border context among the Member States of the European Union.[32]

According to *Bělohlávek*, the scope of application of Art. 15 Insolvency Regulation automatically covers pending arbitration.[33] Firstly, he emphasizes that the Insolvency Regulation, contrary to other instruments regulating the judicial cooperation in the EU, did not exclude the arbitration from its scope of application.[34] In addition, most of the national laws of the Member States conceptualize the arbitration as an authoritative mean of resolving civil disputes.[35] Hence, the term of lawsuit pending shall be considered broader than the "lawsuit pending within the jurisdiction of the courts".[36]

31 BĚLOHLÁVEK, Alexander. Impact of Insolvency of a Party on Pending Arbitration Proceedings i Czech Republic, England and Switzerland and Other Countries. In ROTH, Marianne; GEISTLINGER, Michael. *Yearbook on International Arbitration* [online]. Vol. I. Antverpen/Berlin/Copenhagen/Wien/Graz: EAP. 2010 [cit. 2015-03-02], p. 146; PFEIFFER, Thomas. Article 15 EIR: Effect of the Insolvency Proceedings on Individual Proceedings in Other Member States. In HESS, Burkhard; OBERHAMMER, Paul; PFEIFFER, Thomas. *European Insolvency Law: The Heidelberg-Luxembourg-Vienna Report: On The Application of Regulation No. 1346/2000/EC on Insolvency Proceedings (External Evaluation JUST/2011/JCIV/PR/0049/A4).* München: C.H. Beck, 2014, p. 218; VIRGÓS, Miguel; GARCIMARTÍN, Francisco. *The European Insolvency Regulation: Law and Practice.* The Hague: Kluwer Law International, 2004. p. 142.

32 Preamble, Recital 8 Insolvency Regulation.

33 BĚLOHLÁVEK, Alexander. Impact of Insolvency of a Party on Pending Arbitration Proceedings in Czech Republic, England and Switzerland and Other Countries. In ROTH, Marianne; GEISTLINGER, Michael. *Yearbook on International Arbitration* [online]. Vol. I. Antverpen/Berlin/Copenhagen/Wien/Graz: EAP, 2010 [cit. 2015-03-04], p. 166.

34 *Ibid.,* p. 154.

35 BĚLOHLÁVEK, Alexander J. *Evropské a mezinárodní insolvenční právo: komentář.* 1. ed. Praha: C.H. Beck, 2007. p. 514.

36 BĚLOHLÁVEK, Alexander. Impact of Insolvency of a Party on Pending Arbitration Proceedings in Czech Republic, England and Switzerland and Other Countries. In ROTH, Marianne; GEISTLINGER, Michael. *Yearbook on International Arbitration* [online]. Vol. I. Antverpen/Berlin/Copenhagen/Wien/Graz: EAP, 2010 [cit. 2015-03-04], p. 146.

The Court of Justice of the European Union ("CJEU") had no opportunity to provide interpretation of the respective provisions. Due to the absence of the autonomous interpretation given by the CJEU, most of the experts[37] in cross-border insolvency law operate with the case-law of national courts.[38] They refer primarily to the judgment in Elektrim vs. Vivendi case, issued by the English Court of Appeal ("Court"). The Court brought an assessment of the formulation proceedings brought by individual creditors in light of arbitral proceedings. The summary of facts of the case is as follows. The original dispute was between Elektrim, a company incorporated in Poland, and Vivendi, a company incorporated in France. In 2001, Elektrim and Vivendi concluded an investment agreement including an arbitration agreement. The arbitration agreement provided for arbitral proceedings in London. It subjected the procedure to LCIA rules. The agreement itself was governed by English law. In compliance with this arbitration agreement, the arbitration was opened before the LCIA Arbitral Tribunal. Afterwards, the Polish court declared Elektrim company bankrupt and considered effects of the insolvency proceedings on the parallel pending arbitration. The Court should have decided whether to apply English or Polish law. The Polish law stipulated termination of the arbitral proceedings. In case the English

37 See e.g. PFEIFFER, Thomas. Article 15 EIR: Effect of the Insolvency Proceedings on Individual Proceedings in Other Member States. In HESS, Burkhard; OBERHAMMER, Paul; PFEIFFER, Thomas. *European Insolvency Law: The Heidelberg-Luxembourg-Vienna Report: On The Application of Regulation No. 1346/2000/EC on Insolvency Proceedings (External Evaluation JUST/2011/JCIV/PR/0049/A4)*. München: C.H. Beck, 2014, p. 218; LAZIĆ, Vesna. Cross-Border Insolvency and Arbitration: Which Consequences of Insolvency Proceedings Should be Given Effect in Arbitration? In KRÖLL, Stefan; MISTELIS, Loukas; PERALES VISCASILLAS, Maria Pilar *International Arbitration and International Commercial Law: Synergy Convergence and Evolution*. Alphen aan den Rijn: Kluwer Law International, 2011, p. 338; GE, Yang. *Insolvency Proceedings and Their Effect on International Commercial Arbitration* [online]. LLM The sis. University of Ghent, 2012 [cit. 2015-03-04], p. 47 - 50; BĚLOHLÁVEK, Alexander. Impact of Insolvency of a Party on Pending Arbitration Proceedings in Czech Republic, England and Switzerland and Other Countries. In ROTH, Marianne; GEISTLINGER, Michael. *Yearbook on International Arbitration*. Vol. I. Antverpen/Berlin/Copenhagen/Wien/Graz: EAP, 2010 [cit. 2015-03-04], p. 159 - 160; WAUTELET, Patrick; KRUGER, Thalia; COPPENS, Govert. The Practice of Arbitration: Essays in Honour of Hans van Houtte. Oxford: Hart Publishing, 2012. 382 p.

38 The national case-law serves as a source of inspiration. The autonomous interpretation may be performed solely by the Court of Justice of the European Union. The national courts are not able to ensure uniform interpretation of the EU law (see TÝČ, Vladimír. *Základy práva Evropské unie pro ekonomy*. 6th ed. Prague: Leges, 2010. p. 150 - 151.)

law has been applied, the arbitral proceeding would have remained unaffected. The Court of Appeal of England held that this situation was covered by Art. 15 of the Insolvency Regulation, therefore the effects of declaring bankruptcy in Poland on arbitral proceedings pending in England were governed by the English law.[39]

The General Reporter used the analogy to apply Art. 15 Insolvency Regulation in order to determine law applicable to effects on arbitral proceedings.[40] In other words, for purpose of application of Art. 15 Insolvency Regulation the pending arbitration was classified as the "pending lawsuit."[41]

The Court considered Art. 15 with reference to the Preamble of the Insolvency Regulation providing its main objectives and underlying principles. With regard to Recital 23 of the Preamble, *„this Regulation should set out, for the matters covered by it, uniform rules on conflict of laws which replace, within their scope of application, national rules of private international law"*. Thus the law of the State where the insolvency proceedings are opened shall govern the effects of the opening.[42][43] Afterwards, the Court highlighted the necessity to safeguard legitimate expectations and certainty of transactions connected with other Member State than the state of opening of the insolvency proceedings. In order to achieve this aim, the Insolvency Regulation established several exceptions to the aforementioned general rule on conflict of laws.[44]

The judgment emphasized the urgent need of revision of the Insolvency Regulation which would bring more legal certainty to the sphere of relation between arbitral and insolvency proceedings.

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39 Decision of the Court of Appeal of England and Wales, England of 9 July 2009, No. [2009] EWCA Civ 677 [online]. In *British and Irish Legal Information Institute* [cit. 2015-03-04].

40 HESS, Burkhard; OBERHAMMER, Paul; PFEIFFER, Thomas. *European Insolvency Law: The Heidelberg-Luxembourg-Vienna Report: On the Application of Regulation No. 1346/2000/EC on Insolvency Proceedings (External Evaluation JUST/2011/JCIV/PR/0049/A4).* München: C.H. Beck, 2014. p. 217.

41 GE, Yang. *Insolvency Proceedings and Their Effect on International Commercial Arbitration* [online]. LLM The sis. University of Ghent, 2012 [cit. 2015-02-01], p. 48.

42 By virtue of Art. 4 Insolvency Regulation.

43 KRŐLL, Stefan; MISTELIS, Loukas; PERALES VISCASILLAS, Maria Pilar. *International Arbitration and International Commercial Law: Synergy Convergence and Evolution.* Kluwer Law International, 2011. p. 347.

44 The Court referred to Preamble, Recital 24 Insolvency Regulation.

In light of aforementioned, the authors uniformly conclude that the scope of application of Art. 15 Insolvency Regulation shall cover also effects on pending arbitral proceedings concerning an asset of which the insolvent party has been divested.

Taking into account the opinions of national courts as well as the experts in this area of private international law, we may conclude that the law applicable to effects of the opening of insolvency proceedings shall be determined by virtue of Art. 15 Insolvency Regulation. Pursuant to this provision the law of the Member State where the arbitration is being conducted shall apply. *Lex arbitri* determines whether the opening of the insolvency proceedings shall be suspended. However, the question whether the concrete assumptions have been fulfilled shall be assessed as a preliminary question.[45]

Several authors preferred to amend the discussed provision and provide it with an express regulation of interaction between insolvency proceedings with European cross-border element opened in one of the Member States and arbitral proceedings conducted in any other Member State.[46]

The amendment of Art. 15 the Insolvency Regulation was suggested referring to the aforementioned finding of the English Court of Appeal in the Elektrim vs. Vivendi case.[47, 48]

The proposal suggested replacement of the current version of Art. 15 by following wording: *"The effects of insolvency proceedings on a pending lawsuit or arbitral proceeding concerning an asset or a right of which the debtor has been divested shall be governed solely by the law of the Member State in which that lawsuit is pending or in which the arbitral proceedings have their seat."*[49]

45 The preliminary question will be governed by other law (i.e. the law applicable to the arbitration agreement). See BĚLOHLÁVEK, Alexander. Impact of Insolvency of a Party on Pending Arbitration Proceedings in Czech Republic, England and Switzerland and Other Countries. In ROTH, Marianne; GEISTLINGER, Michael. *Yearbook on International Arbitration* [online]. Vol. I. Antverpen/Berlin/Copenhagen/Wien/Graz: EAP, 2010 [cit. 2015-02-14], p. 161.

46 GALEN, Robert Van; INSOL Europe. *Revision of the European Insolvency Regulation* [online]. INSOL Europe, 2012 [cit. 2015-03-10], p. 11.

47 *Ibid.,* p. 48 and 63.

48 *Ibid.*, p. 64 - 65.

49 The European Parliament did not make any comment to the original proposal of amendment of Art. 15 suggested by the Commission. The revision of the Insolvency Regulation was recently adopted at the second reading on the 20 May 2015 (Proposal for a Regulation of the European Parliament and of the Council amending Council Regulation (EC) No. 1346/2000 on insolvency proceedings. COM(2012)744 final, 12 December 2012. Available from: http://ec.europa.eu/justice/civil/files/insolvency-regulation_en.pdf).

4 Conclusion

The aim of this paper was to bring analysis of the relevant provisions laid down under the Insolvency Regulation and to verify the hypothesis whether it provides regulation of law applicable to effects of the opening of insolvency proceedings on pending arbitration concerning an asset of which the debtor was divested. Considering the aforementioned conclusions, the defined aim was achieved and the hypothesis set above was verified. Art. 15 Insolvency Regulation establishes the uniform rule in order to determine the law applicable to effects of the opening of insolvency proceedings on lawsuits pending to which a debtor is a party. In spite of the absence of express wording, this provision shall apply also with regard to the arbitral proceedings.

In order to improve the sufficient legal certainty, the Proposal for amendment of the Insolvency Regulation suggested changing wording of Art. 15. The European Commission proposed to include an explicit provision related to the arbitral proceedings.

The author of this article shares the prevailing opinions on the discussed question. According to her, the pending arbitration concerning any asset of the insolvent party could results in reduction of the insolvent estate and thus in disruption of equality among ordinary creditors of the debtor. Therefore, it is necessary to regulate interaction between the insolvency proceedings and parallel arbitration proceedings.

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ON PARTICIPATION AND NON-PARTICIPATION OF THIRD PARTIES IN ARBITRATION UNDER SUBSTANTIVE LAW RULES

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Abstract

The paper deals with mechanisms well-established in civil litigation which may face the real obstacles in arbitration due to its contractual nature and its implications. Third party joinder and intervention are procedural mechanisms which have very important goals ensuing from substantive law. Thus, their application shall be made with their consequences borne in mind. The author focuses on third parties participation in arbitration in capacities other than parties to it, i.e. side intervenor or similar and presents some remarks on third party notice of arbitration and on substantive law provisions providing an obligation to inform third person about the very fact of a dispute and its resolution. These rules are presented to analyze potential effect of third party notice of arbitration, i.e. so-called intervention effect, plea of male gesti processus, obviously with necessary reservations ensuing from contractual nature of arbitration. Furthermore, the article deals briefly with a fact determining effect of an arbitral award. The author concludes that it is necessary to distinguish between consent to submit own disputes to an arbitration and a consent to participate in an arbitration in a capacity other than a party. The latter one may cover participation in arbitration in as a so-called side intervenor or in similar ones. The existence of substantive law provisions providing for an obligation to inform third person about the very fact of a dispute and its resolution shall be an important hint used in determination of the scope of consent of the original parties to the ongoing arbitration for joinder of a third person or its intervention in this arbitration. The same apply to third person's consent in that regard. In the author's view, the existence of this substantive law

provisions providing for an obligation to serve third person with a notice of arbitration creates a demand for a research on a so-called side intervention and similar mechanisms in arbitration.

Keywords

Arbitration; Third Parties; Third Party Joinder; Third Party Notice; Intervention.

1 Introduction

Procedural laws contain provisions regulating participation of concerned persons in judicial proceedings in capacities of a party, other than a party and particular consequences of their absence in these proceedings. Issues concerning rights of third parties in dispute resolution are one of the most significant also in modern arbitration which is more and better adjusted to resolve multiparty and multi-contract disputes.

An interest of a third party in an arbitration proceedings, namely in its conduct and outcome, derives from substantive law, more or less directly. Thus, substantive law provisions protecting this interest and consequences of non-participation of third parties in arbitration proceeding under these provisions will be discussed in this article.

The category of third parties in arbitration can be divided through many criteria. In this article I will use the term "third party" for both "third parties *sensu stricto*" and "third parties *sensu largo*".[1] Third parties *sensu stricto* are these who has never consented to arbitration agreement and their consent cannot be derived in any way. The second group covers parties bound by the arbitration agreement notwithstanding not being a signatory of that, so called "non-signatories". Term "third person" will be used, as e.g. in the UNCITRAL Arbitration Rules (as revised in 2010)[2] ("UNCITRAL Rules"), to express that this third person is not one of the original parties to arbitration notwithstanding being or not a party to the underlying arbitration agreement.

1 See e.g. BREKOULAKIS, Stavros. *Third Parties in Arbitration*. New York: Oxford University Press, 2010. p. 2.

2 UNCITRAL Arbitration Rules (as revised in 2010) [online]. United Nations Commission for International Trade Law (UNCITRAL) [cit. 2015-10-19]. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules-revised/arb-rules-revised-2010-e.pdf ("*UNCITRAL Rules*").

In this paper I would like to present some remarks on the issue of third parties participation in arbitration from the point of view of requirement of consent for joinder of a third personor its intervention in arbitration. Moreover, I will discuss the existence and the scope of effects of an arbitral award rendered in third parties' absence, mainly issues of binding force of arbitral award in relations between one of the parties to the arbitration and third person (similar to so-called "intervention effect" of state court decisions) and *exceptio male gesti processus*. I will address also so-called "effect of the facts of the case" of an arbitral award. One shall answer the basic question regarding a possibility of achieving these effects in arbitration and this is the main interest of this article. I will focus on participation of third parties in arbitration in capacities other than so-called full-parties (plaintiff or claimant), i.e. as side intervenors and similar ones.

Development of regulation of participation of third persons in arbitration in a capacity other than ˝the so-called full-parties is a real challenge to resolution of international disputes. It touches upon the efficacy and finality of dispute resolution in multiparty and multi-contract scenarios. The contractual nature of arbitration is in that regard obviously of the highest importance. However, actors of international commercial reality are bound by substantive laws of particular countries. Some provisions of these laws touch upon procedural mechanisms. A perfect example may be rules which provide for obligation to inform third person about a dispute and its resolution. Under these rules one of the parties to arbitration may be obliged to serve this third person with a notice of arbitration. It may face nearly insurmountable obstacle which is consent requirement when consent of one of the parties to the arbitration or third person is lacking. Litigation may be better adjusted to this substantive law background. Thus, arbitration laws and arbitration rules shall take into account the existence of the substantive rules which exert a real influence on dispute resolution mechanisms and touches upon its efficacy and it is a challenge to resolution of international disputes. Some of arbitration laws and rules already contain broad regulation of third party joinder and intervention mechanisms. Permanent development of these mechanisms is of the highest importance and research on it as well in order to address the needs of international commercial reality.

2 The Very Existence of an Arbitral Award as a Part of Factual Circumstances Relevant under Substantive Law Provisions

The very existence of a decision or an award regarding particular claim may be a sole prerequisite of certain legal effect. It is so-called effect of facts of the case or fact determining effect of a decision (in German "*Tatbestandswirkung*")[3] when a state court decision or an arbitral award is the element of factual circumstances described in a hypothesis of a substantive legal provision which connects particular consequences with the very existence of this award. For instance, under Art. 375(2) Polish Civil Code existence of a decision in favor of one of the joint and several debtors other joint and several debtors based on a plea common to all joint and several debtors makes all of them free of their obligation.[4] The question arises whether situation shall be different in case of an arbitral award in favor of one of the joint and several debtors if other debtors are absent in arbitration in which this award was rendered. It shall be decided taking into account particular substantive law provision which derives some consequences from the existence of the previous award. For instance, Art. 375(2) Polish Civil Code seems to make no difference between prescribed effect of state court decisions and arbitral awards.[5]

One may state that an arbitral award may be used in the subsequent arbitration or litigation proceedings as an element of factual circumstances - as in the example discussed above - only after a declaration of its recognition or enforcement by a competent state authority. Moreover, when this subsequent dispute is also submitted to arbitration further question may arise, i.e. whether in international cases it is still necessary to prove recognition and

3 BREKOULAKIS, Stavros. *Third Parties in Arbitration.* New York: Oxford University Press, 2010. p. 73.

4 For opposite solution see e.g. Art. III-4:112.1 *Principles, Definitions and Model Rules of European Civil Law. Draft Common Frame of Reference (DFCR)* [online]. Munich: Sellier European Law Publishers, 2009 [cit. 2015-10-19] ("DFCR") which provides that „a solidary debtor may invoke against the creditor any defence which another solidary debtor can invoke, other than a defence personal to that other debtor. Invoking the defence has no effect with regard to the other solidary debtors".

5 See decision of Sąd Najwyższy, Poland of 5 December 2005, No. II CK 705/2004 where the court indicates that "an award" in Art. 375(2) Polish Civil Code means *inter alia* an arbitral award.

enforcement of an arbitral award and in which country shall this recognition and enforcement be granted in order to use this previous arbitral award in the subsequent arbitration.

The first issue shall be decided accordingly to the provision of law being source of the discussed effect of an arbitral award, i.e. the law applicable to the merits of the dispute at stake in this subsequent arbitration. This provision will be decisive with respect to the type of a decision or an award which produces discussed effect. However, usually such a recognition or enforcement of an arbitral award will be required (as it is for instance under Art. 375(2) Polish Civil Code). When it comes to the second question possible solutions may be various: the country of the place of the subsequent arbitration, the country whose law is applicable to the merits of the dispute (the country of *legis causae),* the country of origin of the previous arbitral award or the country whose law is applicable to an arbitration agreement. One shall notice that this is not a problem of a law applicable to the effects of an international arbitral award.[6] This issue does not raise, in my opinion, any serious doubts since the discussed effect is conferred on arbitral award by the particular provision of the substantive law applicable to the merits of a dispute and is not necessarily subject to the same applicable law as other effects of an arbitral award in general and effects upon a third party. However, the issue discussed here is in some way connected with the topic of recognition and enforcement of the arbitral award because substantive law provision stating facts of the case effect will often require a declaration of recognition or enforcement of an arbitral award.[7]

In my opinion, recognition or enforcement in the country whose law is applicable to the merits of a dispute at stake usually will be irrelevant. It would be sometimes the only purpose of filing a request for recognition or a declaration of enforcement of an arbitral award by authorities of this country and the dispute could have no other connecting factors with the territory of this country. The conclusion could be opposite if the substantive law providing for the effect discussed here would directly provide that only arbitral award

6 On this isse see e.g. BREKOULAKIS, Stavros. *Third Parties in Arbitration.* New York: Oxford University Press 2010. p. 266 - 269.

7 Similarly as in case of state court decisions. See WEITZ, Karol. Skutki uznania zagranicznego orzeczenia. *Przegląd Sadowy.* 1998, No. 9, p. 75.

recognized in the country of this law has this effect. Recognition or of enforcement of an arbitral award by a competent authority of the country of the seat of the subsequent arbitration in which one of the parties is willing to use this previous award seems a bit more suitable, albeit it is often emphasized that international commercial arbitration has no such forum as state courts. Thus, in a phase of arbitration proceedings the existence of an arbitral award in view of law of the country of the seat of the arbitration is relevant only as much as its existence in any other country.

Moreover, even with respect to the effect of facts of the case of state court decisions its recognition in the country other than the country of law applicable to the merits of the dispute is, according to some authors, irrelevant unless this is the same country and the decision is a foreign one.[8] The same arguments will apply to the role of recognition or enforcement in the country of origin of an award having facts of the case effect. Weakness of the connection between the arbitral award and the law of the state of its origin is visible under New York Convention[9] regime.[10] Thus, from arbitrators perspective it is even less relevant than recognition or enforcement in the country of the seat of their arbitration. The legal order of the country whose law is applicable to the underlying arbitration agreement seems to lack legitimacy to interfere with the substantive law applicable to the merits of the dispute and determine indirectly legal consequences prescribed by this law. It is out of the scope of regulation of an arbitration agreement and law applicable to it. Thus, arbitrators will have to examine the substantive law applicable to the merits and check whether this law requires recognition

8 Similarly as in case of state court decisions. See WEITZ, Karol. Skutki uznania zagranicznego orzeczenia. *Przegląd Sadowy*. 1998, No. 9, p. 76 - 77.

9 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf ("New York Convention").

10 POPIOŁEK, Wojciech. The Effects of a Foreign Arbitral Award in Poland under the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. In HABDAS, Magdalena; WUDARSKI, Arkadiusz (eds.). *Festschrift fur Stanisława Kalus. Ius est ars boni et aequi*. Fraknfurt am Main: PETER LANG, 2010, p. 445 et seq.; OLECHOWSKI, Marcin. Prawo właściwe dla oceny skutków uznawanego międzynarodowego wyroku arbitrażowego. In OKOLSKI, Józef et al. (eds.). *Księga pamiątkowa 60-lecia Sądu Arbitrażowego przy Krajowej Izbie Gospodarczej w Warszawie*. Warsaw: 2010, p. 580 - 584.

or declaration of enforcement in a particular country, mainly in a country of this law. In case of the negative answer – in my opinion - decisive factor will be the significance of a connection between a dispute and the country of the law applicable to the merits of a dispute and the country of the seat of the arbitration in which the previous arbitral award is submitted by one of the parties invoking its facts of the case effect. In some instances it may be even plausible for arbitrators to accept and enforce fact determining effect of the previous arbitral award without declaration of recognition or enforcement of arbitral award by any competent state authority.

3 Obligation to Notify Third Person of Arbitration

Visible repercussions of consensual nature of arbitration in national arbitration laws and arbitration rules make arbitration sometimes imperfect from a perspective of substantive law to which litigation is *prima facie* better adjusted as a mean of multiparty and multi-contract disputes resolution. Thus, one shall take into account these substantive law ramifications in analysis of consent to arbitration requirement.

3.1 Sources of the Obligation

One of the parties to the arbitration agreement may be obliged to inform the third person about litigation of a particular dispute or even to join this third person to the proceedings. This obligation can have its source in a substantive law or in a provision of a contract between party to the dispute and this third person who will be at risk of bearing adverse consequences of an award in favor one of the original parties to the proceedings. There are some substantive law provisions which expressly provide for a right to participate in litigation or at least to be informed about it for a third party who has some interest in a way of conduct and outcome of the proceedings. In case of lack of such an express provision the same consequences may be derived from the general theory of law of obligations. The question arises whether such provisions do also apply to arbitration proceedings.

For instance, under Art. 573 Polish Civil Code a buyer is obliged to inform a seller about claims raised by a third person to the sold good and to join the seller to a proceedings initiated by such third person. Unless the buyer

does that, he may loose warranty remedies for legal defects. The seller will be free to prove that the outcome of litigation between the buyer and the third person could be different if he would participate in these proceedings.

Similarly, under Art. 884(1) Polish Civil Code a guarantor sued by a creditor is obliged to inform the debtor about a court proceedings initiated by the creditor and join him in these proceedings. Information for the debtor about creditor's claim against the guarantor shall contain request for joinder of the debtor to the proceedings.[11] When the debtor does not take part in the proceedings he loses the right to raise against the guarantor pleas which the latter could but did not raise against a creditor due to unawareness of them.

An obligation to serve a contractual partner with a notice of a dispute with another person and its forum may also have its source directly in a contract (e.g. in case of insurance and reinsurance contracts). Then discussed issues must be determined with respect to these contractual undertakings of the parties and third persons' (none of the parties to the agreement containing provisions being source of discussed obligation) awareness of these circumstances. They will be at least hints in interpretation process of the underlying arbitration agreement or agreements.

3.2 Exceptio male gesti processus

3.2.1 Does it Exist in Arbitration?

Exceptio male gesti processus is a plea which can be raised by a third person in litigation or arbitration with one of the parties to a previous litigation if this person was absent in this former proceedings. Then such third person is allowed to raise this plea and prove that the outcome of this previous litigation is incorrect and could have been different if the third person was allowed to participate in it and exert real influence on the conduct of the proceedings. Intervention effect and *exceptio male gesti processus* have its source in substantive law and may be raised even if procedural law does

11 See e.g. GOŁACZYŚNKI, Jacek. In GNIEWEK, Edward; MACHNIKOWSKI, Piotr (eds.). *Kodeks cywilny. Komentarz*. Warsaw: C.H. Beck, 2014, p. 1567 who indicates that under this provision the guarantor is obliged to inform the debtor not only about litigation with the creditor, but also about arbitration proceeding with the creditor as a claimant.

not contain its regulation as such.[12] Under many procedural regimes in order to avoid this plea parties to litigation can serve a third person with a notice of the proceedings and invite it to submit so-called "side intervention". As was presented above, sometimes parties to certain kinds of legal relationships are even expressly obliged by the substantive law to serve the third person with a notice of litigation or arbitration proceedings.[13] Background of this obligation is usually a strict interdependence of the legal situation of parties to a legal relationship (e.g. debtor and guarantor) with an another legal relationship between one of the parties and a third person. Procedural law provisions regulating the plea discussed here are directly applicable to litigation.[14] The question arises whether the same can apply to arbitration and whether the debtor can invoke the plea of *male gesti processus* in state court or arbitration proceedings subsequent to arbitration of a dispute between its creditor and other person (e.g. guarantor). Whenever the third party can be regarded as bound by the findings of the previous arbitral award rendered in its absence[15] and this effect has its source in substantive law provisions, the answer shall be affirmative but with necessary reservations ensuing mainly from contractual nature of arbitration.

By third party notice the party to the ongoing arbitration cannot automatically avoid successful raising of the described plea by the third party served with this third party notice. As in litigation, this notice should be made in adequate time and provide the third party with a real opportunity to participate in the arbitration proceedings and contribute to the findings of an arbitral

12 See GOŁĄB, Agnieszka. Przypozwanie w procesie cywilnym (art. 84-85 k.p.c.). *Polski Proces Cywilny*. 2012, No. 1, p. 118 who indicates *inter alia* that there was no regulation of *exceptio male gesti processus* in the previous Polish Code of Civil Procedure from 1930. Nonetheless the effects of third party notice were determined by reference to substantive law.

13 CZECH, Bronisław. In MARCINIAK, Andrzej; PIASECKI, Kazimierz (eds.). *Kodeks postępowania cywilnego. Tom I. Komentarz art. 1-366*. Warsaw: C.H. Beck, 2014, p. 343.

14 On the effect of joinder in case of recognition or enforcement of foreign state court award see WEITZ, Karol. Skutki uznania zagranicznego orzeczenia. *Przegląd Sądowy*. 2006, No. 6, p. 78 et seq.

15 See BREKOULAKIS, Stavros. *Third Parties in Arbitration*. New York: Oxford University Press 2010. p. 260.

panel.[16] One shall stress that the scope of the effect of third party notice will be directly determined by the ramifications of third party participation granted to it by the original parties to the arbitration proceedings. Thus, content of the underlying arbitration agreement, including applicable arbitration rules, with respect to third parties participation in arbitration and a capacity in which they can appear in it will be decisive.

In case of lack of the notice of arbitration third person will be free to raise the plea of *male gesti processus* in subsequent litigation or arbitration proceedings. Certain legal provisions – such as Art. 82 Polish Code of Civil Procedure[17] – only restricts this plea and its general source is not directly expressed in procedural law. Furthermore, it is at least disputable whether this provision may be in any way applicable to arbitration. This plea is ensuing from substantive law which provides for the obligation to inform third persons about a dispute and its resolution. That is why this substantive law shall be examined in order to determine whether this information is also required with respect to an arbitration covering a particular dispute. Under this assumption it seems reasonable to allow the third person to raise *exceptio male gesti processus* to overcome third party effects of an arbitral award issued in arbitration in which this third person did not participate due to lack of information about the pending arbitration or permission for joinder.

3.2.2 Objection of the Opposite Party to the Ongoing Arbitration to the Request for Third-party Joinder

Since an arbitral tribunal is not bound by rules regulating proceedings before state courts, intervention or third party joinder mechanism shall be exercised accordingly to applicable arbitration law and arbitration rules in conjunction with the arbitration agreement. Regulation of intervention and joinder is still not common in national arbitration laws. Most of arbitration rules provides for intervention and joinder only when the original parties expressed their consent to it and usually third person is not allowed

16 See e.g. Decision of Oberster Gerichtshof, Austria of 1 October 2008, No. 6 Ob 170/08f and a comment to this decision published by BRANDSTATTER, Jurgen. Binding Nature and Fact Determining Effect of an Arbitral Award. *Arbitration News* [online]. 2009, Vol. 14, No. 2 [cit. 2015-10-15], p. 14 - 15.

17 POLAND. Act of 17 November 1964, Code of Civil Procedure. Official Journal 1964, No. 43, Item 296.

to appear in arbitration in a capacity other than a party. Moreover, obviously a confidentiality of arbitration may be a serious obstacle for the parties to inform the third person about the dispute or the ongoing arbitration.[18]

However, under particular circumstances of the case at stake the underlying arbitration agreement and its provisions – when it exclude third party notice - may be regarded as a tool to deprive the third person of a right to be informed about a dispute and to participate in its resolution. In such scenarios it may even occur that there was a collusion in that regard between the original parties to the arbitration.

Most of rules allowing joinder of a third party impose consent of all the original parties to the arbitration for the joinder to be allowed. When the party obliged to serve third person with a notice of a dispute resolution with another person submits this dispute to arbitration, it may be reasonable to say that this party should bear a risk of the opposite party's objection to joinder and consequences of absence of the third person in the arbitration.

One shall raise the question whether the opposing party is always free to effectively object to joinder when relevant provisions do not allow joinder in case of such objection. Before signing an arbitration agreement covering particular type of a dispute the parties to this agreement will be often aware of the obligation to inform the third person about the fact that dispute has arisen or about the litigation concerning it. Shall an arbitral tribunal permit joinder notwithstanding the objection to it raised by one of the parties?

The answer could be affirmative if under particular arbitration law or arbitration rules a consent for joinder or intervention may be declared before a motion for joinder or intervention is submitted. Then the parties' awareness may be an argument used in the process of interpretation of the underlying arbitration agreement, including tacit consent to application of joinder and intervention mechanisms. But then the scope of the consent shall be subject to a very careful examination and the burden of proof shall be on the party wishing the third person to be joined and on this third

18 STEINGRUBER, Andrea, M. *Consent in International Arbitration.* Oxford: Oxford University Press, 2012. p. 166.

person. When consent is to be explicitly declared after the request for joinder or intervention is submitted, the objection to it raised by one of the parties will be a serious, practically insurmountable obstacle to joinder and intervention.

However, even then it can be argued, in some special scenarios, that this objection is a manifest abuse of process. One shall stress that party autonomy shall not be used by the parties to arbitration proceedings in order to subject arbitration to obstructive and dilatory tactics which would undermine main goal of arbitration, i.e. effective dispute resolution. It may *de facto* deprive these parties of their real party autonomy which was exercised in the arbitration agreements concluded in order to submit dispute to final and binding dispute resolution. Nonetheless, in case of objection discussed here permission for joinder or intervention seems very improbable. Arbitrators derive their power from parties' consent to submit dispute to arbitration. Their actions contrary to the exact will of the parties shall be extremely well-founded. Awareness of the obligation to join the third person to the dispute resolution shall not be the sole reason for permitting joinder of the third party when the objection to it is raised by one of the original parties to the arbitration. It shall be at least highly substantiated that the party to whom the third person could be joined would be deprived of its rights in case of dismissal of a motion for joinder or intervention. One shall bear in mind that the main aim of side intervention is a protection of a legal interest of an intervening person.[19]

However, this person brings also help to a party to whom has acceded. The party to the arbitration proceedings can substantiate that participation of the third person is necessary to present its case,[20] e.g. by submission of evidences in third person's possession and other efforts aimed to reveal

19 KLIMKOWICZ, Jan. *Interwencja uboczna według Kodeksu postępowania cywilnego*, Warsaw: Wydawnictwo Prawnicze, 1972. p. 11 - 13.

20 STRONG, Stacie, I. Intervention and Joinder as of Right in International Arbitration: Infringement in Individual Contract Rights or a Proper Equitable Measure? *Vanderbit Journal of Transnational Law* [online], 1998. Vol. 31 [cit. 2015-10-15], p. 982 – 983 who indicates that joinder may be seem to be necessary to "present one's case" in the meaning of Art. V(1)(b) New York Convention. Cf. KURKELA, Matti S.; TURUNEN, Santtu; Conflict Management Institute (COMI). *Due Process in International Commercial Arbitration*. New York: Oxford University Press, 2010. p. 186 - 187.

all relevant factual circumstances of the case. Furthermore, one of the original parties to the arbitration may have clear legal interest in third party notice simply because it is willing to a gain legal effect of the arbitral award preventing this third person from raising *exceptio male gesti processus* in subsequent arbitration or litigation or some similar effect.

3.2.3 Objection of a Third Person to its Joinder to the Ongoing Arbitration

Third person invited to join arbitration proceeding cannot be forced to do it if it is not bound by the arbitration agreement in any way. It is *prima facie* not plausible to draw any legal consequences against this person for being absent in arbitration proceedings to which this person has never consented.[21]

Third person who rejects an invitation to join litigation loses at the same time its right to invoke a plea of *male gesti processus* in subsequent proceedings. However, litigation is not based on consent of parties to it as arbitration is. When third person is not bound by the underlying arbitration agreement in any way (it is a third party *sensu stricto),* then it seems reasonable to state that the outcome of the arbitration shall not be binding for this person in a sense discussed here even if the original parties served this person with the notice of arbitration and granted it the possibility to join the arbitration proceedings. Then in the subsequent proceedings – litigation or arbitration – such third person shall usually be free to prove that previous arbitral award is based on incorrect assumptions notwithstanding its recognition or enforcement by competent authority by which it is equated to a domestic judgement in terms of its effects. And this shall almost always be true. However, one shall take into account that before expressing consent to an agreement which creates a legal relationship interrelated with another legal relationship the parties to this agreement are often aware of the arbitration agreement covering disputes arising out of this interrelated legal relationship. Then it shall be decided after case-by-case analysis whether this awareness indicates consent of parties to the agreement to be joined

21 Cf. BREKOULAKIS, Stavros. *Third Parties in Arbitration.* New York: Oxford University Press 2010, p. 256 - 257.

to arbitration covering disputes arising out of this another strongly interrelated legal relationship. Level of interrelatedness will be an important hint in this analysis.

One shall stress again that certain substantive law rules regulating third party notice and its binding effect on third persons are not inevitably limited to litigation. Thus, they may be source of an obligation to servethird person with a notice of arbitration. However, they do not automatically remove a requirement of consent for joinder of the third party or its intervention. It is for the parties to provide concerned third person with a real opportunity to participate in arbitration in order to gain binging effect upon this third person. This real opportunity usually will mean not only a sole permission for joinder or intervention.

The effort of the third person – mainly logistic and financial – which may be caused by possible participation in arbitration will be also an element of the real opportunity test and a hint in third person's consent determination. The scope of this consent will be limited to participation in proceedings which might have been expected by the third person.

Furthermore, this determination shall be made with additional elements taken into consideration when the source of legal relationship between the third person and one of the parties to the arbitration is other than contract or unilateral judicial act of this third person, e.g. tort. Then consent of the third person to participate in arbitration as a result of joinder may be derived only from express act of will of this third person or shall be at least manifestly implied. However, in this analysis the existence of substantive law rules or contractual grounds of obligation of the parties to the arbitration agreement to serve the third person with a notice of the dispute and its resolution and third persons' awareness of it will be of the highest importance.

Furthermore, one shall ask whether the third person who has never consented to be a party to arbitration may be obliged to take part in it in a capacity of a side intervenor. From the opposite point of view, does the lack of consent of the third person to participate in arbitration of a particular dispute in a capacity of so-called full-party automatically and with no exceptions

make this person free to object to participation in this arbitration in a capacity of side intervenor with no consequences? Generally the answer should be affirmative.[22]

But there can be some scenarios in which this result will be manifestly unjust. This may be in case of the strong interdependence of legal situation between one of the parties to the arbitration and third person served with a notice of this arbitration ensuing from the interrelation of their legal relationship with the legal relationship between parties to the ongoing arbitration. When participation in arbitration would not cause any special effort for this third person, raising a plea of *male gesti processus* in the subsequent litigation or arbitration with one of the parties to the previous arbitration as the opponent can be treated as an abuse of process. Thus, the question arises whether parties willing to submit their dispute to arbitration shall be indirectly limited in exercising their party autonomy because of the interest of concerned third persons in their dispute resolution. If they will submit the dispute to arbitration they will have to bear a risk of third party objection to its joinder even if this objection is be based only on this third person's mere convenience notwithstanding substantive background of legal relationships between all the concerned parties and their obligations. One shall emphasize that by an arbitration agreement parties to it submit their dispute or disputes to arbitrators' competence and third party participation in arbitration in a capacity another than so-called party cannot be equated with that. Thus, difference between consent to arbitration expressed in an arbitration agreement shall be differentiated from a consent to participate in arbitration as such.[23] The latter one may be limited to the third party's appearance in arbitration as a side intervenor or in a similar capacity and it does not

22 See e.g. DORDA, Christian; ÖHLBERGER, Veit. Commentary. Vienna Perspective – 2010. *MEALEY's International Arbitration Report* [online]. 2010, Vol. 25, No. 3 [cit. 2015-10-15], p. 4 - 5 and a commentary the rein on docket of the Oberster Gerichtshof, Austria of 1 October 2008, No. 6 Ob 170/08f.

23 Cf. KIM, Keechang; MITCHENSON, Jason. Voluntary Third-Party Intervention in International Arbitration for Construction Disputes: A Contextual Approach to Jurisdictional Issues. *Journal of International Arbitration*. 2013. Vol. 30, No. 4, p. 428. Authors aptly underline – with no reference to any set of arbitration rules - that third party participating in arbitration in a capacity other than so-called full-party does not present any of its claims or defences. They indicates that the most important issue will be the answer to the question how deeply interwined is third party with the main dispute.

necessarily mean "assent to arbitration" discussed in the literature. Then, in my opinion, to analyze discussed issues from the perspective of a contractual nature of arbitration one shall bear in mind this nuance and accordingly differentiate particular scenarios.

Kim and *Mitchenson* indicate that: "*The scope of the award (assuming the third party is permitted to intervene) would not cover the dispute, if any, between objecting contracting party and the intervening third party. As usual, the award will only determine the dispute between the contracting parties. However, the binding force of the award will be extended not only to the parties to the arbitration agreement but also to the parties who are willing to be bound by it (the voluntary third party and the inviting party).*"[24]

This effect obviously cannot be seen wider than in case of third party notice or third party intervention in litigation. Thus, usually it will meet the limits discussed above and will be open to the effective *exceptio male gesti processus*. If the third party will not successfully invoke this plea the arbitral award will be binding in relationship between the third person and the party to whom this person acceded in arbitration or who served this third person with a notice of arbitration. However, the scope of this effect will be limited to the sentence and factual basis of the arbitral award relevant in both disputes, i.e. between the parties to the previous arbitration and between third party and of these parties.[25]

4 Conclusion

Many issues may be touched upon with respect to the participation of third parties in arbitration. Core issue is obviously a determination of a scope of entities bound by an arbitration agreement. However, procedural mechanisms granting third parties possibility to take part in arbitration proceedings and consequences of their participation and non-participation in it should be explored as well.

Many problems can be solved in a quite similar manner as in litigation, albeit not all of them. There are boundaries arising out of the contractual nature

24 KIM, Keechang; MITCHENSON, Jason. Voluntary Third-Party Intervention in International Arbitration for Construction Disputes: A Contextual Approach to Jurisdictional Issues. *Journal of International Arbitration.* 2013. Vol. 30, No. 4, p. 428.

25 GOŁĄB, Agnieszka. Przypozwanie w procesie cywilnym (art. 84-85 k.p.c.). *Polski Proces Cywilny.* 2012, No. 1, p. 119.

of arbitration, nature of an arbitral award and mechanism of its recognition and enforcement etc. After all, the outcome of the arbitration is a part of legal world and an arbitral award needs to have its place in it. Non-participation of concerned persons in arbitration proceedings may induce particular problems regarding scope of a binging force of the arbitral award. At least one of the parties to the arbitration may be interested in pursuing its own rights against the third persons after arbitration and shall be able to do it without unnecessary obstacles and delay. Then effects of previous arbitration may be of high importance in forthcoming litigation or arbitration. Thus the effects of non-participation of the third persons in arbitration shall be analyzed also from point of view presented in this paper.

As arbitration becomes more and more adjusted to cover multiparty and multi-contract disputes, mechanisms of third party joinder and intervention in arbitration will be developed and ramifications ensuing from contractual nature of arbitration will be inevitably slightly relaxed. In my opinion, any *de lege ferenda* discussions shall take into account differentiation of the capacities in which third persons can appear in litigation and subtle differentiation between consent to be a party to an arbitration and a consent to participate in an arbitration in a capacity other than a party. I am far from negating the importance of party autonomy and consent requirement in arbitration. However, its scope shall be deeply explored to respect justified expectations of the parties to all legal relationships at stake in a particular scenario and values comprising a good administration of justice, including efficiency of dispute resolution. The diversity of arbitration scenarios and its substantive law background calls for a more and more nuanced approach to determination of consent to the participation in arbitration proceedings in a capacity other than so-called full-parties.

This paper does not absolutely even aspire to be comprehensive. There are many issues which can be subject to further analysis, *inter alia* the issue of the third party's possibility to obtain an arbitral award to realize the so-called effect of facts of the case (especially in light of confidentiality of arbitration), the issue of declaration of recognition or enforcement of a previous arbitral award in order to use it in a subsequent litigation or arbitration

proceedings against a third party who objected to its joinder during the previous arbitration proceedings and the set of issues regarding nomination of arbitrators,[26] confidentiality etc.

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[26] For very broad review of arbitration laws and arbitration rules on this issue see UGARTE, Ricardo; BEVILACQUA, Thomas. Ensuring Party Equality in the Process of Designating Arbitrators in Multiparty Arbtiration: An Update on the Governing Provisions. *Journal of International Arbitration*. 2010, Vol. 27, No 1, p. 9 - 49.

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SOME ASPECTS OF INTELLECTUAL PROPERTY DISPUTES AND THE QUESTION OF ARBITRABILITY

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Abstract

Intellectual property disputes have become an actual issue thanks to the technological progress. The possibility of solving dispute with an alternative dispute resolution e.g. arbitration is even more appealing. The diversity of the intellectual property rights is raising the question of arbitrability which has already initiated many expert discussions. This paper is focused on examination of current perception on arbitrability of intellectual property disputes in international arbitration and questions which can be created by arbitrability. The main obstacles are especially disputes concerning validity and the moral rights. Both, however, can be found arbitrable by the restrictive usage of the international public policy and by referring to the inter partes effect of the award.

Keywords

Arbitrability; Intellectual Property Disputes; Moral Rights; Public Policy; Validity Disputes.

1 Introduction

Besides the ordinary state judicial system, parties of the cross-border contractual relationships have another possible way of settling their disputes – arbitration. Arbitration spreads wide into various areas of law. The remarkable field for arbitration is intellectual property ("IP") law. Because the extent of IP arbitration is wide the scope of this paper has to be reduced to several aspects. Therefore, this paper will focus only on aspects of arbitrability.

The main aim is to reconsider and analyse the question of arbitrability of IP disputes mainly from the view of public policy, enforcement stage, *inter partes* effect of arbitral award and development of arbitrability issue in patent validity disputes.

The nature of IP rights should be taken into consideration while examining the arbitrability problems of IP disputes. The arbitration of registered IP rights faces especially the problem of the arbitrability of validity disputes, particularly the validity of patent. They are usually granted by the state authority.[1] The arbitration of unregistered rights does not create serious difficulties except for the moral rights.[2] These issues will be addressed in the paper.

2 Arbitrability in General

At the beginning it is important to take a look at the notion of arbitrability in general. The arbitrability basically means that "*the subject-matter… is capable of being resolved by arbitration*".[3] Examination of the subject-matter is the so called objective arbitrability which will be the main object of my interest.

For the sake of completeness it must be stated that the academic world distinguishes between the objective and subjective arbitrability. The subjective arbitrability does not create any serious issues. It is only upon the parties if they want to restrict something which is clearly part of objective arbitrability.[4] There is also another understanding of the notion of subjective arbitrability. Under this understanding the subjective arbitrability means the capacity of public authorities to be the parties of arbitration agreements.[5]

1 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration*. Alphen aan den Rijn: Kluwer Law International, 2010. p. 12 - 14.

2 MANTAKOU, P. Anna. Arbitrability and Intellectual Property Disputes. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives*. Alphen aan den Rijn: Kluwer Law International, 2009. p. 266.

3 FOUCHARD, Philippe; GAILLARD, Emmanuel; GOLDMAN, Berthold; SAVAGE, John ed. *Fouchard, Gaillard, Goldman on International Commercial Arbitration*. The Hague: Kluwer Law International, 1999. p. 312.

4 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Praha: ASPI, 2008. p. 116.

5 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Praha: ASPI, 2008. p. 116; FOUCHARD, Philippe; GAILLARD, Emmanuel; GOLDMAN, Berthold; SAVAGE, John. *Fouchard, Gaillard, Goldman on International Commercial Arbitration*. The Hague: Kluwer Law International, 1999. p. 312 - 313.

However, the arbitrability of IP disputes is interesting mainly from the view of objective arbitrability because subjective arbitrability is an expression of party autonomy and parties only narrow the objective arbitrability. Nonetheless, the objective arbitrability of IP disputes is not unlimited.

Although it is impossible to make general conclusion about arbitrability common for all states, the comparison of national laws enables us to present "the list" of areas where the arbitrability is questionable or not. Usually the disputes concerning economic interests are capable of being solved by arbitration.[6]

The arbitration is characterized by party autonomy which is evident from the arbitration agreement. Parties can also influence several aspects of arbitration, at least by the determination of *lex arbitri*.[7] However, parties do not have the full power over arbitrability and as *Steingruber* states: *"Inarbitrability is a limitation of parties' freedom to consent to arbitration."*[8]

2.1 View of Doctrine

The question of arbitrability can be answered by different arbitration doctrines. The first one creates arbitration as an independent proceeding without any connection to the specific legal order.[9]

But probably the more realistic approach is linking the arbitration to some legal order.[10] As the jurisdictional doctrine states, the arbitration can be linked to at least two national laws: *lex arbitri* and law of the place of enforcement. Other potential related legal orders are the applicable law for the arbitration agreement or for the party of the arbitration agreement.[11]

6 FOUCHARD, Philippe; GAILLARD, Emmanuel; GOLDMAN, Berthold; SAVAGE, John. *Fouchard, Gaillard, Goldman on International Commercial Arbitration.* The Hague: Kluwer Law International, 1999. p. 339; BLACKABY, Nigel; PARTASIDES, Constantine; REDFERN, Alan; HUNTER, Martin. *Redfern and Hunter on International Arbitration.* 5th ed. Oxford: Oxford University Press, 2009. p. 123.

7 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku.* Praha: ASPI, 2008. p. 98 and 114.

8 STEINGRUBER, Andrea Marco. *Consent in International Arbitration.* Oxford: Oxford University Press, 2012. p. 40.

9 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku.* Praha: ASPI, 2008. p. 57.

10 *Ibid.,* p. 117.

11 BLACKABY, Nigel; PARTASIDES, Constantine; REDFERN, Alan; HUNTER, Martin *Redfern and Hunter on International Arbitration.* 5th ed. Oxford: Oxford University Press, 2009. p. 124.

Issue of arbitrability usually arises in several situations: during the process of arbitration when the party raises the question, when tribunal itself considers the question or when the party tries to enforce the award.[12] The paper is focusing mainly on the term public policy used during the enforcement of an award.

2.2 Arbitrability and Public Policy

It is inevitable to clash with the term of public policy while examining the arbitration itself. In the traditional international arbitration doctrine, the inarbitrability of the dispute is connected with the violation of public policy. Although *Brekoulakis* is trying to show that the linkage of arbitrability and public policy is becoming obsolete, he admits that public policy is still present in the question of arbitrability.[13] It supports the opinion that the concept of public policy is fundamental for arbitrability, especially in the IP law. At least, the public policy argument cannot be just put aside without deeper consideration.

Public policy is the term full of obscurity, but that is typical for general terms as such. Therefore, it is possible to distinguish three different terms: national public policy, international public policy and transnational public policy.[14] All of them can somehow affect the process of arbitration and arbitrability itself. National public policy, as was already mentioned above, comes out from the connection of arbitration to the law of particular state. It is important from the view of binding award which will be enforceable. This is supported also by the wording of the New York Convention.[15] From the application of "national" public policy under the New York Convention the term of international public policy

12 HANOTIAU, Bernard. The Law Applicable to the Issue of Arbitrability. *International Business Law Journal* [online]. 1998, No. 7 [cit. 2015-03-05], p. 756.

13 BREKOULAKIS, L. Stavros. On Arbitrability: Persisting Misconceptions and New Areas of Concern. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives.* Alphen aan den Rijn: Kluwer Law International, 2009, p. 21 - 23.

14 SEELIG, Marie Louise. Notion of Transnational Public Policy and Its Impact on Jurisdiction Arbitrability and Admissibility. *Annals of the Faculty of Law in Belgrade International Edition* [online]. 2009, No. 3 [cit. 2015-03-05], p. 119.

15 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL).* Available from: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention.html.

was created. International public policy is narrower and includes mainly fundamental parts of public policy. And finally, the transnational public policy is not connected with any state law or legal order.[16]

Although the idea of transnational public policy is very attractive, especially for the purpose of arbitrability, the New York Convention as a very useful international instrument represents the basis for using the international public policy in the narrow way. Arbitrability of the international validity disputes of IP is thus in relations with international public policy. The reason why the IP disputes have been connected with the issue of public policy can be found in the concept itself. Public policy e.g. from the view of the Art. V(2)(b) New York Convention usually represents the fundamental principles in the specific area of law.[17] The public policy argument has been used against the arbitrability of IP disputes because some aspects of IP law (notably patents) are connected with the state power. Therefore, the state power insures the protection of IP rights and the state or the state organ solely should be settling IP disputes.[18]

3 Intellectual Property Disputes and Arbitration

The arbitration of IP disputes has basically the same advantages as for other areas of law: speed of proceedings, the neutral decisive organ, maintenance of existing legal relationship and expertise. Actually, high level of expertise can be the biggest advantage for the parties of the IP dispute.[19]

There was always a suggestion which had questioned the arbitrability of IP rights in general.[20] According to such an opinion the IP law requires

16 SEELIG, Marie Louise. Notion of Transnational Public Policy and Its Impact on Jurisdiction Arbitrability and Admissibility. *Annals of the Faculty of Law in Belgrade International Edition* [online]. 2009, No. 3 [cit. 2015-03-05], p. 119 - 122.

17 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Praha: ASPI, 2008. p. 334.

18 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 62 - 63; ROHN, Patrick; GROZ, Philipp. Drafting Arbitration Clauses for IP Agreements. *Journal of Intellectual Property Law & Practice* [online]. 2012, Vol. 7, No. 9 [cit. 2015-03-05], p. 653.

19 JURAS, Camille. *International Intellectual Property Disputes and Arbitration: A Comparative Analysis of American, European and International Approaches: the Search for an Acceptable Arbitral Site* [online]. Diploma thesis, McGill University, 2003 [cit. 2015-03-05], p. 24 - 30.

20 CELLI, L. Alessandro; BENZ, Nicola. Arbitration and Intellectual Property. *European Business Organization Law Review* [online]. 2002, Vol. 3, No. 3 [cit. 2015-03-05], p. 596 - 597.

a special approach which is not consistent with the alternative dispute resolution idea e.g. arbitration.[21] Alternative dispute resolutions represent the effort to resolve the dispute without the interference of state power and prefer to find a solution within the interest of parties.[22] However, IP rights are not automatically solely under the will of the parties and without the state or court interference.[23]

However, barrier between IP disputes and arbitration broke down and parties of IP disputes started to use arbitration.[24] For *Garcia* and *Cook* the problem of arbitrability in IP disputes is surpassed and without the great support, especially in international arbitration.[25] Although many areas of IP law are now considered arbitrable, the question of arbitrability still hangs over the arbitration as a sword of Damocles.

The registered IP rights create difficulties because they somehow require the recognition of the state power.[26] To be precise, not all disputes concerning registered IP rights raise the arbitrability issue. The disputes of contractual nature are arbitrable without hesitation.[27]

As was stated in the introduction, the question of arbitrability is still opened for the validity disputes of registered rights and the disputes concerning moral rights.[28] For example, registered patent rights are granted by the state

21 CARON, D. David. World of Intellectual Property and the Decision to Arbitrate. *Arbitration International* [online]. 2003, Vol. 19, No. 4 [cit. 2015-03-05], p. 441; MANTAKOU, P. Anna. Arbitrability and Intellectual Property Disputes. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (eds). *Arbitrability: International & Comparative Perspectives.* Alphen aan den Rijn: Kluwer Law International, 2009, p. 263 - 265.

22 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Praha: ASPI, 2008. p. 12 - 13.

23 MANTAKOU, P. Anna. Arbitrability and Intellectual Property Disputes. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (eds). *Arbitrability: International & Comparative Perspectives.* Alphen aan den Rijn: Kluwer Law International, 2009, p. 265.

24 CARON, D. David. World of Intellectual Property and the Decision to Arbitrate. *Arbitration International* [online]. 2003, Vol. 19, No. 4 [cit. 2015-03-05], p. 441.

25 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 52.

26 BLACKABY, Nigel; PARTASIDES, Constantine; REDFERN, Alan; HUNTER, Martin. *Redfern and Hunter on International Arbitration.* 5th ed. Oxford: Oxford University Press, 2009. p. 125

27 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 52.

28 MANTAKOU, P. Anna. Arbitrability and Intellectual Property Disputes. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives.* Alphen aan den Rijn: Kluwer Law International, 2009, p. 266 - 267.

or an assigned authority.[29] As for the unregistered rights, they do not need the state recognition for their existence.[30] However, the moral rights as a part of copyright represent a non-economic aspect of IP right or can be understood as a personality right.[31] Moral rights are considered arbitrable in some national laws because parties are able to contractually operate with its exercise. Also moral rights can be considered so closely connected with the economical aspect of IP rights that it should be arbitrable. One interesting Canadian case, mentioned by *De Werra*, also comprises the question of arbitrability of moral rights. In this case it was stated that even when the Canadian law does not allow the arbitrability of moral right, it is not the part of its public policy.[32] Then, arbitrability of moral rights should not be a major obstacle in the international arbitration. The application of national and international public policy and what is included in these terms is important not only for moral rights but also for other questionable arbitrable IP matters which can be inspired by this ruling. Those ideas can be useful also for the analysis of inarbitrability of validity disputes.

Although the cases in which the question of arbitrability would arise are rare and the problem of the arbitrability of IP rights is not the most relevant,[33] it is still important to have a look at several possible situations in which the arbitrability can cause the concern e.g. enforcement of the award, usage of international public policy. Those situations will be presented below.

For the sake of completeness, it should be noted that some states as France, Switzerland or Germany have changed the position from the total

29 ČADA, Karel. Patenty, vzory a know-how. In HORÁČEK, Roman; ČADA, Karel; HAJN, Petr. *Práva k průmyslovému vlastnictví*. Praha: C.H. Beck, 2005, p. 156 - 157.

30 CELLI,L. Alessandro; BENZ, Nicola. Arbitration and Intellectual Property. *European Business Organization Law Review* [online]. 2002,Vol. 3, No. 3 [cit. 2015-03-05], p. 595.

31 ADENEY, Elizabeth. *The Moral Rights of Authors and Performers: An International and Comparative Analysis*. Oxford: Oxford University Press, 2006. p. 1 - 3.

32 DE WERRA, Jacques. Arbitrating International Intellectual Property Disputes: Time to Think beyond the Issue of (Non-)Arbitrability. *International Business Law Journal* [online]. 2012, No. 3 [cit. 2015-03-05], p. 301 - 302; MANTAKOU, P. Anna. Arbitrability and Intellectual Property Disputes. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives*. Alphen aan den Rijn: Kluwer Law International, 2009. p. 266 - 267.

33 ROHN, Patrick; GROZ, Philipp. Drafting Arbitration Clauses for IP Agreements. *Journal of Intellectual Property Law & Practice* [online]. 2012, Vol. 7, No. 9 [cit. 2015-03-05], p. 653; COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration*. Alphen aan den Rijn: Wolters Kluwer, 2010, p. 51 - 52.

inarbitrability of IP validity disputes to full acknowledgment of arbitrability (Switzerland), partial arbitrability of validity disputes (France) or rather conservative approach (Germany). But the position of the states is not unified.[34]

4 Public Policy and IP Disputes

The question of arbitrability can occur at the different stages of the arbitration and be examined from the perspective of different subjects.[35]

First situation and also frequent argument against the problem of arbitrability is that parties decide to submit their dispute to the tribunal. If they consentingly agreed on use of this alternative dispute resolution, they will also act for the sake of enforcement.[36]

Another situation or the way how to look at the arbitrability is the view of arbitrator. Is it compulsory for arbitrator to examine the arbitrability? And if, which legal order should be used?[37] Here is a conflict of different doctrines, which connect the arbitration with the legal order or see the arbitration totally unlinked with any legal order. In the case of latter, the arbitrator would probably use the transnational public policy for the determination of arbitrability.[38] However, the transnational public policy includes the most basic aspects of law. The transnational public policy represents the fundamental principles or values. It covers the real public jeopardy such

34 MANTAKOU, P. Anna. Arbitrability and Intellectual Property Disputes. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives*. Alphen aan den Rijn: Kluwer Law International, 2009, p. 267 - 269. For further information on different approach of countries according to type of IP rights see ADAMO R. Kenneth. Overview of International Arbitration in the Intellectual Property Context. *The Global Business Law Review* [online]. 2011, Vol. 2, No. 7 [cit. 2015-03-05], p. 16 - 18; JURAS, Camille. *International Intellectual Property Disputes and Arbitration: A Comparative Analysis of American, European and International Approaches: the Search for an Acceptable Arbitral Site* [online]. Diploma thesis, McGill University, 2003 [cit. 2015-03-05], p. 75 – 76.

35 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration*. Alphen aan den Rijn: Wolters Kluwer, 2010. p. 53 - 54.

36 ROHN, Patrick; GROZ, Philipp. Drafting Arbitration Clauses for IP Agreements. *Journal of Intellectual Property Law & Practice* [online]. 2012, Vol. 7, No. 9 [cit. 2015-03-05], p. 653.

37 HANOTIAU, Bernard. The Law Applicable to the Issue Of Arbitrability. *International Business Law Journal* [online]. 1998, No. 7, [cit. 2015-03-05], p. 763.

38 MAYER, Pierre. Effect of International Public Policy in International Arbitration. In MISTELIS, A. Loukas; LEW, D.M. Julian. *Pervasive Problems in International Arbitration*. Alphen aan den Rijn: Kluwer Law International, 2006, p. 62 - 63.

as international crimes.[39] Thus, the issue of validity of patents as the part of such a public policy is not considered as a part of a transnational public policy.

Finally at the stage of enforcement, the state court has to also consider the question of arbitrability. The New York Convention[40] enables court to decline recognition and enforcement, *inter alia*, in the situations governed by Art. V(2).[41] First situation comes, when the law of the state does not allow the arbitration settlement in disputes over such a subject-matter. The second situation is using the public policy of the state, where the parties seek the enforcement. Here comes the debate over the importance or even existence of public policy argument in arbitration. The existence of transnational public policy was presented above. Thus, the argumentation is related to international public policy.

Why is it important to consider the question of public policy in IP disputes? Because as was presented above, the issue of public policy and especially in the enforcement phase is capable of depreciation of arbitration as the only relevant and remaining issue. Has the discussion moved forward?

It is true that states use and interprets the term „public policy" narrowly.[42] Also the argument of inarbitrability which would lead to denial of enforcement under the New York Convention is rare.[43] Another reason to not to be „afraid" of public policy can be the opinion about its obsolescence and uselessness represents by *Brekoulakis*. *Brekoulakis* states that the argument

39 MAYER, Pierre. Effect of International Public Policy in International Arbitration. In MISTELIS, A. Loukas; LEW, D.M. Julian. *Pervasive Problems in International Arbitration*. Alphen aan den Rijn: Kluwer Law International, 2006, p. 63.

40 For the further examination of the relationship of arbitrability and the New York Convention see ARFAZADEH, Homayoon. Arbitrability under the New York Convention: the Lex Fori Revisited. *Arbitration International* [online]. 2001, Vol. 17, No. 1 [cit. 2015-03-05], p.73 - 87.

41 HANOTIAU, Bernard. The Law Applicable to The Issue of Arbitrability. *International Business Law Journal* [online]. 1998, No. 7 [cit. 2015-03-05], p.770 - 772.

42 CARON, D. David. World of Intellectual Property and the Decision to Arbitrate. *Arbitration International* [online]. 2003, Vol. 19, No. 4 [cit. 2015-03-05], p. 443.

43 DI PIETRO, Dominico. Arbitrability under the New York Convention. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives*. Alphen aan den Rijn: Kluwer Law International, 2009, p. 96.

of public policy is more about the procedural objection and the fair trial.[44] All reservations are common for any disputes in any area of law, so there is no reason to specially exclude some areas from the arbitration, otherwise arbitration can be forbidden in general.[45] All these arguments are directed against the public policy as the part of arbitrability. However, the IP disputes do not concern the state power just from the view of process or making decision or the lack of reasoning. The sensitive part of validity dispute is the state power which grants the patent and the influences on the third party.

From this view, there will always be the concern of public policy until all the states around the world include possibility of arbitration in this kind of disputes into their legislation. The arbitrability problem of validity disputes cannot be denied just because the public policy becomes less prominent thanks to its narrow interpretation or the arguments about its obsolence.

However, as our examined core is based on international arbitration, the argument of international public policy has the strongest position, which allows predicting full arbitrability of IP disputes.[46]

Final approach is the possibility of parties to submit the validity issue to arbitration, however the ruling will be effective only *inter partes*.[47]

The idea looks interesting but it should be made clear what the purpose of the validity dispute is. It can be the clarification of its validity connected with the registration.[48] If there would be award which would try to change also the public register with the effect *erga omnes* it is useless for parties to have valid award, but without following consequences. If the parties just want to clear misunderstanding between them and would respect the award, which would not affect state power, this solution sounds quite progressive.

44 BREKOULAKIS, L. Stavros. On Arbitrability: Persisting Misconceptions and New Areas of Concern. In MISTELIS, A. Loukas; BREKOULAKIS, L. Stavros (*eds*). *Arbitrability: International & Comparative Perspectives.* Alphen aan den Rijn: Kluwer Law International, 2009, p. 23 - 25.

45 *Ibid*., p. 25.

46 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 75 - 76.

47 DE WERRA, Jacques. Arbitrating International Intellectual Property Disputes: Time to Think beyond the Issue of (Non-)Arbitrability. *International Business Law Journal* [online]. 2012, No. 3 [cit. 2015-03-05], p. 303.

48 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 69 - 71.

5 Conclusion

IP disputes no longer create serious issues from the point of view of arbitration. The total exclusion of the IP disputes was refused some time ago and nothing important has changed.[49] However, two aspects of IP disputes still cause uncertainty. The approach of states to disputes over validity (patent, trade marks) is not same and the aspects of moral rights are at least questionable. Another aspect is the examination of the public policy argument namely in the validity disputes. And the highlight of the whole arbitrability question is the possible focus only on the *inter partes* effect of the award.

The arbitrability concerns arise especially at the stage of enforcement, when the state court is allowed to refuse the recognition and enforcement of the award based on the public policy exception. Although one doctrine prefers the use of transnational public policy, more common approach is the way of the international public policy. The narrow interpretation of international public policy *per se* supports the recognition and enforcement of the awards dealing with validity disputes or moral rights.

The other way how to enable the arbitrability of IP disputes is to somehow accept the situation and do not apply for the *erga omnes* effect of the award. The solution with *inter partes* effect of award, which is commonly suggested, can be useful but has to be compared to its desired final goal.

In conclusion, the current academic discussion supports the absolute arbitrability of international IP disputes. However, the award trying to interfere into the registration or granting of IP rights itself would for sure create the public policy concern and the parties of international dispute should be aware of that.[50]

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49 See more about the position towards the arbitration and IP disputes: CARON, D. David. World of Intellectual Property and the Decision to Arbitrate. *Arbitration International* [online]. 2003, Vol. 19, Iss. 4 [cit. 2015-03-05], p. 441-443; COOK, M. Trevor; GARCIA, I. Alejandro. *International intellectual property arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 49-50.

50 COOK, M. Trevor; GARCIA, I. Alejandro. *International Intellectual Property Arbitration.* Alphen aan den Rijn: Wolters Kluwer, 2010. p. 69.

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REDISCOVERING COMPETENCE – COMPETENCE IN LATVIA: INTERNATIONAL IMPACT

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Abstract

The 28 November 2014 judgment of the Constitutional Court of Latvia has re-defined the notion of competence – competence of arbitral tribunals in Latvia and the division of jurisdiction between state and arbitration courts in disputes regarding the effect of arbitration agreement. The challenge of arbitration agreements at state courts, which until the judgment was virtually impossible, has now been given the green light. This marks an important step ahead towards internationally settled standards for the Latvian legal regulation of arbitration which has continually been criticized for lack of adherence thereto. The paper analyzes the changes in Latvian arbitration law brought about by this judgment and its consequences for courts, arbitral tribunals and parties to arbitration agreements both in domestic and international disputes, namely, the possibility to challenge arbitration agreements at state courts and to reopen closed (terminated) cases concerning the effect of arbitration agreement.

Keywords

Arbitration Agreement; Arbitration Clause; Competence – Competence; Effect.

1 Introduction

In the end of 2014 the Constitutional Court of Latvia ("Constitutional Court") recognized that Art. 495(1)[1] of the Civil Procedure Law ("CPL")[2]

1 In force until 31 December 2014.

2 REPUBLIC OF LATVIA. Civil Procedure Law, Act of 14 October 1998, Latvijas Vēstnesis ("LV"), 326/330, 3 November 1998. In *Likumi.lv*. Available from: http://likumi.lv/doc.php?id=50500 ("CPL").

providing for the principle of competence-competence[3] was incompatible with the Latvian Constitution (the *Satversme*),[4] insofar as it did not allow the challenge of arbitration agreements in a state court.[5]

That effectively ended the at least 6–year-long Supreme Court of Latvia ("Supreme Court") settled case-law[6] that the legal force of arbitration agreements cannot be examined by the courts, but only by arbitral tribunals, due to the principle of competence-competence. The author has already expressed an opinion that such case-law was incorrect and contrary to internationally recognized contents of the principle of competence-competence,[7] whereby an arbitration tribunal is merely the first to examine its jurisdiction and its decision is normally subject to a subsequent examination by a national court.[8] Some inferior courts also disagreed with the Supreme Court by delivering judgments on merits examining the effect of arbitration clauses,[9] despite the foreseeable fact that the Supreme Court would terminate the litigation. It was clear that the case-law of the Supreme Court would prove an insurmountable challenge to parties to arbitration agreements, unless the issue is examined by the Constitutional Court.

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3 *„The arbitration court itself shall decide as to jurisdiction regarding a dispute, including in cases where one of the parties disputes the existence or the being in effect of the arbitration court agreement."*

4 REPUBLIC OF LATVIA. Constitution of the Republic of Latvia, Act of 15 February 1922, LV, 43, 1 July 1993. In *Likumi.lv*. Available from: http://likumi.lv/doc.php?id=57980 ("Constitution").

5 Judgment of the Latvijas Republikas Satversmes tiesa, Latvia of 28 November 2014, No. 2014-09-01 [online]. In *Latvijas Republikas Satversmes tiesa.* Constitutional Court [cit. 2015-03-13] ("28 November 2014 judgment").

6 Decision of the Latvijas Republikas Augstākās tiesas Senāta Civillietu departaments, Latvia of 17 June 2014, No. C13047509 (SKC-2228); Decision of the Latvijas Republikas Augstākās tiesas Senāta Civillietu departaments, Latvia of 30 April 2008, No.SKC-179; Decision of the Latvijas Republikas Augstākās tiesas Senāta Civillietu departaments, Latvia of 14 May 2008, No. SKC-213; Decision of the Latvijas Republikas Augstākās tiesas Senāta Civillietu departaments, Latvia of 26 September 2012, No. SKC-514.

7 PIERHUROVIČA, Liene. Vai starptautiskās šķīrējtiesas lēmumam par jurisdikciju var būt res judicata spēks? In ROZENFELDS, Jānis et al. (eds.) *Tiesību efektivas piemērošanas problemātika. Latvijas Universitātes 72.zinātniskās konferences rakstu krājums*. Rīga: LU Akadēmiskais apgāds, 2014, p. 407 – 408.

8 WALTERS, Gretta, L. Fitting a Square Peg into a Round Hole: Do Res Judicata Challenges in International Arbitration Constitute Jurisdictional or Admissibility Problems? *Journal of International Arbitration*, 2012, Vol. 29, No. 6, p. 675.

9 Judgment of the Rīgas pilsētas Centra rajona tiesa, Latvia of 4 February 2013, No. C27208612; Judgment of the Zemgales apgabaltiesa, Latvia of 27 September 2011, No. C13047509.

The 28 November 2014 judgment[10] is important in several aspects. Firstly, it has integrated the Latvian arbitration law in the generally accepted understanding of competence-competence. Secondly, parties can now seek to annul court decisions that previously barred their claims on the effect of arbitration agreements from being adjudicated on merits and request adjudication of their claims afresh. Thirdly, this development, although more of a national nature, may also affect foreign economic and legal interests of parties to domestic disputes.

The author will examine these three points and provide an insight in the legal changes the 28 November 2014 judgment has brought about, as well as its consequences for the Latvian judicial and arbitral branch and possible cross-border impact.

2 Changes Brought by the 28 November 2014 Judgment

2.1 Before the 28 November 2014 Judgment

Until the 28 November 2014 judgment the Supreme Court had consistently held with regard to domestic disputes that arbitration agreements were incapable of being examined by state courts, except for arbitration clauses in consumer contracts.[11] In holding so the Supreme Court referred to Art. 495(1) CPL and Art. 223(6) CPL,[12] the latter serving as grounds to terminate any litigation the parties of which had concluded an arbitration agreement, even if the object of that litigation was the effect of the arbitration clause itself.

As the majority of the lower courts followed that case-law, it was virtually impossible to avoid being subjected to the jurisdiction of an arbitral tribunal in cases when there was no consent to the arbitration agreement or when that consent was questionable.

10 On 6 February 2015, after examining another constitutional claim, the Constitutional Court adopted another judgment by which Art. 495(1) CPL and Art. 24(1) Arbitration Law was declared incompatible with the Constitution on the same grounds, illustrating the amplitude of the problem. See Judgment of the Latvijas Republikas Satversmes tiesa, Latvia of 6 February 2015, No. 2014-32-01 [online]. In *Latvijas Republikas Satversmes tiesa*. Constitutional Court [cit. 2015-03-13].

11 This exception was justified by the EU Consumer law. See, e.g., Judgment of the Latvijas Republikas Augstākās tiesas Senāta Civillietu departaments, Latvia of 1 November 2006, No. SKC-613 [online]. In *Judikatūras nolēmumu arhīvs*. Supreme Court [cit. 2015-05-05].

12 *„The court shall terminate court proceedings if: [.] 6) the parties have agreed, in accordance with procedures laid down in law, to submit the dispute for it to be adjudicated in an arbitration court; [.].”*

Even though it was not expressly provided for in the CPL that arbitration agreements could be challenged in state courts or that they could be examined by the courts at the arbitration award enforcement stage, Art. 536(1)(3) CPL laid out (and still does) the following ground on which recognition of an award could be refused: *"if [.] the arbitration court agreement, pursuant to the law applying thereto, has been set aside or declared null and void"*. It could only have meant examination by a state court, as there would be no award to enforce, had the arbitration tribunal recognized it had no jurisdiction.[13] It follows that, despite the silence of the CPL regarding an action to challenge an arbitration agreement, the system of the CPL actually envisaged the possibility of litigation with that object.

The existing situation was contested at the Constitutional Court when an aggrieved party submitted a constitutional claim requesting to declare Art. 495(1) CPL incompatible with Art. 92 Constitution (right to fair trial).

2.2 Essence of the 28 November 2014 Judgment

The Constitutional Court ruled that competence-competence did not exclude the possibility that the competence of an arbitral tribunal was verified by a state court. It based this finding on the international law binding upon Latvia, namely the New York Convention[14] and the European Convention,[15] as well as the UNCITRAL Model Law[16] and its own findings in previous judgments about the applicability of internationally accepted standards and principles.[17]

13 PIERHUROVIČA, Liene. Vai starptautiskās šķīrējtiesas lēmumam par jurisdikciju var būt res judicata spēks? In ROZENFELDS, Jānis et al. (eds.) *Tiesību efektīvas piemērošanas problemātika. Latvijas Universitātes 72.zinātniskās konferences rakstu krājums*. Rīga: LU Akadēmiskais apgāds, 2014, p. 407.

14 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf.

15 European Convention on International Commercial Arbitration (Geneva, 1961) [online]. *United Nations Treaty Collection*. Available from: https://treaties.un.org/doc/Treaties/1964/01/19640107%2002-01%20AM/Ch_XXII_02p.pdf.

16 UNCITRAL Model Law on International Commercial Arbitration 1985 with amendments as adopted in 2006 [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf ("UNCITRAL Model Law").

17 28 November 2014 judgment, paras 15.1.–15.5.

The Constitutional Court found that it had no grounds to question the considerations of the Supreme Court as an important interpreter of law in compliance with the Constitution that Art. 495(1) CPL did not allow the examination of arbitration agreements by state courts[18] and thus impliedly established a limitation to fundamental right to fair trial. It further found that Art. 495(1) CPL had a legitimate aim – protection of other persons' rights (elimination of overburdening of state courts and possibility to delay arbitration proceedings by having recourse to state court).[19] Although the Constitutional Court acknowledged that the means of reaching the legitimate aim were appropriate,[20] it found that the challenged norm went beyond what was necessary to achieve the legitimate aim – reduction of the case-load of state courts, as, e.g., in the case of the applicant, already six state court decisions regarding the possibility to challenge the arbitration agreement had been taken in search for justice.[21]

It went on to establish that also the case-law regarding the application of Art. 536 CPL did not show that the norm would oblige a judge to examine the competence of the arbitral tribunal and, if it was exceeded, to refuse to enforce the arbitration award.[22] Additionally, the Constitutional Court acknowledged that the regulation of the enforcement of arbitral awards in the CPL was not designed for examining the competence of the arbitral tribunal.[23] Finally, the court concluded that the legitimate aim of the fundamental rights limitation included in Art. 495(1) CPL could be achieved with means less restrictive on an individual's rights and legal interests, for example, the rule included in Art. 8(2) UNCITRAL Model Law[24] providing for the possibility to continue arbitral proceedings while a state court examines the effect of an arbitration agreement in case a substantive claim subject to arbitration has been brought.[25]

18 *28 November 2014 judgment*, para. 16.
19 *Ibid.*, para. 19.
20 *Ibid.*, para. 20.1.
21 *Ibid.*, para. 20.2.1.
22 *Ibid.*, para. 20.2.2.
23 *Ibid.*, para. 20.2.5.
24 "*Where an action referred to in paragraph (1) of this article has been brought, arbitral proceedings may nevertheless be commenced or continued, and an award may be made, while the issue is pending before the court.*"
25 28 November 2014 judgment, para. 20.2.7.

The Constitutional Court declared void not only Art. 495(1) CPL,[26] but also an identical provision (Art. 24(1)) in the recently adopted Arbitration Law[27] (then not yet in force).[28] Moreover, the Constitutional Court repeatedly[29] drew the legislator's attention to the drawbacks of the CPL regulation on arbitration, the absence of the possibility to set aside an arbitral award, in particular.[30]

3 Consequences of the 28 November 2014 Judgment

3.1 The 28 November 2014 Judgment as a Legal Norm

The 28 November 2014 judgment has the force of a law[31] and itself serves as an amendment to the CPL and the Arbitration Law,[32] i.e., it does not modify the text of the legal norms, but both Art. 495(1) CPL[33] and Art. 24(1) Arbitration Law are since 28 November 2014 complemented with a note that they are incompatible with the Constitution insofar as they prohibit to challenge the competence of an arbitral tribunal at a state court.

In practice, this means that claims the object of which is the effect of an arbitration agreement can now be submitted to state courts regardless of an ongoing arbitration procedure, and courts now have to accept such claims and examine them on merits.

The theoretical gain from the 28 November 2014 judgment is that the scope and content of the principle of competence-competence is no longer subject to clash of opinions and the route of action for the courts is now clearly set.

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26 *28 November 2014 judgment*, para. 21.

27 REPUBLIC OF LATVIA. Arbitration Law, Act of 11 September 2014, LV, 194, 1 October 2014. In *Likumi.lv*. Available from: http://likumi.lv/doc.php?id=269189.

28 In force since 1 January 2015.

29 The first warning was made in 2005. See Judgment of the Latvijas Republikas Satversmes tiesa, Latvia of 17 January 2005, No. 2004-10-01, para. 10 [online]. *Latvijas Republikas Satversmes tiesa*. Constitutional Court [cit. 2015-03-15].

30 28 November 2014 judgment, para. 22.

31 Art. 32(2) Constitutional Court Law. REPUBLIC OF LATVIA. Constitutional Court Law, Act of 5 June 1996, LV, 103, 14 June 1996. In *Likumi.lv*. Available from: http://likumi.lv/doc.php?id=63354 („Constitutional Court Law").

32 Art. 32(3) Constitutional Court Law.

33 Until 31 December 2014.

3.2 Annulling Res Judicata Decisions by which Courts Refused to Examine Arbitration Agreements

It might seem surprising that the Constitutional Court did not find that the solution of the problem lied in interpretation of Art. 495(1) CPL in context with Art. 536(1)(3) CPL. However, upon closer analysis it is clear that by declaring the challenged norm void the Court actually provided an indispensable remedy which would not be otherwise accessible. Namely, for parties whose claim to revoke the arbitration clause or declare it null and void was not accepted by a state court for examination on merits, the 28 November 2014 judgment serves as a tool for undoing this injustice, i.e, it is a newly-discovered circumstance to revoke a *res judicata* decision.

According to a general principle of *res judicata,* after a decision has entered into lawful effect, the parties to the case are not entitled to dispute at other court proceedings the facts established by the court, as well as to bring court action anew regarding the same subject-matter and on the same basis, with a few exceptions.[34] This is also provided for by Art. 203(3) CPL. One of the exceptions to *res judicata* is re-adjudicating matters in connection with newly-discovered circumstances, which is the object of Chapter 59 of the CPL. In accordance with Art. 479(5) CPL, the acknowledgement of a norm of law applied in the adjudication of the matter as not in conformity with a higher norm of law shall be deemed to be a newly-discovered circumstance. As lined out in commentary to the CPL, "*only a judgment of the Constitutional Court is relevant in order to establish the incompliance of a legal norm to a higher legal norm.*"[35]

Thus the 28 November 2014 judgment, and especially its operative part, is a ground for finding the existence of newly-discovered circumstances in a case.

Art. 478(1) CPL provides the competent court examining the application on re-adjudicating a matter in connection with newly-discovered circumstances. The application may be submitted within three months from the day

34 BARNETT, Peter, R. *Res Judicata, Estoppel and Foreign Judgments*. Oxford: Oxford University Press, 2001, p. 8 - 9.

35 LAVIŅŠ, Aldis. Civilprocesa likuma 59.nodaļa. In TORGĀNS, Kalvis (ed.) *Civilprocesa likuma komentāri. II daļa (29.-60.[1] nodaļa)*. Rīga: Tiesu namu aģentūra, 2012, p. 880.

when the facts forming a basis for re-adjudication of the matter have been ascertained (Art. 478(2) CPL). It may not be submitted if more than 10 years have elapsed since the judgment or the decision has come into effect (Art. 478(3) CPL). The application shall be adjudicated by written procedure (Art. 481 CPL).

If the court determines that there are newly-discovered circumstances, it shall set aside the challenged judgment or decision in full or as to part thereof and refer the matter for it to be re-adjudicated in a first instance court. An ancillary complaint may be submitted regarding a decision of the court (Art. 482 CPL).

Accordingly, with regard to the 28 November 2014 judgment courts should always satisfy applications on re-adjudicating matters in connection with newly-discovered circumstances, given that in the challenged decision Art. 495(1) CPL is the ground for refusal to examine arbitration agreement, and refer the relevant case file to a first instance court for adjudication *de novo*.

3.3 Is the 28 November 2014 Judgment a Complete Solution to the Problem?

It is submitted that notwithstanding the 28 November 2014 judgment which approved the limitations of competence-competence of arbitral tribunals and expressly declared that challenge of arbitration agreements before state courts has to be made possible in Latvia, there still exist other grounds in the CPL that oblige the court to terminate litigation if parties have concluded an arbitration agreement.

Namely, Art. 223(6) CPL has remained unchanged and still serves as a ground to terminate court proceedings if the parties have agreed to submit their dispute to an arbitration tribunal. Thus, there is a question whether a first instance court, even after receiving a case for re-adjudication due to newly-determined circumstances, is obliged to terminate litigation.

Similarly, Art. 132(1)3) CPL[36] provides for grounds for refusal to accept a statement of claim if the parties have agreed to the transfer of the dispute

36 *„A judge shall refuse to accept a statement of claim if: [.] 3) the parties have, in accordance with procedures laid down by law, agreed to transfer of the dispute for it to be adjudicated by an arbitration court; [.].”*

to an arbitration tribunal. Hence, after 28 November 2014 courts could still refuse to accept a statement of claim on the aforementioned grounds.

The author is convinced that Arts 132(1)(3) and 223(6) CPL should both be interpreted in the light of the 28 November 2014 judgment, bearing in mind that the interpretation of a legal norm provided in a judgment of the Constitutional Court is obligatory.[37]

Respectively, Art. 223(6) CPL should be interpreted in a way that it only obliges the court to terminate litigation in cases when the main dispute between parties is not about the effect of the arbitration agreement or when parties conclude an arbitration agreement during state court proceedings thus waiving their right to litigate. A broader interpretation would contradict the 28 November 2014 judgment.

Art. 132(1)(3) now also has to be read in a way, that only disputes, the subject of which is not arbitration agreement itself, can be refused litigation and must be referred to arbitration. A state court can no longer refuse to accept a statement of claim on the legal force of an arbitration agreement.

From this viewpoint it is recommended that the CPL should be amended in order to ensure legal stability and to harmonize it with Art. 8 UNCITRAL Model Law, which the Constitutional Court has acknowledged "*a globally applicable standard for normative regulation of arbitration*"[38] and which the Latvian legal regulation on arbitration, including the new Arbitration Law, considerably deviates from,[39] as well as Art. II(3) New York Convention[40] and Art. VI(3) European Convention.[41]

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37 Art. 32(2) Constitutional Court Law.

38 28 November 2014 judgment, para. 15. 4. ; Judgment of the Latvijas Republikas Satversmes tiesa, Latvia of 17 January 2005, No. 2004-10-01, para. 9. 1.

39 KAČEVSKA, Inga. Ir normāla situācija, un ir Latvijas situācija. *Jurista Vārds*. 2014, No.22, p. 23-24; 28 November 2014 judgment, para. 22.

40 *"The court of a Contracting State, when seized of an action in a manner in respect of which the parties have made an agreement within the meaning of this article at the request of one of the parties, refer the parties to arbitration unless it finds that the said agreement is null and void, inoperative or incapable of being performed."*

41 *"Where either party to an arbitration agreement has initiated arbitration proceedings before any resort is had to a court, courts of Contracting States subsequently asked to deal with the same subject-matter between the same parties or with the question whether the arbitration agreement was non-existent or null and void or had lapsed, shall stay their ruling on the arbitrator's jurisdiction until the arbitral award is made, unless they have good and substantial reasons to the contrary."*

3.4 International Impact

Technically the topic of the extent to which Latvia had accepted competence-competence should not have concerned disputes between parties to international commercial arbitration agreements. As most of the countries are either parties to the New York Convention (Latvia is a State Party since 13 July 1992)[42] or the European Convention (Latvia is a State Party since 20 March 2003),[43] or both, disputes concerning the effect of arbitration agreement can be submitted to state courts according to Art. II(3) New York Convention and Art. VI(3) European Convention, which supersede national law. The author has come across one judgment of a court of appeal instance[44] examining an arbitration agreement in a dispute between companies registered in Latvia and Jersey on grounds of both aforementioned conventions. Although failing to motivate the applicability *ratione personae* of the conventions to the dispute, the court correctly considered international norms instead of the CPL. There is also no Supreme Court case law on international arbitration agreements, leading to conclude that there is no doubt on the correct application of law in such disputes.

However, the division of disputes into domestic and international is not always so clear-cut. Although incorporated under Latvian laws, companies may often be owned by foreign investors and run with foreign capital, thus representing foreign interests. Consequently, the inability to contest the jurisdiction of an arbitral tribunal which was never chosen by a party as a dispute resolution forum, could have had direct impact on the foreign interests concentrated in an entity registered in Latvia.

Though a very theoretical possibility, the CPL would have also been applied to disputes where one of the parties was from a country not party to either of the conventions and the arbitral proceedings were held in Latvia.

Consequently, the 28 November 2014 judgment has weight with regard to restoration of justice by means of requesting the re-adjudication of a case due to newly-discovered circumstances also in domestic disputes which involve foreign economic and legal interests.

42 *Status. United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958)* [online]. United Nations Commission on International Trade Law (UNCITRAL) [cit. 2015-03-14].

43 *Status. European Convention on International Commercial Arbitration (Geneva, 1961)* [online]. United Nations Treaty Collection [cit. 2015-03-15].

44 Judgment of the Kurzemes apgabaltiesa, Latvia of 29 May 2014, No. C20260612.

4 Conclusion

The 28 November 2014 judgment has a significant impact in the legal system of Latvia: it has been acknowledged that the existing understanding of competence-competence that only arbitration tribunals could decide on their competence was wrong and the definition of the principle has been corrected to correspond to international standards.

The 28 November 2014 judgment has the force of a law and itself serves as an amendment to the CPL and the Arbitration Law. In practice, this means that claims the object of which is the effect of an arbitration agreement can now be submitted to state courts regardless of an ongoing arbitration procedure, and courts now have to accept such claims and examine them on merits.

The 28 November 2014 judgment is also grounds for finding the existence of newly-discovered circumstances in a case where a *res judicata* decision on refusing to examine arbitration agreement has entered into force. This can be an important remedy for parties not only to purely domestic disputes, but also disputes where foreign economic and legal interests are involved.

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ARBITRABILITY OF INDIVIDUAL EMPLOYMENT DISPUTES

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Abstract

The paper deals with arbitrability of individual employment disputes for hearing and decision in the arbitration. The Czech Arbitration Act applies to both national and international arbitration and admits to hear and to decide disputes of property nature only. Claims for various property performances from employment relations are therefore generally considered to be arbitrable. In the case of disputes arising from employment relations with a status character arbitrability is questionable. The aim of this paper is to appraise the admissibility of the arbitration in employment relations. Although the employment relations have a property basis, disputes over the status of these relationships have a fundamentally different objective, especially a decision on whether a particular person is or is not in the position of the employee. Under current legislation of conditions of the arbitrability I assume that the employment disputes of property nature only can be heard and decided in the arbitration. Disputes arising from employment relations with a status character may now be heard by the courts only, because they do not fulfill the conditions of arbitrability. The amendment of the Arbitration Act which would impose the protective elements into the arbitration over the employment disputes would allow to decide all disputes arising from employment relations in the arbitration.

Key words

Arbitration; Arbitrability; Individual Employment Disputes; Arbitration Act.

1 Introduction

The Act No. 91/2012 Coll., on Private International Law ("PILA")[1] contains conflict rules regulating arbitration with international element. Under

1 CZECH REPUBLIC. Act No. 91/2012 Coll., on Private International Law ("PILA").

Sec. 117 the admissibility of an arbitration agreement is assessed according to the Czech law. The Act No. 216/1994 Coll., on Arbitration and Enforcement of Arbitral Awards ("Arbitration Act")[2] thus applies to both national and international arbitration. Conditions of arbitrability under the Czech law are proportionately restrictively defined and application of the Arbitration Act may cause difficulties in international arbitration. The paper deals with arbitrability of individual employment disputes under the Arbitration Act and points to the necessary legislative changes respecting protection of employee, whereas its conclusions apply to both national and international arbitration.

Settlement of employment disputes in the arbitration brings many advantages. Compared to judicial proceedings, main advantages of arbitration are especially shorter duration of the arbitration, its lower costs and broad autonomy given to parties and arbitrators. But arbitrability of individual employment disputes is questionable. The Arbitration Act does not contain positive or negative definition of arbitrability of individual employment disputes. It must therefore be based on the Sec. 2 Arbitration Act which sets out general conditions of arbitrability. The aim of the present paper is to evaluate whether the disputes arising from individual employment relations fulfill the conditions stipulated by the Arbitration Act and whether it can be stated their arbitrability.

2 General Conditions of Arbitrability

In order to solve the dispute in arbitration, the dispute must be arbitrable and there must exist a valid arbitration agreement. Arbitrability of dispute is assessed under Sec. 2 Arbitration Act. It defines the positive and negative conditions of arbitrability of dispute. Under Sec. 2 disputes are arbitrable if they cumulatively fulfill the following conditions. Arbitration agreement may be validly concluded over property disputes which would otherwise fall within the jurisdiction of the courts if the law allows the parties to resolve the subject matter of their dispute by settlement. Arbitrability is expressly excluded in the case of disputes arising from the enforcement of decisions and incidental disputes. Disputes shall be decided by one or more arbitrators

2 CZECH REPUBLIC. Act No. 216/1994 Coll., on Arbitration and Enforcement of Arbitral Awards ("Arbitration Act").

or by a permanent arbitral institution. The arbitration agreement may apply to an individual dispute which has already arisen, i.e. the post-dispute arbitration agreement, or all disputes which would arise in the future under a defined legal relationship or under a defined category of legal relationship, i.e. the arbitration clause.

3 Conditions of Arbitrability of Individual Employment Disputes

Under Sec. 2 Arbitration Act disputes of property nature are arbitrable. The term "property disputes" is not defined by the law. It can be defined such as disputes concerning a particular property performance evaluated in financial terms, i.e. disputes the subject matter of which can be expressed in property values.[3] There are *"disputes discussed in adversary proceedings initiated by lawsuit whereby the claimant demands that the respondent be ordered to provide a property performance, especially pecuniary performance, surrender a thing, or provide any other specific performance"*.[4] For example, claims for redundancy payment, claims for compensation for damages or losses sustained at work or other property performances from an employment relationship, etc.[5]

Another prerequisite of arbitrability which is defined under Sec. 2 is non-exclusive jurisdiction of the courts. In that provision a situation where the court is called for immediate decision of dispute is foreseen. Disputes which fall within the jurisdiction of courts are defined under Sec. 7 Code of Civil Procedure.[6] Under Sec. 7 Code of Civil Procedure in civil proceedings the courts hear and decide disputes and other legal matters arising not only private but also employment and other relationships if it is not dealt with by the law and make decisions about them other organs.[7]

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3 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 298.

4 BĚLOHLÁVEK, Alexander, J. *Arbitration Law of Czech Republic: Practice and Procedure.* Huntington: Juris, 2013. p. 152.

5 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 298. See also LISSE, Luděk. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů s komentářem.* Praha: Linde, a. s., 2012. p. 95.

6 CZECH REPUBLIC. Act No. 99/1963 Coll., Code of Civil Procedure, as subsequently amended.

7 BĚLOHLÁVEK, Alexander, J. Arbitrabilita pracovněprávních sporů. *Bulletin advokacie.* 2007, No. 9, p. 26.

The last condition of arbitrability of disputes which is set out under Sec. 2(2) Arbitration Act is the possibility of the parties to settle the dispute. In terms of procedural law the settlement may be concluded if it accepts the nature of matter under Sec. 99(1) Code of Civil Procedure. There are usually the cases that parties are involved in a typical bilateral relationship and substantive law does not prohibit the parties from regulating their legal relationships by dispositive acts.[8] The settlement can be concluded even in matters of determining whether legal relationship or right is or is not. Conversely, the settlement cannot be concluded in cases the nature of which does not allow settlement at all, for example, in cases where the court may initiate proceedings *ex officio*.[9] Conclusion of settlement is principally excluded in matters of personal status, matters in which the validity agreement requires court approval and matters in which substantive law prohibits the resolution of the matter by an agreement of the parties to the legal relationship.[10] In terms of substantive law the settlement may be concluded in all situations where the parties are free to make dispositions with the claim. The settlement therefore is eligible where a dispute may be settled by conciliation between the parties of legal relationship.[11]

4 Arbitrability of Individual Employment Disputes

Disproportionate length of proceedings before the courts, considerable effort required from the parties and also costs that must be expended for the recovery of rights are reasons that discourage employees to pursue their claims before the courts. The right to speedy proceedings or more precisely the right to the proceedings within a reasonable time with respect to the circumstances of particular case is one of the rights that constitutes a right to a fair trial. Regarding the duration of litigation in the Czech Republic

8 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 297.

9 LISSE, Luděk. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů s komentářem.* Praha: Linde, a. s., 2012. p. 91, 93 – 94.

10 BĚLOHLÁVEK, Alexander, J. Arbitrabilita pracovněprávních sporů. *Bulletin advokacie.* 2007, No. 9, p. 26.

11 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 297.

this is regularly violated.[12] Possible solution of this negative phenomenon is to resolve employment disputes in the arbitration. Settlement of disputes in the arbitration brings many advantages compared with the proceedings before the courts. Compared to judicial proceedings, main advantages of the arbitration are especially shorter duration of the arbitration, its lower costs and broad autonomy given parties and arbitrators.[13]

Arbitrability of individual employment disputes according to the Arbitration Act is questionable.[14] Opinions of arbitrability of individual employment disputes are different in the Czech Republic. The answer is not found even in the case-law. The Arbitration Act admits in the arbitration to hear and to decide disputes of property nature only. Claims for various property performances from employment relations are therefore generally considered to be arbitrable. In the case of disputes arising from employment relations with a status character is arbitrability controversial. An out-of-court resolution of individual employment disputes had a long tradition in the Czech Republic. Ever since the First Republic, numerous institutes of alternative solutions of employment disputes existed here. The individual employment disputes were heard only by the courts since the 1 February 1991. By adopting the new Labour Code[15] in 2006, the decision of individual and employment disputes in arbitration was enabled.[16]

The question of arbitrability of individual employment disputes is clearly resolved abroad. Arbitrability of individual employment disputes in other countries is usually much wider than under the Arbitration Act.[17] For example, under the German Code of Civil Procedure *(Zivilprozessordnung)*, all disputes of property nature are arbitrable and other disputes are arbitrable only

12 PICHRT, Jan. Alternativní způsoby řešení sporů v pracovněprávních vztazích – minulost, současnost a budoucnost. *Právní rozhledy*. 2013, Vol. 21, No. 21, p. 725.

13 See ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Second edition. Praha: ASPI, Wolters Kluwer, 2008. p. 59 – 62.

14 Employment relations arising from the collective agreements are arbitrable *ex lege* under the Act No. 2/1991 Coll., on Collective Bargaining, as subsequently amended.

15 CZECH REPUBLIC. Act No. 262/2006 Coll., Labour Code, as subsequently amended.

16 PICHRT, Jan. Alternativní způsoby řešení sporů v pracovněprávních vztazích – minulost, současnost a budoucnost. *Právní rozhledy*. 2013, Vol. 21, No. 21, p. 726 - 728.

17 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář*. Praha: C. H. Beck, 2008. p. 287.

if the parties may settle on the subject matter of dispute.[18] Arbitrability of employment disputes is treated similarly as arbitrability of consumer disputes due to the requirement to protect the weaker party of the dispute.[19] For example, under the Austrian Code of Civil Procedure *(Zivilprozessordnung)*, the general conditions of arbitrability are identical to the Czech law but the provisions regulating arbitration in consumer disputes are applied similarly to employment disputes defined in the Sec. 50(1) *Arbeits- und Sozialgerichtsgesetz* (for instance, disputes between employer and employee regarding contract of employment, disputes between employer or employee and employment authorities, etc.). Under the Polish Code of Civil Procedure *(Kodeks postępowania cywilnego)*, employment disputes are arbitrable if the arbitration agreement is in writing and is concluded as post-dispute arbitration agreement.[20]

According to the Arbitration Act, for hearing and decision of the individual employment dispute in the arbitration, an arbitration agreement between the employee and the employer must exist. The arbitration agreement may be a part of employment contract, agreement to complete a job or agreement to perform work. The arbitration agreement may also be concluded in a separate document as the procedural agreement which of both parties of employment relationship agree with preclusion of jurisdiction of the courts and admission of hearing and decision of the employment dispute by arbitrators or permanent arbitral institutions in case dispute arising in the future between them.[21]

The arbitration clause may be agreed validly also as a part of internal regulation issued by the employer. Under Sec. 305(1) Labour Code is possible to set out certain rights and obligations arising from employment relations by internal regulation. The arbitration clause could be agreed in the collective agreement also. The employer must explicitly point an employee out

18 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení v zemích Evropy.* Praha: C. H. Beck, 2012. p. 250.

19 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 290.

20 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení v zemích Evropy.* Praha: C. H. Beck, 2012. p. 35, 46, 1209.

21 LISSE, Luděk. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů s komentářem.* Praha: Linde, a. s., 2012. p. 95.

to the arbitration clause in all cases of conclusion of the arbitration clause between them. The arbitration clause is not time-bound to the validity and effectiveness of internal regulation whose it was a part under Sec. 305(5) Labour Code. The arbitration clause obliges parties of the employment relationship even after revocation of internal regulation unilaterally or by an agreement between the employee and the employer respectively by a collective agreement. Protective provisions of the Labour Code, for example Sec. 31 ensure that the employee will be informed about establishment the jurisdiction of an arbitrator or permanent arbitral institution to decision the dispute of his employment relationship with the employer in all cases. Protecting employees is sufficiently secured.[22]

The question remains what employment disputes can be described as arbitrable. According to the prevailing opinions the arbitration agreement is permissible with respect to selected claims arising from employment relationships, providing they have a property nature. Employment disputes concerning a particular property performance, especially pecuniary performance are generally considered to be arbitrable.[23] *"This include, for instance, claims for compensation for damage or losses sustained at work, other property performances from an employment relationship, etc."* [24]

Arbitrability is controversial in the case of disputes regarding the status of employment relation. These include, for example, employment disputes concerning the validity or nullity of termination of an employment relationship. These cases are typically non-arbitrable according to *Bělohlávek*.[25] *"Even though the employment relationship (the status thereof, i.e. its existence, validity, and scope) also has a property basis, i.e. it serves (at least for the employee) the purpose of obtaining the means to satisfy the party's material needs, disputes over the status of these relationship have a principally different objective, i.e. especially a decision on whether a particular*

22 LISSE, Luděk. Arbitrabilita v pracovněprávních sporech. *Obchodní právo*. 2008, Vol. 17, No. 2, p. 5 - 6.

23 BĚLOHLÁVEK, Alexander, J. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů. Komentář.* Second edition. Praha: C. H. Beck, 2012. p. 130.

24 BĚLOHLÁVEK, Alexander, J. *Arbitration Law of Czech Republic: Practice and Procedure.* Huntington: Juris, 2013. p. 171.

25 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 295. See also BĚLOHLÁVEK, Alexander, J. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů. Komentář.* Second edition. Praha: C. H. Beck, 2012. p. 130.

person is or is not an employee of a particular employer."[26] Cited argument of this author is supported by the reference to "court" in Sec. 61(4) Labour Code.[27] *"This is the reason why terminology employed by the Labour Code differentiates between the conclusion of an employment contract which establishes an employment relationship and the termination of the employment relationship."*[28] An arbitration agreement may be validly concluded after the court decision on the validity of the termination of the employment relation, for example, regarding potentially other related claims of the employee for pecuniary performance due from the employer. In such case, the arbitration agreement would be a post-dispute arbitration agreement.[29]

Conversely, *Lisse* finds employment disputes with a status character arbitrable. In the case of employment disputes over determination rights or obligations is their property dimension to the secondary, but nevertheless they are a property disputes and therefore arbitrable. These disputes also fulfill the other conditions prescribed by the Arbitration Act. The law allows parties to resolve the subject matter of their dispute by settlement. These are the disputes which would otherwise fall within the jurisdiction of the courts. Under Sec. 2 Arbitration Act are non-arbitrable only disputes that do not have a property nature, disputes whose do not resolve by a settlement and disputes arising from the enforcement of decisions and incidental disputes *argumentum a contrario*. Employment disputes do not fall within one of these categories. *Argumentum a fortiori* so the employment disputes are arbitrable and fulfill the conditions set out under Sec. 2(1) and 2(2) Arbitration Act.[30]

Conclusion on the property nature of employment disputes with a status character is further justified by *Lisse* by the interpretation of term "property dispute" in the case-law. The property right should be defined

26 BĚLOHLÁVEK, Alexander, J. *Arbitration Law of Czech Republic: Practice and Procedure*. Huntington: Juris, 2013. p. 171.

27 BĚLOHLÁVEK, Alexander, J. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů. Komentář.* Second edition. Praha: C. H. Beck, 2012. p. 130.

28 BĚLOHLÁVEK, Alexander, J. *Arbitration Law of Czech Republic: Practice and Procedure*. Huntington: Juris, 2013. p. 171.

29 BĚLOHLÁVEK, Alexander, J. *Rozhodčí řízení, ordre public a trestní právo. Komentář.* Praha: C. H. Beck, 2008. p. 295. See also BĚLOHLÁVEK, Alexander, J. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů. Komentář.* Second edition. Praha: C. H. Beck, 2012. p. 130.

30 LISSE, Luděk. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů s komentářem.* Praha: Linde, a. s., 2012. p. 91, 96.

as the right to the property performance, i.e. the performance evaluated in financial terms as well as declaratory proposal which relates to the determination of the existence or non-existence of this right.[31] The purpose of a legal act basing the employment relationship is always salary as property performance. Employment dispute with a status character is arbitrable for this reason. Ultimately, it always tends to a property satisfaction of one of the parties. The action, for example, over the validity of dismissal is a declaratory action. Its result is not only to determine whether there is or is not an employment relationship but also implicitly determine whether there is or is not a claim for property performance. This determination which primarily includes a property element then secondarily generates merits decision only on the particular amount of the property performance.[32]

Finally, the employment disputes determining existence of employment relationship cannot be compared to typical disputes regarding the status. For example, an action for dismissal which determining whether particular person is or is not in the position of the employee cannot be compared to a status action which determines perhaps whether particular individual is or is not in a marriage, because to be or not to be in an employment relationship is not an expression a status position of a man in society. Indeed, it is determined only in relation to the nationality (the question of the status of citizen/ stateless person) and the marriage status as the typical matters (the question of the status of husband/ no-husband, married/ unmarried). The dispute over the validity of ever legal act is property dispute provided that the cause of this legal act has a property nature. In this context it is necessary to examine the purpose of legal act consisting in a conclusion an employment contract by an employee. *Lisse* states that the purpose of a conclusion an employment contract is purely property. Dispute over the validity or nullity of termination of the employment relationship is thus property dispute. The term "property disputes" does not include only

31 Decision of the Vrchní soud Prague, Czech Republic of 15 November 1995, No. 10 Cmo 414/95.

32 LISSE, Luděk. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů s komentářem.* Praha: Linde, a. s., 2012. p. 96.

the disputes over the pecuniary performance but logically also disputes over the validity or nullity of legal acts which established a claim for pecuniary performance.[33]

Assertion that every employment dispute is a dispute over property cannot agree. The employment disputes with a status character is not property disputes regarding their subject matter therefore cannot conclude a settlement and thus do not fulfill the conditions of arbitrability. In my opinion, an arbitration agreement can be concluded only regarding the employment disputes which are typically property disputes related to pecuniary performance or performance evaluated in financial terms. Employment relations are characterized by unequal position of their parties. An employee is generally considered for the weaker party and therefore he receives specific legal protection. Special legal protection of position of an employee provided under Sec. 1a Labour Code is one of the basic principle of employment relations. Arbitration Act in the present version does not provide an adequate protection for an employee in a dispute over the status of its employment relationship.

Under Sec. 72 Labour Code, the nullity of termination of an employment relationship by notice, by immediate dismissal, by notice during the trial period or by agreement may be claimed both by the employer and the employee before the court within two months of the date when the employment relationship in question ought to have come to an end as a result of such termination. The above provision refers that disputes regarding the status of employment relationship are decided by courts. The reference to "court" is also contained, for example, in Sec. 39(5) Labour Code which relates to duration of a fixed-term employment relationship and in Sec. 64(1) relating to the nullity of the notice or immediate termination of employment relationship. One of the conditions of the arbitrability stated under Sec. 2 Arbitration Act is otherwise the non-exclusive jurisdiction of the court, but other conditions must be cumulatively fulfilled, too therefore it must be a property dispute whose subject matter can be resolved by the settlement. The essence of dispute over the nullity of termination

33 LISSE, Luděk. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů s komentářem.* Praha: Linde, a. s., 2012, p. 96 - 97.

of employment relationship is whether its termination was under the law. Employment disputes with a status character do not fulfill stated conditions therefore they cannot be resolved in the arbitration and they are decided by courts.

Conclusion of the arbitration agreement regarding the employment property disputes may have an extensive impact for employees also. For example, if this dispute should be resolved under the rules of equity. Sec. 25(3) Arbitration Act allows arbitrators to resolve the dispute under the rules of equity if the parties have explicitly authorized them to do so. In the case that the arbitrators do not resolve cases under the applicable substantive law it could lead to breaking of the protective provisions of the Labour Code. The employee does not acquire an adequate protection in the cases where the dispute has been decided under foreign law also. Ultimately, the employment disputes are decided by chambers before courts. However, in the arbitration agreement a sole arbitrator may be appointed which could be problematic due to the fact that the Code of Civil Procedure shall be applied *mutatis mutandis* to arbitration under Sec. 30 Arbitration Act.

Due to the similar nature of individual employment relations compared to consumer relations would be appropriate to resolve the employment disputes in arbitration adapt similarly as resolving consumer disputes. This solution is usual abroad. The employment relations in the branch of individual employment law are characterized identically as consumer relations relatively higher degree of factually inequality of their parties. The introduction of protective elements into the legislation of arbitration over employment disputes would be referred inequality straightened. The employment disputes of property nature can now be resolved in the arbitration only according to the prevailing opinions. The question remains whether it should be allowed to decide other disputes arising from individual employment relations in the arbitration taking into account the specific position of employees. This solution would lead to the improvement of law enforcement for employees, faster decision of disputes arising from employment relations and fully guaranteeing the right to a fair trial.[34]

34 PICHRT, Jan. Alternativní způsoby řešení sporů v pracovněprávních vztazích – minulost, současnost a budoucnost. *Právní rozhledy*. 2013, Vol. 21, No. 21, p. 729 - 730.

The employee as the weaker party of dispute should be granted the similar degree of protection as consumer in arbitration. The arbitration agreement regarding to resolving disputes arising from employment relations should be thus concluded as separate procedural contract and independently of the main contract under sanction of nullity. The employment disputes should be decided only by permanent arbitral institutions or arbitrators ad hoc inscribed on the list of the Ministry of Justice. The arbitration agreement should be permissible to conclude only as post-dispute arbitration agreement thus permitting the establishment of the jurisdiction of the arbitrators to decide an employment dispute after its inception. Disputes arising from employment relations should be not decided under the rules of equity or as *amiable compositeur* but only under the applicable employment laws. The arbitration clauses concluded for settlement of employment relations should include information about mode of initiation and form of leadership of arbitration, the place of arbitration, its costs and rules for their allocation, method of delivery and enforceability of the arbitration award. Finally, the increased protection of employees would be guaranteed by an obligation to always prescribe an oral hearing before the arbitral tribunal, to justify the arbitration award and to educate the employee about his right to make a proposal for setting aside of arbitration award to the court.

5 Conclusion

The arbitrability of employment disputes is unresolved question which will be answered in the case-law. Under current legislation of conditions of the arbitrability as set out under Sec. 2 Arbitration Act I assume that the employment disputes of property nature only can be heard and decided in the arbitration. Disputes arising from employment relations with a status character may now be, in my opinion, heard by the courts only, because they do not fulfill the conditions of arbitrability specified in Sec. 2. Disputes regarding the status of employment relations are not the property disputes. The objective of dispute over the dismissal or the existence of an employment relationship, for example, is in fact similar to objectives of status disputes because its result is to determine whether a particular person is or is not in the position of the employee. On the subject matter

of employment disputes with a status character a settlement cannot be concluded. The amendment of the Arbitration Act which would impose the protective elements into the arbitration over the employment disputes would allow deciding all disputes arising from employment relations in the arbitration and faster resolution of disputes arising from employment relations would be achieved and thus the right to a fair trial would be fully guaranteed.

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ARE THE DAYS OF THE "ITALIAN TORPEDO" NUMBERED?

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Abstract

The paper examines the interaction between arbitration and court proceedings from the perspective of European international procedural law and the phenomenon of the "Italian torpedo". It deals mainly with two questions, namely what impact Brussels I bis Regulation will have on arbitrations in the EU, whether the "West Tankers' case" was really decided wrongly, or rather, whether the CJEU had any other option, if we take the so called "Brussels' effect" into consideration. Another important question this paper deals with is whether the "Italian torpedo" can be under Brussels I bis' regime torpedoed, by allowing to enforce an award obtained in parallel arbitral proceedings and effectively "sidestep" the CJEU's controversial decision in the West Tankers litigation, as it was the case in High Court's decision in the West Tanker's case. This paper deliberately leaves the question open, to what extend and for how long the "West Tankers' case" may continue to challenge both the CJEU and arbitration professionals, since only the relevant case law can answer those questions.

Keywords

Arbitration; Brussels I bis Regulation; Lis pendens Rule.

1 Introduction

Although all arbitration matters has been formally excluded from the scope of the Brussels I Regulation[1] since its outset, the Brussels I Regulation

[1] Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32001R0044 & rid=1 („Brussels I Regulation").

challenges the arbitration community in the EU since it appears to legitimise court actions in breach of arbitration agreements through the *Lis Pendens* Rule anchored in Art. 27(2) Brussels I Regulation.[2] This article provides a strict „first come & first served rule" in order to avoid irreconcilable judgments and thus it grants a priority to the court seised first without giving any chance to a subsequently seised court to review the grounds of the court first seised jurisdiction. On top of that, in case of proceedings involving the same parties and same cause of action, Art. 27(2) orders a mandatory obligation to the court subsequently seised to decline jurisdiction in favour of the court seised first.[3]

The reason for the exclusion of arbitration from the substantive scope of the Brussels I Regulation is simple. All EU Member States are contracting states of the New York Convention.[4] Decisional practice of the Court of Justice of the EU ("CJEU") conceives arbitration very widely, therefore falls into this category not only arbitration itself, but also auxiliary activities of courts. However, in the (in)famous West Tankers case,[5] the CJEU ruled that despite the clear carve-out for arbitration in the Brussels I Regulation and notwithstanding the existence of the arbitration agreement other member state courts had to stay any related proceedings if a decision by the court first seised is pending. Furthermore, the CJEU decided that the member state courts were not entitled to issue anti-suit injunctions[6] to restrain such

2 HAEBERLING, Walter; SCHULZ, Heike. Key Changes of the Revised Brussels I Regulation [online]. In *Mll-Legal Publications*. Meyerlustenberger Lachenal [cit. 2015-02-12], p. 22.

3 EISENGRABER, Julia. Lis Alibi Pendens under the Brussels I Regulation - How to Minimise 'Torpedo Litigation' and Other Unwanted Effects of the 'First-Come, First-Served' Rule. *Exeter Centre for European Legal Studies* [online]. Vol. 63, No. 16 [cit. 2015-02-12], p. 42.

4 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf ("New York Convention").

5 Judgment of the Court of Justice of 10 February 2009. Allianz SpA and Generali Assicurazioni Generali SpA v. West Tankers Inc. Case C-185/07, point 32. ("West Tankers case").

6 The majority of court systems in the EU member states are civil law systems, which have negative views of anti-suit injunctions and would not to grant the m, so in principle an anti-suit injunction can be issued by a common law courts only. See RAINER, Daniel. The Impact of West Tankers on Parties' Choice of a Seat of Arbitration. *Cornell Law Review* [online]. 2010, Vol. 95, No. 2 [cit. 2015-02-20], p. 434.

actions in the courts of other member states. The revised Brussels I bis Regulation[7] reinforces the exclusion of arbitration. It retains unchanged the exclusion of arbitration but contains an explanatory recital confirming categories of disputes falling outside the Brussels regime.

This article discusses the tension that arises between the Brussels I Regulation, resp. Brussels I bis Regulation and arbitration. It also explores the reasons that apparently led the CJEU to its questionable decision and introduces a phenomenon called "Brussels' effect". Furthermore, this paper will break down the changes that were originally planned (but eventually abandoned) for the "recast" of Brussels I Regulaztion and associated question, whether the "Italian torpedo" can be under Brussels I bis Regulation's regime „torpedoed" by allowing to enforce an award obtained in parallel arbitral proceedings and refuse to enforce a subsequent contradictory judgment of the courts of another EU Member State.

The hypothesis of this paper is the claim that the Brussels' legislator as well as CJEU never planned to restrict arbitration and this whole matter is simply a by-product resulting from efforts to protect the common European values, and especially the principle of mutual trust.

Subsequent analysis will be conducted due to limited capacity of the paper in relation to the EU Member States only.

2 West Tankers and the "Brussels Effect"

In this particular case Allianz brought a claim against West Tankers in Italy, even though the relevant charter party contract contained an arbitration clause in favour of London. West Tankers won a declaration of non-liability in the arbitration in London, but following the CJEU's decision was unable to extricate itself from the simultaneous Italian litigation with an anti-suit injunction.[8] CJEU reasoned that allowing the English court to grant

7 Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/CS/TXT/PDF/?uri=CELEX:32000L0031 & rid=1 ("Brussels I bis Regulation").

8 PAUKNEROVÁ, Monika. *Evropské mezinárodní právo soukromé*. 2nd ed. Praha: C. H. Beck 2013. p. 94; GEOFF, Steward. West Tankers Win the Latest Bottle – Who Will Win the War? [online] In *McFarlanes' Arbitration Notice* [cit. 2015-02-28].

an anti-suit injunction would directly exempt from the other European courts the ability to decide on matters within their competence (their own jurisdiction's questions) in accordance with the Brussels I Regulation and violate the principal of mutual trust among the EU Member States.[9]

The Brussels I Regulation, which is was one of the most important pieces of EU legislation found itself unable to give answers and solutions to several knotty procedural and substantive law problems thrown up by the workings of its provisions relating to arbitration.

There are number of reasons illuminating the background of the decision in West Tankers case, or in other words, explaining why CJEU could have not reached any other decision:

1. The ambivalence of Brussels I Regulation towards the major arbitration principles of party autonomy and competence-competence for the arbitral tribunal on one hand and the core principle of the Brussels I Regulation, namely the mutual trust, that a jurisdiction of one member state court could not be reviewed by courts of another member state, on another. In other words, the courts in a community as the EU must have the confidence that they are regarded as equal partners by their counterparts elsewhere in promoting their shared European values, regardless of all possible obstructions.
2. It is well known that the Commission as well as the CJEU in its decisions consistently favors whichever of several possibilities the most secures the objectives of the EU. As intended in the Brussels I Regulation, the object was, among other things, to create and maintain the above mentioned mutual trust, and with respect to this, favoring other alternatives over that of securing the sanctity of arbitration agreements.
3. It is a well-established principle in the EU law that, although a certain policy area falls within the competence of the Member States, the Member States must nonetheless exercise that competence consistently with EU law.[10]

9 West Tankers case, point 30.

10 Judgment of the Court of Justice of 11 August 1995. G. H. E. J. Wielockx v Inspecteur der Directe Belastingen. Case C-80/94, point 16.

4. The Brussels I Regulation excludes arbitration from its scope, however, and just like New York Convention before it, neither criteria nor guidelines were given in place to assist a court to decide, whether issues are better left for an arbitral tribunal or whether the issues are preliminary or even arbitrable at all. For example, such a court has jurisdiction to entertain question as to whether there was an arbitration agreement or not, then the mere mention of arbitration cannot by that fact alone oust the court's jurisdiction.[11]

One other important thing must be mentioned, namely that the scope of the arbitration exception has been controversial since the accession of the United Kingdom and Ireland to the Brussels Convention, and it has been a matter of dispute between common and civil law whether the arbitration exclusion should be interpreted broadly or narrowly. The reason for it is the different approach of common and continental law. While the common law approach seems to be that the provision should apply to all disputes that the parties have agreed to settle by arbitration, including any secondary disputes before a national court connected with the agreed arbitration, the civil law approach is that the scope should depend on the substantive subject matter of the dispute.[12] This is not surprising, because legal theorists around the world have been dealing with the question of legal nature of arbitration as such for more than 200 years.[13]

Furthermore, it should be taken into account, that parties to arbitration agreements become very human when once a dispute arises. In most cases, one party wants the arbitration clause adhered to and enforced, while the other would want it frustrated or "torpedoed", as actions to frustrate such arbitration contracts came to be known.[14]

Summarizing the above, the CJEU decision in West Tankers restricted the ability of English courts to issue an anti-suit injunction with respect

11 West Tankers case, point 22.

12 ELSING, Siegfried; TOWNSEND, John. Bridging the Common Law Civil Law Divide in Arbitration. *Arbitration International*. Vol. 18, No 1, p. 2 – 3.

13 RUŽIČKA, Květoslav. Rozhodčí smlouva. In PAUKNEROVÁ, Monika; ROZEJNALOVÁ, Naděžda (eds.). *Zákon o mezinárodním právu soukromém. Komentář.* Praha: Wolters Kluver ČR, 2013, p. 763.

14 IBEQE, Patrik. The Arbitration Exception and Provisional Measures in the New Regulation (1215/2012) [online]. In ExpressO. University Colledge Dublin, 2014 [cit. 2015-02-20].

to the other EU member states and this despite the fact that the anti-suit injunction was issued to uphold an arbitration agreement. This has the negative effect of clashing the Member States' obligations of the New York Convention with those of the Brussels I bis Regulation. In fact, the effect of West Tankers case is such that it shows precisely how a party that is not likely to succeed in arbitration, or for whatever reason does not want to be bound by the arbitration agreement, can at least for a time derail the arbitration by forum-shopping for a jurisdiction whereas to start a parallel judicial proceeding on the merits of the dispute.

3 Brussels I bis Regulation

In its Green Paper[15] the Commission made many proposals regarding the existence and scope of the arbitration exclusion from the Brussels I Regulation, some of them were very radical. One proposal even suggested deleting the arbitration exclusion from the Brussels I Regulation and adding a number of new rules regarding the co-ordination of arbitration related proceedings and the enforcement of arbitral awards.[16]

The Commission established an expert group to consider the interface between the arbitration and the Brussels I Regulation and the Commission's initial draft of Brussels I bis Regulation sought to address the West Tankers case problem. This initial draft retained the arbitration exclusion but added new text requiring a court seised of a dispute to stay proceedings if its jurisdiction was contested on the basis of an arbitration agreement and an arbitral tribunal had been seised of the case, or court proceedings relating to the arbitration agreement had been commenced in the Member State of the seat of the arbitration. The Commission also proposed a new rule specifying when an arbitral tribunal was deemed seised for these purposes. However, probably fearing that the "enhanced exclusion" may do more

15 Green Paper on the review of Council Regulation (EC) No 44/2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. In EUR-lex. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009DC0175&rid=1.

16 TROPP, Paul. Arbitration in the EU Following the Revised Brussels I Regulation. A Vote of Confidence for Arbitration, but Uncertainty Remains over 'Italian Torpedo' Actions [online]. In Freshfields Bruckhaus Deringer Knowledge and Insite – Briefing. 2013 [cit. 2014-03-14], p. 2 – 3.

harm than good, the result of the revision is unchanged arbitration exclusion with an added recital in the preamble.[17]

The explanatory recital expressly confirms categories of disputes falling outside the Brussels I bis Regulation regime. These are actions or proceedings ancillary to arbitration, including proceedings relating to the establishment of an arbitral tribunal, the powers of arbitrators, the conduct of an arbitration, or any action or judgment concerning the annulment, review, appeal, recognition or enforcement of an arbitral award and actions seeking or resisting the enforcement of an arbitration agreement, including disputes as to the validity, enforceability or operability of an arbitration agreement.[18]

In addition, the Art. 73(2) Brussels I bis Regulation specifically says that: "*This Regulation shall not affect the application of the 1958 New York Convention.*" The explanatory recital goes further, saying that the obligations of Member State courts under the Brussels I bis Regulation regime should be "without prejudice" to their competence to enforce arbitral agreements and/or awards under the New York Convention and that the New York Convention should "take precedence over this Regulation."[19]

In short, the Brussels I bis Regulation brought some clarification of the relations between arbitration and court proceedings in para 12 of the recital. Unfortunately, even these new explanations adopted only through special reflection in the recital do not fully preclude actions characterized as an Italian torpedo and in this respect the Brussels I bis Regulation did not deliver the expected solution.[20]

4 Impact of West Tankers and Brussels I bis Regualtion on the Arbitration Community

The interpretation of the interface between Brussels I Regulation and arbitration in West Tankers case given by the CJEU remains unpopular within

17 TROPP, Paul. Arbitration in the EU Following the Revised Brussels I Regulation. A Vote of Confidence for Arbitration, but Uncertainty Remains over 'Italian Torpedo' Actions [online]. In Freshfields Bruckhaus Deringer Knowledge and Insite – Briefing. 2013 [cit. 2014-03-14], p. 2 – 3.

18 *Ibid.*

19 *Ibid.*

20 PAUKNEROVÁ, Monika. *Evropské mezinárodní právo soukromé.* 2nd. Praha: C. H. Beck, 2013. p. 95.

the arbitration community. In a sense disappointment brings also the fact that the holding in West Tankers case has not been fully overturned by Brussels I bis Regulation. On the contrary, the EU institutions evidently do not want to fully address this issue.[21]

However, there is a silver lining for all supporters of arbitration in the EU. The Advocate General Melchior Wathelet ("AG") in his Opinion to Gazprom case[22] ("Opinion") has offered a different opinion related to the effect of the Brussels I Regulation in the present case connected with a request to enforce an arbitral award which has almost the similar effect as an anti-suit injunction and has therefore been of considerable interest to the arbitration community. In his Opinion AG concluded that the Brussels I Regulation as well as Brussels I bis Regulation do not require the court of a member state to refuse to recognize and enforce an anti-suit injunction issued by an arbitral tribunal and the fact that an award contains an anti-suit injunction is not a sufficient ground for refusing to recognize and enforce it on the basis of Article V(2)(b) New York Convention because the Brussels I Regulation is not a matter of public policy. His Opinion is the very first that considers its terms, and, if accepted by the CJEU, would lay down a marker for the interpretation of the arbitration exception within the Brussels I Regulation as well as Brussels I bis Regulation, with the effect that an anti-suit injunction issued by an arbitral tribunal would be recognizable and enforceable by Member State courts.[23]

For completeness, author of this paper cannot agree more with the view of AG, as the West Tankers case decision is from purely legal perspective precarious. It may lead in its consequences to endless obstructions in the form of procedural objections of a type that an award which is purely declaratory is not capable of enforcement in the United Kingdom or in any other member state, because it is inconsistent with Brussels I bis Regulation. Fact

21 TROPP, Paul. Arbitration in the EU Following the Revised Brussels I Regulation. A Vote of Confidence for Arbitration, but Uncertainty Remains over 'Italian Torpedo' Actions. [online]. In *Freshfields Bruckhaus Deringer Knowledge and Insite – Briefing.* 2013 [cit. 2015-03-14], p. 3.

22 Opinion of Advocate General Wathelet of 4 December 2014. 'Gazprom' OAO. Case C-536/13 („Opinion").

23 LEATHELY, Christian. Anti-suit Injunctions Within the EU: AG Wathelet Delivers his Opinion in Gazprom [online] In *Herbert, Smith, Freehills Arbitration notes* [cit. 2015-02-28].

is that Brussels I bis Regulation does not foresee, but also does not exclude, anything like this, therefore it remains an open question, whether arbitration agreement and the issues associated with it are pure matters of national arbitration law applying the New York Convention, and so the Brussels I bis Regulation is, in relation to this and other similar objections, simply irrelevant or not. The Brussels I bis Regulation's legislator could have constructed the same rule for an agreed arbitration clause, as he did in case of choice of court clause that is legally provided for in Article 25 in conjunction with Article 31(2) Brussels I bis Regulation, but he did not do so.

5 Conclusion

It is evident that the CJEU by deciding the West Tankers case simply found itself in circumstances, where it was obliged to navigate in uncharted terrains, and simultaneously had to satisfy and retain the respect of a wide range of interests. From this perspective it is understandable that it reached the decision it did. Of course, no spirited commentaries in defense of this and other decisions can change the fact that decisions like this were based more on necessity than on law or logic. The most cogent evidence for this conclusion is how far the Brussels I bis Regulation sought to accommodate the opposing view of the pro arbitration critics in the preamble.

It is perhaps inevitable that the principle of effectiveness of the New York Convention and principle of mutual trust collide within the EU and despite the Opinion, the CJEU may head off in the opposite direction and difficult issues will continue to arise in respect of the interface between the arbitration and the Brussels I bis Regulation.

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ENFORCEMENT OF FOREIGN ANNULLED ARBITRAL AWARDS

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Abstract

This paper focuses on the topic of recognition and enforcement of foreign arbitral awards which have been annulled in the country of their origin. The questions arising from this issue will be answered in the light of New York Convention and by the perspective of the Czech legal regulation. Firstly, it will briefly introduce two leading theories of arbitration since their proper understanding is necessary to follow later text. Secondly, it will examine content of Art. V New York Convention, namely the provision of Art.V(1) (e) which covers the problem of foreign annulled arbitral award. Then it will explain the effect of Art. VII New York Convention and at the same time it will show the relation between the New York Convention and national law. And finally, the paper analyzes current national law in the Czech Republic and its regulation of enforcement of foreign arbitral award that has been annulled. The paper concludes that though the New York Convention recognizes annulment of an award as one of the ground for refusal of enforcement, awards annulled in the country of their origin (primary jurisdiction) can be nevertheless enforced. When it comes to the Czech Republic, the national law comes from traditional theory and foreign annulled award cannot be enforced.

Keywords

Arbitration; Foreign Arbitral Awards; Annulled Arbitral Awards; Enforcement.

1 Introduction

This paper focuses on the topic of recognition and enforcement of foreign arbitral awards which have been annulled in the country of their origin.

The questions arising from this issue will be answered in the light of the New York Convention[1] and by the perspective of the Czech legal regulation.

The paper is organized in the following way. Firstly, it will briefly introduce two leading theories of arbitration since their proper understanding is necessary to follow later text. Secondly, it will examine content of Art. V New York Convention, namely the provision of Art. V(1)(e) which covers the problem of foreign annulled arbitral awards. Then it will explain the effect of Art. VII New York Convention and by doing so, it will show the relation between the New York Convention and national law. Finally, the paper analyzes current national law in the Czech Republic and its regulation of enforcement of foreign arbitral awards that have been annulled.

2 Traditional vs. Delocalization View

We can distinguish two different approaches while discussing recognition and enforcement of foreign arbitral awards – so called traditional one and delocalized one. The distinction between them lies in a different treatment of the fact that an award was annulled by the court of the primary jurisdiction.[2] Each of those theories grants different effects of this fact to the secondary jurisdiction.[3]

Traditional, sometimes also called territorialist, approach connects international arbitration with some national, primary, jurisdiction (*lex arbitri*). This approach is based on the view that though parties submit to arbitration contractually, it is still the national law which decides on validity of arbitration agreement. When the national law does not recognize the agreement between parties, the arbitration agreement does not exist.

The same logic is applied to the existence and validity of arbitral award which stems from the law of the country of origin.[4] Accordingly, when the court of primary jurisdiction annuls an award, the award is not valid

1 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf ("New York Convention").

2 I.e. the jurisdiction under which the arbitral award was rendered.

3 I.e. the jurisdiction under which enforcement of the arbitral award is sought.

4 DAVIS, Kenneth. Unconventional Wisdom: A New Look at Articles V and VII of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. *Texas International Law Journal* [online]. 2002, Vol. 37, No. 1 [cit. 2015-01-12], p. 58.

anymore. Traditional theory recognizes universal effect of such annulment which leads to the unenforceability in any other jurisdiction.[5]

On the other hand, the delocalization approach is based on an idea that international arbitration is not rooted in any national jurisdiction. Hence, it separates the existence of arbitral award from the law of the country of origin. Accordingly, a party may seek to enforce an award anywhere and every court must evaluate the validity of an arbitral award according to its own jurisdiction. This results to the position that potential annulment of an award should be applicable only in its own jurisdiction as the country of origin may not deprive the enforcing country of judicial power.[6] In other words, courts of secondary jurisdiction are not obliged to take an annulment by the courts of primary jurisdiction into consideration. [7]

The delocalization view is rather minor one and is not applied in many national laws. The most known supporter of this approach is undoubtedly France which, based on this view, recognized and enforced a series of annulled awards in the past.[8]

3 New York Convention

New York Convention is indisputably one of the most successful uniform law instruments so far – 154 States have adhered to it until today.[9] It outlines the rules to follow in granting recognition and enforce of foreign arbitral awards and sets limited number of grounds for refusing recognition and enforce. By doing so, New York Convention promotes worldwide simple enforcement of arbitral awards.[10]

5 THADIKKARAN, Manu. Enforcement of Annulled Arbitral Awards: What Is and What Ought to Be? *Journal of International Arbitration* [online]. 2014, Vol. 31, No. 5 [cit. 2015-01-12], p. 576.

6 DAVIS, Kenneth. Unconventional Wisdom: A New Look at Articles V and VII of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. *Texas International Law Journal* [online]. 2002, Vol. 37, No. 1 [cit. 2015-01-12], p. 58.

7 THADIKKARAN, Manu. Enforcement of Annulled Arbitral Awards: What Is and What Ought to Be? *Journal of International Arbitration* [online]. 2014, Vol. 31, No. 5 [cit. 2015-01-12], p. 576.

8 Probably the most famous decision enforcing annulled award is so called Hilmarton case (Decision of the Cour de cassation, France of 23 March 1994, No. 92-15.137).

9 For the list of the current Contracting States see: *Status. Convention on the Recognition and Enforcement of Foreign Arbitral Award (New York, 1958)* [online]. United Nations Commission on International Trade Law (UNCITRAL) [cit. 2015-01-14].

10 SMITH, Erika. Vacated Arbitral Awards: Recognition and Enforcement Outside the Country of Origin. *Boston University International Law Journal* [online]. 2002, Vol. 20 [cit. 2015-01-14], p. 356.

3.1 Art. V(1)(e)

New York Convention obliges Contracting States to recognize arbitral awards as binding and therefore enforce them when all the requirements of the convention are fulfilled. At the same time, it establishes grounds for the denial of enforcement. For purposes of this article, we have to examine Art. V(1)(e) New York Convention which deals with enforcement of nullified award and reads as follows:

> *"[r]ecognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that…*
>
> *(e) the award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made."*

The wording of Art. V(1)(e) enables courts of Contracting States to decline enforcement of annulled awards. It however does not oblige them to do so. The permissive "may"[11] gives the courts discretion to choose whether they will or will not enforce such an award. This interpretation is also accepted by leading commentators to the New York Convention.[12]

There also exists minor opinion dissenting to this interpretation. The position is based on the argument that the combination of the words "may" and "only" in Art. V could mean that the list of grounds for non-enforcement is exclusive and once such a ground is established non-enforcement is mandatory. In other words, supporters of this view state that because enforcement "may only" be refused while applying Art. V ground, courts have to refuse enforcement once such a ground is proven.[13]

This opinion must be rejected. Such interpretation is contrary to Art. VII New York Convention whose purpose is to maximize enforcement of awards. Art. VII will be discussed below.

11 Or the corresponding equivalents in other authentic language versions.

12 BORN, Gary B. *International Commercial Arbitration*. Second volume. Austin: Wolters Kluwer, 2009. p. 2722 - 2723; BERG, Albert Jan van den. *The New York Arbitration Convention of 1958*. The Hague: T.M.C. Asses Institute, 1981. p. 265; ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Second edition. Praha: ASPI, 2008. p. 333.

13 DAVIS, Kenneth. Unconventional Wisdom: A New Look at Articles V and VII of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. *Texas International Law Journal* [online]. 2002, Vol. 37, No. 1 [cit. 2015-01-12], p. 60.

What is more, the New York Convention uses the word "shall" in different parts of its text,[14] e.g. Art. I, Art. II or Art. VII. It is therefore reasonable to assume that drafters of the New York Convention did not intend to make Art. V mandatory. If they did, they would have used word "shall" instead of "may". By choosing this wording the drafters made a clear intention to make Art. V a discretional one.[15]

New York Convention does not provide any guidance to assist courts to decide in what cases they should enforce annulled awards and in what cases they should not. The decision of the court therefore depends particularly on the theory of arbitration which is respected in the state of enforcement. For countries where territorial theory is applied the enforcement is usually refused and on the other hand in countries where delocalization theory is applied the annulled award is usually enforced.

3.2 Art. VII

Art. VII New York Convention, often referred to as "most-favored-right rule", states that:

> *"The provisions of the present Convention shall not […] deprive any interested party of any right he may have to avail himself of an arbitral award in the manner and to the extent allowed by the law or the treaties of the country where such award is sought to be relied upon."*

Art. VII establishes system with two possible ways of enforcement of foreign award - under the New York Convention and under the national law or the treaties of the country where the enforcement is sought. Such interpretation of Art. VII was confirmed by UNCITRAL during its 39th meeting in 2006.[16] The decision which set of rules (New York Convention / national

14 PARK, William. Duty and Discretion in International Arbitration. *American Journal of International Law* [online]. 1999, Vol. 93, No. 4 [cit. 2015-01-13], p. 812.

15 DAVIS, Kenneth. Unconventional Wisdom: A New Look at Articles V and VII of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. *Texas International Law Journal* [online]. 2002, Vol. 37, No. 1 [cit. 2015-01-12], p. 60.

16 *Recommendation regarding the interpretation of Article II, paragraph 2, and Article VII, paragraph 1, of the Convention on the recognition and enforcement of foreign arbitral awards, done in New York, 10 June 1958, adopted by the United Nations Commission on International Trade Law on 7 July 2006 at its thirty-ninth session* [online]. United Nations Commission on International Trade Law (UNCITRAL) [cit. 2015-01-14].

law) shall be applied on the enforcement depends on the will of the party. Party has to base his request for enforcement only on one of those regulations and it is not allowed to combine those regulations.[17]

Generally speaking, Art. VII New York Convention permits the enforcement of foreign awards if enforcement is permitted under the domestic law of the enforcing country even though it is not permitted under the New York Convention. The same applies to the enforcement of arbitral award after its annulment in primary jurisdiction – in case that national law of secondary jurisdiction does not treat it as a ground for refusal, such an award can be enforced. Whether national law permits such enforcement, depends on the theory (traditional/delocalized view) that is applied in the country.

The typical example of application of Art. VII is France where the provision is used to enforce annulled foreign arbitral award because French national law governing enforcement of such awards is in fact more favored than the regulation in the New York Convention. The matter is covered by Art. 1502 New Code of Civil Procedure which says that the order enforcing a foreign award may be appealed only in the following cases:

1. *if the arbitrator has rendered his decision in the absence of an arbitration agreement or on the basis of an arbitration agreement that is invalid or that has expired;*
2. *if the arbitral tribunal was irregularly constituted or the sole arbitrator irregularly appointed;*
3. *if the arbitrator has not rendered his decision in accordance with the mission conferred upon him;*
4. *if due process has not been respected;*
5. *if recognition or enforcement is contrary to international public policy.*[18]

Because a sole annulment of an award in a country of its origin is not listed the re, such awards can be and are enforced in France (provided that any other ground for refusal is occurs).

17 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. Second edition. Praha: ASPI, 2008. p. 96.

18 KOCH, Christopher. The Enforcement of Awards Annulled in their Place of Origin: The French and U.S. Experience. *Journal of International Arbitration* [online]. 2009, Vol. 26, No. 2 [cit. 2015-01-15], p. 269-270.

4 The Czech Republic

International arbitration in the Czech Republic is regulated by the Private International Law Act ("PILA")[19] which is effective only since 1 January 2014.

For the purposes of PILA arbitral award shall be deemed as foreign when it was rendered on the territory of foreign country. This distinction between domestic and foreign award ensues from regulation in the UNCITRAL Model Law[20] and is also applied for example in Germany, England or Switzerland.[21]

Place of arbitration is the only criterion which has to be examined in order to determine whether arbitral award shall be governed as domestic one or as foreign one. In other words, it is not important under which legal order the arbitration was conducted, where the hearings took place or what the nationality of the arbitrators was. Only the place where the award was made, i.e. territorial criterion, is decisive.[22]

Matters of recognition and enforcement of foreign arbitral awards are governed by Sec. 121 PILA which reads as follows:

> *"Recognition or enforcement of a foreign arbitral award will be denied if the foreign arbitral award:*
>
> a) *is not final or enforceable under the law of the State in which it was issued,*
>
> b) *was annulled in the state where it was issued or under whose law it was issued,*
>
> c) *is vitiated by an error which leads to the annulment of a czech arbitration award by the court, or*
>
> d) *is contrary to public policy."*

Grounds for denial of recognition and enforcement are very similar, almost identical, to those in the New York Convention.[23] The main difference between the Czech regulation and the New York Convention lies

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19 CZECH REPUBLIC. Act No. 91/2012 Coll., on private international law.

20 UNCITRAL Model Law on International Commercial Arbitration 1985. With amendments as adopted in 2006 [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf

21 DRLIČKOVÁ, Klára. *Vliv legis arbitri na uznání a výkon cizího rozhodčího nálezu*. Brno: Masarykova univerzita, 2013. p. 23.

22 PAUKNEROVÁ, Monika; ROZEHNALOVÁ, Naděžda et al. (eds.). *Zákon o mezinárodním právu soukromém: komentář*. Praha: Wolters Kluwer, 2014. p. 794.

23 *Ibid*., p. 799.

in the application of the grounds. While in case of the New York Convention the courts have a right to refuse enforcement when debtor proves the existence of one of the grounds, in case of the PILA, the courts are obliged to refuse enforcement when they become aware of existence of any of the grounds.[24] To be precise, some grounds in the New York Convention have to be concerned even without a proposal of debtor (Art. V(2)), but the ground based on nullity of an award is, however, not one of them.

Regulation of recognition and enforcement of a foreign award in PILA is therefore much more strict then the one in the New York Convention. One can therefore ask himself when and why party would choose to seek enforcement under the Czech legislation instead of the convention. *Rozehnalová* believes that the application of the Czech regulation could be only interested in cases where the written form of an arbitral agreement was not fully complied.[25] That is because the conditions of form of an arbitral agreement are the only matter for which the Czech regulation indicates milder requirements.

Before 1 January 2014 the issue of recognition and enforcement of foreign arbitral awards was regulated in Sec. 39 Arbitration Act.[26] It is somewhat surprising that the current reasons for denial do not entirely correspond with the antecedent legislation. Or to be precise, letters a), c) a d) do correspond, but current legislation defines new reason for denial of recognition and enforcement – annulment of the award in the state where it was issued or under whose law it was issued.

Explanatory report to the PILA does not clarify this change and new approach. It only says that regulation of recognition and enforcement of foreign arbitral awards is based on the (then) existing regulation.[27]

24 BŘÍZA, Petr. *Zákon o mezinárodním právu soukromém: komentář.* Praha: C. H. Beck, 2014. p. 702.

25 ROZEHNALOVÁ, Naděžda. Návrh zákona o mezinárodním právu soukromém – dopady do obchodní oblasti. *Obchodněprávní revue*. 2011, Vol. 3, No. 10, p. 293.

26 CZECH REPUBLIC. Act No 216/1994 Coll., on arbitration proceeding and on enforcement of arbitral awards.

27 Důvodová zpráva k ZMPS [online]. *Nový občanský zákoník*. Ministerstvo spravedlnosti České republiky [cit. 2015-01-15]. Available at: http://obcanskyzakonik.justice.cz/file-admin/Duvodova-zprava-k-ZMPS.pdf

It unfortunately does not comment on the fact that the new legislation actually introduces new ground for denial.

Motivation of the legislator to increase the number of grounds for denial can be therefore only theoretically discussed. It is an author's opinion that letter b) was most probably added in order to confirm what legal theory was already deriving anyway, i.e. annulled arbitral award is not enforceable and therefore cannot be enforced based on ground establish in letter a) of Sec. 121 PILA which corresponds with previous legislation.

To sum up, the Czech Republic applies traditional view when it comes to recognition and enforcement of foreign arbitral awards. Therefore it is generally forbidden to enforce arbitral award there in case that the award was annulled in its state of origin. However, as explained earlier in this paper, when party seeks for enforcement under the New York Convention instead of the PILA, a judge can theoretically apply Art. V(1)(e), therefore decide upon his discretion and enforce such annulled arbitral award anyway. In author's opinion this scenario is however not very likely to happen in the Czech Republic.

5 Conclusion

This paper analysed the issue of enforcement of foreign annulled arbitral awards. It concluded that though the New York Convention recognizes annulment of an award as one of the ground for refusal of enforcement, awards annulled in the country of their origin (primary jurisdiction) can be nevertheless enforced. That is firstly because Art. V(1)(e) is of discretional nature. Secondly, party can also successfully seek the enforcement under law of the secondary jurisdiction and some countries' national laws do not considered an annulment as a ground for non-enforceability. Countries' approaches to this question usually arise from the fact whether the country support traditional (territorialist) or delocalization view.

When it comes to the Czech Republic, the national law comes from traditional theory and foreign annulled awards cannot be enforced. Hence, if the party sought for enforcement of such award in the Czech Republic, it would almost certainly fail in doing so. It is author's opinion that such party would fail even if it tried to support its position with discretional nature of Art. V(1)(e) New York Convention.

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INTERNATIONAL INVESTMENT ARBITRATION

INVESTOR´S NATIONALITY AS A CONDITION RATIONE PERSONAE IN INTERNATIONAL INVESTMENT ARBITRATION UNDER ICSID CONVENTION

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Abstract

This paper focuses on exploring how nationality of an investor (either natural or legal person) plays a crucial role in establishing ratione personae jurisdiction of arbitration tribunal in investment disputes. The paper examines two current challenges in assessing the jurisdiction ratione personae: i) specific cases when an investor (natural person exercising effective control in the investment structure) is holder of nationalities, one of them being a nationality of a host state and ii) the so-called nationality planning, which refers to planning a structure of a legal entity (ownership and shareholder structure) so that the entity can benefit from the most suitable investment protection regime.

Keywords

Bilateral Investment Treaties (BIT); Dual Nationality; Investor; ICSID; Nationality Planning; National Gas S.A.E. v. Arab Republic of Egypt; Phoenix Action; Ltd. v. The Czech Republic; Burumi and Eagle Games v. Republic of Albania.

1 Investment Dispute Arbitration

1.1 Creating International Regime of Protection to Attract Foreign Investments

In today's global economy, investments in foreign countries represent an important business strategy for legal entities as well for natural persons

and such cross-border investment is likely to create certain economic advantages and boost the overall economy of a country receiving the investment (host state). However, investors might hesitate investing in a foreign country since there do exist real risks stemming from foreign investment, such as potential political instability, uncertain regulatory regimes, or risks of expropriation.

In order to attract investors to invest in countries other than their homeland, international community has made efforts to create effective legal tools granting protection of foreign investment in host states and as a result of such efforts, international investment law, as a new branch of law, has appeared. This area of law can be characterised as an area featuring many specifics, which have been undergoing a gradual separation from the main stream of international legal practice, and have been evolving into a *sui generis* domain of international legal practice.[1]

Whilst recognising the multitude of international legal instruments existing under international investment law, this paper places its primary focus on the system of protection under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States ("ICSID Convention")[2] and bilateral investment treaties ("BIT").

1.2 Investment Disputes Resolution - ICSID Convention and ICSID Centre

ICSID Convention represents a key document within the system of international protection of foreign investments. Its final text being a result of work of the expert group set-up by the World Bank, the ICSID Convention has become widely recognised – as of 2015, it has been signed and ratified by over 150 states.

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1 BELOHLAVEK, Alexander J. Institutionalized Promotion and Protection of Investments in the Energy Sector. In BELOHLAVEK, Alexander J.; ROZEHNALOVA, Naděžda; CERNY, Filip (eds.). *Czech Yearbook of International Law 2014: The Role of Governmental and Non-governmental Organizations in the 21st Century*. New York: Juris Publishing, Inc., 2014, p. 107 - 108.

2 Convention on the Settlement of Investment Disputes between States anad Nationals of Other States (Washington, 1966) [online]. *International Centre for Settlement of Investment Disputes*. Available from: https://icsid.worldbank.org/apps/ICSIDWEB/icsiddocs/Documents/ICSID%20Convention%20English.pdf

In the 1960 s, even before adoption of the ICSID Convention, BITs began to appear. Whilst the exact content of each individual BIT may vary, in general that every BIT defines the notion of investment, sets forth broad undertaking to guarantee investment's protection and provides for a dispute resolution mechanism in case dispute arises between investor and a host state. With regards to dispute mechanism, BITs usually contain a clause according to which the disputes arising between investor and a host state concerning the investment are to be submitted to International Centre for Settlement of Investment Disputes ("ICSID" or the "Centre"), which is a judicial organ established under the ICSID Convention for resolving the international investment disputes. The Centre is nowadays considered to be the leading international arbitration institution devoted to resolving disputes between States and foreign investors.

1.3 Determining the Jurisdiction of the ICSID

When the case is brought to the attention of ICSID, the tribunal composed of arbitrators is appointed to decide the case. Upon receiving the claimant's claim, ICSID proceeds to determine whether it has the jurisdiction to resolve the dispute. In order to determine the existence of its jurisdiction in any given case, ICSID tribunal has to analyse the fulfilment of the requirements set in the ICSID Convention, and the requirements of the contract, the national law, the BIT of the multilateral treaty providing for the submission of investment disputes to ICSID arbitration.[3]

ICSID Convention sets forth the requirements of meeting the conditions *ratione personae*, *ratione materiae*, *ratione voluntatis* and *ratione temporis.*

Condition *ratione materiae* is satisfied when the dispute brought before the ICSID tribunal is a legal dispute arising directly out of an investment (the definition of term „investment" is often found in a particular BIT, under which the claim is brought before ICSID).

3 ICSID Case No. ARB/06/5, Phoenix Action, Ltd. v. the Czech Republic [online]. In *italaw* [cit. 2015-09-27], point 52.

Condition *ratione voluntatis* is satisfied when there is a consent in writing that the dispute be settled through ICSID arbitration. When concluding the BIT, state parties usually expressly agree that any investment dispute arising under it shall be submitted to ICSID.

In order to satisfy the condition *ratione temporis,* the ICSID Convention must have been applicable at the relevant time, i.e. during the period when the alleged acts violating the rules on protection of investment were committed by the host state.

Finally, condition *ratione personae* is satisfied when the dispute opposes a host state and an investor - national of another state (party to the ICSID Convention, other than the host state).

The ICSID Convention sets the limitation to investor´s nationality in investment disputes. The following part of the paper critically analyses how the Centre is applying the limitation to nationality in specific circumstances.

2 Specific Challenges when Assessing Ratione Personae

Investor´s nationality plays a crucial role when gaining access to the investment arbitration.

As professor *Schreuer* expressed in his work, there is a certain paradox in assessing the importance of the issue of nationality in investment dispute resolution: "W*hen it comes to access to investment arbitration, or generally to protection under BIT, nationality is extremely important. A lot of ink is split and lot of time is spent to prove a particular nationality. However, when the case reaches the merits, strangely enough, distinction on the basis of nationality is prohibited.*"[4]

In order to gain access to dispute settlement under the ICSID Convention, there is a positive as well as negative nationality requirement: an investor is required to be national of a state that is party to the ICSID Convention and the investor must not be a national of a host state (he can only be a national of "another contracting state").[5]

4 SCHREUER, Christoph. Nationality of Investors: Legitimate Restrictions vs. Business Interests. *ICSID Review*. 2009, Vol. 24, No. 2.

5 *Ibid.*

The limitation of investor's nationality is expressed in Article 25(2)(a)(b) ICSID Convention, which reads:

"National of another Contracting State means:

a) *any natural person who had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration as well as on the date on which the request was registered pursuant to paragraph (3) of Article 28 or paragraph (3) of Article 36, but does not include any person who on either date also had the nationality of the Contracting State party to the dispute; and*

b) *any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention."*

2.1 Investor – a Dual National

Specific challenges to the assessment of *ratione personae* may arise when investor is a dual national, i.e. holder of a nationality of more than one state; especially if one of the nationalities is also the one of the host state. According to a general principle of international law stating that states cannot be sued internationally by their own nationals, foreign investor holding also a nationality of a host state is likely to be banned from international investment protection regime.[6]

Challenge arising from assessing the status of dual nationals in investment arbitration is particularly obvious when there is a dispute in which claims are made by an investor – legal entity, incorporated in a host state, in which an "ultimate effective control" is exercised by a natural person – a dual national of a host state. In such case, the arbitration tribunal needs to determine whether the condition of "foreign control" under Article 25(2)(b) is met even if the ultimate control of the company is in the hands of an individual holding also a nationality of a host state.

6 MUCHLINSKI, Peter; ORTINO, Federico; SCHREUER, Christoph. *The Oxford Handbook of International Investment Law*. Oxford: Oxford University Press, 2008. p. 889.

Reasons for which persons can become holders of dual (or even multiple) nationality are various, usually they result from diverging approaches to granting nationality in national legal systems.[7] Even though the concept of dual nationality used to be considered as something undesirable that need to be avoided at all costs, in the past decades the international community has witnessed the increase of dual nationality and the international community has started to adopt a trend towards acceptance of dual nationality.[8]

The ICSID has already had several occasions to deal with situation in which investor was a dual national. It has already been suggested that the concept of "effective nationality" may provide a solution to the definition of nationality in the ICSID Convention.[9] However, the paper re-examines this concept in the light of more recent case law of the ICSID tribunals and restates the argumentation in favour of the concept of effective nationality as a means of determining the "true" nationality of an investor, based on which jurisdiction or lack of jurisdiction of the ICSID tribunal can be determined. This re-examination proves to be useful, taking into account the fact that the ICSID tribunals have established a trend of lifting the corporate veil and carefully searching for natural persons executing the ultimate control over the locally incorporated corporations (investors), and the fact that the dual nationality is on the rise on the global scale, which suggests that another cases in which ISCID Tribunals will have to deal with dual nationality are yet to come.

2.1.1 Dual Nationality in the Case Law of ICSID

The wording of Article 25(2)(a) ICSID Convention suggests that if an investor is a dual national and one of his or her nationalities is that of a host state, the jurisdiction of the Centre has to be denied.

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7 For example, if a child is born to parents – nationals of a country granting citizenship on the basis of the principle of *jus sanguinis* on the terriotry of the state following the principle of jus soli, the child is entitled to two citizenships (one of his/her parents and one of the country in which the child is born). For further details, see: KIVISTO, Peter; FAIST, Thomas. *Citizenship. Discourse, The ory, and Transnational Prospects.* Malden: Blackwell Publishing, 2007. p. 106.

8 MARTIN, David. *Rights and Duties of Dual Nationals*. Kluwer Law International. 2003. p. 3 - 4.

9 MUCHLINSKI, Peter; ORTINO, Federico; SCHREUER, Christoph. *The Oxford Handbook of International Investment Law*. Oxford: Oxford University Press, 2008. p. 885.

Such restrictive approach towards dual nationals was confirmed in the relevant case-law of the Centre. In Burimi & Eagle Games v. Albania[10] the ICSID tribunal held: "*The ICSID Convention makes it very clear that a dual national may not invoke one of his two nationalities to establish jurisdiction over a claim brought in his own name under Article 25(2)(a).*"

Furthermore, the ICSID tribunal in this particular case elaborated that the principle against the use of dual nationality as set in Article 25(2)(a) "*should be applied to the cases falling within the scope of Article 25(2)(b) otherwise any dual national who is national of Contracting State to a dispute could circumvent the bar on claims in Article 25(2)(a) by establishing a company in that state and asserting foreign control of that company by virtue of his (foreign) nationality.*"

The above stated interpretation was also reiterated in more recent ICSID case National Gas S.A.E. v. Arab Republic of Egypt.[11]

In this case, the claimant was a joint stock company National Gas S.A.E. incorporated under the laws of Arab Republic of Egypt (Egypt), whilst majority of its shares was owned by another legal entities established in United Arabic Emirates (UAE). The more exact corporate structure of the claimant can be explained as follows: National Gas S.A.E. was owned by UAE company, which in turn was owned by another UAE company and both of these companies were indeed shell companies fully controlled by a physical person, Mr. Ginena, who was a national of Egypt and also claimed he was a national of Canada.

The claim was brought under Egypt - UAE BIT and the claimant's main argument was that its investment in Egypt was endangered by expropriation performed by Egypt through denial of justice and abuse of process. Claimant relied on UAE-Egypt BIT allowing for a situation in which, to put it simply, foreign control of a company established under law of one state may be defined as a foreign investment in that state. The responded opposed

10 ICSID Case No. ARB/11/18, Burimi Srl. and Eagle Games Sh.A. v. Republic of Albania [online]. In *italaw* [cit. 2015-09-27].

11 ICSID Case No. ARB/11/7, *National Gas S.A.E. v. Arab Republic of Egypt [online]*. In *italaw* [cit. 2015-09-27].

the argument of foreign control, relying on the fact that the true controller of the claimant was Mr. Ginena, who is a national of a state party to dispute, which should prevent the jurisdiction of the ICSID.

The ICSID tribunal, whilst reiterating that "foreign control" must satisfy also an objective test, confirmed that Mr. Ginena should be regarded as the true controller of the claimant since he controls the claimant in commercial reality.[12] The nationality should be the key element in assessing the tribunal's jurisdiction.

The tribunal held that Mr. Ginena was a dual national and thus general limitation (provided for in Art. 25(2) ICSID Convention) should be applied in this case. The tribunal even admitted that if the circumstances of the case where different – such as if a true controller was not a dual national – the tribunal would assume its jurisdiction. However, in this case, the tribunal recalled the principles set already in Burimi & Eagle Games v. Albania case (cited above) and rejected its jurisdiction. Even though Mr. Ginena advanced the argument that he is to be considered as a national of Canada for the purposes of "foreign control", the tribunal dismissed this argument by stating that deemed Canadian nationality cannot be factor under Article 25(2)(b) ICSID Convention, and for that purpose, he was and remains a dual national of Egypt and Canada.

The above-mentioned argumentation put forward in ICSID arbitration awards suggests that ICSID tribunals tend to adopt a restrictive approach towards investors-dual nationals when determining the jurisdiction. In its next sub-section, this paper aims to deal with the question whether such approach is in compliance with principles of international law in the matters of dual nationality.

2.1.2 Dual Nationality and ICJ – Principle of Genuine Link

The issue of dual nationality was addressed in the International Court of Justice ("ICJ") case known as Nottebohm case (Lichtenstein v. Guatemala).[13]

12 ICSID Case No. ARB/11/7, *National Gas S.A.E. v. Arab Republic of Egypt [online]*. In *italaw* [cit. 2015-09-27], point 144.

13 Judgment of the International Court of Justice of 6 April 1955, Nottebohm case (Lichtenstein v. Guatemala) [online]. *International Court of Justice* [2015-09-27].

In this case the ICJ expressed its view on the definition of the term nationality:

"According to the practice of States, to arbitral and judicial decisions and to the opinions of writers, nationality is a legal bond having as its basics a social fact of attachment, a genuine connection of existence, interests and sentiments, together with the existence of reciprocal right and duties. It may be said to constitute a juridical expression of the fact that the individual upon whom it is conferred, either directly by the law or as the result of an act of the authorities, is in fact more closely connected with the population of the state conferring nationality than with that of any other state.

Conferred by a State, it only entitles that State to exercise protection vis-a-vis another State, if it constitutes a translation into juridical terms of the individual's connection with the State which has made him its national."

As the cited definition suggests, it order to determine the nationality of state, it is crucial to establish whether there exists a link between a state and its alleged national.[14] In fact, the Nottebohm case dealt with the issue of the doctrine of the so-called "genuine link" between an individual and a state.

The background of the case is that Mr. Nottebohm, a German national living in Guatemala has decided, shortly before the outbreak of the World War II ("WWII") to obtain a nationality of another country – Lichtenstein. In order to do so, Mr. Nottebohm came to Lichtenstein and applied for obtaining nationality through a process of naturalisation. He paid certain fee that according to applicable legal provisions allowed him to acquire nationality without the need of proving the permanent residency in the country. However, upon his return to Guatemala and after the declaration of WWII, he was arrested in Guatemala and held in custody on the grounds of being a national of enemy state – Germany. Competent authorities of Guatemala did not accept the argument of Mr. Nottebohm according to which he was not supposed to be regarded as a national of Guatemala, since he successfully acquired nationality of Lichtenstein and Mr. Nottenbohm was kept in custody and his possession was confiscated. On the basis of the institute of diplomatic protection, Lichtenstein defended the claims of Mr. Nottenbohm.

14 EWERLING, Viktor. Medzinárodné, európske a národné právne aspekty spornej úpravy maďarského občianstva. *Bulletin slovenskej advokácie*. 2011, No. 9, p. 26 - 27.

The ICJ held that in this particular case, there is a lack of a genuine link between a state (Lichtenstein) and its citizen (Mr. Nottebohm) and therefore, there are no grounds for application of diplomatic protection.

This case has been a subject to vivid scholarly discussion,[15] nevertheless, one aspect of this judgment seems to bear certain importance – that nationality of an individual does not need to be accepted automatically by third states, but they have a right to "verify" whether there is a genuine link between the individual and a state and decide whether they will treat this individual as a national of this particular state the national of which he claims to be or appears to be.

The application of this principle in investment arbitration could be an effective way of dealing with specific problematic issues of establishing nationality of an investor – when the investor appears to be a national of two states, arbitration body would examine the existence of the genuine link and decide on its jurisdiction based on such examination.

2.1.3 Partial Conclusion

Taking into account the result of the National Gas S.A.E. v. Arab Republic of Egypt case, it appears that at least as far as arbitration under BITs is concerned, ruling of Nottebohm case has been laid to rest and a doctrine of genuine link will not overcome the general limitation imposed on investors-dual nationals in Art. 25(2)(a) ICSID Convention. Such approach suggests that there might be a clash between principles of investment law and principle of genuine link established in international law.

It is noteworthy to point out that the ICSID tribunals, by applying this restrictive approach to investors - dual nationals somehow "lessen" the legal effects of nationality of investor – as if the mere existence of dual nationality would automatically mean that the effects of one of those nationalities cannot be fully enjoyed.

15 Among scholars and commentators, this judgment, or certain aspects of this judgment, generated some controversy and have been subject to critique. See, for example: SLOANE, Robert D. Breaking the Genuine Link: The Contemporary International Legal Regulation of Nationality. *Harvard International Law Journal.* 2009, Vol. 50*,* No. 1, p. 3 - 4.

The base for such reasoning is that investor cannot rely on this nationality for the purposes of investment dispute arbitration to establish that he is a "national of other contracting state". The tribunals expands this principle in order to reject jurisdiction on the grounds of the lack of "foreign control" in the corporate structure of investor-legal entity controlled by a natural person, holder of dual nationality status.

Such expansive interpretation and the consequent denial of jurisdiction, without further examining the specific circumstances behind the status of a dual national, suggests, to certain extent, that tribunals (and drafters of the ICSID Convention) might have assumed that in investment law, investors would speculate and become dual nationals only to gain access to arbitration.

Certainly, drafters of the ICSID Convention intended to provide for a strong protection against a possible abuse of right, which is a real risk. However, abuse of right should not be assumed; rather, ICSID tribunals should be willing to examine in further details whether an investor invokes his other nationality out of pure speculation, or simply as a result of an existing economic reality. After all, there could be instances when one nationality is a purely formal one and does not reflect any deeper link to state. In Burimi and Eagle Games v. Albania case and National Gas SAE v. Egypt case, it seems that not enough focus was placed on the necessity to examine whether host state's nationality of an investor is not only a "formal" one; hypothetically, if host state's nationality was indeed only a formal one, Tribunal could have established a foreign control and accept its jurisdiction.

2.2 Nationality Planning

Nationality planning concerns legal persons. Nationality of legal persons is a complex issue and there are no universally applicable rules to it; states determine in their own national legislation under what conditions thee regard legal persons as their nationals. Companies today operate in ways that can make it rather troublesome to determine their nationality. Tribunals have usually adopted the test of incorporation or seat rather than control when determining the nationality of a juridical person, unless the test of control is provided for in the agreement.[16]

16 *International Investment Law: Understanding Concepts and Tracking Innovations.* OECD, 2008.

It follows that a legal person can actually determine its own corporate structure so that is can acquire certain nationality. In investment law, nationality planning means setting a corporate structure that would allow acquiring nationality that seems to be the most benefiting for the purposes of investment protection.

It is not unusual for a prudent investor to carefully decide on the company structure - advantages anticipated often include the protection of particular bilateral or other treaty covering foreign investment. Arbitration tribunals accept this and do not automatically consider nationality planning illegal or prohibited.

However, the questions arise: to what extent is it possible for the investor (legal person) to structure its nationality in order to benefit from the most convenient regime of investment protection? What is the threshold to establish that certain structure and resulting acts amount to the abuse of rights?

There certainly are limits to nationality planning and ICSID Tribunals have already denied its jurisdiction when it came to the conclusion that certain nationality was acquired in a speculative manner.

Phoenix Action, Ltd. v. Czech Republic is an ICSID case in which the legal entity established under the law of Israel brought a claim under Israeli-Czech republic BIT to the attention of ICSID tribunal on the ground that its investment in the Czech Republic is endangered by the repressive actions taken by Czech authorities.

The background of the case is that there were two Czech companies against which various legal proceedings were initiated and repressive actions were involved (freeze of companies' assets). The owner of these Czech companies then transferred his interest to an Israeli company which subsequently brought claim before ICSID tribunal. Acquisition of a Czech company was regarded as investment under the Czech – Israeli BIT, thus the condition *ratione materiae* was satisfied.

The ICSID tribunal stated that "*investor cannot modify the protection granted once the acts damaging its investments have already been committed*" and found it had no jurisdiction to consider claims that had arisen prior to the alleged investment by the Israeli company.

Tribunal was particularly concerned with the fact that the claimant had made an investment not for the purpose of engaging in economic activity but for the sole purpose of bringing international arbitration against the Czech Republic.

3 Conclusive Remarks

The paper shows that ICSID tribunals have adopted slightly different approaches when dealing with particular challenges to assessment of condition of *ratione personae*.

When an investor is a dual national, whilst being a holder of a nationality of a state party to dispute of a state party to dispute, the tribunal denies its jurisdiction without even considering applying the principle of a genuine link.

On the other hand, tribunals seem to be willing to examine background of acquiring nationality of a legal persons for the purposes of investment arbitration in order to find out whether legal person merely used available advantages offered by legal order or whether it misused the concept of nationality planning and made use of the system to gain access to arbitration in highly speculative manner.

It follows that there might be time for the ICSID to reconsider the relevance of principle of genuine link and reconsider whether it would not be appropriate to be willing to examine the "true" nationality of investor-natural person, just as much as it is willing to evaluate the complex issue of nationality of investors-legal persons.

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Court decisions and arbitral awards

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ISSUE OF ATTRIBUTION IN INTERNATIONAL INVESTMENT DISPUTES - THE ICSID HAMESTER CASE

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Abstract

In the field of foreign investment, matters of state responsibility and attribution play a very important role. This article addresses the attribution issues of state responsibility in an investment dispute case under International Centre for Settlement of Investment Disputes (ICSID) - Gustav F W Hamester GmbH & Co KG v. Republic of Ghana. Research within this article focuses on summarizing the key elements of attribution relating to state responsibility within the work of the International Law Commission (ILC) and tries to give an overview of the investment case and author's opinion and conclusions on the legal arguments presented in the final decision, relating to attribution. One of the challenges to the resolution of this particular dispute case is the specific approach of the relevant Tribunal.

Keywords

Attribution; Customary International Law; International Investment Dispute; State Responsibility.

1 Introduction

In my article I would like to address the attribution issues of state responsibility in an investment dispute case under the International Centre for Settlement of Investment Disputes ("ICSID") - Gustav F W Hamester GmbH & Co KG v. Republic of Ghana ("Hamester case").[1]

1 Award of ICSID Tribunal of 18 June 2010, No. ARB/07/24, Gustav F W Hamester GmbH & Co KG v. Republic of Ghana [online]. In *italaw* [cit. 2015-03-22] ("Hamester case").

In the field of foreign investment, matters of state responsibility and attribution play a very important role. Under customary international law, a state is responsible for all its organs as well as for its territorial units such as provinces and municipalities. The principle applies to organs at all levels and positions in the state's administrative organization and extends to all branches of the government, that is, to the executive, the legislature, and to the judiciary. In general, matters of state responsibility, including attribution are regulated in customary law. Exceptionally, there are provisions in treaties that provide for the responsibility of states for action of their entities.

The relevant rules of attribution of conduct to a state are set out in Chapter II of the Draft Articles on Responsibility of States for Internationally Wrongful Acts ("Draft Articles") from the work of International Law Commission ("ILC").[2] The purpose of the work carried out by the ILC was partly to avoid situations where no state could be held accountable for actions or omissions, which implies a breach of an international obligation.

The Hamester case refers to a dispute submitted to ICSID on the basis of the Treaty between the Federal Republic of Germany and the Republic of Ghana for the encouragement and reciprocal protection of investments of February 24, 1995 ("BIT"), which entered into force on 23 November 1998, and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States[3] ("ICSID Convention"). The dispute relates to a cocoa beans processing and trade joint-venture between a German investor and a statutory company established under the laws of Ghana. The joint-venture partners created a new company registered in Ghana which took over the assets of an existing factory for the processing of cocoa beans, sheanuts and other related products. The agreement was that partner in Ghana would supply cocoa beans to the joint-venture company and the partner in Germany modernizes the factory and purchases

2 *Draft Articles on Responsibility of States for Internationally Wrongful Acts, 2001* [online]. International Law Commission [cit. 2015-03-22] ("Draft Articles").

3 Convention on the Settlement of Investment Disputes between States anad Nationals of Other States (Washington, 1966) [online]. *International Centre for Settlement of Investment Disputes*. Available from: https://icsid.worldbank.org/apps/ICSIDWEB/icsiddocs/Documents/ICSID%20Convention%20English.pdf.

the refined products. The dispute arose due to the contractual relationship between the joint-venture partners and concerns claims for breaches of the joint-venture agreement as well as breaches of the BIT. [4]

The German company Gustav F W Hamester GmbH & Co KG, claimed damages in connection with a dispute with its joint venture partner, the Ghana Cocoa Board ("Cocobod"). The German company complained that Cocobod refused to supply cocoa at a pre-agreed price to the joint venture. Furthermore, it also complained that the management of the joint venture newly established company - West African Mills Company, was affected by actions that can be attributed to the Ghanaian state. Ghana in one of its statements stated that the claimant had no investment in Ghana as a matter of Ghanaian law because, from the very beginning, the investment involved fraud and breaches of fiduciary duty. Ghana also argued that the conduct complained about by the claimant was that of the Cocobod and not Ghana itself, and the Cocobod's actions were not attributable to Ghana. Furthermore, the claims were, in truth, contractual in nature and were not "elevated" to treaty breaches by the umbrella clause in Art. 9(2) BIT.[5]

One of the challenges to the resolution of this particular dispute is the specific approach of the Tribunal, for example by avoiding the analysis of the merits on the relationship between the parties.

2 Attribution

One of the requirements for the international responsibility of a state is that the conduct in question is attributable to the state under international law.[6]

To some extent it is confusing and difficult to present the principles guiding attribution and non-attribution clearly, coherently and concisely at the same time. *Szigeti* in his work states that the articles related to attribution are somewhat redundant. The law of attribution could be stated much more clearly. On one hand, the particular articles derive their authority from the case law

4 Hamester case, para 1.

5 ICSID Tribunal Rejects Contractual Claims Brought under BIT [online]. In *Practical Law* [cit. 2015-03-22].

6 *Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries, 2001* [online]. International Law Commission [cit. 2015-03-22], Part one, Chapter I, Art. 2 (Draft Articles with Commentaries").

and the state practice cited in the commentaries, so presumably analyzing only the case law would give a more exact picture of attribution and state responsibility.[7]

Chapter II of the Draft Articles defines when the conduct in question, which may have the form of an act or omission, is to be related to as the conduct of the state. In international law, responsibility is limited to conduct which engages the state as an organization, and also so as to recognize the autonomy of persons acting on their own account and not at the instigation of a public authority.[8] "*The only conduct attributed to the State at the international level is that of its organs of government, or of others who have acted under the direction, instigation or control of those organs - as agents of the state.*"[9] Conduct of private persons is not as such considered attributable to the state. This was established in many cases, for example, in the Tellini case. This case involved an incident between Italy and Greece, relating to the assassination on Greek territory of the Italian general who was sent by the League of Nations with a team of Italians to survey the disputed border between Greece and Albania. The Special Commission of Jurists stated in this matter: "*The responsibility of a State is only involved by the commission in its territory of a political crime against the persons of foreigners if the State has neglected to take all reasonable measures for the prevention of the crime and the pursuit, arrest and bringing to justice of the criminal.*"[10]

The attribution of conduct to the state is based on requirements determined by international law and not on the mere recognition of a link of factual causality. A clear distinguishment of attribution from the characterization of conduct should be stated as internationally wrongful. Chapter II of the Dratf Articles includes several different rules of attribution. These rules have a cumulative effect. Meaning that a state may be responsible for the effects of the conduct of private parties, if it failed to take necessary measures to prevent those effects.[11] For example in the Tehran case,

7 SZIGETI D. Peter. *Territorial Bias in International Law: Attribution in State and Corporate Responsibility*. Journal of Transnational Law & Policy, 2010, p. 317.

8 *Draft Articles with Commentaries*, Part one, Chapter II, para. 1 - 2.

9 BROWNLIE Ian. *System of the Law of Nations: State Responsibility, Part I*. City: Oxford, 1983. p. 132 – 166.

10 *Draft Articles with Commentaries,* Part one, Chapter II, para. 3.

11 *Draft Articles with Commentaries*, Part one, Chapter II, para. 4.

the receiving state shall not be responsible for the acts of private individuals in seizing an embassy, but it would be responsible if it failed to take all necessary steps to protect the embassy from seizure, or to regain control over it. [12]

The Vienna Convention on the Law of Treaties[13] stipulates that the Head of State or Government or the Minister of Foreign Affairs is regarded as having authority to represent the state. It must be clearly distinguished that these rules have nothing to do with attribution for the purposes of state responsibility. Rules concerning attribution in chapter II are not defined for purposes for which it may be necessary to define the state or its government. The domestic law and practice of each state is important when determining what constitutes an organ of a state for the purposes of responsibility. Each state shall decide how its administration is to be structured and what functions the government should have. This aspect is not governed by international law, but there are cases when the conduct of certain institutions performing public functions are attributed to the state even if those institutions are regarded in domestic law as independent. There is also a possibility of a conduct engaged in by organs of the state in excess of their competence to be attributed to a state under international law, no matter of its position under domestic law.[14]

The Chapter II of the Draft Articles as mentioned before deals with the conditions under which conduct is attributed to the state as a subject of international law not as subject of domestic law for the purpose of determining its international responsibility. Within the domestic law a state usually is subdivided into component units of different type, like ministries, departments etc. Each may have separate legal personalities. This fact under international law is not relevant, because state still keeps its international responsibility even in the case of internal subdivision.[15] In the case of Yeager v. Iran,

12 Judgment of International Court of Justice of 24 May 1980, United States Diplomatic and Consular Staff in Tehran – Untied States of America v. Iran [online]. *International Court of Justice* [cit. 2015-03-22].

13 Vienna Convention on the law of treaties (Vienna, 1969) [online]. United Nations Treaty Collection. Available from: https://treaties.un.org/doc/Publication/UNTS/Volume%201155/volume-1155-I-18232-English.pdf.

14 *Draft Articles with Commentaries*, Part one, Chapter II, para. 5 – 6.

15 *Ibid.*, Part one, Chapter II, para. 7 – 8.

the tribunal observed: "*In order to attribute an act to the State, it is necessary to identify with reasonable certainty the actors and their association with the State.*"[16]

Conception of the state, what the state is and what we believe what it should be compose the basis of state responsibility. The codification and progressive development of the customary law of state responsibility including attribution has been on the agenda of the ILC for over forty years. "*The work of the ILC has run the risk of theoretically spinning out and valuing generally applicable principles rather than conducting the usual hunt for rules on the basis of state practice where coherency is not always entirely apparent.*"[17]

3 Issue of Attribution in Hamester case

3.1 The Status of Cocobod Regarding Attribution

Regarding the link between the status of Cocobod and attribution, the Tribunal observes whether Cocobod is a state organ *de jure* or *de facto* under Art. 4 Draft Articles[18] or an entity qualifying under Art. 5 Draft Articles,[19] or if the acts of Cocobod are attributable to Ghana because they were performed under the direction or control of the state, under Art. 8 Draft Articles.[20]

When dealing with the fact whether Cocobod is an organ of Ghana under the Art. 4, the Tribunal firstly observes the law of Ghana. As mentioned

16 ANDERSSON, Teresa. *State Responsibility during State Failure – A Question of Attribution and States Definition*. Master Thesis [online]. University of Lund, Faculty of Law [cit. 2015-03-22], p. 25.

17 CARON D. David. The Basis of Responsibility: Attribution and Other Transubstantive Rules of State responsibility, 2014 [online]. In *Social Science Research Network* [cit. 2015-03-22].

18 *1. The conduct of any State organ shall be considered an act of that State under international law, whether the organ exercises legislative, executive, judicial or any other functions, whatever position it holds in the organization of the State, and whatever its character as an organ of the central Government or of a territorial unit of the State. 2. An organ includes any person or entity which has that status in accordance with the internal law of the State.*

19 *The conduct of a person or entity which is not an organ of the State under article 4 but which is empowered by the law of that State to exercise elements of the governmental authority shall be considered an act of the State under international law, provided the person or entity is acting in that capacity in the particular instance*

20 *The conduct of a person or group of persons shall be considered an act of a State under international law if the person or group of persons is in fact acting on the instructions of, or under the direction or control of, that State in carrying out the conduct.*

before, Cocobod was created by the Ghana Cocoa Board Law. "*It appears that the Ghana Cocoa Board is not classified as a State organ under Ghanaian law, but was created as a corporate body, which can be sued in its corporate name. Cocobod is a commercial corporation whose principal purpose is to trade in cocoa beans and generate a profit for the Government, as provided for in the provisions of the domestic law: It shall be the duty of the Board to conduct its affairs on sound commercial lines and in such a manner as to ensure a reasonable return on its capital.*"[21]

Claimant's refers to the Cocobod as to the state organ *de facto*. The Claimant tries to support this statement by focusing on the case of Eureko v. Poland,[22] The Tribunal stated that the decision in Eureko v. Poland is not applicable to this case.[23]

"*The contract in the Eureko v. Poland case was signed by the State Treasury of the Republic of Poland represented by the Minister of the State Treasury, which is quite different from the situation of the Joint-Venture Agreement which was signed by the Claimant and Cocobod, and did not involve any Minister of Ghana. The Award in Eureko discussed the status of the State Treasury because under Polish Law the State Treasury had a separate personality. In fact, however, the tribunal did not expressly decide on the status of the State Treasury, but rather canvassed a range of possible analyses. It suggested that the State Treasury could be classified as a State organ. However, the tribunal also suggested that acts of the State Treasury could be attributed to the State under Article 5 or 8.*"[24]

According to the Tribunal, the decision in Eureko v. Poland case does not support the Claimant's allegation that the Cocobod is a state organ for two reasons. First, the situation of the State Treasury was very different from the situation of Cocobod. Secondly, even if it were the same, the tribunal in Eureko v. Poland case did not actually decide that the State Treasury was a state organ. [25]

21 Hamester case, para. 184.
22 Award of Ad Hoc Arbitration of 19 August 2005, Eureko B.V. v. Republic of Poland [online]. In *italaw* [cit. 2015-03-22] ("Euroco v. Poland case").
23 Hamester case, para. 186.
24 Hamester case, para. 186.
25 *Ibid.*

The tribunal in the Eureko v. Poland case concluded: "*In brief, whatever may be the status of the State Treasury in Polish law, in the perspective of international law, which this Tribunal is bound to apply, the Republic of Poland is responsible for the actions of the State Treasury.*"[26]

After analyzing all the arguments from both parties, the Tribunal concluded that Cocobod can "*by no means be considered an organ of Ghana, either de jure or de facto.*"[27]

The Tribunal noted, that it is obvious, that Cocobod is indeed entrusted with governmental functions. In order to regulate the marketing and export of cocoa, coffee or sheanuts and to encourage the development of all aspects of cocoa production and transformation, Cocobod was allocated with governmental powers.[28] However, referring to UPS v. Canada Post case,[29] the Tribunal agrees with the Respondent's statement: "*Like Canada Post and the Suez Canal Authority, the Ghana Cocoa Board is a public corporation, dominates a particular economic activity, and has some governmental powers (such as the power to make regulations). But that does not, and cannot, lead to the conclusion that all of its conduct, including purely commercial business decisions in relation to a joint venture for processing agricultural commodities, are governmental in nature.*"[30]

The Tribunal from its analysis concludes that Cocobod is an entity exercising elements of governmental authority, referred to in Art. 5 Draft Articles. The Tribunal emphasizes that the distinction between a state organ and a separate public entity is fundamentally important within this analysis.

"As organs participate in the structural setting of the State, all their acts are attributed to the State, whether commercial or not. In contrast, it is well established that for an act of a separate entity exercising elements of governmental authority to be attributed to the State, it must be shown that the precise act in question was an exercise of such governmental authority and not merely an act that could be performed by a commercial entity. This approach has been followed in national as well as international case law."[31]

26 Eureco v. Poland case, para. 134.
27 Hamester case, para. 188.
28 *Ibid.*, para. 191.
29 Award of Ad Hoc Arbitration of 11 June 2007, United Parcel Services of America Inc. (UPS) v. Government of Canada [online]. *Government of Canada. Foreign Affairs, Trade and Development Canada* [cit. 2015-03-22].
30 Hamester case, para. 191.
31 Hamester case, para. 193.

After the Tribunal's analysis of different variety of cases dealing with these issues, such as Rolimpex case,[32] Trendtex v. Central Bank of Nigeria case,[33] Maffezini v. Spain case,[34] the Tribunal stated that the conclusion which arises from these decisions is that "*only the acts of Cocobod utilizing State prerogatives are attributable to the State for the purpose of international responsibility, and that the Tribunal therefore only has jurisdiction over acts of Cocobod that would have been performed in the exercise of elements of governmental authority. This, in turn, requires an inquiry into the nature of each and every act of which the Claimant complains.*"[35]

The Tribunal has also observed whether all the acts complained of, in situation if they are not attributable to the state under Art. 5 Draft Articles, may be attributable under Art. 8. The attribution or non-attribution under Art. 8 was analyzed as being independent of the status of Cocobod, and dependent only on whether the acts were performed "on the instructions of, or under the direction or control" of the state. In that case, these acts would be attributable because they are under the direct command or effective control of the state, not the result of the use of governmental power. The Tribunal stated that it found no evidence of such a strong control by the state, as Art. 8 presumes. The Tribunal in this part of its analysis, concluded that the acts of Cocobod do not seem to be exercised under the direct command of Ghana. As a result of this, the acts do not appear to be attributable under Art. 8 to the Government.[36]

To summarize the result of Tribunal's findings on the part of observing status of Cocobod in relation to attribution, the Tribunal makes it clear that: "*Under Article 5 of the ILC Articles, if the acts of Cocobod which are the subject of complaint were performed in the exercise of governmental power, they will be attributed to the State. If they were performed in the fulfillment of commercial relations, they will not be attributable on that basis to the State. In so far as acts are not attributable under*

32 Award of Ad hoc Arbitration of 18 May 1978, C. Czarnikow Ltd v. Centrala handle zagraniczneho Rolimpex [online]. In *uniset.ca* [cit. 2015-03-22].

33 Award of Ad Hoc Arbitration of 1 January 1977, Trendtex Trading Corporation v. Central Bank of Nigeria [online]. In *uniset.ca* [cit. 2015-03-22].

34 Award of ICSID Tribunal of 13 November 2000, No. ARB/97/7, Maffezini v. Spain [online]. In *italaw* [cit. 2015-03-22].

35 Hamester case, para. 196 – 197.

36 Hamester case, para. 198 – 200.

Article 5, they could also be attributed to the State under Article 8 of the ILC Articles, if they can be shown as having been performed on the instructions of, or under the direction or control of the State."[37]

3.2 The International Legality of the Acts Attributable to the State

Relating to the the police investigation and the alleged harassment of the managing director of Wamco[38] (Mr. Holzäpfel), the Respondent submits: "*Messrs Holzäpfel and Opferkuch have given incoherent and patently dishonest explanations as to why they caused false receipts for consultancy services and public relations to be issued to Wamco. The criminal proceeding was entirely justified.*"[39]

The Tribunal observed that relating to certain evidence, the criminal proceedings are based on relevant foundation. Furthermore, the Tribunal finds that the allegations concerning physical threats to his life and his family from the chief executive of Cocobod and the employees of Wamco were completely baseless.[40] The Tribunal concludes regarding these aspects that: "*Although police investigations are undoubtedly attributable to the Government, the investigation of Mr. Holzäpfel's conduct cannot, in the circumstances of this case, be analyzed as contributing to an alleged expropriation of Hamester, in violation of the BIT.*"[41]

The Claimant in his memorial stated also that: "*The minutes of a meeting between the General Manager Operations at Wamco and the Finance Minister on 14 April 2003 makes clear that the Respondent was now directly instructing the Operations Minister of Wamco, without proper approval from the Board of Directors.*"[42]

The Respondent to these allegations counter-responded: "*As Mr. Clement explains in his witness statement, the meeting minutes cited by Hamester relate to a meeting with the Minister requested, and attended, by various Ghanaian cocoa processing companies (including Barry Callebaut and CPC Tema) for the purpose of requesting discounts. The minutes then record what was said at an internal Wamco meeting as to how*

37 *Hamester case,* para. 201.
38 West African Mills Company Limited.
39 Hamester case, para. 90.
40 *Ibid.*, para. 299.
41 *Ibid.*, para. 300.
42 Hamester case, para. 145.

Wamco could improve its financial performance. In no way did the Minister of Finance personally take control of Wamco. Nor did he give instructions to Mr. Clement at any time."[43]

The Tribunal observed that the meeting with the Minister was a general meeting with three cocoa processing companies, with the aim of reviewing the pricing policies of cocoa beans sales and that the companies were asking for a premium on beans to be waived for local producers. To this the government said, it may give a necessary consideration to this kind of proposal.[44]

The Tribunal concludes that: "*The Minutes of the meeting of April 14, 2003 do not reveal any act that could have resulted in the expropriation of Hamester's management rights or control of Wamco, in violation of the BIT.*"[45]

As stated before not all acts within this dispute were found by the Tribunal non-attributable to Ghana. The Tribunal's mission was to analyze if these kind of acts would represent any legality in regards to the international context and thus constitute a violation of the BIT. Focus was on three separate situations with the first one being the police investigation and the alleged harassment of a representative of Cocobod. Since these circumstances are undoubtedly State actions of sovereign powers I think the Tribunal correctly stated that they do not contribute to an alleged expropriation of Hamester, in violation of the BIT. Regarding the meeting of General Manager Operations at Wamco with the Ministry of finance of April 14, 2003, I think it was bit difficult to resolve this issue since the arguments from both sides were in contradiction as to the factual base. However, the Tribunal concluded that within the meeting nothing came up that would result in the expropriation of Hamester's management rights or control of Wamco, in violation of the BIT.

4 Critical Remarks

At the beginning of the dispute between a German based company and the Republic of Ghana, the Claimant wanted to commence arbitration under the provisions of ICSID Convention relying on the dispute-settlement

43 *Hamester case,* para. 174.
44 *Ibid.,* para. 303.
45 *Ibid.,* para 305.

clause in the Joint-Venture Agreement concluded between the parties. Since this was refused by the ICSID Secretariat, the Claimant based its claims under the BIT claiming treaty breaches and breaches of the Joint-Venture Agreement through the application of umbrella clause.[46]

As to the Claimant's position, from a structural point of view, the Cocobod is – due to its complete dependence – *a de facto* State entity, discharging essentially governmental functions delegated to it by the state. In other words, the acts of the Cocobod are attributable to the government as sovereign acts. This also means, that the Cocobod can be treated – for the purpose of the BIT – as the Government of the Republic of Ghana. The tribunal concluded that significant amount of the actions complained about by the claimant were not attributable to Ghana and none caused a breach of the BIT. This was because activities of Cocobod were by the opinion of the tribunal fundamentally commercial in nature and thus the claimant's claims were contractual claims.

However, even if the acts complained of by the Claimant were attributable to Ghana, the Tribunal observed that no liability would have arisen due to the contractual character of these acts. It is a fact that, the Tribunal avoided analyzing the merits of the relationship between the parties, rather concentrating more on the jurisdictional issues.

5 Conclusion

The aim of this article was to give a brief summary of the work of ILA on general rules of attribution relating to state responsibility and then to address the issue of attribution regarding state responsibility in the investment dispute case – Hamester case.

I agree with some authors who claim that the area of attribution is to some extent a very important technical topic. There has been a substantial evolution in the attribution area. There has been some shifting of substantive norms occasioned under the rubric of either the attribution or nonattribution of acts to a state and a variety of state entities.[47]

46 Hamester case, para. 90.

47 LILLICH B. Richard; CHRISTENSON J. Ch.; CARON D.; DUPUY P. M. Proceedings of the Annual Meeting. *American Society of International Law*. 1990, Vol. 84, No. 1, p. 51.

To constitute a violation of the BIT, an act has to be attributable to the state and a violation of an international obligation stipulated in the BIT must occur. This means that the questions of attribution and illegality need to be distinguished. Only after such analysis has answered this question in the affirmative, the Tribunal addressed the second question, which is the qualification of the act attributed to the state as an illegal act. The question of "attribution" does not itself dictate whether there has been a violation of international law. Art. 2[48] is not an autonomous basis for attribution, but gives a general definition of what constitutes an internationally wrongful act of a state. It does not create a general obligation on the part of states to prevent any act interfering with an investor's right.

Relating to the application of the umbrella clause by the Claimant, the Tribunal stipulated that the umbrella clause in Article 9(2) BIT[49] was not supposed to relate to the transformation of contractual claims into treaty claims. This provision when properly interpreted, should apply to only obligations assumed not by separate entities, but the state itself. I agree that one of the most controversial issues in international investment law is the relationship between BIT claims and contractual claims. Hamester case is a very good example of the situation where the Claimant by swift application and interpretation of the umbrella clause, transforms purely contractual and commercial claims into investment treaty claims. The Tribunal made it very clear that these types of claims should not be the subject of the investment protection provided by investment treaty arbitration.

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INTERNATIONAL INVESTMENT ARBITRATION: INVESTOR-TO-STATE DISPUTE SETTLEMENT IN EU AGREEMENTS

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Abstract

The Treaty of Lisbon conferred new exclusive competence in the field of foreign direct investments on the European Union. It seems that 50-year-old fragmented system of investment law, based on bilateral investment treaties, took a new direction towards a comprehensive European international investment policy. Popularity and efficiency of international investment agreements derive mainly from the concept of investor-state dispute resolution (investment arbitration). New competences of the EU significantly impact on the resolution of disputes. This paper is focused on the role of both Commission and member states in arbitral proceedings. It analyses a new framework for managing financial responsibility when the investment agreement to which the European Union is party is breached. The Paper reveals that arbitration under European IIAs raise questions of responsibility and attribution. In order to prevent this uncertainty the character of European IIAs has to be clarified. Moreover, a division of responsibility included in the Regulation should be implemented into the IAAs.

Keywords

Treaty of Lisbon; International Investment Arbitration; Dispute Resolution; International Investment Agreements; European Union.

1 Introduction

Bilateral investment treaties ("BIT") are treaties concluded between two states intended to strengthen the economic cooperation between them and to create

favourable and predictable environment for investments.[1] In other words the main objective of the investment law is the promotion and protection of investments leading to economic development of the contracting parties.

It has constantly been proved that foreign investments have significantly positive effect on the economic development of states.[2]

The first German-Pakistani BIT was enacted more than 50 years ago and since that many countries have followed this policy.[3]

All attempts to draft a multilateral agreement such as Havana Charter introduced by the International Trade Organization in 1948 or the Multilateral Agreement on Investment drafted by Organisation for Economic Cooperation and Development ("OECD") failed. The last effort to revive the concept of a global investment agreement providing investors with both material and procedural protection within the World Trade Organization ("WTO") has also not led to success.[4] Thus, the system of international investment law is based on fragmented and chaotic bundle of bilateral or regional investment treaties. The last United Nations Commission for Trade and Development ("UNCTAD") Report states there were 3 196 international investment agreements (including both bilateral and multilateral treaties) in 2013.[5]

The Treaty of Lisbon[6] conferred a new exclusive competence in the field of the foreign direct investments on the European Union ("EU"). Such step

1 ANDERER, Carrie E. Bilateral Investment Treaties and the EU Legal Order: Implications of the Lisbon Treaty. *Brooklyn Journal of International Law*, 2010, Vol. 35, No. 3, p. 852.

2 BENEDICT, Christoph G. The Multilateralization of Investment Protection under the Lisbon Treaty: Fears and Hopes of Investors. *ICSID Review Foreign Investment Law Journal*. 2009, Vol. 24, No. 2, p. 451.

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5 World Investment Report 2013: Global Value Chains Investment and Trade for Development [online]. *United Nations Conference on Trade and Development* [cit. 2015-02-28].

6 The Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community, signed at Lisbon, 13 December 2007. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1443444799599 & uri=CELEX:12007L/TXT („Treaty of Lisbon").

can lead to unprecedented consequences for the whole system of the international investment law. However, this new comprehensive European international investment policy raises both expectations and concerns.

2 International Arbitration

International investment law has achieved such popularity mainly because of its unique dispute settlement mechanism. Instead of relying on their home states to espouse their claims through diplomatic protection, the investors are provided with a direct dispute settlement mechanism – investor-state arbitration. Investors can initiate direct arbitral proceedings against the host state for a violation of the international investment agreement ("IIA").[7]

New competences of the EU significantly impact on the resolution of disputes under the EU investment agreements. This paper is focused on the role of both the Commission and the Member States in arbitral proceedings and on a new framework for managing the financial responsibility when the investment agreement is breached.

3 The Treaty of Lisbon

The Treaty of Lisbon has extended the Common Commercial policy Arts. 206 and 207 Treaty on the Functioning of the European Union ("TFEU")[8] to embrace "foreign direct investment". It must be emphasized provision not only empowers the EU. The TFEU goes further, since the Common Commercial Policy is considered to fall within exclusive powers of the EU. The Member States may act in this field only with permission of the EU.[9] All this leads to an inevitable consequence – because of this exclusiveness states are no longer empowered to enact BITs.[10]

7 SORNARAJAH, M. *The International Law on Foreign Investment*. 3rd ed. New York: Cambridge University Press, 2010. p. 36.

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4 Financial Responsibility and the Respondent Status

The Member States of the EU have confined power to negotiate and to conclude IIAs to the EU. It means that only the EU becomes the contracting party of such agreement. Thus, it may seem logical that as being a contracting party, the EU should bear responsibility for the violation of the investment agreement.

However, in this particular case, the perception of responsibility usually applied in the investment law seems to be unfair and simplified and does not sufficiently differentiate between EU as an international organization *sui generis* and the Member States as members of this international organization. It does not take into account that not only acts of the EU can lead to the violation of the IIA, but also acts of the member states. It is highly unlikely that especially more developed member states would accept the concept of responsibility that any violation of IIA is attributable to the EU and thus will be paid from the common European budget.

For a long time it has been unclear who will bear responsibility for a violation of European IIAs. Since the Treaty of Lisbon has come into force, the functioning of the dispute settlement mechanism has raised a lot of questions and the negotiations within the EU concerning those issues took almost 4 years.

With respect to the responsibility international law does not provide us with any rules how to divide responsibility between an international organization and its members. Under Art. 29 Vienna Convention on the Law of Treaties ("VCLT")[11] state is bound by a treaty for the whole of its territory unless provided otherwise. Even though this provision is considered as a rule of customary law,[12] it is not applicable for the responsibility of an international organization *sui generis*.

The conduct of territorial sub-units of a state is attributable to the state itself as stated in Article 4(1) Draft Articles on Responsibility of States

11 Vienna Convention on the law of treaties (Vienna, 1969) [online]. United Nations Treaty Collection. Available from: https://treaties.un.org/doc/Publication/UNTS/Volume%201155/volume-1155-I-18232-English.pdf ("VCLT").

12 DÖRR, Oliver; SCHMALENBACH, Kirsten. Vienna Convention on the Law of Treaties: A Commentary. Berlin: Springer, 2012. p. 140.

for Internationally Wrongful Acts ("Draft Articles").[13] Nevertheless, there is no such rule applicable for the international organizations.

There is no rule similar to the Article 29 VCLT applicable for the responsibility of an international organization in the international law it might be used as an analogy. Even Draft Articles does not seem to fit to abovementioned division of responsibility. International organizations are only liable for the conduct of their own organs.[14] According to Art.16 Draft Articles on the Responsibility of International Organizations,[15] the organs of an international organization may be held liable if they adopt a decision binding on the member states to commit an act that would be internationally wrongful if committed by the organization. However, *Bishchoff* argues that the EU law is generally not implemented by the organs of the EU, but by the organs of its Member States and this situation is not covered by the Draft Articles.[16]

By the same token, international organizations are responsible only for the conduct of their own organs or for the conduct of the member state acting exclusively in compliance with a binding decision adopted by the international organization. According to the positive international law, these two acts would be attributable to the international organization and would lead to its liability.

The EU has to be treated differently and all its uniqueness has to be taken into account. Due to the division of powers between the EU and its Member States there are two possible scenarios:

1. Conduct of the EU can be considered as a violation of the IIA.
2. Conduct of the Member State can be considered as a violation of the IIA.

Because these two eventualities exist, it was absolutely necessary to adopt a mechanism "managing financial responsibility" arising from arbitration

13 *Draft Articles on Responsibility of States for Internationally Wrongful Acts, 2001* [online]. International Law Commission [cit. 2015-09-28] ("Draft Articles").

14 BISCHOFF, Jan Asmus. Just a Little Bit of „Mixity"? The EU's Role in the Field of International Investment Protection Law. *Common Market Review*, 2011, 48, p. 1566.

15 *Draft Articles on Responsibility of International Organisations, 2011* [online]. International Law Commission [cit. 2015-09-28].

16 BISCHOFF, Jan Asmus. Just a Little Bit of „Mixity"? The EU's Role in the Field of International Investment Protection Law. *Common Market Review*. 2011, Vol. 48, p. 1566.

under the IIA between the EU and a non-member state. Stable and investment friendly environment can only be created with predictable and operational mechanism of financial responsibility.[17]

The Commission adopted the Proposal for the Regulation concerning financial responsibility on June 21, 2012 ("Proposal").[18] The European Parliament and the Council adopted Regulation (EU) No 912/2014 of 23 July 2014 establishing a framework for managing financial responsibility linked to investor-to-state dispute settlement tribunals established by international agreements to which the European Union is party ("Regulation").[19]

5 Regulation

The central principle of the Regulation is that financial responsibility flowing from investor-state dispute settlement should be attributed to the actor which has afforded the treatment in dispute. This concept has not been disputed during the whole legislative procedure. "*The regulation stipulates that where the treatment concerned is afforded by the Union institutions then the financial responsibility should rest with the Union institutions. Where the treatment concerned is afforded by a member state of the European Union, the financial responsibility should rest with that member state. Where the actions of the member state are required by the law of the Union, than financial responsibility should lie with the Union.*"[20]

The framework for managing financial responsibility is closely related to the role of the EU and of the Member States in the arbitral proceeding. The basic rule states that the subject which is financially responsible should act as respondent. This principle is accompanied by a number of exceptions providing the Commission with a broad discretion and primacy in deciding

17 SORNARAJAH, M. *The International Law on Foreign Investment.* 3rd ed. New York: Cambridge University Press, 2010, p. 34.

18 Proposal for a Regulation of the European Parliament and of the Council establishing a framework for managing financial responsibility linked to investor-state dispute settlement tribunals established by international agreements to which the European Union is party, COM (2012) 335 final. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52012PC0335 & rid=1 ("Proposal").

19 Regulation (EU) No 912/2014 of the European Parliament and of the Council of 23 July 2014 establishing a framework for managing financial responsibility linked to investor-to-state dispute settlement tribunals established by international agreements to which the European Union is party. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32014R0912 & from=EN ("Regulation").

20 Proposal.

whether it nevertheless wishes to act as respondent.[21] The Regulation envisages the following scenarios:

1. The Commission acts as a respondent automatically if it receives within 45 days in writing a confirmation of the member state that it does not intend to act as a respondent. However, this decision not to act as a respondent made by a Member State does not affect apportionment of financial responsibility.
2. The Commission may decide by means of implementing acts, based on a full and balanced factual analysis and legal reasoning provided to the member states, that the EU is to act as respondent where similar treatment is being challenged in a related claim against the EU in the WTO, where a panel has been established and the claim concerns the same specific legal issue, and where it is necessary to ensure a consistent argumentation in the WTO case.[22]
3. The Commission may decide by means of implementing acts, based on a full and balanced factual analysis and legal reasoning provided to the member states, that the EU is to act as the respondent where one or more of the following circumstances arise: i) the EU would bear all or at least part of the potential financial responsibility arising from the dispute, or ii) the dispute also concerns treatment afforded by the institutions, bodies, offices or agencies of the EU. [23]

6 Critical Remark

The adoption of the Regulation has to be considered as an important achievement of the Commission, which paves the path to the first IIA concluded between the EU and a non-member state - the Comprehensive Trade and Economic Agreement ("CETA") with Canada.[24] The consolidated version of CETA follows the trend set by BITs and includes investor-to-state dispute settlement mechanism.

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21 BETENS Freya; KREIJEN Gerard; VARGA Andrea, August. Determining International Responsibility Under the New Extra-EU Investment Agreements: What Foreign Investors in the EU Should Know. *Vanderbilt Journal of Transnational Law*. 2014, Vol. 47, No. 5, p. 1226.

22 Art. 9 Regulation.

23 Art. 9 Regulation.

24 Consolidated Comprehensive Trade and Economic Agreement Text, published on 26 September 2014. Available from: http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf ("CETA").

The consolidated text of CETA has been completed after long years of negotiations. At the first glance the EU can self-confidently enter an era of its investment policy. However, from the international law perspective there are still serious difficulties mainly with respect to the responsibility for a violation of an international agreement together with the nature of the EU.

Firstly, there has been a passionate academic discussion over the character of European IIAs. The wording of Article 207 TFEU referring explicitly to "foreign direct investments" falls under exclusive EU competence. However, the scope of the classic BIT (the EU has an ambition to replace all BITs of Member States by European IIAs)[25] is not limited only to the foreign direct investments but covers also so called portfolio investments. There is a consensus that portfolio investments fall under shared competence. Thus, in order to bypass this obstacle it is necessary to treat IIAs as mixed agreements.[26]

The question of the character of the investment agreements is not only the oretical. The Commission constantly argues that the EU has an exclusive competence with respect to the Common Commercial policy and may be the only party of international agreements covering provisions on foreign direct investments.[27] On contrary the Member States are of the opinion that the European IIAs should be considered as mixed agreements.[28]

Mixed agreements require ratification by all Member States that become together with the EU Contracting Parties to the agreement. Contours of responsibility are usually very unclear and raise a lot of questions.[29] Until

25 KLEINHEISTERKAMP, Jan. Financial Responsibility in the European International Investment Policy. *International and Comparative Law Quarterly*. 2014, Vol. 63, p. 451

26 MESTRAL, Armad. Is a Model EU BIT Possible-or Even Desirable? [online]. *Columbia FDI Perspective* [cit. 2015-02-28].

27 Preamble of the Regulation.

28 CETA - Comprehensive Economic and Trade Agreement [online]. *Federal Ministry of Economic Affairs and Energy* [cit. 2015-02-28]; Convenience translation of the summary of the legal expertise by Prof. Dr. Franz C. Mayer, LL.M. (Yale), University of Bielefeld, for the Federal Ministry of Economics and Energy regarding the question: "Is the planned free trade agreement of the EU with Canada (Comprehensive Economic and Trade Agreement, CETA) a mixed agreement?" [online]. *Federal Ministry of Economic Affairs and Energy*. [cit. 2015-02-28].

29 STEINBERGER, Eva. The WTO Treaty as a Mixed Agreement: Problems with the EC's and the EC Member States Membership of the WTO. *The European Journal of International Law*. Vol. 17, No. 4. p. 839.

these days it is not clear whether the European IIAs are going to be considered as mixed agreements. Supposing that they are, the Regulation loses its relevance, because both the EU and its Member States are to be responsible for the violation of the IIA. The Regulation is only an internal document and has no binding effect on the other Contracting Party of the IIA (a third Party). The decision whether to initiate arbitral proceedings against the EU or against the Member State would depend purely on investor's deliberation. For these reasons a mixed agreements usually include a competence clause which helps divide responsibility between organization and its member states.

As regards the CETA it does not include a classic competence clause. CETA in its Article X.20 only deals with determination of the respondent for disputes with the EU or its Member States. Although such provision clearly derives from the mechanism introduced by the Regulation its coverage is limited. Article X.20 refers only to respondent status, however financial responsibility is left completely (!) untouched. Respondent status is absolutely irrelevant for the responsibility flowing from a violation of treaty. Moreover, the Regulation itself expects situations, when respondent does not necessarily bear the responsibility (situation when the EU acts as a respondent and responsibility is borne by a member state).

Thus, the only applicable provision seems to be the Article X.06 of the following wording: *"Each Party is fully responsible for the observance of all provisions of this Agreement."* In consequence of the lack of any provision managing financial responsibility, assuming a mixed character of this agreement, both EU and Member States are fully responsible for a violation of CETA.

Moreover, responsibility raises question of attribution. According to the leaked mandates approved by the Council at its 3109th meeting on 12 September 2011 "*the respective provisions of the future European IIA shall be built upon the Member State's experience and best practice regarding their bilateral investment agreements*".[30] In addition the EU declares its ambition to replace existing BITs by European IIAs. The question is whether conduct of purely national character of Member States can be attributable to the international

30 See the leaked mandates approved by the Council at its 3109th meeting, 12 September 2011 [online]. 2015 [cit. 2015-02-28].

organization. I am of the opinion that IIA concluded between the EU and non-member state can never replace existing BITs clearly because of non-existing attribution of a wrongful act caused by a member state to the EU. IIA providing protection only against the acts the EU and replacing existing BITs would significantly lower protection of investors. For this reasons a mix character of the agreement is absolutely necessary.

The wording of Article X.06 leads to the conclusion (assuming a mixed character of the agreement) that the EU would be plausibly responsible for the acts attributable to the EU and the Member States would be plausibly responsible for the acts attributable to them. Drafts Articles and Draft Articles on the Responsibility of International Organizations set the rules of attribution. Taking into account both Article X.06 and Article X.20 it seems that the investment arbitration under European IIA can have a very exceptional character. To be precise, arbitration between claimant and respondent can plausibly lead to the award in favour of a claimant ordering not the respondent, but another Contracting Party of the IIA, to pay a compensation.

7 Conclusion

As described investment arbitration under European IIA raises questions of responsibility and attribution. In order to prevent this uncertainty the character of European IIA has to be clarified. Moreover a division of responsibility included in the Regulation should be implemented into the IAA.

Investment agreements are intended to strengthen the economic cooperation between states and to create favourable and predictable environment for investments. Drafters of future European agreements should bear on mind that the purpose of investment law is to provide maximum legal certainty for both investors and host states. Unfortunately it seems that the first European IIA still brings more uncertainty than confidence.

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OTHER FORMS OF DISPUTE RESOLUTION

RESOLUTION OF CROSS-BORDER DISPUTES BETWEEN CONSUMERS AND FINANCIAL SERVICES PROVIDERS

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Abstract

Legal issues of financial services are distinctly unclear for most consumers. Measures that are adopted by the European Union in the area of financial services are not always sufficient to prevent consumers from disputes. Apart from regulating minimum standards of the offered services or providing consumers with protection against unfair terms in financial contracts, there is another challenge. What consumers also need is to ensure effective cross-border alternative dispute resolution. While contracts with providers from another Member State are getting more and more popular because of freedoms of internal market, consumers may still have problems with pursuing their claims in case of dispute. It is possible to overcome this problem due to cross-border initiatives inter alia FIN-NET. The FIN-NET is a network of out-of-court complaint entities in the European Economic Area countries. It enables consumers to find ADR institution in a specific country. Consumer may also ask his/her domestic institution for information in native language about complaint procedures provided by a foreign institution which is associated with the FIN-NET. The question that should be raised is if the financial dispute resolution network provides consumers effective protection. The analysis leads to the conclusion that the network may be valuable for consumers because the information given consists of the most important issues concerning ADR body in the foreign Member State. However, the number of cross-border consumer disputes is growing and the coverage and visibility of the network may be seen as a major current challenge for the FIN-NET.

Keywords

Cross-border Consumer Disputes; Financial Services; Fin-Net.

1 Introduction

The financial services are widely regarded as complicated and risk-generating for the consumers. The asymmetry of information between the consumer and the financial services provider may lead to potential disputes, which can be solved in the court proceedings or by the means of an alternative dispute resolution.

Both issues described in this paper, i.e. the consumer alternative dispute resolution ("ADR") and financial services, are the concern of the European Union ("EU") authorities.[1] The area of the financial services was the subject of Financial Services Action Plan ("FSAP"), Financial Services Policy and legislative measures taken by the EU. The ADR is a subject of the EU legislation as well e.g. European Commission recommendations,[2] green papers

1 See more: MOLONEY, Niamh. Reform or Revolution? The Financial Crisis, EU Financial Markets Law, and the European Securities and Markets Authority. *International and Comparative Law Quaterly* [online]. 2011, Vol. 60, No. 4 [cit. 2015-03-13], p. 521 - 533; MARAK, Katarzyna; POROŚ, Katarzyna. Ochrona konsumenta usług finansowych w świetle prawa wspólnotowego - wybrane zagadnienia. In GNELA, Bogusława (ed.). *Ochrona konsumenta usług finansowych*. Warszawa: Wolters Kluwer, 2007, p. 135 – 146; CORCORAN, Andrea M.; HART Terry L. The Regulation of Cross-border Financial Services in the EU Internal Market. *Columbia Journal of European Law* [online]. 2002, Vol. 8 [cit. 2015-03-14], p. 221 – 292; BENÖHR, Iris. Consumer Dispute Resolution after The Lisbon Treaty: Collective Actions and Alternative Procedures. *Journal of Consumer Policy* [online]. 2013, Vol. 36, No. 3 [cit. 2015-03-15], p. 87 – 110; CREUTZFELDT Naomi. How important is Procedural Justice for Consumer Dispute Resolution? A Case Study of an Ombudsman Model for European Consumers. *Journal of Consumer Policy* [online]. 2014, Vol. 37, No. 4 [cit. 2015-03-15], p. 527 – 546; HODGES, Christopher. Current Discussions on Consumer Redress: Collective Redress and ADR. *ERA Forum* [online]. 2012, Vol. 13, No. 6 [cit. 2015-03-15], p. 20 – 32; HODGES, Christopher. Collective Redress at European Level: Existing Mechanisms. In *The Reform of Class and Representative Actions in European Legal Systems: A New Framework for Collective Redress in Europe* [online]. London: Hart Publishing, 2008 [cit. 2015-03-09], p. 93 – 116; PILECKA, Aleksandra. Plan działań w zakresie usług finansowych (FSAP) - założenia, realizacja i wpływ na rynki finansowe w Unii Europejskiej. *Bank i Kredyt. Integracja rynków finansowych w Unii Europejskiej od A do Z* [online]. 2007, Vol. 38, No. 2 [cit. 2015-03-13], p. 3 – 26; BENÖHR, Iris. Alternative Dispute Resolution in the EU. In HODGES, Christopher J.S.; BENÖHR, Iris; CREUTZFELDT-BANDA, Naomi (ed.). *Consumer ADR in Europe* [online]. London: Hart Publishing, 2012 [cit. 2015-03-09], p. 2 - 23.

2 *Inter alia* Commission Recommendation of 30 March 1998 on the principles applicable to the bodies responsible for out-of-court settlement of consumer disputes. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:31998H0257; Commission Recommendation of 4 April 2001 on the principles for out-of-court bodies involved in the consensual resolution of consumer disputes. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32001H0310.

and directives[3] *inter alia* recently issued ADR directive[4] and also ODR regulation.[5]

Art. 169(1) Treaty of Functioning of European Union ("TFEU") states: "*In order to promote the interests of consumers and to ensure a high level of consumer protection, the Union shall contribute to protecting the health, safety and economic interests of consumers, as well as to promoting their right to information, education and to organise themselves in order to safeguard their interests."* Because of ambiguity of financial services this area is of the particular interest of the EU authorities. It is important to protect consumers either in a preventive manner or in case of dispute, both in domestic and cross-border disputes.

Cross-border consumer disputes concerning financial services may be seen as the most challenging among the other international disputes, because the consumers' awareness of the law and financial services is not sufficient and the consumers deserve specific protection. ADR could be an efficient method of resolution of cross-border disputes between consumers and financial services providers, but the major current challenge is to familiarize consumers with ADR in financial disputes.

One of the initiatives, which is intended to provide information about ADR in financial services is Cross-Border Out-of-Court Complaints Network for Financial Services in the European Economic Area called the FIN-NET. The main aim of the paper is to explain how the FIN-NET works and if it may be assessed as effective network for consumers facing cross-border financial services dispute or if some challenges for this network still exist.

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3 Directive 2008/52/EC of the European Parliament and of the Council of 21 May 2008 on certain aspects of mediation in civil and commercial matters. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32008L0052.

4 Directive 2013/11/EU of the European Parliament and of the Council of 21 May 2013 on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1426354350881 & uri=CELEX:32013L0011 ("ADR directive").

5 Regulation (EU) No 524/2013 of the European Parliament and of the Council of 21 May 2013 on online dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1426354278716 & uri=CELEX:32013R0524 ("ODR Regulation")..

2 Financial Services and the Role of ADR

Financial service is defined as "*any service of a banking, credit, insurance, personal pension, investment or payment nature*".[6] These services are distinctive against the other services because of the complicated matter and economic risk connected with it.

2.1 Ambiguity of Financial Services

As it was mentioned before, the financial services belong to the services most unclear for the consumers. The agreements and general conditions are written in specific legal language and with the use of financial terms. Moreover, the agreements consist of detailed and complicated regulations because of the EU legislation which impose wide-ranging disclosure requirements on the financial services providers. However, the consumers may have difficulties with analysing all information given by service provider by themselves and finding the most important issues in the agreement. Financial services agreements may cause consumer's apprehension because of the higher level of the economic risk and shortage of transparency.[7] This may lead the consumers to unreasonable decisions which they would not have made, if they had had extensive knowledge adequate to assess the consequences of the contract. These obstacles gain much more importance insofar as cross-border services are concerned. Language, cultural preferences and consideration of geographical proximity are also mentioned as natural barriers for integration of the market in financial services.[8]

2.2 The Role of ADR in Financial Services

In such a situation it is vital to provide the consumers, especially those dealing with cross-border financial services, with proper procedures of solving

6 Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32002L0065 ("Directive 2002/65/EC").

7 ŁĘTOWSKA, Ewa. *Prawo umów konsumenckich*. Warszawa: C.H. Beck, 2002. p. 453 - 458.

8 ČULINOVIĆ HERC, Edita; ŽUNIĆ KOVAČEVIĆ Nataša. *Extrajudicial Settlement of Consumers Disputes in Domain of Financial Services- EU and Croatia* [online]. March 2013. [cit. 2015-03-09], p. 4; MARAK, Katarzyna; POROŚ, Katarzyna. Ochrona konsumenta usług finansowych w świetle prawa wspólnotowego - wybrane zagadnienia. In GNELA, Bogusława (ed.). *Ochrona konsumenta usług finansowych*. Warszawa: Wolters Kluwer, 2007, p. 144.

potential dispute. Lack of procedures may be considered as a serious barrier of development of cross-border financial services. Despite the benefits of freedom of services, consumers would not use financial services from another Member State if they are not sure whether some procedures in case of dispute are provided. The European Commission underlined that quick and simple out-of-court dispute resolutions are essential to the creation of an integrated internal market in financial services.[9] In case of a court dispute, the consumers may meet with difficulties such as costs, need of finding legal assist and probably extended time period required to get the ruling. Some scholars underline that availability and quality of court mechanisms may also be not adjusted to consumer's needs, possibilities and knowledge, especially in cross-border disputes.[10] In the court proceedings there might be disproportion between costs and value of the object of litigation.[11] All these aspects have negative effects on the consumer and affect their decision on whether or not to use the cross-border financial services. ADR can contribute to elimination of these barriers. This is also noticed directly in the text of some directives regulating financial services which encourage or require Member States to ensure the development of adequate and effective out-of-court complaints and redress procedures for the settlement of consumer disputes.[12]

The reports revealed that although the need to raise consumer confidence in cross-border financial services is rather caused by language barriers, incomplete information and consumer's preference of ability to meet the provider, the network of ADR bodies is an appropriate mechanism for the consumers need for assist in the resolution of cross-border disputes.[13]

9 See *Financial Services: Commission Launches Out-of-court Complaints Network to Improve Consumer Confidence* [online]. European Commission Press Release, IP/01/152, Brussels, 1 February 2001 [cit. 2015-03-09].

10 WOJTCZAK, Dorota. *Usługi bankowe w regulacjach Unii Europejskiej*. Warszawa: Wolters Kluwer, 2012. p. 130.

11 BANASZEWSKA, Anna. Nowe unijne regulacje w zakresie ADR w sporach konsumenckich. *ADR - Arbitraż i mediacja*. 2014, No. 4, p. 88.

12 For example Art. 14 Directive 2002/65/EC. See more BENÖHR, Iris. Alternative Dispute Resolution in the EU. In HODGES, Christopher J.S.; BENÖHR, Iris; CREUTZFELDT-BANDA, Naomi (ed.). *Consumer ADR in Europe* [online]. London: Hart Publishing, 2012 [cit. 2015-03-09], p. 10 - 11.

13 *Evaluation of FIN-NET. Final Report* [online]. Centre for Strategy & Evaluation Services, June 2009 [cit. 2015-03-09], p. ii. See also FRIZON, Francis; THOMAS, David. *Resolving Disputes Between Consumers and Financial Businesses: Fundamentals for a Financial Ombudsman. A Practical Guide Based on Experience in Western Europe. The World Bank Global Program on Consumer Protection and Financial Literacy* [online]. January 2012 [cit. 2015-03-10], p. 10.

3 The FIN-NET

As it was previously explained, financial services are widely regarded as one of the most problematic for the consumers, especially those which are cross-border. In order to mitigate the risk of long and expensive trials, initiative of creating a cross-border dispute resolution network has been taken.

The result of this initiative is called FIN-NET, which means the network intended to simplify the resolution of cross-border disputes in specific area such as financial services.[14] The network consists of national out-of-court schemes. Financial disputes are implied as disputes between consumers and financial service providers such as banks, insurance companies or investment firms. The territorial area covered by FIN-NET includes countries of the EU and also Norway, Iceland and Liechtenstein.

3.1 The Creation of the FIN-NET

The idea of strengthening out-of-court procedures in financial services was mentioned in Financial Services Action Plan in 1999. European Commission determined fresh priorities for a single financial market. One of them was to find efficient judicial and extra-judicial settlement of disputes in the retail markets. According to the European Commission the network should promote cooperation in order to resolve cross-border consumer disputes and to enable consumers to refer such dispute to the competent extra-judicial body in the foreign country via the corresponding extra-judicial body in their own country.[15] As a result of these plans the network was launched by the European Commission on 1 February 2001.[16]

A body may become a member of the network, if it is responsible for out-of-court settlement between consumers and financial services providers and if it meets the criteria determined in Commission Recommendation 98/257/EC of 30 March 1998 on the principles applicable to the bodies

14 Apart from the FIN-NET there are other consumer complaints networks such as ECC-net or SOLVIT.

15 *Financial Services: Implementing the Framework For Financial Markets: Action Plan* [online]. Communication of the Commission, COM(1999)232, 11 May 1999 [cit. 2015-03-09], p. 10 - 11.

16 *Financial services: Commission Launches Out-of-court Complaints Network to Improve Consumer Confidence* [online]. European Commission Press Release, IP/01/152, Brussels, 1 February 2001 [cit. 2015-03-09].

responsible for out-of-court settlement of consumer disputes, such as independence, transparency, adversarial procedure, effectiveness, legality, liberty and representation.[17] All these principles may be referred as "fair procedure".[18]

At the moment, the FIN-NET consists of 58 members from 25 European Economic Area Countries.[19] In Poland there are three members of the FIN-NET which are Banking Ombudsman, Insurance Ombudsman and Arbitration Court at the Polish Financial Supervision Authority.[20] Each institution has its own scope of operation.

3.2 The Objectives of the FIN-NET

The most important aim of the FIN-NET is cooperation between the members in order to facilitate extra-judicial settlement of cross-border disputes between consumers and financial services providers.[21] The three detailed objectives of the FIN-NET are described in the Consumer Guide:

1. To provide consumer with easy and informed access to out-of-court redress in cross-border disputes.
2. To ensure efficient exchange of information between European schemes in order to ensure quick, efficient and professional handling of the cross-border complaints.
3. To ensure that out-of-court dispute settlement schemes from different EEA countries are applied with a common set of minimum guarantees.[22]

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17 *Memorandum of Understanding on a Cross-Border Out-of-Court Complaints Network for Financial Services in the European Economic Area* [online] [cit. 2015-03-09], p. 2 („Memorandum").

18 ŁĘTOWSKA, Ewa. *Europejskie prawo umów konsumenckich*. Warszawa: C.H. Beck, 2004. p. 385 - 390.

19 *Members of FIN-NET. FIN-NET Financial Dispute Resolution Network* [online] [cit. 2015-03-10].

20 See more TULIBACKA, Magdalena. Poland. In HODGES, Christopher J.S.; BENÖHR, Iris; CREUTZFELDT-BANDA, Naomi (ed.). *Consumer ADR in Europe* [online]. London: Hart Publishing, 2012 [cit. 2015-03-10], p. 185 – 193; RUTKOWSKA-TOMASZEWSKA, Edyta. *Ochrona prawna klienta na rynku usług bankowych*. Warszawa: Wolters Kluwer, 2013. p. 781 - 796. Insurance Ombudsman will transform into Financial Ombudsman on 11 October 2015.

21 Memorandum, p. 1.

22 *FIN-NET Settling Cross-border Financial Disputes Out of Court. Consumer Guide* [online]. European Commission [cit. 2015-03-10], p. 4.

3.3 The Procedure

The mechanisms and conditions of cooperation are outlined in the Memorandum of Understanding on a Cross-Border Out-of-Court Complaints Network for Financial Services in the European Economic Area ("Memorandum"). As it is stated directly in the Memorandum the provisions are not legally binding on the Parties and do not create any legal rights or obligations to the Parties or any third persons.[23]

Memorandum contains a few definitions necessary in determining the rules of functioning the FIN-NET. Firstly, "Out-of-court settlement" means "*a method which, regardless of the detailed procedure, leads to the settlement of disputes between consumers and providers in the area of financial services through the active intervention of a dispute settlement body that proposes or imposes a solution*". "Cross-border disputes" are construed by the Parties as "*a dispute between a consumer and financial services provider when the supplier is established in one Member State and the consumer has his residence in another Member State*". "The competent scheme" means "*the appropriate dispute settlement body for financial services in the country where the service provider is established*", while "the nearest scheme" means "*a dispute settlement body for the appropriate financial services sector in the consumer's country of residence*".

According to paragraph 6.1 Memorandum, firstly consumer may ask the nearest scheme for the information about the network and the competent scheme outlining contact information, coverage, organisation, languages, any charges payable by the consumer, whether the decision is binding on the financial institution or the consumer, typical times for handling complaints, limits, availability of an annual report and the fact of notification the scheme to the Commission (paragraph 8.1 Memorandum). The important thing is that the complaint procedures often differs in the model of the scheme, the scope of the body, charges, languages, binding force and limits. Some schemes are organised as an ombudsman, while the others provide complaint boards or consumer arbitration boards.[24] All the necessary information can be also found on the FIN-NET website on the information sheets.

23 Memorandum, p. 1.

24 *FIN-NET Settling Cross-border Financial Disputes Out of Court. Consumer Guide* [online]. European Commission [cit. 2015-03-11], p. 5.

In most cases consumer has to file complaint to the financial services provider directly before dispute settlement body is involved. The nearest scheme will inform the consumer if it is applicable and if any other limits (e.g. time) are provided (paragraph 6.2 Memorandum).

Consumer may obtain assistance in his or her dispute by the member of the FIN-NET in the state of residency. It is possible to ask only for information in mother tongue about proceedings in the other state and contact the competent scheme directly. However, the consumer may leave the complaint with the domestic nearest scheme which will transfer the case to the competent scheme. The Memorandum also presents the possibility to resolve the complaint by the nearest scheme if the financial service provider has accepted the jurisdiction of it or if the legal obligations of the nearest scheme oblige it to do so (paragraph 6.3 Memorandum).

According to paragraph 6.5 Memorandum from the moment of receiving the cross-border complaint, the competent scheme has to try to resolve the dispute on the basis of its terms of reference, legal obligations and in compliance with EU legislative acts.

Apart from the above basic rules of cooperation, the parties may agree on different way of cooperation if it is justified by the interest of settling the dispute more efficiently (paragraph 6.5 Memorandum).

3.4 The Result of the Procedure

It depends whether the ADR body helps the parties reach a settlement or issues a decision upholding or rejecting the claim. Some of them provide both kinds of solution.[25] In case of issuance a decision by the ADR body the binding or non-binding effect differs among the members of the network, so the consumer should be aware of that. On the website of the FIN-NET consumer may find Information sheets describing ADR schemes from all members including information about the result of the procedure. In the information sheets issued decisions are divided into three groups:

25 For example Dutch Financial Services Complaints Institute. It is determined by the type of the body and type of the ADR procedure (e.g. mediation or arbitration). *ADR Scheme. The Netherlands. Klachteninstituut Financiële Dienstverlening (Kifid)* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

recommendation not binding on either party, binding on the financial institution but not the consumer, binding on both the financial institution and the consumer.[26]

The analysis of the information sheets, which has been done for the purpose of this paper, has led to some remarks concerning the result of the procedure. In most schemes the consumer and the financial institution obtain recommendations, which are not binding on either party. Despite the non-binding character, some procedures provide possible sanctions in case of punishable behaviours determined in supervision acts (e.g. Spain).[27] Only in 15 schemes the decision is binding on the financial institution but not the consumer. However, in these cases some schemes provide condition that the decision is binding unless the financial institution informs of non-compliance within a specific period (for example in Denmark or in Iceland).[28] In Belgium cases solved by the body called *Ombudsfin* are binding on the financial institution only for basic banking account while in other cases the decision is only a recommendation.[29] Disputes solved by German Ombudsman Scheme of the Private Commercial Banks divide into two groups when criterion of binding force is taken into account. When the amount involved does not exceed 5000 €, the decision is binding on the bank, but not on the consumer. The bank is not bound if the amount exceeds mentioned sum.[30] Resolution agreement signed in the procedure enabled by the Mediation Centre of the Croatian Insurance Bureau is binding as it represents an execution title and entails the distraint clause.[31] In Hungary whether the decision

26 *Members of FIN-NET. FIN-NET Financial Dispute Resolution Network* [online] [cit. 2015-03-26].

27 *ADR Scheme. Spain. Complaints Service of the Directorate-General of Insurance and Pension Funds (DGSFP)* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

28 *ADR Scheme. Denmark. Danish Complaint Board of Banking Services* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Iceland. The Complaints Committee on Transactions with Financial Firms* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

29 *ADR Scheme. Belgium. Ombudsfin* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

30 *ADR Scheme. Germany. Ombudsman Scheme of the Private Commercial Banks* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

31 *ADR Scheme. Croatia. Mediation Centre of the Croatian Insurance Bureau* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

is binding or only a recommendation depends on the declaration of acceptance made by the financial institution.[32] Disputes addressed to Dutch Financial Services Complaints Institute are divided to Ombudsman cases and Tribunal cases. The Ombudsman gives the parties only a recommendation while the Tribunal issues a decision binding on both the financial institution and the consumer.[33] In 9 schemes out of 58 the ADR body issues a decision binding both the financial institution and the consumer (however some of these bodies issue also the other types of decisions).[34]

4 Efficiency of Resolution of Financial Services-disputes

The number of cross-border cases is growing from 1041 in 2007 to 2727 in 2012. The biggest growth can be observed in 2012, because of change from 1854 cases in 2011 to 2727.[35] This data proves that the role of the FIN-NET may grow as the number of cross-border cases is growing. The network was launched 14 years ago, therefore it is possible to assess the efficiency of it.

32 *ADR Scheme. Hungary. Arbitration Board of Budapest* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

33 *ADR Scheme. The Netherlands. Klachteninstituut Financiële Dienstverlening (Kifid)* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

34 *ADR Scheme. Czech republic. Financial Arbiter of the Czech Republic* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Ireland. Financial Services Ombudsman's Bureau* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Croatia. Mediation Centre of the Croatian Insurance Bureau* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Hungary. Arbitration Board of Budapest* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Hungary. Financial Arbitration Board (FAB)* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Poland. Arbitration Court at the Polish Financial Supervision Authority* [online] Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Portugal. CMVM - Portuguese Securities Market Commision.* [online] Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. Portugal. Lisbon Arbitration Centre for Consumer Conflicts.* [online] Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26]; *ADR Scheme. The Netherlands. Klachteninstituut Financiële Dienstverlening (Kifid)* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

35 *FIN-NET Activity Report 2012* [online]. European Commission [cit. 2015-03-11], p. 4.

4.1 General Impression about the Network

The network has been subject to numerous assessments, comments and one complex report called "Evaluation of FIN-NET" which was prepared in 2009.[36] In this document Centre for Strategy & Evaluation Services assessed the network whether it complies with the following criteria: Relevance, Effectiveness and Efficiency.

In general the idea of creating the network is appreciated. The FIN-NET network is appreciated for support, guidance and information given.[37] The exchange of information and experience by the bodies which are members is regarded as a positive effect of the network.[38] Another advantage of the members of the FIN-NET is the specific qualification and knowledge in the branch of financial services necessary to solve such dispute.[39]

Furthermore, the guidelines for the procedure are not binding the ADR bodies. As it is directly stated in the paragraph 6.5 Memorandum, the cooperation may be formed in different way provided that it is more efficient for solving the dispute. This flexibility should be assessed positively, because the most important in solving cross-border dispute is the desirable effect - namely the resolution of the dispute.

One of the weaknesses of the FIN-NET is the fact that the system does not cover all sectors (banking, payments, insurance and securities) in all European Economic Area countries.[40] However, in spite of the 6 years that passed since the Evaluation report was published, some of the countries still do not have the schemes which take part in the network. These countries

36 *Evaluation of FIN-NET. Final Report* [online]. Centre for Strategy & Evaluation Services. June 2009 [cit. 2015-03-11]. Some remarks was also made in White Paper - Financial Services Policy 2005-2010. Commision of the European Communities, 1. 12. 2005. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52005DC0629.

37 *Cross Border Alternative Dispute Resolution in the European Union* [online]. European Parliament, IP/A/IMCO/ST/2010-15, June 2011 [cit. 2015-03-11], p. 46.

38 *Evaluation of FIN-NET. Final Report* [online]. Centre for Strategy & Evaluation Services, June 2009 [cit. 2015-03-11]. p. iii.

39 TARGAŃSKI, Bartosz. Formula polubownego rozstrzygania sporów transgranicznych z udziałem konsumenta usług finansowych. In GNELA, Bogusława (ed.). *Ochrona konsumenta usług finansowych*. Warszawa: Wolters Kluwer, 2007, p. 319.

40 *Evaluation of FIN-NET. Final Report* [online]. Centre for Strategy & Evaluation Services. June 2009 [cit. 2015-03-11], p. iii.

are Bulgaria, Romania, Cyprus, Latvia, Slovakia and Slovenia and there are no bodies from these countries listed as the FIN-NET members.[41] If the network is not covering all countries, the consumers may have difficulties in the case of potential dispute.

The voluntariness of the membership in the network is regarded as one of the most important issues concerned with the role of the FIN-NET.[42] The opinion differs, although obligatory membership in the network would not guarantee the cooperation of the ADR institutions. In the Report about cross-border ADR the authors underlined that the procedure of ADR would be more effective when Member States were required to have at least one ADR scheme in each sector.[43] The lack of adhering ADR scheme is regarded as serious obstacle in solving of cross-border disputes.[44]

The essential issue which may also create a barrier for the FIN-NET is low awareness of the network among European consumers.[45] It is said that the key factor is persuading both consumers and financial institutions about the advantages of the schemes.[46] They should be informed about possibilities which the FIN-NET gives if the network is intended to fulfill their objectives effectively.

4.2 Aspects of Efficiency

Scholars underline that alternative dispute resolution methods are more effective than court proceedings when it differs in the amount of fee,

41 *Members of FIN-NET. FIN-NET Financial Dispute Resolution Network* [online] [cit. 2015-03-26].

42 Petrauskas, Feliksas; Gasiūnaitė, Aida. Alternative Dispute Resolution in the Field of Consumer Financial Services. *Jurisprudence* [online]. 2012, Vol. 19, No.1 [cit. 2015-03-12], p. 184.

43 *Cross Border Alternative Dispute Resolution in the European Union* [online]. European Parliament, IP/A/IMCO/ST/2010-15, June 2011 [cit. 2015-03-12], p. 84.

44 WIĘCKO-TUŁOWIECKA, Małgorzata. Alternatywne metody rozwiązywania sporów z zakresu umów ubezpieczenia - dyrektywa ADR, europejska sieć rozstrzygania sporów Fin-Net. *ADR - Arbitraż i Mediacja.* 2013, No. 3. p. 71.

45 *Evaluation of FIN-NET. Final report* [online]. Centre for Strategy & Evaluation Services. June 2009 [cit. 2015-03-12], p. iv; PENCZAR, Marta. Ochrona konsumenta na integrujących się rynkach finansowych w Unii Europejskiej. *Bank i Kredyt. Integracja rynków finansowych w Unii Europejskiej od A do Z* [online]. 2007, Vol. 38, No.7 [cit. 2015-03-13], p. 14.

46 Petrauskas, Feliksas; Gasiūnaitė, Aida. Alternative Dispute Resolution in the Field of Consumer Financial Services. *Jurisprudence* [online]. 2012, Vol. 19, No. 1 [cit. 2015-03-12]. p. 184.

duration and the level of complexity.[47] Furthermore, the issue of languages should be analysed in the context of network's efficiency.

4.2.1 The Cost of the Procedure

The first criterion mentioned above, as analysis of information sheets of the FIN-NET members shows, is fulfilled by the most of the schemes. Only 12 of 58 members impose the obligation to pay the fee for the proceedings.[48] However, there are further provisions in some schemes that the fee is refunded in case of acceptance of consumer's claim. What may be surprising in some information sheets the maximum fee is at a high level (such as 900 € in Liechtenstein).[49]

4.2.2 Duration of the Procedure

Moving to the next aspect which may determine the efficiency of out-of-court procedure is duration of the resolution of the dispute. This can be considered as one of the most important issues of solving a dispute. Alternative dispute resolution is widely regarded as a much shorter procedure than the court proceedings. However, the analysis of the information sheets has brought ambiguous results.[50] For example in Denmark average time to resolve the dispute is determined as 9-10 months,[51] while as the statistics in 2010 show that the average time of civil litigious case was 180 days, which is a result even 30% shorter.[52] Poland may be a proper

47 RUTKOWSKA-TOMASZEWSKA, Edyta. Bankowość konsumencka. In GÓRALCZYK, Wojciech (ed.). *Problemy współczesnej bankowości. Zagadnienia prawne*. Warszawa: Wolters Kluwer, 2014, p. 225.

48 The statistics and information about costs of the ADR have been created for the purpose of the paper by the analysis of the information sheets published on the FIN-NET website. *Members of FIN-NET. FIN-NET Financial Dispute Resolution Network* [online] [cit. 2015-03-26]

49 *ADR Scheme. Liechtenstein. Arbitration Board for the Settlement of Disputes Concerning Cross-border Credit Transfers* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [online] [cit. 2015-03-26].

50 The statistics and information about duration have been created for the purpose of the paper by the analysis of the information sheets published on the FIN-NET website. *Members of FIN-NET. FIN-NET Financial Dispute Resolution Network* [online] [cit. 2015-03-26].

51 *Inter alia ADR Scheme. Denmark. Danish Complaint Board of Banking Services* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

52 *Compiled Report. The Functioning of Judicial Systems and the Situation of the Economy in the European Union Member States* [online]. European Commision for the Efficiency of Justice, Strasbourg, 15 January 2013 [cit. 2015-03-12], p. 625.

example of positive effect of alternative dispute resolution for consumers. The average time of the litigious civil case is 180 days, while the scheme states average time to solve the case at the level of 4-5 weeks.[53] The duration of the out-of-court resolution of the dispute should be beneficiary for the consumer if ADR is intended to be competitive to the court proceedings. What is more, quickness of the alternative dispute resolution is often presented to the consumers as an inevitable attribute of ADR.

4.2.3 Languages

The other vital issue is the language in which a complaint can be made and in which decision may be issued. Some schemes provide issuing it in more languages instead of only the native language. In my opinion, efficient resolution of cross-border disputes between financial services providers and consumers is not possible without ADR institutions operating in more than one language. In order to ensure clear and effective out-of-court procedures of solving the cross-border financial services disputes, especially with consumers, the network should consist of schemes which can be undertaken not only in mother tongue but also at least in English. As the analysis of information sheets revealed most of the schemes have already met this criterion, although there are still some which do not. It may be surprising in the light of paragraph 7 Memorandum which states that the consumer, who does not choose to operate with the usual working language of the competent scheme, may do it in the language either of his contract with the financial services provider or in which he normally dealt with it. What could be observed as well is that more institutions only enable consumers to fill a complaint in foreign language while the decisions can be issued only in the native language. As an unquestionable conclusion, the topic of quantity of languages used in out-of-court schemes should be taken into consideration by the FIN-NET members. The problem of languages was noticed in the Evaluation in 2009[54] and it has still not been solved.

53 *ADR Scheme. Poland. Banking Ombudsman* [online]. Members of FIN-NET. FIN-NET Financial Dispute Resolution Network [cit. 2015-03-26].

54 *Evaluation of FIN-NET. Final Report* [online]. Centre for Strategy & Evaluation Services. June 2009 [cit. 2015-03-14], p. iv.

4.3 Potential Improvement of the Network's Efficiency

In the Evaluation of the network some recommendations have been given. The most important ones are changing existing coverage gaps, increasing the visibility and awareness of out-of-court dispute resolution and the network.[55] These suggestions deserve for approval.

Some changes may be brought by recently issued acts such as ADR directive and ODR regulation.[56] Scholars underline that the difference of the availability and quality of the schemes across the Member States is an obstacle. However, this drawback may be eliminated by the ADR directive[57] the aim of which is to ensure access to simple, efficient, fast and low-cost ways of resolving both domestic and cross-border disputes (motive 4). The European legislator underlines that ADR is not yet sufficiently and consistently developed across the EU (motive 5), so the action on EU level is needful. However, mentioned acts are also under criticism because of a few aspects such as possible effect of impeding the access to the court or the risk of insufficient law acquaintance of ADR bodies.[58]

5 Conclusion

In conclusion, the idea of the network of schemes solving the disputes between the financial service providers and consumers might be regarded as necessary to create common market in this branch and to improve trust of consumers. The information provided by the FIN-NET members are valuable and facilitates the access to the competent schemes in the state which is not the state of consumer's residence. The information given consists of the most important issues concerning ADR body in the foreign Member State. The possibility of filling the complaint to the nearest scheme which

55 *Evaluation of FIN-NET. Final Report* [online]. Centre for Strategy & Evaluation Services. June 2009 [cit. 2015-03-14], p. vi-vii.

56 The wide issue of possible impact of ADR directive and ODR regulation exceeds the scope and volume of these paper.

57 BENÖHR, Iris. Alternative Dispute Resolution in the EU. In HODGES, Christopher J.S.; BENÖHR, Iris; CREUTZFELDT-BANDA, Naomi (ed.). *Consumer ADR in Europe* [online]. London: Hart Publishing, 2012 [cit. 2015-03-14], p. 17.

58 See more MUCHA, Jagna. Alternatywne metody rozwiązywania sporów konsumenckich w prawie unijnym - nowe rozwiązania prawne (dyrektywa 2013/11/UE w sprawie ADR oraz rozporządzenie nr 524/2013 w sprawie ODR). *Internetowy Kwartalnik Antymonopolowy i Regulacyjny* [online]. 2014, No. 4(3) [cit. 2015-03-15], p. 79 - 89.

may pass it to the competent scheme should also be approved. The lack of costs for the consumers in most schemes may be determined as a significant advantage of the ADR in financial services as well. The possibility of exchanging information is also beneficiary to notice the differences between the ADR bodies in various European countries.

However, there are still issues which may be seen as a challenge for the FIN-NET, such as coverage of the network or its accessibility. Unfortunately, these drawbacks were noticed some time ago and in some cases the FIN-NET still has not improved. The network should consist of the ADR bodies of all European Economic Area countries. This criterion has not been met yet, so the consumers cannot obtain all essential information and solve the cross-border financial services dispute easily in all cases. It is likely that the number of cross-border financial services disputes will grow, so the consumers should be ensured with the out-of-court schemes which enable them to solve their dispute in quick and effective manner. Meanwhile, the efficiency of the system ought to be improved especially in the field of coverage gaps, languages of the procedures and increasing visibility of the network and awareness of consumers. This last issue may be seen as the most important because the network is not widely known among the consumers. The concept of the FIN-NET should be promoted in order to convince the consumers to benefit from ADR in financial services in cross-border disputes as well.

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ONLINE DISPUTE RESOLUTION AND THE LATEST DEVELOPMENT OF UNCITRAL MODEL LAW

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Abstract

The influence of modern technologies (especially of the Internet) has been enormous in last two decades. It had crucial impact mainly on the swift growth of cross-border electronic commerce. Traditional judicial mechanisms were unable to offer proportionate solution to deal with e-commerce disputes. Such situation had opened up an area for Online Dispute Resolution. Online Dispute Resolution rules are however being developed ad hoc recently. The necessity to unify this shattered area was foreseen by the UNCITRAL which had charged Working Group III with creation of the model law. This paper will focus on the main aspects of the model law. It will try to describe problematic areas as well as the current state of the development of such rules. It was predicted that model law should be already prepared however major conflicts between different law cultures slow down and limit further advancement. The paper in the end expresses the necessity to clearly define the scope of the model law to be possible to move further and to offer highly needed UNICTRAL rules for Online Dispute Resolution.

Keywords

UNCITRAL; Online Dispute Resolution; Working Group III; Electronic Commerce.

1 Introduction[1]

The popularity of the Internet continues to grow rapidly and the interconnected network is used for many different purposes. Electronic

[1] This article cannot unfortunately cover all Working Group III activities but it focuses on the most important aspects concerning drafting global online dispute resolution rules.

commerce[2] is one of the major fields from which the Internet users can benefit and which allows them to purchase a plentiful range of goods or provide services anywhere in the world. With increasing use of e-commerce[3] also the number of potential disputes can arise. "Traditional judicial mechanisms for legal recourse did not offer an adequate solution for cross-border electronic commerce disputes, and that the solution (providing a quick resolution and enforcement of disputes across borders) might reside in a global online dispute resolution system for small value, high volume B2B and B2C disputes."[4]

Online dispute resolution ("ODR") is "*dispute resolution carried out by combining the information processing powers of computers with the networked communication facilities of the Internet.*"[5]

The costs to deal with above indicated disputes in traditional way are over exceeding the value of the goods or offered services, thus the costs of the proceedings to solve the dispute at court would be inadequately high. Available options granted by national mechanisms for resolving disputes of this kind are therefore not appropriate.[6]

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2 The term of electronic commerce is not new and not connected only to the development of the trade through the internet. It could be defined as any business transaction where the participants are not located at same place and they communicate electronically. The exchange of information electronically uses six basic tools: telephone, fax, television, electronic payment system and money transfer, electronic data interchange and the Internet. TODD, Paul. *E-commerce Law.* Oxon: Routledge-Cavendish, 2005. p. 3.

3 To see more: *E-commerce statistics* [online]. [cit. 2015-03-03].

4 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Twenty second session, Vienna, 13 - 17 December 2010, A/CN.9/WG.III/WP.105 [cit. 2015-03-09], para. 25.

5 ODR is frequently defined as out of courts solution however it cannot be fully agreed with such point of view. ODR mechanisms can often offer the tools even for court proceedings and those can serve as the inspiration in deepening of eJustice mechanisms. HÖRNLE, Julia. *Cross-border Internet Dispute Resolution.* Cambridge: Cambridge University Press, 2009. p. 75.

6 „*The view was also expressed that enforcement of awards cross-border was difficult if not impossible in light of the lack of treaties providing for cross-border enforcement of awards in B2C transactions.*" *Report of Working Group III (Online Dispute Resolution) on the Work of its Twenty-second Session (Vienna, 13 - 17 December 2010)* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution),Twenty second session, Vienna, 13 - 17 December 2010, A/CN.9/716 [cit. 2015-03-07].

One of the key aspects of online dispute resolution is that value of the goods or services meant to be solved by ODR is usually small, but the number of possible disputes is very high (low-value high-volume cases). "*This suggests the need for specific legal standards for ODR, being more than a simple adaptation of existing arbitration and electronic communication rules.*"[7] ODR however does not offer the solution to solve only low-value disputes although this is its primary mission. "Low-value" is not anyhow defined and it should be reflected that small value is not same in each state.[8]

However there is no global standard on ODR and the rules of providers are created *ad hoc*, thus there is no supervision and the providers cannot follow any model law created. The set of rules is definitely needed despite the voices that private providers will continue to follow an *ad hoc* trend in the future.[9]

Such situation lead to the establishment of Working Group III: Online Dispute Resolution by the United Nations Commission on International Trade Law ("UNCITRAL") in 2010 ("Working Group"). The main purpose is to develop set of model laws and to stabilize uncontrollable development of different ODR systems without any further harmonization. It is however necessary to state that the main purpose of such model laws is to offer an inspiration for the states, which are preparing the adaptation

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7 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions* [online]. United Nations Commission on International Trade Law. Working Group III (Online Dispute Resolution), Twenty second session, Vienna, 13 - 17 December 2010, A/CN.9/WG.III/WP.105 [cit. 2015-03-12], para. 25.

8 The option to buy / sell e.g. vehicles at eBay auction house could be stated as an example. This means also the possibility to solve the disputes arising from such trading. The value of the dispute solved by ODR is limited to the range between $ 100 and $50.000. Hence ODR is not generally limited only to a low-value disputes, how we could typically understand it. This is because of the nature of the dispute-not the amount of money is decisive, but the character of the dispute is. Even if the disputes are higher value, ODR can offer the possibility of its effective resolution in the case that the dispute keeps its elementary character and simple background. *Vehicle Purchase Protection. eBay* [online]. [cit. 2015-03-09].

9 The main aim of the rules is to apply to the disputes arising from e-commerce and on online transactions (sale of goods and offering the services). ODR tools can be however applied to various types of conflict resolution situation, thus wide range of disputes can be solved by ODR. It mainly depends on the design of the system. ODR can solve business disputes, disputes with government, specialized disputes (e.g. health payments) or disputes from arising from divorce. Modria, Cybersettle, Juripax or Youstice ODR providers can be given as good example of the complexity of possible ODR solutions.

of the regulation into the national legislation. Thus offering the general guideline how to incorporate definite legislation in the state shall be the main role of model law.

2 Working Group and Model Law

The main purpose of the model law is to offer normative framework for being possible to solve "*cross-border electronic commerce transactions, including business-to-business (B2B) and business-to-consumer (B2C) transactions*"[10] using online dispute resolution.[11] Narrow model would non-adequately limit the possibilities of out of court dispute resolution, thus draft procedural rules will offer negotiation between the parties using automated software tools, mediation/conciliation (called facilitated settlement stage) and arbitration. There are however "*reasons to doubt the suitability of the approach adopted by UNCITRAL. It is submitted that 'one size fits all' procedure that culminates in arbitration does not take account of the diversity of e-commerce disputes; nor does the legally binding nature of an award necessarily ensure that it will be enforced in a context where final outcomes should be primarily enforced outside the courts.*"[12]

Online negotiation and mediation as the first two stages of the process are trying to offer quick non-binding solution for the dispute settlement thus the time periods are broadly limited (10 days in both stages).[13] They are however fully using the possibilities offered by the Internet and modern

10 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions* [online]. United Nations Commission on International Trade Law. Working Group III (Online Dispute Resolution), Twenty second session, Vienna, 13 - 17 December 2010, A/CN.9/WG.III/WP.105 [cit. 2015-03-10], para. 2.

11 UNCITRAL is planning to draft procedural rules, guidelines and minimum standards for neutrals, guidelines and minimum standards for providers, substantive legal principles for resolving disputes and cross-border mechanisms for enforcement. In current stage Working Group is still struggling to agree on basic framework of the rules and main aspects of model law. *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirty first session, New York, 9 - 13 February 2015, A/CN.9/WG.III/WP.105 [cit. 2015-03-09], Draft Preamble.

12 CORTES, Pablo; DE LA ROSA, Esteban. Building a Global Redress System for Low-value Cross-border Disputes. *International & Comparative Law Quarterly*. 2013, Vol. 62, No. 2, p. 407 - 440.

13 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirty first session, New York, 9 - 13 February 2015, A/CN.9/WG.III/WP.105 [cit. 2015-03-10], Draft Art. 5, para. 4.

technologies-email, audio/video communication and assistance of the software including online platform serving for exchange of information. Great advantage of those stages is seen mainly in the dynamic form which is possible to react at the direction of the dispute by modulating the process (different disputes need different approaches).[14]

Online arbitration phase should lead to the decision which is final and binding. This is one of the main problematic areas of the draft rules and in the progress in the negotiations, because not every national provision grants the possibility to solve consumer disputes in arbitration (or allows to conclude pre-dispute arbitration clause in consumer disputes).

Global rules are offering the mechanisms to improve the confidence in ODR by implementing the trustmarks. These mechanisms should provide approval of online merchants (and offer mechanisms to attest the merchant); the trustmark logo will inform the buyers that the merchant is offering decent level of service by displaying the logo at his pages, thus it should persuade the buyers about the attractiveness of the offered service.[15]

The representatives from United States of America and Columbia have proposed at the latest session of Working Group the implementation of the chargeback payment enforcement mechanism. "*In order for any non-binding recommendation to provide sufficient consumer protection, the recommendation would need to be legally linked to the same money transfer payment channel as the original payment, given the general lack of judicial remedies in cross-border e-commerce transactions.*"[16] Chargeback mechanisms offer the possibility to return

14 Different software solutions can be seen at every ODR provider. The role of the software is important in the meaning, that it offers the parties communication platform which then helps them and assists with solving the dispute. It is statistically proved, that in the first two stages the parties just by communication and with assistance of the software can reach an agreement (settlement) in 80 % of the disputes. *Modria* [online]. [cit. 2015-03-14].

15 Trustmark mechanisms are generally seen as very important tools to convince the customers, that the service is secured and quality. It has to be stated that the list of providers of trustmark at the pages of UNCITRAL is very limited and one of the listed providers even does not offer the service any more (Better Business Bureau (BBB) OnLine)! This can be verified here: *Online Dispute Resolution: On-line Resources* [online]. [cit. 2015-03-12].

16 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions Proposal by the Governments of Colombia and the United States of America Note by the Secretariat* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirty first session, New York, 9 - 13 February 2015, A/CN.9/WG.III/WP.105 [cit. 2015-03-10], para. 3.

the funds back to the customer, when the contract of purchase of goods or services has been breached. As it was stated in the proposal the charge-back is not limited only to the credit card payments; it can include debit card payments or any other electronic payment (electronic money). Such presented mechanisms are ideal to be incorporated into ODR system thus into draft ODR rules. "*A chargeback legal framework provides many benefits including: (1) mandatory application to vendors through use of a payment channel (rather than voluntary application based on a private agreement with a specific ODR provider); (2) buyers may opt into the system post-dispute; (3) buyers do not waive court remedies; and (4) enforcement of a decision is guaranteed cross-border without costly court intervention.*"[17]

3 Selected Issues of Global ODR Rules

3.1 Scope of the Rules

UNCITRAL is trying to offer wide scope of the rules. This could appear as problematic because of high complexity and dissimilarity of the dispute issues. UNCITRAL is "*considering the possibility of narrowing the scope of the Rules to so-called 'simple fact-based claims' arising from the sale of goods and the provision of services.*"[18] The scope limited to sale of goods and providing services can undoubtedly use the advantage of modern technologies more by offering more concrete normative framework. On the other hand as the character of the model law is mainly inspirational, disproportionate limitation would harm the main purpose of the model law-to "*establish new paradigm for dispute resolution for e-commerce, in a similar way that the Uniform Domain Name Dispute Resolution Procedure (UDRP) adopted by International Corporation for Assigned Names and Numbers (ICANN) has changed the paradigm for disputes arising out of the conflict between domain names and trademarks.*"[19] Hence the limitation

17 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions Proposal by the Governments of Colombia and the United States of America Note by the Secretariat* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirty first session, New York, 9 - 13 February 2015, A/CN.9/WG.III/WP.105 [cit. 2015-03-12], para. 6.

18 CORTES, Pablo; DE LA ROSA, Esteban. Building a Global Redress System for Low-Value Cross-border Disputes. *International & Comparative Law Quarterly*. 2013, Vol. 62, No. 2, p. 407 - 440.

19 HÖRNLE, Julia. Encouraging Online Alternative Dispute Resolution (ADR) in the EU and Beyond. *European Law Review*. 2013, Vol. 38, p. 187 - 208.

to only few types of disputes (sale of goods and providing services) would be inappropriate.[20] The main advantage of ODR especially in non-binding stages can be utilized mainly in the simple fact-based claims. Such limitation of the model law is seen as beneficial, however hard to be defined *in concreto.* "*It is also important to point out, that the UNCITRAL initiative is designed for cross-border low-value, high-volume disputes, which are mass claims not involving complex factual or legal issues. The Working Group has decided not to define the terms "cross-border low value and high volume disputes" but intends to provide more guidance in a commentary.*"[21]

3.2 "Two Track" or "Second Click"?

The process of dispute settlement starts in the phase of consensual settlement. Automated negotiation as the first step should provide the parties the space to exchange information and offer them decent software environment. When the parties fail to settle the dispute, they continue through the second phase-facilitated settlement ended by the recommendation by neutral.[22] If the dispute is still unresolved and the parties had not accepted the recommendation the dispute is then escalated into arbitration phase, which shall be binding. The final phase is causing the main problems in the moment why the negotiations and drafting the model law are not moving further. The model law is not primarily focused on the consumer

20 As it was mentioned previously, the type of the disputes possibly being solved by ODR mechanisms is very broad and it would be unfortunate on the global level to limit the rules only to few types of the disputes.

21 HÖRNLE, Julia. Encouraging Online Alternative Dispute Resolution (ADR) in the EU and Beyond. *European Law Review*. 2013, Vol. 38, p. 187 - 208.

22 „*The neutral shall, within fifteen (15) calendar days of the expiry of the facilitated settlement stage, evaluate the dispute based on the information submitted by the parties, and having regard to the terms of the agreement, shall make a recommendation in relation to the resolution of the dispute. The ODR administrator shall communicate that recommendation to the parties and the recommendation shall be recorded on the ODR platform.*" *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules (Track II)* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirtieth session, Vienna, 20 - 24 October 2014, A/CN.9/WG.III/WP.130 [cit. 2015-03-13], Draft Art. 7, para. 3.

protection[23] thus the rules do not distinct between B2B, B2C or consumer-to-consumer disputes and will apply on every type of the dispute. This causes the main divergence of the views into two groups. The first one is represented by the delegations where the binding arbitration has a long tradition (especially United States of America). The second group is represented mainly by the delegations from the European Union states. "*Whether a pre-dispute arbitration agreement in a consumer contract is valid, is a question to which different national laws provide different answers.*"[24]

Whereas in many European states the pre-dispute consumer arbitration agreement is forbidden or broadly limited to the listed cases and whereas in the US it is one of the frequently used mechanism to settle the dispute (and hardly limited), this dichotomy creates the main discrepancy between the delegations and blocked further progress. Fortunately the discussions are going on, thus so called two track system was introduced.

It was also expressly stated that "*the Rules shall not apply where the law of the buyer's state of residence provides that agreements to submit a dispute within the scope of the ODR Rules are binding on the buyer only if they were made after the dispute has arisen and the buyer has not given such agreement after the dispute has arisen or confirmed such agreement which it had given at the time of the transaction.*"[25] This provision led to the development of the two track system when the draft rules were introduced at the meeting in Vienna in 2014.

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23 EU initiative can be stated here as choosing the opposite approach, hence the main target of the proposed legislation is consumer protection. Regulation (EU) No 524/2013 of the European Parliament and of the Council of 21 May 2013 on online dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC (Regulation on Consumer ODR) In *EUR-lex*. Available from: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:165:0001:0012:EN:PDF Directive 2013/11/EU of the European Parliament and of the Council of 21 May 2013 on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC (Directive on Consumer ADR). In *EUR-lex*. Available from: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:165:0063:0079:EN:PDF

24 HÖRNLE, Julia. Encouraging Online Alternative Dispute Resolution (ADR) in the EU and Beyond. *European Law Review*. 2013, Vol. 38, p. 187 - 208.

25 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Twenty sixth session, Vienna, 5 - 9 November 2012, A/CN.9/WG.III/WP.117 [cit. 2015-03-13], Draft Art. 1, option 1.

Track I of the draft rules is ended by the binding arbitration phase. If the parties did not agree on the settlement "*the ODR administrator shall promptly notify the parties* […] *that they have moved from the consensual stage of proceedings to the binding arbitration stage.*"[26]

Track II respects the pre-arbitration clause exclusion and draft the text of the rules without any possibility to end in a binding arbitration phase.[27] The rules in this case will apply to the disputes where the parties "*explicitly agreed that disputes relating to that transaction and falling within the scope of the Rules shall be resolved under the Rules.*"[28] It is also proposed that the "*agreement separate and independent from that transaction, and notice in plain language that disputes relating to the transaction and falling within the scope of the Rules will be resolved through ODR proceedings under the Rules*"[29]

	Track I	Track II
Binding or non-binding ODR	Binding	Non-binding
Number of phases in the settlement process	Three (negotiation, facilitated settlement, arbitration)	Two (negotiation, facilitated settlement)
Final degree of settlement	Arbitration	Non-binding recommendation (after facilitated settlement is unsuccessful)
Cost and time demands	Successful settlement: low	Successful settlement: low
	Arbitration settlement: Low to Middle	Unsuccessful settlement: very high (if the dispute is solved at court proceedings)

Chart 1: Comparison of Track I and Track II of the draft procedural rules

26 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules (Track I)* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirtieth session, Vienna, 20 - 24 October 2014, A/CN.9/WG.III/WP.131 [cit. 2015-03-13], Draft Art. 6, para 3.

27 It was also proposed that under the model law there should be the list of countries which agreed on using Track I or Track II, because of the possible conflicts when one party of the dispute would be able to follow "only" Track II mechanisms.

28 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules (Track II)* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirtieth session, Vienna, 20 - 24 October 2014, A/CN.9/WG.III/WP.130, [cit. 2015-03-14], Draft Art. 1.

29 *Online Dispute Resolution for Cross-border Electronic Commerce Transactions: Draft Procedural Rules (Track II)* [online]. United Nations Commission on International Trade Law, Working Group III (Online Dispute Resolution), Thirtieth session, Vienna, 20 - 24 October 2014, A/CN.9/WG.III/WP.130 [cit. 2015-03-14], Draft Art. 1bis.

As the chart above shows Working Group did not choose to harmonize law or law approximation. It is also not an intention to force the states to change their law (or avoid it completely) because of the customer pre-arbitration agreement issues. The main intent is to provide practical "*avenues of redress for small-value disputes where currently none exists.*"[30]

Dividing the rules into two tracks is not ideal mainly because of the possible complicated situations when one of the parties of the dispute would be located in the state with higher consumer protection (no possibility of pre-dispute arbitration clause) and the second party would be located in the state where there is no limitation to conclude consumer pre-arbitration clause. That is why it was proposed at the meeting at Vienna in 2014 that so called second click approval would be more efficient and would deal with above stated issues more conveniently. The mechanism could be described as the second choice option how to participate in binding arbitration phase. If negotiation or facilitated settlement would be unsuccessful, than the parties will be offered to decide if they want to proceed to arbitration phase or not. In that case pre-dispute consumer arbitration clause would be avoided (or at least reduced to the minimum) and the freedom of the parties to decide, how they want to solve their case would be increased to the maximum.[31]

3.3 Briefly to Further Issues

Procedural rules, costs and the speed of the process have to be adequate to the dispute-its value and the importance of the solved issues. As it is expected that the rules will be applied mainly to low-value high-volume disputes which are simple fact based thus their essence is quite repetitive, the rules are not ensuring the same level of due process as it is at the court proceedings. "*However, this rough-justice approach is* […] *justified in low–value, high-volume cases; hence it is all the more important that (1) the application of the Rules is clearly defined, and (2) redress to the courts for consumers is still possible* […]*, unless*

30 HÖRNLE, Julia. Encouraging Online Alternative Dispute Resolution (ADR) in the EU and Beyond. *European Law Review*. 2013, Vol. 38, p. 187 - 208.

31 The states which do not want to participate on the second click possibility would be listed in the annex to inform the counter parties about such level of consumer protection.

the consumer has agreed to the arbitration after the dispute has arisen. In low-value, high-volume claims it is unlikely that consumers will regularly resort to litigation in any event."[32]

Above described issues concerning the preparation of model law are not the only one discussed. Some issues are appearing also with choosing the language of the proceedings (especially when the parties are speaking different languages), limited time frame of the proceedings, concerns with designing the ODR platform or general problems with the arbitration stage of the process (the lack of transparency and the lack of precedents are establishing untrustworthiness).

All these questions raise a lot of concern and provide a wide field for future discussions and analysis.

4 Conclusion

This paper had focused on the main aspects of the model law created by UNCITRAL Working Group. It has chosen the most problematic areas and tried to offer current state of the development of the rules. Unfortunately many different opinions are tying up further advancement in drafting such model law.

"*The expansion of e-commerce* (and not only e-commerce) *is limited by the default channel for resolving problems, this being courts, which are unable to deal with high-volume of low-value disputes arising from the online market.*"[33]

After four years of discussions and the activity of Working Group, the rules are still in the earlier stage. The direction and the scope of the rules is still not clearly decided and it is not uncommon, that the discussions are dealing with the same question for more than once without any clearer consensus. These afflictions have to be eliminated despite the onerous consensus on the basic issues as was stated above. Global ODR rules would strongly contribute to the expansion of the out of court dispute resolution and online merchants and customers would have appropriate and fast instrument to solve their

32 HÖRNLE, Julia. Encouraging Online Alternative Dispute Resolution (ADR) in the EU and Beyond. *European Law Review*. 2013, Vol. 38, p. 187 - 208.

33 CORTES, Pablo; DE LA ROSA, Esteban. Building a Global Redress System for Low-value Cross-border Disputes. *International & Comparative Law Quarterly*. 2013, Vol. 62, No. 2, p. 407 - 440.

dispute as could be seen in the European Union's Directive on ADR and Regulation on ODR. Also the success of UNCITRAL initiatives depends mainly on their compatibility and mutual respect with EU ODR provisions.

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ALTERNATIVE DISPUTES RESOLUTION FOR CONSUMER CONTRACTS: CHALLENGES FOR EU AND ITS IMPLEMENTATION IN SLOVAKIA

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Abstract

This paper focuses on current challenges in arbitration law in the context of consumer contracts. It starts with a brief introduction on need to regulate this very specific area by considering arguments for and against the arbitration clauses in consumer contracts in general. The authors then move onto short history excursion on "prohibition" of alternative dispute resolution in the EU with emphasis on current EU legal framework - Directive 2013/11/EU on alternative dispute resolution for consumer disputes (the "Directive") and Regulation (EU) No. 524/2013 on online dispute resolution for consumer disputes. As a result of this activity on EU level, a new Slovak legislation implementing the Directive has come into force on January 1, 2015 separating the consumer arbitration from the "general commercial arbitration" which raised several questions by public that remained unanswered. Authors discuss this new legislation in depth taking into consideration practical aspects and implications. Final remarks contain predictions on further development of consumer arbitration.

Keywords

Arbitration Law; Arbitration Clauses in Consumer Contracts; Online Dispute Resolution; New Slovak Consumer Arbitration Law.

1 Introductory Remarks

The consumer protection in the European Union ("EU") has enjoyed in recent years significant level of attention and activity on the EU level

as well as on the Member States level with a goal to secure a certain level of protection to consumers as a weaker party in B2C contracts and to ensure access to simple, efficient, fast and low-cost out-of-court resolution of disputes between consumers and traders. With litigation taking in some Member States several years on average, bringing uncertainty to B2C contracts, it is definitely desirable to create an alternative improving functioning of the retail internal market and enhance redress for consumers. According to various conducted studies at that time, a substantial portion of European consumers encounter problems when buying goods and services in the internal market. Unfortunately, despite the best efforts, the previous attempts to create an effective consumer dispute resolution ("CDR") network were unsuccessful and patchy. The main identified shortcomings were gaps in the coverage, the lack of consumer and business awareness as well as the uneven quality of alternative dispute resolution ("ADR") procedures. Should CDR become a successful tool, it would need to ensure quality and maintain high standards of independence, transparency, legal expertise and fair-decision making in every single Member State.

The purpose of this article is to examine the development of law in respect to resolution of the consumer disputes firstly on EU level and then, specifically review the new legislation in the Slovak Republic with aim to provide the reader overview of the legislation as well as insights in respect to specific implementation questions relevant for the Act No 335/2014 Coll., Consumer Abitration Act ("Consumer Arbitration Act").[1]

2 Arbitration in the EU Law in General

Arbitration rules (e.g. arbitrability, arbitration proceedings, recognition and enforcement of arbitral awards) are not contained in any binding source of the EU nor do they have any explicit legal basis in EU primary law.

It is a matter of fact that the original version of the Treaty on Establishing of the European Economic Community ("TEEC") as of January 1, 1958 contained in Article 220 provisions according to which:

1 SLOVAK REPUBLIC. Act No. 335/2014 Coll., Consumer Arbitration Act.

"*Member States shall, so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals:*

- *the protection of persons and the enjoyment and protection of rights under the same conditions as those accorded by each State to its own nationals;*
- *the abolition of double taxation within the Community;*
- *the mutual recognition of companies or firms within the meaning of the second paragraph of Article 48, the retention of legal personality in the event of transfer of their seat from one country to another, and the possibility of mergers between companies or firms governed by the laws of different countries;*
- *the simplification of formalities governing the reciprocal recognition and enforcement of judgments of courts or tribunals and of arbitration awards.*"

The original wording of the TEEC thus established the possibility ("so far as is necessary") for the Member States to conclude among themselves a specific international agreement, which should have regulated rules "governing the mutual recognition and enforcement of arbitral awards".

The abovementioned mandate of the Member States was never exercised because on June 10, 1958 (i.e., 6 months after the formation of the EEC) was entered into the New York Convention[2] which was subsequently executed and ratified by all six founding Member States. This was also the reason why there was no further need to adopt similar legislation on EEC level.[3] This position of the Member States was also maintained during accessions of further Member States and was, at the end, confirmed by conclusion of the Treaty of Lisbon, which omitted Article 220 of TEEC, renumbered by the Amsterdam Treaty as Article 293. The current legal basis provided for in Article 81 of the Treaty on Functioning of the European Union[4] ("TFEU") does not allow adoption of legal acts of the EU on the recognition and enforcement of arbitral awards, but only judicial and extrajudicial decisions (e.g., public deeds, notarial deeds).

2 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXII_1_e.pdf ("New York Convention").

3 Parties to the New York Convention are currently all 28 EU Member States.

4 Treaty on Functioning of the European Union. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:12012E/TXT.

The current wording of primary EU law does not contain the power to adopt binding (mainly secondary) source of EU law in area of jurisdiction or the recognition and enforcement of arbitral awards. Furthermore, under paragraph 12(3) Preamble to Regulation (EU) No. 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters ("Brussels I recast")[5] the New York Convention takes precedence over this regulation.

The primary EU law does not contain express powers of the EU to adopt binding EU legal acts not only in the area of the recognition and enforcement of arbitral awards, but also in areas of other (basic) procedural aspects of arbitration proceedings.

Despite abovementioned, the supervision in respect to the arbitration proceedings is exercised primarily on the basis of powers established under Arts. 4(2)(f) and 169 TFEU[6] within the limits of Art. 12 TFEU (*"Consumer protection requirements shall be taken into account in defining and implementing other Union policies and activities."*) mainly through binding secondary legislation (regulations, directives, decisions), but also non-binding (recommendations, opinions, white papers, green papers etc.). The specific legal basis for adoption of the secondary law in areas of consumer protection is Art. 169 TFEU (as part of Title XV "Consumer Protection" of the Part Three "Union Policies and Internal Actions" of TFEU), which reads as follows:

"1. In order to promote the interests of consumers and to ensure a high level of consumer protection, the Union shall contribute to protecting the health, safety and economic interests of consumers, as well as to promoting their right to information, education and to organise themselves in order to safeguard their interests.

2. The Union shall contribute to the attainment of the objectives referred to in paragraph 1 through:

2.1 measures adopted pursuant to Article 114 in the context of the completion of the internal market;

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5 Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/CS/TXT/PDF/?uri=CELEX:32000L0031 & rid=1

6 See BĚLOHLÁVEK, Alexander J. *Ochrana spotřebitelů v rozhodčím řízení*. Praha: C.H. Beck, 2012. p. 79.

2.2 measures which support, supplement and monitor the policy pursued by the Member States.

3. The European Parliament and the Council, acting in accordance with the ordinary legislative procedure and after consulting the Economic and Social Committee, shall adopt the measures referred to in paragraph 2(b).

4. Measures adopted pursuant to paragraph 3 shall not prevent any Member State from maintaining or introducing more stringent protective measures. Such measures must be compatible with the Treaties. The Commission shall be notified of them."

In addition, it is possible, either independently, or together with provisions on consumer protection, to apply a relating legal basis contained in Art. 114 TFEU (Approximation of Laws).[7] Such legal basis was recently used for creation of two mechanisms of out-of-court consumer dispute resolution, specifically, for adoption of:

- Regulation (EU) No 524/2013 of the European Parliament and of the Council of 21 May 2013 on online dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC Regulation on consumer ODR)[8] ("ODR Regulation"),
- Directive 2013/11/EU of the European Parliament and of the Council of 21 May 2013 on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC (Directive on consumer ADR)[9] ("CDR Directive").

7 Under Article 114 TFEU, the European Parliament and the Council shall, acting in accordance with the ordinary legislative procedure and after consulting the Economic and Social Committee, adopt the measures (i.e. regulations, directives or decisions) for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market, save where the Treaty on European Union or Treaty on Functioning of the European Union do not contain (special) legal basis (for details see SVOBODA, Pavel *Úvod do evropského práva*. 4th ed. Praha: C.H. Beck, 2011. p. 111 - 116).

8 Regulation (EU) No 524/2013 of the European Parliament and of the Council of 21 May 2013 on online dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC (Regulation on consumer ODR). In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013R0524 & rid=1 ("ODR Regulation").

9 Directive 2013/11/EU of the European Parliament and of the Council of 21 May 2013 on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC (Directive on consumer ADR). In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013L0011 & rid=1 ("CDR Directive").

In EU primary law, there is a specific provision included also in the Art. 38 Charter of Fundamental Rights of the European Union,[10] which provides that the Union policies shall ensure a high level of consumer protection. Explanatory notes[11] to Art. 38 provide that *"the principles contained in this Article are based on Article 169 of the Treaty on Functioning of the European Union."*

3 Significance of the Directive 93/13/EEC on Unfair Terms in Consumer Contracts

A significant impact on the possibility to decide consumer disputes in arbitration proceedings have provisions of the Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts[12] ("Directive 93/13/EEC") and the related case law of the European Court of Justice, which interprets the relevant provisions of the directive.

The basic goal of the Directive 93/13/EEC is for the Member States to "*ensure that unfair terms are not used in contracts concluded with consumers by a seller or supplier and that if, nevertheless, such terms are so used, they will not bind the consumer, and the contract will continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair provisions*" (paragraph 25 Preamble to the Directive 93/13/EEC). This means that in the definition of "unfair terms", the directive specifies the obligations on Member States to provide in their national legislation that unfair terms used in a contract concluded with a consumer by seller or supplier under their national law shall not be binding on the consumer and that the contract shall continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair terms (see Art. 6(1) Directive 93/13/EEC).

10 Charter of Fundamental Rights of the European Union. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:12012P/TXT

11 Under Article 52(7) Charter of Fundamental Rights of the European Union: *"The explanations drawn up as a way of providing guidance in the interpretation of this Charter shall be given due regard by the courts of the Union and of the Member States."*

12 Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts. In *EUR-lex*. Available from: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31993L0013 & rid=2 ("Directive 93/13/EEC").

For the purposes of the Directive 93/13/EEC "unfair terms" mean contractual terms defined in Art. 3 (see Art. 2 letter a)). Unfair terms are as provided in provisions of Art. 3:

- a contractual term which has not been individually negotiated (i.e. it was drafted in advance and the consumer has therefore not been able to influence the substance of contractual term,[13] particularly in the context of a pre-formulated standard contract[14]) and, at the same time;
- contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer.

The definition of "unfair terms" in the Directive 93/13/EEC is general in its nature, particularly in relation to term "causes a significant imbalance in the parties' rights and obligations arising under the contract". Therefore, the Directive 93/13/EEC further specifies criteria in Art. 4(1) for assessing the aspect of unfairness providing that: *"the unfairness of a contractual term shall be assessed, taking into account the nature of the goods or services for which the contract was concluded and by referring, at the time of conclusion of the contract, to all the circumstances attending the conclusion of the contract and to all the other terms of the contract or of another contract on which it is dependent."*

This definition can be complemented with an authentic interpretation provided in paragraph 20 Preamble to the Directive 93/13/EEC, according to which in the evaluation of unfair contract terms, it is necessary to take into account:

"1. overall evaluation of the different interests involved [consumer and seller or supplier];

2. requirement of good faith,[15] *when making an assessment of good faith, the following shall be taken into account:*

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13 Under Art. 3(2) Directive 93/13/EEC: *"Where any seller or supplier claims that a standard term has been individually negotiated, the burden of proof in this respect shall be incumbent on him."*

14 Under Art. 3(2) Directive 93/13/EEC: *"The fact that certain aspects of a term or one specific term have been individually negotiated shall not exclude the application of this Article to the rest of a contract if an overall assessment of the contract indicates that it is nevertheless a pre-formulated standard contract."*

15 The Slovak wording of this provision does not reflect, for example, French or English wording of the Directive 93/13(EEC (use of term „dobrá viera" instead of word „dôvera" in Slovak wording). An incorrect translation is confirmed in judgment of the Court of Justice of 14 March 2013. Mohamed Aziz vs. Caixa d'Estalvis de Catalunya, Tarragona i Manresa (Catalunyacaixa). Case C-415/11 ("Case C-415/11").

2.1 strength of the bargaining positions of the parties, whether the consumer had an inducement to agree to the term and whether the goods or services were sold or supplied to the special order of the consumer;

2.2 the requirement of good faith may be satisfied by the seller or supplier where he deals fairly and equitably with the other party whose legitimate interests he has to take into account."

An assessment of unfair terms under several provisions of the Directive 93/13/EEC cannot be carried out in relation to all (any) provisions of consumer contract. The Directive 93/13/EEC lays down in this respect two exceptions, which without any further condition and with immediate effect (automatically) cause an exclusion from the scope of application of the directive:

- the contractual terms which reflect mandatory statutory or regulatory provisions and the provisions or principles of international conventions to which the Member States or the EU are party, particularly in the transport area, shall not be subject to the provisions of the directive (Art. 1(2));
- assessment of the unfair nature of the terms does not relate neither to the definition of the main subject matter of the contract nor to the adequacy of the price and remuneration, on the one hand, as against the services or goods supplies in exchange, on the other, in so far as these terms are in plain intelligible language (Art. 1(2)).[16]

As an additional exception, which, on the other hand, does not cause immediate exclusion from the scope of application of the Directive 93/13/EEC, includes the terms in consumer disputes which has been individually negotiated (i.e., and contrary, provisions of Art. 3(2) were included subsequently and the consumer has therefore been able to influence the substance of the term, or acceptance of this condition was not subject to the consent of different/other terms of the contract).

Under Art. 3(2) Directive 93/13/EEC: "*Where any seller or supplier claims that a standard term has been individually negotiated, the burden of proof in this respect shall*

16 Slovak wording does not reflect accurately for example French, English or Czech wording of the Directive 93/13/EEC in respect to "adequacy of the price and remuneration" a "intelligible language" (compare, for example, Czech wording: "*Posouzení nepřiměřené povahy podmínek se netýká ani definice hlavního předmětu smlouvy, ani přiměřenosti ceny a odměny na straně jedné, ani služeb nebo zboží dodávaných výměnou na straně druhé, pokud jsou tyto podmínky sepsány jasným a srozumitelným jazykem.*")

be incumbent on him." and further, in addition it specifies that, "the fact that certain aspects of a term or one specific term have been individually negotiated shall not exclude the application of this Article to the rest of a contract if an overall assessment of the contract indicates that it is nevertheless a pre-formulated standard contract."

In respect to this specific exception, it can be concluded, that its application does not occur automatically, but only on the basis of an objection by seller or supplier (Art. 3(2) Directive 93/13/EEC) and other terms and conditions are not excluded from the scope of application of the directive (which applies also to both abovementioned conditions).

Art. 3(3) Directive 93/13/EEC further refers to the Annex attached to the directive containing an indicative and non-exhaustive list of the terms, which may be regarded as unfair. Under paragraph 21 Preamble to the Directive 93/13/EEC, "*the annexed list of terms can be of indicative value only and, because of the cause of the minimal character of the Directive, the scope of these terms may be the subject of amplification or more restrictive editing by the Member States in their national laws*".

Under the findings of the Court of Justice in the judgment of 14 March 2013, Mohamed Aziz vs. Caixa d'Estalvis de Catalunya, Tarragona i Manresa (Catalunyacaixa), case C-415/11 ("Case C-415/11"),[17] Art. 3(3) Directive 93/13/EEC shall be interpreted as meaning that the annex referred to in this provision contains only indicative and non-exhaustive list of the terms, which may be regarded as unfair.[18] Based on the content of that Annex, it cannot be automatically established that the disputed contract term is unfair in its nature. Nevertheless, it constitutes an essential element on which the relevant court may base its assessment of the unfair nature of such contractual term (see para. 26 of the judgment of the Court of Justice of 26 April 2012, Nemzeti Fogyasztóvédelmi Hatóság vs. Invitel Távközlési Zrt, case C-472/10[19]).

17 Case C-415/11.

18 Case C-415/11; Judgment of the Court of Justice of 4 June 2009. Pannon GSM Zrt vs. Erzsébet Sustikné Győrfi. Case C-243/08, paras 37 – 38; Order of the Court of Justice of 16 November 2010, Pohotovost', s. r. o. vs. Iveta Korčkovská. Case C-76/10, paras 56 and 58.

19 Judgment of the Court of Justice of 26 April 2012. Nemzeti Fogyasztóvédelmi Hatóság vs. Invitel Távközlési Zrt. Case C-472/10.

The condition provided in the Directive does not necessarily cause for the unfairness of the contract terms, and contrary, not always and under every circumstances can be any condition regarded as fair on the basis that it is not included in the Annex. The list of terms provided in the Annex to the Directive 93/13/EEC allows for a high degree of probability on the basis of long-term monitoring. It is clear from all language mutations of the provisions of Directive 93/13/EEC that it shows only examples, i.e. indicative tools, and not binding provisions.[20]

It can also be noted that under the case law of the Court of Justice, the list of unfair terms provided in Annex to the Directive 93/13/EEC does not have to be transposed into national legislation due to the fact that it does not confer additional rights to individuals to the rights resulting from provisions of Arts. 3 and 7 Directive 93/13/EEC, i.e. the Annex has only informative and demonstrative nature, constitutes a source of information for national authorities responsible for application of transposed provisions and for individuals affected by those measures.[21]

In respect to possibility of including a separate arbitration agreement or arbitration clause in the consumer contract as a method of deciding consumer disputes within the scope of Annex to the Directive 93/13/EEC it must be noted that:

- Letter i) of the Annex under which as unfair terms can be considered those terms of contracts which have the object or effect of "*irrevocably binding the consumer to terms with which he had no real opportunity of becoming acquainted before the conclusion of the contract*" and, particularly,
- letter q) of the Annex under which as unfair terms can be considered terms which have the object or effect of "*excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract.*"

20 See BĚLOHLÁVEK, Alexander J. *Ochrana spotřebitelů v rozhodčím řízení*. Praha: C.H. Beck, 2012. p. 82 – 83.

21 See Judgment of the Court of Justice of 7 May 2002. Commission of the European Communities vs. Kingdom of Sweden. Case C-478/99, paras. 21 - 23.

Ad 1)

This condition does not preclude the inclusion of such a contractual term that prescribes dispute resolution in form of an arbitration proceedings, which irrevocably obliges the consumer to participate in arbitration despite inability to get familiar with them before the conclusion of the contract (an example is the reference to the general terms and conditions which are not readily available to consumer or are not properly disclosed in any manner).

Ad 2)

In particular, it should be noted that the said provision of the Slovak translation of Directive 93/13/EEC is incorrectly translated as "*vyžadovat' od spotrebiteľa, aby riešil spory neupravené právnymi ustanoveniami výhradne arbitrážou*" (meaning: requiring the consumer to take disputes not covered by legal provisions exclusively to arbitration). We would like to point to other language mutations of the directive in this respect:

English wording:

"*excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions*" […];

French wording:

"*de supprimer ou d'entraver l'exercice d'actions en justice ou des voies de recours par le consommateur, notamment en obligeant le consommateur à saisir exclusivement une juridiction d'arbitrage non couverte par des dispositions légales*" […];

German wording:

"*dem Verbraucher die Möglichkeit, Rechtsbehelfe bei Gericht einzulegen oder sonstige Beschwerdemittel zu ergreifen, genommen oder erschwert wird, und zwar insbesondere dadurch, daß er ausschließlich auf ein nicht unter die rechtlichen Bestimmungen fallenden Schiedsgerichtsverfahren verwiesen wird*" […].

As correct wording (translation) can be considered also Czech version of letter q) subs. 1 of Annex to the Directive 93/13/EEC:

"*zbavení spotřebitele práva podat žalobu nebo použít jiný opravný prostředek, zejména požadovat na spotřebiteli, aby předkládal spory výlučně rozhodčímu soudu, na který se nevztahují ustanovení právních předpisů*" […].

It is clear from the above language versions of letter q) subs. 1 of Annex 1 to the Directive 93/13/EEC that the attribute "*not covered by legal provisions*" refers to arbitration. This means that a consumer contract shall not require a consumer to settle any disputes by some special type of arbitration, which is not regulated by legal provisions and where judges are probably not required to apply relevant substantive law.[22] In respect to the abovementioned erroneous translation of letter q) of the Annex to the Directive 93/13/EEC in Slovak version of Official Journal of EU we include also the relevant case law of the Court of Justice, which held that to satisfy the requirement of uniform application and uniform interpretation of the EU law, it is necessary to examine the wording of EU legislation in all of its official languages and take into consideration actual intentions of the legislator and the objective of the legislation itself.[23] If the interpretation of a provision of EU law in various language versions is different, it must be interpreted according to the general scope and objective of the legislation, of which it forms a part.[24] In this context of Cour of Justice's decisions, the Slovak general courts is obliged to apply letter q) sec. 1 of Annex to the Directive 93/13/EEC having regard to the wording in other language versions.

In order to determine whether the beforementioned provisions of Directive 93/13/EEC prohibits deciding of consumer disputes in arbitration, the case law of the Court of Justice should also be mentioned, particularly in respect to interpretation of the relevant provisions directly concerned and/or in different context relating to issues of arbitration of consumer disputes. Court of Justice has issued several judgements and reasoned orders without precise and clear statement, that deciding of consumer disputes

22 Besides this argument we can provide also provisions of Sec. 31(3) SLOVAK REPUBLIC. Act No. 244/2002 Coll., Arbitration Act ("Arbitration Act") valid for consumer disputes until 31. 12. 2014: "*An arbitration tribunal shall apply, in same manner as courts, the generally binding legal regulations in respect to consumer protection.*"

23 Judgment of the Court of Justice of 1 April 2004. Privat-Molkerei Borgmann GmbH & Co. KG vs. Hauptzollamt Dortmund. Case C-1/02, para. 25; Judgment of the Court of Justice of 6 October 1982. Srl CILFIT and Lanificio di Gavardo SpA vs. Ministry of Health. Case 283/81, para. 18.

24 See e.g. Judgment of the Court of Justice of 3 Apirl 2008. Criminal proceedings against Dirk Endendijk. Case C-187/07, para. 22 - 24 and Judgment of the Court of Justice of 19 April 2007. UAB Profisa vs. Muitinės departamentas prie Lietuvos Respublikos finansų ministerijos. Case C-63/06, para 13 and 14.

in arbitration is prohibited. Slovak courts have misinterpreted for example judgment of the Court of Justice of 26 October 2006, Elisa María Mostaza Claro vs. Centro Móvil Milenium SL, case C-168/05 ("Case C-168/05"),[25] stating that the Court of Justice has ruled out that the arbitration clause is always unfair condition within B2C contracts.[26] Within "*Preliminary observations"* of the Court of Justice (paras. 21 to 23) there is clear, that: *"It is apparent from the documents sent to the Court by the Audiencia Provincial that the latter has established that the arbitration clause contained in the contract concluded between Móvil and Ms Mostaza Claro was unfair. In that respect, it must be recalled that the Court may not rule on the application of general criteria used by the Community legislature in order to define the concept of unfair term to a particular term, which must be considered in the light of the particular circumstances of the case in question (Case C-237/02 Freiburger Kommunalbauten [2004] ECR I-3403, paragraph 22)*." Some Member States (esp. Czech Republic, Latvia and the Netherlands) act on the provision that unfair clauses are binding unless the consumer invokes unfairness. This legal consequence contradicts the requirements of the Court of Justice, which explicitly emphasised, that unfairness is to be determined on the court's own motion.

4 Progressive Building of Consumer Dispute Resolution Bodies Network

As a further step in improving consumers' rights in respect to resolution of disputes involving consumers, two pieces of legislation were passed in 2013 with an ambitious goal to build by 2015 a comprehensive network of consumer alternative dispute resolution bodies - ODR Regulation and CDR Directive.

The ODR Regulation obliges the European Commission to build an online platform to facilitate communication between the parties and a certified ADR provider, in the event of a contractual dispute arising from an online transaction. It should be noted, that this platform shall not seek to resolve

25 Judgment of the Court of Justice of 26 October 2006. Elisa María Mostaza Claro vs. Centro Móvil Milenium SL. Case C-168/05 ("Case C-168/05").

26 See e.g. Decision of District Court Topolcany, Slovak Republic of 5 September 2012, No. 11Er/192/2006-90 or Decision of Regional Court Banska Bystrica, Slovak Republic of 11 July 2012, No. 41 CoE/147/2012.

the disputes itself, but rather channel the disputes to a relevant ADR scheme and make available an electronic case management system tool for ADR providers. The platform shall be operational by January 2016.

The CDR Directive requires creation of CDR system in each Member State to cover all disputes initiated by an EU consumer against any trader in its territory relating to online and offline sales and services contracts, domestic as well as cross-border. The focus is put on the entities conducting the ADR and quality of the decision making-process. The main goal is to improve the internal market by encouraging cross-border trade while ensuring EU-wide access by consumers in every Member State to ADR entities which, in combination, comprehensively cover all business sectors in every territory, and which comply with a number of quality criteria. Such qualified ADR entities will then be listed by competent authorities within each Member State, and by the Commission. Inclusion in the list will therefore be a guarantee to a consumer anywhere in the EU that the ADR entity has the requisite characteristics to ensure an independent, impartial, transparent, effective, fast and fair resolution of the dispute in question.

It is important to note, that despite promoting ADR, the system is built on voluntary basis and according to Art. 1 CDR Directive does not prevent the parties from exercising their right of access to the judicial system of Member States. As mentioned above, under Art. 1 CDR Directive, it applies to sales contracts or service contracts between a trader established in the EU and a consumer resident in the EU. Excluded from the scope of the CDR Directive, under Art. 2 are B2B disputes, disputes initiated by a business against a customer, disputes regarding health services provided by health services professionals to patients and disputes regarding public providers of further or higher education. To summarize the requirements into few sentences, the CDR Directive requires Member States to facilitate access by consumers to ADR procedures on their respective territories allowing to submit the dispute covered in the CDR Directive to an "ADR entity" which is under Art. 4(1)(h) defined broadly as an entity, however named or referred to which is established on a durable basis and offers the resolution of a dispute through and ADR procedure and that is listed by a competent authority upon assessment of quality requirements for these entities set

out in the CDR Directive. Such a broad definition of an ADR entity offers various possible solutions for implementation by Member States. It further sets out requirements on natural persons who are in charge of ADR processes and rules ensuring transparency of ADR processes through ensuring that ADR entities make publicly available (on their websites, on a durable medium upon request, and by any other means they consider appropriate) information relevant to the ADR processes.

In respect to effectiveness, as consumers are very sensitive group in respect to costs of proceedings, it is required that the ADR procedure is free of charge or available at a nominal fee without consumer being obliged to retain a lawyer or legal advisor. Strong arguments were made for dropping any charge for consumers, *"the historical rationale for imposing a charge on both parties to arbitration may no longer apply in relation to contemporary ideas on encouraging consumers to raise problems with low values, especially if ill-founded claims are weeded out at an initial triage stage. A counterargument might be that requiring a modest change in some types of case is a rational barrier that assists some consumers to reduce inflated demands to reasonable levels."*[27] In relation to funding of CDR, there were calls made for business support of CDR funding and in some Member States it is believed that costs of CDR shall be borne by Member States as a matter of social policy.

Furthermore, the CDR Directive sets forth the framework for ensuring fairness, liberty (in the sense that an agreement between a consumer and a trader to submit complaints to an ADR entity is not binding on the consumer if it was concluded before the dispute has materialised and if it has the effect of depriving the consumer of his right to bring an action before the courts for the settlement of the dispute) and provision of information to overcome what has been called an "information barrier" that consumers had to face as in many Member States they simply were not aware of their respective rights.

The CDR Directive aims also to ensure designing an effective control of the whole CDR system as well as ADR entities and conducting of dispute resolution by a duty of designating a competent authority that shall carry out these controlling functions.

27 HODGES, Christopher; CREUTZFELDT, Naomi. *Implementing the EU Consumer ADR Directive* [online]. [cit. 2015-05-04], p. 4.

Under Art. 25(1) CDR Directive, the Member States shall comply with CDR Directive and implement the respective provisions by 9 July 2015. This is considered by some Member States, with not as highly developed system of CDR, as quite challenging deadline. The uncertainty grows also in respect to interpretation of certain standards set out in the CDR Directive, for example, what are the indicators for "quality of ADR entity" – is it only institutional capacity and natural persons with high expertise? What should be the dimensions of expertise, independence and impartiality? Another issue stems from lack of use of online CDR in particular in Eastern Europe. The imposition of a single point of entry for the out-of-court resolution of online disputes, through ADR entities which are linked to the platform will require data arrangements so that case information can be transferred from the platform to a specific provider.

Another important question is the balance between rights of consumers and need for their protection and potential misuse of the rights of consumers for their own benefit. As *Bělohlávek* noted in his work: "… *consumers have grown accustomed to the practice of exercising their right to rescind (cancel) the contract by statutory deadline while, in the meantime, they actively used the goods and the reby fulfil the purpose of the purchase. Besides, even a consumer ought to be required to exhibit a reasonable and usual degree of responsibility for his or her legal (juridical) acts, including the conclusion of contracts and assumption of obligations.*"[28]

Currently, there are over 750 ADR schemes in the EU. They work differently in each Member State, having also different names, such as arbitration, mediation, ombudsmen and complaints boards.[29] One feature that is common to all ADR schemes in Member States is to ensure for consumers faster access to a redress. The good news definitely is that on average, the ADR complaints were handled within three months of their lodgement.[30]

28 BĚLOHLÁVEK, Alexander: Arbitrability Limitation in Consumer (B2C) Disputes?: Consumers' Protection as Legal and Economic Phenomenon. *Risk Governance & Control: Financial Markets & Institutions.* 2011, Vol. 1, No 3.

29 *Alternative and Online Distpute Resolution (ADR/ODR)* [online]. European Commission [cit. 2015-10-19].

30 *Swiss Re/CMS Research Programme on Civil Justice Systems* [online]. Third Oxford Consumer ADR Conference, Consumer Dispute Resolution – Implementing the Directive [cit. 2015-05-04], p. 6.

5 CDR in the Slovak Republic - Consumer Arbitration Act

After, in Slovak conditions, a long legislative process of 2 years, came into effect on 1 January 2015, a substantial change to Slovakia's arbitration system which separated consumer arbitration from the "general" commercial arbitration and created a dispute resolution system that is, according to the Explanatory notes to the new Consumer Arbitration Act, a system of dispute resolution "very similar" to arbitration proceedings which creates grounds for institutional guarantees of fair and impartial decisions of the consumer matters by creating very strict borderlines to arbitration in this sensitive and much discussed area of the law.

First obvious goal of this new legislation was an implementation of the CDR Directive. Second goal was to address current, not very flattering, state of the matters, because in recent years arbitration was considered and seen by public in a very negative context due to exponential increase of bad experiences with decision-making of arbitral tribunal in consumer matters. General view in respect to consumer matters and arbitration proceedings was that although arbitration proceedings existed in Slovak legislation and could be used in consumer matters the previous scheme which was the same for consumer matters as well as commercial matters granted insufficient protection to consumers as weaker parties.

There were numerous issues with the arbitration proceedings in respect to consumers interlinked to each other that needed to be addressed in the new piece of legislation. First issue was Sec. 12(1) Arbitration Act. Under this provision, any legal entity may set up and maintain an arbitration court on its own cost and under conditions provided by the Arbitration Act. Indeed, in recent years, the Slovak Republic has seen mushrooming of the arbitration courts in the Slovak Republic, most of them focusing on CDR. As of today, there are 160 registered arbitration courts in the Slovak Republic out of which only couple of them are inactive.[31] Some academics and also public claimed that situation with arbitration courts got out of hands. For example, *Kubíček* noted: *"Practice proved concerns about potential abuse of the arbitration courts and their malpractice towards those who agreed that*

31 *Zoznam stálých rozhodcovských súdov* [online]. Ministerstvo spravedlivosti Slovenskej republiky [cit. 2015-10-19].

their future dispute will be decided by these newly established arbitration courts."[32] One of the reasons why consumer arbitration has become such a prolific area was the fact that litigation proceedings in the Slovak Republic, even in very simple cases, tend to take several years. Another reason for the malpractice is the increased availability of consumer credit from non-banking institutions, as consumer credit provided by banks has become less available to low-income groups of public after global financial crisis.

The issue was clearly visible in enforcement proceedings where courts often denied enforcement of judgments rendered in the arbitration against consumers by not granting a mandate to the court executor due to various reasons, most of them lying in a gross disproportion between rights and obligations of the consumer and the business, denying consumers' right of access to the state courts, unacceptable place of arbitration or inclusion of arbitration agreement in general terms and conditions of contracts where consumers could not affect the content of such terms and conditions or where they created part of so called formulary contract. In all of these cases the courts concluded that the arbitration agreement has not been agreed in valid manner and therefore a decision of an arbitral tribunal is not enforceable. As a result, courts denied enforcement for thousands of these decisions rendered in consumer arbitration.

As can be seen from examples above, the Slovak Republic stood in front of a very difficult task to address these issues and create a reliable consumer arbitration mechanism. The Consumer Arbitration Act as it stands is fully compliant with the CDR Directive and implements it without significant deviations and adapting the requirements to Slovak conditions. In this regard, *Chovancová* pointed out, while comparing consumer arbitration framework in various European jurisdiction that a thorough legal regulation of the arbitration with consumers proved to be significant for their protection. On the other hand, she also stressed that it needs to be kept in mind that protection of consumers has also its limits and cannot be regarded

32 KUBÍČEK, Pavol. Stále rozhodcovské súdy a príprava novej právnej úpravy rozhodcovského konania. In SUCHOŹA, Jozef; HUSÁR, Ján (ed.). *Právo, Obchod, Ekonomika IV., Zborník vedeckých prác*. Košice: UPJŠ Košice, 2014, p. 542

as protection against frivolousness and recklessness.[33] During the consultation period, the Consumer Arbitration Act has been subjected to criticism. For example, the former Minister of Justice, *Žitňanská* stated that *"the effect of the new legislation would be minimal and the costs of the implementation would be unnecessarily high."*[34] Others criticized the separation from the Arbitration Act as unnecessary step that is not required by the CDR Directive and as an alternative suggested conducting CDR by courts rather than arbitration courts.

Below is a short overview of CDR under the Consumer Arbitration Act. The scope of the Consumer Arbitration Act, set forth in Sec. 1 is expressed differently comparing to the CDR Directive. It provides that the Consumer Arbitration Act applies to consumer disputes regarding to which can be concluded an agreement on settlement under Sec. 585 Slovak Civil Code,[35] including the disputes on determination whether a right or legal relationship exists or not. Only consumer would have an urgent legal interest on the matter under the Consumer Arbitration Act. The Consumer Arbitration Act does not apply to disputes in relation to creation, change or termination of the ownership rights, disputes relating to personal status, disputes in connection with forced enforcement of the decision or those which arose in connection with bankruptcy proceedings or restructuring.

The place of arbitration can be only in the territory of the Slovak Republic. The Arbitration Act remains governing the recognition and enforcement of arbitral decisions.

The Consumer Arbitration Act further contains a definition of consumer dispute – "a consumer dispute is a dispute arising from the consumer contract or in connection with the consumer contract". The Consumer Arbitration Act does not contain definitions of consumer or supplier as these terms are defined in the Slovak Civil Code.

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33 CHOVANCOVÁ, Katarína. Rozhodcovské doložky v spotrebiteľských zmluvách. In SUCHOŹA, Jozef; HUSÁR, Ján (ed.). *Právo, Obchod, Ekonomika IV., Zborník vedeckých prác*. Košice: UPJŠ Košice, 2014, p.506 – 520.

34 *Borecov návrh spotrebiteľov účinne neochráni, tvrdí Žitňanská* [online]. SME Ekonomika [cit. 2015-10-19].

35 SLOVAK REPUBLIC. Act No. 40/1964 Coll., Civil Code.

One of the major changes brought by the Consumer Arbitration Act are the changes in respect to formal requirement of conclusion of the arbitration contract. The essential elements of the consumer arbitration agreement are set forth in Sec. 3, the consumer arbitration agreement must be in writing, the content and form has to be separated from the remainder of the consumer contract and shall not include any ancillary arrangements that are not relevant to the consumer arbitration agreement. This new provision is in contrast with previous state, where up to December 2014 an agreement on arbitration could take form of an arbitration clause, which was directly incorporated into the contract, usually in general terms and conditions. The written form is maintained even if the agreement has been concluded by electronic means that allow capturing of the content and identification of the contracting parties who concluded the consumer arbitration agreement. The consumer arbitration agreement shall not contain an agreement on certain arbitrator. Last but not the least, the conclusion of the consumer agreement cannot be conditioned by conclusion of the consumer arbitration agreement.

As an important duty for the suppliers that had to be implemented in their business workflow is the provision of information to consumers, sample of which appears in the Annex to the Consumer Arbitration Act. This information sheet provides a consumer with a brief guide on how to proceed in case of a dispute listing, in particular, respective rights of the consumers.

A very important right granted to consumer by the Consumer Arbitration Act is to turn with the dispute, even though there is a valid arbitration agreement, to the Slovak courts. This is obviously not the case for commercial arbitration where conclusion of the arbitration agreement precludes the jurisdiction of the courts. As a result the businesses would have to deal with the option that despite validly concluded arbitration clause, the consumer can choose whether to lodge the action with the selected arbitration court or with general courts. This exemption however ceases to be available if the respective arbitration proceedings commenced at consumer arbitration tribunal, i.e. *lis pendens* rule.

The approach in respect to fees and costs is that CDR should be approachable to consumers. Therefore, an initiation of proceedings, any other related

submissions including submission of evidence are free of charge for consumers and the arbitration court might only require court fees from the party which is not a consumer. Any remuneration of the arbitration in CDR disputes is independent from the outcome of the proceedings. An action for annulment of the arbitral award can be lodged by filling out a sample form attached to the Consumer Arbitration Act within three months after delivery of the arbitral award. The time period of three months was also criticized as unnecessarily long comparing to time period for appeal, which is 15 days under Slovak Civil Procedure Code.[36]

Becoming an arbitrator or to set up a arbitration court was not difficult before commencement of the Consumer Arbitration Act. Currently, the special permanent CDR arbitration courts set up under the Consumer Arbitration Act are under stricter supervision and have notification duties in compliance with CDR Directive as consumers and consumer disputes are a separate category. The arbitrators shall also meet stringent criteria that include university education in area of law, at least 5 years of legal experience and the professional examination before a commission appointed by the Minister of Justice. After successfully passing the examination they will be registered to the list of arbitrators eligible to decide consumer disputes.

At this stage, it is too early for evaluation of success rate of this new legislation. As of today, only one permanent CDR arbitration court has been registered with the Slovak Ministry of Justice[37] and the new procedure has not become fully operative. It has to be also noted that as part of second stage of implementation of ADR Directive, there is currently at consultative stage a new draft of legislation on alternative resolution of consumer disputes which draft was lodged for consultation on 12 March 2015. One of the objectives of the legislation draft is to even strengthen the position of consumers by offering to consumers other methods of dispute resolution in addition to arbitration proceedings.

36 SLOVAK REPUBLIC. Act No. 99/1963 Coll., Civil Procedure Code.

37 *Zoznam rozhodcovských súdov oprávnených rozhodovať spotrebiteľské spory* [online]. Ministerstvo spravedlivosti Slovenskej republiky [cit. 2015-10-19].

6 Conclusion

The implementation of CDR methods in Central and Eastern Europe proved to be challenging as historically these countries do not have such a CDR heritage to build upon as countries in Western Europe. As a result, when improving our CDR system, we can definitely repurpose what has been successful in other Member States.

A regular strengthening of consumer protection in EU legal system has become a standard, so the new Slovak legislation copying this trend certainly makes sense from the consumer perspective. The Slovak Consumer Arbitration Act creates new system of CDR which is separated from commercial arbitration and aims to create safeguards that should prevent misuse of arbitration by some entities (particularly non-banking institutions) and creates a separate network of permanent consumer arbitration courts with trained arbitrators that have to have a legal degree and certain experience in the area. When comparing the Slovak CDR system to other systems in Europe we can definitely see the lack of other dispute resolution methods such as mediation of consumer disputes or creation of specific CDR bodies such as ombudsmans for certain specific areas of disputes, however a draft of new legislation on resolution of consumer disputes shall address this shortcoming. Despite certain criticism, the new legislation is definitely a step forward. On the other hand, it is too early to see how successful the legislation would be in improving position of consumers. Questions remain whether in practice the Consumer Arbitration Act fulfils its purpose, since the very purpose of arbitration itself is its speed and simplicity. What is certain is that consumer rights in the arbitration proceedings have been considerably strengthened and should ensure that suppliers, when concluding the arbitration agreements, have to comply with all formalities required by law. Ultimately, the new legislation can contribute to fast and smooth decisions in respect to consumer disputes without the need for intervention by the state courts.

On the other hand, it has to be emphasized that nothing is only black or white and traders in the context of the Slovak Republic have to tackle their own challenges. Their position was described by *Bělohlávek* as *"sometimes the position of "hostages", who are not able to protect themselves due to some*

abuse of broad rights to consumers". It is therefore very important to find balance between rights and obligations of both parties despite need to protect the one which is weaker and prevent any frivolous and vexations claims feared by some business sectors.

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CONCLUDING REMARKS

THE END OF ARBITRATION IN BOHEMIA?

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1 Introduction

The title of this paper actually paraphrases the name of a Czech comedy. Just like in that film, it is a slight exaggeration: the possibility of resolving disputes through arbitration is not going to disappear in the Czech Republic. However, there are symptoms pointing to the existence of certain issues. They hinder and complicate the proceedings and the enforcement of the ensuing arbitral award to such an extent that, in a certain timeframe, they could impact the choice of arbitration as a way of resolving disputes.[1] These issues cannot be ignored. The article further deals with the question of whether the way arbitral proceedings are regulated in the Czech Republic is sufficient to meet the goals which form the rationale behind the existence of arbitral proceedings. This, in fact, is the same rationale why arbitral proceedings became a popular method of resolving disputes at a certain time in history. We will also share our thoughts on the desirability of a different regulation of certain other matters.

This paper aims to comment on these issues on the basis of our discussions, contributions and other observations. We provisionally divided the range of issues into several categories: "two in one – can consumer and

[1] To the history of the regulation in Czech Republic: BĚLOHLÁVEK, Alexander, J. *Zákon o rozhodčím řízení a o výkonu rozhodčích nálezů: Komentář*. 2nd ed. Praha: C. H. Beck, 2012; ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. 3rd ed. Praha: Wolters Kluwer, 2013; LISSE, Luděk et al. *Euronovela* zákona o rozhodčím řízení s judikaturou. Praha: Ústav práva a právní vědy, 2012; RŮŽIČKA, Květoslav. *Rozhodčí řízení před Rozhodčím soudem při Hospodářské komoře České republiky a Agrární komoře České republiky*. Plzeň: Vydavatelství a nakladatelství Aleš Čeněk, 2003; RABAN, Přemysl. *Alternativní řešení sporů, arbitráž a rozhodci v* České *a Slovenské republice a zahraničí*. Praha: C.H. Beck, 2004; DRLIČKOVÁ, Klára. *Vliv legis arbitri na uznání a výkon cizího rozhodčího nálezu*. Brno: Masarykova univerzita, 2013.

commercial arbitration be regulated by a single law?"; "overregulation – can legal regulation substitute for the lack of ethics?"; and "the reach of judicial review of arbitral proceedings."

2 Two in One – Can Consumer and Commercial Arbitration be Regulated by a Single Law?

The first category of issues concerns the combination of rules governing consumer and commercial arbitration in a single law. The legal regulation of individual types of arbitration has undergone an interesting development in the Czech Republic. Until 1994, arbitration was only allowed in disputes concerning international commercial relationships. There was a special regulation with regard to disputes among organisations from the COMECON countries. The law adopted in 1994 did not distinguish between the individual types of arbitral proceedings in terms of regulation. It applied to both domestic and international disputes. In domestic disputes, it did not distinguish between consumer disputes and disputes between entrepreneurs. The chief inspiration for the law was drawn especially from the UNCITRAL Model Law.[2] Given the fact that until then, the Czech Republic had only had an experience with international commercial arbitration, the law accentuated solutions and principles fully corresponding to resolution of disputes between entrepreneurs. It did not comprise any protective elements. Following several minor amendments to the law adopted in the following years, the most important amendment was eventually introduced in 2012 and concerned a regulation of consumer arbitration.[3]

This was motivated by the requirements of European Union law and also by the very circumstances in the Czech Republic, where the situation regarding consumer protection had become politically untenable. The newly

2 UNCITRAL Model Law on International Commercial Arbitration 1985 with amendments as adopted in 2006 [online]. *United Nations Commission on International Trade Law (UNCITRAL)*. Available from: http://www.uncitral.org/pdf/english/texts/arbitration/ml-arb/07-86998_Ebook.pdf.

3 BĚLOHLÁVEK, Alexander. J. *Ochrana spotřebitelů v rozhodčím řízení*. Praha: C. H. Beck, 2012; BĚLOHLÁVEK, Alexander, J. Rozhodčí řízení v tzv. smluvních vztazích spotřebitelského typu. *Právní fórum*. 2010, No. 3, p. 89; KYSELOVSKÁ, Tereza. Rozhodčí doložky (nejen) ve spotřebitelských smlouvách a ochrana lidských práv. In DÁVID, Radovan; NECKÁŘ Jan; SEHNÁLEK, David (eds.). *COFOLA 2009: The Conference Proceedings*. Brno: Masaryk University, 2009.

appearing arbitration centres and even the individual arbitrators often abused arbitral proceedings, which gave it a bad reputation, especially in connection with certain activities pursued by distrainers. A change in legislation became necessary.

The provisions concerning consumer arbitration were not embodied in a special law (as in e.g. Slovakia[4]). Although proposals were made in the relevant working group to separate consumer arbitration and introduce a new law incorporating both mediation and consumer arbitration, the Ministry responsible for the draft law rejected such a solution. The new provisions on consumer protection in arbitral proceedings were thus incorporated into the existing law (Act No. 216/1994 Coll.[5]). As already mentioned, the original law was firmly based on the principle of equality and granted both the arbitrators and the parties a relatively high degree of autonomy. Therefore, certain protective elements were incorporated in the individual stages of the proceedings. Of these, we should mention primarily the following: provisions concerning the so-called "pre-contracting stage"; a new form of the consumer arbitration agreement; a special regulation of the procedure in *ad hoc* arbitration; the duty to apply consumer protection rules; the adoption of a special reason for cancelling arbitral awards in consumer matters.

2.1 Pre-contracting Stage

Pursuant to Sec. 3(4), in respect of consumer arbitral proceedings, an entrepreneur must provide – sufficiently in advance prior to the conclusion of the arbitration clause – the consumer with proper advice, including the consequences of the arbitration clause, to enable the consumer to fully understand the implications of his or her acts. The form is not specified. Everyday practice eventually established the written form in order to ensure a written proof that the advice was given. Its specific effects in practice – except for the fact that the consumer mechanically signs another document together with documents such as the arbitration agreement and, as a matter of fact, the main agreement – are, however, doubtful.

4 SLOVAK REPUBLIC. Act No. 335/2014 Coll., on cosumer arbitration.

5 CZECH REPUBLIC. Act. No. 216/1994 Coll., on arbitration and on enforcement of arbitral awards.

2.2 Arbitration Agreement[6]

An arbitration agreement concerning consumer matters must newly be executed separately and in writing. Aside from the usual requirements, it also has to include the following in respect of *ad hoc* proceedings: the type of proceedings (*ad hoc* or institutionalised); the manner of initiation and the form of the proceedings; the fee and other costs of the arbitrator; the venue; the manner of serving the arbitral award; and advice on enforceability of the arbitral award (Sec. 3(5)). In proceedings held before permanent arbitration courts, a reference to their rules and regulations is sufficient (Sec. 3(6)).

2.3 Arbitrators

Only a person registered in the list of arbitrators kept by the Ministry of Justice can serve as an arbitrator in consumer disputes (Sec. 40(a) - (d)).

2.4 Procedural Rules in Ad Hoc Proceedings

Sec. 19, which provides for the regulation of proceedings (the will of the parties; the will of the arbitrators; the rules of a permanent arbitration court), was amended to the greatest degree. Sec. 19(4) now reads: *"The parties may specify the procedure also in the rules of the arbitral proceedings if the rules are attached to the arbitration agreement. This shall not affect the application of the permanent arbitration court's rules."* However, such a general provision, not limited to consumer arbitral proceedings, has one flaw: it affects all *ad hoc* proceedings, e.g. also proceedings held in the Czech Republic under the ICC Rules. Therefore, an arbitration agreement is not sufficient for arbitral proceedings within the Czech Republic. In order to apply the rules of the court, its rules must be attached to the agreement, which is a relatively unusual requirement for international arbitral proceedings.

6 KOHOUT, Martin. Obligatorní náležitosti rozhodčí smlouvy jako součásti spotřebitelských smluv, dnes již de lege lata. In LISSE, Luděk et al. *Euronovela* zákona o rozhodčím řízení s judikaturou. Praha: Ústav práva a právní vědy, 2012, p. 123 – 130; NOVÝ, Zdeněk. Nekalá rozhodčí doložka v českém právu. In KYNCL, Libor; SEHNÁLEK, David; DÁVID, Radovan; VALDHANS, Jiří (eds). *Days of Law*. Brno: Masarykova univerzita, 2009, p. 1797-1817.

2.5 Governing Law

Pursuant to Sec. 25(3), *"[i]n disputes arising from consumer agreements, the arbitrators shall always comply with the legal rules for consumer protection"*. The wording does not explicitly exclude a decision based on the principle of equity; nevertheless, this is the way this provision is usually interpreted.[7]

2.6 New Reasons for Cancellation of an Arbitral Award

New additions include review on the basis of failure to comply with protective regulations in the area of substantive laws and extension of the mandatory requisites of an arbitration agreement in case of consumer disputes, for example: the arbitrator or a permanent arbitration court resolved a consumer agreement dispute at variance with legal regulations concerning consumer protection or clearly at variance with good morals or public order; an arbitral agreement concerning consumer agreement disputes does not include the information set forth by Sec. 3(5), or the information is incomplete, inaccurate or untrue, either intentionally or to more than negligible extent. In cases where cancellation of an arbitral award is claimed in a consumer dispute, certain pleas need not be raised within the proceedings although this is otherwise required for enforcing the relevant ground for cancellation (Sec. 33).[8]

With regard to arbitration in consumer and in commercial matters, it must be stressed that, despite the procedural similarity, these proceedings are based on different principles. While in commercial arbitration, the parties are considered equal and a degree of professional understanding of the proceedings (which are only generally regulated by law) is expected, consumer arbitration is different. In consumer arbitration, the underlying principle rests in consumer protection. A thoughtless incorporation of elements of consumer protection into a law based on different principles brings about a number of problems, which have so far been evident. The most visible result of this has been a decrease in the number of arbitral proceedings in the Czech Republic.

7 HAVLÍČEK, Jan; HAVLÍČKOVÁ, Petra. Rozhodčí řízení a možnost rozhodování podle zásad spravedlnosti. *Právní a ekonomické problémy současnosti XII*. Ostrava: Key Publishing, 2010, XVII, p. 16-20.

8 See KYSELOVSKÁ, Tereza. *Institut zrušení rozhodčího nálezu z pohledu ochrany spotřebitele a judikatury Soudního dvora Evropské unie*. Brno: Masarykova univerzita, 2013, p. 98-102.

3 To Regulate, or to Regulate Even More?

The Czech legislation in the area of arbitral proceedings exhibits certain incoherence. On the one hand, legal regulation has been gradually strengthened. On the other hand, some issues that have long been a source of problems in practice remain unresolved. Alternatively, their interpretation, especially by the courts, suppresses the characteristic features of arbitral proceedings and automatically subjects them to the rules set forth by the Code of Civil Procedure.[9] Even the doctrinal starting points are different. There are mainly two relevant examples. First of them is the issue of challenging the existence or validity of the arbitration agreement in arbitral proceedings

Under Sec. 15, the arbitrators may determine their own competence. This does not pose a problem as the Czech legislation follows both the "competence-competence" principle and the autonomy of the arbitration agreement with respect to the main agreement. What is problematic in practice is that an application for cancellation of such resolution may only be lodged after the arbitral award is rendered. As a result, the whole proceedings are encumbered, from the outset, with a defect which may ultimately lead to a cancellation of the rendered arbitral award. Although the working group strongly recommended in 2012 to adopt a measure similar to the one set forth in Sec. 16(3) UNCITRAL Model Law, the Ministry did not accept the recommendation.

The second issue is the recognition and enforcement of foreign arbitral awards under national law. This issue is newly incorporated in Sec. 121 Private International Law Act.[10] Despite the fact that since late 1950 s, the Czech Republic has been a party to the New York Convention,[11] the potential recognition and enforcement under national law is significantly different. All the grounds are grounds applicable *ex officio* and their scope is quite significant. Aside from the usual grounds (variance with public policy, the award has not entered legal force or was cancelled setting aside), it also covers

9 CZECH REPUBLIC. Act No. 99/1963 Coll., Code of Civil Procedure.

10 CZECH REPUBLIC. Act No. 91/2012 Coll., on Private International Law.

11 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) [online]. *United Nations Commission on International Trade Law (UNCITRAL).* Available from: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention.html

the grounds for cancellation of a domestic arbitral award. Recognition and enforcement thus combines grounds usual for this process with grounds otherwise applied to achieve cancellation setting aside of the arbitral award. Considering the number of signatories of the New York Convention, the regulation is redundant and, under the conditions laid down in Sec. 121, inapplicable. Indeed, one can hardly imagine applicants for recognition and enforcement who would voluntarily subject themselves to such a complicated procedure bound by heavy State regulation.

There are many other reasons as well. One is the connection of Sec. 19 (the procedure of the arbitrators in the proceedings) with Sec. 30 (analogous application of the Code of Civil Procedure). This is a matter where there is no consensus between the arbitrators and the courts tend to decide differently. Ambiguities concerning the scope of the arbitrators' and parties' autonomy in the proceedings also are a cause for concern.

What are the conclusions? A constantly increasing legal regulation of arbitral proceedings cannot substitute for something which the proceedings have clearly began lacking after their broadening: an ethics-based perception of the whole procedure. This is a matter for further discussions. Legal regulations can be circumvented. If an ethical dimension is not present, the law can only punish certain specific acts. It cannot substitute for the lack of ethics.

4 General Courts, Constitutional Court and Arbitration Courts

The relationship between the courts and arbitration courts is a special issue, and recently the profile of the Constitutional Court of the Czech Republic in this matter has also been raised. Many who study arbitral proceedings have been left confounded by some of the Constitutional Court's decisions. The differences in opinion between the Supreme Court of the Czech Republic and the Constitutional Court are well-known. However, a relatively significant gap between the older and newer decisions of the Constitutional Court (after the appointment of new constitutional judges) has now opened up.

The differences concern a number of issues, including the very doctrinal basis of arbitral proceedings,[12] albeit the differences are not as obvious and explicit. On the one hand, there is the contractual doctrinal approach, which is reflected in a majority of the Constitutional Court's decisions. The opinion concerning the mixed nature of arbitral proceedings has so far been rather marginal.

However, the Constitutional Court has now come up with a fairly revolutionary notion of interference into the arbitrator's resolution. This applies not only to relationships between the parties, but also to relationships between the arbitrator (the arbitration court) and one of the parties. In other words, it applies to a relationship which is, from the point of view of the contractual doctrine, considered as clearly contractual. Even the mixed doctrine accentuates the contractual elements of the relationship, especially with regard to subjecting oneself to the rules and regulations. The interference thus means at least reinforcement of the supervisory powers of the courts in arbitral proceedings. This is true even though it goes directly against the contemporary wording of the Arbitration Act as well as doctrinal grounds.

Basically until 2014, the Constitutional Court rejected constitutional complaints in cases involving resolutions of arbitration courts. This included cases where the resolution was challenged through an application for cancellation and the general courts (including the Supreme Court) rejected the application on the grounds that only arbitral awards could be subject to cancellation. In 2014, the situation changed due to two judgements of the Constitutional Court.

4.1 Decision No. I.ÚS 1794/1013

In this case, arbitral proceedings were discontinued by a resolution, with a justification that the arbitrator lacked competence. Interestingly, the value in dispute was first determined in that the fee equalled seven thousand Czech crowns. Subsequently, following an oral hearing and clarification of the value in dispute, the arbitrator evaluated this value differently and increased the fee

12 ROZEHNALOVÁ, Naděžda. *Rozhodčí řízení v mezinárodním a vnitrostátním obchodním styku*. 3rd ed. Praha: Wolters Kluwer, 2013, p. 71-80.

13 Decision of the Ústavní soud České republiky of 16 July 2013, No. I.ÚS 1794/10.

to one million Czech crowns. Shortly thereafter he resolved to terminate the proceedings on the grounds of a lack of competence. The fee already paid (one million Czech crowns) was to be borne by the claimant. The general courts rejected the application for cancellation setting aside on the grounds that solely an arbitral award could be subject to cancellation; the same did not apply to a mere resolution. On the other hand, the Constitutional Court ruled to cancel the resolution. One of the arguments given in the reasoning was as follows: "The Constitutional Court notes that it could have decided the case differently if it involved the originally imposed fee of CZK 7,000. The principle of proportionality is a basic principle of the rule of law; it is not necessary to prove that an amount of CZK 1,000.000,- in contrast with the amount of CZK 7,000, is neither proportionate nor reasonable with respect to the circumstances of the case. In this case, quantity becomes a quality."

It is true that the arbitrator's actions were incomprehensible, yet the above judgement focuses more on the amount of the fee. It is hard to set aside doubt as to the qualitative difference of the problematic amount of fee.

4.2 Decision No. III.ÚS 2407/1314

The second case involves a challenge to the very relationship between a party and the arbitration court, specifically the wording of the arbitration court's rules in the part dealing with arbitration fees. Pursuant to the rules, 50 % of the fee may be returned if the claim is withdrawn before oral hearing is ordered. However, the oral hearing did not take place and the claim was subsequently withdrawn. Nevertheless, the claimant sought a refund of the fee, which was rejected with reference to the rules of the arbitration court. The general courts refused to cancel the resolution with reference to its character and the fact that the given case involved a relationship between the arbitration court and a party, not a relationship between two parties. The Constitutional Court reasoned differently. Specifically, it stated as follows: *"Decision-making concerning property disputes between parties to an arbitration agreement can be put outside the competence of general courts. General courts may interfere with these proceedings and review the resulting rulings only on the basis of a law, as a sign*

14 Decision of the Ústavní soud České republiky of 3 July 2014, No. III.ÚS 2407/13.

of the State's respect to the autonomy of will of the parties to arbitration agreements. A court review of a ruling of an arbitration court not affecting relationships between the parties to an arbitration agreement and their dispute, but rather a dispute between the claimant and the arbitration court itself, is generally permissible, although not anticipated by the law, because a mere standard law, let alone arbitration court rules, cannot exclude the effect of the fundamental right to court protection in relationships between two parties subject to private law, and similarly cannot divest the general court of its duty to provide such protection (see Art. 36(1) and Art.11(1) of the Charter of Fundamental Rights and Freedoms and Art. 4 of the Constitution of the Czech Republic)."

The above-mentioned judgements of the Constitutional Court were unexpected and, to some degree, even surprising with respect to the doctrine followed by the Constitutional Court in evaluation of arbitral proceedings – i.e. the contractual doctrine.

5 Conclusion

Resolving issues through arbitral proceedings offers many benefits. Nevertheless, the old saying about a "good servant but a bad master" applies here, too. Provided that a party is familiar with this type of proceedings and is aware of the problems that could arise during the proceedings or due to legal regulations, and provided that the party knows how to pre-empt certain risks, incorporating an arbitration clause in an agreement or contract may still represent an effective instrument for resolving potential disputes with business partners. This is true especially if a good arbitrator is available and it applies to both commercial and consumer arbitration concerning international as well as domestic disputes. However, the core of all problems with arbitrations lies, as always, in the person of the arbitrator. If this person's moral integrity is sound and he or she bases his/her decisions on ethical principles, it is not necessary to continuously strengthen legal regulation and repression in the area of arbitral proceedings.

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