

Arbitration & ADR - Poland

Elektrim case era comes to an end

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Introduction

Main legal issues

Arbitration and bankruptcy under previous regulations

Arbitration agreement after declaration of bankruptcy

Impact of bankruptcy on ongoing arbitration

Comment

Introduction

On June 9 2015 the president signed the new Law on Restructuring. This new statute (which will fully come into force on January 1 2016) will reshape the Polish bankruptcy, insolvency and restructuring rules to make it easier for companies to get back on their feet after a period of financial difficulty. From the perspective of arbitration, the new law derogates from the controversial provisions – well known to the arbitration world from the *Elektrim* case – under which a declaration of bankruptcy rendered arbitration agreements concluded by an insolvent company ineffective. In principle, in future a declaration of bankruptcy will not impede ongoing arbitration. The new provisions deserve a closer look by any foreign party that has entered into an arbitration agreement with a Polish company.

Main legal issues

The main issues that arise regarding the relationship between bankruptcy and arbitration under the new legislation are:

- the effectiveness of arbitration agreements after a declaration of bankruptcy; and
- the impact of a declaration of bankruptcy on ongoing arbitration proceedings.

Arbitration and bankruptcy under previous regulations

Before the introduction of the new Law on Restructuring, Articles 142 and 147 of the Bankruptcy and Rehabilitation Law of February 28 2003 provided that arbitration agreements concluded by an insolvent company became ineffective at the date of the declaration of bankruptcy, and all ongoing arbitration proceedings had to be discontinued. There was no equivalent rule in the legal system of any other European country – Articles 142 and 147 were unique in their severe and unequal treatment of arbitration. In contrast, when bankruptcy was declared, normal court proceedings before a state court had to be suspended only until the official receiver or administrator of the bankruptcy estate replaced the insolvent company in the capacity of a party to the proceedings.

Articles 142 and 147 had a significant impact on international arbitration proceedings with Polish parties. When a foreign party entered into arbitration proceedings with a Polish company which later declared bankruptcy, it was faced with a dilemma.

If the arbitration proceedings were not discontinued by the tribunal after the declaration of bankruptcy by the Polish party, then it could not be ruled out that the Polish courts would refuse to allow enforcement of the rendered award in Poland. This is because, from the perspective of the Polish courts, Articles 142 and 147 could be treated as mandatory provisions.

It made little sense for an arbitral tribunal (and even less for a foreign party) to discontinue proceedings that had already taken up a substantial amount of time and resources and were on a fast track to a conclusion with an award. Therefore, some tribunals and foreign parties decided to continue the arbitration, despite the risk of having an unenforceable award.

Elektrim case

The most notable example of the difficult relationship between Articles 142 and 147 and arbitration was the *Elektrim* case, in which Polish company Elektrim SA was a party to series of arbitration proceedings at the London Court of International Arbitration (LCIA) and the International Chamber of Commerce (ICC) in Geneva. In the course of the arbitration, Elektrim filed for bankruptcy, triggering the application of Article 142. Each tribunal approached the effects of that provision differently. The

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English tribunal decided to continue the proceedings, whereas the Swiss tribunal terminated the arbitration. In both cases the contrasting decisions of the arbitral tribunals were upheld by state courts in Switzerland⁽¹⁾ and England.⁽²⁾ Neither court concluded that Article 142 was a mandatory provision; rather the findings of the courts contrasted regarding the applicable law to determine Elektrim's ability to participate in the arbitration. The Swiss court found it to be Polish law, whereas the English court ruled that it should be English law. Subsequently, the struggle for enforcement of the LCIA award in Poland began.

At first instance, the Polish court denied the enforcement of the LCIA award in Poland.⁽³⁾ The court stated that Article 142 was a mandatory rule and its omission would violate public policy. However, that decision was overruled on appeal. The Warsaw Appellate Court refused to treat Article 142 as a mandatory rule.⁽⁴⁾ The court moved to apply Article 15 of the EU Insolvency Regulation (1346/2000). This provides that "the effects of insolvency proceedings on a lawsuit pending concerning an asset or a right of which the debtor has been divested shall be governed solely by the law of the Member State in which that lawsuit is pending". As a result, the court concluded that in the case of the LCIA award, English law applied, not Article 142.

The uncertainty regarding the legal effects of Articles 142 and 147 of the Bankruptcy and Rehabilitation Law on arbitration with Polish parties called for legislative action.

Arbitration agreement after declaration of bankruptcy

The new Law on Restructuring introduces substantial changes to the relationship between rules on insolvency and arbitration:

- A declaration of bankruptcy will no longer render arbitration agreements ineffective. However, any new arbitration proceedings will have to be conducted against the official receiver of the bankruptcy estate if the bankrupt company is the respondent, or can be initiated only by the receiver if the bankrupt company is the claimant.
- If, at the date of the declaration of bankruptcy, arbitration has not yet commenced, the official receiver will be empowered to declare the avoidance of the arbitration agreement. However, this will be allowed only when:
 - pursuing claims in arbitration would impede the liquidation of the bankruptcy estate – this will particularly be the case when there are insufficient assets in the estate to cover the arbitration fees; and
 - the official receiver obtains consent from the court to terminate the arbitration agreement.

The other party will also be able to avoid the arbitration agreement. If the official receiver does not declare avoidance and yet refuses to pay its share of the costs, then the other party may terminate the arbitration agreement.

Similarly, before that point the other party may request the official receiver to declare in writing – within 30 days – whether it will avoid the arbitration agreement. If the receiver fails to make a declaration, the arbitration agreement is deemed to have been avoided.

Impact of bankruptcy on ongoing arbitration

The new Law on Restructuring introduces an important change regarding the impact of bankruptcy on ongoing arbitration. According to the new law, arbitration will no longer have to be discontinued and will be treated in the same way as proceedings before the state courts.

This means that if arbitration proceedings are in progress, the tribunal will be expected to suspend the proceedings. The tribunal will then have to wait for the official receiver to enter the proceedings in the capacity of a party (in place of the insolvent company).

However, what is clear is that when the arbitration concerns a claim that should be reported to the bankruptcy estate, the proceedings before the tribunal may continue only when the claim is not included on the list of claims in accordance with Polish law. The list of claims is a court-approved document that contains all claims to be satisfied from the liquidation of assets of the bankruptcy estate.

Comment

The introduction of this new law is another step on Poland's path towards becoming a more arbitration-friendly jurisdiction. However, there are still issues in that regard. Foreign parties should be aware that, even if Polish law is not applicable to the case examined by the arbitral tribunal, Polish courts may expect the arbitrators to honour the provisions that regulate the effects of bankruptcy on arbitration and may refuse to enforce an award that is rendered with disregard of those rules.

For further information on this topic please contact [Rafal Kos](mailto:Rafal.Kos@kkg.pl) or [Kuba Gasiorowski](mailto:Kuba.Gasiorowski@kkg.pl) at [Kubas Kos Gałkowski](tel:+48222068300) by telephone (+48 22 206 83 00) or email (rafal.kos@kkg.pl or kuba.gasiorowski@kkg.pl). The [Kubas Kos Gałkowski](http://www.kkg.pl) website can be accessed at www.kkg.pl.

Endnotes

(1) Swiss Federal Tribunal, March 31 2009, *Vivendi v 4A*, 428/2008.

(2) English Court of Appeal, July 9 2009, *Syska & Anor v Vivendi Universal SA & Ors*, [2009] EWCA Civ

677.

(3) Warsaw Regional Court, August 20 2009, file ref No VII Co 388/08.

(4) November 16 2009 decision, file ref No I ACz 1883/09 and November 18 2009 decision, file ref No I ACz 1686/09.

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