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# Arbitration and Insolvency Proceedings

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**LLM Thesis**

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## INTRODUCTION

Nowadays due to the global financial crisis more and more corporations are forced to proceed to insolvency due to the fact that they don't have any more the financial means to satisfy all their creditors and pay for their debts. States in order to protect the creditors of the debtor have legal mechanisms which centralize and secure the procedure of the satisfaction of non secured creditors in a collective way. The most important principles of insolvency is the equality of creditors and the transparency of the procedure.

In the meanwhile, arbitration become more and more popular way of dispute resolution especially concerning disputes which have international character, because of its advantages such as privity, free choice of law by the parties , neutrality of the forum and party autonomy. The right to arbitrate arises by the agreement between the parties.

When arbitration and insolvency meet each other many questions and dilemmas arise. Do the arbitration agreements lose their validity when a party becomes insolvent? Is the trustee bound to an arbitration agreement made prior to the initiation of insolvency proceedings? One should consider arbitration proceedings as individual acts of creditors which violate the principle of equal treatment of the creditors and therefore should be suspended? These are some of the main issues we are going to examine in the present thesis.

The thesis consists of two chapters. In the first chapter the institutions of arbitration and bankruptcy are described and especially in an international context. The second Chapter discusses the conflict between arbitration and insolvency and in specific the effects of insolvency proceedings in arbitration.

Finally, the terms of insolvency and bankruptcy are used with the same meaning and cover both reorganization and liquidation. The term trustee is used to describe the person appointed by the bankruptcy court to manage the insolvent estate, in some jurisdictions is called also administrator, liquidator etc.

## CHAPTER I

### A. ARBITRATION

Arbitration is an alternative to national courts chosen by the parties and independent of national courts. The principal characteristics of arbitration are: a) is a mechanism for the settlement of disputes b) is consensual c) is a private procedure d) leads to final and binding determination of the rights and obligations of the parties. Arbitration must be founded on the agreement of the parties. Not only does this mean that they must have consented to arbitrate the dispute that has arisen between them, it also means that the authority of the arbitral tribunal is limited to that which the parties have agreed. Arbitration is not part of the State system of courts. Nevertheless, it fulfills the same function as litigation in the State court system. The end result is an award that is enforceable by the courts, usually following the same or similar procedure as the enforcement of a court judgment.<sup>1</sup>

#### *International Arbitration*

International arbitration is a specially established mechanism for the final and binding determination of disputes concerning a contractual or other relationship with an international element by independent arbitrators in accordance with procedures structures and substantive legal or non legal standards chosen directly or indirectly by the parties.<sup>2</sup> International arbitration is based upon the ability of parties to confer jurisdiction to arbitrators to resolve their disputes arising from international commercial arbitration agreements or other international relationships. This jurisdiction is only meaningful if it is recognized by states and able to be enforced through a state's judicial system.

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<sup>1</sup> Dispute Settlement, International Commercial Arbitration, 5.1 International Commercial Arbitration, United Nations Conference on trade and development, UN 2005

<sup>2</sup> Loukas Mistelis, Stefan Kroll comparative international commercial arbitration, Julian DM Lew, Kluwer Law International, 2003, The Hague, The Netherlands Chapter 1 pg 1

### ***Applicable law to International Arbitration***

In most international arbitrations, there will be more than one system of law or legal rules that are relevant to the conduct of the proceedings and enforcement. It is possible to identify at least five different laws which may affect the conduct of an international arbitration. These are: A) the law governing the parties' capacity to enter into an arbitration agreement; b) The law governing the arbitration agreement and the performance of that agreement; c) c) The law governing the existence and proceedings of the arbitral tribunal – the “lex arbitri;” d) The law (or the relevant legal rules) governing the substantive issues in dispute - “the substantive law;” e) The law governing recognition and enforcement of the award (which may be more than one law if recognition and enforcement is sought in more than one country in which the losing party has, or is thought to have, assets).<sup>3</sup>

The procedural law of arbitration is different from the governing law of the contract: is the law by which an arbitration will operate. The procedural law is assumed to be the law of the seat of arbitration.

Parties are free to choose the lex arbitri and any procedural rules they wish. In the absence of a choice the arbitral tribunal, is free to determine procedural rules that considers they are appropriate.

### ***Arbitration clause***

Arbitration clauses (also known as arbitration agreements) may refer either in specific or general disputes arising out of a contractual or other legal relationship to arbitration<sup>4</sup>. Arbitration agreement is the foundation of almost every arbitration, which is based on the parties' intention and not on procedural rules of law. The direct effect of a valid arbitration agreement is that confer jurisdiction on the arbitral

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<sup>3</sup> Robert Covacs, A Transnational Approach to the Arbitrability of Insolvency Proceedings in International Arbitration

<sup>4</sup> Irene Welser/Susanne Molitoris, The Scope of Arbitration Clauses – Or “All Disputes Arising out of or in Connection with this Contract ...” [http://www.chsh.com/fileadmin/docs/publications/Welser/WelserMolitoris\\_AYIA\\_2012.pdf](http://www.chsh.com/fileadmin/docs/publications/Welser/WelserMolitoris_AYIA_2012.pdf)

tribunal to decide over the dispute.<sup>5</sup> Formal validity of an arbitration agreement is closely related to the issue of whether the party actually consented to arbitration for a dispute that may arise between them.

According to article II (3) New York Convention unless the arbitration clause is null and void, inoperable or incapable to be performed a court should refer the parties to arbitration.

### *Arbitrability*

States retain the power to prohibit the resolution of certain categories of disputes outside their courts. Such categories of disputes are said to be not arbitrable and if an arbitration agreement is entered into to resolve such dispute, it will not be valid. Arbitrability is a condition of validity of the arbitration agreement and consequently, of the arbitral tribunal's jurisdiction. While the principle of party autonomy espouses the right of parties to submit any dispute to arbitration, national laws often impose restrictions or limitations on what matters can be referred to and resolved by arbitration. The term "arbitrability" is used here to mean the capability of a subject matter to be submitted to dispute resolution by way of arbitration, it is generally acknowledged that countries are free to define the arbitrability of a dispute in accordance with their own public policy considerations.

While recognizing party autonomy to submit disputes to arbitration, states retain the power to impose restrictions or limitations on what matters can be referred to and resolved by arbitration. Article II of the New York Convention on Recognition and enforcement of foreign arbitral awards and art 2 (a) of the UNCITRAL Model Law on International Commercial Arbitration permit signatory States to treat categories of claims as incapable of settlement by arbitration- or non arbitrable.

According to Youssef “arbitrability is the fundamental expression of the freedom to arbitrate. It defines the scope of the parties’ power of reference or the boundaries of the right to go to arbitration in the first place.” Arbitrability of insolvency related matters is divided in two categories: subjective or objective Arbitrability. Subjective

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<sup>5</sup> Lew, The law applicable to the form and substance of the a arbitration clause , ICCA Congress series no 9

arbitrability (*ratione personae*) concerns the entitlement of the persons or entities to submit their dispute to arbitration.

Objective arbitrability (*ratione materiae*) concerns whether the disputes referred to arbitration are capable to be settled by arbitration in the light of relevant public policy..

The restrictions placed by State legislators and on the matters that may be submitted and resolved by arbitration are usually in the form of provisions called "loi d'application immediate" ("laws of immediate application"), "lois de police" ("police laws") or "mandatory rules".<sup>6</sup>

However, the question of arbitrability may arise at various points: a) Before the arbitral tribunal which will decide on it itself, in accordance with the principle of "Kompetenz-Kompetenz"; b) Before a state court (either at the seat of arbitration or elsewhere) where a party which considers that the dispute is not arbitrable, submits it to the state court, which will have to decide upon the objection to the jurisdiction of the arbitral tribunal prior to any award being issued; c) Before a state court, at the seat of arbitration, where a party may invoke the issue of arbitrability as a ground for a setting-aside procedure after an award has been issued; d) Before a state court, at a court of an enforcing country, where an objection to arbitrability may be raised by a party before the state court deciding on the recognition and enforcement of the award; and e) Before a bankruptcy court where the issue of the tribunal's jurisdiction may also arise where the trustee tries to bring a claim against one of the creditors who then invokes the existence of the arbitration agreement as a bar to the proceedings.<sup>7</sup>

### ***Enforcement of arbitral awards***

While the majority of arbitral awards are satisfied through the voluntary compliance of the parties involved, on some occasions a party must invoke external authority to enforce a losing party's obligation and collect the damages awarded. Such external

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<sup>6</sup> Robert Covacs, A Transnational Approach to the Arbitrability of Insolvency Proceedings in International Arbitration

<sup>7</sup> Robert Covacs, A Transnational Approach to the Arbitrability of Insolvency Proceedings in International Arbitration

authority resides in state courts.<sup>8</sup> The State courts may refuse the enforcement of an arbitral award especially if they found that violates public policy. The New York Convention on Recognition and Enforcement of arbitral awards, which is adopted by many States in art. V introduces the reason for which a state court may deny recognition and enforcement of awards.

## B. INSOLVENCY

Insolvency is a financial condition where the debtor who may be a natural or legal person or even a State may no longer satisfy its creditors and pay its debt obligations when they become due. The intervention of insolvency law is an external legal factor to tackle the situation by replacing debtor's control and restraining creditor's actions – for the collective benefit of all the stakeholders concerned.<sup>9</sup>

In most jurisdictions, insolvency proceeding can be either voluntarily or involuntarily. An involuntarily proceedings is commenced by the creditors or others stakeholders, while a voluntary proceeding is commenced by the distressed company.

The basic purposes of the insolvency is to allow where possible the survival of the insolvent company or to ensure the orderly dissolution guaranteeing equal treatment of all the creditors of the same class.

A number of US commentators inspired by the law and economic movement have argued that proper function of insolvency law can be seen in terms of a single objective: to maximize the collective return to creditors<sup>10</sup>. Bankruptcy law according to Paul Kirgis, is designed to serve two primary purposes. First, bankruptcy gives an overburdened debtor a fresh start. By relieving debtors of unmanageable obligations, bankruptcy allows debtors to resume or continue productive activity in society. Second, bankruptcy serves the interests of creditors by providing them with an equitable distribution of the debtor's nonexempt assets creating a process in which

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<sup>8</sup> Joseph T. McLaughlin Laurie Genevro, Enforcement of arbitral awards under the New York Convention- Practice in US Courts , Berkeley journal of international law Vol 3 Issue 2, art. 2 1986

<sup>9</sup> Role of public international law in cross border insolvency regime : an overview, PR Thulasidhass from the selected works of thulasidhass

<sup>10</sup> Corporate insolvency law perspectives and principles, Vanessa Fich Cambridge University Press 2002, Cambridge UK

creditors as a group can receive the highest possible return, while ensuring that no creditor benefits unfairly at the expense of others.

The three essential features of bankruptcy are often said to be the following:

- a) Actions by individual creditors against the bankrupt are frozen. The piecemeal seizure of assets by disappointed creditors through attachment or execution are stayed and replaced by a right to claim for a dividend against the pool
- b) All assets of the bankrupt belong to the pool which is available to pay creditor claims
- c) Creditors are paid *pari passu pro rata* out of the assets according to their claims.<sup>11</sup>

Professor Roy Goode in his book “Principles of corporate insolvency law” suggested ten principles of corporate insolvency law are as follows

1. corporate insolvency law recognizes rights accrued under the general law prior to liquidation
2. only the assets of the debtor company are available for its creditors
3. security interests and other real rights created prior to the insolvency proceeding are unaffected by the winding up
4. the liquidator takes the assets subject to all limitations and defences
5. the pursuit of personal rights against the company is converted into a right to prove for a dividend in the liquidation
6. on liquidation the company ceases to be the beneficial owner of its assets
7. no creditor has any interest *in specie* in the company's assets or realizations
8. liquidations accelerates creditors' rights to payment
9. unsecured creditors rank *pari passu*
10. members of a company are not as such liable for its debts

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<sup>11</sup> Principles of international insolvency 2nd edition, Philip Wool London Sweet an Maxwell 2007 pg 3

When a debtor is unable to pay its debts and other liabilities as they become due most legal systems provide a legal mechanism to address the collective satisfaction of the outstanding claims from assets (tangible or intangible) of the debtor.<sup>12</sup> When a debtor files for bankruptcy an estate is created and it includes the debtor's legal and equitable interests in property as of the date of the bankruptcy petition. The property of the estate is the pool of assets from which the creditors will be paid after the bankruptcy case is finished.<sup>13</sup>

A range of interests need to be accommodated by the legal mechanism: those of the parties affected by the proceedings including the debtor, the owners and management of the debtor the creditors who may be secured to varying degrees employees guarantors of debt and suppliers of goods and services as well as the legal, commercial and social institutions and practices that are relevant to the design of insolvency law and required for its operation. Most legal systems contain various types of proceedings that can be initiated to resolve a debtor's financial difficulties. These proceedings may be described as formal or informal. Formal insolvency proceedings are commenced under the insolvency law and governed by that law. In most jurisdictions insolvency proceedings are administered by a judicial authority. In addition to possessing the necessary business or economic attributes a debtor must have a sufficient connection to the State to be subject to its insolvency laws. Informal processes are not regulated by law and will generally involve voluntary negotiations between the debtor and some or all its creditors. While not regulated by insolvency law these voluntary negotiations nevertheless depend for their effectiveness upon the existence of an insolvency law which can provide indirect incentives or persuasive force to achieve reorganization. There is no universal solution to the design of insolvency law because the States vary significantly in their needs and so do the laws. With regard to the creditors one of the fundamental principles of insolvency law is that insolvency proceedings are collective proceedings which require the interests of all creditors to be protected against individual action by one of them. Parties of the insolvency are a) the debtor b) the insolvency representative which is the person

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<sup>12</sup> Legislative guide on insolvency law- UNCITRAL, New York United Nations Publication 2005

<sup>13</sup> Matthew Dameron, Stop the Stay: Interrupting Bankruptcy to conduct arbitration- Slipped Disc Inc v. CD Warehouse Inc., Journal of Dispute Resolution, Vol 2001, Issue 2, No 2, Article 5

responsible for administering the insolvency proceedings know also as “trustee”, “administrator”, supervisor”, “liquidator” etc. The insolvency representative may be an individual , corporation or different legal entity and has the duty to protect the estate and the the interests of the creditors and employees c) the creditors. <sup>14</sup>

### ***Reorganization and liquidation***

Two main types of insolvency proceedings are common to the majority of insolvency laws: reorganization and liquidation. Reorganization is designed to save a debtor. Reorganization is a long process during which the debtor has the opportunity to continue operating his business while repaying his creditors. The debtor negotiates with the creditors to reschedule payments within a specific time without necessarily selling assets of the business. On the other hand, liquidation which is a faster and closely controlled mechanism, demands the selling of the assets in order to repay the creditors. Once the assets are liquidated and the proceeds are distributed the company is resolved permanently.

### ***Territorialism v. Universalism***

There are two main theories regarding international or cross-border insolvency: universalism and territorialism.

The national bankruptcy laws that express worldwide jurisdiction over property of the debtor as well as claims against the debtor and its assets are often called extraterritorial national laws, while many other national bankruptcy laws express jurisdiction over the assets within the Country where the Bankruptcy Court sits are called non extraterritorial bankruptcy laws. <sup>15</sup>Extraterritorial national laws represent the principle of universality, when non extraterritorial national bankruptcy laws represent the principle of territorialism.

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<sup>14</sup> Legislative guide on insolvency law- UNCITRAL, New York United Nations Publication 2005

<sup>15</sup> Zack Clement Fulbright & Jaworski LLP, November 2006 Background Memorandum for the international insolvency institute’s proposal to UNCITRAL concerning international insolvency/ arbitration, International Insolvency Institute Conference New York , USA, 2007

Universalism, also known as pure universalism or unity, ubiquity is a system in which all aspects of a debtor's insolvency are conducted in one central proceeding under one insolvency law.<sup>16</sup>

Universalist system usually relies on international treaties or conventions as it is as States are unwilling to confer the control over the local assets to another state's court. Universalism generates economies in a number of areas, avoiding duplication of administration expenses, selling cross border assets as a whole coordination of reorganization efforts and encouraging efficient investment patterns. Modified universalism accepts that a country may unilaterally control its own territory and laws creating a system that is open to cooperation while seeking the broadest impact possible for its own laws. Territorialism is the default system for all cross border insolvency systems because it relies on actual in rem control over assets. Under this territorial approach a separate and independent plenary case is pursued in each forum in which the debtor's assets are located.<sup>17</sup> The major advantage of territorialism would be from the debtor's perspective where assets are held for the benefit of a smaller pool than might be otherwise be the case. The major disadvantages would be that reorganizing a company or group of companies is difficult or impossible, produces unequal results for creditors.

Professor Westbrook has noted that practice generally falls into two distinct forms: secondary bankruptcies and modified universality. Both of these practices modify territorialism principle by allowing a single judicial forum access to other courts minded to co-operate in order to preserve and deal with assets belonging to the debtor for the benefit of the insolvency overall.

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<sup>16</sup> Donald Trautman et al four models for international bankruptcy 41 am j comp.l. 1993

<sup>17</sup> The cross border insolvency paradigm: a defence of the modified universal approach considering the japanese experience, kent anderson u. pa. j. int'l. econ. l. 21:4 2000 pg

The logic of modified universalism tends in general to favor choice of law rules that apply the law of the main insolvency proceedings in many circumstances. The EU Regulation adopts that approach.<sup>18</sup>

### ***Cross- border insolvency***

The term cross border insolvency is used to describe the circumstances in which an insolvent debtor has assets or creditors in more than one country.<sup>19</sup>

Cross border insolvency is referred to an insolvency where the assets and/ or the liabilities of the debtor are located in two or more separated jurisdictions or where the personal circumstances of a debtor are such as to render him or it simultaneously subject to the insolvency laws of more than one country.<sup>20</sup>

Although the number of cross-border insolvency cases has increased significantly since the 1990s, the adoption of national or international legal regimes equipped to address the issues raised by those cases has not kept pace. The lack of such regimes has often resulted in inadequate and uncoordinated approaches to cross-border insolvency that are not only unpredictable and time-consuming in their application, but lack both transparency and the tools necessary to address the disparities and, in some cases, conflicts that may occur between national laws and insolvency regimes. These factors have impeded the protection of the value of the assets of financially troubled businesses and hampered their rescue.

### ***UNCITRAL Model Law on Cross Border Insolvency***

UNCITRAL has already twice addressed the international insolvency process in: (1) the UNCITRAL Model Law on Cross-Border Insolvency and (2) the UNCITRAL Legislative Guide on Insolvency Law. To reduce the chances that there would be

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<sup>18</sup> International arbitration and multinational insolvency Lay Lawrence Westbrook

<sup>19</sup> Role of public international law in cross border insolvency regime : an overview, PR Thulasidhass from the selected works of Thulasidhass)

<sup>20</sup> Max- Planck Institut Cross Border Insolvency: national and comparative studies; reports , 1992, JCB Mohr D Tubingen).

public policy reasons not to cooperate with a main case, UNCITRAL also published its Legislative Guide for Insolvency Law to encourage a similar approach among the various nations in their public policy and laws concerning bankruptcy and insolvency. The UNCITRAL Model Law was adopted in 30th of May 1997.

The UNCITRAL Model Law is designed to apply where: assistance is sought in a State by a foreign court or a foreign representative in a connection with a foreign insolvency proceeding b) assistance is sought in a foreign State in connection with a specified insolvency under the laws of that State c) a foreign proceeding and an insolvency proceeding under specified laws of the enacting State are taking place concurrently in respect of the same debtor and d) creditors or other interested persons in requesting of or participating in an insolvency proceeding under specified laws of the enacting State.<sup>21</sup>

The Model Law is designed to assist States to equip their insolvency laws with a modern legal framework to more effectively address cross-border insolvency proceedings concerning debtors experiencing severe financial distress or insolvency. It focuses on authorizing and encouraging cooperation and coordination between jurisdictions, rather than attempting the unification of substantive insolvency law, and respects the differences among national procedural laws. For the purposes of the Model Law, a cross-border insolvency is one where the insolvent debtor has assets in more than one State or where some of the creditors of the debtor are not from the State where the insolvency proceeding is taking place.<sup>22</sup>

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

### ***European Regulation on Insolvency Proceedings***

The EU Regulation provides a set of uniform conflict of laws rules that are binding and directly applicable in the Member States overriding the national conflict of laws

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<sup>21</sup> UNCITRAL Model Law on Cross border insolvency: the judicial perspective, UN New York 2012,

<sup>22</sup> [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency/1997Model.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model.html)

rules. The European Insolvency Regulation has been in force since 31 May 2002, embodying the principle of mitigated universality which means as aforementioned that foreign insolvency proceedings are recognized by the domestic courts.

The Regulation established a European framework for cross- border insolvency proceedings. It applies whenever the debtor has assets or creditors in more than one State, irrespective of whether he is a natural or legal person. The Regulation determines which court has jurisdiction to open insolvency proceedings and ensures the recognition and enforcement of the ensuing decision throughout the Union. It also establishes uniform rules on applicable law and provides for the coordination of main and secondary proceedings.<sup>23</sup> With respect to jurisdiction, the EU Regulation provides that the Member State where the debtor's "centre of main interests" (COMI) is situated shall have jurisdiction to open the main insolvency proceedings. The phrase Center of the debtor's main interests is not specifically defined, though the preamble of the Regulation states that COMI should correspond to the place where the debtor conducts the administration of his interests in a regular basis and is therefore ascertainable by third parties. In general, these criteria are fulfilled at the place where the debtor performs his business activities or where his main administration is located. The EU Regulation sets also a rebuttable presumption that the COMI is the country where the company's registered office is located, in the absence of proof to the contrary. These proceedings have universal scope with regard to both a) the insolvency estate b) the body of creditors. All assets of the debtor, regardless of the Member State where they are situated are subject to these proceedings; and all creditors are entitled to ( and obliged to) participate in them.<sup>24</sup> Moreover, the EU Regulation apart of the main proceedings opened in the place of COMI, gives the opportunity to open secondary or territorial insolvency proceedings in a Member State other where the COMI is, if the debtor has an "establishment" in that other State. The secondary insolvency proceeding are limited to the assets within the State of secondary insolvency proceedings and are governed by its domestic law. They aim to protect local creditors or they play an ancillary role to the main

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<sup>23</sup> Report from the Commission to the European Parliament, The Council And the European Economic and Social Committee 2012

<sup>24</sup> Francisco Garcimartin, The EU Insoveny Regulation: Rules on jurisdiction, [http://www.ejtn.eu/PageFiles/6333/Rules\\_on\\_jurisdiction.pdf](http://www.ejtn.eu/PageFiles/6333/Rules_on_jurisdiction.pdf)

insolvency proceedings. Another liquidator is appointed by the domestic courts of the State where the secondary proceedings are opened; although the liquidator of the main insolvency proceedings may intervene.

The Regulation introduces an exception of the general conflict of law rule which is as already mentioned, *lex concursus*. According to ar. 15 of the Regulation “the effects of the insolvency proceedings on 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 the lawsuit is pending” (*lex rei sitae*). Article 15 exclusively regulates procedural aspects.

Contrary to established rules of party autonomy in international arbitration, the Regulation, arguably, restricts the freedom of the arbitral tribunal to apply the choice of law rules chosen by the parties or that the arbitral tribunal deems are otherwise appropriate and replaces them with the mandatory choice of law rules provided for in the Regulation.<sup>25</sup>

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<sup>25</sup> Mark Robertson, *Cross Border Insolvency and International Arbitration Characterization and choice of law issues in light of Electrim SA ( in bankruptcy) v. Vivendi SA*, MLB thesis, Bucerius Law School, 2009

## CHAPTER II

### *Effects of insolvency in arbitration proceedings*

Insolvency law often may interfere with arbitration because it reflects different policy objectives. The underlying principle of insolvency as mentioned in Chapter I, is the equality of creditors, hence the centralization of claims, the high degree of state control and the mandatory substantive and procedural law provisions affecting the insolvent party's assets. On the other hand, arbitration is concerned with privity of contract and party autonomy.<sup>26</sup> As the US District Court held in the case *Societe Nationale Algerienne v. Distrigas Corp.* a dispute involving both bankruptcy and arbitration presents a conflict of near polar extremes: Bankruptcy policy exerts an inexorable pull towards centralization while arbitration policy advocates a decentralized approach towards dispute resolution.

Court jurisdiction is based on the power of nations which have the coercive power of state officials (coercive jurisdiction). By contrast, international arbitration is a private system which is based upon an agreement to arbitrate ("Consensual Jurisdiction").<sup>27</sup>

Where a party to an arbitration proceeding argues that the dispute is not arbitrable due to the insolvency of another party, the general rule is that the arbitral tribunal should, in principle, decide the issue with reference to the law which is applicable in the seat of arbitration (the *lex arbitri*). It may therefore be prudent for arbitral tribunals to take into account the law of the likely place of enforcement. Some commentators consider that key provisions of insolvency law (in particular those aimed at guaranteeing the equal treatment of creditors and the proper administration of the insolvent party's estate by the trustee) are considered mandatory provisions of domestic law (*lois de police* or *lois d'application imperative*), and sometimes are part of the domestic and international public policy of the state.

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<sup>26</sup> Domitille Baizeau, *Arbitration and Insolvency: issues of applicable law*, New Developments in International Commercial Arbitration 2009, Schulthess Editions Romandes

<sup>27</sup> Zack Clement Fulbright & Jaworski LLP, November 2006 Background Memorandum for the international insolvency institute's proposal to UNCITRAL concerning international insolvency/ arbitration, International Insolvency Institute Conference New York, USA, 2007

Since arbitral tribunals have no *lex fori*, it is suggested that they should not be concerned with the mandatory law provisions or the domestic public policy of the country of the seat. Such provisions should only be binding on the arbitral tribunal where they form part of the international public policy recognized by the law of the seat.<sup>28</sup>

The first task of a court asked to stay litigating pending arbitration is to determine if there is an arbitration agreement. If there is an arbitration agreement, then the court must consider whether the claims are arbitrable under the agreement.<sup>29</sup> Most jurisdictions provide debtors with some opportunity to discharge rescind or minimize contractual obligations subject to certain limitations.

### ***Validity of the arbitration agreement***

Vesna Lazic making a compare to Dutch, English, German and French law at her book *Insolvency Proceedings and Commercial Arbitration* concluded that the commencement of bankruptcy proceedings does not influence the validity of the arbitration agreement and that the prevailing view in Dutch, French and German literature.

In order the parties of an arbitration agreement to feel legal certainty, it is more appropriate to consider that the validity of an arbitration agreement should be examined and decided based upon the law chosen by the parties or if no such a choice has been made by *lex arbitri*. When the parties choose to resolve their disputes outside the state courts of the seat of arbitration, express their desire of the application of laws of another legal system. Thus by forcing them to accept the national laws that they have already exclude, sets aside their will and the purpose of arbitration.

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<sup>28</sup> Pr. Doug Jones *Insolvency and Arbitration: An arbitral tribunal's perspective*, INSOL ASIA PASIFIC RIM REGION ANNUAL CONFERENCE, 2011

<sup>29</sup> Mark Salzberg, Gary Zingraf, *When words collide: The enforceability of arbitration agreements in bankruptcy*, *Franchise law journal*, volume 27, number 1, Summer 2007

### ***Arbitrability of bankruptcy issues***

It is commonly accepted that insolvency issues are not arbitrable. Declaration of bankruptcy itself cannot be subject to arbitration because it concerns all the creditors of the debtor and not just the parties of the arbitration agreement (ICC AWARD No 9163, IDI 2005). Moreover, the effects of insolvency law cannot be subject to an agreement between the parties since insolvency law, in particular the European Insolvency Regulation, protects certain matters of public interest such as the equal treatment of creditors.<sup>30</sup>

However, for what kind of matters has jurisdiction an arbitral tribunal when insolvency procedures against one party have commenced and the arbitration is still on?

It is commonly accepted that the request made by a party before the arbitral tribunal, for the insolvency administrator to pay money or to release an asset would violate the principle of equality among creditors and would be against the collective centralized character of insolvency. Thus, an insolvency creditor may only ask the arbitral tribunal to determine that the creditor's claim is valid in order the creditor to register the claim in creditor's list before the bankruptcy court.

The French Supreme Court in *Jean X. v. International Company for Commercial Exchanges (Income)* held that "pursuant to French bankruptcy law, and as a matter of public policy, legal proceedings (including arbitration) against an insolvent party in bankruptcy proceeding should be stayed until the claimant has filed a declaration of its claim with the liquidator and, thereafter, legal proceedings should be limited to the validation and the quantification of claims"

### ***Legal capacity of an insolvent party regarding arbitration procedure***

The general rule is that every person who has the capacity to enter into a valid contract has also the capacity to conclude a valid arbitration agreement.

The personal law of a party will determine its capacity to enter into arbitration agreements and, consequently, its ability to be a party to arbitration proceedings. Capacity is related on the one hand with the capacity of an entity or a person to enter

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<sup>30</sup> Philipp Wagner When international insolvency law meets international arbitration  
Dispute resolution international vol 3 no 1 March

in an arbitration agreement on its own behalf and act as a party to arbitral proceedings and on the other hand it deals with the capacity of the party to enter into an arbitration agreement in the name and on behalf of another person or entity.<sup>31</sup> It may also affect the operability of the arbitration agreement.

The personal law of a corporation usually is the law of the state of the company's incorporation, real seat or COMI (center of main interests). As mentioned above the UNCITRAL and EU Regulation on Cross Border Insolvency follow the COMI approach. By definition there only can be one COMI, therefore only one lex concursus. A company cannot simply contract out of its personal law. As a result the effects of the insolvency of a corporation will have effect on the enforceability of the current contracts against the insolvent estate, including arbitration agreements or on pending arbitral proceeding to which it is a party, are highly related to the personal law of the corporation.

Article V (1) (a) of the New York Convention states that recognition and enforcement of an award may be refused if the parties to the agreement under the law applicable to them under some incapacity. From this provision it is clear that the NY Convention applies the personal law regarding the legal incapacity and not the law applicable to arbitration agreement. Vesna Lazic, though, argues that article V(1) (a) refers to the legal capacity of the party at the time entering the arbitration agreement and not at the time of or during the arbitration.

### ***Recognition of foreign insolvency proceedings by the arbitral tribunal***

Another question that arises is if the arbitral tribunal has to recognize foreign insolvency proceedings or only state courts have that competence. It is assumed, that when one refers to "foreign" insolvency proceedings and since the arbitral tribunal has no lex fori, means the proceedings opened outside the country of the seat of arbitration.

In most countries foreign judgments (including insolvency) are not automatically recognized by State courts. It is necessary to apply for recognition of the foreign

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<sup>31</sup> Abdulla, Z., in Kaufmann-Kohler, G. and Stucki, B (eds), International Commercial Arbitration in Switzerland: a handbook for practitioners, Kluwer Law International, The Hague, 2004

insolvency order pursuant to the private international law. Therefore, the arbitral tribunals may examine if the foreign insolvency decisions are capable to be recognized according to the law of the seat of arbitration. If the answer is negative, then the tribunal refuses to stay the arbitration.

The recognition of the foreign insolvency order shall be made in accordance with the rules of private international law of the State in which the procedure is pending. The situation seems to be clear in those countries that incorporated the UNCITRAL Model Law on Cross Border Insolvency or in EU Member States, where the recognition of the suspension provision follows from the application of the Insolvency Regulation.<sup>32</sup>

### ***Is the trustee bound by a previous arbitration agreement?***

Where a potential corporate respondent is under some form administration and is represented by a third party administrator, national legislation frequently provides that the administrator has the power to decide whether that respondent can be party to arbitration proceedings.<sup>33</sup>

What is common in the most if not all jurisdiction concerning the liquidation is that the debtor loses his possession over his assets and has no longer the right to dispose his estate. The consequence of dispossession is that the debtor lacks legal capacity to take actions concerning his estate and to sue or to be sued in the legal proceedings regarding the estate. These rights are “transferred” to the trustee. Consequently, after the commencement of bankruptcy liquidation, arbitral proceedings may be, in principle, initiated or continued only by or against the trustee, with respect to the property forming part of the estate. Arbitration agreements entered into by the debtor prior to the commencement of arbitration proceedings may be attempted to be invoked against the trustee and not the debtor. However, the proceedings aiming at

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<sup>32</sup> Alexander J. Bělohávek\* Impact of insolvency of a party on pending arbitration proceedings in Czech Republic, England and Switzerland and other countries

<sup>33</sup> Bird & Bird Insolvency in international Arbitration: a growing concern

the reorganization and rehabilitation of business do not necessarily have to entail dispossession.<sup>34</sup>

The administrator acts in his own name such as if he were the debtor's legal successor, so any claim against the debtor has to be directed against the insolvency administrator in person.<sup>35</sup> The main duty of the trustee is to secure the estate in order to fulfill the principle of equal treatment of the creditors. Therefore, usually the trustees hesitate to participate in arbitration proceedings.

However, most national jurisdictions consider that the arbitration agreement is not affected by the commencement of insolvency proceedings, though there are domestic laws providing for the exact opposite.<sup>36</sup> In any event the trustee will only be bound by the arbitration agreement if the subject matter of the dispute remains arbitrable in insolvency. As a general rule and with certain exceptions this is the case at least for most European jurisdictions.<sup>37</sup>

US Bankruptcy Code Section 365 states "the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor". There is no definition of what can be characterized as an executory contract. However, the majority of courts have adopted the definition of Pr. Countryman according to which an executory contract is the following: "A contract under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing performance of the other". An arbitration agreement could be characterized as an executory contract, therefore one could say that the trustee has the right to approve or reject it. Some scholars propose that the arbitration clauses should be considered as executory contracts, because the arbitration agreement obligates the parties to a future performance, as such they could be assumable or rejectable. The problem which arises when one follows this approach is that the

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<sup>34</sup> Vesna Lazic, Arbitration and insolvency proceedings : claims of ordinary bankruptcy creditors, *Insolvency Proceedings and commercial arbitration*, Chapter VI, Kluwer Law International, The Hague, The Netherlands

<sup>35</sup> Dr. Jan Kraayvagner, Dr Mark Hilgard, *The impact of general insolvency proceedings on international arbitration*, Mayer and Brown, 19-7-2010

<sup>36</sup> Philip Wagner,

<sup>37</sup> Stefan Kroll, *Arbitration and Insolvency in Loukas Mistelis/ Julian Lew (eds), Pervasive problems in international arbitration*, Alphen aan den Rijn, 2006

arbitration clause cannot be treated differently from the rest of the contract unless the arbitration agreement is considered an entirely separate contract. In *Prima Paint Corp. v. Flood & Conklin Mfg*, the US Supreme Court held that the arbitration clauses are separable from the agreements in which they are contained. This way, the arbitration agreements should be considered separate executory contracts for purposes of assumption or rejection under the Bankruptcy Code.

In England, on the other hand, the trustee is bound by the arbitration agreement if he decides to adopt the main contract.<sup>38</sup> If he does not adopt the main contract, it is the discretion of the state court whether or not to refer the parties to arbitration.<sup>39</sup>

In *Baytur SA v. Finagro*, the English Court of Appeal held that the assignee of all the assets of a party to arbitration did not automatically assume in the arbitral proceedings the role of assignor.<sup>40</sup>

In Germany, the insolvency administrator is bound by arbitration agreements and cannot set them aside. Though, according to German perspective, a creditor can only ask the arbitral tribunal to determine that his claim is valid, otherwise discrimination among creditors would be made.

The prevailing view in Dutch Literature is that the trustee is bound by an arbitration agreement entered into by the debtor prior to bankruptcy. A similar view is expressed in France, where arbitration is considered to be enforceable against the liquidator/administrator.<sup>41</sup>

### ***Cost of arbitration as reason to deny enforcement of arbitration agreement***

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<sup>38</sup> 349 A par. 1, Insolvency Act 1986

<sup>39</sup> Gabrielle Nater- Bass/ Olivier Mosimann, *Effects of Foreign Bankruptcy on International Arbitration*, Austrian Yearbook on International Arbitration 2011

<sup>40</sup> Sarah Walker, Alejandro Garcia, *Insolvency in international arbitration: a growing concern, An examination of the impact of the insolvent respondent in arbitration*, 2009, [www.twobirds.com](http://www.twobirds.com)

<sup>41</sup> Vesna Lazic, *Arbitration and insolvency proceedings : claims of ordinary bankruptcy creditors* <http://www.ejcl.org/33/abs33-2.html>

One could argue against the enforcement of arbitration agreements because the potential high cost of an arbitration procedure may preclude the debtor from effectively exercising his rights in the arbitral forum.

The US Supreme Court held in *Green Tree Fin. Corp – Alabama v. Randolph*, that though the arbitration agreement included in a consumer credit agreement was indeed valid and enforceable “the existence of large arbitration costs could preclude a litigant such as Randolph from effectively vindicating her federal statutory rights in the arbitral forum.”

Moreover, the Fourth Circuit in *Bradford v. Rockwell*, stated that “we believe that the appropriate inquiry is one that evaluates whether the arbitral forum in a particular case is an adequate and accessible substitute to litigation i.e. a case by case analysis that focuses among other things upon the claimant’s liability to pay the arbitration fees and costs, the expected cost differential between arbitration and litigation in court, and whether that cost differential is so substantial as to deter the bringing of claims .”

In addition, the German Federal Supreme Court Justice held that an arbitration agreement may be incapable of being performed, if the claimant lacks the financial means to initiate arbitration proceedings specifically as regards the payment of the advance on costs required under most arbitration laws and rules and provided that the respondent is not willing to forward the costs of the arbitration.<sup>42</sup>

The purpose of denying arbitration agreement’s enforcement because of the high procedural cost is the protection of the estate.

### ***Recognition- Enforcement of the arbitral award***

Arbitrators have the duty to render award which is enforceable. As aforementioned if an arbitral tribunal ignore a mandatory law or international public policy of the seat of arbitration there is a risk of annulment of the award.<sup>43</sup> It is commonly accepted that many of the provisions of bankruptcy law such as the automatic stay are mandatory law therefore should be respected by the arbitral tribunal if the tribunal wishes to render an enforceable award. Moreover, the principle of equality of creditors that

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<sup>42</sup> Philip K. Wagner When two words collide – the dilemma between insolvency and arbitration- yearbook on international arbitration vol II edited by Marianne Roth , Michael Geistlinger with the assistance of Marianne Stegner Antwerp, Copenhagen, Zurich, Vienna, Graz 2012

<sup>43</sup> Ge Yang, Insolvency proceedings and their effect on international commercial arbitration, University of Ghent

governs all insolvency proceedings could be considered as public policy. Thus, recognition and consequently enforcement of an award may be denied if such recognition would violate public policy.

However, under the New York Convention the enforcement courts have discretion; they may refuse recognition and enforcement, but will not necessarily do so, in particular where the courts are minded to promote and support international arbitration.<sup>44</sup>

### *Stay of arbitration proceedings*

Many insolvency laws include a mechanism for the protection of the insolvency estate which a) prevents creditors from commencing actions to enforce their rights through legal remedies during some or all the period of reorganization or liquidation and b) suspends actions already under way against the debtor. Such mechanisms they are usually called “suspension” “stay” or “moratorium”.<sup>45</sup>

The imposition of an automatic stay is seen as important not only to protect the debtor from undue harassment but also as an intra-director device designed to prevent creditors to gaining advantages over each other by pursuing unilateral collection efforts.<sup>46</sup> "Because the automatic stay serves the interests of both debtors and creditors," debtors generally cannot waive or limit its scope in pre or post-petition contracts (Acands, Inc. v. Travelers Cas. & Sur. Co.,)

In some jurisdictions public policy is relied upon as a basis for requiring a mandatory stay of arbitration against the insolvent party. Other jurisdictions leave decisions whether to stay arbitral proceedings to the arbitral tribunal's discretion. This latter

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<sup>44</sup> Domitille Baizeau, Arbitration and Insolvency: issues of applicable law, New Developments in International Commercial Arbitration 2009, Schulthess Editions Romandes

<sup>45</sup> Legislative guide on insolvency law- UNCITRAL, New York United Nations Publication 2005

<sup>46</sup> International insolvency law Paul . j. Omar 2008 Ashgate Publishing Limited England

view is more consistent with the terms of both the New York Convention and EU Regulation<sup>47</sup>

Few national law contain provisions which directly address the effect of insolvency proceedings on arbitration such as article 142 of Polish Bankruptcy and Reorganization Law article 487 of the Latvian CCP. In most systems the rights of a way at the crossroad of insolvency and arbitration have to be deduced from general provisions dealing with the effect of insolvency on proceedings before State Courts. Strong public interest involved in insolvency it is possible to establish hierarchy of provisions where in case of conflict the insolvency principles prevail.

There is a link between the stay of pending proceedings and the principle of equal treatment of the creditors in the bankruptcy proceedings, and this principle could be said to be part of public policy. In Italy the arbitration is not only suspended but the dispute is to be referred to the bankruptcy court, which excludes the powers of the arbitrators ( *vis attractiva*). The automatic stay of the arbitral proceedings is also advocated by authors in the Netherlands. Furthermore, decisions of the English Commercial court and the court of appeal illustrate that the principle of the preclusion of the individual actions by creditors may be disregarded by arbitrators and consequently also by national courts even if there is an international instrument on the recognition of foreign insolvency proceedings such as the EU Insolvency Regulation.<sup>48</sup>

## *USA*

In the United States, companies seeking bankruptcy protection generally remain bound by pre- existing international arbitration agreements. In general, the “automatic stay” provision of US federal bankruptcy law suspends all legal proceedings against the putatively bankrupt company, subject to court approval to permit particular proceedings to continue. In deciding whether to permit particular proceedings to go forward US courts generally require debtors to perform their arbitration agreements,

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<sup>47</sup> Gary Born, *International Commercial Arbitration*, Vol 1, Kluwer Law International, 2009, The Netherlands

<sup>48</sup> Jean Francois Poudret , Sebastien Besson, *Comparative law of international arbitration 2007*, Sweet & Maxwell London UK

particularly as to claims that do not involve “core” bankruptcy jurisdiction. USA Bankruptcy Act in article 157 makes a distinction between the core and non-core insolvency proceedings. The Act provides for a list which though is non exhaustive, of the core proceedings without defining what can be characterized as a core or non core issue. It is up to the bankruptcy court to decide case by case which issues are core and which non-core. These core issues cannot be arbitrated. In Germany according to the German Code of Civil Procedure, any claim involving economic interest can be subject to an arbitration agreement. Nevertheless, there are exceptions, where arbitration proceedings would conflict with the purposes of the Bankruptcy Code. It is sometimes argued that even if an arbitration agreement survives the bankruptcy of one of its parties and even if the parties’ disputes are arbitrable, any arbitral proceeding should be stayed as a discretionary matter.<sup>49</sup>

The source of arbitration law in the USA is the Federal Arbitration Act which states that “a court must stay its proceedings if it is satisfied that an issue before it is arbitrable under the agreement”.

The US Supreme Court has held that courts are generally obligated to enforce arbitration clauses absent a countervailing federal statute. However, the Bankruptcy Code is grounded on a policy of centralized dispute resolution. Different circuits have started to develop their own jurisprudence to determine when arbitration clauses should be enforceable in bankruptcy.<sup>50</sup>

#### *Shearson American Express Inc. v. Mc Mahon*

The Supreme Court fashioned a three- pronged test to determine whether a mandate may be overridden in the context of a statutory scheme. The McMahon Court addressed the arbitrability of claims arising from the Securities Exchange Act as well as the Racketeer Influenced and Corrupt Organization Act. With respect to these claims, issues were raised as to whether there was a strong federal policy that these

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<sup>49</sup> Gary Born, *International Commercial Arbitration*, Vol 1, Kluwer Law International 2009 The Netherlands

<sup>50</sup> Eva Kang, *Do arbitration clauses survive into bankruptcy? Lifting the automatic stay to compel debtors into arbitration.* CBLR Online, Vol. 13 Issue 2, February 2013

federal statutory claims may be litigated in federal court instead of being subject to arbitration. The Court noted that the policy in favor of arbitration is not diminished because the outcome of the subject matter is based on federal statutes. Instead, the mandate to arbitrate may only be overridden where there is conflicting congressional instruction within other statutes. A conflicting congressional instruction may be ascertained by 1) an examination of the text of the statute in controversy 2) a review of the legislative history of the statute or 3) finding an inherent conflict between arbitration and the statute's underlying purpose.<sup>51</sup>

This "inherent conflict" must be resolved by first recognizing that bankruptcy courts have jurisdiction and authority in all instances to determine if an arbitration agreement is enforceable in a particular proceeding. In turn, when called upon to enforce an arbitration agreement, bankruptcy courts must analyze the subject matter of a particular claim under the rubric of section 1334(c)(1) of title 28 and in the context of the particular bankruptcy case. Only after such analysis should the bankruptcy court determine whether to enforce the arbitration agreement or, conversely, require the parties to adjudicate the dispute as an adversary proceeding in a pending bankruptcy case. The "inherent conflict" between the federal bankruptcy statutory scheme and the FAA has its genesis in the United States Constitution, which expressly confers on Congress the powers to establish uniform laws on bankruptcy throughout the nation, create an inferior federal court system, and regulate interstate commerce.<sup>52</sup>

Shearson, the US Supreme Court held that the Federal Arbitration Act establishes a federal policy favoring arbitration and required courts to rigorously enforce agreements to arbitrate.

*Zimmerman v. Continental Airlines Inc.*

The Court concluded that the underlying purposes of the Bankruptcy Code impliedly modify the policies of the Federal Arbitration Act and that the enforcement of arbitration agreements in a bankruptcy procedure was to be left to the sound

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<sup>51</sup> In re Maureen Roberson US Bankruptcy Court for the District of Maryland 2010

<sup>52</sup> Patrick M. Birney Reawakening section 1334: Resolving the conflict between bankruptcy and Arbitration through an abstention analysis

discretion of the bankruptcy judge. This decision became the dominant rule in similar cases.<sup>53</sup>

The Zimmerman court found an "inherent conflict" between the FAA and Bankruptcy jurisdiction, and resolved it in favor of the latter. This conflict authorized the policies and purpose of the 1978 Bankruptcy Act and jurisdictional legislation—and the discretion of the bankruptcy courts—to override the legislative mandate of the FAA.<sup>54</sup>

Different approach was followed in later decisions of the US Courts especially after the adoption of “the Bankruptcy Amendments and Federal Judgeship Act of 1984” where the provision in Section 157 introduced a distinction between the core bankruptcy issues for which the only competent to adjudicate for is the bankruptcy judge and the non – core or related matters where the power of the bankruptcy judge is limited. Regarding the non core issues, the bankruptcy judges are competent to hear and to issue findings of fact but they lack competence to issue final orders.

As Vesna Lazic has noted, the creditors’ claims will always fall under the core category as they are considered either as a matter of allowance or disallowance of claims or as a cause for relief from an automatic stay under Section 362.

*Hays and Co. v. Merrill Lynch, Pierce, Fenner and Smith, Inc.*

After the Act of 1984, the same Third Circuit decided in *Hays & Co. v. Merrill Lynch* that the Zimmerman theory was no longer applicable, and it was proper to enforce an arbitration clause in a non-core bankruptcy proceeding. The Third Circuit Court of Appeals held that a bankruptcy trustee was bound by an arbitration clause contained in the debtor’s prepetition contract. In so holding, the court ruled that a lower court is required to enforce arbitration of "non-core" claims brought by the trustee unless the trustee can demonstrate that the purpose of the Bankruptcy Code somehow conflicts with the enforcement of an arbitration clause. The Court held that there is no discretion for the bankruptcy courts when deciding on the enforcement of arbitration

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<sup>53</sup> Vesna Lazic, *Arbitration and Insolvency Proceedings, Insolvency Proceedings and International Commercial Arbitration*, Chapter VI, Kluwer Law International, The Hague, The Netherlands, 1998

<sup>54</sup> Patrick m. Birney *Reawakening section 1334: Resolving the conflict between bankruptcy and Arbitration through an abstention analysis*

agreements in non- core matters, unless it is proved that the text, legislative history or the purpose of the Bankruptcy Code conflicts with the enforcement of an arbitration clause.

Some Courts held that the reasoning in *Hays* denied discretion in non- core matters while implied that it was to be retained in disputes involving core matters.

Even in core matters, the bankruptcy court may lack discretion to override an arbitration agreement unless it finds an inherent conflict between the nature of the claims or rights asserted in Federal Arbitration Act or that arbitration would jeopardize the objectives of the Bankruptcy Code.

When considering whether to compel arbitration in bankruptcy cases, bankruptcy courts in the Second Circuit consider four factors: 1.) whether the parties agreed to arbitrate; 2.) the scope of the arbitration agreement; 3.) whether, if federal statutory claims are at issue, Congress intended those claims to be non-arbitrable; and 4.) whether the entire proceeding should be stayed pending arbitration if only some of the claims at issue are arbitrable. Courts applying this analysis, and particularly when considering the first and third factors, are swayed by whether the matter in question is "substantially core," or, in other words, a central function of the multi-party bankruptcy process. Further, even if a core matter is arbitrable under this analysis, bankruptcy courts may exercise their discretion to deny an arbitration demand if the matter is unique to bankruptcy cases, and the proceedings are a core bankruptcy function invoking substantial rights under the Bankruptcy Code and conflict with resolution by arbitration.<sup>55</sup>

A matter falls within a bankruptcy court's "core" jurisdiction if it either invokes a substantive right created by federal bankruptcy law or could not exist outside of a bankruptcy case. By contrast, "non-core" matters generally involve disputes that have only a tenuous relationship to the bankruptcy case and would in all likelihood have been litigated elsewhere but for the broad nexus created by the debtor's bankruptcy filing. For example, a contract dispute between the debtor and a third party is a non-core matter. The distinction between core and non-core matters is a crucial, yet not

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<sup>55</sup> United States: bankruptcy court refuses to send cash collateral dispute to arbitration article by Michael A. Stevens and Michele C. Maman [www.mondaq.com](http://www.mondaq.com)

necessarily determinative, one in defining a bankruptcy court's discretion when confronting an arbitrable dispute.<sup>56</sup>

*MBNA American Bank, NA v. Hill*

The Court did not follow the core/ non- core distinction entirely but held that the distinction does not necessarily confer bankruptcy court discretion only the potential for bankruptcy court discretion. According to the Court, *the bankruptcy Court has discretion to waive arbitration agreements in core proceedings only if it finds the proceedings are based on provisions of the Bankruptcy Code that "inherently conflict" with the Arbitration Act or that arbitration of the claim would necessarily jeopardize the objectives of the Bankruptcy Code.*

Under the Federal Arbitration Act par.2 arbitration agreements shall be valid, irrevocable and enforceable save upon such grounds as exist at law or in equity for the revocation of any contract. This mandatory enforcement cannot be overridden absent strong congressional intent ( Shearson, Societe Nationale Algerienne). It is well settled that in order to overcome the strong federal policy in favor of arbitration, the burden is on the party opposing arbitration to show that arbitration is not warranted.

*Mintze v. American Financial Services*

The Court held that the bankruptcy court had no discretion to refuse to compel arbitration. Moreover, although there was a core proceeding, there was no inherent conflict between arbitration and the underlying purposes of the Bankruptcy Code, because the claims were not created by the Bankruptcy Code.

*Electric Machinery Enterprise Inc*

The bankruptcy court may deny enforcement of an arbitration clause when the claim sought to be arbitrated is a core claim and the arbitration will interfere with the bankruptcy process or affect rights granted by the Bankruptcy Code However, the court observed that "even if a proceeding is determined to be a core proceeding, the bankruptcy court must still analyze whether enforcing [the] arbitration agreement would inherently conflict with the underlying purposes of the Bankruptcy Code. Like

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<sup>56</sup> Jones Day Publications When the federal arbitration act and the bankruptcy code collide, JULY 2002 <http://www.jonesday.com/when-the-federal-arbitration-act-and-the-bankruptcy-code-collide-07-02-2002/>

the Eleventh Circuit, the Second Circuit concluded that even as to core proceedings, the bankruptcy court will not have discretion to override an arbitration agreement unless it finds the proceedings are based on provisions of the Bankruptcy Code that “inherently conflict” with the Arbitration Act or that arbitration of the claims would “necessarily jeopardize” the objectives of the Bankruptcy Code<sup>57</sup>

*In Re Hostess Brands Inc*

The court held that substantially core proceedings or those that are truly a function of the bankruptcy process are less likely to be arbitrated. The court also emphasized the fact that allowing arbitration would reduce the proceeding to a two- party dispute whereas keeping the proceeding within the bankruptcy court would provide other interested parties with notice of hearings and the right to intervene. The decision reflects a view that emphasizes the multi party aspects of bankruptcy. If a debtor were to try and enforce arbitration of their disputes with the debtor, it would quickly lead to deterioration of the bankruptcy process.<sup>58</sup>

*Microblit Corp. v. Fidelity National Information Services Inc.*

The Court allowed certain claims, including claims related to the violations of the automatic stay, to be subject to binding arbitration rather than being resolved in the bankruptcy court. The court concluded that as long as a valid agreement to arbitrate exists and the dispute falls within the scope of the agreement, the court must refer the case to arbitration without reviewing the merits. Because of the disputed conduct did not give possession or control over the debtor’s assets on advance their interests over competing creditor constituencies, the court determined that arbitration of the stay violation claims would not impede the administration of the bankruptcy estate.<sup>59</sup>

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<sup>57</sup> Mark Salzberg, Gary Zingraf, When words collide: The enforceability of arbitration agreements in bankruptcy, Franchise law journal, volume 27, number 1, Summer 2007

<sup>58</sup> Eva Kang, Do arbitration clauses survive into bankruptcy? Lifting the automatic stay to compel debtors into arbitration.CBLR Online, Vol. 13 Issue 2, February 2013

<sup>59</sup> Eva Kang, Do arbitration clauses survive into bankruptcy? Lifting the automatic stay to compel debtors into arbitration.CBLR Online, Vol. 13 Issue 2, February 2013

In general, it can be said that the claims of ordinary creditors are core bankruptcy matter and therefore the pending arbitration and litigation proceedings have to be suspended.

Assuming the parties have agreed to arbitrate a particular dispute, a bankruptcy court must then determine whether it has discretion to adjudicate it. If the dispute represents a non-core matter, the bankruptcy court will lack this discretion. If the matter is core, the court cannot refuse to compel arbitration without performing further analysis. It must first evaluate the nature and reason for the dispute's "coreness." If a proceeding is core only as a matter of procedure (e.g., it arguably has some impact on the liquidation of the assets of the bankruptcy estate or the adjustment of the debtor-creditor relationship, but nothing more), the enforcement of an arbitration clause will likely not conflict with the policy of the Bankruptcy Code, and the bankruptcy court should defer to arbitration. On the other hand, if a proceeding is core as a matter of substance, i.e., the dispute involves rights created under the Bankruptcy Code, the parties likely did not agree (or could not have agreed) to arbitrate the dispute and the bankruptcy court retains the discretion to refuse to compel arbitration. Finally, given the important policy considerations favoring the arbitration of disputes between parties who have agreed to arbitrate, any waiver of that right must be unequivocal and will be subjected to strict scrutiny by the courts.<sup>60</sup> Under the framework established by the Bankruptcy Code and the federal statutes governing the jurisdiction of the bankruptcy courts, virtually all disputes concerning the debtor are to be resolved by the bankruptcy court. An arbitration clause instead requires any issue within its scope to be resolved in an arbitration forum. Neither the Bankruptcy Code nor its legislative history contains any reference to an exception to the FAA. As a result, courts considering whether to enforce an arbitration clause in the bankruptcy context have focused on the third prong of the McMahon test, namely, whether there is an inherent conflict between the Bankruptcy Code and the FAA. In applying the inherent conflict test, many courts have concentrated upon whether the claim sought to be arbitrated is "core" or "noncore." Core proceedings involve matters that arise either under the Bankruptcy Code or only in bankruptcy cases.

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<sup>60</sup> Jones Day Publications When the Federal Arbitration Act and the bankruptcy code collide, July 2002 <http://www.jonesday.com/when-the-federal-arbitration-act-and-the-bankruptcy-code-collide-07-02-2002/>

Unfortunately, neither the Bankruptcy Code nor any of its related statutory provisions define exactly what a core proceeding is. Instead, 28 U.S.C. § 157 contains a nonexclusive list of fifteen core matters. These fall into four general categories: (a) proceedings concerning the administration of the estate, (b) proceedings involving the trustee's or debtor-in-possession's avoidance powers, (c) proceedings involving property of the estate, and (d) a catchall category. The statute itself neither defines nor provides examples of noncore proceedings. Instead, a noncore proceeding is generally defined as a proceeding other than a core proceeding that is "otherwise related to a case under title Courts will allow arbitration of noncore claims because arbitration of these claims will not interfere with the Bankruptcy Code or its objectives or policies.

### *England and Wales*

The formal insolvency regime in England and Wales is governed by the provisions of the Insolvency Act 1986, related legislation, UNCITRAL Model Law and EU Regulation on Insolvency Proceedings. When an entity enters either compulsory liquidation or administration, proceedings against that entity are automatically stayed. It is commonly accepted that the stay of proceedings extends to arbitration proceedings as well.

Under the insolvency act Section 130(2) a party must make an application for court permission to bring against a company in compulsory liquidation. The general practice is that the application will be granted unless the claim can be dealt more efficiently in the liquidations proceedings. Where a moratorium is imposed a party that wants to bring or continue with an arbitration against the insolvent company can only do so with the permission of the court. The English court in the case *A Straume Ltd v. Bradlor Developments Ltd* has held that the moratoria include arbitration proceedings.

#### *Atlantic Computer Systems Plc*

The guidelines for when a court will grant permission were set out in this decision: a) there must be a good case made out by the applicant, b) if the question relates to proprietary rights and will not affect the administration the application is normally granted c) otherwise the court must conduct a balancing exercise of the parties' interests d) in the balancing exercise the interests of proprietary creditors outweigh the interests of unsecured creditors and e) the court will not make the decisions on the

validity of security unless it is very straightforward. A liquidator may at his own volition commence or continue claims in the insolvent's company name.<sup>61</sup>

### ***Spain***

According to the Spanish Bankruptcy Law which refers to domestic arbitration, an arbitration agreement to which a debtor is a party shall not remain valid and effective while bankruptcy is open save the provisions of international treaties. On the other hand a declaration of bankruptcy does not suspend the arbitration proceedings which will continue until the award is rendered.

### ***France***

French arbitration law contains an express provision on the interruption of arbitration proceedings. Certain principles and provisions of insolvency law such as the principle of suspension of individual actions by creditors in relation to insolvency have been considered to be part of domestic and international public policy, the violation of which presents a reason for the setting aside of an arbitral award such as the principle of permission of individual actions (respected outside the jurisdiction where the insolvency procedures have been opened is not necessarily guaranteed) dispossession of the debtor, interruption of proceedings, equality among debtors.

Moreover, the French Code of Civil Procedure (art. 369) includes provisions according to which when an order commencing insolvency proceedings is issued, the pending proceedings must be interrupted. This is a principle not only of French but also of international public policy ( Cass civ 1, 2009, 08-10281, Bull 2009 I no 86).

After the declaration of the claim in bankruptcy the pending arbitration proceedings is assumed that they may be continue without the order/ allowance of the court. Such a view may be problematic in relation to the enforcement of the award which may be annulled for reasons of public policy (stay of individual actions).

Once insolvency proceedings are opened against one party the arbitration tribunal can only render a declaratory award and cannot order the insolvent estate to pay from its assets.<sup>62</sup>

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<sup>61</sup> James Hargrove and Vanessa Liborio, *Arbitration and insolvency: English and Swiss perspective*, 2009 Sweet & Maxwell, London, UK

## ***Brazil***

The Brazilian Supreme Court of Justice in its decision concerning the case *Interclinicas v. Saude ABC* held that the arbitral clause in the underlying transaction was valid and enforceable because the clause had been agreed between the parties before *Interclinicas* commenced winding up proceedings. Moreover, the Court emphasized that the company's participation in the arbitration represented no risk to any public interest related to the winding up proceedings, particularly since the rights of the liquidated company could be adequately protected during the arbitration.

In the case *Jackson Empreimentos v. Diagrama Construtora*, the Sao – Paolo Court of Appeals authorized the inclusion of a claim awarded by an arbitral tribunal in bankruptcy proceedings involving the debtor despite the opposition of the court appointed bankruptcy administrator to the arbitration. The Court held that the parties were fully capable of executing arbitration agreements at the time that the underlying contract was signed and the supervening facts such as the company's bankruptcy cannot retroactively annul a validly executed and legally enforceable clause. The aforementioned cases demonstrate the trend to uphold arbitration agreements during insolvency proceedings and to respect the arbitrator's ability to decide in their own competence.<sup>63</sup>

## ***Germany***

German insolvency law follows the principle of universality pursuant to EU Regulation on Insolvency Proceedings and to Sec.335 et seq. of the German Insolvency Code. In other words, German Insolvency Law demands recognition in any other jurisdiction. Therefore, the arbitral tribunal should recognize the German Insolvency proceedings. If they do not, there is a risk that any arbitral award would violate German public policy and therefore would not be enforceable in Germany. A conflict, though, may arise if the jurisdiction applicable at the seat of arbitration follows the principle of territoriality and therefore does not recognize the German

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<sup>62</sup> Poudret, Jean-François, Besson Sébastien, Ponti, Annette, *Comparative Law of International Arbitration*, Sweet & Maxwell, London, 2007

<sup>63</sup> Arbitration and Insolvency Proceedings: Recent Developments 2008 Fernando Eduardo Serec, Antonio M Barbuto Neto ,[www.internationallawoffice.com](http://www.internationallawoffice.com)

Insolvency proceedings. German insolvency law does not affect the validity of arbitration clauses the insolvent debtor entered into with creditors. Therefore, in principle, any creditor can file arbitral proceedings while insolvency proceedings are pending not against the debtor but against the administrator. A motion requesting the insolvency administrator to pay a certain amount of money would discriminate against the competing insolvency creditors. Therefore, an insolvency creditor can only ask the arbitral tribunal to determine that the creditor's claim is valid.<sup>64</sup>

### ***Russia***

The trend is that once insolvency proceedings commence, all claims have to be resolved and judged by a court in Russia. The purpose is to prevent bankruptcy creditors obtaining any priority or privileged position in relation to the parties to the arbitration proceedings seeking to enforce their rights and vice versa. That is, as soon as insolvency proceedings are commenced in respect of a Russian corporation, arbitration clauses and agreements that the insolvent company is a party to become void. All the claims then have to be transferred. Once the company declared bankrupt, all claims against the company have to be filed with the *arbitrazh* court handling the bankruptcy proceedings. Under article 33 of the Russian Federation Law on insolvency, the competent court in such case is the judicial district where the respondent is domiciled. Enforcement of arbitral awards issued prior to bankruptcy has to be sought in the same courts. The award remains valid despite the bankruptcy. The fate of pending arbitration filed prior to bankruptcy but the award is not rendered yet remains unsettled.<sup>65</sup> In the case *Slovenska Konsolidachna AS v. KB SR Yakimanka* the Court following the aforementioned approach held that the adjudication of claims against a bankrupt company is within exclusive jurisdiction of a national court seized with bankruptcy proceedings and when the arbitration proceedings are initiated after the commencement of bankruptcy proceedings, the enforcement of the award would contravene public policy.

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<sup>64</sup> Dr. Jan Kraayvagner, Dr. Mark Hilgard, 2013, *The Mayer Brown Practices*, [www.mayerbrown.com](http://www.mayerbrown.com)

<sup>65</sup> Interpretation of Article V of the NY Convention by Russian Courts, Ilya Nikiforov, *Journal of International Arbitration*, Kluwer Law International 2008, Vol 25 Issue 6

## *Australia*

In Australia the only guidance concerning the insolvency law- arbitration conflict is the Corporations Act 2001- Section 440D, where the section provides an automatic stay against commencing or continuing proceedings against a company in administration. As the term proceeding is not defined by the Act, the application of this provision in relation to arbitral proceedings, depends on whether such proceedings fall within the interpretation of “a proceeding in a court”. In the case *Auburn Council v. Austin Australia Pty Ltd*, the judge closely considered the matter and held that arbitral proceedings are not proceedings in the court. Therefore, arbitration under the Commercial Arbitration Act of any State or Territory will not be automatically stayed on the appointment of an administrator and no leave of the court is required to commence or continue arbitral proceedings against a company in administration.<sup>66</sup>

## *Singapore*

In the case *Petroprod Ltd*,<sup>67</sup> Justice Tan Lee Meng referred to s11(1) of the International Arbitration Act and held that when a court is asked to exercise its discretion to grant a stay under s6 of the Arbitration Act, it should take into account the general concept that any dispute which the parties have agreed to submit to arbitration under an arbitration agreement should generally be determined by arbitration unless it is contrary to public policy to do so. In that context, the court looked at the underlying policy behind the avoidance claims being made by Petroprod in the substantive proceedings and held that the rights created by avoidance provisions exist for the benefit of the general bodies of creditors in insolvency or insolvency related context.

Justice Tan Lee Meng took the view that the policy underlying the avoidance provisions in question would be compromised if their enforcement were subject to private arrangements, including an agreement to arbitrate between the company and the wrongfully advantaged creditor or transferee. On that basis, Larsen's application to stay the proceedings in favour of arbitration was dismissed.

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<sup>66</sup> Pr. Doug Jones Insolvency and Arbitration: An arbitral tribunal's perspective, INSOL ASIA PASIFIC RIM REGION annual conference, 2011

<sup>67</sup> *Larsen Oil and Gas Pte Lts v. Petroprod Ltd* 2011

### ***The Netherlands***

According to the Dutch Bankruptcy Law, after the opening of insolvency proceedings, the claims for payment against the estate can only be asserted in verification proceedings.

### ***Vivendi v. Electrim***

In 2006, Vivendi and certain of its subsidiaries initiated arbitration under the ICC Rules against Deutsche Telecom AG and other companies including Electrim S.A which is a Polish company.

The Electrim decision is short, therefore very little information are given regarding the facts of the case or the parties' arguments and positions. However, the seat of arbitration was Geneva. In August 2007, Electrim was declared bankrupt in Poland. According to article 142 of the Polish Bankruptcy Law "any arbitration clause concluded by the bankrupt shall lose its legal effect as at the date that bankruptcy is declared and any pending arbitration proceedings shall be discontinued". Electrim, based on this article asked the discontinuation of the pending arbitration proceedings.

The arbitral tribunal considered that this article of the Polish Bankruptcy law, creates lack of subjective capacity (*ratione personae*) of Electrim to participate in the arbitration proceedings. Because this was a matter of legal capacity the arbitral tribunal had to take into consideration the general laws on conflicts of law of the Private International Law Act (PILA). According to this, the capacity of a legal entity is governed by the law of its place of incorporation (ar. 154 and 155). Therefore, the arbitral tribunal held that the place of incorporation of Electrim was Poland and Polish Law should be applied. As a consequence, the arbitration proceeding were discontinued against Electrim. The Swiss Federal Supreme Court confirmed the award. Moreover, the Supreme Court held that from the moment that PILA is silent about the legal capacity to arbitrate of non State parties, then the personal law of the parties should determine this matter.

However, in this case the Swiss perspective falls in legal blanks and controversies.

It is difficult to understand the rationale of a regulation whereby both a trustee and its creditors are deprived of the possibility to opt for resolving a dispute by arbitration,

even when the advantages of such a choice would be obvious such for example the situation where there is a claim on behalf of the estate against the third party. The relevant provision of Polish law renders an arbitration clause invalid *ex lege* depriving the trustee of the right to pursue such a claim in arbitration even though the creditors could benefit. Moreover, pending arbitration proceedings are *ex lege* terminated even if they are in an advanced stage and money and time have been both spent.<sup>68</sup>

The question that arises regarding the Polish provision is if the rule concerns legal capacity, the validity of the arbitration agreement, or the effects of bankruptcy on a pending lawsuit.

First of all, the provision of the PBL nowhere refers to the bankrupt's capacity to arbitrate or to the capacity of the estate to arbitrate. The provision simply refers to the effect of the declaration of bankruptcy and the continuance of pending arbitration proceedings. Even if the aim of art 142 of the PBL had been to exclude arbitral jurisdiction over insolvent Polish parties it does not follow that the issue is one of capacity. It could just easily be an issue of validity of the arbitration agreement or of subject matter arbitrability. In addition, according to PILA, an arbitration agreement would be valid if it would conform to the least demanding of a) the law governing the subject matter of the dispute, b) the law chosen by the parties or c) the Swiss law. Given that PBL has to do with the termination of effects of arbitration agreements concluded by a party who is declared bankrupt, it would be more accurate to characterize this legal issue as a matter of validity. As aforementioned, under PILA an arbitration agreement is valid if it is valid under one of these three laws mentioned above. Therefore, an arbitral tribunal seated in Switzerland should apply Swiss law, uphold the arbitration agreement and continue the arbitration proceedings.<sup>69</sup>

Abundant arbitral case law (ICC 2139, ICC 11714, ICC 10507) other than *Electrim* has repeatedly considered the arbitral tribunal to be unaffected by the sudden bankruptcy of a party pursuant to the *lex arbitri* notwithstanding foreign bankruptcy legislation aiming to affect the arbitration agreement or the bankrupt party's legal

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<sup>68</sup> Vesna Lazic, *Cross border Insolvency and Arbitration, Which consequences of insolvency proceedings should be given effect in arbitration?* Chapter 18, *Liber Amoricum* Eric Bergstenpg 343

<sup>69</sup> Gabriel Kaufmann- Kohler, Laurent Levy, Sabina Sacco, *The survival of the arbitration agreement and arbitration proceedings in cases of cross border insolvency : an analysis from the Swiss Perspective,* *The Paris Journal of International Arbitration*, 2010 Vol 2 Lextenso editions

capacity. This is in line with the parties' expectations that the validity of the arbitration agreement and the jurisdiction and the jurisdiction of the arbitral tribunal are governed by the chosen law or the law of the seat of arbitration, but not by the law of the place of incorporation, unless this later qualifies as *loi d' application immediate*.<sup>70</sup>

On the other hand, the English perspective on the same matter is completely different. In 2003, Vivendi had commenced LCIA arbitration proceedings against Electrim and others with its seat of arbitration London. As aforementioned, Electrim was declared bankrupt in August 2007 and again invoked the Polish Bankruptcy Code asking for discontinuation of the arbitration proceedings. Contrary to the Swiss Arbitral tribunal the LCIA decided that the English law governed the issues and not the Polish one, and according to the English law the arbitral tribunal had jurisdiction to arbitrate despite Electrim's bankruptcy. The English High Court confirmed the award.

The arbitral tribunal and the English High Court were based on the EU Regulation on Cross- Border Insolvency which in article 15 states "the effects of insolvency proceedings on a lawsuit pending concerning an asset or a right of which a debtor has been divested shall be governed solely by the law of the Member State in which that lawsuit is pending".

The English High Court confirmed that the lawsuit pending included pending arbitral proceedings and thus the arbitral tribunal had correctly applied English law to determine the effect of Electrim's insolvency on the pending arbitration. Arbitration agreements that relate to future, non pending arbitral proceedings constitute current contracts for the purposes of art. 4.2(f) of the EC Regulation and are thus governed by the *lex concursus* while arbitration agreements that relate to existing pending arbitration proceedings are covered by the exception in ar. 4.2 (f) and 15 of the EU Regulation.<sup>71</sup>

Moreover, According to Miguel Virgos and Francisco Garcimartin the Insolvency Regulation does not make any express reference to the effects of the insolvency proceedings on lawsuits pending before arbitral tribunals in Member States. Arbitration is not excluded from the general effects of *lex concursus* under Art. 4 and the literal wording of Art. 15 is broad enough to include arbitration in the exception it

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<sup>70</sup> Gabrielle Nater- Bass/ Olivier Mosimann, *Effects of Foreign Bankruptcy on International Arbitration*, Austrian Yearbook on International Arbitration 2011

<sup>71</sup> Syska and another v. Vivendi Universal SA and others 2008, EWHC 2155

provides to the application of that law. Arbitration proceedings are equivalent substitutes to ordinary legal proceedings in all Member States, and there is no substantive or procedural reason justifying a different solution.<sup>72</sup>

Vivendi's attempt to enforce the award rendered by LCIA was unsuccessful at first, but the Warsaw Court of Appeal finally granted the recognition and enforcement of the award.

However, the Swiss Federal Supreme Court (decision 4A\_50/2012) had to face the same argument regarding the lack of capacity of the insolvent party to participate to arbitration proceedings as was the case in *Vivendi v. Electrim*. The dispute this time concerned a Chinese company and a Portuguese insolvent company who had entered into an arbitration agreement choosing Geneva as seat of arbitration. The arbitral tribunal held that according to provisions of PILA, the insolvent legal entities retain their legal capacity and they may still participate in arbitration when it becomes insolvent. Article 87 of PILA does not use the term "legal capacity" but "efficacy of arbitral agreements", addressing the validity of the arbitration clause which is an issue of *lex arbitri*. The Supreme Court rejected the challenge of the award made by the Portuguese company, reaffirming that the question of legal capacity is determined by the law of the place of incorporation while the validity of the arbitration clause by the *lex arbitri*.<sup>73</sup> The Swiss Supreme Court in this case stated that the insolvency of a party does not affect the arbitral tribunal's jurisdiction.

### *Conclusion*

As aforementioned, bankruptcy is based on a policy of centralization while arbitration is based on exactly the opposite, on a policy of decentralization.

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

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<sup>72</sup> Miguel Virgós/Francisco Garcimartín, *The European Insolvency Regulation: Law and Practice*, The Hague 2004

<sup>73</sup> Georg von Segesser, *X v. Y* Federal Supreme Court of Switzerland, 1st civil law chamber, 16 October 2012, A contribution by the ITA Board of Reporters, Kluwer Law International, [www.kluwerarbitration.com](http://www.kluwerarbitration.com)

contract law.<sup>74</sup> After the commencement of bankruptcy proceedings any non secured creditor may only pursue his payment claim against the state before the bankruptcy court. Claims of ordinary non- secured, non preferred creditors are dealt with in a single, collective procedure, since these claims are in the very essence of the bankruptcy procedure.<sup>75</sup>

When a court faces the dilemma to compel arbitration or not has to answer two basic questions; first, is there an agreement by the parties to arbitrate and second, does the Court have the discretion to deny arbitration?

It can be said that the effects of insolvency proceedings should be recognized outside the jurisdiction where such proceedings are opened and respected by arbitrators, when they are of such a nature that serve the purposes and objectives of the insolvency laws which are generally accepted. The principles of the preclusion of individual actions and of the equal treatment of the non- secured creditors may be mentioned as examples. The same is true with respect to other principle intended to maximize the assets and to distribute the estate in an orderly fashion or reorganize the business, as the case may be.<sup>76</sup>

The effect of core, non- core distinction in the arbitration context is that a bankruptcy judge has exclusive jurisdiction over the issue if it is a core proceeding. However, if an issue is a non- core proceeding then the bankruptcy judge has discretion to hear the case or refer it to another appropriate forum.<sup>77</sup> Generally, one could say that noncore ( non pure) insolvency matters most of the times are non arbitrable.

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<sup>74</sup> Kroll, "Arbitration and Insolvency Proceedings" IN Mistelis and Lew (EDS), " pervasive problems in international arbitration (2006), P.374

<sup>75</sup> Vesna Lazic, Arbitration and Insolvency proceedings claims of ordinary bankruptcy creditors, Insolvency and Arbitration Proceedings, Chapter VI, Kluwer Law International, 1998

<sup>76</sup> V. Lazic cross border insolvency and arbitration: synergy, convergence and evolution: liber , international arbitration and international commercial law , 2011 Kluwer Law International , The Netherlands

<sup>77</sup> Matthew Dameron, Stop the Stay: Interrupting Bankruptcy to conduct arbitration- Slipped Disc Inc v. CD Warehouse Inc., Journal of Dispute Resolution, Vol 2001, Issue 2, No 2, Article 5

Regarding the effects of insolvency on arbitration proceedings and how the issues which arise can be settled, there is no clear answer from the moment that national laws vary from country to country and no universal uniformity exists. However, UN Model Law on Cross Border Insolvency and EU Regulation may lead to the adoption of a uniform common approach for the courts when confronting relevant issues.