



ARBITRATION e-REVIEW

No. 1-2 (12-13)/2013

ARBITRATION E-REVIEW

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EDYTORIAL

4  dr Beata Gessel-Kalinowska vel Kalisz

ANALYSES & OPINION

- 6 Fast-Track & Emergency Measures in M&A & JV Disputes in ICC Arbitration
 Mirèze Philippe
- 24 Calculation of damages in M&A arbitration Proceedings
 Witold Rzewuski, Zbigniew Jusiś
- 32 Arbitration in Corporate Disputes in Brazil
 Nelson Eizirik
- 39 EU Commitment Arbitrations – A Brief Introduction
 Gordon Blanke
- 47 Deadlock provisions in shareholders' agreements: corporate and litigation perspectives
 Cécile Amayen, François Hellot, Xavier Nyssen, Guillaume Briant

CONFERENCE REPORTS

- 56 Report from the conference "Dispute Resolution in M&A Transactions: Tactics, Challenges, Defences" 2nd edition, 6-7th June 2013, Warsaw
 mec. Agnieszka Wolińska
- 60 Panel on arbitration and competition – report
 Jana Plaňavová-Latanowicz
- 66 Mandatory public law in M&A arbitration.
 Courtenay Griffiths
- 72 Report from the Panel on Mandatory Public Law in M&A Arbitration
 dr Marek Jeżewski

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DR. BEATA GESSEL-
-KALINOWSKA
vel KALISZ

President of the Lewiatan
Court of Arbitration

Dear Readers,

The second edition of the 'Dispute Resolution in M&A Transactions – Tactics, Challenges, Defenses' conference took place in June in Warsaw this year. The conference fulfilled its thoughts provoking role and became a jumping-off point to further develop some of the issues raised during the conference. Therefore, today in the pages of our review we host Ms. Mirèze Philippe (ICC International Court of Arbitration), who shared with us her thoughts on expedited and emergency measures in disputes related to M&A transactions, illustrating them with numerous examples of the cases submitted to the ICC International Court of Arbitration in Paris.

Mr. Witold Rzewuski (Ernst & Young) and Mr. Zbigniew Jusis (Ernst & Young) presented the issue of damage calculation and compensation in M&A transactions, considering these aspects from the experts' point of view. Mr. Nelson Eizirik (Carvalho e Eizirik Advogados) concentrated on corporate disputes in the light of recent changes to the Brazilian Corporate Law, which expanded the area of arbitration disputes, allowing for arbitration in disputes involving public companies. It is important to notice the way arbitrability and proprietary nature of corporate disputes resulting from the company resolutions are interpreted.

Mr. Gordon Blanke (Baker & McKenzie Habib Al Mulla) has decided to present an overview of the new type of arbitration which may arise out of individual claims for damages suffered by a third party as a result of non-compliance with the EU obligations by the merging companies. Such obligations may be imposed by the relevant antitrust authorities in the event of issuance of a conditional merger clearance decision.

Ms. Cécile Amayen, an in-house counsel at the Telecom-Orange

Group, Mr. François Hellot (Dechert LLP) and Mr. Xavier Nyssen (Dechert LLP), who has been working together on various transactions, shared their thoughts on methods of resolution of a deadlock situation in the joint venture transactions, which as correctly noticed by the authors, are frequently used as an alternative to M&A transactions.

It is worth to take a look at the full text of Mr. Courtney Griffith's (25 Bedford Row Chambers) address, who in a very strict manner points out the dangers the international arbitration may be threatened by when encounters the criminal activity, in particular money laundering.

Finally, we present to you the report on the first day of the conference, prepared by Ms. Agnieszka Wolińska (Wolińska Attorney at Law), second part dedicated to antitrust law in arbitration reported by Ms. Jana Planavova-Latanowicz (Centre for Europe University of Warsaw), and finally panel on mandatory public law in M&A arbitration by Mr. Marek Jeżewski (Kochański, Zięba, Rapala & Partners). Full video coverage from the conference can be found on the Lewiatan Court of Arbitration website in the section devoted to the conference: <http://www.sadarbitrazowy.org.pl/pl/ma>

Have a nice reading!!

Dr. Beata Gessel-Kalinowska vel Kalisz
President of the Lewiatan Court of Arbitration

Fast-Track & Emergency Measures in M&A & JV Disputes in ICC Arbitration

■ Mirèze Philippe

Special Counsel at the Secretariat of the ICC International Court of Arbitration.

The views expressed are those of the author alone and should not be regarded as representative of or binding upon the ICC, the Court or its Secretariat.

Summary

This article examines the use of fast-track procedures in M&A related disputes submitted to ICC arbitration and whether specific fast-track arbitration rules are necessary. It distinguishes from the outset speed from urgency. It presents the ICC Emergency Arbitrator Rules that the parties can use for urgent measures, and underlines the possibility for the parties to use other dispute resolution services of the ICC, mediation and expertise, to accelerate resolution of disputes. It discusses a more realistic approach than fast-track by controlling the duration of the procedure with the help of case management techniques.

Introduction

M&A transactions and Joint Ventures (“JV”) constitute an important aspect of the business arena, and as such, represent a significant share of the type of disputes settled through arbitration. The International Chamber of

Commerce (“ICC”) counts among the cases submitted to its Arbitration Rules a major number of cases involving M&A. ICC statistics show that agreements relating to share purchase agreements and joint ventures agreements have steadily accounted for an average of 15% of the cases in the last fifteen years, the peak being in 2011 with 17.71%.

In many of the M&A transactions parties insert an arbitration clause in their agreements and prefer to travel the avenue of arbitration rather than litigation. M&A transactions usually involve complex issues arising often from a series of agreements (for instance a letter of intent, a shareholders’ agreement and a joint venture agreement), frequently between several parties. One third of the M&A disputes submitted to ICC arbitration involve several parties, which is in line with the ICC overall statistics. In three quarter of the cases, the parties opt for a three-member arbitral tribunal and the president is nominated by the co-arbitrators.

Considering the complexity of the transactions, especially in the context of trans-border transactions, and the disputed issues that may arise thereof, settling disputes stemming from such type of contracts through arbitration is more appropriate. The advantages of arbitration as opposed to litigation are the reason for that choice (1), although some of them have been controversial in recent years, including the possibility to ensure confidentiality in arbitration and the benefit of shorter time and reduced costs. The author considers that two advantages remain uncontested and outweigh the others. They deserve to be flagged: the first is the fact that the parties benefit from some control over the procedure and thus feel more confident; the second is the possibility to enforce awards thanks to the New York Convention.

The parties and their representatives generally feel more confident in an environment where they have a certain control over the procedure. They can entrust their disputes to knowledgeable arbitrators, who are not only familiar but also have expertise in a specific business field, for instance M&A transactions, who are capable of dealing with disputes in the languages chosen by the parties and applying rules of law that the parties agreed upon. In addition to the time limits they are free to agree upon in their arbitration agreement, the parties contribute to the organisation of the procedure together with the arbitral tribunal and may agree on shorter time limits to conduct the procedure, including on a fast-track basis; they may call the arbitral tribunal during the procedure to see

1. See B. Ehle “Arbitration as a Dispute Resolution Mechanism in Mergers and Acquisitions”, *Comparative Law Yearbook of International Business*, vol.27, 2005, p. 287

where matters stand. In summary, the parties feel “closer” to the arbitral tribunal than to state courts, although the physical distance may be bigger with the former than with the latter, given the opportunity they have to contact the arbitral tribunal any time during the procedure unlike state courts.

With respect to enforcement of awards, arbitration users may be faced with situations where losing parties are not willing to respect decisions rendered. The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards allow winning parties to request the enforcement of the awards in one or several of the nearly 150 countries which signed this convention. State judgements do not benefit from the same scope as no international instrument for the enforcement of commercial judgements is signed by so many countries as the New York Convention. This is a valuable advantage especially when parties come from different horizons with assets in various countries as may be the case in M&A disputes.

The purpose of this paper is to assess whether fast-track procedures are used in M&A and JV disputes submitted to the ICC International Court of Arbitration (“Court”) (2). The paper will also discuss whether specific rules are necessary for fast-track procedures (3). The discussion then turns to examining which ICC dispute resolution services may be used for expedited decisions (4). Finally, it will examine how case management techniques may help accelerate procedures (5). Before addressing these issues, expeditious procedures must be differentiated from the urgent measures (1).

1. Fast-track Procedures Versus Urgent Measures

A fast-track procedure which terminates with a final award on the merits is one thing, and an urgent measure which provides an interim decision to enable an urgent action awaiting a final decision is another thing. Although there may be some similarity with respect to the fact that both are meant to be dealt with in a short period of time, the end result is not the same.

a) Fast-Track, Expedited, Accelerated Procedures

A distinction must first be made between fast-track, expedited and accelerated procedures. Interestingly, three types of short deadlines were distinguished by some authors².

The first type defined as “fast-track arbitration” concerns the arbitration agreement whereby the parties decide to apply shorter time limits to some aspects of their disputes or to some stages of the procedure; normally the time limits are not extendable although in reality they may be extended where necessary. ICC fast-track arbitrations concern cases where the parties have departed from the time limits of the ICC Arbitration Rules and shortened them.

Whereas the second type identified as “expedited arbitration”, refers to expedited rules chosen by the parties which do not require that they agree on the time limits, as the time limits will be those foreseen in the institutional expedited rules. Many arbitration institutions

2. B. Davis, O. Lagace, M. Volkovitch “When Doctrines Meet: Fast Track Arbitration and the ICC Experience”, *Journal of International Arbitration*, vol.10, n°4, 1993, p. 69

have adopted expedited rules in the last decade, such as the World Intellectual Property Organization (WIPO), the Stockholm Chamber of Commerce (SCC), and the American Arbitration Association (AAA)³.

Finally, the third type described as “accelerated arbitration” is the situation where the parties have neither incorporated in their arbitration agreement shorter time limits nor referred to expedited rules, but decided after the dispute has arisen that the urgency of the matter warrants an accelerated pace.

Incidentally, where both parties are motivated to move expeditiously, the fact of being either claimant or respondent is irrelevant.⁴

Irrespective of the type chosen by the parties, fast-track, expedited or accelerated, the procedure normally ends with a final decision on the merits.

b) Urgent Measures

The second distinction that must be made concerns a final decision rendered expeditiously as opposed to an urgent measure awaiting a final decision.

Urgent measures are intended to preserve a situation until a final decision on the merits is rendered. It is thus a temporary solution for parties that require immediate relief. Interim or conservatory measures may be requested by

3. See for discussion about the various expedited rules E. Castineira “The Emergency Arbitrator in the 2012 ICC Rules of Arbitration”, *The Paris Journal of International Arbitration (Les Cahiers de l'Arbitrage)*, 2012-1, p. 65

4. M. Silverman “The Fast-Track Arbitration of the International Chamber of Commerce – the User’s Point of View”, *10(4) Journal of International Arbitration*, vol.10, n°4, 1993, p. 113

parties during an arbitration procedure or before an arbitration request is filed. The request may be submitted to the arbitral tribunal if such tribunal is already constituted and has received the documents of the case. If the tribunal is not in place the request may be submitted to an emergency arbitrator procedure, as will be discussed further, or to a state court. A party may indeed consider that a state court can prove more efficient if it appears likely that a party against which the requested measure is directed will fail to comply with the order; state court decisions are directly enforceable, as opposed to arbitrators’ orders.

It may happen that during a fast-track, expedited or accelerated procedure an urgent measure is requested to obtain an interim measure until a final decision is rendered.

Having drawn the line between expeditious procedures and urgent measures, the discussion will concentrate on fast-track procedures and other tools that may assist the parties in getting a rapid solution or in limiting the period of time necessary to get a final decision.

2. The First Issue To Be Addressed Is To Assess Whether Fast-Track Procedures Are Used In M&A Disputes Submitted To ICC Arbitration

a) Statistics of Fast-Track Cases

ICC statistics show that 15 cases related to M&A disputes are or were conducted on the basis of shorter deadlines out of 175 fast-track arbitrations administered by the ICC between 1990 and 2011, which represent 8,50% of the fast-track cases. If the 175 fast-track cases are compared with the 11.701 cases filed in

22 years, the result demonstrates that fast-track cases including the M&A cases represent an infinitesimal percentage of 1.50%.

Interestingly, 10 out of the 15 cases were multi-party disputes and 4 involved State parties. The parties originated from various countries around the globe except Asia (Australia, Brazil, France, Indonesia, Israel, Ivory Coast, Japan, Luxembourg, Netherlands, Norway, Rwanda, Spain, Turkey, United Arab Emirates, United Kingdom, United States). The contracts were signed between 1985 and 2011 and concerned mainly construction, energy, finance and insurance, telecommunications and chemical industry. The amounts in dispute ranged from 2.000.000 to 776.000.000 US Dollars. Finally, in two third of the cases disputes arose less than five years after the signature of the agreement, which is also in line with ICC statistics about the time elapsing between the signature of a contract and the date on which a dispute is submitted to ICC arbitration⁵.

Four of the 15 fast-track cases in M&A disputes were withdrawn before the award. In 2 cases partial awards were rendered, one on jurisdiction and the other on jurisdiction and liability; in the latter case the arbitral tribunal reserved the decisions on quantum and costs for the final award; both cases are still pending. Five other cases are pending. Final awards were rendered in 4 cases.

5. See for further details M. Philippe «Les pouvoirs de l'arbitre et de la Cour d'arbitrage de la CCI relatifs à leur compétence» (The Powers of the Arbitrator and of the ICC Court of Arbitration in Relation to their Jurisdiction), *Revue de l'arbitrage*, 2006, p. 591

b) Shorter Time Limits in Arbitration Agreements

The parties agreed in 2 of the 15 cases on shorter periods only for the notice of the dispute and the answer to be submitted or for the constitution of the arbitral tribunal. In all other cases the shortened periods related to the rendering of the award and ranged from a minimum of 30 to a maximum of 120 days starting from different stages: filing of the request for arbitration, appointment of the last arbitrator, date of the first meeting (which corresponds to a case management meeting), final hearing or closing of the proceedings. In some cases, the fast-track aspect concerned both the phase of the constitution of the arbitral tribunal and the phase of the rendering of the award.

In one of the arbitration agreements the parties decided that after 14 days following acceptance by the chairman of the arbitral tribunal of his appointment, the latter will convoke a meeting during which the disputed issues will be “fixed” and the documents to be produced throughout the arbitration will be determined. It was also decided that at the end of the meeting an “arbitration compromise” would be signed which would state “the disputed facts and the questions to be solved”, and that the arbitral tribunal should render a detailed award within 90 days from the establishment of the arbitration compromise.

In another arbitration agreement, the parties included some case management aspects intended to facilitate the expedited procedure. It was agreed that claimant shall serve its claim within 20 days of the appointment of the arbitrator, the defence within 20 days after that,

and the reply 20 days thereafter. It was further agreed that: (i) no statement of case, witness statement, expert report or submission shall exceed 15 pages, excluding attachments; (ii) the shareholders of party A and party A itself shall provide the arbitral tribunal with any information which it may reasonably request; (iii) factual witnesses shall give evidence in chief by witness statement; (iv) cross-examination of any factual or expert witness shall not exceed a day; (v) there shall be no oral submissions, though the arbitral tribunal may ask questions to the parties orally or in writing. Finally, the arbitral tribunal was expected to render its award within 45 days of the appointment of the last arbitrator. The parties subsequently decided to depart from the time limits provided in their clause and agreed on a different procedural timetable; it was also agreed to bifurcate the procedure and decide separately on the liability and the quantum.

It is interesting to note that in the final award of one case the arbitral tribunal stated that it has been unable to render the award within the time period provided for in the arbitration agreement due to the additional safeguards necessitated by respondent’s non-participation in the proceedings.

It comes as no surprise that in almost all cases, the time limit for rendering the award was extended for a few more weeks and in some instances for several months. There may be various reasons for such extensions: in many cases the parties realised that the time limits agreed upon in the arbitration clause may have been unrealistic and waived the deadline requirement; sometimes the arbitral tribunal with the parties agreed on extensions at the time of

establishing a procedural timetable; in some instances the arbitral tribunal requested an extension. Irrespective of any initial or subsequent agreement about short deadlines, the Court extended time limits on its own initiative when it considered that it was necessary to do so in order that the arbitral tribunal and the Court fulfil their responsibilities in accordance with Article 38 of the ICC Arbitration Rules. In *ad hoc* arbitrations, fast-track procedures may be at risk if longer periods are required and the parties do not agree to extend them.

Arbitration users may be interested in having their disputes settled in an expedited manner, but in reality the complexity of the disputes overrides speed. Striking a balance between speed and quality of the proceedings⁶, especially in the context of M&A disputes, is necessary.

ICC statistics and the examples provided in this paper illustrate that, while being attractive, (i) fast-track is not adapted to all types of disputes, (ii) unrealistic short time limits are usually extended, and (iii) fast-track is scarcely used in M&A disputes. Moreover, it is difficult to understand how time limits can be significantly shortened in complex disputes especially where bifurcation is sometimes indispensable, for instance in cases where the arbitral tribunal is required to decide about liability before hearing the parties on the quantum⁷. It is true that the constraints of time required on the one hand for

the parties to prepare and plead their case, and on the other hand for the arbitrators to deliberate and render their decision, makes it hard to compress the time limits when disputes involve complex issues. However, this does not mean that parties may not make use of the fast-track lane, since there exist other avenues that the parties may travel to benefit from swifter procedures as will be explained in the further parts of this paper.

Finally, practitioners approached on the subject of fast-track in M&A disputes reveal that, due to the complexity of the issues disputed in M&A transactions, it is unlikely to see a case decided on an expedited basis. Parties may however require that some aspects be decided expeditiously through interim measures, for instance to protect a *status quo*, as will be discussed below.

c) Fast-Track Disputes Administered

The issues submitted to ICC arbitration in the 15 M&A/JV fast-track cases typically concerned: respondent’s failure to comply with the implementation of a project and claimant’s claim for damages, respondent’s wrongful transfer of shares and claimant’s claim for damages and loss of profit, respondent’s breach of obligations preventing claimant from achieving the objectives and claimant’s request for declaratory relief, damages and interim relief, claimant’s request for declaratory relief and repayment of an amount in a case related to several representations, respondent’s breach of an option agreement and claimant’s request for specific performance.

Two connected ICC cases 7385 and 7402 filed in 1991 and amply commented are

6. J. Fornalik and K. Szczudlik “Fast-track Procedure in the Rules of the PKPP Lewiatan Court of Arbitration – a step forward in Polish arbitration?” *e-Arbitration Review* 3-4(10-11) 2012

7. See for bifurcation in M&A disputes, A. Carlevaris “Arbitration and M&A Transactions”, *ICC Bulletin*, 2013, vol.24, n°1, and B. Gessel-Kalinowska vel Kalisz “Breach of Representations and Warranties: the biggest trouble maker in M&A Arbitration?”, *ICC Bulletin*, 2013, vol.24, n°1

interesting to highlight⁸. In both cases, the fast track procedures were a true success as all players, the parties, the arbitrators and obviously the ICC, fully cooperated and followed scrupulously the short deadlines of all stages. In these multi-billion US Dollars cases, the procedures were conducted in 7 weeks for the first one and 8 weeks for the second, from the time the request for arbitration was filed until the award was notified to the parties. The president of the Court used the power vested upon him by the ICC Arbitration Rules (Article 1(3)) to make the necessary decisions within a few hours or days throughout the procedure, to appoint the arbitrators, control the Terms of Reference, and scrutinise and approve the award.

The dispute concerned re-determination of commodity charges and minimum volume obligations. The co-arbitrators nominated by the parties and the chairman appointed by the Court were the same in both procedures. They rendered in both cases a final award in which they re-determined the prices for the commodity charges, did not change the minimum volumes, and deferred to further slow track proceedings the frustration and demand charges questions. The Tribunal suggested to the parties that they consider the desirability of agreeing upon a somewhat more relaxed,

8. See e.g., B. Davis with R. Amoussou-Guenou, G. Affaki, R.T. Madaan, M. Sawano, F. Mantilla Serrano, O. Lagacé Glain, D. Brown and R.H. Smit, "International Fast-Track Commercial Arbitration", *Comparative Law Yearbook of International Business* (Susan Cotter ed.), Kluwer Academic Publishers, 1995, p. 357; B. Davis, O. Lagace, M. Volkovitch "When Doctrines Meet: Fast Track Arbitration and the ICC Experience", *Journal of International Arbitration*, vol.10, n°4, 1993, p. 69; M. Philippe "Are specific fast-track arbitration rules necessary?", *Arbitration in Air and Space Law including Telecommunications Activities, Peace Palace Papers, International Bureau of the Permanent Court of Arbitration*, Kluwer Law International, 2001, p. 253

modified, fast-track procedure in which the Tribunal would address all issues raised by the parties. However, since the parties had not reached an agreement to this effect, the Tribunal had to address the problem. Although it was of the view that the parties cannot force the Tribunal to follow procedures that deviate from those of the ICC International Court of Arbitration, the Tribunal preferred to avoid a possible attack upon its award on the ground that it exceeded its authority. It therefore ruled that issues that do not properly arise in the redetermination process regulated by Clause 9D.6. would be addressed under a schedule that would afford the parties more time than allowed by Clause 9D.6.6 to present their cases. This schedule was to be set by the Tribunal after consultation with the parties. It would meet Defendant 2's objection that it has not had an adequate opportunity to address these issues in the fast-track procedure⁹.

The published extract of this award confirms once again that fast-tracking complex M&A issues may not be realistic¹⁰.

In an unpublished case where the award was to be rendered within 90 days from the appointment of the chairman of the arbitral tribunal, the parties agreed to extend the time limit by an additional month but refused to extend it any further. The Court had to extend the time limit by 3 other months on its own initiative to allow

9. Final award in ICC arbitration cases 7385 and 7402, *ICCA Yearbook*, vol. XVIII, 1993, p. 68; Extracts of Award in Cases 7385 & 7402, *ICC Bulletin*, 1997, vol.8, n°1, p. 56

10. See in this respect p. 147 of A. Broichmann article on "Disputes in the Fast Lane: Fast-Track Arbitration in Merger and Acquisition Disputes", *International Arbitration Law Review*, issue 4, 2008, p. 143

the arbitral tribunal to render its award. The tribunal had difficulties to agree on all claims and therefore submitted a draft majority award for scrutiny by the Court. The minority arbitrator dissented on some decisions but did not issue a dissenting opinion. The majority found that there was no misrepresentation, that the accelerated payment clause was not triggered and therefore claimant's claim failed in this regard, that respondent's counterclaim was contingent on the misrepresentation claims and therefore dismissed it, that the non-compete clause was valid and enforceable and that claimant was in breach of such clause, and finally, that respondent failed to demonstrate the damage caused to it and therefore only nominal damages were awarded to it.

It results from the examination of the first question that, despite the urgency to solve disagreements in M&A transactions, the parties do not seem to use often fast-track procedures for M&A/JV disputes as reflected from the small number of cases in ICC arbitration, probably due to the complexity of such transactions.

3. The Second Question That Needs To Be Answered Is Whether Specific Fast-Track Rules Are Required

In a talk and a paper in 2001, the author answered this question in the negative¹¹. A decade later the author remains of the same opinion: no specific fast-track rules are necessary. Parties may tailor their arbitration

11. M. Philippe "Are specific fast-track arbitration rules necessary?", *Arbitration in Air and Space Law including Telecommunications Activities, Peace Palace Papers, International Bureau of the Permanent Court of Arbitration*, Kluwer Law International, 2001, p. 253

agreement to their needs and foresee shorter time limits. They may agree later with the arbitral tribunal on procedural aspects that may help gain time.

Although expedited rules issued by several arbitration institutions, which provide for procedures to be carried out in short time limits may be useful, the absence of expedited rules do not prevent a procedure from being accelerated if the parties decide to move in this direction.

The ICC Arbitration Rules are very flexible and have perfectly allowed under any version of the Rules to administer expedited procedures. Article 1 sub-paragraph 3 of the Rules empowers the president of the Court or any vice-president in the absence of the president to take urgent decisions. This was precisely the experience in the two cases discussed above (7385 and 7402).

What distinguishes a classical arbitration procedure from a fast-track arbitration procedure? The answer is shorter time limits. What would specific fast-track arbitration rules bring over traditional arbitration rules? The answer is again shorter time limits¹². Therefore, considering that any decision related to the administration of ICC arbitration can be made very quickly, adapting a separate set of rules dedicated to fast-track arbitration is unnecessary. Needless to say also that it is not necessary to adapt the arbitration rules to any specific type of disputes, such as M&A disputes. The arbitration procedure remains the same and the ICC

12. M. Philippe, op. cit. footnote 11

Arbitration Rules may apply to all types of disputes and to any variety of time limits. The only difference is the fact that the procedure is managed in shorter time limits to comply with the parties' agreement.

Fast-track must be treated with caution. While being attractive, what purpose does it serve if expedited rules are not adaptable to all situations, and if an unfamiliar user is tempted by a prompt decision but is unaware of the constraints of accelerated procedures? Even if an arbitration institution can assist the parties in organising their procedure expeditiously, it cannot help parties unfamiliar with fast-track procedures to prepare their case within short time limits. Moreover, parties must not only ensure that the opposing parties are capable of handling a fast-track procedure, but also – in case they both have similar interests in “fast-tracking” their procedure – consider to what extent the process must be accelerated or which aspects need to be expedited. Furthermore, parties, lawyers, arbitrators and the arbitration institution must all be capable of drawing on the resources necessary for the accelerated resolution of the dispute and of carrying out their tasks quickly and simultaneously¹³. Fast-track arbitration may be achievable if the parties are willing to cooperate fully, if the lawyers' submissions are of a high quality, if the arbitrators are authoritarian without being rigid, and if all the participants comply with the tight schedules¹⁴.

13. B. Davis with R. Amoussou-Guenou, G. Affaki, R.T. Madaan, M. Sawano, F. Mantilla Serrano, O. Lagacé Glain, D. Brown and R.H. Smit, “International Fast-Track Commercial Arbitration”, *Comparative Law Yearbook of International Business* (Susan Cotter ed.), Kluwer Academic Publishers, 1995, p. 357

14. See B. Davis, “Laying Down a Gauntlet: The Thirty-Six Hour Chairman”, *The American Review: Essays in Honor of Hans Smit*, volume 3, n°1, 1992, p. 170

The conclusion of this question is that, despite the utility of expedited rules issued by several arbitration institutions, the ICC has so far considered that adapting a specific set of rules for fast-track procedures will not offer more than what ICC Arbitration Rules already offer: parties are free to draft an arbitration agreement providing for a procedure tailored to their needs, and the ICC is capable of administering procedures in compliance with the parties' agreement.

4. ICC Dispute Resolution Rules That May Be Used for Expedited Procedures and Urgent Measures

In addition to interim measures (b) which can be obtained from the arbitral tribunal during an arbitration procedure, the parties now have another instrument, the ICC Emergency Arbitrator Rules (a) that they can use for emergency measures before an arbitral tribunal is put in place. This measure may be useful for instance to obtain an order forbidding a party from transferring shares before the closing, from selling shares to another shareholder or from modifying the composition of the board of directors¹⁵, so long as a decision has not been rendered on the merits. The ICC also offers other dispute resolution services, i.e. expertise and mediation (c), which may help solve disagreements in shorter periods of time.

a) Emergency Arbitrator

The 2012 ICC Arbitration Rules include an emergency arbitrator procedure that the

15. See D. Bensaude “S.A. Otor Participations v. S.A.R.L. Carlyle (Luxembourg) Holdings 1: Interim Awards on Provisional Measures in International Arbitration”, *Journal of International Arbitration*, 2005 Volume 22 Issue 4, p. 357

parties may use instead of rushing to state courts for urgent measures. Like Article 28, Article 29 provides the parties with an alternative to state courts for seeking interim or conservatory relief¹⁶, but at different points in time. Either an arbitral tribunal is already in place and the parties can request interim or conservatory measures in accordance with Article 28, or the arbitral tribunal is not yet in place and the parties now benefit from the possibility of filing an application for an emergency arbitrator in accordance with Article 29 and Appendix V of the Rules. The emergency arbitrator provisions under Article 29 do not replace Article 28 devoted to interim and conservatory measures, but come in addition to it. The emergency arbitrator is not an exclusive procedure and the parties retain the right to apply to state courts for emergency measures (Articles 28(2) and 29(7)).

An application for an emergency arbitrator may be submitted (i) before a request for arbitration is filed, (ii) or simultaneously, with the request for arbitration, (iii) or prior to the constitution of an arbitral tribunal in a pending arbitration (Article 29(1)). The procedure starts with the filing of an application for an emergency arbitrator and ends with the rendering of an order no later than 15 days from the date on which the file is transmitted to the emergency arbitrator. An order may thus be obtained within 18 days from the date of the Secretariat's receipt of the application (Article 6(4) Appendix V of the Rules). The emergency arbitrator is thus an ideal way of dealing expeditiously with an urgent matter.

16. See J. Fry, S. Greenberg, F. Mazza, with the assistance of B. Moss “The Secretariat's Guide to ICC Arbitration”, 2012, number 3-1051

However, it was decided to adopt a restrictive approach to avoid dilatory tactics and that the scope of the emergency arbitrator should be strictly limited. Several conditions or gatekeepers were provided to protect a responding party from the risk of abuse by an applicant, who may for instance put pressure on the other party to settle a case, but who does not intend to pursue the case on the merits.

The first gatekeeper, is the fact that the emergency arbitrator provisions shall not apply if the arbitration agreement was concluded before the entry into force of the new ICC Rules on January 1st, 2012 (Article 29(6)(a)). This reflects the fact that the emergency arbitrator being a particularly significant change, it must be ensured that the provisions do not apply to parties who were unaware about the new provisions and unable to opt-out. Therefore, to avoid taking the parties by surprise, these provisions will not apply retro-actively and will apply only to agreements concluded after January 1st, 2012.

Second, if an arbitral tribunal is already in place, the applicant must submit any request for emergency measures directly to it pursuant to Article 28. A party cannot request an emergency arbitrator (Article 29(1)), and if it does, the emergency arbitrator procedure may not take place.

Third, an emergency arbitrator procedure may only apply to signatories to the arbitration agreement or their successors (Article 29(5)). The rationale behind this requirement is to ensure that the responding party unequivocally agreed to submit to arbitration under the 2012 ICC Arbitration Rules. This limitation prevents a party from being drawn into an emergency

arbitrator procedure without having clearly agreed to such Rules¹⁷. Moreover, unlike arbitration where respondents are granted 30 days to file an answer and raise any objections, in an emergency arbitrator procedure responding parties have no time for raising objections before the file is transmitted to the emergency arbitrator, given the fact that the latter is appointed in 2 days. Responding party may submit any objections to the emergency arbitrator once in place.

The fourth gatekeeper prevents the emergency arbitrator provisions from applying when parties have expressly opted out of the emergency arbitrator provisions, which form an integral part of the ICC Arbitration Rules in force as of January 2012 (Article 29(6)(b)). When drafting the Rules it was considered that opt-out provisions are more efficient than opt-in provisions for very simple reasons¹⁸. It was first considered that the parties may be unaware of the existence of the Emergency Arbitrator Rules or forget about them when the need arises, and therefore lose the benefit of such out-of-court emergency measure. Also, dispute resolution clauses are frequently drafted by corporate or business people who may not know about this feature or know about it but not understand its purpose. The second reason

17. Regarding States and state entities which may apply for an emergency arbitrator procedure, see the discussions in: N. Voser and Ch. Boog "ICC Emergency Arbitrator Proceedings: An Overview", ICC Bulletin, Special Supplement, 2011, vol.22, p. 81, particularly point 2.2.3; E. Castineira "The Emergency Arbitrator in the 2012 ICC Rules of Arbitration", *The Paris Journal of International Arbitration (Les Cahiers de l'Arbitrage)*, 2012-1, p. 65, particularly point 1.5(b); "Arbitration Involving States and State Entities under the ICC Rules of Arbitration", ICC Arbitration Commission Report, 2012, ICC Publication 862

18. N. Voser and Christopher Boog "ICC Emergency Arbitrator Proceedings: An Overview", ICC Bulletin, Special Supplement, 2011, vol.22, p. 81

concerns a question of opportunity: when a party needs an emergency measure, it is because it considers that the opposing party is doing something wrong, therefore why would an abusing party accept to opt-in and avoid delaying a procedure. Finally, experience has shown that the Pre-Arbitral Referee Rules which exist since 1990 have been used in an insignificant number of cases, probably because parties were unaware of them or because they were not included from the outset in their arbitration agreement. It was therefore decided that the emergency arbitrator provisions should be included in the rules so as to ensure that the parties have the ability to use emergency measures if need be, unless they expressly opt-out. In the "Standard and Suggested Clauses" appended to the 2012 ICC Arbitration Rules, an opt-out provision is provided and the parties are warned that they must expressly exclude the emergency arbitrator if they do not wish this procedure to apply.

Likewise, the fifth condition applies where the parties have already agreed on another pre-arbitral procedure that provides for the granting of conservatory, interim or similar measures (Article 29(6)(c)). Agreeing to another pre-arbitral procedure would amount to an implied opt-out. This provision therefore avoids conflicts between pre-arbitral systems¹⁹.

The sixth safeguard is the requirement for the payment upfront of US\$ 40.000, failing which the proceedings will not be set in motion (Article 7(1) Appendix V of the Rules). The procedure is so short that it does not leave room for payment of an advance to cover the

19. N. Voser and Christopher Boog, op. cit. footnote 18

costs later during the procedure and must therefore be paid upfront. Considering that the emergency arbitrator will be appointed in 2 days and an order will be rendered within 15 days, the ICC must ensure that payment is made before transmission of the file to the emergency arbitrator, and thus, that it will be able to cover the emergency arbitrator's fees and expenses.

Once all these safeguard tests are passed and the procedure is set in motion, the applicant must still fulfill a last condition: if it has not filed a request for arbitration prior to filing a request for emergency arbitrator or simultaneously, it must file a request within 10 days from the receipt of the application by the Secretariat of the Court, unless the emergency arbitrator determines that a longer period of time is necessary. The rationale behind it is that the emergency arbitrator's order is temporary and not final and allows the applicant to preserve a situation only until a decision on the merits is rendered by an arbitral tribunal. If no request for arbitration is filed, the emergency procedure has no reason to be. The direct consequence is the termination of the emergency arbitrator proceedings by the President of the Court (Article 1(6) Appendix V of the Rules).

Finally, when the above tests are not passed, the Secretariat will inform the parties that the emergency arbitrator procedure shall not take place with respect to some or all of the parties and shall transmit a copy of the application to them for information (Article 1(5) Appendix V of the Rules).

Two applications for emergency measures pursuant to the new emergency arbitrator

provisions were so far submitted. In one of these applications the emergency arbitrator was appointed within two days and involved parties from the United Kingdom. The place of the emergency procedure and of the arbitration was in London. The other application was not admissible pursuant to Article 29(6), because the agreement was signed before the entry into force of the 2012 ICC Arbitration Rules.

b) Interim Measures in M&A Disputes

The limited number of fast-track cases in M&A did not reveal any interim measures requested by the parties. However, interim, conservatory or emergency measures are sometimes requested in M&A arbitrations. A few examples of ICC awards published in the ICC Bulletins of the Court will illustrate requests made by parties to the arbitral tribunal²⁰.

In ICC Case N°10021²¹, claimant and the respondents were shareholders in a manufacturing company. They "entered into an agreement to set up an export company as a joint venture with another company in the same group as the claimant and made a related agreement on exclusive export rights. The aim of these agreements was to make the manufacturing company a market leader, through financial assistance and investments. Claimant accused respondents of violating these agreements by entering into competing agreements and engaging in uncooperative conduct. Fearing that respondents

20. See for interim measures in M&A disputes, A. Carlevaris "Arbitration and M&A Transactions", ICC Bulletin, 2013, vol.24, n°1

21. ICC Bulletin, Special Supplement, 2011, vol.22, p. 26

were planning to dispose of all of their assets, claimant brought an application for conservatory measures, in which it requested the arbitral tribunal to attach various assets belonging to the respondents as a means of securing a possible award of damages in its favour". The arbitral tribunal issued an interim conservatory award and decided that "in order to secure compliance with the final award up to an estimated amount not to exceed... per Respondent, each Respondent is ordered to refrain from selling, encumbering, leasing or otherwise disposing of his interest in shares in [companies] as well as his interest in real property vested in his name as follows:... This order may be amended upon production by Respondent (or any one or more of them) of alternative security which the arbitral tribunal deems to be acceptable. In respect of each Respondent this order shall remain in force [for three months], unless one of the following events shall first occur: (1) the arbitral tribunal issues a final award dismissing the Claimant's claims against that Respondent; or (2) the arbitral tribunal issues a final award against that Respondent in an amount, including interests and costs, which is less than the value of the security provided by that Respondent (in which case the amount of such security will be reduced accordingly); or (3) the arbitral tribunal issues an award which is satisfied in full by that Respondent".

In ICC Case N°13194²², respondent accused claimant of breaching a shareholders' agreement to which both were parties. "The respondent sought the appointment of an independent analyst to determine the price of

shares held by the claimant. The claimant objected to this evaluation and brought proceedings in a US court to prevent the analyst from publishing his report. The court granted the injunction pending the outcome of arbitration proceedings, which the claimant was required to initiate in accordance with the shareholders' agreement. In the arbitration commenced in compliance with this order, the claimant requested the arbitral tribunal to find that it had not breached the shareholders' agreement. The respondent requested the arbitral tribunal to issue an interim award authorizing the analyst to issue his price determination and report. After considering the arguments of the parties, the tribunal was not persuaded that there were new, different or changed conditions sufficient to justify reversal of the preliminary injunction issued by the court. Further, Respondent failed to convince the tribunal that there was any urgency for an order releasing the valuation report, or the existence of irreparable harm to it if the valuation report was not released. Respondent's contention that the report would aid the parties in considering whether to proceed to arbitration is not sufficient to override the irreparable harm determined by the US court to exist if the valuation report were to be published. Furthermore, the request's lack of urgency was reflected by the fact that Respondent did not even request in its counterclaim that the tribunal order the transfer of the disputed shares. In light of Respondent's failure to provide any evidence of urgency with respect to its request, or to prove irreparable harm if its request was not granted, the tribunal was of the opinion that publication of the independent analyst's report should continue to be enjoined until further order of this tribunal".

c) Expertise and Mediation

Expertise and mediation are in general faster than arbitration and less expensive and time consuming. They are other instruments which may be used for settling disagreements before going to arbitration and possibly avoid reaching that point. Although expertise and mediation do not seem to override arbitration, parties may benefit from these instruments. The assistance of mediators may help avoiding deadlock situations.

Parties chose from time to time a multi-tiered process, but they must be careful in drafting unequivocal dispute resolution clauses: they must clearly define the type of mechanism for each tier (for instance ad hoc, institutional and which institution), specify whether each phase is mandatory (in such case the parties are required to submit to mediation prior to any arbitration procedure), and determine the time which should be allocated to each tier before moving to the last phase foreseen in the dispute resolution clause. They must also clearly indicate the delimitation between expert determination and arbitration²³.

In one of the cases filed before the ICC the parties agreed in their arbitration clause on the following two-tier process:

23. B. Ehle and M. Scherer "Arbitration of International M&A Disputes", Inter-Pacific Bar Association, n°47, September 2007, p. 23, <http://ipba.org/media/fck/files/IPBA%20Journal%20September%202007.pdf>. See also about the arbitration clause in M&A disputes: B. Gross "M&A disputes and expert determination: getting to grips with the issues", Cross-Border Handbooks, Arbitration 2010/2011, <http://www.practicallaw.com/4-502-2504?q=M%26A+disputes+and+expert+determination>; I. Welser "M&A Post Closing Issues: Arbitration and Third Party Joinder", Austrian Yearbook on International Arbitration, 2011, p. 3)

"1. If the Shareholders or the Board have been unable to resolve the Arbitration Matter [...] then the Shareholders shall seek to resolve the Arbitration Matter amicably by using the following procedure:

1.1 the Shareholders shall submit the Arbitration Matter to a neutral adviser appointed by agreement between the Parties to assist them in resolving the dispute. Either Shareholder may give written notice to the other [...] and propose the name of a suitable person to be appointed. If no such person is appointed by agreement between the Parties within 14 days after such notice is given, either Party may request ICC Dispute Resolution Services ADR in Paris to appoint a neutral adviser;

1.2 the Shareholders shall, with the assistance of the neutral adviser appointed in accordance with paragraph 1.1 above, seek to resolve the dispute by using an alternative dispute resolution ("ADR") procedure agreed between the Parties or, in default of such agreement, the settlement proceedings under the ICC ADR Rules; [...]

2. If the Arbitration Matter is not resolved within 30 days after the appointment of the neutral adviser or commencement of settlement proceedings under the ICC ADR Rules pursuant to paragraph 1, or any Uncured Event of Default dispute is referred to the ICC Arbitrator [...] the Arbitration Matter or any such Uncured Event of Default dispute shall be referred to and finally resolved by arbitration under the ICC Rules, which Rules are deemed to be incorporated by reference into this Part 1. [...]

22. Ibidem, footnote 21

2.4 any neutral adviser involved in the ADR procedure instituted pursuant to paragraph 1 shall not take any part in the arbitration, whether as a witness or otherwise, and any recommendations made by him in connection with the ADR procedure shall not be relied upon by either Party without the consent of the other Party and the neutral adviser; and neither Party shall make use of or rely upon any without prejudice statements or admissions made by the other Party in the ADR procedure; [...].”

In ICC arbitration case N°11477 (unpublished) the parties having disagreed on the amount of the price readjusted they submitted their dispute to an expert of an accounting firm in accordance with their contract. The expertise procedure was pending when claimants filed its request of arbitration. Respondents alleged that claimants denied the solidarity between both respondents for the sole purpose of paralyzing the expertise procedure. In a partial award the arbitral tribunal decided to examine first the standing of Respondent 2 who notified the price adjustment. If the tribunal considered that Respondent 2 had the standing to act and notify the price readjustment, the second issue to examine was whether the notification was made in accordance with the contract's requirements. If the tribunal decided that the notification was invalid, respondents would not be entitled to the price readjustment. If the tribunal decided otherwise, the price readjustment procedure pending before the expert should proceed. The majority of the tribunal decided that both respondents had the standing to notify the price readjustment, on the one hand, and on the other hand, that the notification was valid given the fact that the documents provided by respondents with the notification were in conformity with the

contractual requirements. Although the documents were not perfect, the majority considered that this default does not suffice to invalidate the notification. Consequently, the majority declared that the expert was validly entrusted with the readjustment of the price and invited respondents to take the necessary measures to proceed with the expertise. Finally, the majority decided to suspend the arbitration. After notification of the partial award to the parties, the latter have resumed the expertise procedure.

M&A disputes are submitted from time to time to the Expertise Rules of the ICC International Center for Technical Expertise or to the ADR Rules of the ICC International Centre for ADR.

In 2011, 3 out of 35 expertise cases concerned M&A disputes and 3 out of 27 ADR cases were also M&A related. In addition, 21 out of 27 of the cases were filed pursuant to a clause providing for ICC ADR contained in the contract giving rise to the dispute, and 17 of those clauses provided for a two-tiered dispute resolution process, with arbitration as a second step if the ADR proceedings were unsuccessful²⁴.

Two of the disputes submitted to expertise mainly concerned determination of the value of the shares, and the third one determination of the option price.

In one of the mediation cases, claimant claimed for an alleged overpayment of some shares, as well as post-closing and other damages. In another case, claimant alleged that respondent did not comply with its obligations with regard to the option to buy and sell, and

24. Statistical Report, ICC Bulletin, 2012, vol.23, n°1, p. 5

claimed to have suffered material losses in addition to further material and moral damages in an amount to be determined. In the third case, claimant submitted that respondent failed to indemnify claimant pursuant to the warranties and indemnities clauses.

5. ICC Case Management Techniques To Assist in Accelerating Procedures

Complexity of M&A transactions renders fast-track procedures difficult while remaining feasible. A more practical approach could be to organise and agree on the different phases of the procedure in collaboration with the arbitrators in order to control its duration.

Case management techniques may assist in achieving this goal, for instance those recommended by the ICC in Appendix IV to the ICC Arbitration Rules. A report from the ICC Commission on Arbitration on “Techniques for Controlling Time and Costs in Arbitration” published in 2007²⁵ provides a checklist of points that parties may consider when drafting an arbitration agreement and initiating an arbitration procedure, and that parties and arbitrators may contemplate during the procedure²⁶.

25. Report from the ICC Commission on Arbitration on “Techniques for Controlling Time and Costs in Arbitration”, ICC Publication n°843

26. See also Debevoise & Plimpton LLP Protocol to Promote Efficiency in International Arbitration, 2010, http://www.debevoise.com/files/News/2_cd13af2-2530-40de-808a-a903f5813bad/Presentation/NewsAttachment/79302949-69b6-49eb-9a75-a9ebf1675572/DebevoiseProtocolToPromoteEfficiencyinInternationalArbitration.pdf; UNCITRAL Notes on Organizing Arbitral Proceedings, 1996, http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1996Notes_proceedings.html; A. J. van den Berg “Organizing an International Arbitration: Practice Pointers”, The Leading Arbitrators' Guide to International Arbitration, second edition 2008, Newman Hill Editors, p. 149

The selection of experienced lawyers is among the recommendations; lawyers should not only have the necessary skills to handle M&A/JV matters, but also have experience in arbitration and be capable of devising an efficient procedure together with the opposing lawyers and the arbitrators. Similarly, the choice of the arbitrators is of utmost importance; the arbitrators must have the necessary expertise in M&A transactions, as well as experience in arbitration with strong case management skills to enable them to keep the procedure under control. The parties should make sure that the arbitrators they nominate have the required availability to devote to the arbitration entrusted to them and to render their award in a reasonable period of time. Such period and any period of the procedure may well be agreed upon when establishing the procedural timetable. In addition, the parties must make sure to appoint arbitrators who do not risk to conflict out, causing delays in the composition of the arbitral tribunal.

Likewise, the parties must ensure that some preliminary procedural aspects have been addressed either in the arbitration agreement or at the beginning of the arbitration, and will not contribute to delay the procedure, such as choice of the place of arbitration, language of the procedure, applicable rules of law, or issues of confidentiality.

Directions for the organisation of the procedure agreed upon with the parties or ordered by the arbitrators is equally important in order to put a procedure on the right track from the outset. It is the ideal occasion for trying to have all players agree on short time limits if the parties' intention is to have an expedited procedure. In ICC arbitration, when drawing up the

terms of reference or as soon as possible thereafter, the arbitral tribunal must convene a case management conference to consult the parties on procedural measures that may be adopted and establish a procedural timetable that it intends to follow for the conduct of the arbitration (Article 24 of the ICC Arbitration Rules).

Some of the measures which may be considered are for instance limitation of number and length of the submissions, identification of issues to be decided solely on the basis of documents, identification of issues that can be resolved by agreement between the parties or their experts, matters related to the production of documents (the Redfern Schedule collaborative document may be very helpful²⁷; also, parties must be conscious that discovery is not compatible with accelerated procedures²⁸), number of hearing, use of telephone or video conferences rather than meetings in person whenever possible, bifurcation of the procedure only where it is expected to result in a more efficient resolution of the case, use of information technology facilities for communications and electronic exchanges of documents. Such procedure control aimed at reducing time naturally contributes to reducing costs.

Organising an arbitration procedure and adopting appropriate measures depend on the needs of each case. Both the tribunal and the parties must be pro-active to achieve this task in the most suitable way, whether the procedure will be fast-track or will follow a normal pace.

27. (http://law.academic.ru/6270/Redfern_Schedule)

28. Y. Derains « Les responsabilités des conseils », in *Improving International Arbitration*, Liber Amicorum Michelgautet, ICC Publishing 1998, p. 119

Conclusion

A distinction must be made between fast-tracking a procedure which terminates with a final award on the merits, and an urgent measure which provides an interim decision to enable an urgent action awaiting a final decision.

Given the complexity of M&A transactions, fast-track procedures for disputes arising therefrom are rare, as can be noted from ICC statistics on fast-track cases.

The experience of the ICC which can administer arbitration procedures in any period of time agreed upon by the parties, shows that adapting specific fast-track rules will not offer more than what ICC Arbitration Rules already offer.

In addition to interim measures which can be obtained from an arbitral tribunal during an arbitration procedure, the parties may apply for emergency measures under the ICC Emergency Arbitrator before an arbitral tribunal is put in place.

The ICC also offers other dispute resolution services, expertise and mediation, which may help solve disagreements in shorter periods of time.

Considering that the complexity of M&A transactions may render fast-track procedures difficult, the parties may opt for a pragmatic approach and control the duration of the procedure by agreeing on shorter time limits for the various phases of the procedure in collaboration with the arbitrators.

Calculation of damages in M&A arbitration proceedings

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Disputes in M&A transactions

The list of disputed situations arising in the context of mergers and acquisitions is very extensive. The objective of this article is to identify the main dilemmas and issues facing the financial expert and the arbitration panel in the case of a dispute arising in connection with M&A transactions at various stages of the transaction process, in particular at the post-closing phase.

The most common reason for disputes arising at the pre-signing stage, i.e. prior to signing the SPA (Sale and Purchase Agreement) are claims arising from the failure to comply with the terms and conditions of letters of intent, preliminary contracts, non-disclosure agreements, preliminary transaction term sheets, exclusivity clauses and breaches of the principles of negotiations in good faith.¹

1. A. Carlevaris, *The Arbitration of Disputes Relating to Mergers and Acquisitions: A Study of ICC Cases*, ICC International Court of Arbitration Bulletin, vol. 24/number 1, 2013, p. 21.

The period between the signing of the SPA and the closing of the transaction (post-signing disputes) is primarily related to the performance of the conditions which must be met to finalize the process, such as obtaining the necessary permits or concessions. In these cases arbitration clauses are more frequent and sometimes include provisions related to fast track arbitration.² However, practice shows that this instrument is used to a very limited extent and is rarely associated with engaging experts for calculating damages.

The most frequently disputed situations faced by arbitration tribunals and financial experts appointed as expert witnesses are claims arising after the closing of the transaction (post-closing disputes). The problems that appear at this stage are, inter alia, issues related to the adjustment of purchase price or the breach of representations and warranties made by the seller.

2. B. Gessel-Kalinowska vel Kalisz, *Rozstrzygnięcie sporów korporacyjnych w postępowaniu arbitrażowym* [Settlement of corporate disputes in arbitration], in: *Arbitraż w Polsce* [Arbitration in Poland], PKPP Lewiatan, Warsaw 2011, p. 58.

Because of their importance and complexity, the focus in this article will be on disputes arising after the closing of the transaction. Due to the value of the claims, these are also situations in which the involvement of financial experts is the most common.

Representations and warranties

The competing interests of two parties to the transaction mean that contracts need to contain clauses mitigating the risk, for instance, related to the acquisition of contingent liabilities, as well as protecting against material adverse changes and the distortion of historical financial results, which could constitute the basis of the investment decision.

Representations and warranties in practice are frequently used as joint formulations and that is how we shall also use them for the purposes of this article. In principle, representations apply to historical events or current status³, whereas warranties apply to future events.⁴

The distortion of historical results in the financial statements, which constituted the basis of the investment decision, including the decision regarding the price based, inter alia, on the valuation methods which are applicable based on the available data, constitutes a significant category of breaches of the representations and warranties made by the seller.

3. B. Gessel-Kalinowska vel Kalisz, *Oświadczenia i zapewnienia w umowie sprzedaży udziałów w spółce z ograniczoną odpowiedzialnością (w świetle zasady swobody umów)* [Representations and warranties in a contract of sale of shares in a limited-liability company (in the light of the principle of contractual freedom)], Wolters Kluwer Polska Sp. z o.o., 2010, p. 165, 169-174. B.

4. B. Gessel-Kalinowska vel Kalisz, *Oświadczenia i zapewnienia...* [Representations and warranties...], op cit. p. 166, 169-174.

Given that the list of distortions can be extensive, we shall try to present selected, most frequently recurring areas of possible irregularities:⁵

- improper recognition or classification of revenues or expenses in the accounts;
- overstatement or understatement of balance sheet items, such as inventories, receivables and liabilities;
- overstatement or understatement of off-balance-sheet items such as contingent liabilities.

In the context of calculating damages in such situations (except in case of those regulated by the contract), depending on whether it is based on the business valuation or the valuation of lost cash flows, it is important to remember the concept of actual damage (*damnum emergens*), which the injured party suffered, as well as lost profits (*lucrum cessans*), which it could have gained had the damage not occurred. Actual damage means a deterioration of the financial situation, involving a reduction in assets or an increase in liabilities, while lost profits means the hypothetical increase in assets or reduction in liabilities, which would have taken place had the event causing the injury not occurred.

The transposition of the irregularities in the financial statements onto the value of the company and the price paid is relatively less complicated in case of adjustments closing the transaction (price adjustment). The structure of adjusting the transaction price most

5. M. Panfil, A. Szablewski, *Dylematy Wyceny Przedsiębiorstwa* [Dilemmas in Valuing a Business], Poltext Sp. z o.o., Warsaw 2013, p. 286.

frequently takes place in the locked box or completion accounts convention. The locked box model assumes that the transaction price is settled in advance using the company's existing balance sheet, with no adjustments to the closing balance. Under this approach the buyer bears a higher risk, as compared to the completion accounts mechanism, in which the transaction price is adjusted based on the closing balance of accounts, including the changes in the level of net debt and changes in working capital.

The role of this type of provision is obvious and has the purpose of protecting the purchaser against material changes in the operating activities of the business in terms of the level of cash or working capital requirements. Even so, clauses regarding, for instance, changes in working capital do not completely protect the purchaser against the seller's desire to maximize the price. In this case (i.e., when such a clause is included in the contract), the seller may be interested in disclosing as much value as possible in receivables and inventory in the closing balance – for instance, by failing to make write-offs to overdue receivables or obsolete inventory. As a result of an adjustment the purchaser will pay for assets which, theoretically, should generate a cash flow – but which the purchaser will not receive.⁶ The role of the advisors and financial personnel of the buyer is to identify those issues, as well as reduce the risk associated with them.

The determination of the value of damages in the above-mentioned example is relatively

less complicated from a financial expert's point of view, provided that he has appropriate accounting evidence. In general, damage on the part of the purchaser can be determined on a 1:1 basis – it is as much as the purchaser needs to add to the working capital to restore it to the operational level or as the amount he paid for the receivables which were not written-off and would not generate any cash flows. Of course, even in such a case, the situation may require additional analyses, for example, if there is a chance of recovery of part of the receivables. An expert should determine to what extent the amount is recoverable, which would effectively result in respective claim decrease. There is a similar situation in the case of the discovery of undisclosed liabilities, which may be also associated with the costs of interest charged by creditors, constituting part of the claim's value.

The business' ability to generate cash flows

The calculation of damages suffered by the purchaser can be a much more difficult issue in cases where not only has the balance sheet been distorted, but so have the profits and the company's profitability or, in a broader context, the loss or reduction of the capacity to generate profits. This is because the nature of these issues can have a multi-dimensional impact on the final valuation or the assessment of the value of the company, which constituted the basis of the investment decision (the question of whether the valuation was revealed in the contract is a separate issue of a legal nature). In order to properly understand these topics, the arbitrators need the financial expert to explain the methods of company valuation used by strategic or financial investors.

The two main approaches to valuation used in transactions are the comparable companies analysis or comparable transactions analysis in the market approach and the discounted cash flow (DCF) method in the income approach. These approaches can be used jointly or separately, depending on the specific nature of the transaction process, the company's business or the availability of information.

In the case of using market multiples in the market approach, the valuation is based on multiples of listed peer companies or acquisition transactions of businesses similar to the subject of the valuation, which were conducted in a period which is close to the valuation date. An investor uses the market multiple as an indication of how the market or purchasers perceive the value of companies with similar characteristics to the target, from the point of view of:

- financial results;
- factors taken into account in the capitalization: industry development prospects, profitability, capital needs (in terms of capital expenditure and working capital), liquidity, etc.

Let us look at a simplified situation of a potential investor, who acquired a company, preparing a valuation based on a P/E of 10.0x and net profit in the last year of PLN 100 million, which was significantly higher than the profits in previous years, which oscillated around PLN 80 million.

During the post-transaction analyses, the purchaser learned that the financial statements encompassed by the representations in the SPA, on the basis of which he made his investment decisions, overstated the annual net

profit in the previous year by approx. PLN 20 million. As a result of the adjustment, the net profit for the last financial year proved to be similar to the level in previous years. If the irregularities in accounting are confirmed, the main issue will be to specify whether the result of the damages calculation should be PLN 20 million, or a multiple of the unrealized profit arising from the market multiple used. Is it possible that this result will be within or outside the range set by these values?

The role of the valuation expert is to interpret the irregularities discovered and convert them into a value. In this respect, the expert has to demonstrate to the tribunal that he has extensive analytical skills and has to take into consideration a number of less obvious aspects related to the company's value. The expert has to answer the question of the nature of the possible adjustments – are they of a cash nature, i.e. resulting in actual cash outflow or are they a result of non-recurring events of an accounting nature (for instance, the previously recognized provision was reversed, which does not impact the cash flows and resulting cash level)? Will the adjustments affect the company's activities in the future? Can the profit generated in later years be lower than assumed on the basis of the distorted historical results? How can the adjustment to the profit affect the forecast of the future results in the context of the economic cycle in which the company is? Finally, can the historical distortion of the results affect the method of valuing and selecting the peer companies used for the valuation?

The extent of comparability of companies is assessed, inter alia, on the basis of the level

⁶ M. Panfil, A. Szablewski, Dylematy Wyceny... [Dilemmas in Valuing ...], op cit p. 285.

of profitability, the historical and forecasted rate of growth and the size of the company. The aspects of advantages and disadvantages as compared to the peer group are analysed in the next stage and the appropriate value of the multiple is selected on the basis of this analysis. Incorrect assumptions regarding historical profitability can therefore give rise to implications extending beyond the areas arising from the use of straightforward models.

In the case of the DCF method, within the framework of the income approach, the impact of the adjustment on the valuation can also be multi-dimensional. The questions posed in the market multiples valuation method are just as important. In the income approach, in which the value of the target is determined on the basis of expected future economic benefits arising from ownership of the target, these benefits are expressed as a revenue stream. Adjustments to the historical results can affect the forecast of that stream (in particular, the level and growth in revenues, as well as the profitability) and the assessment of the company's ability to generate profit in future years.

It is highly likely that, in the case we described earlier, the actual profitability and the level of profit will affect the entire forecast period, together with the residual period, causing a multiplier effect, just as in the case of the market approach valuation. However, the final conclusion in this respect depends on additional analyses, which are unique to every case.

Just as in the market multiples valuation, the choice of peer companies from the point of view of profitability can also affect the results of the DCF method through the calcu-

lation of the cost of capital used to discount the future cash flows (because the calculation of the cost of capital is generally based on an analysis of the parameters of peer companies). When free cash flows to equity (free cash flows to equity, FCFE) formula is used in the DCF – through the beta parameter (specifying the volatility of the stock as compared to market index), as well as through market capital structure used to relever beta and calculate the cost of equity. In the case of free cash flow to equity owners and creditors (free cash flow to firm, FCFF), the same cost of equity and capital structure are the elements of the calculation of weighted average cost of capital (WACC).

Ex ante and ex post approach in respect of business valuation and lost profits analysis

The aforementioned methods are used, inter alia, in disputes concerning irregularities in the presented financial results, which would eventually affect the final price paid, or in case of permanent loss or total destruction of the business value. The damage resulting from the breach of contract or associated with the loss of other identifiable cash flows (for example related to a specific investment project) is often analyzed under lost profits approach. Lost profits methodology compares the actual stream of cash flows as at the dispute date (legal proceedings date) with the hypothetical stream of cash flows that would have been achieved if the alleged wrongdoing had not occurred.

Business valuation is performed most commonly under ex ante approach. This approach is based on the knowledge that the parties had or could have had if all the necessary

Table 1. Summary of differences in damages calculations.

	Business Valuation	Lost Profits Analysis
Valuation date	Date of legal wrongdoing	Date close to legal proceedings
Information used	Available or forecasted as at the valuation date (ex ante)	Available as at legal proceedings date or report preparation date (ex post)
Cash flows	Cash flows expected as at the valuation date	Expected cash flows, adjusted by information after alleged wrongdoing
Discount rate	Higher, including risk related to the uncertainty of realization of the forecasted cash flows	Lower, including limited risk related to current knowledge
Discounting	Discount cash flows as at the valuation date	1) Historical cash flows indexation in relation to the valuation date 2) Discount expected lost cash flows after the valuation date

Source: Based on Damages Measurement and the Business Valuation Report – Challenges and Pitfalls, Everett P. Harry, Business Valuation Review, Volume 30, Number 2, 2011, p. 58.

information had been disclosed before or during the transaction.⁷ It takes into account the effect of uncertainty of future cash flows (the economic benefits which the purchaser is to obtain after the transfer of ownership), among others, through the use of an appropriate discount rate, taking into account the risk related to a particular business. This rate most frequently reflects the cost of equity or weighted average cost of capital, depending on the valuation methodology and may be significantly higher than the rate used in the case of an ex post analysis.

Lost profits analysis is based in vast majority of cases on ex post approach. It is applicable, inter alia, in the calculation of damages, resulting from a loss of contract through

the fault of the seller or the contract parameters, with respect to which incorrect warranties were made. An ex post approach assumes the calculation of damages based on all the knowledge available and events known after the alleged wrongdoing has taken place (after the transaction date) as at the date close to the date of the statement of claim or the date on which the expert report is prepared. The damage is then valued on the basis of actual data by comparing the facts (revenues, profitability) of the given contract with the hypothetical situation, which could have taken place “but for” the alleged wrongdoing. The use of an ex post methodology and the use of all available information reduces to some extent the risk related to the uncertainty of events. In order to analyze the hypothetical scenario we still use assumptions and forecasts, however, they are based on current knowledge about the market trends and economic conditions.

7. M.J. Wagner, M.K. Dunbar, R.L. Weil, Ex ante versus ex post damages calculations, in: Litigation Services Handbook: The Role of the Financial Expert, 4th Ed., John Wiley & Sons, Inc., New Jersey 2007, p. 2.

A good example of differences between the ex ante and ex post approaches may be a hypothetical transaction of the purchase of a real estate developer. Let us assume that one of the warranties regarding the conditions for the development of one of the plots of the developer's land proves to be untrue, which, consequently, results in the failure to develop the project at this site. In his analysis (valuation of the company), the investor assumed the successful development of all projects and therefore filed a claim against the seller.

An expert calculating the damage based on an ex ante analysis can apply an approach based on the difference between a valuation of the company under the original assumptions (which will be based exclusively on the costs of construction, sales prices of real estates and other information which has been or could be available on the date of the transaction) and a valuation that would have been prepared if the project was not taken into account for formal reasons, i.e. on the basis of the factual situation as of the transaction date.⁸ Meanwhile, unfavourable trends could have appeared on the construction materials market (increase in prices) or the real estate market (drop in prices) after the transaction, which, even if the appropriate permits were obtained, would result in a reduction in profitability or even lack of feasibility of the given project. These elements should be taken into account in the hypothetical scenario, the value of which would be compared with the actual scenario (failure to develop the project) in an

8. Another issue to be considered by the expert is whether the initial valuation was properly performed, for example, whether the discount rate was properly selected.

ex post approach.⁹ In this example the value of the damages estimated on the basis of the two approaches mentioned above may differ substantially.

From the point of view of an expert in arbitration proceedings, a good understanding of the economic events for which the seller is not responsible or information which the seller could not have had on the date of making the warranties is also important. This may also be of importance in case of adverse changes in the operations of the acquired business, which emerge after the transaction. They can be a part of the risk borne by the purchaser (e.g. loss of some customers or a loss of key employees), which the purchaser can try to include as an element of the claim against the seller, even though the seller may not necessarily be liable for them.

A specific situation, in which arguments "for and against" individual approaches to the valuation of damages should be considered, is that in which it is possible to eliminate the effects of the defective representations or warranties and restore the company to the condition which was expected by the investor. A hypothetical purchaser of a manufacturing company with defective production technology, resulting in the withdrawal of certain products from the market may incur capital expenditures to modify the production line. This situation will require additional cash to be invested, but if this causes the loss of profits to be temporary, it may become a profitable solution. In the

9. It should be noted that despite the discount rate in ex ante approach should take into account the risk of not performing the financial projections and is higher than in ex post approach, it may still not include highly improbable events.

situation in which the expert was to value the company, for instance using the income approach (DCF), by permanently eliminating the cash flows (forecasted as at valuation date) related to the problematic category of products, the damage arising from the comparison with the original valuation could be significantly higher than the actual loss of cash flows.

An alternative method of assessing damages is therefore the analysis of the cash flows in the period in which it has an actual impact on the company's business. At the same time, it is important to carefully analyse any possible capital expenditures which will have to be incurred to recover the desired condition of the acquired business and to take that into account in the calculation (effectively increasing the amount of the claim). The scenario prepared under these assumptions should then be compared with the hypothetical situation which the purchaser assumed, i.e. in which it could sell the products on the market without any obstacles. If such an analysis is carried out on the basis of the ex post concept, the expert should also remember to consider the effects of any possible external factors – for example, a sudden and unexpected decline or growth in demand on the market of similar products.

In the selection of the method of calculating damages, whether using the described methods or opting for different solutions (e.g., the hybrid approach, which combines the elements of an ex post and ex ante approach), an expert should always be guided by the circumstances of the case and the economic legitimacy of the approach applied to the calculation. Most importantly he should be aware of the key principle,

according to which the interpretation of the legal aspects is beyond the area of his competence and should remain the exclusive domain of the arbitrators.

Arbitration in Corporate Disputes in Brazil

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Introduction

The Brazilian Corporate Law (Law n. 6.404/1976) was amended by Law n. 10.303/2001, which introduced a set of important changes aiming to improve the Brazilian securities market. One of these modifications was the introduction of paragraph 3 in Article 109¹ of Law n. 6.404/1976, allowing companies to provide for arbitration clauses incorporated into their bylaws, applicable to the disputes between the company and its shareholders, or between minority and controlling shareholders.

The development of the domestic legal system, with the enactment of Law n. 9.307/1996, the Brazilian Arbitration Law, together with advances in corporate governance, ushered in progress of initiatives regarding choice of arbitration for resolving corporate disputes².

1. Law n. 10.303/2001 introduced paragraph 3 in Article 109 of the Law n. 6.404/1976: "Corporate bylaws may set forth that controversies between the shareholders and the corporation or between the controlling shareholders and the minority shareholders, be solved by the use of arbitration".

2. It is important to stress that the Brazilian Supreme Court declared, only in 2001, the constitutionality of relevant provisions of the Arbitration Law, as Art. 7, which provides for specific performance of arbitration clauses.

Moreover, securities market entities, both governmental and private, began to encourage inclusion of arbitration clauses into corporate bylaws, particularly into those of publicly-held companies³, which have their shares negotiated at BM&FBovespa (the Stock Exchange).

This article analyzes the most recent corporate governance and arbitration developments in Brazil. With this purpose, the figure and the importance of the New Market (Novo Mercado), created by BM&FBovespa (Brazilian Stock Exchange) will be described, as well as its recent evolution, followed by the description of the new arbitration rules of the Market Arbitration Chamber (CAM – Câmara de Arbitragem do Mercado).

The New Market

In December 2000, BM&FBovespa created the New Market and set up corporate

3. N. Eizirik, *Some Remarks on Arbitration in Corporate Law*, in: J. de Paiva Muniz and A.T. Palhares Basilio, *Arbitration Law of Brazil: practice and procedure*, New York: JurisNet, 2006, APP E-2.

governance listing levels for the shares negotiated in the Stock Exchange, seeking to adopt the best corporate governance practices, beyond the scope of Brazilian Corporate Law. Corporations which opted to have their shares listed in one of those segments would have to comply with the rules of each listing level. There are three corporate governance listing levels (Level 1, Level 2 and "New Market").

Level 1 basically requires improvements in disclosing information to the market and to investors in general, as, e.g. for example, the disclosure of securities transactions involving company management or controlling shareholder and disclosure of contracts between the company and related-parties. It also requires keeping a free-float of at least 25% of total capital; improvements in quarterly information reports, including disclosure of consolidated financial statements, cash flow statement, and special audit review; also, disclosure of an annual corporate events⁴ calendar.

Level 2 requires compliance with the following rules, in addition to Level 1 rules: disclosure of financial statements in accordance with the US GAAP or IFRS standards; a unified maximum two year term for the entire board of directors, which must be comprised of at least five members, out of which 20% must be considered independent, in accordance with the definition provided by the

4. Available at: <http://www.bmfbovespa.com.br/en-us/markets/equities/companies/corporate-governance.aspx?idioma=en-us>.

rules⁵; voting rights granted to non-voting (preferred) shares in certain corporate decisions such as mergers, spin-offs, approval of contracts between the company and other firms in the same group when deliberation occurs at the general meeting; tag-along rights for non-voting shareholders, who ought to receive at least 80% of the price paid for the controlling shareholder's voting shares in a transfer of control; obligation to hold a tender offer for the economic value of the shares in case of delisting or going-private transactions; and adherence to the Arbitration Chamber of the Stock Exchange for corporate dispute resolution.

New Market requires compliance not only with Level 1 and Level 2 provisions but also with the following rules: all shares must be voting shares; and in case of a transfer of control, tag-along rights must be granted to all minority shareholders, who must receive the same price paid for the shares held by the controlling shareholder.

5. According to the New Market Listing Rules: "Independent Member" is a member of the Board of Directors who: (i) has no ties to the Company except for owning an equity share in its capital stock; (ii) is not a Controlling Shareholder, the Controlling Shareholder's spouse or a relative to the second degree, is not, or has not been linked in the last 3 (three) years, to a company or entity with ties to the Controlling Shareholder (this restriction does not apply to persons linked to governmental educational and research institutions); (iii) has not been a Senior Manager of the Company or employed by, or worked for the Company, the Controlling Shareholder or any other company controlled by the Company; (iv) is not a direct or indirect supplier or purchaser of the Company's services or products or both, to a degree resulting in loss of independence; (v) is not an employee or manager of a company or entity supplying services or products or both to, or buys these from, the Company; (vi) is not a spouse or a relative to the second degree of any Senior Manager of the Company; (vii) does not receive any compensation from the Company except for that related to his/her activities as member of the Board of Directors (this restriction does not apply to cash from equity interests in the capital stock).

The listing level rules were subject to debate in 2010. A new set of provisions was proposed and subjected to the approval of the listed companies. According to level rules, the new rules would be deemed approved in case no more than 1/3 of the listed companies expressly rejected the change.

Certain changes in the rules were denied, e.g. for example, increase in the number of independent board of directors members, requirement for listed company bylaws to establish an obligatory audit committee, and a mandatory bid in the case of a shareholder purchasing more than 30% of the issued shares.

However, new provisions were added to the New Market rules: prohibition for the same person to hold both positions of CEO and chairman of the board of directors; a prohibition of establishing bylaws rules, known as “Brazilian poison pills”, which are designed to inhibit hostile take-overs, and the requirement that the Board of Directors state its position, regarding tender offers, bearing as object the Company-issued shares.

The set of protections imposed by the New Market is deemed to increase company attractiveness to the Brazilian Stock Exchange. From 2004 to 2010, over 72% of all Brazilian IPOs were held in the New Market, and all new listings since 2004 have taken place in one of the listing segments. A significant part of the recent Brazilian capital market success is attributed, to a significant extent, to the credibility created by the New Market regulations⁶.

6. R. J. Gilson, H. Hansmann and M. Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the U.S., and the EU*, March 1, 2010, available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1541226.

At present, 129 corporations are listed in the New Market, 20 in Level 2 and 33 in Level 1⁷. In comparison, the Market Arbitration Chamber has dealt with only 5 cases in 2010, increasing to 16 in 2012. From all 28 arbitral proceedings handled by the Chamber, 13 involved M&A cases.

Mandatory Arbitration Clause in bylaws

As mentioned above, the publicly-held companies which have their shares listed in one of the premium BM&FBovespa listing segments must include an arbitration clause in their bylaws. These companies have to adhere to the Market Arbitration Chamber, the institution created by BM&FBovespa in June 2001⁸.

The Market Arbitration Chamber stands as the forum to settle both corporate and stock market disputes. It was initially designed for the resolution of disputes arising out of an environment where the companies from the special BM&FBovespa listing segments operate. Nevertheless, anyone willing to settle conflicts whose core is related to corporate issues or the stock market may

7. Data about IPOs in Brazil are available at: <http://www.cvm.gov.br/ingl/indexing.asp>

8. Article 1 of the Market Arbitration Chamber Rules states: “1.1 These rules govern the use of arbitration to settle disputes among Participants in the markets managed by BM&FBovespa S.A. – Securities, Commodities and Futures Exchange (“BM&FBovespa”) in connection with shareholder and partnership issues or contractual matters disciplined by corporate law (Lei das S.A.), company bylaws, or the rules and regulations applicable to the capital markets in general. 1.2 The term “Participants” used in these Rules refers to the companies whose securities are admitted for trading on BM&FBovespa’s special listing segments, their controlling shareholders and other shareholders, their directors, managers and supervisory board members, and investors and intermediaries in transactions involving securities issued by such companies or instruments linked to such securities”.

use it, either as BM&FBovespa-listed, or institutional investors⁹.

In this sense, the New Market regulation, in its article 13.1, specifically sets forth that “BOVESPA, the Company, its Controlling Shareholder, Senior Managers and Fiscal Council members agree to refer to arbitration any disputes related to these Listing Rules, the Novo Mercado Agreement, the Arbitration Clause, particularly regarding their enforcement, validity, effectiveness, construction, violation and related effects, before the Market Arbitration Chamber, under the Arbitration Rules”.

At the end of 2010, in addition to the publicly-held companies which have their shares in the segments that require an arbitration clause in their corporate bylaws, an important Brazilian company, Petrobras, not listed in any of these segments, decided to include arbitral clauses. A total of 135 Brazilian companies opted to adhere to arbitration for settlement of their corporate disputes. In June 2011, this number had already increased to a total of 140 publicly-held companies.

The Chamber’s rules were modified, in 2011, in order to improve the quality of the proceedings held before the Market Arbitration Chamber, seeking to consolidate arbitration as the best path to solve corporate matters. Reflecting international best practices in arbitration, the current rules allow the joinder

9. Article 1.3 of the Market Arbitration Chamber Rules: “In addition to Participants, any other natural or legal persons, funds or estates may adopt these Rules to settle disputes provided such disputes relate to business law”.

of third parties¹⁰ (Article 6.1)¹¹ and the consolidation of proceedings involving issues of fact or law in common with proceedings already underway (Art. 6.2)¹². The 2012 ICC Arbitration Rules, as well as the 2012 Lewiatan Court of Arbitration Rules, for example, have also established the possibility of joinder of third parties¹³ and consolidation¹⁴.

Consolidation became possible when the commission tasked with proposing amendments to the rules concluded that different shareholders could commence different arbitral proceedings, regarding the same arbitral clause and facts. Thus, the new rules establish that, upon receiving an application for arbitration with the same object or cause of action as from

10. About Joinder: “Joinder of third parties or their intervention in the proceedings is a well known feature in litigation in state courts. For reasons of efficient administration of justice national court rules allow the joinder of third parties, irrespective of whether all parties concerned agree. The only requirement is, in general, that such joinder is necessary for reasons of procedural economy and the effective administration of justice, since the cases involve the same issues and are closely related. The power to compel the parties to participate in those proceedings stems from the national court’s sovereign power.” J. M. Lew, Loukas A. Misteli, S. M. Kröll. *Comparative International Commercial Arbitration*. Kluwer Law International, 2003, p. 389.

11. “6.1. Joinder of parties. Before any arbitrators have been appointed, the parties may request the inclusion of one or more additional parties in the arbitration proceedings by filing a Motion for Joinder of Parties (“Motion for Joinder”). Third parties with a legitimate claim to join or intervene in the proceedings may request permission to do so by filing a Motion for Joinder”.

12. “6.2. Consolidation of proceedings. When Requests for Arbitration involve issues of fact or law in common with arbitration proceedings that are already under way and are governed by these Rules, the President of the Arbitration Chamber may direct that the proceedings be consolidated after hearing the parties and taking into consideration the circumstances and progress already achieved in the proceedings in question”.

13. Article 7 of the 2012 ICC Arbitration Rules and §20 of the 2012 Lewiatan Court of Arbitration Rules.

14. Article 10 of the 2012 ICC Arbitration Rules and §28 of the 2012 Lewiatan Court of Arbitration Rules.

another proceeding, the President of the Chamber may decide to consolidate such proceedings after hearing the parties. However, the rules also limit the period for consolidation to take place to the evidence-production stage¹⁵, in order to prevent the arbitral tribunal from issuing an arbitral award based on different evidence.

Subjective and Objective arbitrability

Finally, it is important, when referring to arbitration in M&A matters, to examine a number of concerns regarding objective and subjective arbitrability.

The issue of arbitrability of a dispute arises under two circumstances. The first refers to the possibility of certain individuals or entities being deemed able to submit their disputes to arbitration because of their status or function, known as “subjective arbitrability” or “arbitrability *ratione personae*.” The second circumstance emerges when a discussion exists regarding the subject submitted to the arbitral tribunal, known as “objective arbitrability” or “arbitrability *ratione materiae*”¹⁶.

Regarding objective arbitrability, the Brazilian Arbitration Law established that arbitration disputes be related to freely disposable patrimonial rights¹⁷. This means that only conflicts related to rights which can be evaluated

15. “6.2.1. Consolidation of proceedings is possible only in evidence production stage of the arbitration proceeding”.

16. N. Eizirik, *Lei das S/A Comentada*, v. 1, São Paulo: Quartier Latin, pp. 612-613 and E. Gaillard and J. Savage (eds.), *Fouchard, Gaillard and Goldman on International Commercial Arbitration*, Kluwer Law International, 1999, pp. 312-313.

17. Article 1 of the Brazilian Arbitration Law: “persons capable of contracting may settle through arbitration disputes related to patrimonial rights over which they may dispose”.

monetarily and disposed of by the parties be subjected to arbitral proceedings in Brazil.

As the companies’ main purpose is to make profits and share them among shareholders, corporate matters commonly refer to patrimonial rights, and are, therefore, subject to arbitral proceedings, if so envisaged in the corporate bylaws.

For example, all issues related to decisions made at shareholders’ meetings can be considered arbitrable. The shareholders’ meeting has the power of changing its own previous decisions. This means that the general meeting may replace a null decision by a valid one. There is, therefore, a certain power to dispose on the resolution effects, which clearly makes this matter likely to be subjected to an arbitral decision.

In this sense, an objective standard to define arbitrability questions was created: everything that can be validly decided inside corporation is arbitrable, because it is within the corporation’s private autonomy¹⁸. So, for example, there are arbitrable questions related to: distribution of dividends; liability of officers; voting rights; appraisal rights.

Subjective arbitrability leads to further problems in arbitrations related to corporate matters. This refers to the identification of those bound by the arbitration clause. The intention

18. N. Eizirik, *Some Remarks on Arbitration in Corporate Law*, in: J. de Paiva Muniz and A. T. Palhares Basilio, *Arbitration Law of Brazil: practice and procedure*, New York: JurisNet, 2006, p. APP E-13 and A. Zoppini, *I diritti disponibili relative al rapporto sociale el nuovo arbitro societario*, *Rivista delle società*, set./ott/ 2004, fasc. 5, pp. 1180-1181.

of the parties has to be clear and undisputed¹⁹, as this is the cornerstone of arbitration, considering that the parties must decide together to place state power aside. One of the major issues regarding the use of arbitration in corporate disputes is related to agreement by the shareholders to have their disputes resolved through arbitration.

If the arbitral clause is included in the corporate bylaws when the company is formed, all shareholders will be bound by it. Those that become shareholders at a later stage will also have to adhere to the arbitration clause, since this clause also reflects the shareholders duties and rights. They agree to the corporate bylaws as a whole²⁰, albeit not expressly agreeing to the arbitration clause, upon their becoming shareholders.

Nevertheless, the problem arises when the corporate bylaws is modified to include the arbitration clause. Would all shareholders be automatically bound by it? Considering that arbitration is connected to the principle of parties’ autonomy, it would not be possible to force shareholders, who have expressly voted against the inclusion of this clause.

In our opinion, the arbitration clause will only have effect upon those who have agreed to it, those who have abstained from it, or those who were not present at the general shareholders’ meeting which decided about arbitral clause inclusion in the bylaws.

19. The only formal requirement of the arbitration clause is to be in written form, according to Article 4, § 1 of the Brazilian Arbitration Law: “The arbitration clause shall be in writing contained in the contract itself or in a separate document referring thereto”.

20. N. Eizirik, *Lei das S/A Comentada*, v. 1, São Paulo: Quartier Latin, pp. 616-617.

Most scholars in Brazil understand that arbitrations involving corporate disputes do not represent a special situation requiring encompasses different treatment as to other private relations in which the arbitral clause is found. This means that, in case the majority of the shareholders decides to include it in the corporate bylaw, this decision should not be overruled by the minority’s wish²¹.

In this sense, the company should find no problem regarding the efficacy of the arbitral clause, considering that the issues of objective and subjective arbitrability can be overcome.

Conclusion

In the past 16 years, Brazilian corporate rules have undergone several changes regarding corporate governance and arbitration. The listing levels and the New Market have created a system in which the corporations, seeking to achieve a “quality standard”, adhere to these segments and, as a consequence, to the Market Arbitration Chamber for resolving of corporate disputes.

Arbitration is becoming the most common form of resolving commercial and corporate issues in Brazil. Although the Brazilian Arbitration Law is still recent, Act n° 36/2012 was enacted on 22 November 2012, by the president of the Brazilian national congress, creating a commission to analyze a new arbitration bill.

21. D. Bessone Barbosa Moreira, *Notas sobre a Eficácia da Cláusula Compromissória Estatutária*, *Revista de Direito Mercantil, Industrial, Econômico e Financeiro*, v. 126. São Paulo: Malheiros, 2002, pp. 129-139; P. A. Batista Martins, *A Arbitragem nas Sociedades de Responsabilidade Limitada*, in: J. M. Rossani Garcez and P. A. Batista Martins (coords.), *Reflexões sobre Arbitragem – In Memoriam do Desembargador Cláudio Vianna de Lima*. São Paulo: Ltr, 2002.

The Brazilian arbitration community appears to be content with the current law, but the Brazilian Senate seems to believe that it is time to adapt it to new international trade demands.

The suggested amendments concern, among others, submission to corporate dispute arbitration. The Committee will discuss whether there is a need for the Brazilian Arbitration Law to address the issue as to whether minority shareholders should have to comply with the arbitration clause contained in the corporate bylaws.

Publicly-held companies, through the corporate governance and arbitration advances in Brazil, as well as the introduction of paragraph 3, Article 109, into the Brazilian Corporate Law, have been leaning towards adopting arbitration for dispute resolution. This is exactly one of the goals of the New Market and of the Market Arbitration Chamber, as arbitral proceedings render quicker and technically more consistent solutions than state courts.

EU Commitment Arbitrations – A Brief Introduction

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Introduction

This article endeavours to provide an introduction to a novel type of arbitrations that have increasingly arisen in the context of the European Commission's behavioural remedy practice in the field of European Union (EU) competition law. These arbitrations are commonly referred to as "EU commitment arbitrations" and typically serve the private enforcement of behavioural commitments under the EU Merger Regulation¹ or the EU Modernisation Regulation, Regulation 1/2003^{2,3}.

1. Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (OJ L 24, 29.1.2004, p 1).

2. Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty [now Articles 101 and 102 TFEU] (OJ L 1, 04.01.2003, pp 1-25).

3. For an in-depth discussion, see M. Blessing, *Arbitrating Antitrust and Merger Control Issues* (Helbing & Lichtenhahn, 2003); F. Heukamp, *Schiedszusagen in der Europäischen Fusionskontrolle* (Carl Heymanns Verlag, 2006); G. Blanke, *The Use and Utility of International Arbitration in EU Commission Merger Remedies: A Supranational Paradigm in the Making?* (Europa Law Publishing, 2006); and G. Blanke & P. Landolt (eds), *EU and US Antitrust Arbitration: A Handbook for Practitioners* (Kluwer Law International, 2011), in particular Chapters 30 and 46, and the extensive bibliography cited there. For a summary overview, also see G. Blanke, "EU Competition Arbitration", in L. Ortiz-Blanco, *EU Competition Procedure* (Oxford University Press, forthcoming 2013) pp 1071-1108.

By way of background, under Articles 6 and 8 of the EU Merger Regulation, undertakings may obtain conditional clearance of a proposed concentration that raises competition concerns in the internal market from the EU Commission provided they offer sufficient remedies to allay the prevailing competition concerns. Such remedies may be either structural (e.g. a divestiture) or behavioural (e.g. a promise to adopt competition-compliant market behavior post merger) in nature, or a combination of the two. A similar regime has been adopted within the context of anticompetitive practices and dominant positions under Articles 101 and 102 of the Treaty on the Functioning of the European Union (TFEU) by virtue of Articles 7 and 9 of Regulation 1/2003. These Articles empower the EU Commission to make binding on potentially infringing undertakings behavioural commitments to allay the Commission's competition concerns. The EU General Court has expressly accepted the admissibility of behavioural in lieu of structural commitments in EU merger control.⁴ Likewise, out of considerations of proportionality, the EU Commission has expressed a clear policy

4. Case T-102/96 – *Gencor v Commission*, Judgment of the European Court of First Instance of 25 March 1999, [1999] ECR II-753.

preference for behavioural over more burdensome structural commitments within the context of Regulation 1/2003⁵.

To be viable, a behavioural commitment requires medium- to long-term monitoring. Given its own limited resources, the EU Commission has accepted to outsource such monitoring through arbitration commitments to the market itself. This practice has variously been endorsed by the EU Commission as well as the EU General Court⁶. More specifically, the revised Notice on Remedies elevates the use of arbitration commitments for monitoring purposes in EU merger control to a policy objective⁷ and the EU General Court has affirmed the quasi-structural effect of a purely behavioural commitment that is supported by an

5. See Recital (12), Regulation 1/2003.

6. See Case T-158/00 - ARD v. Commission, Judgment of the Court of First Instance of 30 September 2003; and T-177/04 - easyJet Airline Co Ltd v European Commission, Judgment of the European Court of First Instance of 4 July 2006.

7. Paras 66 ("[...] In order to render them effective, those [i.e. non-structural] commitments have to contain the procedural requirements necessary for monitoring them, such as the requirement of separate accounts for the infrastructure in order to allow a review of the costs involved, and suitable monitoring devices. Normally, such monitoring has to be done by the market participants themselves, e.g. by those undertakings wishing to benefit from the commitments. Measures allowing third parties themselves to enforce the commitments are in particular access to a fast dispute resolution mechanism via arbitration proceedings (together with trustees) or via arbitration proceedings involving national regulatory authorities if existing for the markets concerned. If the Commission can conclude that the mechanisms foreseen in the commitments will allow the market participants themselves to effectively enforce them in a timely manner, no permanent monitoring of the commitments by the Commission is required. In those cases, an intervention by the Commission would only be necessary in cases where the parties do not comply with the solutions found by those dispute resolution mechanisms."; my emphasis), Commission notice on remedies acceptable under Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004 (OJ C267/1, 22.10.2008).

arbitration commitment⁸. Other European institutions have equally greeted the Commission's practice with approval.⁹

The importance of the Commission's practice is also borne out by its statistical significance. Since 1992 to date, the Commission has deployed around 65 arbitration commitments from amongst a total of 318 conditional merger clearance decisions, which translates into around 20% of the Commission's overall *acquis* in the area.¹⁰ Equally, in the context of Regulation 1/2003, the Commission has adopted a total of six Article 9 commitment decisions making arbitration commitments binding on the undertakings concerned under both Articles 101 and 102 TFEU.¹¹ For the avoidance of doubt, any considerations made in the following apply to commitment arbitrations in EU merger control and under Regulation 1/2003 *mutatis mutandis*. Given the overall more significant *acquis* of the EU Commission in the former, the remainder

8. See fn 6.

9. E.g. the Organization for Economic Cooperation and Development (OECD), Report on Remedies in Merger Cases, DAF/COMP(2011)13, electronically accessible at www.oecd.org/daf/competition/RemediesinMergerCases2011.pdf, especially at 13 and 25 et seq.

10. For relevant statistics and a detailed table of the Commission's *acquis* as at September 2009, see G. Blanke & P. Landolt, EU and US Antitrust Arbitration: A Handbook for Practitioners (Kluwer Law International, 2011) pp 1925-2062. For more recent additions, see G. Blanke, "EU Competition Arbitration" in L. Ortiz-Blanco, EU Competition Procedure (Oxford University Press, forthcoming 2013) para 29.35.

11. For a complete inventory, see G. Blanke, "International Arbitration and ADR in Remedy Scenarios Arising under Articles 101 and 102 TFEU" in G. Blanke & P. Landolt (eds), EU and US Antitrust Arbitration: A Handbook for Practitioners (Kluwer Law International, 2011) paras 30-166 et seq. For more recent additions, see G. Blanke, "EU Competition Arbitration" in L. Ortiz-Blanco, EU Competition Procedure (Oxford University Press, forthcoming 2013) para 29.34.

of this article will disproportionately focus on the use of arbitration commitments in EU merger control.

I. Access commitments, implementation agreements and arbitration commitments

Arbitration commitments are invariably deployed to enforce so-called access commitments, i.e. promises from e.g. a merged entity to provide access on fair, reasonable and non-discriminatory (FRAND) terms to a third-party beneficiary (invariably a competitor) to an essential facility controlled by the merged entity post merger. As a corollary, arbitration commitments typically feature in the implementation of behavioural commitments in network industries, such as aviation¹², rail¹³, information technology¹⁴,

12. In relation to arbitration commitments in EU merger control: E.g. Comp./M.3280 - Air France/KLM, Commission decision of 11 February 2004 (OJ 060, 9.3.2004, at p.5); IV/M.616 - Swissair/Sabena II, Commission decision of 20 July 1995 (OJ C200, 4.8.1995, at p.10); Comp./M.3770 - Lufthansa/Swiss, Commission decision of 4 July 2005 (OJ C204, 20.8.2005, at p.3); Comp./M.3940 - Lufthansa/Eurowings, Commission decision of 22 December 2005 (OJ C18, 25.1.2006, at p.22); Comp./M.5335 - Lufthansa/SNAH, Commission decision of 22 June 2009; Comp./M.5364 - Iberia/Vueling/Clickair, Commission decision of 9 January 2009; Comp./M.5440 - Lufthansa/Austrian Airlines, Commission decision of 28 August 2009; and Comp./M.6447 - IAG/BMI, Commission decision of 30 March 2012. In relation to commitments under Article 9 of Regulation 1/2003: COMP/39.596 - BA/AA/IB, Commission decision of 14 July 2010.

13. In relation to commitments in EU merger control: Comp./M.4746 - Deutsche Bahn/English Welsh & Scottish Railway Holdings (EWS), Commission decision of 6 November 2007 (not yet published) Comp./M.5579 - TLP/ERMEWA, Commission decision of 22nd January 2010.

14. E.g. Comp./M.5984 - Intel/McAfee, Commission decision of 26 January 2011 in relation to commitments under EU merger control.

telecommunications¹⁵ and oil and gas¹⁶, which lend themselves to access commitments. These commitments seek to regulate the way and manner of access granted to eligible third-party beneficiaries, including e.g. the pricing terms and the volume of access to be provided.

In practice, access commitments are implemented through implementation or access agreements that provide for third-party access on the terms and conditions prescribed in the underlying conditional merger clearance or commitment decision. The access agreement will contain all relevant terms and conditions necessary for the full implementation in practice of the access commitments. As such, it will also contain an arbitration clause that replicates the wording of the arbitration commitment and essentially provides for the reference to arbitration of any disputes arising from the implementation of the access agreement. The access agreement will be concluded between

15. E.g. IV/M.1185 - Alcatel/Thomson CSF-SCS, Commission decision of 4 June 1998; Comp./JV.37 - BskyB/Kirch Pay TV, Commission decision of 21st March 2000; Comp./M.1795 - Vodafone Airtouch/Mannesmann, Commission decision of 12 April 2000; Comp./M.2050 - Vivendi/Canal+/Seagram, Commission decision of 13 October 2000; Comp./M.2803 - Telia/Sonera, Commission decision of 10 July 2002; Comp./M.2903 - Daimler-Chrysler/Deutsche Telecom/JV, Commission decision of 30 April 2003; Comp./M.3916 - T-Mobile Austria/Tele.ring, Commission decision of 26 April 2006; Comp./M.3998 - Axalto/Gemplus, Commission decision of 19 May 2006; Comp./M.4504 - SFR/Tele 2 France, Commission decision of 18 July 2007; Comp./M.6095 - Ericsson/Nortel Group (MSS & Global Services), Commission decision of 2nd March 2011 (not yet published) in relation to commitments under EU merger control.

16. E.g. IV/M.235 - Elf Aquitaine-Thyssen/Minol, Commission decision of 4 September 1992; Comp./M.2389 - Shell/DEA, Commission decision of 20 December 2001; Comp./M.2533 - BP/E.ON, Commission decision of 20 December 2001; Comp./M.4180 - Gaz de France/Suez, Commission decision of 14 November 2006 in relation to commitments under EU merger control.

the commitment debtor, e.g. the merged entity, and the third-party beneficiary. Being a private law instrument concluded between the commitment debtor and the third-party beneficiary, its terms and conditions – including the arbitration clause – will produce binding effects on both of them.

This stands in marked contrast to the arbitration commitment, which is unilaterally binding on the commitment debtor only and thus resembles the notion of “arbitration without privity” known from the investment arbitration context¹⁷. In this sense, arbitration commitments constitute unilateral standing offers to arbitrate from e.g. the commitment debtor to the third party-beneficiary. The arbitration commitment, which is directly effective within the meaning of EU law,¹⁸ may be triggered at the discretion of the third-party beneficiary only. This being said, in the alternative, the third-party beneficiary remains free to seek enforcement of the deficient implementation of the commitments either through a private enforcement action against the commitment debtor before a competent Member State court or by way of third-party complaint to the EU Commission.

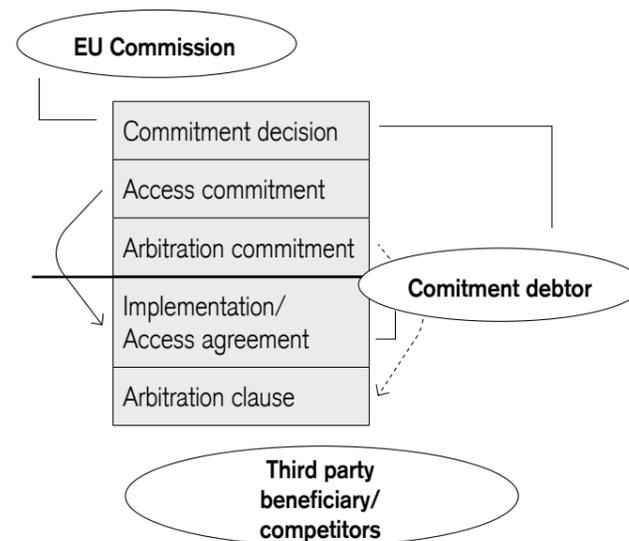
This being said, once an access agreement has been put in place, it is more likely than not that the arbitration obligation of the original

17. G. Blanke & B. Sabahi, “The New World of Unilateral Offers to Arbitrate: Investment Arbitration and EC Merger Control”, 74(3) *Arbitration* (2008) pp 211–224.

18. Given that it (i) is sufficiently precise (which most of the arbitration commitments are, their wording being sufficiently clear to enable the commencement and conduct of entire arbitration proceedings); (ii) does not require any national implementing measures (*idem*); and (iii) confers a right upon an individual (most arbitration commitments entitle third-party beneficiaries to enforce the substantive rights they derive from a commitment decision before an arbitration tribunal).

arbitration commitment has been extended to the third-party beneficiary through a widening of the arbitration clause, as a result of which the arbitration provision contained in the access agreement will be mutually binding on both the commitment debtor and the third-party beneficiary.

The following diagram visualises this logic:



II. Advantages of EU commitment arbitration

EU commitment arbitrations entail a number of advantages over alternative proceedings before the EU Commission or the competent EU Member State court. Apart from the fact that the EU Commission is not empowered to provide any form of civil law redress to injured third-party beneficiaries, the main advantages militating in favour of recourse to arbitration over either third-party complaints to the Commission or private litigation before a Member State court, as the case may be, can be summarized as follows: First, arbitration proceedings are private and confidential,

thus allowing the undertakings involved to avoid any form of adverse publicity, which in turn may affect currently prevailing trade patterns. Second, the arbitrating parties are free to choose a suitable arbitrator/arbitration tribunal taking account of an individual candidate’s competition law experience and industry-sector-specific expertise. Third, a resultant award is final and binding (and as such cannot be appealed on the merits) and will be enforceable in over 140 leading industrial nations worldwide (including all EU Member States) under the New York Convention¹⁹. This will contribute to the overall speed and efficiency of the proceedings. Fourth, the procedural conduct of the arbitration may be adapted to the specific requirements of EU commitment arbitrations.

Procedural flexibility more particularly translates into a variety of more specific advantages at the micro level, including in particular:

Reliance on the *prima facie* evidence rule²⁰ or a reversal of the burden of proof in favour of the third-party beneficiary in order to counterbalance the often existing information asymmetry between the commitment debtor and the third-party beneficiary.

The availability of preliminary rulings, which allow the arbitrator to make preliminary findings against the commitment debtor pending the final outcome of the arbitration proceedings. This will assist in preventing the

19. Convention on the Recognition and Enforcement of foreign arbitral awards, done at New York, on 10 June 1958.

20. Whereby in the event that a commitment debtor fails to refute a *prima facie* case made against it by a third-party beneficiary, the arbitrator will have to find in the latter’s favour.

premature exit of a third-party beneficiary from the relevant market.

A fast-track dispute resolution procedure, which is the common framework of an EU commitment arbitration. This helps in keeping the procedural pace of the proceedings to ensure a swift resolution of time-sensitive competition disputes in real time, allowing early settlement by way of amicable settlement or mediation or in the event of escalation to arbitration, a swift arbitration process taking no more than a maximum of two to six months in total.

III. The scope of the arbitrator’s jurisdiction

The scope of the arbitrator’s jurisdiction in EU commitment arbitrations is confined to drawing the civil law consequences from the commitment debtor’s deficient implementation of or its failure to implement the commitments underlying the original commitment decision.

In particular, the arbitrator will be mandated to determine whether:

- the commitment debtor has complied with the underlying access commitments or the terms and condition of the access agreement, taking account of the intended competitive effect, i.e. the regulatory objectives of the underlying commitments; and
- whether compliance with the access commitments does not produce any anti-competitive effects on the relevant product and geographic market.

The arbitrator will further be empowered to award appropriate interim relief to the third-party beneficiary, e.g. specific performance of the disputed access commitments, pending the final determination of the parties' dispute in order to save a third-party beneficiary from exiting the market prematurely.

Importantly, whereas the arbitrator's mandate is confined to the adjudication of the private law consequences of the deficient implementation of the disputed commitments, the European Commission preserves its regulatory functions, in particular the prerogative to impose public law sanctions (such as fines, the withdrawal of the underlying commitment decision or the dismantling of an already-consumed merger) and ultimately remains responsible for the accurate implementation of the commitments. In this sense, the arbitrator does not usurp the public administrative law functions of the EU Commission; to the contrary, the EU Commission's and the arbitrator's mandates in EU commitment arbitration are truly complementary.

IV. The arbitrator's findings

In reliance on the scope of his/her mandate, the arbitrator's findings may vary depending on whether or not an access agreement has already been concluded between the commitment debtor and the intended third-party beneficiary. Where an access agreement is already in place, the arbitrator may, for instance:

- declare that the commitment debtor has failed to implement the underlying access commitments or the terms and conditions of

- the access agreement and order specific performance;

- declare that the access agreement concluded between the commitment debtor and the third-party beneficiary is defective and order its variation or modification in order to bring it into line with the underlying access commitments;

- declare that, albeit correctly implemented through the access agreement, the underlying access commitments prove insufficient *ex post facto* and refer them back to the EU Commission for review; or

- declare that the terms and conditions of the access agreement have properly been complied with by the commitment debtor and render an exculpatory award in favour of the commitment debtor; and

- award civil law redress (including compensatory damages) for the commitment debtor's past non-compliance as appropriate.

Where no access agreement is yet in place, the arbitrator may, for instance:

- declare that in violation of the original commitments, the commitment debtor has to date failed to conclude a suitable access agreement with the third-party beneficiary; and

- order the parties to negotiate suitable terms and conditions of such an agreement, taking into account the regulatory objectives underlying the original commitment decision; and

- award civil law redress (including compensatory damages) for the commitment debtor's past non-compliance as appropriate.

V. Relationship between the arbitrator and the EU Commission

EU commitment arbitrations impose a number of procedural requirements that go beyond what is usually expected of international commercial arbitrations. These requirements have, in the past, justified reference to EU commitment arbitrations as a form of 'supranational arbitration'²¹. Supranational arbitration is a form of arbitration à l'europpéenne, which requires the parties and the arbitrator to take into account the constitutional idiosyncracies of the EU legal order as a separate and autonomous legal order *sui generis*²². These include, for present purposes, in particular the principles of direct effect and supremacy and the principle of loyal (or sincere) co-operation. Correctly applied, these principles require supervisory Member State courts to take into account a previous conditional merger clearance decision or an Article 9 commitment decision in the enforcement of awards resulting from an EU commitment arbitration arising from those decisions: A supervisory Member State court will thus be prevented from enforcing an award that does not comply with the conditions and obligations of the original commitment decision and violates e.g. the regulatory objectives of the commitments underlying those decisions.

21. For this terminology in the EU merger control context, see G. Blanke, *The Use and Utility of International Arbitration in EU Commission Merger Remedies: A Supranational Paradigm in the Making?* (Europa Law Publishing, 2006).

22. Cf. Case 26/62 - *Van Gend en Loos v Administratie der Belastingen*, Judgment of the European Court of Justice of 5 February 1963, Rec 1963, [1963] ECR 1.

This is in particular so on the basis of a literal reading of the ruling of the Court of Justice of the European Union in *Eco Swiss*²³, which qualifies any infringement of EU competition law as caught by the public policy concept under the New York Convention.²⁴ The approach is likely to differ outside the EU, as non-Member State courts are not bound by the principle of loyal co-operation in the exercise of their supervisory functions.

In order to ensure the enforceability of awards resulting from EU commitment arbitrations, the underlying arbitration commitments typically provide for a number of procedural safeguards. These include:

- some form of co-ordinated co-operation between the EU Commission and the arbitrator and in particular (i) requests for information from the arbitrator to the Commission, especially to assist in the accurate definition of the intended product and geographic markets; and (ii) requests for interpretation from the arbitrator to the Commission in relation to the correct interpretation of the regulatory objectives and effects behind individual commitments in order to ensure that the arbitrator have an accurate understanding of the intended competition-compliant operation of the commitments;

- the EU Commission's role as *amicus arbitri*, including in particular the Commission's

23. Case C-126/97, *Eco Swiss China Ltd and Benetton International NV*, Judgment of the European Court of Justice of 1st June 1999.

24. For a literal reading of *Eco Swiss* and its importance in context, see G. Blanke, "The Supranational Dimension of Arbitrating Competition Law Issues within the EU" in G. Blanke & P. Landolt, *supra*, at paras 10-014 et seq.

entitlement (i) to receive the main submissions and procedural documentation issued over the course of the arbitration procedure; (ii) to make submissions to the arbitrator at all stages of the arbitration procedure; and (iii) to participate in the main evidentiary hearing as observer, expert witness or otherwise (including an entitlement to ask questions),²⁵ and

– a general reporting requirement, whereby the arbitrator is required to report procedural developments in the arbitration to the EU Commission in regular, specified intervals.

As all these safeguards are expressly provided for in the underlying arbitration commitment and given that a third-party beneficiary will have consented to these once he/she has triggered his/her arbitration option in compliance with the arbitration commitment (or a corresponding arbitration clause in the event that a suitable implementation agreement has been put in place), they firmly form part of the underlying arbitration reference and hence the arbitrator's mandate. There can therefore be little controversy about the propriety of such procedural safeguards in the context of EU commitment arbitration.

25. C. Nisser & G. Blanke, "ICC Draft Best Practice Note on the European Commission Acting as Amicus Curiae in International Arbitration Proceedings – The Text" in G. Blanke (ed), *Arbitrating Competition Law Issues*, EBLR Special Edition (2008) pp 198-217. For a background note, see *idem*, "ICC Draft Best Practice Note on the European Commission Acting as Amicus Curiae in International Arbitration Proceedings – An Explanatory Note" in *ibid* pp 193-197. For further commentary, see *idem*, "Reflections on the Role of the European Commission as Amicus Curiae in International Arbitration Proceedings", 4 ECLR (2006) pp 174-183.

VI. Conclusion

EU commitment arbitrations are a useful tool to provide a merging or dominant entity with a welcome opportunity to obtain clearance of a problematic merger or problematic market conduct by offering behavioural commitments supported by an arbitration commitment, thus avoiding more burdensome structural commitments. What is more, arbitration commitments may serve as an effective deterrent to commitment debtors, who – rather than exposing themselves to liability in costly arbitration proceedings – are likely to prefer amicable settlement prior to escalation to arbitration over a commitment dispute in which they are unlikely to prevail.

Deadlock provisions in shareholders' agreements: corporate and litigation perspectives

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Joint ventures are frequently used as an alternative to traditional Merger & Acquisition transactions, as each joint venture partner brings his financial, technological or local expertise to a common project. In such context, shareholders' agreements are an important tool to organize a governance procedure that will prevent or help solve strategic disagreements. However, despite the parties' best intentions, diverging interests and cultural differences may result in deadlocks. Like weddings between individuals where prenuptial agreements can help deal with the consequences of a divorce, shareholders' agreements need to adequately address potential disagreements and their consequences.

The following hypothetical "nightmare" scenario illustrates the difficulties in solving deadlocks and implementing dispute resolution provisions:

A major international company (let's call it "MajorCo") sets up an energy business

in a Middle Eastern country. Local regulations impose the presence of a local partner, hence MajorCo teams up with a minority shareholder ("LocalCo"). The shareholders' agreement between MajorCo and LocalCo provides that in case of "serious disagreement" among the shareholders, MajorCo will purchase LocalCo's stake in the joint-venture at a price determined by an independent expert. Such independent expert will be appointed by the parties among the Big Four, and if the parties fail to agree, the expert will be appointed by the President of the Paris commercial court at the request of the most diligent party.

A disagreement occurs between MajorCo and LocalCo on a contract that is essential for the joint venture's operations and for which there is no alternative provider. On the basis of the shareholders' agreement, MajorCo determines that a deadlock has occurred. It contacts LocalCo to offer to purchase LocalCo's stake in the joint venture and

to propose the appointment of an independent expert who will determine the price of such stake, both in accordance with the shareholders' agreement.

As LocalCo does not want to sell its stake in the joint venture, it engages in a guerrilla strategy which prevents the prompt resolution of the deadlock. Firstly, LocalCo refuses to acknowledge that a deadlock has occurred and refuses to appoint an independent expert. Secondly, it challenges the competence of the President of the Paris commercial court to appoint an independent expert on the ground that there is no deadlock. An arbitration procedure is initiated by MajorCo, and the arbitral tribunal rules that LocalCo must sell its stake to MajorCo at the price determined by the independent expert. Then, LocalCo refuses to transfer its shares in the joint venture on the ground that the deadlock provisions contravene the local country's public policy rules.

Finally, there is a change in local law which grants to the local State a pre-emption right on any transfer of shares by a local shareholder to an international investor. Hence, if LocalCo eventually accepts the transfer of its stake in the joint venture to MajorCo, such transfer may be pre-empted by the local State. In that case, MajorCo will be forced to accept a new public shareholder that it has not chosen, without the benefits of protection of a shareholders' agreement.

Overall, after several years, the deadlock situation is still not solved. To avoid such a nightmare scenario, share-holders need to: define what constitutes a deadlock (A); decide on a process that will allow them to solve such deadlocks (B); and take into account external

constraints that may interfere with the deadlock resolution (C).

A. Various types of deadlock situations

Different shareholders have different priorities, depending on their level of shareholding or their nature. The founders of a company, who subsequently sold a majority interest and remained as minority shareholders in their venture, will have more difficulties relinquishing the operational control of what started as an entrepreneurial project. On the other hand, a State monitoring an investment in a company that plays a strategic role in its economy may balance the interests of the company with the interests of its citizens and its economy as a whole.

Based on their respective preferences, shareholders will negotiate the allocation of powers within the company ex ante and determine the governance and decision-making rules applicable to the management of their joint-venture and the solving of disagreements. As illustrated above, general provisions stating that a deadlock occurs in case of "serious disagreement between the shareholders" do not offer sufficient protection to the joint venture partners. Instead, the shareholders' agreement should identify the specific issues which, in case of continuing disagreement among the shareholders, will be deemed to constitute a deadlock. This ensures that each shareholder is entitled to have his say on such issues, with increased majority requirements and possibly veto rights in favor of the minority shareholder.

Across the board, the following subjects will typically form deadlocks if the shareholders cannot agree and implement any related decision: (i) determining the strategy of the

joint-venture as well as approving strategic operations, (ii) approving or amending the various budgets and business plans, (iii) resolving accounting and consolidation issues, (iv) agreeing on financial strategy, (v) deciding on changes in the joint-venture's share capital and/or issuance of shares, bonds, and/or convertible instruments.

Once a deadlock is characterized, it is often tied up with exit mechanisms. This ensures that the parties are not forced to retain a joint interest in the project if their views are so contradictory that further disagreeing could paralyze the joint-venture. This would only damage their respective investments. Hence, the way the deadlock resolution mechanism is set up will be critical to promote good faith and a prompt resolution of the parties' disagreement.

B. Ways of Resolution

There are several possible methods to facilitate the resolution of a deadlock while maintaining the continuity of relations among the shareholders. Eventually, if the parties cannot agree on a mutually acceptable solution, the deadlock may culminate in the exit of one of the joint venture partners.

Management or Board Member Removal. Often, the shareholders' agreement entitles each partner to appoint a certain number of board members (whether to a board of directors, a supervisory board, or any ad hoc committee). The parties may also be entitled to appoint managers of the joint venture in accordance with an allocation of operational positions determined in the shareholders' agreement. This is to ensure that each party is truly involved in managing the company,

and to prevent one party from shielding the other. However, a deadlock may originate in communication problems among such appointees. As an illustration, a manager of the joint venture may be perceived as favoring the interests of the party that appointed him. A board member representing a party may appear obstructive during board meetings. Cultural differences may also render communication more difficult. To address such issues, the provisions of the shareholders' agreement can entitle each party to request the revocation and replacement of a specific appointee of the other party. To prevent abuses, such a revocation may be limited to revocation for cause, or such a right may be limited to once per year.

Escalation Clauses. An alternative solution to address interpersonal communication issues is implementing escalation clauses. If the parties cannot agree on a solution to their disagreement at board level, they can escalate the issue to senior executives of their respective groups (directly or through an ad hoc committee set up in the shareholders' agreement). The underlying assumption behind such escalation clauses is that if the disagreement is merely operational and due to interpersonal communication issues, these senior executives are more likely to discuss the issue in a dispassionate fashion and to find compromises, including by changing their board representatives or managers. However, such a process will not be effective should the disagreement relate to strategic or financial issues (as may be the case if there is a strong difference in the level of financial resources of the parties), or should the local shareholder be a wealthy individual attending the board meetings himself.

Business Continuity. An important concern in case of deadlocks is that the parties' disagreement could damage the activities of the joint venture company, in particular when operational managers have been appointed by both parties and therefore tend to daily oppose to each other. Several factors can contribute to such a damaging effect: e.g., disagreement on the marketing strategy results in no marketing strategy being implemented; disagreement on the company financing results in a lack of funding and the joint venture's infrastructure becoming out-dated; disagreement on the choice of the appropriate candidate to fill in a management position results in such position not being filled; and persisting disagreement on the financing of the joint venture leads the company into financial distress. For example, such a disagreement can occur if a shareholder with deep pockets prefers to finance the joint venture through capital increases or convertible shareholders loans, whereas the other shareholder prefers resorting to third-party debt financing in order to avoid any equity dilution. To address the risk that the shareholders' disagreement will damage the asset, the shareholders' agreement can provide that upon failing to reach an agreement among the parties on the resolution of the deadlock, the parties undertake to agree in good faith on an intermediate solution to limit the disruptive effect of the deadlock and to vote in favor of all related decisions. When (i) additional equity financing is required to ensure that the joint venture avoid bankruptcy proceedings, and (ii) there is a significant difference in the financial means of the shareholders, a possibility is to provide that the shares to be subscribed by the minority shareholder will be funded by the majority

shareholder, up to a certain level, to facilitate the minority shareholder's acceptance of the decision.

Suspension of contractual veto rights. To prevent the parties from disagreeing for too long, the shareholders' agreement can provide that if the deadlock is not resolved within a certain period of time and after a certain number of meetings, the veto rights of the minority shareholder as per the shareholders' agreement will be suspended, with the minority shareholder being offered the possibility to sell its stake in the joint venture to the majority shareholder. This suspension of contractual veto rights will allow the majority shareholder to implement the decision alone. This is particularly useful when the minority shareholder has a veto right on any decision which could have a dilutive effect on its investment, and more specifically when the joint venture project requires continued investments and additional financing during a relatively long period.

Suspension of voting rights. Local regulations often impose a specific majority requirement with respect to shareholders' decisions qualified as "extraordinary", such as a merger of the company with another entity or a share capital increase. In other circumstances, the shareholders' unanimous consent is required. In such cases, regulatory requirements result in the minority shareholder's voting rights giving him a de facto veto right. To address that issue, the shareholders' agreement can provide that both: (i) the contractual veto rights granted to the minority shareholder, and (ii) the minority shareholder's voting rights as per the by-laws, will be

suspended, with an independent third party being appointed to vote in the name of the defaulting shareholder at shareholders meetings and board meetings. Such a solution can also be implemented if a shareholder fails to comply with the above mentioned voting undertaking to preserve the business continuity of the company. This solution will be particularly relevant in the event that a share capital increase is required to preserve the company's viability, while facing the threat of bankruptcy procedure, as the minority shareholder may refuse to approve any decision that would have a dilutive effect on its stake. However, the validity of contractual provisions suspending the voting rights of a shareholder should be checked to ensure that they are in compliance with public policy rules and *lex societatis* in the relevant jurisdiction. It should be noted that such a solution, as well as the suspension of veto rights, can only apply if there is a significant difference in the level of shares held by the parties. If both parties hold the same level of shares in the joint venture, it is unlikely that any party will accept to have its voting rights suspended in case of disagreement. Such a suspension of rights may be coupled with an exit mechanism allowing the shareholder whose rights are suspended to request that the other shareholder buys back its shares within a certain timeframe.

Exit mechanisms. An ultimate solution, if the parties cannot solve their disagreement, is for one of them to quit the joint venture. Hence, the joint venture agreement can provide for several exit mechanisms to prevent the partners from being forced to remain together. Call option and put option clauses

can be envisaged, either to allow the majority shareholder to buy out the minority, or to allow the minority to sell its stake to the majority. If there is no significant difference between the level of shareholding of the two joint venture partners, "Russian roulette" clauses, also called "Buy or Sell" clauses, can be utilized. These clauses are often encountered in 50:50 joint ventures and work as follows: each party is entitled to initiate the Russian roulette process. When initiating the process, the initiating party makes a purchase offer for the other party's stake in the joint venture and indicates the price at which it is willing to purchase such stake. Two outcomes are possible: (i) the party receiving the offer can either accept it and sell its shares to the offering party at the offered price, or (ii) the party receiving the offer can refuse it, in which case it is required to purchase the offering party's shares in the joint venture. In the latter case, the price per share to be retained will be the one initially proposed by the party who initiated the Russian roulette process. It should be noted that such Russian roulette clauses tend to favor the party with the greatest financial capacity, as it is more likely to be in a position to finance a higher price to purchase the other party's shares. It should be noted that exit clauses may also be used by a party to obtain the liquidity of its investment in the joint venture outside of the contractually agreed cases (by artificially setting-up a deadlock). Depending on the parties' respective situations, such clauses can provide "hold-up" opportunities to a party, or place a weaker party on an "ejector seat".

Price Determination. An important issue with put and call options is determining the

price for the transferred shares. For publicly-listed companies, the stock price (increased by a premium to be negotiated) will often serve as the basis upon which the transfer price is determined. The issue is more complex for a non-publicly-listed company, as the parties will need to agree on how to determine the fair market value of the shares. There is a wide range of available technical options, however, the methods below are worth noting:

Price determined pursuant to an auction process. In order to set the transfer price of the shares of the shareholder exiting the joint venture, the auction can be organized among the parties to the shareholders' agreement (if there are more than two shareholders) or involve external bidders. Such a method may not be favorable to the exiting shareholder: if the third parties are aware of the disagreement among the shareholders, they are more likely to offer a discounted price;

Price determined by experts. Each party appoints an expert who assesses the value of the shares to be sold. If the experts' respective estimates differ by more than 10% or 15%, a third expert will be appointed jointly by the first two appointed experts to determine the fair price within that range. Alternatively, the third expert will decide which of the other experts' two prices it deems fairest. To avoid litigation on the expert appointment, the expert should, to the extent possible, be identified in the shareholders' agreement, with an alternative expert also being designated if the first one is not in a position to accept the mission. If neither expert can accept the mission, then the most diligent party will be entitled to go to courts to request the

appointment of an expert by the courts. The shareholders' agreement should also state that the expert's report will be binding on the parties, except for cases of gross negligence or willful misconduct.

In the case of a publicly-listed company, the exit mechanism may create perverse incentives should the exit price resulting from the contractual provisions be likely higher or lower than the trading price of the stock, thus creating arbitrage opportunities. Hence, merely being able to use a deadlock to activate an exit mechanism may give shareholders an incentive to artificially set up a deadlock. This means either forcing out a minority shareholder (from the standpoint of majority shareholder) or obliging a majority shareholder to buy back the minority's stake (from the standpoint of the minority shareholder). To prevent such abuses, the parties can establish contractual provisions to limit their respective incentives to artificially create a deadlock. Imposing financial sanctions on the party bringing up the deadlock may be a solution. However, the line between a good faith deadlock and a bad faith deadlock is often blurry.

C. Impediments and deadlock enforcement

In order to determine the most efficient and rapid way to solve such a deadlock, the parties need to identify the various impediments to their situation and deadlock enforcement. Therefore, the regulatory and economic environment of the joint venture company, as well as its business and financial plans, must be analyzed and addressed when setting up the joint venture and negotiating deadlock resolution mechanisms. Several types of regulations

may impact the parties' agreement and we will give an overview of the most common ones below.

Deadlock acknowledgment. As one may expect, a deadlock is likely to occur in a situation where the parties disagree on the management of the company. This does not necessarily mean that both parties will agree to implement the deadlock resolution provisions. This is because such provisions may be less favorable to a party depending on the particular circumstances at the time. Hence, the acknowledgment that a deadlock has occurred may itself be controversial, thus preventing any deadlock resolution and threatening the management of the joint venture. To address this issue, the parties can stipulate that such disagreement on the acknowledgment of a deadlock will be submitted to local courts. However, this may be detrimental to a foreign investor situation. The reason is that local courts may favor the interests of a national shareholder opposing a foreign investor. An arbitration procedure can also be initiated to recognize the existence of the deadlock. In this case, the duration of the arbitration procedure may affect the financial situation of the joint venture. Another alternative consists of imposing financial penalties to the party refusing to acknowledge that a deadlock has been reached beyond a certain period of time.

Securities regulations. For publicly-listed companies, a shareholder purchasing the shareholding interest of its joint venture partner may be required to launch a mandatory public offering, depending on the applicable triggering threshold. This requirement creates

additional financial and administrative burdens which need to be addressed earlier on while setting up the deadlock resolution mechanism. This is to ensure that the purchasing shareholder has the capacity to finance a public offering (he may need to set aside specific provisions in his accounts) and that implementing the deadlock resolution will be compatible with listing rules and securities regulations.

Level of local shareholding. Local laws may also impose a minimum level of shareholding from local investors in companies involved in public sector activities. Alternatively, such laws may limit the level of foreign shareholding in these companies. Tunisia, for example, restricts the level of foreign shareholding in companies operating under a telecom license. These laws force international groups to seek further partnerships with national investors. Should the deadlock resolution result in the sale by the national investor of its interest in the joint venture, the foreign shareholder will need to find an alternative national investor to replace the existing one. Depending on the financial prospects of the joint venture and the economy of the local country as a whole, the foreign shareholder may be forced to sell a stake to a local investor at a significantly discounted price.

Restrictions on transfer of shares. The approval of a local public body may be required prior to any change of control or any transfer of shares of a company entrusted with public procurement. Failure to obtain such approval may result in the transfer of shares being blocked or in the public procurement being revoked. This may delay or prevent the parties from resolving the deadlock smoothly.

Enforcement of court decisions or arbitral awards. Regardless of the provisions of the shareholders' agreement, a party may object to the sale of its shares in the joint venture as a way of resolving the deadlock. This may result in the other party seeking and obtaining a judicial or arbitral award to enforce the deadlock resolution provisions and order the transfer of the first party's shares, usually under penalty. However, it should be noted that in several jurisdictions, obtaining an arbitral award ordering the transfer of shares is not sufficient to effect such transfer of shares, as local formalities will be required to complete such transfer. For example, several civil law countries require that transfers of shares be notarized by deed. In such countries, the consent of the party forced to exit will be required to effect the notarization of the deed. This requirement provides such a party with an opportunity to further delay its exit. Indeed, should the shareholder refuse to proceed with the formalities, the only available remedy is to recover the penalties if any. If the shareholder has no asset out of its country of residence, no recovery is possible without obtaining an enforcement judgment. This will cause additional delay and uncertainty since the shareholder may object to the enforcement, notably on the ground of public policy, a notion which varies greatly from one jurisdiction to the other. When setting up the joint venture, the parties may address such concern by establishing a holding company, above the operational entity, in a more favorable forum where the formalities required to effect the transfer of shares will be less burdensome. Hence, Civil Law and Common Law should be compared to identify the most favorable legal system to enforce the deadlock

resolution provisions. Pledges over shares and escrow mechanisms can also be used as a mechanism to force the resisting party to transfer to the other party its shares in the joint venture.

Change in law. Although this is a factor that the parties can hardly anticipate, local regulations may change and affect the way of solving deadlocks. As an illustration, preemption rights in case of transfer of shares to foreign investors may be established in favor of local States. Here again, setting up a holding above the joint venture in a more favorable jurisdiction gives the parties more security concerning the implementation of the contractual provisions negotiated *ex ante*.

* * *

In light of the above, there is no one-size-fits-all solution to deadlocks. At the contract negotiation stage, it is necessary to take the time to identify the potential risks deriving from (i) the parties' respective situations, (ii) local political and regulatory hurdles, (iii) the joint-venture's business plan and financial plan, and (iv) critical calendar aspects relating to the joint-venture's development. It is also recommended to perform a "crash test", so as to anticipate how the counterpart may try to circumvent the deadlock resolution mechanism. Once exit provisions apply, it is often difficult to determine what is the loss suffered by the majority shareholder if a minority shareholder refuses to transfer its shares in the joint venture to such a majority partner. To speed up the process and avoid delaying tactics, setting up indemnity provisions and contractual damages in the shareholders' agreement is also a viable mechanism to ensure that the

defaulting shareholder will comply with any arbitral award forcing it to sell its stake in the joint venture.

Report from the conference “Dispute Resolution in M&A Transactions: Tactics, Challenges, Defences” 2nd edition

6-7th June 2013, Warsaw

■ **mec. Agnieszka Wolińska**

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The second edition of the international conference “Dispute Resolution in M&A Transactions: Tactics, Challenges, Defences” was held on 6-7th June, 2013 in Warsaw. Like the previous edition held in 2010, this year’s conference was organised by the Lewiatan Court of Arbitration. Poland’s Foreign Minister assumed the honorary patronage and the conference was partnered by the International Court of Arbitration ICC, ICC Polska, ABA Section of International Law and Arbitral Women. The media partners were TDM Transnational Dispute Management, Swiss Chambers Arbitration Institution and Polish Private Equity and Venture Capital Association. The conference was organised in the framework of the project “Konkurencyjność Arbitrażu” (Competitive Arbitration) co-financed by the European Social Fund.

The conference was chaired by the President of the Lewiatan Court of Arbitration, Ms. Beata

Gessel-Kalinowska vel Kalisz PhD, who had initiated the whole cycle and in her keynote address, announced that the third edition of the conference „Dispute Resolution in M&A Transactions” would be held on 28-29th May, 2015 in Warsaw. Mr. Artur Nowak-Far, Undersecretary of State for Legal and Treaty Affairs, Ministry of Foreign Affairs of the Republic of Poland and Mr. Henryk Orfinger, on behalf of the Polish Confederation of Private Employers Lewiatan also delivered their welcome addresses. Eminent experts from around the world attended the conference. They presented the most recent and significant issues in M&A disputes settled by arbitration under various jurisdictions, which allowed the participants to have a world tour and familiarize themselves with the hottest M&A issues settled by arbitration.

The first day of the conference included four panels on the following issues: 1. Hot

topics in M&A Arbitration, 2. To Bifurcate or Not to Bifurcate - This and Other Procedural Issues in M&A Arbitration, 3. Shareholders Dispute - Case Study under the Patronage of Dechert LLP and 4. Computation of Damages – Panel of Witness Experts. Ms. Catherine Kessedjian from the University of Panthéon-Assas, France delivered the closing remarks summing up the first day of the conference. She said that during this first day, the participants managed to familiarize themselves with the most important issues taught at business law studies during the whole academic year. After the panels, the participants were invited to take a tour of the National Stadium, which hosted this year’s conference and, not so long ago, the UEFA Football Championship. In the evening, there was a banquet, at which Mr. Tomasz Wardyński of the firm Wardyński & Partners delivered a speech. The morning panel of the second day of the conference dealt with M&A and Shareholders Disputes in the CEE Region from the Perspective of Arbitral Institutions. This was followed by a lecture by Mr. Marc Blessing from Bär & Karrer AG, Switzerland. There were also two last panels on Antitrust Law in M&A Disputes and Mandatory Public Law in M&A arbitration.

During the first panel, moderated by Ms. Beata Gessel-Kalinowska vel Kalisz, PhD, in her opening remarks for the panel discussion, presented statistics on the number of M&A disputes settled by arbitration over the past ten-odd years. Mr. Andrea Carlevaris, (Secretary General, ICC International Court of Arbitration, France) used the examples of disputes solved by the ICC to present the most important issues in the settlement

of international M&A disputes by arbitration. He emphasized that M&A disputes could come up at any transaction stage, because the transactions are complex and complicated. Traditionally, the distinction is made between the following stages of these transactions: pre-signing, post-signing, pre-closing and post-closing. Pre-signing controversies very rarely end up in arbitration. If a problem comes up at this stage, the parties will tend to try to finalize the deal and institute arbitration proceedings only after closing. M&A disputes deal mostly with the breach of exclusivity and confidentiality clauses, representations and warranties and price determination mechanisms. Mr. Nelson Eizirik (Carvalho e Eizirik Advogados, Brazil) discussed the recent trends in Brazil’s arbitration law. He pointed out that Brazilian law allows the inclusion of dispute resolution by arbitration in the Articles of Association and, in the case of companies listed on the Brazilian Stock Exchange, the companies have the obligation to include arbitration clauses in their statutes and refer their disputes to settlement by arbitration. Mr. Daniel Busse (Allen & Overy, Germany) covered the most recent and meaningful trends in M&A arbitration in Germany. He said that most of the issues and procedural problems discussed at the conference were characteristic of all disputes, rather than only M&A disputes. In his presentation, he offered an assessment and a comparison of the procedures of expert determination and arbitration with regard to their effectiveness in M&A dispute settlement. He also discussed parties’ responsibility in M&A transactions, methods for the computation of damages, as well as the risks and benefits associated with using standard contract terms & conditions in M&A deals. In turn,

Ms. Penny Madden (Skadden Arps, UK) presented the current trends in British law. Using multimillion or even multibillion M&A deals as examples, she discussed the premises associated with obtaining injunctions preventing one of the parties from taking certain steps. She drew attention to pro-arbitration decisions by English courts, which might influence the choice of English law as the ruling law for dispute settlement. Mr. Michael Hwang S.C. (Michael Hwang Chambers, Singapore) then discussed M&A dispute settlement in Asia, where the dynamic growth of the region is accompanied by an increasing number of M&A deals, as well as disputes arising out of these deals. He also pointed out to the growing popularity of settlements in M&A disputes.

The second panel was devoted to procedures in M&A dispute resolution proceedings by arbitration. Ms. Mirese Philippe of the ICC International Court of Arbitration, France moderated this panel and the panelists were: Mr. Philipp Habegger (Walder Wyss, Switzerland), Mr. Pawel Pietkiewicz (White& Case, Poland), Mr. Soteris Pittas (Soteris Pittas & Co., Cyprus) and Mr. Jakob Ragnwaldh (SCC, Mannheimer Swartling, Sweden). During the discussion the panelist were supposed to answer the question, whether arbitration proceedings should be bifurcated or not and, if the bifurcation of arbitration proceedings actually lent itself to speeding them up and to cost reductions. The panelists agreed that bifurcation arbitration proceedings does not always cut down the time or costs of the proceedings. They also discussed issues related to the discovery procedure in arbitration. They drew attention to differences in the approach,

depending on whether a dispute is settled under common law or civil law, as well as to the problems, which may come up when certain documents should be disclosed by a third party – in M&A disputes, it is typically the target company or its shares. Special attention has been devoted to Cypriot companies with international equity. In the case of these companies, certain differences and problems may come up with regard to M&A dispute resolution, because of the ruling law in individual cases. The panelists also discussed procedures designed to expedite dispute resolution, such as fast-track arbitration or emergency arbitrator. They emphasized that the two are different mechanisms, though often confused. These mechanisms may be particularly important for disputes arising in the pre-closing stage, where the expediency of dispute settlement is crucial not only to the transaction itself, but may also affect the financial condition of the parties.

The third panel, moderated by Mr. Krzysztof Stefanowicz (Lewiatan Court of Arbitration, Poland) was a case study reconstructing a dispute between shareholders. The panelists were: Ms. Cecile Amayen (Telecom-Orange Group, France), Mr. François Hellot (Dechert, France) and Mr. Xavier Nyssen (Dechert, France). Drawing on their personal experience in disputes, which they had helped settle, they pointed out to a particularly dangerous element in M&A transactions, i.e. the deadlock, meaning the lack of agreement between the parties, which can last for several years or even more than a decade. They pointed out to the possible reasons behind deadlocks, such as an inappropriate strategy or plan for the deal, entailing the lack of

agreement in implementation, as well as misunderstandings regarding financing or the rights and obligations of the individual parties.

The fourth panel dealt with one of the crucial elements in disputes, i.e. computation of damages. This panel was moderated by Mr. Julian Lew (Queen Mary University of London, UK). The other panelists were Mr. Vladimir Bosiljevac (Harvard University, USA), Mr. Anthony Charlton (FTI Consulting, France), Mr. Nick Andrews (Grant Thornton, UK) and Mr. Frank Ilett (Deloitte, UK). The panel focused on discussing the difference in settling M&A disputes in arbitration proceedings and in the common courts of law. All the panelists were experts and they felt that there was no difference, whether a dispute was settled by an arbitration court, or a common court of law, because the evidence, which is the basis for drawing up their opinions in both situations is the same. Only the rules applicable to the two types of proceedings may affect how effective the experts are at their work, facilitating their job, or making it more difficult. The experts also pointed out that while arbitrators were bound to observe the ethical rules set out in ethics codes and arbitration rules of arbitral courts, oftentimes there were no similar rules for experts, especially those appointed by the parties. Regardless of who had appointed them, experts should be impartial and independent, which is not always the case, if they had been appointed by one of the parties. In turn, experts appointed by an arbitral court should always abide by the same rules as the arbitrators. For example, Article 21 of LCIA Arbitration Rules mandates experts appointed by the court to remain impartial and objective. In their opinions, the experts should

consider all the evidence gathered, both that, which is beneficial to a party, but also otherwise. A part of the panel has been devoted to the valuation of M&A deals and the computation of damages for breach of the provisions of M&A agreements. Among other things, M&A deals are intended to lead to better revenue growth, more efficient use of capital or cost reductions. They are supposed to produce synergies, i.e. situations, where the outcome of a transaction is higher than the sum of the elements invested by both parties. It has been emphasized that the price is not always equal to the value of what was purchased. This is why determining the damages in the event of an M&A dispute is hardly an easy feat and a number of different computations are used to establish the appropriate damages, depending on the reasons for the dispute and its object.

Ms. Catherine Kessedjian summed up the discussions of the first day of the conference by stating that it would be extremely difficult to find issues, which would be completely different in M&A disputes settled by arbitration and other arbitration disputes. She also pointed to the large volume of M&A deals and resulting disputes in the present times of economic downturn, which is a crucial factor, also capable of affecting the amount of damages awarded by arbitration settlements in M&A deals.

Panel on arbitration and competition – report

■ Jana Plananova-Latanowicz

European Center at University of Warsaw

The fifth panel was preceded by a lecture held by Mr. Marc Blessing. He discussed the interplay between arbitration and the EU anti-trust law (i.e. art. 101 and 102 TFEU). According to his account he have served as an arbitrator in more than 50 arbitrations involving anti-trust issues up to now. In his experience, there are three possible scenarios of mergers with overriding anti-trust concerns. First, the vertical distribution agreements concluded by a (target) company may collide with prohibition contained in art. 101 par. 1 TFEU. As a result, relevant provisions of the contract will become null and void from the beginning. Furthermore, M&A lawyers must be aware of these questions as they may lead to the EU Commission's investigation. It may conceivably fine the target company after the transaction. It is definitely cheaper to spot these problems during the due diligence and make adequate reservations in the M&A contract.

Second scenario relates to horizontal co-operation. The non-dominant competing companies decide to join their efforts and form a joint venture. The transaction may lead to either a concentrative (i.e. full function) joint venture and then it would be subject to

merger control or it may lead to cooperation for particular functions (R&D, joint production, joint distribution). For M&A lawyers this second scenario is even more challenging as the breach of 101 par. 1 TFEU in horizontal relations may lead to more extensive fines from the EU Commission and to ab initio and ex lege nullity of the relevant contractual provisions as well as claims for damages.

Third scenario requires M&A lawyers to assess a transaction with a dominant firm under art. 102 TFEU. A transaction may constitute an abuse of a dominant position even if it is not subject to the EU merger control provisions.

All three scenarios are likely to be discussed in arbitration proceedings related to M&A disputes. The essence of Mr. Blessing's presentation may be abbreviated into a form of a question directed to M&A lawyers: Are you able to recognize an anti-competitive clause if you see one in a contract or other companies document? Limitations of competition may form not only the intended result of company's behavior (restrictions by object) but also it may happen as unintended side effect of company's economic policy. The

company is equally responsible for both types of restrictions (the difference matters only for purpose of fining policy). Typically, there is a certain amount of resistance to application of competition law on the part of business people and many companies managers perceive hard-core restrictions as a valid form of "organizing the market".

With regard to the enforcement of competition rules Marc Blessing outlined three possible options: first, to submit a complaint to a competition authority. This way works effectively but from the point of view of private law claims it brings no material results. Second and third options are based on private enforcement. The claimant may either (where arbitration clause is lacking) bring the case to the state court or, when arbitration clause is present, start the arbitration proceedings. Only very few civil court judges are trained in competition law. On the other hand a number of arbitrators has extensive experience with anti-trust disputes. They are ready to face parties' claims based on competition law arguments. Especially in the case of complex M&A transactions the arbitration leads to a more foreseeable result.

In what type of contracts do anti-trust matters matter? There is only one kind of contract which is absolutely free of any troubles or impediments and that is the direct sales contract. Other kinds of contract are susceptible to difficulties under competition law. These include namely: general business conditions, supply contracts including rebate schemes, work contracts, R&D contracts, agency and distribution contracts, joint-venture agreements, franchising agreements, licensing and techno-

logy transfer agreements, know-how agreements, M&A transactions (including share deals and assets deals), shareholder agreements and all types of financing agreements. All these types of agreements are vulnerable to breaches of competition law that may be brought up in a lawsuit or arbitration proceedings. In that respect it is important for the company to collect and preserve market data in case of a dispute that may arise several years later.

The fifth panel was chaired by Marc Blessing and discussed application competition law in M&A disputes. The first speaker was Gordon Blanke of Habib Mulla from United Arab Emirates presented EU commitment arbitration arising out of the EU Commission's decisions on mergers. He admitted, that the issue is rather theoretical than practical as there have not been many arbitrations arising from the EU commitments. There have been just a couple of cases reported in the relevant specialist press including Global Arbitration Review. Importance of EU commitments arbitration is rather a strategic one. The EU commitment arbitration can arise out of behavioral access commitments contained in either clearance merger decisions adopted by the European Commission under art. 6 and 8 of the Merger Regulation (139/2004) or out of its decisions based on articles 7 and 9 of the EU Modernization Regulation (1/2003). In both cases the reason for the behavioral commitments is to ensure the access to an essential facility controlled by a merged undertaking. As a matter of general policy the European Commission accepts behavioral commitments only when structural commitments prove to be ineffective or impossible. The behavioral commitment

is a promise on the part of the merged entity to provide third party beneficiaries (competitors) with an access to essential facility on fair, reasonable and non-discriminatory (FRAND) terms. By means of arbitration the Commission passes a mandate of monitoring of these medium and long term commitments back to the market. Arbitration commitments thus form part of a Commission decision. From the legal point of view they represent the unilateral standing offer to arbitrate from a merged entity to any third party competitor who derives rights from the commitment package under the merger clearance decision. Should any dispute arise from the implementation of that particular commitment package the third party beneficiary can invoke the arbitration provision and start arbitration proceedings against the merged entity. The EU courts tend to see behavioral commitments combined with arbitration commitments as good as the structural commitments. There have been 65 arbitration commitments from 1992 to the present day and they correspond to 20% of total number of merger clearance decisions. The arbitration commitments are in fact the escalated dispute resolution mechanisms (expert determination or mediation being the amicable settlement phase prior to arbitration proceedings). That is possibly why there are so few reported arbitrations. Presumably, the parties managed to settle the dispute prior to arbitration and the arbitration obligation operated as a deterrent.

The arbitration commitment would be the most usually replicated in the implementation agreement concluded between the merged entity and third party beneficiary. Through the insertion of the arbitration commitment into

implementation agreement it would make it proper private law instrument for the settlement of disputes. This the unilateral promise to arbitrate turns into a mutually binding arbitration agreement.

Arbitration commitments under the EU Modernization Regulation are less frequent. There have been about 6 Commission decisions under art. 101 or 102 TFEU where arbitration commitment has been used up to now.

With regard to sectors, the arbitration commitments are generally found in sectors where access to network plays crucial role like aviation, rail, IT, telecommunication, gas and oil.

Next speaker on the panel was Anna Maria Pukszto of Dentons, Poland. She discussed interrelation between EU state aid rules (art. 107 TFEU) and arbitration. Until recently this issue attracted little interest, as it was generally believed, there were no meeting points between these two aspects. However, the practice shows that arbitration is not immune from state aid considerations. It is true in case of investment arbitration as well as commercial arbitration. Further, M&A transactions itself may constitute a form of state aid. Asset deals, share deals, mergers, restructuring can be a way of state support of an individual undertaking. Broad range of issues that may arise before arbitral tribunal encompass two fundamental questions: first, what is the legal consequence of granting of an illegal state aid in M&A transaction? Would it be a valid reason for refusing the performance by a party or even ground for invalidity or inoperability of the transaction in question? Second, what are potential civil law conseque-

nces of the fact that the Commission ordered a recovery of illegal aid granted to a target company before the M&A transaction?

As to the first issue: an allegation that M&A transaction involves illegal state aid may be used as a pretext for one of the parties of M&A transaction from freeing itself from contractual obligations. Particularly, the state may refuse performance and argue, that the performance of a contract would constitute an illegal aid. The arbitral tribunal then may have to decide whether this fact constitutes the valid reason for refusing the performance. It will have to decide whether the contract is null and void or merely ineffective as a whole or in part. In recent judgment issued in a case C-275/10 *Residex Capital IV CV v Gemeente Rotterdam* the CJEU (formerly ECJ) expressed opinion that invalidity should be the last resort sanction. If the state has other ways of recovering the state aid they should be used in the first place.

With regard to the second issue: the question arises whether the buyer may be held liable for the return of the state aid granted to the target before M&A transaction. This situation may happen in connection with the target companies that were subject to privatization in the past. In speaker's opinion this question should be answered while taking into account the price paid by the buyer. If the price paid for the target company was fair, there should be no liability on the part of the buyer. The EU principle on extension of liability on the buyer may generate post-closing disputes that may end up in arbitration. In these dispute the arbitral tribunal should take into account the scope of due diligence and the extend of documents made available to the

buyer. It would be for the arbitral tribunal to decide whether the buyer is entitled to damages, price reduction or the right to abate the contract on the basis of such legal concepts as deceit. On the other hand, if the parties anticipated possibility of state aid recovery in the M&A contract (with regard to price reduction) these provisions may be applicable in arbitration.

The second part of presentation was devoted to state aid issues in investment arbitration. During the privatization of undertakings in Central and Eastern Europe, the buyers were offered incentives (usually in a form of mixture of state aid measures) as well as BIT protection. After the accession of these countries to the EU relevant incentives may potentially conflict with the EU competition law. However, the adjustment of the incentives to the EU law may be viewed as a change conditions under which the investment was made. With regard to these issues an award was issued in ICSID arbitration according to European Energy Charter Treaty (*AES v. Republic of Hungary*) in relation to pricing mechanism that, after the accession to the EU, became contrary to the provisions of EU law. In the award the arbitral tribunal treated EU state aid law not just as a part of the international treaty but treated it as a part of the national law. Consequently, the investor lost the case. It was concluded that state aid cases became more and more frequent in arbitration and the arbitrators are requested to implement private investor test in their decision making.

Jean-Claude Najar of Curtis Mallet-Prevost Colt & Mosle presented his views on

application of competition law and arbitration based his long-time practical experience as GE in-house counsel. He stressed that a position of in-house lawyers is extremely difficult in anti-trust case as EU law as well as national law of many European states deprives in-house counsel of a legal privilege in anti-trust proceedings. With regard to application of competition law in the company, the key function of an in-house lawyer is to identify the risks and to build up an adequate protection (usually in a form of a compliance program). Further, he explained conditions under which the arbitration clause and choice of law clause are made in M&A contracts in practice. With respect to a considerable number of pathological clauses in contracts he labeled in-house lawyers as the weakest parts of the transaction. As these clauses are negotiated at the very last second of negotiations they are more results of a cut-and-paste work than results of an informed choice.

With regard to application of competition law in arbitration, he pointed out that the Commission's intervention as *amicus curiae* impedes the confidentiality of the arbitration as any Commission's involvement in proceedings inevitably attracts public attention. With reference to his practical experience Jean-Claude Najjar opposed a view that speed constitutes an advantage of arbitration as compared to litigation. On the other hand, he presented an opinion that the major advantage of arbitration is that arbitrators tend to induce the settlement whenever they see the occasion for it. The settlement gives companies an opportunity to resume the business relationship with an opponent and that makes arbitration attractive.

Mark Kantor, the last speaker on the panel, presented the issue of remedies from the point of US competition law. The most typical feature of US system is an overlap of jurisdiction among several independent agencies and the main competition authority (the US Department of Justice, Antitrust Division). As a matter of example he presented a case of joint-venture in media sector that could negatively influence the access of third parties beneficiaries (competitors) to the essential facility. Both competition authorities involved in the case, that are the US Department of Justice and the Federal Communications Commission (FCC) provided for a baseball (final offer) arbitration to secure behavioral commitments. In both kinds of arbitration the arbitrator must choose one between the two competing offers. However each authority introduced a different type of a final offer arbitration. The FCC introduced an arbitration that constituted merely a first step on the ladder of three instances authorized to deal with the case.

The alternative type of arbitration available in the US Department of Justice can be pursued only with the consent of this agency. It would be an expedited baseball arbitration. In this type of arbitration there would be more finality since the only review allowed is the traditional review in US courts.

The important difference between the FCC arbitration and the US Department of Justice arbitration is the in the confidentiality standard. The FCC arbitration is fully transparent process with third parties being able to intervene as *amicus curiae*. On the other hand, the US Department of Justice proceedings are held in camera. In both types of arbitration the

arbitrator is requested to choose one of the two competing commercial offers. For that purpose he or she must be very well informed what the other companies do in this type of business. For this reason the parties may be asked to reveal the terms of licensing agreements concluded previously with third parties. That is why FCC issued confidentiality order limiting access to certain documents to a limited number of people. Despite the protective order there were continuing confidentiality concerns on the part of the third parties.

The discussion that followed the presentations was connected with a wide scope of issues. Notably, Mark Kantor answered the question on quantification of future looking damages. He outlined two distinct approaches to this issue and stressed that the option chosen by the particular tribunal will depend on the legal tradition that influence personal opinions of the individual arbitrator.

The following conclusions may be drawn on the basis of the discussion in the panel:

The regulatory arbitration gains more and more importance both in the EU and in the US. It is generally used to monitor access commitments contained in decisions of competition authorities. In the EU there only few arbitrations have been reported until present time. Presumably, it has been due to the fact that the Commission uses elevation arbitration clauses and most dispute might have been settled prior to arbitration proceedings.

There is an increasing number of M&A arbitrations where parties make claims on the basis of competition law provisions. Although the

discussion on the panel concentrated on application of EU competition law the same may be said about application of national competition rules.

The application of anti-trust rules requires adequate knowledge and skills on the part of arbitrators. This makes arbitration attractive in comparison to litigation.

The application of EU anti-trust rules would likely deprive arbitration of its confidential character as any involvement of the EU Commission attracts public attention.

Anti-trust rules are applied on the basis of parties respective claims. Only in exceptional cases where the most serious infringement blatantly occurs the arbitral tribunal should raise anti-trust issues *ex officio*.

Compliance programs in companies form important element of prevention of risks related to the application. It is a task for in-house lawyers to increase awareness of competition law issues among companies managers.

Mandatory public law in M&A arbitration¹

■ Courtenay Griffiths

QC

INTRODUCTION

I would first of all like to thank Beata Gessel-Kalinowska vel Kalisz for inviting me to speak at this conference and the people of Warsaw for their warm welcome to me on this my first trip to the historic heart and crossroad of central Europe.

Nonetheless one has to be careful when you break into someone's house, the house-owner is likely to kill you, if he or she is around. I hope you won't kill me, because I am here committing an act of burglary.

I say that because I have a confession to make, I have limited experience of this area of law, arbitration. Rather I do know a few things about crime, because for over 30 years I have been engaged in crime, not literally, but rather defending those who commit the most grave and heinous of crimes, although, from the media coverage, the highpoint of my legal career, of which I am often reminded, is my cross-examination of a fading but still beautiful supermodel with an ongoing anger management problem, Naomi Campbell, about her alleged receipt of blood diamonds from my then client Charles Taylor.

¹. Address to international conference for promoting arbitration, Warsaw, Poland, June 6-7 2013

Nonetheless, I feel that I have something important to contribute to this gathering. Being an outsider, my experiences provide me with a dreadful objectivity when asked to examine an unfamiliar area. It enables you to examine this legal process like a scientist viewing a specimen under a microscope, with no preconceived prejudices or judgments.

That vantage point suggests to me the following outline of my brief presentation, which is necessarily foreshortened by the time constraints.

Point one is the proposition that the basic legal and practical assumption underlying arbitration, that is that the growth of business opportunities is the primary and overriding consideration, is and will come under increasing attack from other important considerations which have come to the fore globally since the New York Convention came into existence in 1959.

A quick overview of what money laundering is about, and what you should be alert to when operating in the field of international commercial arbitration. Including, in particular, cross-border M&A's.

We will then shortly look at the susceptibility of the arbitration process, because of its nature and priorities, to penetration and abuse by ruthless, unscrupulous international criminals for their own gain.

We will then examine the future growth areas for arbitration, one of which, from my experience and knowledge of current development trends, is likely to be in Africa, where a rapacious desire to acquire raw materials is leading to a new scramble for the supposed dark continent. Also of course, closer to Poland, in the former Soviet Asian Republics.

Finally, if time allows, I will provide you with a brief synopsis of a real life situation in which real concerns about an arbitral award being tainted and in effect hijacked by criminality, have demonstrated the level of scrutiny which should be employed in such proceedings. It suggests and demonstrates that such proceedings are not geared to dealing with issues of criminality when they arise.

HISTORICAL PERSPECTIVE

The New York Convention has to be viewed in its historical context. It was introduced to underpin international commerce. This was fourteen years after an Iron Curtain fell and divided a war-ravaged Europe. The priorities for the West, then, was to demonstrate that free-market capitalism was intellectually and economically a preferable model for development. In contrast one only has to look at that monument built by Stalin opposite the hotel Intercontinental here in Warsaw to see the dead weight, literally, that dehumanizing cult called democratic socialism placed upon the people of Poland. Against that back-

ground the principles and priorities underlying the New York Convention made sense. It enshrined, amongst other things:

- privatized justice, a necessary corollary of a free market,
- flexibility,
- almost universal enforceability

In contrast money laundering as a legal concept and legislation to combat it are barely 30 years old, but most countries in the world now have legislation that criminalizes money laundering and facilitates the recovery of the proceeds of crime.

Further almost thirty years after the introduction of the New York Convention in 1959, two wars waged by the United States of America have given a motivational thrust to other competing norms, and thereby have come to entrench other over-arching considerations on the global landscape, one of these being money laundering. One consideration was the deep concern of governments, not just the United States, and financial and other institutions as to the extent of the risks to stability and security thrown up by organized crime and more latterly by economic crime.

The first war was, the "War on drugs". The years 1988 to 1991 laid the foundation for the current global anti-money laundering measures. The primary concern that generated international action during this period was the immense profit being made by drug cartels in South America and elsewhere, allied to concerns at the destabilizing effect of huge sums of dirty money having a distorting effect on the global economy, particularly in the major

market for those drugs in the United States. Money laundering legislation was aimed at depriving the purveyors of this misery of their profits.

The next war was the “War on Terror”. The objective, in combating money laundering, now extended to depriving international terrorist groups of the finance, which provided their lifeblood. 9/11 provided the impetus to give money laundering teeth.

As a consequence anti-money laundering laws and regulations, which are now a feature of the law and practice of most countries in the world, now have a number of distinctive features:

- there is a common core of anti-money laundering measures in each jurisdiction which have been ratified or adopted by governments throughout the world and have, to a considerable degree, given a global consistency to attempts to combat money laundering,
- this common core of anti-money laundering measures uses not only the criminal law, but also civil law and the regulation of relevant businesses and professions in order to combat and criminalize money laundering at every stage.
- this is supplemented by, at both national and international levels, a range of public and private sector bodies contributing to the overall effort. At an international level, bodies such as the Basel Committee on Banking Supervision and the Wolfsberg Group, as well as major institutions such as the IMF and the World Bank, contribute to the

setting of industry-specific standards and to establishing best practice in this area of concern. Within countries, representative industry and professional bodies have an important role in providing detailed guidance on compliance and training.

The consistency of the international approach is largely due to the United Nations Vienna Convention (1988), the 40 + 9 Recommendations of the Financial Action Task Force (Established in 1989), and the UN Palermo Convention (2000). These three major developments on the international stage coordinated a global approach and promoted an international perspective on money laundering. Further, the UN Merida Convention of 2003, although primarily concerned with corruption, also dealt with again with money laundering.

Today international criminal activity in relation to money laundering is now policed by the Financial Action Task Force’s 40 + 9 Recommendations (FATF), which developed out of a G7 initiative in 1990. Today recommendations on combating money laundering and countering the financing of terrorism are now an integral part of the global “good governance” agenda. The fact is that more than 189 states have now signed up to what is in practice, if not in law, a competing global convention akin to the New York Convention.

The FATF is headquartered at the Organisation for Economic Cooperation and Development in Paris. At present there is very little democratic control, oversight or accountability in relation to the FATF, yet countries subject to the FATF’s Anti Money Laundering or Counter Terrorism requirements must, (note mandatory):

- introduce specific criminal laws;
- law enforcement powers;
- surveillance and data retention systems;
- financial services industry regulations and
- international police cooperation arrangements in accordance with FATF guidance.

Participating countries must also undergo a rigorous evaluation of their national police and judicial systems in a peer-review-style assessment of their compliance with the Recommendations. Developed out of World Bank and IMF financial sector assessment programs, this process significantly extends the scope of the Recommendations by imposing extraordinarily detailed guidance – over 250 criteria – on the measures states must take to comply with the 40+9 Recommendations. The reward for FATF compliance is to be seen as a safe country in which to do business; the sanction for non-compliance is designation as a “non-cooperating territory” and international finance capital steering clear.

The question I now ask is this: which is to be given priority, The New York Convention and business and economic development or these real concerns about money laundering and this new “convention” which has arisen in response. There is an obvious tension between the two which will need to be resolved.

WHAT IS MONEY LAUNDERING?

So what is money laundering? A senior English Judge defined it in this way: “In its typical form money-laundering occurs when criminals who profit from their criminal enterprises seek to bring their profits within the legitimate financial sector with a view to disguising their true origins. Their aim is to avoid prosecution for

the offences that they committed and confiscation of the proceeds of their crime.”

SUSCEPTABILITY FOR ARBITRAL PROCEEDINGS TO BE ABUSED

Despite the obvious advantages to business of arbitration as a means of resolving disputes, it has to be recognized that this is a means to dispense justice which carries within its operation two main factors which make it susceptible to misuse by criminals.

There are limited avenues for appeal against an arbitral award, so that an erroneous decision cannot be easily overturned once made.

The confidentiality of the proceedings, reduces the opportunity for outside impartial scrutiny. There is an inbuilt lack of transparency.

One can see why confidentiality of arbitral proceedings assuages the legitimate concerns of business. They do not want to wash their “dirty linen” in public. However this conceals the fact that the proceedings may also be used for less legitimate purposes. One can see why such proceedings might be preferred by certain businesses if they have transgressed into crime, more importantly, in its simplest form, the parties to the “dispute” might engage arbitration as a vehicle for money laundering by creating a fictitious dispute and obtaining awards which are free from scrutiny, thereby obtaining funds which are prima facie clean.

Thus, financial institutions amongst others, are enjoined by the Financial Action Task Force to pay: “...special attention to all complex, unusual transactions, and all unusual patterns

of transactions, which have no apparent economic or visible lawful purpose. The background and purpose of such transactions should, as far as possible, be examined, the funding established in writing, and be available to help competent authorities and auditors.”

Furthermore, as well as issuing its recommendations, the Financial Action Task Force has also listed countries considered to be deficient in combating money laundering. This is of particular significance in the context of cross border M&A's.

FUTURE CONCERNS

These concerns will over the next few years, be of pressing importance and concern. Economic progress in several parts of Africa and former Soviet Asian Republics is likely to boom over the next few years. Disputes over oil and gas, land water and other resources are going to be a major growth area for arbitration. (Develop).

Taking Africa as an example, remember this is a continent with a long history of corruption and misappropriation of state assets over many decades by so-called “Exposed Individuals”. That phrase forms part of the lexicon of anti-money laundering legislation worldwide. Bribery, as we all recognize, is a major issue on that continent. This could taint much work in the field of arbitration over the coming years, especially as demands for the lifting of banking secrecy, exposes ill-gotten gains, to seizure and safer havens are sought for their continued retention. The principle of Caveat emptor does not begin to describe the minefields awaiting the unwary.

A CONCRETE EXAMPLE

An award was made providing for specific performance of an option agreement between Company A and Company B. In particular the award in favour of Company A required Company B to pay several million dollars in return for a percentage of the share capital of Company C.

The option agreement provided for a detailed mechanism for the completion of the sale and purchase of the shares. One of the requirements was for Company C to resolve to approve the sale and transfer of the shares by Company A to Company B, and for Company C to issue a new share certificate.

What happens in this situation if there is strong evidence to suggest that: the transaction under which Company A acquired the shares in company C was part of a criminal conspiracy to defraud the government of a country thus: performance of the sale of the shares under the option agreement would thereby realize for Company A part of the proceeds of that conspiracy to defraud, for: by approving the transfer of the shares company C would be facilitating or assisting in the laundering of those funds.

Could Company C go to court and say, we should not be required to transfer these shares because so to do would make us party to a criminal conspiracy to breach anti-money laundering legislation?

It will not have escaped your attention that such a situation has three possible consequences:

- the court could give primacy to the New York Convention, thus turning a blind eye to issues of money laundering, or
- it could give primacy to the new global norm regarding money laundering and thus protect Company C from potential criminal liability, but such an outcome would
- assist Company B, if successful, in undermining the award.

This example illustrates the tension that I mentioned earlier between two global norms. What should a court rule when faced with such a dilemma?

CONCLUSION

As they increasingly must, official agencies seek support from and collaborate with the private sector in preventing, controlling and interdicting criminal and subversive activity. Also the near collapse of the financial sector, particularly in the west, has given rise to fundamental changes in the architecture of supervision and the content of regulation. It has also emphasized the resource and other limitation of traditional policing practices and models.

The development of new, and in some cases unconventional, arrangements between law enforcement, regulatory bodies and those in the professions and business will inevitably throw up a host of issues. This may well prove inconvenient for business and for the process of arbitration, but I suggest that this is going to be an important debate in the coming years.

Report from the Panel on Mandatory Public Law in M&A Arbitration

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The last panel was devoted to the issues of the mandatory public law in M&A arbitration, beyond the issues of competition law which were discussed in a separate panel. The panel was moderated by J. Michaelson of Fried Frank with the participation of M. Jamka of K&L Gates, S. Tonova of Jones Day, S. Wilske of Gleiss Lutz, I. Nazarova of Engarde and C. Griffiths, QC of 25 Bedford Row Chambers.

J. Michaelson presented his view on why States impose mandatory public law in international arbitration. Firstly, he pointed to the States' need to regulate the spheres beyond the autonomy of individuals, such as antitrust regulations or tax law. Secondly, he pointed to the States' control over the impact of unconnected third parties which are unable to participate in a bilateral arbitration process, which is the case with respect to bankruptcy law and regulation of patents. In situations when the parties' autonomy clashes with the mandatory public law the following questions need to be answered:

How is it dealt with?

Who deals with it?

What is the standard of proof with respect to it?

These questions were touched upon by all the panelists, however by each of them with regard to a different sphere of mandatory public law.

In M. Jamka's presentation, he discussed the relationship between international arbitration and the bankruptcy law. As he boldly stated: "bankruptcy is from Mars and arbitration is from Venus". Tensions result from the different nature of the legal relationship present in both these spheres of law. Whilst bankruptcy law constitutes part of a State's public policy, arbitration is based on private autonomy which is usually put outside the control of public bodies. M. Jamka rightly underlined the tension between the underlying concepts of both spheres of law, with bankruptcy focusing on the collective interest and arbitration focusing on satisfaction of individual claims.

M. Jamka adopted the comparative approach in discussing the impact of bankruptcy law on an arbitration agreement. He recalled the legal systems of Switzerland, France, Germany, the Netherlands, England and the USA as examples of the systems in which despite the bankruptcy of one of the parties to arbitration, the agreement in question remains valid. On the other hand, these legal systems

put a stay on arbitration proceedings, however, the stay is usually temporary. M. Jamka presented examples of Section 362 of the US Bankruptcy Code and Article 47 of the French Bankruptcy Code to show the consequences that bankruptcy may have on arbitration proceedings. In both these systems the arbitration proceedings may lead only to the valuation of the amount of the claim without the possibility to order payment, which usually is dependent on the bankruptcy proceedings. M. Jamka described the systems in which the bankruptcy does not lead to the invalidity of the arbitration agreement as "arbitration friendly".

M. Jamka presented also the less arbitration friendly jurisdictions, such as Spain, Italy and, in particular, Poland. According to Articles 142 and 147 of the Polish Bankruptcy Code the declaration of bankruptcy leads to the arbitration agreement becoming invalid and unenforceable. Furthermore, according to Polish law, even pending proceedings should be discontinued.

In the context of international arbitration, the key issue becomes the law governing the bankruptcy of either of the parties to the arbitration agreement since the consequences may differ significantly. In the context of the European Union, M. Jamka referred to Council Regulation (EC) No. 1346/2000 of May 29, 2000 on insolvency proceedings (the "EU Regulation")¹. Whilst the EU Regulation stipulates that for the bankruptcy proceedings the applicable law is the law of the Member State in which the bankruptcy proceedings commence, with respect to the effect of

1. O.J. of June 30, 2000, Series L-160, at p. 1.

insolvency on the pending lawsuit, it is the law of the Member State in which that lawsuit is pending.

As a case study, M. Jamka referred to the Elektrim case, which was subject to two arbitration proceedings, one in London and one in Geneva. Pointing to the differences between the EU Regulation and the Swiss Private International Law, M. Jamka demonstrated how important the bankruptcy laws are for the outcome of arbitration proceedings. According to M. Jamka the different outcome of these proceedings resulted from different questions which were posed to the arbitration panels and consequently to the courts. The English court was asked about the validity of the arbitration clause, whereas the Swiss court was asked about the standing/capacity of the party to such a clause.

M. Jamka concluded that the Elektrim case may serve as an example of arbitration tribunals' position towards the bankruptcy laws. He stated that it would be the *lex loci arbitri* which would be applied by the tribunals in order to determine the consequences of bankruptcy on the arbitration proceedings. However, it is more likely that the arbitration tribunal would, and should, apply the private international law to determine the law governing that question.

The last part of M. Jamka's presentation was devoted to the enforcement of arbitration awards issued against bankrupt companies. He referred to Article V of the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention") and distinguished between the situation in which the enforcement court in one country

has to enforce an award which was based on an invalid arbitration agreement or which was issued with respect to an entity which did not possess legal capacity to participate in the proceedings (under Article V(1) of the New York Convention this would make the award unenforceable) and the situation in which the enforcement court has to deal with the public policy ground under Article V(2) of the New York Convention. He underlined that bankruptcy laws are usually part of public policy. M. Jamka invoked the French courts' practice of annulling awards which were issued in contravention of the principle of equal treatment of creditors. A similar practice, though based on a case-by-case approach, is applied by the US courts.

Finally, M. Jamka presented the main reasons why the bankruptcy of one party to the arbitration agreement should not lead to the automatic invalidation of that agreement. In particular, a claimant in the arbitration proceedings is better suited to evaluate whether there is any point in pursuing a claim against the bankrupt company. In some cases the claimant may wish for a declaratory judgment instead of financial reparation. In other cases, the arbitration award against the bankrupt company may be vital for other stakeholders, such as insurers, guarantors or members of the consortium established with the now bankrupt company.

The second presentation, given by S. Tonova, dealt with the topic of "Illegality in investment arbitration", which is now heavily debated by practitioners of investment arbitration throughout the world. At the beginning of her presentation, S. Tonova presented a brief overview

of investment arbitration. Apart from presenting the basics of investment arbitration, she focused on the Polish example.

Focusing on the definition of "investment" in the Polish-Denmark bilateral investment treaty, S. Tonova referred to the typical requirement of such definitions that an investment must be made "in accordance with the laws of the Contracting Party". This requirement, even though this need not be spelled out explicitly in bilateral investment treaties, is embodied in the customary international law principle of states' permanent sovereignty over natural resources expressed in United Nations General Assembly Resolution No. 1803(XVII) of 1962.

The requirement that investment should be made in accordance with the laws of the host State led certain tribunals to an obvious conclusion that investments which were made illegally cannot benefit from bilateral investment treaty protection (as stated by the tribunal in the *Phoenix v. Czech Republic* case). S. Tonova rightly pointed to the concept of *de minimis* violations of the host State's law which do not lead to such an extreme result.

S. Tonova presented the line of case law on the impact of the violation of a host State's law by an investor on its accessibility to bilateral investment treaty protection. She presented such cases as the *Inceysa v. Salvador* case, *Plama v. Bulgaria* case or *World Duty v. Kenya* case and discussed different types of investor misconduct with respect to mandatory public law. Whilst she did not mention explicitly the "clean hands" doctrine, it is clear that investment tribunals which apply international law should bear that doctrine in mind, which is well

established in the context of rules on diplomatic protection.

S. Tonova picked the very specific example of charges of bribery which were discussed by a few tribunals in investment arbitration. She emphasized the discrepancies the *World Duty v. Kenya* case with the *EDF v. Romania* case to show how the approach may differ depending on whether it is a respondent State or an investor who claims that corruption takes place.

Finally, S. Tonova discussed, albeit inconclusively, the issue of whether the question of illegality should be dealt with at the jurisdictional or on the merit-related stage of arbitration proceedings. It is important however to stress that when the compliance with a host State's law is embodied in a definition of "investment" in particular in a bilateral investment treaty it is an issue of the tribunal's jurisdiction *ratione materiae*. Yet, as shown by the *Saluka v. Czech Republic* case, an investor's misconduct should also be taken into account, providing it did not bar a tribunal's jurisdiction, at the merits phase particularly in the context of fair and equitable treatment.

The next presentation, by S. Wilske, was devoted to the impact of corruption and other misdeeds on M&A issues. Interestingly, S. Wilske started by evaluating the morality issues in the context of arbitration, referring, *inter alia*, to the award in ICC case no. 1110 of 1963. In that case the sole arbitrator dismissed the claim on the basis of good morals and public policy.

In the context of M&A transactions he presented different instances in which corruption

may be involved in M&A transactions including bribing of an individual director or employee of another party or target company, bribing an anti-monopoly office to give clearance for a transaction or a state official in the context of privatization of a state-owned company.

S. Wilske underlined the role of corruption charges in arbitration proceedings. He described the corruption argument as a last resort in an otherwise lost case. Indeed, if a contract containing an arbitration clause was awarded through illegal means, it should be determined invalid by an arbitration panel thus preventing any arbitration between parties to the contract. The corruption charges may work on both sides. Finally, he discussed the arbitrariness of the corruption claims which are usually subject to national criminal laws and thus outside any arbitration tribunal's jurisdiction. Ultimately, the main role of corruption arguments is to kill the arbitration proceedings by invalidating either the whole arbitration agreement or a particular claim.

S. Wilske also reviewed other problems of arbitrability of such matters as insolvency, tax matters or IP rights. He concluded that, as such, these issues may be dealt with in arbitration despite being subject to mandatory public laws. Whilst he admitted that criminal matters are generally excluded from arbitration, certain consequences of these issues may be raised in arbitration. At the end of the day, the criminal issues should be dealt with outside arbitration without hindering the related arbitration proceedings.

At the end, S. Wilske presented an example of an arbitration agreement itself being the

target of corruption. According to S. Wilske this would be the only example when corruption could affect the jurisdiction of the arbitration panel. Apart from that, the tribunals should apply and do apply the separability doctrine, which means that even if the main contract is invalidated due to the corruption, the arbitration clause remains valid and enforceable.

To conclude, S. Wilske discussed the consequences of potential invalidity of an arbitration claim based on corruption, asserting that a respondent should not benefit from its own misconduct by pointing to the corrupting of the opposing party. This would lead to the punishment of only one party to the transaction who would be left with no remedy. Whilst there is a reason for not allowing the respondent to benefit from its own misconduct, it is equally necessary not to allow the claimant to get away with serious charges, assuming of course that they can be proven during arbitration. The solution is, possibly, that the misconduct of the claimant should be evaluated and weighted against the rest of its claim at the merits phase of arbitration.

The fourth presentation was given by I. Nazarova on the issues of burden and standard of proof with respect to corruption in international investment arbitration. She underlined the extent of the problem of corruption of public officials and its particular importance in the context of foreign investments. In her attempt to define "corruption", I. Nazarova referred to the definition by Transparency International and doctrinal definition by F. Haugeneder and Ch. Liebscher. Interestingly, she did not invoke the OECD Convention on Combating Bribery of Foreign

Public Officials in International Business Transactions of 1997, which seems to set an international standard for what constitutes "corruption". The main requirement for corruption to occur is that its aim is to induce "the official to act or refrain from acting in relation to the performance of official duties, in order to obtain or retain business or other improper advantage in the conduct of international business" (Article 1(1)).

In her presentation, I. Nazarova endorsed the tribunal in the *World Duty Free v. Kenya* case and stated that the tribunal set the standard for corruption at the international level. In particular, the endorsement regarded the tribunal's reference to the principles of international public policy, which otherwise remain undefined. Importantly, she put the prohibition of corruption among such concepts as *ius cogens*, which are uncommon in investment arbitration and which are treated rather with a certain sense of perspective by other international courts and tribunals, maybe with the exception of human rights bodies. Rather than mixing these concepts, it is necessary to underline the meaning and significance of international/transnational public policy, within the meaning giving to it by E. Gaillard, for a specific field of international arbitration.

Surprisingly, I. Nazarova endorsed also the tribunal for stating that the corruption of an official cannot be attributable to a State. However, one needs to point out that "corruption" can be defined as such only when it concerns a public official with respect to that person's official capacity. Thus, one should come to the same conclusion as stated above with respect to S. Wilke's presentation, that

all issues of corruption should be dealt with at the merit-related stage of the proceedings.

Subsequently, I. Nazarova presented the issue of burden of proof, relying on the *AAPL v. Sri Lanka*, *Tradex v. Albania* and *Alpha Project v. Ukraine* cases. She put particular emphasis on the *prima facie* standard according to which the party asserting a fact has the burden of proving it but once it has done so the burden of proof shifts to the other party.

With respect to the standard of proof I. Nazarova rightly made a distinction between the approaches adopted in continental law and in common law. She also emphasized that the standard of proof should primarily be determined by the applicable law with the due discretion left to arbitration panel. Among the applicable standards of proof in the common law system she presented the "balance of probabilities" standard, the "clear and convincing evidence" standard and the "beyond reasonable doubt" standard. In the continental law system she referred to the "inner conviction principle" standard. She concluded by stating that the international arbitration tribunals often apply the "clear and convincing proof" standard with respect to corruption charges. However, she rightly pointed out that there is no uniform standard for proof of corruption in international arbitration.

The last presentation was given by C. Griffiths on the topic of arbitration treated as money laundering. He presented an interesting perspective of not an arbitration lawyer but rather of a criminal lawyer. Whereas he presented himself as an "outsider", he made a very specific proposal that the "basic legal

and practical assumption behind the use of arbitration, that is that the growth of business opportunities is the primary and overriding consideration, is and will come under increasing attack from other important considerations which have come to the floor globally since the New York Convention came into existence".

C. Griffith also presented the basics of the money laundering concept and the problems which should be considered in particular by the arbitration lawyers. He also showed the susceptibility of the arbitration process to penetration and abuse by international crime.

C. Griffith's presentation led to the important conclusion on the necessity of cooperation between public bodies and arbitration stakeholders in the field of combating international crime. Bearing in mind the importance of these issues on the one hand, and their obvious intrusion into the private nature of international and national arbitration on the other, they will be the subject of heated debate in the near future.

Conclusions:

There is growing interplay between public law and international arbitration, both in investment arbitration and commercial arbitration;

The main issue is whether the public law issues are arbitrable and to what extent arbitration panels may exercise jurisdiction over such issues. It seems that the basic concepts to limit the arbitrability of public law issues are already in force, including such concepts as public policy or good morals;

On the other hand, dealing with mandatory public law is sometimes necessary to establish

the rights and obligations of the parties to the proceedings, which may be an issue, for instance, with respect to the bankruptcy law;

There must be a clear distinction between the state's mandatory public law and public policy considerations at the international level, which is particularly present with respect to corruption. At the same time, it is vital to establish which law governs a particular question of public law;

With respect to corruption, there is a very important question as to whether corruption may constitute a bar for the tribunal's jurisdiction. Whilst S. Wilske argued against this consequence, I. Nazarova endorsed the statement to the contrary made by the tribunal in the *World Duty v. Kenya* case. It seems that the best option would be to allow a tribunal to deal with such issues at the merits phase or even at the quantum stage of the proceedings and to take them into account when deciding on the existence and scope of the liability of a respondent;

Finally, as stated by T. Gizbert-Studnicki in his closing remarks, the whole judicial or legal thinking is organized around the distinction between public and private law. At the same time, he emphasized the disappearing boundary between issues of private and public law, which will certainly define arbitration law practice in the near future.



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