Arbitrability of Company Law Disputes in Central and Eastern Europe

The Societas - Central and Eastern European Company Law Research Network organised a conference on October 20, 2017 on the interesting and complex issue of arbitrability in company law disputes. The geographical area covered was Central and Eastern Europe. The conference, part of a broader research project, was hosted by the Law Department of the Sapientia University, in the multicultural city of Cluj-Napoca (Kolozsvár, Klausenburg), Romania. At the conference, comparative and national reports were presented, which reflect very different attitudes towards arbitrability in the context of company law litigation. This book comprises these reports, intended to be used for continuation of the comparative research efforts in order to have a relatively clear image regarding the present status and possible future developments of this important subject.

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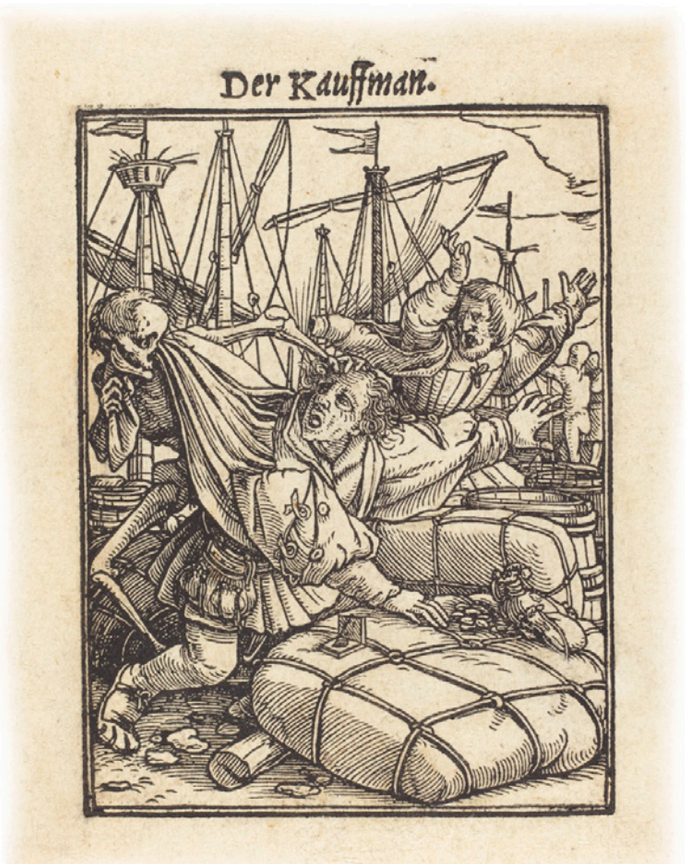

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I. Arbitrability of Company Law Disputes: A Comparative Patchworking

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1. Introduction

While companies (corporations) are claimed to be the economic alternative of contracts,[1] from a legal perspective, they have a number of different characteristics.

This short paper addresses three questions related to the arbitrability of corporate disputes: the rationale behind the

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[1] Coase, Ronald (1937). "The Nature of the Firm". Economica. Blackwell Publishing. 4 (16): 386–405 ("It is clear that [contracts and firms] are alternative methods of co-ordinating production. (…) Outside the firm, price movements direct production, which is co-ordinated through a series of exchange transactions on the market. Within a firm, these market transactions are eliminated and in place of the complicated market structure with exchange transactions is substituted the entrepreneur-co-ordinator, who directs production.").

concept of arbitrability at large; the law governing the question of arbitrability and the major arbitrability issues of company law disputes. It argues that arbitrability is predominantly not a public policy but a jurisdictional question and, thus, the exclusive application of the *lex fori* is not warranted in this regard. This leads to the conclusion, that in matters outside exclusive court jurisdiction, arbitrability should be limited only in case of genuine public policy reasons. Finally, it is argued that, in company law disputes, the third-party effects should, as far as possible, not be treated as an arbitrability issue but rather as a question of the arbitral award's scope (*inter-partes* effects).

2. Rationale of Arbitrability

The rationale behind treating certain matters as non-arbitrable (objective arbitrability) may be traced back to two considerations.

Arbitrability may be conceived as a question of public policy.[1] This conception is based on the notion that the very stipulation of arbitration (the settlement of a particular set of cases in an arbitral proceeding) would in itself violate the forum's most basic notions of morality and justice[2] or would lead to a result manifestly incompatible with the

[1] Loukas A. Mistelis, Part I Fundamental Observations and Applicable Law, Chapter 1 – Arbitrability – International and Comparative Perspectives, in Arbitrability: International and Comparative Perspectives 1:19-1:24 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

[2] For a definition of public policy in US law see Parsons & Whittemore, 508 F.2d 969, 974 (2d Cir. 1974). See also Termorio S.A. E.S.P. v. Electranta S.P., 487 F.3d 928, 938 (D.C. Cir. 2007), Newco Limited v. Government of Belize, No. 15-7077 (D.C. Cir. May 13, 2016).

fundamental principles of forum law.[1] There are, indeed, cases where arbitration may be considered so outrageously unfair, e.g. the involvement of a weaker party who merits asymmetric protection and thus abandoning the procedural pattern of the courts may appear to be unacceptable. In the same vein, in certain matters, such as the dissolution of a company, the strong requirement of public notice and the highly significant third-party effects, which cannot be reasonable handled through limiting the award's scope to *inter-partes* effects, may be antagonistic to the privacy and confidentiality of arbitration. Nonetheless, in quite a few cases, the resolution of the dispute in an arbitral proceeding would breach no basic notions of morality and justice and would not bring about an intolerable result. It needs to be stressed that the mere fact that a norm to be applied by the arbitrators have a public policy character should not necessarily imply that the matter itself is not arbitrable. The application of mandatory rules by arbitrators means that they may equally apply imperative norms. The involvement of these norms should not turn the dispute itself non-arbitrable. Evidently, the flawed or erroneous application of an imperative norm, as these are the manifestations of public policy, may easily imply the breach of public policy, what, in turn, may serve as a basis for annulment or non-recognition.[2]

The second consideration is that arbitrability may be conceived as a question of jurisdiction.[3] The starting point of

[1] For a definition of public policy in German law, see Einführungsgesetzes zum Bürgerlichen Gesetzbuche (EGBGB), Article 6.

[2] Mitsubishi v. Soler Chrysler-Plymouth, 473 U.S. 614 (1985).

[3] Stavros Brekoulakis, Law Applicable to Arbitrability: Revisiting the Revisited lex fori, Queen Mary University of London, School of Law Legal Studies Research Paper No. 21/2009.

arbitration, even though it relies on the parties' autonomy, is that the state privatizes a parcel of court jurisdiction. The parties' right to opt for arbitration is based up on the state's general license. In this sense, arbitration may operate only in the sphere where it was allowed to operate, and the state may have any reason, even milder than public policy, to insist on any parcel of court jurisdiction. This conception grasps arbitrability as a question of delegation or privatization, whose ambit is not delimited by an obscure and elusive legal concept but by a discretionary political choice.

The lack of an imminent link between arbitrability and public policy is suggested both by the 1958 New York Convention and the UNCITRAL Model Law on Arbitration. Notably, both of them set out two identical grounds for *ex officio* objecting to an arbitral award (the former for recognition and enforcement; the latter for annulment) – the lack of arbitrability and public policy. This suggests that the former cannot be a parcel of the latter.

The above doctrinal characterization has a very significant impact on international arbitration cases. However, it makes very little difference why a controversy is not arbitrable. However, in international cases, where the seat of the arbitration, the place of the court procedure declining jurisdiction and referring the parties to arbitration (due to a valid arbitration agreement) and the place of recognition and enforcement may easily differ, it is highly important whether arbitrability is based on public policy or on exclusive jurisdiction. Namely, while public policy may play a role also in cases having no impact on the forum (a less rigorous scrutiny is justified if the internal link is less intensive), the ignorance of the state's political decision as to which parcels of court jurisdiction to cede to arbitration

should generate a little upheaval in cases which have no impact on the forum.

Assuming that country "A", led by the distrust of arbitration, pronounces concession contracts non-arbitrable, while in country "B" and country "C" such matters are perfectly arbitrable. In a case, country "B" sues a concessionaire operating one of the country's airports, a company of country "C", for breach of contract and is awarded damages by an arbitral tribunal seated in country "B". The company's assets in country "B" do not cover the award so the government of country "B" seeks enforcement in country "A". Is it reasonable for the courts of country "A" to reject enforcement? If the non-arbitrability of concession agreements can be traced back to public policy reasons, then allowing arbitration as to such contracts would violate the forum's most basic notions of morality and justice. However, if the courts of country "A" see this as only a question of division of competences, why should they reject enforcement of an award which did not in any sense encroach on their exclusive jurisdiction and has an impact exclusively on countries where such agreements are perfectly arbitrable. This example shows well how the stubborn insistence on the *lex fori* may lead to unreasonable outcomes.

Nonetheless, international treaty law gives rather little room from departing from the principle of *lex fori*.

3. The Law Governing the Law Applicable to Arbitrability

In theory, there are various candidates for the choice-of-law connecting factor of arbitrability.[1] These overlapping concepts may include connecting factors like *lex fori*, *lex contractus*, *lex arbitri* and party autonomy.[2] Nonetheless, as a matter of practice and as a rule of thumb, arbitrability is considered to be governed by the *lex fori*. The 1961 Geneva Convention, as to the recognition of arbitration agreements; the 1958 New York Convention, as to recognition and enforcement and the UNCITRAL Model Law, as to the annulment of the arbitral award, establish the law applicable to arbitrability and point to the *lex fori*. However, the 1958 New York Convention contains no connecting factor as to the recognition of an arbitration agreement: whilst it provides for the non-recognition of agreements covering non-arbitrable matters, it is silent as to the applicable law.

The question of arbitrability may emerge in four stages of arbitration: the referral stage where arbitration is compelled; the annulment (setting aside) stage where the awards validity is judged, ; the recognition and enforcement stage where the question is whether to let in a foreign arbitral award into the domestic legal space and before the arbitral tribunal where arbitrators decide on their own

[1] See Loukas A. Mistelis, Part I Fundamental Observations and Applicable Law, Chapter 1 - Arbitrability – International and Comparative Perspectives, in Arbitrability: International and Comparative Perspectives 1:25-1:38 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

[2] Hamayoon Arfazadeh, "Arbitrability under the New York Convention: The Lex Fori Revisited", 17(1) Arbitration International 73, 73 (2001).

competence (*Kompetenz-Kompetenz*)[1] and try to make sure that their award will not be annulled and will be recognized and enforced.[2]

Courts, as a general principle, are obliged to compel arbitration if the parties concluded a valid arbitration agreement. This implies that the agreement needs to cover an arbitrable subject. However, it is questionable which law to apply to the issue of arbitrability. Article II of the 1958 New York Convention does prescribe that Contracting States shall recognize arbitration agreements provided they cover a subject capable of settlement by arbitration, but it fails to give any guidance under which law the subject needs to be arbitrable.

> *Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen, or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.*

Article VI(2) of the 1961 Geneva Convention, on the other hand, refers to the *lex fori* when it comes to the non-recognition of an arbitration agreement for lack of arbitrability.

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[1] See Bernard Hanotiau, The Law Applicable to Arbitrability, 26 Singapore Academy of Law Journal 874, 878-883 (2014).

[2] See Bernard Hanotiau, What law governs the issue of arbitrability? 12(4) Arbitration International 391 (1996).

The courts may also refuse recognition of the arbitration agreement if under the law of their country the dispute is not capable of settlement by arbitration.

Accordingly, the law applicable to the arbitration agreement and, hence, to the question of arbitrability at large is not addressed by the New York but may be deduced from the Geneva conventions. Article VI(2) of the 1961 Geneva Convention only provides that a court may refuse to recognize an arbitration agreement if that is not arbitrable according to its own law. This provision sets out no connecting factor as to the issue of arbitrability, as it provides that court may apply the *lex fori*, but does not say that this is the law that governs the question of arbitrability.

Interestingly, while both the 1961 Geneva Convention, in Article VII, and the UNCITRAL Model Law, in Article 28, provides for the law applicable to the substance of the dispute, none of them establishes the law applicable to the arbitration agreement itself.

Art VII – 1961 Geneva Convention

The parties shall be free to determine, by agreement, the law 51 to be applied by the arbitrators to the substance of the dispute. Failing any indication by the parties as to the applicable law, the arbitrators shall apply the proper law under the rule of conflict that the arbitrators deem applicable. In both cases the arbitrators shall take account of the terms of the contract and trade usages.

UNCITRAL Model Law

Article 28. Rules applicable to substance of dispute

(1) The arbitral tribunal shall decide the dispute in accordance with such rules of law as are chosen by the

parties as applicable to the substance of the dispute. Any designation of the law or legal system of a given State shall be construed, unless otherwise expressed, as directly referring to the substantive law of that State and not to its conflict of laws rules.

(2) Failing any designation by the parties, the arbitral tribunal shall apply the law determined by the conflict of laws rules which it considers applicable.

Nonetheless, Article VI(2) of the 1961 Geneva Convention may be extrapolated. it may be prudent for the arbitrators to take into consideration the law of the arbitration's sear as this may easily be relied upon in the eventual annulment proceedings. This seems to be highly relevant given the arbitrators' general duty to render an enforceable award.

Likewise, annulment (setting aside) by reason of non-arbitrability is generally accepted to come under the *lex fori*.[1]

Article 34 – UNCITRAL Model Law

Application for setting aside as exclusive recourse against arbitral award

(1) Recourse to a court against an arbitral award may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

(2) An arbitral award may be set aside by the court specified in article 6 only if:

(b) the court finds that:

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or

[1] See Bernard Hanotiau, The Law Applicable to Arbitrability, 26 Singapore Academy of Law Journal 874, 884-885 (2014).

(ii) the award is in conflict with the public policy of this State.

The recognition and enforcement of an arbitral award may be rejected if the matter is not considered to be arbitrable in the country where recognition and enforcement is sought. According to Article V of the 1958 New York Convention, non-arbitrability under the *lex fori* is considered, along with public policy, to be a ground of refusal that may relied upon *ex officio*.

> *Article V – 1958 New York Convention*
> *2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:*
> *(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or*
> *(b) The recognition or enforcement of the award would be contrary to the public policy of that country.*

In summary, it is fair to say that arbitrability, as a rule of thumb and as a matter of practice, is governed by the *lex fori*. There are gaps in treaty law that may permit the use of more adequate connecting factors, but these are fairly narrow in comparison to the realm of forum law.

4. Arbitrability and Company Law Disputes

Corporate disputes encompass a wide array of matters which may have fairly different features from the perspective of arbitrability.

Intra-company disputes may be considered arbitrable as a rule of thumb. Problems concerning arbitrability may emerge as to issues whose legal character is dubious; in cases where there are third party effects and as to issues involving public policy or exclusive court jurisdiction.

There is no reason not to treat intra-company disputes, in general, as non-arbitrable. This extends to the interpretation of the company's articles (memorandum) of association; and the application of its by-laws, including, for instance, the restrictions on transfer of shares, the dismissal of directors, the adjudication of disputes related to syndicate agreements and to the rule governing payment of dividends.[1]

In some jurisdictions, the notion has emerged that certain corporate disputes may have no legal character and as arbitration deals with legal differences, it should not be available for the settlement of such non-legal disputes.[2] This argument is, of course, highly dogmatic, and relates to issues

[1] See See Pilar Perales Viscasillas, Part II Substantive Rules on Arbitrability, Chapter 14 Arbitrability of (Intra-) Corporate Disputes, in Arbitrability: International and Comparative Perspectives 14:15 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

[2] See Pilar Perales Viscasillas, Part II Substantive Rules on Arbitrability, Chapter 14 Arbitrability of (Intra-) Corporate Disputes, in Arbitrability: International and Comparative Perspectives 14:4-14:10 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

may not come under the competence of state courts. This may include filling the gaps in the articles of association or contractual arrangements, modifying these contracts, appraising the value of shares or assets, determining the price, resolving conflicts of interest and deciding in case of tie votes. The legal nature of these disputes cannot be fully called into question if they may be entertained by state courts or can be related to general legal obligations, such as good faith or the parties' duty to cooperate.

Third parties represent another peculiarity of corporate disputes as they appear to be intra-company differences but in fact they usually have a significant impact on creditors and the company's business partners (suppliers, buyers etc.), let alone its employees and the revenue service. Third party effects, however, may be prevalent also in case of disputes between shareholders: the settlement of the dispute between two shareholders may easily impact the third one. Nonetheless, quite often, the presence of third party effects is not a circumstance that should warrant the extension of arbitrability and may be treated as a question of the award's scope.[1]

There is a certain set of corporate disputes that have been traditionally regarded as non-arbitrable, such as the nullity of the decisions of the shareholders' meeting,[2] the

[1] See Pilar Perales Viscasillas, Part II Substantive Rules on Arbitrability, Chapter 14 Arbitrability of (Intra-) Corporate Disputes, in Arbitrability: International and Comparative Perspectives 14:26-14:29 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

[2] For a contrary approach, see BGH, Urteil vom 6. April 2009 – Az. II ZR 255/08; BGH, Beschluss vom 6. April 2017 – I ZB 23/16. See also DIS-Supplementary Rules for Corporate Law Disputes 09 (SRCoLD), available at http://www.disarb.org/en/16/regeln/dis-supplementary-rules-for-corporate-law-disputes-09-srcold-id15.

nullity of the company and the dissolution or winding-up of the company, though the rigidity of this notion has melted in quite a few jurisdictions.[1] While imperative rules should normally not turn a case non-arbitrable, the foregoing three matters have highly intensive third party effects, which cannot be effectively handled through *inter-partes* limitations. Similarly, public notice (public registries) may also be an important factor.

These matters are considered to come under exclusive jurisdiction under the Brussels I (Recast) Regulation.[2]

> *Article 24*
>
> *The following courts of a Member State shall have exclusive*
>
> *jurisdiction, regardless of the domicile of the parties:*
>
> *(2) in proceedings which have as their object the validity of the constitution, the nullity or the dissolution of companies or other legal persons or associations of natural or legal persons, or the validity of the decisions of their organs, the courts of the Member State in which the company, legal person or association has its seat. In order to determine that seat, the court shall apply its rules of private international law;*

[1] Stavros Brekoulakis, Chapter 6: Law Applicable to Arbitrability: Revisiting the Revisited lex fori, in Arbitrability: International and Comparative Perspectives 14:20-14:22 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

[2] 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. OJ L 351, 20.12.2012, p. 1-32.

> *(3) in proceedings which have as their object the validity of entries in public registers, the courts of the Member State in which the register is kept;*

While the Brussels I Regulation pronounces the territorially competent court's jurisdiction to be exclusive against other state courts, the message may be reasonably deduced that these matters are so closely related to a single state court that they should come under its remit without exception.[1] It should be stressed that the parties have no autonomy to stipulate the jurisdiction of another state court. Article 24(4) of the Brussels I Regulation states that "[a]greements or provisions of a trust instrument conferring jurisdiction shall have no legal force (…) if the courts whose jurisdiction they purport to exclude have exclusive jurisdiction by virtue of Article 24." If the parties have no possibility to choose another state court, why should they have the possibility to choose arbitration?

5. Conclusions

This paper demonstrated that the issue whether a matter is arbitrable should not be conceived as a public policy

[1] See Stavros Brekoulakis, Chapter 6: Law Applicable to Arbitrability: Revisiting the Revisited lex fori, in Arbitrability: International and Comparative Perspectives 6:6 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009). For a contrary view, see Eric Loquin, "L'Exécution des sentences arbitrales dans l'espace judiciaire européen", in Les effets des jugements nationaux dans les autres Etats membres de l'Union européenne. Bruxelles: Bruylant, 2001, p. 166; Pilar Perales Viscasillas, Part II Substantive Rules on Arbitrability, Chapter 14 Arbitrability of (Intra-) Corporate Disputes, in Arbitrability: International and Comparative Perspectives 14-25 (Loukas A. Mistelis, Stavros & L. Brekoulakis eds., Kluwer Law International 2009).

question but rather as a question of jurisdiction. This implies that the prevalent application of the *lex fori*, which is considered the connecting factor generally applicable to the issue, is not reasonably justified. Finally, this theorem is applied to corporate disputes.

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