Effect of Party Insolvency on Arbitration Proceedings: Pause for Thought in Testing Times

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1. INTRODUCTION

The recent global recession has seen a marked rise in the number of corporate insolvencies. In the United Kingdom, first quarter 2009 insolvencies saw an increase of 56 per cent on the same period a year earlier, while mid-year expectations were that KPMG’s prediction of 5,000 corporate insolvencies in 2009 would be met. This experience has been echoed in the United States where, for example, 52 banks failed in the first six months of the year followed by a further seven in one day in early July 2009.

For the third year in a row Fulbright and Jaworski’s Annual Litigation Trends Survey (2009) saw an increase in the number of respondent companies expecting more disputes over the following 12 months. Chief among the reasons given were the repercussions of the economic downturn.

Accordingly, with insolvencies on the rise and commercial disputes also expected to increase, many parties will find themselves contemplating claims against insolvent entities or in dispute with a party who becomes insolvent. In cross-border disputes, claimants will have the added hurdle of dealing with unfamiliar foreign insolvency legislation. Moreover, as arbitration arguably remains the favoured means of dispute resolution in international contracts, many such disputes will fall to be resolved in arbitration rather than litigation.

Recent high-profile decisions in the Swiss and English courts in the long-running battle between Elektrim SA and Vivendi serve to highlight the impact of one party’s insolvency on ongoing international arbitration proceedings and the complex issues which can arise. The opposing decisions reached in the English and Swiss courts highlight the need to give timely consideration to these issues. This article discusses the tension between the competing public policy interests of arbitration and national insolvency legislation and describes the mechanisms for dealing with that tension employed in different jurisdictions and in the context of international arbitration. Finally, a summary of the Elektrim Vivendi case is provided as a cautionary tale.

2. A CONFLICT OF NEAR POLAR EXTREMES

Arbitration and insolvency are not easy bedfellows. The essence of arbitration is its consensual nature (a “creature of contract” is the commonly-heard phrase). The right to

1 The authors thank Alan N. Resnick of Hofstra University School of Law and Fried, Frank, Harris, Shriver & Jacobson LLP for his helpful comments. An earlier version of this article was distributed at the CPR Institute 2010 Annual Meeting, January 14–15, 2010 in New York and on Transnational Dispute Management [Accessed March 17, 2001]).


3 “Second Wave of UK Corp Insolvencies Expected in Q3, Q4—KPMG” in Dow Jones Newswires, July 2, 2009.


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Arbitrate and the jurisdiction of the arbitral tribunal arise by agreement between the parties and the process is largely shaped by that agreement. The arbitration agreement determines who may be a party to a dispute, the curial law of the arbitration (usually by virtue of designating the seat of the arbitration) and the procedure to be followed. The parties will normally also agree in their contract the law governing the substance of their dispute. Moreover, the arbitral process is typically confidential and the resulting award has no binding effect upon third parties who were not privy to the arbitration agreement.

Arbitration depends on the parties’ intentions evidenced by their agreement and not on procedural rules of law.6 As the US Supreme Court has recognised, arbitration is a “trade-off” of the procedures and opportunity for review of the courtroom for the simplicity, informality, and expedition7 which arbitration allows. In contrast, insolvency proceedings seek to apportion the assets of an insolvent party among all of its unrelated creditors. Additionally, insolvency policy typically allows for the reorganisation and survival of undertakings and employments, considerations which have wider social, economic and political consequences.8

The objectives of most national insolvency schemes depend on the type of proceeding. The considerations differ in administration proceedings, where reorganisation and the survival of the subject company are sought, as opposed to liquidation proceedings. However, in either situation the overriding intent is to maximise the value of the insolvent’s estate by way of a centralised, transparent and efficient process.

The courts in the United States have recognised that US bankruptcy law was reformed:

“[T]o allow the bankruptcy court to centralise all disputes concerning all property of the debtor’s estate so that reorganisation can proceed efficiently, protecting creditors and reorganising debtors from piecemeal litigation and supporting the power of the bankruptcy court to enforce its own orders.”9

As such, insolvency and bankruptcy procedures are centralised, public processes where the state alone is considered appropriately placed to legislate for and expeditiously administer such procedures and to determine competing interests between otherwise unrelated third parties.10

Thus, arbitration policy aims to recognise and uphold the parties’ agreement to arbitrate their dispute as sacrosanct, regardless of the circumstances in which the parties find themselves when a dispute later arises. Bankruptcy policy, however, allows for a change in circumstance to override the parties’ earlier agreement to arbitrate, in favour of centralised proceedings designed to ensure the protection and fair treatment of creditors and the insolvent debtor. Accordingly, between arbitration on the one hand and insolvency and bankruptcy policy on the other, there arises:

“[A] conflict of near polar extremes: bankruptcy policy exerts an inexorable pull towards centralization while arbitration policy advocates a decentralized approach towards dispute resolution.”11

7 Mitsubishi Motors v Soler Chrysler-Plymouth 473 U.S. 614 at 628.
11 United States Lines Inc, Re 197 F.3d 631, 640 (2d Cir. 1999).
3. SUBORDINATION OF ARBITRATION POLICY: THE ENGLISH EXAMPLE

To achieve its aims of ensuring equality (or fairness) among creditors by way of a transparent process, national insolvency legislation and policy typically restrict the contractual freedom of both debtor and creditor and alter general principles of contract law. This means that, despite the existence of freely-entered court jurisdiction and arbitration agreements, both insolvent parties and their creditors are commonly restricted in their ability to commence and continue legal proceedings, including arbitration. The public policy behind arbitration as a consensual and decentralised process for resolving disputes is thereby often made subordinate to the public interest of ensuring a transparent and centralised insolvency procedure.

It is generally acknowledged that national legislators are free to define the arbitrability of a dispute in accordance with their own public policy considerations. This freedom is, for example, reflected in arts II and V(2)(a) of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (NYC). Article II obliges contracting states to recognise and enforce only written arbitration agreements which concern a “subject matter capable of settlement by arbitration”. Article V(2)(a) provides that the recognition and enforcement of an award may be refused if “the subject matter of the difference is not capable of settlement by arbitration under the law of that country”. Accordingly, national legislators commonly preclude certain subject matter from arbitration, e.g. in some jurisdictions patent and employment disputes. In principle, national legislators are free to impose restrictions on arbitrability when a party becomes insolvent.

The English system provides an illustration of this restriction in the insolvency and bankruptcy context. The legislation, which includes the English Insolvency Act, the European Community Council Regulation on Insolvency Proceedings and the UNCITRAL Model Law on Cross-Border Insolvency, also highlights the complexity of the substantive and procedural legal issues faced by arbitration participants when one party becomes insolvent.

The English Insolvency Act 1986

In England, the Insolvency Act 1986 Sch.1 paras 5 and 6 gives an administrator or administrative receiver the power to bring or defend any proceedings in the name and on behalf of the insolvent company and the power to refer to arbitration any question affecting the company (if there is an arbitration agreement). On a voluntary winding-up, the liquidator may also bring or defend any proceedings in the name and on behalf of the insolvent company, s.165(3) and Sch.4 Pt II(4); but, if the winding up is compulsory, the liquidator may do so only with the court’s permission, s.167(1)(a) and Sch.4 Pt II(4).

Thus, English insolvency legislation determines the subjective arbitrability of a dispute by determining the capacity of the administrator or liquidator to bring and defend proceedings in the name of the insolvent party. It does so by reference to the type of insolvency proceeding envisaged, distinguishing between voluntary and compulsory winding up proceedings. Likewise, the objective arbitrability of a dispute is affected by provisions which provide for the stay of other legal proceedings in favour of insolvency proceedings. Such provisions perhaps “generate the most obvious conflicts between arbitration and insolvency law”. In England, once a company enters administration, no arbitration proceedings may be instituted or continued against it without the consent of its administrator or the permission of the

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court, Sch.B1 para.43(6). Whether the court will grant an application for leave to pursue proceedings (including arbitration proceedings) against a company in administration is a matter of discretion, subject to the guidelines set out in Atlantic Computer Systems, Re.\textsuperscript{16} Essentially, the courts must carry out a balancing exercise between the legitimate interests of the applicant and those of the other creditors. In doing so, they will consider the potential financial loss to be suffered by the creditor if permission to commence proceedings is refused, compared with the loss potentially suffered by the other creditors if permission is granted. The burden is on the creditor to show that it would be inequitable for it to be denied the right to commence legal proceedings. Ultimately, if the action is unlikely to impede the achievement of the purpose of the administration, leave should be granted. Where the claim is for monetary relief alone, leave is less likely to be granted.

The leave of the court is not required in order to pursue proceedings against a company in a voluntary winding-up. However, in a compulsory winding up, proceedings may not be commenced or instituted against the company without leave, s.130. Where a company is under a compulsory winding up order the court will apply similar reasoning to that in Atlantic Computer Systems, Re and will seek to do what is “right and fair in all the circumstances”.\textsuperscript{17} Accordingly, in England, not only the relevant legislative scheme but also the related case law operate to potentially impact upon the objective arbitrability of a dispute where one of the parties is engulfed by insolvency proceedings.

European Community Regulation

Regulation 1346/2000 on insolvency proceedings [2000] OJ L160/1 (the Regulation) provides an additional layer of regulation in determining arbitrability. It recognises the need for efficient cross-border insolvency proceedings in the proper functioning of the European Community. However, it also recognises that each of the EC members has widely differing substantive laws and that it is therefore not practical to introduce insolvency proceedings with universal scope across the entire European Community. Accordingly, the Regulation provides a regime relating to the commencement of insolvency proceedings whereby “main” insolvency proceedings are to be opened and conducted in the Member State where the debtor has “the centre of his main interests”, while secondary proceedings may be opened and run in parallel in the Member State where the debtor has an “establishment”. It provides for immediate recognition of judgments concerning the opening, conduct and closure of insolvency proceedings within the European Community. It also sets out mandatory choice of law rules, which provide that the law of the Member State in which insolvency proceedings have been opened is applicable. Such law determines, inter alia, the effects of insolvency proceedings “on current contracts to which the debtor is party” and other proceedings brought by individual creditors, “with the exception of lawsuits pending”, arts 4 and 15. The English courts have recently affirmed that the question of whether a dispute is arbitrable depends on whether an arbitration (i.e. a “lawsuit”) in respect of that dispute is “pending” or not. If an arbitration is already pending, the law of the seat of the arbitration (as opposed the law of the state in which insolvency proceedings were opened) shall determine arbitrability.\textsuperscript{18}

UNCITRAL Model Law on Cross-Border Insolvency

By the English Cross-Border Insolvency Regulations 2006 the United Kingdom adopted the UNCITRAL Model Law on Cross-Border Insolvency (the Model Law), which contains further restrictions on arbitrability. Its purpose is to ensure a fair distribution of an insolvent’s


\textsuperscript{17} HIH Casualty & General Insurance Ltd, Re [2002] EWCA Civ 300; [2002] 2 B.C.L.C. 228.

assets where they are in more than one country. It aims to do this by setting rules governing the co-operation of courts, the provision of assistance to insolvency administrators, the co-ordination of two or more proceedings in different countries and the opening of insolvency proceedings. Unlike the Regulation, which has automatic effect throughout the European Community, states are free to enter into the Model Law if they wish and to adapt the law to their own country’s particular circumstances. Countries that have adopted the Model Law include the United States, Australia and Japan.

For our purposes the most important provision of the Model Law is art.20, which provides that, where foreign insolvency proceedings have been recognised, the “commencement or continuation of individual actions or individual proceedings concerning the debtor’s assets, rights, obligations or liabilities is stayed”. The Guide to the Model Law clarifies that the generic reference to “individual actions” is intended to cover actions before an arbitral tribunal, para.145.

4. SOME DIFFERENCES IN APPROACH
The United States
Of course such solutions are neither uniform, nor uniformly applied, from jurisdiction to jurisdiction. In the United States, the Federal Bankruptcy Code provides a general rule that any ongoing proceedings brought against an insolvent party, including arbitration proceedings, shall be stayed. However, a party may apply for relief from such a stay “for cause”, ss.362, 362(d)(i). Factors relevant to determining whether sufficient cause exists to allow proceedings to continue include issues of economy and expediency and also whether there is any connection or interference between those proceedings and the bankruptcy proceedings; and whether litigation in another forum would prejudice the rights of other creditors. Further case law suggests that US courts would be reluctant to enforce such a stay where a valid arbitration agreement exists. The influential Second Circuit Court concluded in United States Lines, Re that the Federal Arbitration Act:

“... as interpreted by the Supreme Court dictates that an arbitration clause should be enforced unless [doing so] would seriously jeopardize the objectives of the [Bankruptcy] Code.”

But it distinguished between core proceedings, which may not be arbitrable, and other proceedings generally considered to be arbitrable. This distinction was made on the value of the claim and its effect on the bankrupt estate. Substantial claims affecting that were considered core and possibly non-arbitrable. Accordingly, the court accepted a wide discretion to determine whether a matter should be decided by arbitration, guided primarily by the value of the claim.

United States Lines, Re involved a post-insolvency breach of a pre-insolvency contract with litigation commenced by (rather than against) the debtor. It is likely that a distinction between core and non-core proceedings based primarily on the value of the claim and its

19 Sonnax Indus Inc v Tri Component Prods Corp (Sonnax Industries Inc, Re), 907 F. 2d 1280, 1286 (2d Cir. 1990).
21 The court concluded that the “impacts” of certain contracts, although pre-dating the bankruptcy, “render the proceedings core... Resolving disputes relating to major insurance contracts are bound to have a significant impact on the administration of the estate”. See Kröll, “Arbitration and Insolvency Proceedings” in Mistelis and Lew (eds), Pervasive Problems in International Arbitration, 2006, para.18-25.
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impact on the estate is limited to circumstances where the law is not clear, as in this case. However, where a creditor asserts a claim against the bankruptcy estate for money damages arising from a pre-insolvency breach of contract, it is clear that the claim is core, regardless of its size.\(^2\) If the debtor sues a non-bankruptcy party to a pre-insolvency contract for a pre-insolvency breach, that would be a non-core matter (unless the non-debtor filed a related claim in the bankruptcy case).\(^2\) However, where the law is unclear, the various US court circuits have approached the distinction between “core” and “non-core” proceedings differently, with a heavy reliance on the unique circumstances of each case.

This distinction between core and non-core proceedings is drawn from a decision of the US Supreme Court which subsequently led to legislative amendments with respect to the jurisdiction of specialist bankruptcy courts.\(^2\) These amendments gave bankruptcy judges authority to hear and determine “core” proceedings otherwise within the jurisdiction of the district courts.\(^2\) Although the Federal Bankruptcy Code provides a non-exhaustive list of what constitute core proceedings within the jurisdiction of the bankruptcy courts,\(^2\) a “horribly murky” and inconsistent case law has developed in applying this distinction to the treatment of arbitration agreements.\(^2\) This lack of clear precedent has resulted in unpredictability, resulting in further time consuming and costly proceedings to determine the issue. The aim of efficiency for which both arbitration and bankruptcy strive is therefore often frustrated. Commentators acknowledge a need for Congress or the Supreme Court to step in and clarify the extent to which arbitration is subordinate to破产 policy.\(^2\)

France

United States Lines, Re (where the size and impact of the claim rendered the arbitration a “core” proceeding) is to be compared to European jurisdictions where the arbitrability of a claim is determined by the nature of the dispute. Only “pure” bankruptcy disputes, which involve matters to do with the supervision of bankruptcy procedures, are non-arbitrable. Because those matters directly concern competing interests of otherwise unrelated third parties, the state alone remains competent to deal with them. Contractual matters, regardless of size or impact on the bankrupt estate, are by contrast arbitrable.\(^2\)

French law makes similar provision to the US Federal Bankruptcy Code by effecting a stay of any proceedings involving an insolvent party.\(^2\) French courts have recognised the requirement for a stay of proceedings as a principle of both domestic and international public policy that, “takes precedence even where an arbitration taking place in France is

\(^2\) 28 USC s.157(b).
\(^2\) Northern Pipeline Construction Co v Marathon Pipeline Co 458 U.S. 50 (1982).
\(^2\) Northern Pipeline Construction Co v Marathon Pipeline Co 458 U.S. 50 (1982).
\(^2\) 28 USC s.157. The bankruptcy courts have only limited jurisdiction to recommend findings of fact and conclusions of law to the district court in respect of “non-core” proceedings.
\(^2\) 28 USC s.157(b)(A)–(O).
\(^2\) Code de Commerce L.621-40.
not subject to French law”\(^{31}\). However, proceedings are only stayed until the creditor files a declaration of claim, after which proceedings, including international arbitration proceedings, are resumed.\(^{32}\) The scope of the resumed proceedings is limited only to the extent that an order for the payment of any amount must be made in the bankruptcy proceedings. An arbitral tribunal can still determine the issues in dispute between the parties but it cannot order payment by the bankrupt party.\(^{33}\)

The position in France was recently tested and restated in Jean X v International Co for Commercial Exchanges (Income)\(^{34}\) where, despite the French respondent company being made subject to a liquidation order of a French court during the course of arbitration proceedings, an arbitration tribunal found against the French company and ordered it to pay damages to an Egyptian company. Although such an award was apparently in clear contravention of French bankruptcy law, the Paris Court of Appeal determined that this violation was merely formal and of no effect in practice, the bankrupt company having no means in any event to pay the damages.\(^{35}\) The Cour de Cassation disagreed and held that the tribunal’s award, which ordered the payment of damages by an insolvent party, was a violation of French public policy, holding that the tribunal should have limited itself to validating and quantifying the damages sought, as opposed to actually ordering the insolvent respondent to pay the damages.

Germany

In Germany the arbitrability of a dispute with an insolvent party is derived not from the relevant insolvency legislation but from the arbitration law contained in the Code of Civil Procedure. It provides that, “[a]ny claim involving an economic interest can be the subject of an arbitration agreement”, para.1030(1). Accordingly, the courts are rarely concerned with questions of arbitrability when faced with an insolvent party. The case law focuses on the interpretation of the arbitration agreement and the extent to which the insolvent party, or its trustee, is bound by it or whether certain issues fall within its scope. Unlike France, the tribunal is not restricted from ordering payment by an insolvent party.

It is argued that the rationale for allowing contractual claims to be arbitrated notwithstanding the insolvency of one party is that third-party interests are sufficiently protected by the insolvent’s trustee’s participation in the arbitration.\(^{36}\) The German Code of Civil Procedure does provide for a mandatory stay of proceedings after the initiation of insolvency proceedings. The primary purpose of this stay is merely to ensure that the original debtor is...
suitably substituted in ongoing proceedings by its trustee and to afford the trustee sufficient preparation time.37

Switzerland
The position in Switzerland is similar to that of Germany. The Swiss Federal Private International Law Act provides, s.170(1): “The subject matter of the arbitration may be any matter involving a financial interest.” Likewise, although there is no mandatory stay of proceedings, time will be allowed for the trustee to be substituted and to prepare its case.38

It is worth noting, however, especially given the recent conflicting Swiss and English court decisions in *Elektrim SA and Vivendi* discussed below, that Switzerland is not a member of the EC and therefore not subject to the Regulation 1346/2000 on insolvency proceedings.

Italy
In Italy, once a party is adjudged insolvent, any arbitration agreement to which it is a party is deemed to be inoperable and all future claims made by or against the insolvent party are subject to the exclusive jurisdiction of the bankruptcy court.39 With respect to ongoing arbitration proceedings, arbitrability depends upon whether the insolvent party is the claimant or respondent. Pending proceedings brought against the insolvent party must be filed with the bankruptcy court.40 However, where the pending proceedings were initiated by the insolvent party as claimant, although initially suspended, proceedings may be continued by the insolvent party’s trustee six months after the claimant is adjudged insolvent.41

Spain
The situation in Spain is similar to that of Italy in that, upon a declaration of insolvency, all arbitration agreements to which the insolvent party is a party become inoperable for the duration of the insolvency proceedings. The commercial courts in charge of insolvency proceedings acquire exclusive jurisdiction over future claims involving the insolvent party.42 However, proceedings which have already been commenced, whether by or against the insolvent party, may normally be continued. Any award rendered in such proceedings shall be binding upon the commercial court overseeing the insolvency proceedings.43

Poland
The above examples are to be contrasted with the somewhat more severe position in Poland. As will be seen in the discussion of *Elektrim and Vivendi*, upon a declaration of bankruptcy Polish law renders any arbitration agreement concluded by an insolvent party ineffective and discontinues any pending arbitration proceedings.44

37 For the German position see Kröll, “Arbitration and Insolvency Proceedings” in Mistelis and Lew (eds), *Pervasive Problems in International Arbitration*, 2006, paras 18-28/30 and 18-36/37.
39 Corte di Cassazione, October 14, 1992, n.11216.
40 Italian Bankruptcy Code arts 51 and 52.
41 Italian Bankruptcy Code art.43.
42 Spanish Insolvency Act art.52.1.
43 Spanish Insolvency Act arts 52.2 and 53.1.
44 Polish Bankruptcy and Reorganisation Law art.142.
An Aside: the Ukraine
A recent case in the European Court of Human Rights (ECtHR), dealing with unique and somewhat controversial provisions of Ukrainian law, dramatically illustrates the concerns of a claimant forced to deal with unfamiliar foreign insolvency legislation. In *Regent Co v Ukraine*, Regent was the assignee of an award rendered in December 1998 against Oriana, a Ukrainian company majority owned by the Ukrainian state. Enforcement proceedings were commenced in the Ukraine in July 1999 by Regent’s predecessor, continued by Regent and were still pending nine years later when the case went before the ECtHR in 2008. During that period bankruptcy proceedings were instituted against Oriana, bringing into effect the relevant Ukrainian insolvency law. Under the Ukrainian Law of May 14, 1992 s.12, a Ukrainian commercial court is entitled to order a moratorium on debt recovery from a company which is the subject of insolvency proceedings. Additionally, the Ukrainian Law of November 29, 2001 s.2 stays the execution of all writs by the State Bailiff’s Service in respect of the assets of undertakings in which the state holds at least 25 per cent of the share capital. These provisions were relied upon to prevent Regent from enforcing its award. Ultimately, Regent was successful in arguing before the ECtHR that the continued non-enforcement of the award constituted a violation of its rights to a fair hearing and the peaceful enjoyment of its possessions as protected by the European Convention on Human Rights. Regent got there in the end but first endured a painful lesson on the application of foreign insolvency law.

5. INTERNATIONAL ARBITRAL CASE LAW
The application of foreign insolvency law
Given that policy differs from jurisdiction to jurisdiction, matters are further complicated when claims in arbitration are pending against a bankrupt party from a foreign country. This gives rise to the question whether foreign insolvency law provisions, which are peculiar to the jurisdiction in which the bankrupt party is incorporated, apply to an arbitration seated in another jurisdiction. In other words, which law, the law of the insolvency proceedings or the law of the seat of the arbitration, is to govern the effect of one party’s bankruptcy upon ongoing arbitration proceedings?
Most arbitration texts give little or no consideration to the effect that one party’s insolvency has on arbitration proceedings. What commentary there is tends to review the matter from a domestic perspective. There is even less commentary on the more specific questions arising where a declaration of insolvency is made in one jurisdiction while the relevant arbitration is seated in another. However, a number of ICC arbitration cases have addressed this issue and provide some guidance as to the approach arbitrators may take in the absence of legislative guidance. Analysis of these cases and subsequent commentary suggests that arbitrators are inclined to continue arbitration proceedings notwithstanding the insolvency of one of the parties.
In *Casa v Cambior*, Casa, having already been placed into an early form of administration in its home jurisdiction of Luxembourg, commenced ICC arbitration against Cambior in Paris. However, upon being placed into a more advanced level of administration and faced with counterclaims, Casa subsequently requested the arbitral tribunal to decline jurisdiction on the basis of its status. It argued that:

“[T]he public policy provisions adopted in the context of administration proceedings have a substantial influence on the dispute, to the extent that they render it non-arbitral.”

46 European Convention on Human Rights art.6(1) and art.1 of Protocol No.1 respectively.
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The tribunal was not persuaded by this argument, pointing to the fact that Casa had itself commenced the arbitration while already in administration. It concluded:

"[T]he fact that one of the parties is subject to bankruptcy proceedings is not in itself sufficient to render a dispute non-arbitrable per se... The only disputes which are excluded are those which have a direct link with the bankruptcy proceedings, namely those disputes arising from the application of rules specific to those proceedings."

Although the tribunal accepted jurisdiction, it recognised that "disputes arising from the application of rules specific to [the bankruptcy] proceedings" were possibly beyond the scope of its jurisdiction. Those matters, concerning the rules which govern bankruptcy proceedings, necessarily affect the rights of third parties (who are not privy to the arbitration agreement from which the tribunal’s jurisdiction arises). The tribunal thereby acknowledged that the state alone is in a position to determine such matters.

Another ICC tribunal sitting in Brussels reached a similar decision when considering a claim for security for costs against an Italian company subject to Italian bankruptcy proceedings.48 However, following a 1995 review of relevant ICC cases, one commentator, Fernando Mantialla-Serrano, suggests that the nature of the dispute (whether or not it concerns the specific rules of the bankruptcy proceedings) is not determinative. Rather, "arbitrators seem to rely heavily on the territorial effects of insolvency proceedings" when considering whether or not to suspend proceedings in light of one party’s bankruptcy.49

One tribunal sitting in Damascus and applying Syrian law considered that:

"[I]ts mission... is not to be affected by a Court’s decision rendered subsequently in France, which without more, is not intended to produce effects in Syria."50

Another tribunal, sitting in Tunis, considered that it was:

"[N]ot bound by a particular (substantive or procedural) national law and, least of all, by the French [insolvency] law that is completely foreign to the present proceedings."51

Grounds of challenge to an award

Mantialla-Serrano notes that the reasons given in these awards suggest the approach of national judges restricted to their territorial forum rather than that of international arbitrators. He argues that international tribunals should not equate the place of arbitration to a judicial forum so as to restrict the application of insolvency proceedings and orders made in other jurisdictions. International arbitrators, with an eye on enforcement of the award, should examine and take into account appropriate mandatory rules of international public policy in jurisdictions where enforcement may ultimately be sought.52

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The position in France will cause arbitrators to pause in considering possible grounds of challenge to their awards. Arguably, the failure of an international award to observe unique national insolvency laws might not be considered a violation of public policy. Resort to arbitration does not deprive a debtor, and by extension its creditors, of the fair resolution of a dispute. Nor does the resolution of a dispute by arbitration deprive third-party creditors of their right to equal treatment in the distribution of the debtor’s assets. Accordingly, such an award does not breach the public policy underpinning the insolvency legislation. However, the relevant French case law makes clear that the failure of an award to observe the mandatory (albeit temporary) stay of proceedings required by French insolvency law amounts to a breach of both national and international public policy. Such a failure may, therefore, lead to the challenge of an award and its non-enforcement in France. International arbitrators are well-advised to closely monitor any foreign insolvency legislation that may be applicable to an insolvent party participating in an arbitration before them.

Locus standi
Mantialla-Serrano notes that the locus standi of an insolvent party, or its trustees, administrators or assignees, was the issue that most tested tribunals faced with an insolvent party. However, his survey did not reveal any departure from the generally accepted criteria normally followed by international arbitrators when considering locus standi arguments. The insolvency or enforced reorganisation of a company leads to questions of whether the company or its trustees or administrators have the capacity to continue proceedings. A London-seated arbitration applying English law and involving a Japanese defendant corporation undergoing reorganisation provides an interesting example of the type of issues which must be grappled with. The tribunal refused to dismiss a claim on the ground that it could not be maintained against the insolvent party but only against its trustees who had not been named in the Request for Arbitration. It concluded that, under Japanese law, the proper respondent to the proceedings was the “Trustees of Company A”. However, although the request was addressed to the insolvent company (i.e. to “Company A”), the tribunal accepted that as just one means of addressing the request to the entity or person responsible for the company. For example, the request could have otherwise been expressly addressed to the CEO of the company or, in this case, the trustees. Even if that reasoning was wrong, the tribunal went on to conclude that the trustees were estopped from avoiding the arbitration, having participated fully in it by responding to the request and nominating an arbitrator.

If an insolvent party or its trustees or administrators has assigned certain claims, Mantialla-Serrano’s review suggests that arbitrators will look to the law of the contract concerned. This can be seen in the approach of a tribunal sitting in Zurich when dealing with a contract governed by Swiss law which concluded:

“It is undisputed that, the Agreement being subjected to the substantive rules of Swiss law, the assignment should conform to Swiss law in order to be valid.”

6. A CAUTIONARY TALE: THE ELEKTRIM/VIVENDI DECISIONS
Opposing decisions in the English and Swiss courts in the long-running battle between Elektrim SA and Vivendi highlight the need to give timely consideration to the issues considered in this article and provide a practical illustration of the difficulties arbitration
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participants can face when one party becomes insolvent, especially when the parties’ dispute concerns numerous jurisdictions and arises across a number of agreements with competing forum selection clauses.

Elektrim SA was a Polish company that was previously a substantial shareholder in PTC, a Polish mobile telephone company. In 2001, Elektrim entered into an agreement with Vivendi Universal SA and Vivendi Telecom International SA (together Vivendi) as part of a series of agreements by which Vivendi was to acquire PTC. The 2001 agreement provided for arbitration in London under the LCIA arbitration rules. In 2003, Vivendi commenced an LCIA arbitration against Elektrim in London seeking €1.9 billion. It claimed that Elektrim had interfered with or failed to secure the interest in PTC which Vivendi was to purchase. Vivendi subsequently commenced a second arbitration against Elektrim in 2006 in reliance upon a purported settlement agreement between the parties. The second arbitration was seated in Geneva and commenced pursuant to the ICC arbitration rules. In August 2007, Elektrim was declared bankrupt by the Warsaw District Court and an administrator was appointed. Elektrim thereby became bound by the Polish Bankruptcy and Reorganisation Law art.142:

“Any arbitration clause concluded by the bankrupt shall lose its legal effect as at the date bankruptcy is declared and any pending arbitration proceedings shall be discontinued.”

As a matter of Polish law, therefore, Elektrim’s bankruptcy operated to cancel any arbitration agreement into which it had entered. This arguably deprived both the London and Geneva tribunals of jurisdiction over Vivendi’s claims against Elektrim. Under Polish law, those claims fell to be determined in accordance with Polish insolvency law in the course of Elektrim’s administration.

Elektrim raised objections to the jurisdiction of both the London and Geneva tribunals. In March 2008, the London tribunal rejected Elektrim’s objections in its interim partial award, accepting jurisdiction over Vivendi’s claims and declaring that Elektrim had breached its agreement with Vivendi. The Geneva tribunal, however, refused jurisdiction to determine Vivendi’s claims under the purported settlement agreement. Elektrim challenged the award of the London tribunal under the English Arbitration Act 1996 s.67 on the grounds that, as a result of Elektrim’s bankruptcy, the tribunal lacked substantive jurisdiction over the dispute referred to it. Vivendi challenged the award of the Geneva tribunal under art.190(2)(b) of the Swiss Private International Law on the grounds that the tribunal had erroneously refused jurisdiction.

The English decisions

The Regulation lays down mandatory rules for choice of law, jurisdiction, recognition, enforcement and co-operation for cross-border insolvencies within the European Community. It forms part of English law and was therefore central to the English decisions. It provides:

“Article 4

1. Save as otherwise provided in this Regulation, the law applicable to insolvency proceedings and their effects shall be that of the Member State within the territory of which such proceedings are opened, hereafter referred to as the 'State of the opening of proceedings'.

2. 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: ... (e) the effects of insolvency proceedings on current contracts to which the debtor is party; (f) the effects of the insolvency proceedings on proceedings brought by individual creditors, with the exception of lawsuits pending. ...

Article 15
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.”

At first instance, Elektrim argued that the parties’ arbitration agreement was a “current contract” within the meaning of art.4.2(e): as “the law of the State of the opening of the [insolvency] proceedings” (i.e. Polish law) was to determine the effect of insolvency proceedings on current contracts, Polish law applied. Vivendi argued that the arbitration was a “lawsuit pending” within arts 4.2(f) and 15, and so English law, as “the law of the Member State in which that lawsuit is pending”, governed that effect.

In the English High Court, Christopher Clarke J. held that “lawsuit pending” was sufficiently wide as to include a reference to arbitration for the purposes of arts 4.2(f) and 15. If the legislators had wanted to distinguish between lawsuits pending before a court and arbitration, they could have easily done so. Accordingly, arts 4.2(f) and 15 applied and English law, as “the law of the Member State in which that lawsuit is pending”, determined the effects of Elektrim’s bankruptcy upon the arbitration.

Elektrim had argued that, by operation of Polish law and art.4.2(e), the arbitration agreement, as a “current contract”, lost “its legal effect as at the date bankruptcy [was] declared”. Accordingly, the arbitral proceedings already commenced in accordance with that contract must also come to an end. Clarke J. recognised that this argument created a potential conflict. Articles 4.2(f) and 15 would have been practically made redundant by art.4.2(e). This could not have been the legislators’ intention. The more specific provision of art.4.2(f) should be given effect. Where arbitration proceedings had already been commenced, arts 4.2(f) and 15 were to apply. Accordingly, English not Polish law determined whether the arbitral proceedings could continue.

Clark J.’s decision was affirmed by the Court of Appeal on July 9, 2009. In the leading judgment, Longmore L.J. down-played the suggestion that there was any conflict between art.4.2(e) and arts 4.2(f) and 15. They have their:

“[O]wn sphere of operation and once it is clear that there is a ‘lawsuit pending’ the question whether that lawsuit should continue or be discontinued by reason of the insolvency is to be determined ‘solely’ by English law as ‘the law of the Member State in which the lawsuit is pending.’”

59 In November 2009, a Polish appeal court agreed to enforce the award ultimately rendered in Vivendi’s favour in the London seated LCIA arbitration. The Warsaw Court of Appeal, overturning the District Court in Warsaw, rejected arguments that Elektrim’s bankruptcy was an intervening event that cancelled the arbitration clause. It has been reported that the Warsaw Court of Appeal was asked to consider the application of NYC art.V(1)(a) and art.V(2)(b), which provide grounds for non-enforcement where a party can prove that it is “under some incapacity” under the law applicable to it or “enforcement of the award would be contrary to the public policy” of the country where enforcement is sought. The Warsaw Court of Appeal’s rejection of the these grounds, notwithstanding art.142 of the Polish Bankruptcy and Reorganisation Law, reflects a pro-arbitration view and a reluctance to use the NYC exceptions to interfere with the arbitral process. (See http://www.globalarbitrationreview.com/news/article/19693/polish-court-finds-arbitration-agreement-valid-despite-bankruptcy/[Accessed March 17, 2010]).
The Swiss case\textsuperscript{60}

In the Swiss case, Vivendi argued that it was a matter for the \textit{lex arbitri}, the law of the seat of the arbitration, to determine whether the tribunal retained jurisdiction over Elektrim, notwithstanding its bankruptcy. Vivendi was not able to rely on the Regulation, which does not form part of Swiss Law. The Swiss Supreme Court was guided by arts 154 and 155(c) of the Swiss Private International Law, by which companies are governed by the law of the state under which they are organised, which law “shall govern in particular: (c) The legal capacity and the capacity to act”. The Supreme Court therefore agreed with the Geneva tribunal that the effect of art.142 of the Polish Bankruptcy and Reorganisation Law was that Elektrim no longer had the capacity to participate in the arbitration. Upon its bankruptcy, any arbitration clauses concluded by it lost their legal effect and any pending arbitration proceedings were discontinued.

Conclusion

When confronted by the question of which law governs the effect of a party’s bankruptcy on ongoing arbitration proceedings, the Swiss and English courts were, quite correctly, led to opposite conclusions by their respective legislation. These cases highlight the need for parties to give close consideration to potential jurisdictional issues when concluding arbitration agreements, including the laws of the state in which insolvency proceedings may be commenced, the laws of the seat of the arbitration and the laws likely to be applied by the tribunal. The increased threat of insolvency in the current environment reinforces that need.

\textsuperscript{60} Decision 4A_428/2008 dated March 31, 2009.