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# Exceptions to the *lex fori concursus* – ongoing arbitral proceedings

**Contribution of GRIP 21**

## I. Introduction

1. The working documents of UNCITRAL Working Group V (Insolvency Law) contain some significant points, which merit examination from the comparative perspective of the draft texts and the principles of French law.

## II. General comments

2. The distinction made among the three phases mentioned (arbitration agreement, arbitration proceedings and enforcement of the award) is relevant.

3. Similarly, a distinction is warranted between the law chosen by the parties (for the arbitration *per se*) and the law of the seat of the arbitral tribunal (the legal place of arbitration for procedural matters although the law where the arbitration physically takes place, if it does not coincide with the State where the tribunal is seated (legal place of arbitration), may also have an effect on certain procedural aspects such as the summoning of witnesses, etc. ...).

4. This should enable the UNCITRAL working group to draw up a matrix for each of the three phases (agreement, procedure and enforcement) with proposals for the applicable law.

## III. Comments on the application of the *lex fori concursus* in arbitral matters

5. As far as the arbitration agreement is concerned, the arbitral law should undoubtedly govern for its definition and validity, while introducing an additional distinction, depending on whether the debtor party to the arbitration proceedings is in possession or divested.

6. Indeed, in point 22 (WP. 190, p. 20 (EN)) the reference to the New York Convention (which requires the courts of the States parties to give full effect to

arbitration agreements by referring parties to a dispute in breach of their arbitration agreement to the law of arbitration) does not address the situation of the insolvent debtor (in possession or divested).

7. Furthermore, it might also be useful to include this sub-distinction at all stages in the draft legislative provisions.

8. The draft legislative provisions also include arbitration agreements within the category of "treatment of contracts (...)" in point 1 (h) (WP. 190, p. 1 (EN)).

9. An arbitration agreement should not, in our view, be classified as a "contract" in this sense as it is an agreement limited to the arrangements for settling a dispute and not a contractual framework relating to the provision of services to or by the debtor.

10. In this respect (see below), the comparison should undoubtedly be made with a pending individual lawsuit, especially as the arbitration award is essentially equivalent to a court judgment and is therefore distinct from a contract containing an arbitration clause.

# IV. Comments on exceptions to the *lex fori concursus* in arbitral matters

## 1. General comment

11. As regards the enforcement phase of an arbitration award, the *lex fori concursus* should govern, unless the law of the place of enforcement applies, because of the mandatory rule of the stay of proceedings arising from the opening of insolvency proceedings and public policy.

12. The procedural situation of an ongoing arbitration proceeding and its procedures requires specific consideration, since here the arbitration proceeding and the *lex fori concursus* must be combined; a pure and simple reference to the law of the arbitration only is not satisfactory (a similar remark could be made for a pending lawsuit), as is the case with the UNCITRAL redrafting proposal submitted to the next meeting of the working group:

> "The effects of insolvency proceedings on [*any limits of the scope of application of this exception, as may be agreed upon by the Working Group*] of ongoing arbitral proceedings concerning the insolvency estate that is administered in that insolvency proceeding shall be governed by the lex arbitri."

13. In our view, a distinction should first be made according to the debtor's situation and the type of proceedings.

14. The solution would be different:

(a) Depending on whether the debtor is in possession or divested;

(b) According to its procedural status, as plaintiff or defendant;

(c) According to the rules of the insolvency proceedings opened.

## 2. If the exception to the *lex fori concursus* is to be retained, but with a view to reducing its scope

15. At this stage, the UNCITRAL working group discussed the law that would govern the stay of an ongoing arbitration proceeding on the commencement of insolvency proceedings, including the conduct of the arbitration.

16. However, it was noted that other issues would need to be addressed, such as which law would govern the effects of insolvency proceedings on the debtor's ability to initiate arbitration proceedings.

17. GRIP 21 proposes a distributive application of laws by subject. This distribution could lead to the following approaches:

**(a) Retain within the scope of the *lex fori concursus*:**

(i) The effect of the opening of proceedings on the debtor's capacity to act;

(ii) The powers of the insolvency practitioner;

(iii) The effect of the stay of individual proceedings;

(iv) The public policy exception (including when applying for recognition of an arbitration award);

(v) The possible annulment of a payment obtained in execution of an arbitration award (through the use of avoidance actions).

18. It should be noted that the stay of individual proceedings applies as a general rule to arbitration proceedings, except in cases where insolvency law does not consider this rule to be absolute. In such cases, the court which has jurisdiction over the insolvency proceedings may authorise the continuation of the arbitration proceedings by means of a reasoned court order. This could occur, for example, in the following cases:

(a) Where the debtor is the claimant in the arbitration proceedings and is not divested by the opening of the insolvency proceedings;

(b) Where the continuation of the arbitration proceedings is in the interests of the creditors;

(c) When the stay of individual proceedings may have an effect that is prejudicial to the other parties; and

(d) In the case of international arbitration proceedings (to be discussed).

19. As regards the enforcement phase of an arbitral award, the stay of proceedings resulting from the opening of insolvency proceedings shall normally prevent the enforcement of that award in respect of the debtor's assets situated in the State where the insolvency proceedings are opened, as well as in cases where the insolvency proceedings have universal effect or have been expressly recognized in the State where enforcement is sought.

**(b) Retain application of the *lex arbitri* for:**

(i) The definition of the moment when the arbitration proceeding begins (referral to the arbitration institution, constitution of the tribunal, agreement on the arbitrators, etc.);

(ii) The manner in which the insolvency practitioner may become involved in the arbitration proceedings;

(iii) Any restrictions on the debtor's power to seek international recognition of the insolvency proceedings before the arbitral tribunal;

(iv) The procedural aspects of the stay of individual proceedings;

(v) The possible application of the insolvency law of the State where the arbitral tribunal is established (in the sense of the legal seat of arbitration) or, depending on the question raised, the insolvency law of the State where the arbitration physically takes place (for example for the summoning of witnesses).

### 3. On the impact of article 18 of the European Insolvency Regulation (2015)

20. The relevant provisions of the Insolvency Regulation (EU 2015/848) of 20 May 2015 are drafted in very general terms:

> "The effects of insolvency proceedings on a pending lawsuit or pending arbitral proceedings concerning an asset or a right which forms part of a debtor's

> insolvency estate shall be governed solely by the law of the Member State in which that lawsuit is pending or in which the arbitral tribunal has its seat" (EU Reg. 2015/848, art. 18).

21. This rule does not address the difficulties mentioned above.

22. At most, a reconciliation could be envisaged by the UNCITRAL working group between an arbitral proceeding and a pending lawsuit, for example by considering that the rules relating to a pending lawsuit apply to an arbitration as well unless there are special provisions in the law applicable to the arbitration proceedings.

**OTHER OUTSTANDING ISSUES:**

**4. Should the exception to the *lex fori concursus* be limited to foreign arbitral proceedings taking place outside the State in which the insolvency proceedings are opened?**

23. According to the working document (WP. 190, p. 35 (EN), pt. 27), the draft legislative provision to be adopted should be read as follows:

> "where foreign arbitral proceedings take place in the territory of a State other than the State where insolvency proceedings have commenced", "the effects of insolvency proceedings on (…)."

24. GRIP 21 proposes the following amendments:

> "Where **foreign** arbitral proceedings take place **in the territory of *before an arbitral tribunal seated in*** a State other than the State in which the insolvency proceedings have been opened", "the effects of the insolvency proceedings on […]."

25. The reference to "foreign" arbitration proceedings is unnecessary because the proceedings "take place in the territory of a State other than the State in which the insolvency proceedings have been opened".

26. If the legislative provision above is not intended to be limited to foreign arbitration proceedings, attention should be paid to maintaining consistency with the impact of the opening of insolvency proceedings on domestic arbitration proceedings subject to French law.

27. The proceedings are opened before an arbitral tribunal and not in the territory of a State; this amendment would be in line with UNCITRAL's concerns about the "place of arbitration".

28. In the commentary on the legislative provisions, and whenever necessary, the difference highlighted into the working document (WP. 190, p. 35 (EN), pt. 27, *in fine*) between the legal seat of arbitration (law applicable to procedural issues) and the law where the arbitration physically takes place (law applicable to certain issues relating to the conduct of the proceedings, e.g. the ability to seek mandatory attendance of a witness through the courts (see below) should be pointed out.

**5. Proposal on a definition of the *"lex arbitri"* if it might appear in the draft legislative provisions**

29. In the WP. 190, p. 35 (EN) pt. 28, it is stated that:

> It might be beneficial to clarify in that definition or accompanying commentary that that law would encompass not only arbitration law but also insolvency law of the State where arbitration takes place and that the reference to the place of arbitration should be understood as reference to the legal place of arbitration, not the geographical physical venue or an online venue where proceedings may be held.

30. GRIP 21 agrees with the need to differentiate between the legal seat of arbitration and where the arbitration physically takes place, given that the seat of arbitration is not necessarily the place where the hearings or meetings are held, which

may be in a different State or virtual, although this dissociation could be a source of difficulties in the context of an appeal against the arbitral award, its annulment or during the enforcement phase.

31. In the end, the "*lex arbitri*" should be, unless otherwise provided, the law of the State where the arbitral tribunal is seated (legal place of registration), regardless of where arbitral proceedings take place.

32. As for the reference to the "*lex arbitri*", which would include "*the insolvency law of the State where the arbitration takes place*" (understood as the legal place of registration), this interpretation should be considered carefully as it may create confusion.[1]

# V. Amendments to the commentary

33. The following amendments (***in italic and bold***) are proposed on pt. 34 of WP. 190 (pp. 36–37 (EN)):

"A commentary may note that:

(i) Not all States envisage a stay of ongoing arbitral proceeding, envisaging instead a stay of the enforcement of arbitral awards;

(ii) Practical difficulties may arise from enforcing a stay of ongoing arbitral proceedings because of relative independence of foreign arbitral proceedings from the legal system of the State where the proceedings take place;

(iii) In some States, arbitral awards emanating from the arbitral proceedings that proceeded in defiance of the stay or other rules imposed by the *lex fori concursus* (e.g. displacement of the debtor from the operation of the business with no capacity to represent the insolv**ent** estate in the arbitral proceedings) are void ***or maybe voidable*** while in other States they may be recognized and enforced ***in specific circumstances***;

(iv) Limited grounds exist in most States for setting aside or refusing recognition or enforcement of a foreign arbitral award; and

(v) The need for recognition and enforcement of the award may not arise, for example where the award is implemented voluntarily, increasing risks of the ***execution*** of the award for the benefit of the wrong person (e.g. the displaced debtor), necessitating a subsequent tracing and recovery action and thereby defeating the objectives of effective and efficient insolvency proceedings, ***including any breach of public policy***."

# VI. Conclusion

34. While the distinction made between substantive law and procedural law is the very essence of private international law, we are of the view that certain recommendations providing for a distributive selection of applicable rules (distributive application of the rules according to the debtor's situation) should be acceptable to all.

[1] See point IV.2 of the present note on GRIP 21's proposal to assign the applicable law according to the subject matter, and in particular the possible application of the insolvency law of the State where the arbitral tribunal is established (in the sense of the legal place of arbitration) or, depending on the question raised, the insolvency law of the State where the arbitration takes place (for example, for the summoning of witnesses).